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REVENUE ACT OF 1962

REPORT

OF THE

COMMITTEE ON FINANCE
UNITED STATES SENATE

TO ACCOMPANY

H.R. 10650

A BILL TO AMEND THE INTERNAL REVENUE CODE OF
1954 TO PROVIDE A CREDIT FOR INVESTMENT IN
CERTAIN DEPRECIABLE PROPERTY, TO
ELIMINATE CERTAIN DEFECTS AND
INEQUITIES, AND FOR
OTHER PURPOSES

TOGETHER WITH

INDIVIDUAL, ADDITIONAL, DISSENTING, SUPPLEMENTAL
AND MINORITY VIEWS



AUGUST 16 (legislative day, August 15), 1962.—Ordered to be printed

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REVENUE ACT OF 1962

AUGUST 16 (legislative day, AUGUST 15), 1962.—Ordered to be printed

Mr. KERR, from the Committee on Finance, submitted the following

REPORT

together with

INDIVIDUAL, ADDITIONAL, DISSENTING, SUPPLEMENTAL AND MINORITY VIEWS

[To accompany H.R. 10650]

The Committee on Finance, to whom was referred the bill (H.R. 10650) to amend the Internal Revenue Code of 1954 to provide a credit for investment in certain depreciable property, to eliminate certain defects and inequities, and for other purposes, having considered the same, report favorably thereon with amendments and recommend that the bill as amended do pass.

I. GENERAL STATEMENT

This bill, H.R. 10650, represents a major revision and reform of our Federal tax system. This is a matter which has been under consideration by Congress since April 20, 1961, when the President sent up his tax message. Most of his recommendations, modified as the House and your committee believe desirable, are incorporated in the amended bill reported by your committee.

The bill contains three principal groupings of tax revision measures. The central element in the bill is the investment credit. This allows a 7-percent credit against tax for most taxpayers for their purchases of machinery and equipment and certain other property (not including buildings). This investment credit, coupled with the depreciation guidelines recently liberalized by the administration, by stimulating capital formation will provide growth in the economy consistent with the principles of a free economy. This investment credit, by encouraging the modernization and expanded use of capital equipment, will improve our competitive position abroad and thus aid in meeting the balance-of-payments problem. Moreover, the capital formation

induced by this credit will both aid in providing the longrun growth needed by our domestic economy and be of major assistance in our more immediate problem of economic recovery.

The remaining provisions in the bill are concerned primarily with improving tax equity and eliminating tax evasion or avoidance, either in the domestic economy or with respect to income earned abroad by American interests. In the latter case, the primary concern of your committee has been with the removal of special tax advantages accruing to "tax havens."

One of the measures in the House bill, designed to decrease tax evasion (whether or not deliberate) was a provision for withholding on dividends, interest, and patronage dividends. Because of both the burden of such a provision on individuals owing little or no tax and its many complexities, your committee has deleted it, but has added a requirement for the reporting of payments of dividends, interest, and patronage dividends exceeding \$10 annually per recipient, both to the Government and to the recipient. Your committee believes that in the long run this will have at least as great an impact on tax evasion as a withholding system.

Both the bill as passed by the House and as amended by your committee reduce tax avoidance by providing ordinary income treatment for gains from the sale of depreciable property to the extent of depreciation taken. Moreover, by preventing the conversion of ordinary income into capital gains this has been an important factor in making the new liberalized depreciation guidelines feasible.

Among the more publicized and troublesome problems with which the bill is concerned is the deduction for entertainment expenses. Your committee believes that its version of this provision provides a balanced approach which neither prevents deductions for legitimate entertainment expenditures nor permits them for the continuation of abuse situations.

Your committee's bill also is concerned with competitive advantages of specific groups of taxpayers. In this regard your committee, in general agreement with the House, concluded that the reserve deductions of mutual savings banks and savings and loan associations are too large and should be reduced, that mutual insurance companies should be taxed not only on investment income but on their underwriting gains as well, and that in the case of cooperatives a full tax should be paid currently at either the level of the cooperative or at that of the patron.

In the case of foreign income, your committee has been primarily concerned with ending tax haven abuses; namely, devices to avoid either the United States or foreign taxes which could be expected to be imposed under normal business operating conditions. To achieve this goal the bill ends the deferral of the U.S. tax in the case of certain forms of income arising from insurance abroad of U.S. risks, from passive investments, from sales and service subsidiaries separately incorporated from the producing companies, and from funds which are brought back to this country without the payment of U.S. tax. A number of other measures dealing with foreign income or property are also included. Provision is made for the payment of a full 52-percent tax through a "gross-up" procedure when income is brought back to the United States from a foreign subsidiary; for the taxation of income at ordinary income tax rates when controlled foreign corpo-

rations are liquidated or the stock interests sold; and for the full taxation by the United States of income distributed to American beneficiaries by foreign trusts set up by American grantors. In addition, a ceiling has been placed on the earned income exclusion for Americans who are residents abroad; and foreign real property holdings are to be included in the estate tax base of U.S. citizens.

Your committee began hearings on this bill on April 2 of this year. These hearings extended until July 3 and included 29 days on which testimony was heard. This material is contained in 12 volumes of nearly 5,000 printed pages. In addition, your committee has considered this bill in executive session for a period of several weeks. The bill, therefore, represents decisions reached by your committee after careful deliberation over an extended period of time.

A. Summary

The provisions contained in the bill as amended by your committee can be summarized by section numbers as follows:

- (1) The act is to be cited as the "Revenue Act of 1962."
- (2) An investment credit against tax liability is provided. Generally it is 7 percent of investments in new tangible personal property and certain other depreciable property, excluding buildings. A credit also is available for limited amounts of investments in used property. The taxpayer's depreciation base for tax purposes is to be reduced by the amount of the investment credit.
- (3) A deduction is provided for expenses relating to appearances before, and communications with, a legislative body, a legislative committee or individual legislator, if the expenses are otherwise ordinary and necessary business expenses. Also included are expenses of communications between an organization and its members and between a business and its employees or stockholders. This provision does not cover advertising expenses or those concerned with political campaigns.
- (4) Deductible expenses for entertainment, amusement or recreation generally are limited to those directly related to, or associated with, the active conduct of a trade or business. In the case of expenses related to facilities, to be deductible they must also be used primarily for the furtherance of the taxpayer's trade or business. Limitations are provided in the case of traveling expenses and business gifts. In addition, rules are set forth providing that deduction of entertainment, etc., expenses will be denied unless substantiated.
- (5) Distributions in kind from foreign corporations to corporate stockholders are treated as having a value equal to their fair market value (rather than the adjusted basis of the property), and the foreign tax credit available likewise is based on the fair market value of the property.
- (6) The present tax treatment of mutual savings banks, savings and loan associations, etc., is revised so that their additions to bad debt reserves generally may not exceed 60 percent of their taxable income (before this deduction) or, if larger, an amount bringing their reserves up to 3 percent of loans on real property. Certain other limitations are also provided, and in the case of stock savings and loan associations the deduction is to be 50 percent instead of 60 percent of taxable income. In addition, a new definition of domestic savings and loan associations is provided and certain excise tax exemptions these organizations presently enjoy are removed.

(7) Distributions of accumulated income by foreign trusts, to the extent the trust was established or added to by American grantors, are to be taxed to the U.S. beneficiaries in substantially the same manner as if they had received this income directly instead of through the intermediary of a foreign trust.

(8) Mutual fire and casualty insurance companies are to be taxed on their "total" income less a deduction for loss reserves equal to one-fourth of their underwriting gain plus 1 percent of their insurance claims. Most of this reserve, to the extent not used to offset losses, at the end of 5 years is to be brought back into the company's tax base. Exemptions are provided for small companies whose total receipts do not exceed \$150,000, while those whose total receipts are between \$150,000 and \$600,000 are taxed on investment income but not underwriting gain. The bill also deals with the special problems of reciprocal underwriters and interinsurers, of factory mutual insurance companies, of mutual marine insurance companies, and of companies whose risks such as windstorm, hail, or flood insurance are concentrated in a relatively small geographical area.

(9) Where a domestic corporation receives dividends from a foreign corporation, the amount included in its tax base, if it elects the foreign tax credit, is to be not only the dividend itself, but also the tax paid by the foreign corporation as well. This provision is not to apply with respect to dividends received from "less developed country corporations" or from certain holding companies for such corporations.

(10) The foreign tax credit limitation for certain interest income is to be computed separately from the limitation for other types of income. The interest income referred to here does not include that derived from the active conduct of a trade or business, from a banking or similar business, or from a corporation in which the taxpayer has a 10-percent voting interest.

(11) The unlimited exclusion from U.S. tax for income earned abroad by U.S. citizens who are bona fide foreign residents is reduced to \$35,000 (\$20,000 for the first 3 years). However, in applying this ceiling, certain fringe benefits will be gradually taken into account for purposes of this limitation over a 4-year period. In addition, the contributions which employers make hereafter toward employee pension plans, based on foreign employment, will be taxable to the employee when received.

(12) Shareholders of controlled foreign corporations are to report for tax purposes the undistributed earnings of these corporations to the extent they represent income from insuring U.S. risks, increases in earnings invested in U.S. property (generally not related to foreign business), passive investment income, and income from sales or service subsidiaries involving transactions with related persons outside of the country of incorporation of the subsidiary. Dividend and interest income derived from 10-percent-related corporations actively doing business in less developed countries and reinvested in such countries, however, is excluded from the amount taxed to the U.S. shareholders. The bill also provides that if certain minimum amounts of income are distributed (which vary in accordance with effective foreign tax rates) the shareholders are not to be taxed on the undistributed income. In addition, export trade income of "export trade corporations" within certain limits is not to be taxed to U.S. shareholders in the case of most of the categories of income described above. Other relief provisions are also provided.

(13) Any gain after 1962 on the sale of personal property and most other tangible property, other than buildings and structural components, to the extent of depreciation taken in 1962 and subsequent years, is to be treated as ordinary income for tax purposes.

(14) When stock in foreign investment companies is sold, the gain realized by U.S. shareholders is to be ordinary income to the extent of the earnings and profits accumulated since 1962. The companies and shareholders can avoid this treatment if the companies distribute currently 90 percent or more of their taxable income, other than capital gains, and the shareholders report the capital gains, whether distributed or not. In addition, until January 1, 1964, where certain conditions are met, these corporations are permitted to reincorporate as domestic corporations on a tax-free basis without obtaining prior clearance for the reorganization from the Internal Revenue Service.

(15) Where stock in a controlled foreign corporation is redeemed, such a corporation is liquidated, or the stock of such a corporation is sold, any gain realized which represents earnings and profits accumulated after 1962 is to be taxed to 10-percent-U.S.-shareholders as ordinary income. If the shareholder is an individual, his tax on this income is to be no greater than if the foreign corporation were a domestic corporation which paid the 52-percent U.S. tax (offset by any foreign tax credits) and then made a distribution of the balance to the U.S. shareholder who then is subject to a capital gains tax. (The combined tax in this case cannot exceed 64 percent.) Alternatively, the individual shareholder will not have to pay a total tax greater than the sum of the taxes he would have paid had he received the earnings and profits in the years actually earned.

(16) Gain from the sale or exchange after 1962 of a patent, invention, model or design, copyright, secret formula or process, or other similar property by a U.S. person to a foreign corporation which it controls is to be treated as ordinary income rather than capital gain. This does not apply where the transfer is to a controlled foreign corporation for use in its own manufacturing operations.

(17) Cooperatives are to receive a deduction for patronage dividends paid to the patrons in cash or by allocations if the patron has the option to redeem the allocations in cash during a 90-day period after issuance, or consents to treating this income as constructively received and reinvested in the cooperative. The patron may give his consent individually in writing, the cooperative may by its bylaws require members to give this consent, or patrons may give their consent by endorsing a check representing at least 20 percent of the total patronage dividend. For any allocation to be deductible to the cooperative, however, at least 20 percent of the patronage dividend must be paid in cash. Any of these amounts which are deductible to the cooperative must be included in the income of the patron for tax purposes when received if the amounts arise from business activity of the patron.

(18) Real estate located outside the United States, in the case of citizens or residents of the United States, is to be included in their tax base for purposes of the estate tax imposed at the time of death.

(19) Payors of interest, dividends, and patronage dividends of more than \$10 per year per person must report these payments to the Government on an annual basis and also send a statement to the dividend, patronage dividend, or interest recipient indicating the annual amount so reported. Civil penalties of \$10 per statement or information re-

turn are specified for each failure, other than for reasonable cause, to send the statement or information return to the recipient or to the Government. However, the aggregate penalty per payor is not to exceed \$25,000 per year with respect to returns to the Government or \$25,000 with respect to statements to recipients.

(20) A number of changes are made in the annual information return which domestic corporations presently are required to file with respect to foreign corporations which they control. In addition, a number of changes have been made in the return which must be filed by U.S. citizens or residents who are officers or directors of a foreign corporation and also by 5-percent shareholders of such corporations. Not only is information required to be submitted by those who are officers, directors, or 5-percent U.S. shareholders within 60 days of the organization or reorganization of the corporation but also those who presently are, or subsequently become, officers or directors or 5-percent U.S. shareholders. In the case of officers or directors, the only information required to be furnished is the names and addresses of 5-percent U.S. shareholders.

(21) In the case of farmers, expenditures incurred in the clearing of land may be deducted to the extent of \$5,000 or 25 percent of the taxable income from farming for the year, whichever is the lesser.

(22) When an individual is entitled in effect to spread his income for tax purposes back over the years to which it is attributable, he may also elect to apply the 20- or 30-percent limitation on charitable contributions before the income is spread.

(23) The provision in present law which treats a husband and wife as one shareholder in the case of community property and property held as joint tenants, tenants by the entirety, or tenants in common for purposes of the election for certain small business corporations to have their income taxed directly to their shareholders is to be made effective, if the taxpayers so elect, with respect to taxable years beginning after December 31, 1957, instead of 1959.

(24) Net operating losses incurred in 1953 and 1954 by a street railway company in converting from streetcar to bus service, which are not absorbed in the normal carryover period, are to be treated as a net loss occurring in 1959. This permits these losses to be carried forward to the years 1960 through 1964.

(25) The union-negotiated pension plan of Local Union No. 435 of the International Hod Carriers' Building and Common Laborers' Union of America is to be treated as a qualified tax-exempt trust for the period from May 1, 1960, to April 20, 1961, if the trust was not operated during this period in a manner to jeopardize the interests of its beneficiaries. This also permits employers to deduct contributions made to the trust in this period.

(26) The 1939 code is amended to provide that where one partner in a two-man partnership dies, the partnership year for the surviving partner is not to close prior to the time the partnership year would have closed had neither partner died or otherwise disposed of his interest.

(27) No provision in the bill is to apply in any case where its application would be contrary to any treaty obligation of the United States.

B. Revenue estimates

1. *Estimates of the Joint Committee Staff.*—As indicated in the tables below, the staff of the Joint Committee on Internal Revenue Taxation has estimated your committee's bill will result in a revenue loss of \$555 million on a full-year basis, based upon income levels for the calendar year 1962.¹ This can be compared with an estimated loss of \$285 million under the House bill on a full-year basis.

For the fiscal year 1963 (July 1, 1962, to June 30, 1963, inclusive), the staff estimates that your committee's bill will result in a revenue loss of \$630 million as contrasted to a loss under the House bill for that year of \$1,090 million. None of these estimates takes into account any possible effect of the provisions on economic conditions. Table 1 shows the details of the staff's estimates of the effect of your committee's amendments as compared with the House bill on a full-year basis. Table 2 shows the details of the estimates for the fiscal year 1963.

As indicated in table 1, the version of the investment credit provided by your committee's amendments is expected by the staff to result in a full-year revenue loss of \$1,340 million. The other provisions of the bill, on a full-year basis, are expected to raise revenues by \$785 million, resulting in the net loss of \$555 million. Under the House bill the full-year loss from the investment credit was \$55 million more than under your committee's action. However, the additional revenue derived from the other provisions under the House bill would have amounted to \$1,110 million, which accounts for the smaller revenue loss. Most of the revenue difference in these other provisions between your committee's and the House version of the bill is attributable to the substitution of reporting for withholding on dividend and interest payments. Other differences are the revenue gain from mutual savings banks, etc., under your committee's bill (largely as a result of the amendment affecting stock companies), the decreases in revenue resulting from changes made by your committee in the provisions relating to entertainment, ordinary income on depreciable property, and the "gross-up" of dividends received from foreign corporations. The entertainment provisions are somewhat less restrictive under your committee's bill than under the House bill. In the case of the provision relating to ordinary income on depreciable property the revenue loss is attributable to the change for mining companies made in the method of computing "taxable income from the property" in the case of depreciable property. In the case of the "gross-up" provision, the lesser revenue under your committee's action can be attributed to the fact that this provision is made inapplicable to income from less developed country corporations. Other provisions added by your committee also are expected to result in a \$5 million revenue loss. The most significant item here is the deduction allowed farmers for clearing land. There are, of course, also differences within the various other provisions but the losses and gains involved approximately offset each other.

¹ The various provisions, of course, will not have uniform effect in future years. In the case of mutual fire and casualty insurance companies, for example, the full year revenue effect will not be reached until after an elapse of 5 years when most of what remains in the protection against loss account begins to be restored to taxable income. On the other hand, the method of charging losses in the case of dividend-paying companies may reduce tax liability in the fourth or fifth year by as much as \$5 million but this will be largely offset in later years when the amounts added to this account are restored to income.

As indicated in table 2, your committee's action according to the staff's estimates results in a revenue loss of \$630 million in the fiscal year as contrasted to the \$1,090 million under the House bill. Most of this difference is attributable to your committee's action in making the investment credit effective only with respect to acquisitions or construction after June 30, 1962, instead of January 1, 1962, as provided by the House bill. Other differences with respect to the fiscal year 1963 estimates between your committee's action and the House bill are largely attributable to the fact that the reporting of dividends and interest is not expected to have a revenue effect until after the end of the fiscal year 1963, while part of the revenue impact from withholding would have been felt during the last half of the fiscal year 1963. The remaining difference between the two versions of the bill is attributable to the fact that the House bill would have made the entertainment provisions effective as of July 1, 1962, while under your committee's action these are not effective until January 1, 1963.

TABLE 1.—*Estimated full-year revenue effect of H.R. 10650¹ as passed by the House and as amended by the Senate Committee on Finance*

[Millions of dollars]

	As passed by the House	As amended by the Committee on Finance
Investment tax credit.....	-1,395	-1,340
Withholding on dividends and interest.....	+550	
Reporting of dividend and interest payments.....		+275
Mutual banks and savings and loan associations.....	² +170	² +180
Entertainment, etc., expenses.....	+125	+85
Capital gains on depreciable property.....	+110	+105
Mutual fire and casualty companies.....	³ +25	³ +25
Cooperatives.....	+30	+30
Foreign items:		
Controlled foreign corporations.....	+50	+50
Gross-up of dividends.....	+25	+15
All other foreign items.....	+25	+25
Other (secs. 21-26 of Senate Finance Committee bill).....		-5
Total.....	-285	-555

¹ At levels of income and investment estimated for the calendar year 1962, without taking into account effect of provisions on the economy; estimates are rounded to nearest \$5,000,000.

² The level of income for these thrift institutions in 1962 has been revised upward since the preparation of the revenue estimates for the House bill.

³ Revenue gain which would result if this provision were in effect for 1962 and had been in effect for the 5 preceding years, so that amounts added to the protection against loss account in the first year and not offset by losses would be brought into taxable income in 1962.

Source: Staff of the Joint Committee on Internal Revenue Taxation.

TABLE 2.—*Estimated revenue effect of H.R. 10650 for the fiscal year 1963 as passed by the House and as amended by the Senate Committee on Finance*

[Millions of dollars]

	As passed by the House ¹	As amended by the Committee on Finance ¹
Investment tax credit.....	-1,340	-650
Withholding on dividends and interest.....	+170	-----
Reporting of dividend and interest payments.....		0
Mutual banks and savings and loan associations.....	+10	+10
Entertainment, etc., expenses.....	+60	+(²)
Capital gains on depreciable property.....	0	0
Mutual fire and casualty companies.....	0	0
Cooperatives.....	0	0
Foreign items:		
Controlled foreign corporations.....	0	0
Gross-up of dividends.....	0	0
All other foreign items.....	+10	+10
Other (secs. 21-26 of Senate Finance Committee bill).....		-(²)
Total.....	-1,090	-630

¹ Estimates are rounded to nearest \$5,000,000.² Less than \$2,500,000.

Source: Staff of the Joint Committee on Internal Revenue Taxation.

2. *Estimates of the Treasury Department.*—As shown in table 3, the Treasury Department has estimated that your committee's bill will result in a revenue loss of \$210 million on a full-year basis, if no effect is given to the stimulative effect of the bill. With this effect taken into account the loss is expected to be only \$15 million. These estimates can be compared with the Treasury Department's full-year estimates for the House bill, which show an increase in revenues of \$325 million without taking into account the stimulative effect of the bill and \$430 million if account is taken of this factor.

Table 3 also shows the Treasury Department's estimate of the effect of the bill in the fiscal year 1963. In that year the estimate is expected to result in a revenue decrease of \$485 million without taking into account the stimulative effect of the bill and \$210 million decrease with this effect. Under the House bill the estimated effect in the fiscal year 1963 would be a \$325 million increase in revenues without the stimulative effect and \$430 million increase with this effect.

The stimulative effect of the investment credit under the Treasury Department's estimates is based upon statistical relationships in past years between investment and gradual changes in the cost of capital goods (profit ability) and cash flow. This does not take into account the especially favorable impact on businessmen's decisions to invest or the sudden improvement in these factors resulting from the enactment of the credit.

TABLE 3.—*Estimated revenue effect of H.R. 10650 as amended by the Senate Finance Committee*

[In millions of dollars]

	As passed by House of Representatives				As amended by Senate Finance Committee			
	Full year		Fiscal year 1963		Full year		Fiscal year 1963	
	Gross	Net	Gross	Net	Gross	Net	Gross	Net
Investment tax credit ¹	-1,105	-555	-1,040	-525	-1,020	-580	-520	-235
Capital gains on depreciable property.....	+100	+50	-----	-----	+100	+50	-----	-----
Withholding on dividends and interest.....	+780	+520	+245	+235	² +240	² +155	-----	-----
Expense accounts.....	+125	+80	+65	+40	+60	+40	+30	+20
Mutual savings banks and savings and loan associations.....	+200	+135	-----	-----	+205	+140	-----	-----
Mutual fire and casualty companies.....	+40	+25	-----	-----	+35	+20	-----	-----
Cooperatives.....	+35	+25	-----	-----	+35	+25	-----	-----
Foreign items:								
Controlled foreign corporations.....	+85	+85	-----	-----	+85	+85	-----	-----
Gross-up of dividends.....	+35	+35	-----	-----	+25	+25	-----	-----
All other foreign items.....	+30	+30	+5	+5	+30	+30	+5	+5
Miscellaneous provisions.....	-----	-----	-----	-----	-5	-5	0	0
Total.....	+325	+430	-725	-245	-210	-15	-485	-210

¹ At levels of income and investment estimated for 1962; modified from published estimates because of current results of the Commerce-SEC survey of planned capital expenditures. In estimating the net revenue cost of the investment credit, its favorable effects on the level of investment were computed from statistical relationships in the past years between investment and gradual changes in the cost of capital goods (profitability) and cash flow. This procedure thus does not take into account the especially favorable impact on businessmen's decisions to invest, of the sudden major improvements in these factors resulting from the enactment of the credit. Taking this into account should produce more favorable effects than those shown in the table.

² Estimated gain from increased compliance because of reporting requirements.

Source: Office of the Secretary of the Treasury, Office of Tax Analysis, Aug. 13, 1962.

II. INVESTMENT CREDIT

(Sec. 2 of the bill and secs. 38, 46-48, and 181 of the code)

A. Reasons for provision

The Secretary of the Treasury in his appearance before your committee stated:

The central element in the bill is the tax credit for investment in depreciable machinery and equipment.

At another point he said, with respect to the investment credit:

This matter has top priority in the agenda for tax reform. As chief financial officer of the Nation, I do not lightly regard tax abatements on the scale proposed here. I urge this legislation because it will make a real addition to growth consistent with the principles of a free economy; because it will provide substantial help in alleviating our balance-of-payments problem, both by substantially increasing the relative attractiveness of domestic as compared with foreign investment and by helping to improve the competitive position of American industry in markets at home and abroad; and because, far from adding to the forces responsible for alternative recessions and recoveries, it will be of major assistance in strengthening our present recovery and enabling us to attain a higher rate of growth

and sustained full employment. Early action will resolve uncertainty or hesitancy and begin at once a strong and lasting incentive for modernization of the productive facilities of our national economy.

The Secretary pointed out that American industry today must compete in a world of diminishing trade barriers in which the advantages of a vast market, so long enjoyed here in the United States, are now being, or are about to be, realized by many of our foreign competitors. An increase in efficiency and productivity at a rate at least equal to that of other leading industrial nations is in the long run necessary, therefore, both from the standpoint of the U.S. balance-of-payments position and to continue to improve our standard of living. The investment credit as a form of investment stimulation already is in use by the United Kingdom, Belgium, and the Netherlands, and is in the process of being enacted by the Australian Parliament.

To achieve an increased rate of capital formation, a two-pronged course of action is being followed in the area of capital formation. First, the Treasury Department has recently announced a series of depreciation revisions. The objective of these revisions is to provide realistic tax lives in light of past actual practices and present and foreseeable technological innovations and other factors affecting obsolescence. The new guideline lives are expected initially to result in an annual revenue reduction of \$1.5 billion and to reduce depreciable lives in the case of corporations surveyed by 21 percent. Another facet of this objective is to achieve a more simple and flexible system of depreciation through the use of guideline lives for broad classes of assets used by each of the industries in our economy.

Realistic depreciation alone, however, is not enough to provide the essential economic growth. In addition, a specific incentive must be provided if a higher rate of growth is to be achieved. The investment credit will stimulate investment, first by reducing the net cost of acquiring depreciable assets, which in turn increases the rate of return after taxes arising from their acquisition. Second, investment decisions are also influenced by the availability of funds. The credit by increasing the flow of cash available for investment, will stimulate investment. The increased cash flow will be particularly important for new and smaller firms which do not have ready access to the capital markets. Third, the credit can be expected to stimulate investments through a reduction in the "payoff" period for investment in a particular asset. This reduction in risk, coupled with the higher rate of profitability and increased cash flow, will lower the level at which decisions to invest are made and will help to restore to past levels the proportion of the annual national output devoted, through investment in machinery and equipment, to capital formation.

The objective of the investment credit is to encourage modernization and expansion of the Nation's productive facilities and thereby improve the economic potential of the country, with a resultant increase in job opportunities and betterment of our competitive position in the world economy. The objective of the credit is to reduce the net cost of acquiring new equipment; this will have the effect of increasing the earnings of new facilities over their productive lives and increasing the profitability of productive investment. It is your com-

mittee's intent that the financial assistance represented by the credit should itself be used for new investment, thereby further advancing the economy. Only in this way will the investment credit fully serve the overall national interest in greater productivity, a healthy and sustained economic growth, and a better balance in international payments.

Some have suggested that tax changes designed to add to consumer demand are the appropriate way to raise the level of investment. However, to rely only on such an approach suggests primarily expansion of existing kinds of equipment and techniques, rather than more efficient and larger quantities of capital per worker and therefore greater productivity. The credit adds to the quantity and quality of capital available per worker, and increases the relative attractiveness of investment at home compared with investment abroad.

Finally, the statement sometimes made that the credit is a subsidy overlooks the fact that other alternatives, such as faster depreciation, for example, share the same characteristics of giving the investor in equipment a monetary reward beyond what he would receive on the basis of realistic accounting. The credit, however, is preferable to higher depreciation charges because the latter tend to distort income accounting and produce higher costs for book purposes, which frequently could be expected to be reflected in higher product prices.

B. Comparison of committee amendments with House provision

Your committee has retained the basic House provision on the investment credit. As in the House bill, the credit generally allowable is 7 percent of the investment (3 percent in the case of certain public utilities) and this amount may be offset in full against tax liability up to \$25,000, and against one-quarter of the tax liability above this level. Again, as in the House bill, property with an estimated useful life of 8 years or more is fully taken into account in computing the credit, property with an estimated life from 6 to 8 years is taken into account at two-thirds of its basis, while property with an estimated life from 4 years up to 6 years is taken into account at one-third of its basis. In addition, as provided by the House bill, machinery and equipment are the principal types of investments eligible for the credit.

Despite the substantial similarity of your committee's and the House versions of the investment credit, there are important differences. The most important of these is the reduction of the amount on which depreciation may be taken, in the case of assets eligible for the investment credit, by the amount of the investment credit allowable. Your committee believes that where a taxpayer purchases a \$100 asset, for example, if \$7 of this purchase price is to be allowed as a direct reduction in his tax in the form of a credit, this same amount should not be allowed to him again as a depreciation deduction in computing income subject to tax. In such a case the taxpayer's real contribution toward the purchase of the \$100 property is limited to \$93 and therefore it seemed appropriate to your committee to limit the depreciation recovery to this same \$93.

A second change made by your committee provides that where property is lost or destroyed as a result of a casualty or is stolen and is insured, reinvestment of the insurance proceeds in replacement property is not to be eligible for an investment credit. This eliminates the

allowance of a credit in such cases, where the taxpayer has not made a contribution of additional funds toward the acquisition of new property.

A third change made by your committee provides that the investment credit is to be available only with respect to property acquired or constructed after June 30, 1962, rather than on or after January 1, 1962. Your committee concluded that taxpayers had no basis for assuming that an investment credit would be provided by Congress during the first half of 1962 when, for most of this period, the provision had not yet been even considered by the Senate or your committee. The allowance of the investment credit for this period, therefore, would represent a windfall for the taxpayers involved.

A fourth change made provides that livestock (including race horses) are not to be eligible for the investment credit since they are not included in the category of property resulting in ordinary income (to the extent of depreciation deductions) at the time of sale.

A fifth change made in the investment credit by your committee was to provide a 3-year carryback of unused investment credits. As pointed out above, the investment credit, in the case of a taxpayer with a tax liability of more than \$25,000, could offset only one-quarter of the tax liability in excess of \$25,000. Under the House bill any "unused" investment credit remaining could only be carried forward and used in any of the 5 succeeding years, again subject to the applicable limitations for those years. Testimony before your committee pointed out that the absence of a carryback of an unused credit in such cases would tend to encourage investment in prosperous periods and discourage it in depressed periods, when tax liability was relatively low. To offset this effect, your committee's bill provides for a 3-year carryback of any unused investment credit (but not to a period before June 30, 1962).

In a sixth and final change, your committee has deleted the requirement that one electing to treat a lessee of property as a purchaser must be engaged in the business of leasing property. Under your committee's change, any lessor of property meeting the other requirements may make the election.

C. General explanation of provision

1. *The general pattern of the credit.*—The bill provides a credit (in code sec. 38), which may be offset directly against income tax liability. The credit generally is an amount equal to 7 percent of "qualified investment" which includes both purchases of new equipment, and also, to a limited extent, purchases of used equipment. In the case of property with an expected useful life of 4 up to 8 years, the investment taken into account in computing the 7 percent credit is graduated from one-third in the case of the 4-year assets up to 100 percent in the case of property with a useful life of 8 years or more. In the case of most public utilities, however, only what amounts to a 3-percent investment credit is allowed. Under your committee's amendments the depreciation base of the assets involved is reduced (except for purposes of computing the credit) by the amount of the investment credit involved.

The types of property, whether new or used, which are included in qualified investment are described as "section 38 property." This property includes most tangible personal property. It also includes

certain real property, other than buildings (or structural components) if the property is used directly in manufacturing, production, transportation, etc.

Once the amount of the 7-percent credit against tax is determined, the amount which may be claimed in any one year is limited to the tax liability, or if this tax liability exceeds \$25,000, the credit (to the extent it exceeds this amount) is limited to 25 percent of the tax liability. However, a 3-year carryback and a 5-year carryforward are provided for any of these credits which because of this limitation are unused. The bill also provides that where the property is disposed of (within 8 years) before the end of its life as estimated for the credit the credit is reduced to the amount which would have been allowed initially had the useful life of the asset been correctly estimated.

These provisions are described briefly below.

2. *Qualified investment.*—Investment which is eligible for the 7-percent investment credit is referred to in the bill as “qualified investment” (sec. 46(c)). Qualified investment includes both new property and a limited amount of used property. Property qualifies for the investment credit in the year it is placed in service by the taxpayer, even though under the depreciation convention used by the taxpayer, he may not be eligible to start depreciation on the property until the coming year.

The percentage of investment which the taxpayer may take into account as qualified investment varies to some degree with the expected useful life of the property in his business. No part of the investment in property with an expected useful life of less than 4 years is taken into account. Property with an expected useful life of 4 years and up to (but not including) 6 years is taken into account at one-third of the amount of the investment actually made; property with an expected useful life of 6 years and up to (but not including) 8 years is taken into account on the basis of two-thirds of the investment made; and property with a longer life is taken into account at the full amount of the investment.

Public utility property is taken into account as qualified investment at three-sevenths of the amount otherwise allowable. Thus, in the case of 4- or 5-year public utility property, one-seventh of the investment is taken into account; in the case of 6- or 7-year property, two-sevenths of the investment is taken into account; in the case of property with a life of 8 years or more, three-sevenths is taken into account. This means that in the case of public utility property with an expected useful life of 8 years or more, in effect a 3-percent credit is allowed. Public utility property for this purpose means property used predominantly in an electrical energy, water or sewage disposal business, a local gas distribution business, a telephone business, or a domestic telegraph business, but only if the rates involved in all of these cases are subject to regulation by a governmental agency or commission.

Your committee's amendments provide that “qualified investment” is to be reduced in the case of property which is a replacement for other property destroyed or damaged by fire, storm, shipwreck, or other casualty or stolen, where this latter property was insured (or compensation was otherwise received). In such cases the amount treated as qualified investment in the case of the property acquired as

a replacement is reduced by the amount of the insurance (or other compensation) or by the amount of the basis of the replaced property if lesser. This prevents a taxpayer from obtaining an investment credit windfall from insurance proceeds where the taxpayer neither puts up new funds nor expands his business. (This provision applies only when it results in a larger cutback in qualified investment allowable than the recapture rule described subsequently.)

3. *New and used property.*—The new property taken into account as qualified investment (sec. 48(b)), under your committee's amendments must be purchased or otherwise acquired after June 30, 1962, and its first use commenced by the taxpayer after that date. Other new property eligible for the credit also includes property constructed, reconstructed, or erected by the taxpayer after that date. These are the same rules which applied with respect to the new forms of depreciation provided in 1954.

Used property (sec. 48(c)), eligible for the credit, also must be purchased after June 30, 1962, but, of course, is not property which is new in use with the taxpayer. To prevent abuse, however, there has been omitted from the term "used property," available for the credit that which (after acquisition by the taxpayer) is used by a person who used the property before such acquisition (and also that which is so used by a person who is related to a person who used the property before its present acquisition).

The cost of any used property which may be taken into account is limited to \$50,000 a year. Where used property with varying useful lives is acquired the taxpayer may select the property to be taken into account for the investment credit. Presumably he will select assets with lives of 8 years or more since there is no one-third or two-thirds reduction in such cases.

In the case of a husband and wife filing separate returns, the amount of used property which may be taken into account by each is \$25,000 instead of \$50,000, unless one of the two has not purchased any used section 38 property, in which case the other spouse may claim the entire amount up to \$50,000. This prevents any double allowance for married couples. In the case of affiliated groups of corporations (with a 50-percent test of common ownership instead of the 80 percent usually applied), there is to be one \$50,000 used property allowance for the group and it is to be apportioned among the members of the group in accordance with their purchases of this property. In the case of partnerships, this limitation applies both at the partnership level and also with respect to each partner. Thus, \$50,000 is the limit with respect to used property which may be qualified for any partnership, and then there is a further \$50,000 limit at the partner level. This latter limit may further restrict the used property eligible for the credit where a partner, in addition to his share of investment in one partnership, has, either from another partnership or as a sole proprietor, additional used property investment for which he may receive a credit. The total of these which qualify for the credit may not exceed \$50,000.

To prevent a double allowance where used property is traded in on used property, or where used property is disposed of (otherwise than by casualty or theft) and other used property "similar or related in service or use" is acquired as a replacement, the cost otherwise allowable for the used property acquired is reduced by the adjusted basis

of the property disposed of in both of these types of cases. However, this "replacement" reduction in the credit is not to apply where there otherwise is a reduction in the credit for the property disposed of because of its disposal within 8 years and before the end of what had been its estimated useful life. (See heading 6 below.)

4. "*Section 38*" property.—Section 38 property (defined in sec. 48(a)), is the only property (either new or used) which is treated as "qualified investment." Except for the exclusions noted below, all tangible personal property qualifies as section 38 property. Except for buildings and their structural components, real property which is used as an integral part of manufacturing, production or extraction or of furnishing transportation, communications, electrical energy, gas, water or sewage disposal services also qualifies as section 38 property. This is also true of real property (other than buildings and structural components) used for research or storage facilities with respect to any of the above categories. Tangible personal property is not intended to be defined narrowly here, nor to necessarily follow the rules of State law. It is intended that assets accessory to a business such as grocery store counters, printing presses, individual air-conditioning units, etc., even though fixtures under local law, are to qualify for the credit. Similarly, assets of a mechanical nature, even though located outside a building, such as gasoline pumps, are to qualify for the credit. Real property (other than buildings and structural components) which qualifies as integral parts of categories referred to above includes such assets as blast furnaces, oil and gas pipelines, railroad track and signals, and fences used in connection with raising cattle.

Section 38 property must be depreciable property and have a useful life of 4 years or more. As indicated elsewhere property with estimated useful lives of from 4 to 8 years is only partially taken into account for purposes of the investment credit.

There also are certain categories of property which are excluded from the definition of section 38 property and, therefore, cannot qualify for the credit. These exclusions are:

(1) Property used predominantly to furnish lodging or in connection with the furnishing of lodging. However, there are two exceptions to this exclusion. First, property used in nonlodging commercial facilities (such as a restaurant) located in lodging facilities (such as a hotel) may qualify for the credit if the nonlodging commercial facilities are available for use by the general public on the same basis as for the lodgers. Second, property used in a hotel or motel which primarily serves transient guests may qualify for the credit. The first of these two rules is essential to place nonlodging commercial facilities located in an apartment building, etc., on an equal competitive basis with similar facilities located elsewhere. Property necessary for the operation of a hotel or motel also is used in a regular commercial venture and, therefore, it was believed that it too should be eligible for the investment credit.

(2) Property used by a tax-exempt organization (other than in a business to which the unrelated business income tax applies). The limitation on the allowance of the credit in this case is designed to prevent an investment for use in connection with an exempt function from decreasing any tax on an unrelated trade or business.

(3) Property used by (or leased to or by) governmental units. Property leased to governmental units is omitted since allowing the lessor in such cases an investment credit would not be expected to increase the use of such property by the governmental units.

(4) Property used predominantly outside of the United States. However, there are certain exceptions where this type of property is eligible for the credit, namely, in the case of domestically owned aircraft, rolling stock of railroads, vessels and motor vehicles, where the use is partially within and partially without the United States. Similarly, an exception is made for domestically owned containers which are used in the transportation of property to or from the United States. A further exception is made for domestically owned property used in exploring for, developing, removing, or transporting natural resources from the outer Continental Shelf of the United States. Property used predominantly outside of the United States (with the exceptions noted) is omitted, since the primary purpose of the credit is to encourage investment within the United States.

(5) Livestock (including racehorses).

5. *Limitation on tax credit.*—The tax credit, under the bill, as amended by your committee (sec. 46(a)(2)) may not exceed the tax liability, or if the tax liability is in excess of \$25,000, may not exceed \$25,000 plus 25 percent of the tax liability over this amount. This limitation, while leaving substantial leeway for utilizing the credit, is designed to prevent it (in combination with other tax benefits) from relieving the taxpayer from any substantial tax contribution. However, in recognition of the problems of small business, the bill does not impose this limitation with respect to the first \$25,000 of any tax liability.

Although this limitation with respect to the allowance of the investment credit is imposed for the year in which the investment is made, nevertheless, any investment credit which, because of this limitation, cannot be used in the current year may be carried to other years by the taxpayer. Under your committee's amendments the taxpayer may first carry an unused credit back to the 3 prior years (but not before June 30, 1962) and then forward to any of the succeeding 5 years using the credit in any of these years to the extent it is less than the applicable tax limitation.

Tax liability for purposes of this limitation is computed without regard to the accumulated earnings tax or personal holding company tax liability, but after the application of the foreign tax credit, the 4-percent dividends-received credit, the credit for partially tax-exempt interest and the retirement income credit. In order to prevent a full allowance with respect to \$50,000 of tax liability (instead of \$25,000) in the case of a married couple, the bill provides that for a married individual filing a separate return the tax liability limitation is \$12,500 instead of \$25,000. However, if either the husband or the wife has no qualified investment (or unused credit carryback or carryover), the one having the investment or carryover may make use of the entire \$25,000. In the case of an affiliated group there is one \$25,000 of tax liability which can be fully offset by an investment credit and this is by regulations to be apportioned among the members of the affiliated group.

6. *Recapture rule.*—To guard against a quick turnover of assets by those seeking multiple credit—the bill provides (in sec. 47) a special adjustment or recapture. Under this provision if property is disposed of, or otherwise ceases to be section 38 property, the tax for the current year is to be increased by the reductions in investment credits (which would have resulted in the prior years) had the investment credits allowable been determined on the basis of the *actual* useful life of the property rather than its *estimated* useful life. This means, for example, that if an asset which had previously been estimated to have a useful life in the business of 8 years or more actually is used by the taxpayer only for 6 years, the investment credit for the year in which the investment was originally made will be recomputed on the basis of two-thirds the investment made. Had this asset been sold after 4 or 5 years' use, the allowable investment would have been recomputed on the basis of one-third of the actual investment and had it been sold after a still shorter period, the credit would have been eliminated.

Although the credit is recomputed for the earlier year in which the investment was made, the actual adjustment in tax occurs in the current year, namely, the year in which the asset is disposed of (or otherwise ceases to be sec. 38 property). This makes it unnecessary actually to recompute taxes in the prior years, or to extend the statutory periods of limitations. An adjustment is also made in any carrybacks and carryovers of unused credits so that they too will reflect the reduced amount of investment to be taken into account.

Although disposal of assets (where this is less than 8 years) within a shorter period of time than their estimated useful life usually will be the factor resulting in downward adjustments in the credit allowed, the credit must also be adjusted if property ceases to qualify as section 38 property; where, for example, it is converted to use predominantly outside of the United States. A downward adjustment in the credit also is required where property is converted to public utility property for which only a reduced credit is available. As indicated previously, a credit is allowed for certain types of public utility property equal only to three-sevenths of the credit generally allowable. Where property is converted to such use (again, before the end of its estimated useful life and within the 8-year period) a downward adjustment must be made. In this case, however, instead of disqualifying one-third, two-thirds, or all of the property, depending upon the period of time involved before the conversion to public utility use is made, four-sevenths of such an adjustment is made, since the public utility property itself qualifies for the credit for the remaining period of time but on a reduced basis.

Few exceptions are made to the adjustment rule described above because in no case does this result in a lesser credit than would be available had the useful life of the property been estimated accurately. Moreover, since the tax increase occurs in the current year, and not with respect to the prior year in which the investment occurred, no interest is charged with respect to the increase in tax resulting from the reduction in credit. As a result, your committee believed that it was necessary to forego the application of the adjustment rule only in the case of the transfer of property by reason of the death of the taxpayer or in the case of corporations where a successor corporation "stands in the shoes" of the predecessor corporation. The successor

corporation in such a case, of course, must continue to hold the property for the appropriate period of time, or an increase will be made in its tax because of the disposition of the property prior to the end of its estimated useful life. In addition, the recapture rule is not to apply where the replacement rule, applicable where insurance proceeds are received for casualty losses or thefts, results in a revenue reduction in qualified investment. (See No. 2 above.)

7. *Downward adjustment in basis of property.*—The bill as amended by your committee provides (sec. 48 (g)) that the cost or other basis of "section 38 property" is to be reduced by 7 percent of the qualified investment except for purposes of computing the credit itself. As previously indicated, this downward adjustment is provided because your committee believes that there is no reason to allow the taxpayer depreciation with respect to the portion of the investment in effect paid for by the Government.

The bill provides that the basis of all qualified investments is to be reduced by 7 percent. Since "qualified investment" is after adjustment for different estimated lives (and also after the special adjustment where the property involved is public utility property) the uniform 7-percent downward adjustment provides the appropriate result in most cases. However, there are cases where this adjustment may be too large. This is true, for example, where because of the limitation to 25 percent of tax liability, not all of the credit is used in the taxable year, 3 years to which the credit may be carried back and 5 years to which it may be carried forward. To compensate for this overadjustment the bill provides taxpayers with a special deduction in computing taxable income in the first year after all carryforwards for a credit have expired, equal in amount to any unused portion of the credit. If the taxpayer dies or ceases to exist prior to that time this special deduction (or appropriate portion of it) is allowed the taxpayer in his last year.

A second circumstance under which the downward adjustment referred to here may be too great is that where a property is disposed of before its full estimated life has expired and in less than 8 years. In such cases the investment credit is cut back under the recapture rule explained in the prior section with the result that the original adjustment to the basis of the property was too large. To the extent of this cutback in the investment credit, the bill provides for an increase in the basis of the property at the time just preceding its disposition.

8. *Election for leased property.*—The bill provides (in sec. 48(d)) that a lessor may elect with respect to new property to treat the investment as if made by the lessee instead of the lessor. This election applies only with respect to new property and is not available for used property. Permitting the investment credit to be passed on to the lessee in these cases is believed to be desirable since, as a result of this provision, it is possible for the lessor to pass the benefit of the investment credit on to the party actually generating the demand for the investment.

If the lessor makes this election, then the lessee is treated for purposes of this provision as if he had acquired the property himself, that is, generally he will be treated as if he had acquired the property for the lessor's cost or other basis for the property. However, if the lessor constructed the property (or a corporation controlled by or

which controlled the lessor did so) the lessee is treated as having acquired the property for its fair market value. The useful life of the property in the hands of the lessee in such cases is to be its useful life in the hands of the lessor for purposes of computing the size of the credit available. This is true whether or not the lease itself is for a shorter period of time. Of course, in such cases if the lessee does not renew the lease and hold the property for the estimated useful life of the property in the hands of the lessor, then a downward adjustment will be made in his investment credit.

Where the lessee is allowed the investment credit there is no adjustment of the lessor's basis for depreciation (as discussed in No. 7 above) but a reduction of the lessee's deduction for rent is provided.

9. *Special classes of taxpayers.*—A number of special categories of taxpayers receive special tax treatment under the Internal Revenue Code which makes it inappropriate in their cases to allow the full investment credit. For other taxpayers, the code provides that income may be taxed in part to the organization and in part to its shareholders or beneficiaries. In these situations your committee's bill either cuts down the allowance of the tax credit in proportion to the special benefit received, or provides for the apportioning of the investment credit between the organization and its shareholders or beneficiaries in accordance with their sharing of income for tax purposes. Similar adjustments are also provided in the \$25,000 tax liability limitation.

In the case of mutual savings banks, building and loan associations and cooperative banks, the investment credit allowable is reduced by 50 percent (largely offsetting the 60 or 50 percent special deductions they are allowed). The \$25,000 tax liability limitation is also similarly reduced for these organizations.

In the case of regulated investment companies and real estate investment trusts, the qualified investment allowed them and the applicable \$25,000 tax liability limitation are reduced in the same proportion in which their taxable income is reduced by dividends paid to shareholders or beneficiaries. Similarly, in the case of cooperatives, the qualified investment and \$25,000 tax liability limitation to be taken into account are reduced in the same proportion in which their taxable income is reduced for patronage dividends (and in the case of exempt cooperatives its deductions for dividend payments on capital stock, patronage distributions with respect to U.S. business and income distributed to patrons from sources other than patronage).

In the case of subchapter S corporations, i.e., corporations treated in a manner similar to that of partnerships, since it is the shareholders, rather than the corporation, who are taxed on the income of the corporation, the bill (sec. 48(e)) divides the qualified investment for each year on a pro rata basis among the shareholders of the corporation at the end of the year. In this case since the shareholders are treated as the taxpayer, the investment maintains its character as new or used section 38 property in their hands. Similarly, the bill (in sec. 48(f)) provides that qualified investment in the case of estates or trusts is to be apportioned between the estate or trust on one hand and the beneficiaries on the other on the basis of the income of the estate or trust allocable to each. As in the case of the subchapter S corporations, the beneficiary is treated as the taxpayer with respect to the

investment apportioned to him and therefore the investment retains its character in his hands as new or used section 38 property. The \$25,000 tax liability limitation in the case of the estate or trust is reduced in proportion to the total income allocated to other than the estate or trust.

10. *Carryovers in the case of certain corporate acquisitions.*—Generally, in the case of certain tax-free acquisitions of assets of one corporation by another, present law provides that certain items of the first corporation are to be carried over and attributed to the second. This includes such items as net operating loss carryovers, earnings and profits, methods of accounting, methods of computing depreciation allowance, etc. The bill adds to this list (sec. 381(c)(23)) a carryover to the acquiring corporation in the case of these tax-free reorganizations of the status of the prior corporation with respect to items required to be taken into account for purposes of the investment credit. This mainly is concerned with (1) the carryover of the possibility of adjustment with respect to the investment credit where an asset is held for less than the full period of its estimated useful life and (2) the carryover of any unused investment credit in the prior 5 years.

11. *Effective date.*—The bill provides that the investment credit is to apply to taxable years ending after June 30, 1962. However, in the definition of new section 38 property and also used section 38 property (the only types of property eligible for the credit) it is provided that a credit is to be available only with respect to acquisitions after June 30, 1962, or in the case of property newly constructed, reconstructed or erected by the taxpayer, only with respect to the portion of the property which is constructed, reconstructed or erected after that date. The combination of the effective date and these definitions of new and used section 38 property in effect provide that the investment credit is to be available only with respect to property acquired (also property constructed, reconstructed, or erected by the taxpayer) after June 30, 1962, with respect to taxable years ending after that date.

III. APPEARANCES, ETC., WITH RESPECT TO LEGISLATION

(Sec. 3 of the bill and sec. 162(e) of the code)

A. *Reasons for provision*

Present law allows deductions for income tax purposes for ordinary and necessary expenses paid or incurred in carrying on a trade or business. No mention, however, is made in the statute of expenses incurred in making appearances, submitting material, or communicating with respect to legislative matters. However, Treasury regulations in effect prior to the enactment of the 1954 Code disallowed deductions for expenditures for such purposes (regulations 118, secs. 39.23(o)-1(f) and 39.23(q)-1(a)).

In 1959, the Supreme Court handed down two companion decisions upholding the validity of these regulations, *Cammarano v. U.S.* and *F. Straus & Sons, Inc. v. U.S.* (358 U.S. 498 (1959)). The Court held that although the amounts expended for legislative matters were "ordinary and necessary"—in fact essential to the very survival of the taxpayer's business—nevertheless they were not deductible because the regulations barred the deduction of this particular type of expense.

The Court recognized that the statute contained no provisions specifically supporting the regulations, but stated that they had acquired the force of law by reason of congressional reenactment of the underlying statute.

Following the *Cammarano* decision, the Treasury Department promulgated new regulations relating to deductions incurred with respect to legislative matters. These regulations, while following the general rules set forth in the earlier regulations, for the first time stated specifically that several different classes of expenditures are to be disallowed as deductions. For example, the new regulations require the disallowance of a deduction for the portion of dues and other payments to any organization, a "substantial part" of the activities of which consist of lobbying to the extent that such amounts are "attributable to" these activities. Similarly, the regulations now state that expenditures for the promotion or defeat of legislation include expenditures for the purpose of attempting to influence members of a legislative body, directly or indirectly, by urging or encouraging the public to contact the members.

The regulations issued by the Treasury Department in 1959 brought to a head many administrative and enforcement problems and uncertainties which have plagued both the Government and taxpayers. The difficulty in allowing trade or business expenses generally, but isolating expenses relating to legislative matters and denying deductions for them, stems in part from the difficulty in segregating and classifying such expenses. This is a form of detailed recordkeeping to which taxpayers are not accustomed. Moreover, in the case of many expenses which may primarily be incurred to inform the business itself as to the application of certain proposed legislation, when such information is also made available to legislators it is difficult to determine how an allocation of the expense should be made between legislation and mere planning of the company. Moreover, in the case of an organization, a determination must also be made as to whether the expenses of this type are substantial—a term which involves a difficult line of demarkation.

More important than the administrative and enforcement problems, however, are the policy considerations involved in denying expenses with respect to legislative matters. It appears anomalous, for example, that expenses incurred in appearing before legislative bodies or before legislators are not deductible while appearances before executive or administrative officials with respect to administrative matters, or before the courts with respect to judicial matters, are deductible where the expenses otherwise qualify as trade or business expenses. Your committee believes that the present bar on deductions with respect to legislative matters must be modified to place presentations to the legislative branch of Government on substantially the same footing in this respect as that which obtains in the other two coordinate branches of Government.

It also is desirable that taxpayers who have information bearing on the impact of present laws, or proposed legislation, on their trades or businesses not be discouraged in making this information available to the Members of Congress or legislators at other levels of Government. The presentation of such information to the legislators is necessary to a proper evaluation on their part of the impact of present or proposed legislation. The deduction of such expenditures on the

part of business also is necessary to arrive at a true reflection of their real income for tax purposes. In many cases making sure that legislators are aware of the effect of proposed legislation may be essential to the very existence of a business. The deduction of legislative expenses for those who incur them for personal reasons is not proposed here, since personal expenses generally are not deductible with respect to administrative or judicial presentations and have no bearing on the determination of true taxable income of a business.

B. Comparison of committee amendment with House provision

Your committee has retained the House provision relating to appearances, etc., with respect to legislation. The only change made is the addition of one category of deductible expenses. Your committee's amendment provides, in addition to the categories specified in the House bill, for the deduction of expenses incurred by a taxpayer in carrying on a trade or business if the expenses are in direct connection with the communication of information between the taxpayer and employees or stockholders with respect to legislation, or proposed legislation, of direct interest to the taxpayer. As in the case of the categories referred to in the House bill, expenses of this type, in order to be deductible, may not be for participation or intervention in political campaigns on behalf of candidates for public office or in connection with attempts to influence the general public (or segments thereof) with respect to legislative matters, etc.

C. General explanation of provision

The bill adds a new subsection (sec. 162(e)) to the provision of present law relating to the deduction of trade or business expenses. It provides that certain types of expenses incurred with respect to legislative matters are to be deductible if in all other respects they qualify as trade or business expenses.

The expenses which may be deducted are divided into three categories. The first category relates to expenses in direct connection with appearances, submission of statements or sending of communications. These appearances, statements or communications may be presented either to committees or individual Members of Congress or to committees or individual members of State or local governmental legislatures. The second category of expenses which may be deducted are those in direct connection with the communication of information between the taxpayer and an organization of which he is a member. The third category of expenses which may be deducted are those in direct connection with the communication of information between the taxpayer and an employee or stockholder. This communication of information may be either from the organization, employee or stockholder to the taxpayer or vice versa. In the case of all three categories of expenses referred to above, in order for the expense item to be deductible, it must be concerned with legislation or proposed legislation of direct interest to the taxpayer (and to the organization in the second case). Thus, the expenses may not be in connection with legislative matters such as nominations, etc., but rather must be in connection with specific legislation or proposals for legislation.

The bill also provides that where a taxpayer is a member of an organization and the organization pays or incurs the expenses of the types referred to above on behalf of its members, the dues which the

taxpayer pays to the organization in carrying on his trade or business are to be deductible to the extent they are used for such purposes. The remainder of the dues is likely already to be deductible as an ordinary and necessary business expense. Of course, the dues to an organization may be deductible although not all of the organization's legislative activity is connected with each specific member's trade or business. It is sufficient if all of the organization's legislative activity is related to the trade or business of a significant number of the members.

The bill provides two limitations on the deductions of the above-specified expenses for the specified types of legislative activity. It is not intended by your committee that any deduction be allowed for an amount paid or incurred for participation or intervention in any political campaign for any candidate. Of course, this includes participation or intervention in political campaigns in opposition to a candidate as well.

Your committee's bill further provides that no expense deduction is to be allowed for expenditures to influence the general public, or segments thereof, with respect to legislative matters, elections, or referendums. Thus, except to the extent allowed by existing law, no deduction is intended to be allowed for expenses incurred in connection with what is usually called "grassroot" campaigns intended to develop a point of view among the public generally which in turn is directed toward the legislators. However, your committee does not intend that this limitation should have any effect upon the deductibility of dues, contributions or other payments to organizations whose activities consist primarily of gathering and disseminating factual information, data and statistics. For example, a nonprofit organization would not be affected by the limitation if it were organized and operated for the purpose of studying governmental affairs, Federal, State, or local (which might include analysis of legislation or proposed legislation) and of publishing and distributing to its members and the public factual reports and information on such governmental affairs. Such factual reports might contain data which could be used by subscribers and others to promote or defeat legislation, but so long as the organization itself did not engage in lobbying activities to promote or defeat legislation, payments to such organization will continue to be deductible to the same extent as under existing law.

Nothing in this provision is intended to permit the deduction of entertainment expenses. Such amounts, if deductible at all, must meet the tests set forth in section 4 of the bill, explained below, without regard to this provision.

This provision is to be effective with respect to taxable years beginning after December 31, 1962.

IV. DISALLOWANCE OF CERTAIN ENTERTAINMENT, ETC., EXPENSES

(Sec. 4 of the bill and sec. 274 of the code)

A. Reasons for provision

The Treasury brought to the attention of Congress that widespread abuses have developed through the use of the expense account. In his tax message to the Congress last year, the President stated his

conviction that entertainment and related expenses, even though having a connection with the needs of business, confer substantial tax-free personal benefits on the recipients, and that in many instances deductions are obtained by disguising personal expenses as business expenses. He recommended that the cost of such business entertainment and the maintenance of entertainment facilities be disallowed in full as a tax deduction and that restrictions be imposed on the deductibility of business gifts and travel expenses.

Much of the abuse described by the President can be traced to the broad judicial and administrative interpretation given to the term "ordinary and necessary" which has resulted in many entertainment expenses being allowed as deductions where their connection with a trade or business is quite remote. Under present law, where a business purpose, however slight, exists, then the entertainment expenses generally are fully deductible if they are "ordinary and necessary" business expenses.

After careful consideration of the proposal, your committee has concluded that deductions for entertainment and traveling expenses and business gifts should be restricted to prevent abuses. The committee agrees that this abuse of the tax law should not be condoned, but on the other hand it does not believe that complete disallowance as recommended by the President is the proper solution to the problem. Rather, your committee is convinced that expenses incurred for valid business purposes should not be discouraged since such expenses serve to increase business income, which in turn produces additional tax revenues for the Treasury. If valid business expenses were to be disallowed as a deduction (particularly expenses associated with selling functions), there might be a substantial loss of revenue where business transactions are discouraged, or where they fail to be consummated. Moreover, the entertainment industry employs large numbers of service personnel, most of whom are unskilled workers who would find it difficult to obtain new employment in other fields if the disallowance of entertainment expenses created considerable unemployment in the entertainment industry. In such cases, taxes now paid by these workers would be lost to the Treasury.

B. Comparison of committee amendment with House provision

The House bill provides rules which in general would: (1) disallow a deduction with respect to entertainment activities, except to the extent that the expense is directly related to the active conduct of a trade or business; (2) disallow a deduction with respect to entertainment facilities, unless the facility is used primarily for the furtherance of the taxpayer's trade or business and the expense is directly related to the active conduct of the trade or business; (3) abolish the Cohan rule by requiring the taxpayer to substantiate, by adequate records or by sufficient evidence corroborating his own statement, all expenditures for entertainment and related facilities, and for travel and gifts; and (4) limit the deduction for gifts to \$25 per year per recipient.

Your committee's bill to a considerable degree retains the basic structure of the House bill. However, the effect of the principal provision (the disallowing of a deduction for certain entertainment expenses) has been modified to permit the deduction of expenses for goodwill where a close association is established between the expense and the active conduct of a trade or business.

The report of the Committee on Ways and Means made it clear that the House bill was not designed to disallow completely deductions for entertainment, amusement or recreation expenses, but rather it was intended to eliminate abuses. Under the general rule, no deduction would be allowed for any such expenses except to the extent that such expenses are directly related to the active conduct of a trade or business. Despite the clear language of the House bill and the stated intent of the provision, considerable uncertainty and confusion as to the actual effect of the House draft has been created by the interpretation given this language in the House committee report. It in effect interprets the proposed statutory language to disallow a deduction for any expense for entertainment, amusement, or recreation unless the expense is described in one of a series of specific exceptions to the general rule. Where the expense is covered by an exception, the rules of existing law would continue to govern the deductibility of the expense.

To eliminate the harshness resulting from the House report, amendment of the language of the House bill is necessary. Despite amendment of the House bill your committee has made certain that entertainment expense abuses are eliminated. By your committee's amendment an alternative rule is added to the House bill under which expenses for entertainment, amusement, or recreation (with respect to both activities and facilities) also will be deductible to the extent that such expenses are associated with the active conduct of a trade or business. This new language will permit deduction of expenses for entertainment, amusement, or recreation incurred for the creation or maintenance of business goodwill without regard to whether a particular exception applies. However, this new language will apply only if the taxpayer demonstrates a clear business purpose and shows a reasonable expectation of deriving some income or other benefit to his business as a result of the expenditure. If he meets this test, the expenditure will be considered to be associated with the active conduct of his trade or business; otherwise, the expense will be disallowed under your committee's amendment.

With respect to disallowance of a deduction for gifts in excess of \$25, your committee has adopted the rule of the House bill but has modified the definition of "gift" for purposes of applying the limitation. Under the modified definition: (a) certain specialty advertising gifts, (b) advertising material for use in connection with the recipient's business, and (c) certain awards to employees costing not more than \$100, will not be taken into account in determining whether the \$25 limitation has been exceeded.

The requirements of the House bill regarding substantiation of claimed deductions for entertainment, amusement, or recreation expenses, gifts, and traveling expenses, have been approved without change.

The provision of the House bill which provided that expenses for meals and lodging included in the term "traveling expenses" were to be deductible only if "reasonable" has been clarified to assure that "traveling expenses" are not to include expenses for meals and lodging which are lavish or extravagant. In addition, your committee has added to the House-passed bill a new rule for the allocation of traveling expenses where the trip involves both business and pleasure. Under this rule, which would eliminate abuses involving tax deduction for vacation trips, if the trip is for more than 1 week and the personal

portion of the travel time is in excess of 25 percent of the total time away from home, the traveling expenses (including meals and lodging) must be allocated between business and pleasure and only the portion allocated to business will be deductible.

As amended by your committee, the provisions of this section of the bill are to apply to taxable years ending after December 31, 1962, but only with respect to expenditures incurred after that date.

C. General explanation of provision

Your committee's bill adds a new provision to the code (sec. 274), which disallows, in whole, or in part, certain expenses which would be fully deductible under present law. The requirements imposed by this bill are in addition to the requirements for deductibility imposed by other provisions of existing law, which must be met by the taxpayer before this new provision becomes operative. Hence, if an expenditure is claimed as a business expense deduction under section 162, the taxpayer must first establish that it constitutes an ordinary and necessary expense incurred in carrying on a trade or business, before the new provisions of this bill become applicable.

Since the only purpose of this section is to disallow deductions, it will not make deductible any expense which is disallowed under the "ordinary and necessary" test of present law. Moreover, this section does not affect the question of the includibility or excludibility of an item in income of any individual. The rules presently applicable under present law will continue to govern in this respect.

1. *Disallowance of expenses for entertainment activities.*—The first part of the provision provides that no deduction is to be allowed for any expense with respect to an activity which is of a type generally considered to constitute entertainment, amusement, or recreation, except to the extent that the taxpayer establishes that the expense was directly related to the active conduct of his trade or business, or that the expense was associated with the active conduct of his trade or business. Certain exceptions to this rule are provided, however, for expenses not required to meet the new tests. They are discussed in No. 6 below.

Entertaining guests at night clubs, country clubs, theaters, football games, and prizefights, and on hunting, fishing, vacation and similar trips are examples of activities that constitute "entertainment, amusement, and recreation." In addition, "entertainment" includes any business expense incurred in the furnishing of food and beverages, a hotel suite, a vacation cottage, or an automobile either to a customer (present or potential) or to any member of such a customer's family. If deduction is claimed for any expense for "entertainment, amusement, or recreation" the facts and circumstances of each particular case will determine the extent to which the expenses will be disallowed.

The trade or business of the taxpayer will determine whether an activity is of a type generally considered to constitute entertainment, amusement, or recreation. For example, with respect to a taxpayer who is a professional hunter, a hunting trip would not generally be considered a recreation-type activity. On the other hand, with respect to a taxpayer whose trade or business consists of selling machine tools or manufacturing clothing, a hunting trip generally would be considered a recreation-type activity. Similarly, attending a theatrical performance would generally be considered an entertain-

ment-type activity, but in the case of a professional theater critic, attending a theatrical performance would not constitute an entertainment activity.

An objective standard also will overrule arguments such as the one which prevailed in *Sanitary Farms Dairy, Inc.* (25 TC 463 (1955)) that a particular item was incurred, not for entertainment, but for advertising purposes. That case involved a big-game safari to Africa. The taxpayer argued successfully before the Tax Court that the expense of the hunt (including costs of making motion pictures which were later shown to customers and potential customers) were incurred solely for advertising purposes. Under the bill, if the activity typically is considered to be entertainment, amusement, or recreation, it will be so treated under this provision regardless of whether the activity can also be described in some other category of deductible items. This will be so even where the expense relates to the taxpayer alone.

Many entertainment expenses which have a business connection nevertheless will not be deductible. To justify their deduction, a taxpayer must establish that the incurring of the expenses relating to the entertainment activities was directly related to or associated with his effort to obtain new business or to encourage the continuation of an existing business relationship. This means that he must show a greater degree of proximate relation between the expenditure and his trade or business than is required under present law. To illustrate this principle, assume a taxpayer entertains a buyer and the buyer's family at lunch and the theater. Under existing law, he claims a deduction for the entire expense; under your committee's bill no deduction would be allowed for any portion of the expense attributable to the buyer's family since as to them he is unable to show a sufficiently close relationship between the expense and his trade or business.

It will not be sufficient that the entertainment expense is vaguely or remotely connected with a business motive; it must be demonstrated that the predominant purpose of the expense is to further the trade or business of the taxpayer. Where goodwill generated by the expense is vague or where the possibility of the expenditure resulting in the production of income is remote, no deduction will be permitted. For instance, under present law a taxpayer may deduct expenses of entertaining buyers and others associated with his trade or business even though at the time he does the entertaining he already has more business than he can handle. Under your committee's amendment, however, no deduction will be allowed because, with a large backlog of unfilled orders, such entertainment ordinarily cannot be regarded as being associated with efforts to produce income.

Under the bill, although deduction for entertainment expenses is restricted, such expenses will not be disallowed merely because they are incurred for the purpose of generating business goodwill. Goodwill has long been recognized as a legitimate objective of business entertaining and where the purpose of the expense and its clear relationship to a business is firmly established, the expense ordinarily will continue to be deductible. However, nothing in your committee's bill is to be construed as allowing a deduction for any expense which is against public policy or which violates the public conscience. Deducting an expense incurred for such purpose under the guise of generating "business goodwill" will not be condoned and under your

committee's amendment is not deductible. Thus, the cost of liquor purchased for the entertainment of customers and the promotion of goodwill (which under existing law has been held deductible) will be disallowed if the serving of liquor violates the public morals of the community as expressed in local law. Another example of expenses for immoral purposes which have been claimed on tax returns under existing law involves expenditures to provide "call girls" for the purpose of entertaining clients. Under your committee's amendment no deduction whatsoever is to be allowed for expenditures of this nature. In no legitimate sense are they "directly related to or associated with the active conduct" of a trade or business.

On the other hand, the following examples are indicative of circumstances under which entertainment expenses ordinarily will not be disallowed. Where the taxpayer conducts lengthy negotiations with a group of business associates and that evening the group goes to a night club, theater, or sporting event for relaxation, such entertainment expenses are regarded as directly related to the active conduct of business. Moreover, if a group of business associates with whom the taxpayer is conducting business meetings comes from out of town to the taxpayer's place of business to hold substantial business discussions, the entertainment of such business guests prior to the business discussions also is directly related to the conduct of the business. Similarly, if in between business meetings at a convention the taxpayer entertains his business associates attending such meetings, such expenses will be allowable.

Although your committee's bill permits entertainment expenses to continue to be deducted where a business purpose is shown, deduction will be limited to the portion of the expense which is directly related to or associated with business.

Objective standards will be employed to determine the apportionment between the part of the expense which meets either of these tests and the part which does not. Expenses not so related may not be deducted. Under this rule, if a taxpayer entertains a group of 10 individuals, 3 of whom are business prospects and 7 of whom are social guests, deduction will be allowed under the bill only for three-tenths of expenses incurred. Since the taxpayer's motive is not relevant to this determination, it would make no difference that the taxpayer in the above example would not have done the entertaining but for the attendance of the three business-related guests. This rule would disallow deductions for expenses in the following cases which, under existing law, are fully deductible:

A. Officer-shareholder and wife accompanied customer and wife to Las Vegas for 12-day vacation. Taxpayer paid the expenses for the four individuals. Officer-shareholder asserted that he would not have made the trip except for business purposes and that his wife's presence was required by the customer and his wife.

B. Officer-shareholder and his wife traveled to Alaska with customer and wife. Expense of wife was allowed based on representation that customer would not go without his wife and his wife would not go without such shareholder's wife.

C. Expenses for tractor demonstration attended by corporate taxpayer's principal officer-shareholder and his wife. A purported business reason for the wife's travel was established based on allowance of expenses for similar travel in the past.

In example A, no deduction would be allowed under your committee's bill because a vacation trip for a customer and his wife is not "directly related to the active conduct of the taxpayer's trade or business." In example B, deduction will be disallowed for expenses attributable to the taxpayer's wife and the customer's wife. In example C, no deduction would be allowed for expenses attributable to the taxpayer's wife.

D. Customers and their wives are entertained by taxpayer at Derby parties such as breakfasts and luncheons, etc.; by furnishing box seats and tickets for the Kentucky Derby; and entertainment at the Derby.

Under existing law, the entire amount expended was claimed as a deduction and was allowed. Under your committee's amendment, no deduction is permitted for expenses attributable to customers' wives because their connection with the taxpayer's trade or business is remote.

No deduction will be allowable under this provision for any "entertainment, amusement, or recreation" expenses which under the circumstances in which they are incurred are lavish or extravagant. This will be so even where a direct business purpose is firmly established. The application of this rule can be demonstrated by the following example:

E. The taxpayer, which is located in the midwest, asserted that lavish entertainment is essential in obtaining business and it established a Miami Beach residence for this purpose. The two principal officers and their wives are usually present at the residence when entertaining customers. Deductions allowed included depreciation on residence, food, liquor, boat expense and salaries of service employees and entertainment. Disallowance was made for amounts deemed to be personal expense.

Under the bill, no deduction would be allowed for any expenses attributable to the wives of either the principal officers or their customers (present or potential), or for any portion of the expenses incurred in example E which are lavish or extravagant. (The expenses of maintaining the residence are treated as expenses with respect to a facility, discussed in No. 2 below.)

Expenses for entertainment, amusement, and recreation should be identified by the taxpayer on his return and treated under the new rules of this bill. It will not be appropriate to include these expense items in other categories of business deductions, where their character will not be apparent, such as advertising, public relations, cost of goods sold, reimbursed expenses, etc. Failure to substantiate the claimed entertainment expenses by adequate records or other sufficient evidence may result in complete disallowance of the deduction.

2. *Disallowance of expenses for entertainment facilities.*—Your committee's bill (sec. 274(a)) also limits the deduction for expenditures incurred with respect to facilities used for entertaining. As in the case of expenses with respect to activities the new rules of this provision apply only if the expenses with respect to facilities qualify under existing law for deduction of business expenses. Moreover, these new rules establish additional tests which must be satisfied (in addition to the "ordinary and necessary" test of present law) in determining whether any deduction is to be allowed for expenses with respect to facilities. Under the bill, no deduction is to be allowed with respect to

expenses relating to facilities unless the taxpayer establishes (1) that the facility was used primarily for the furtherance of his trade or business and (2) that the expenditure was directly related to the active conduct of his trade or business, or that it was associated with the active conduct of his trade or business. In no event can the deduction exceed the portion of the expense which is directly related to (or associated with) the active conduct of the taxpayer's trade or business. Certain exceptions to this rule are provided, however, for expenses not required to meet the new tests. They are discussed in No. 6 below.

The term "facility" includes any item of personal or real property owned or rented by the taxpayer, such as a yacht, hunting lodge, fishing camp, swimming pool, tennis court, bowling alley, automobile, airplane, apartment, hotel suite, home in vacation resort, dining room, and cafeteria. In addition to items commonly regarded as expenses "with respect to a facility," such as expenditures for the maintenance, preservation, or protection of the facility, this provision also relates to depreciation and losses realized on certain sales of entertainment facilities.

Under the bill, if a facility is used more than one-half for business entertaining, so that more than one-half of the entertainment expense with respect to such facility would be deductible as a business expense under present law, that portion would continue to be deductible to the extent it meets the test of being directly related to (or associated with) the active conduct of the taxpayer's trade or business. If less than one-half of such entertainment expense would be deductible under present law, no deduction would be allowed. For example, if the taxpayer acquires a fishing camp which he uses almost exclusively for entertaining business guests, deduction of the expenses of the camp will be disallowed only to the extent that it was used for personal or other nonbusiness purposes. On the other hand, if he uses it almost exclusively for personal purposes, but occasionally takes business guests to the camp, no deduction is to be allowed. A further illustration of this rule is as follows:

A. The taxpayer corporation claims the purpose of maintaining a resort residence is to have a place available for business conferences. The resort residence has facilities for boating, fishing, and entertainment. It was established that the personal convenience, pleasure, and health of the chairman of the board of the taxpayer corporation was the principal reason for maintaining the residence. However, the evidence did indicate that there was some entertainment expense incurred for business purposes and a portion of the expense was therefore allowed.

Under the bill no deduction would be allowed in the foregoing example because the facts established that the primary use of the resort residence was not in furtherance of the taxpayer's trade or business.

Under this provision the facility must actually be used in furtherance of the taxpayer's trade or business; it is not sufficient that the facility is merely "available" for business use. And where the facility is one which is likely to serve the personal purposes of the taxpayer, it will be presumed that the facility was primarily used by the taxpayer for his personal purposes. To justify a deduction under such circumstances the taxpayer will have to clearly establish that the primary

use of the facility was not for his personal purposes but was directly related to or associated with the active conduct of his trade or business. The following example illustrates the operation of this rule:

B. Closely held corporate taxpayer located in midwest maintains a summer home in Maine. Principal stockholder and wife spend $2\frac{1}{2}$ months each summer at the Maine home and entertained high officials (and wives) of customers.

Under existing law the taxpayer in this case established that the summer home was used partly for business entertainment and was permitted to deduct a portion of the expenses attributable to the summer home. Under the bill, however, because the personal purposes of the principal stockholder are served by use of the corporation's summer home, it will be presumed that his personal purposes were primarily served by such use.

These rules will prevent tax abuses involving the use of luxury facilities for entertainment, amusement, or recreational purposes. Under these rules a taxpayer who lives in a luxurious apartment and who presently deducts a portion of its rent on the ground that the apartment is used for occasional entertaining of business guests (and thus has a business purpose), no longer will be able to deduct any portion of the rent because the principal purpose of the apartment is personal, rather than business. Moreover, a swimming pool constructed at the taxpayer's residence may not be charged off for tax purposes as an ordinary and necessary business expense because such a facility is presumed to be used primarily for personal, family or living purposes unless the taxpayer can establish by a preponderance of the evidence that it was used principally in connection with his trade or business.

As in the case of activities described above, no deduction will be permitted for lavish or extravagant expenses incurred with respect to facilities. This means that luxurious resort facilities maintained for the purpose of entertaining will no longer be fully deductible. This rule is illustrated as follows:

C. Taxpayer, a domestic manufacturing corporation, owns luxurious facilities on a subtropical island. The principal use of the property is for entertainment of executives and key personnel of customer firms. Fishing cruisers are maintained and air transportation furnished guests. The chairman of the board, who is the controlling stockholder, and other officers and key employees accompanied by their families spent considerable time at the island.

Under existing law the entire amount expended for maintenance of the resort and the airplanes (other than adjustments for amounts considered personal expenses of officers and employees) is deductible. Under the bill no deduction would be allowed for any expense which under the circumstances is either lavish or extravagant. Moreover, no deduction will be allowed with respect to expenses attributable to a member of the customer's (present or potential) family but the family's use of the facility will be considered in determining whether the use of the facility is primarily for personal purposes. In addition, as indicated in the portion of this report describing the deductibility of expenses for entertainment activities, expenses for vacations for customers may not be deducted. Where the expenses with respect to the facility are for "vacations," they will be disallowed under your committee's bill.

Club dues and fees paid to any social, athletic or sporting club or organization are treated by the bill as an expense with respect to a facility used for entertainment and therefore will not be deductible where the primary use of the club facilities is personal. If membership entitles the member's entire family to use the facilities of the club, their use as well as his will be considered in determining whether business use of the club exceeds personal use. Where the primary use of the club facilities is in furtherance of a trade or business the cost of the club dues or fees will be deductible to the extent of the use directly related to (or associated with) the active conduct of business. Thus, if membership in a club costs \$100 per year and the club is used for such clear business purposes three-fourths of the time, \$75 will be deductible. As in the case of other facilities, it is the actual use of the club which establishes the deductibility of the club dues, not its availability for use, and not the taxpayer's principal purpose for joining the club. However, this does not mean that out-of-pocket business entertainment expenses incurred at a club will not be deductible where the required relationship between the entertainment and the taxpayer's trade or business is shown to exist. Such expenses will be deductible under the rules applicable to entertainment activities without regard to the tax treatment of club dues.

Club dues for this purpose do not include dues or fees paid for membership in such civic organizations as Kiwanis, Lions Club, Rotary, Civitan, and similar groups because these organizations are not social, athletic or sporting clubs. Similarly, professional associations such as bar associations and medical associations are not considered social, athletic or sporting clubs. Deductibility of these dues will not be affected by the new rules of this bill, but will continue to be governed by the rules of existing law.

3. *Business gifts*.—Under the bill, deduction for business gifts will be disallowed to the extent that the total gifts during the year exceed \$25 with respect to any person. Where gifts are made to the wife of a man who has a business contact with the donor, these gifts are considered as made indirectly to the husband (for purposes of the limitation).

However, your committee has modified the definition of "gift" contained in the House provision so that items of a clear advertising nature which cost \$4 or less will not be required to be taken into account in applying the \$25 limitation. The purpose of this modification is to assure that businessmen who advertise their products or services by means of gifts of small value, commonly described as specialty advertising, may continue to do so without being burdened with the maintenance of detailed records of the amount of specialty advertising used with respect to each business prospect. This exception which includes such items as pens, desk sets, and plastic bags and cases, will apply only if the donor's name is clearly and permanently imprinted on the article.

Another modification of the definition of "gift" involves items such as signs, display racks, or other promotional material donated to a retailer by a producer or wholesaler for use on the business premises of the retailer. This material, generally referred to as point-of-purchase advertising, is not a gift; it is simply a form of advertising used right in the store to aid in the marketing process. As in the case of specialty advertising referred to in the preceding paragraph,

this exception for point-of-purchase promotional devices used in normal business operations will eliminate the necessity of manufacturers or wholesalers (who donate the promotional material to retailers) maintaining detailed records and accumulating costs of promotional material with respect to each donee.

The third modification of the definition of "gift" excludes items of tangible personal property which have a cost to the taxpayer of \$100 or less if the item is awarded to employees by reason of length of service or for safety achievement. It is a common practice of many employers to give such items as pins or watches to employees upon their completion of a specified number of years of satisfactory employment or in recognition of some safety achievement. Your committee felt that gifts for these purposes which serve to strengthen the relationship between business and its employees should not be discouraged by the tax law. This exception will permit the practice to continue under the rules of existing law.

There is the possibility of overlapping application of the entertainment expense and gift provisions in this new section. An item which might be held to be a gift might also be held to be an entertainment expense. For example, tickets to a theater might fall in either category. Since different rules will apply depending upon the category in which the expense item falls, specific regulatory authority is given to the Secretary of the Treasury or his delegate to prescribe, in cases where both provisions would otherwise apply, which provision is to govern. Thus, a "gift" of theater tickets probably would be classified as coming under the entertainment provision, while a book probably would be classified as coming under the gift provision.

4. *Allocation of traveling expenses.*—Your committee has added to the House bill a provision which will require taxpayers to allocate traveling expenses (including meals and lodging) between the portion of a trip which is for a business purpose and the portion which is for pleasure. This new rule will eliminate, in many cases, the "but for" rule of existing law under which a taxpayer is permitted to deduct his entire traveling expenses (even where a substantial portion of the time away from home is for purely personal purposes) if he is able to establish that the primary purpose of the trip was connected with a trade or business. This amendment will eliminate abuses whereby taxpayers often arrange vacations to coincide with a business trip so that they thereby, in effect, obtain a deduction for the vacation travel. However, to insure that this new rule will not impose unreasonable burdens on taxpayers to allocate trips between business and personal purposes where the duration of travel is only for a short period, your committee has provided that the allocation rule is not to apply where the period the taxpayer is away from home does not exceed 1 week, or where the time spent on the personal portion of the trip is less than 25 percent of the entire period the taxpayer is away from home on the trip. Where no allocation is required to be made, deduction of traveling expenses will continue to be governed by the primary purpose test of existing law.

5. *Disallowance of expenditures not substantiated.*—Under the bill, taxpayers will be required to substantiate their entertainment and related expenses, their traveling expenses and gift expenses. The bill provides that the taxpayer must substantiate by adequate records or by other sufficient evidence corroborating his own statement: the

amount of such expense or other item; the time and place of the travel, entertainment, amusement, recreation, or use of the facility, or the date and description of the gift; the business purpose of the expense; and the business relationship to the taxpayer of the person entertained, using the facility, or receiving the gift.

This provision is intended to overrule, with respect to such expenses the so-called *Cohan* rule. In the case of *Cohan v. Commissioner*, 39 F. 2d 540 (C.A. 2d, 1930), it was held that where the evidence indicated that a taxpayer had incurred deductible expenses but their exact amount could not be determined, the court must make "as close an approximation as it can" rather than disallow the deduction entirely. Under your committee's bill, the entertainment, etc., expenses in such a case would be disallowed entirely.

The requirement that the taxpayer's statements be corroborated will insure that no deduction is allowed solely on the basis of his own unsupported, self-serving testimony. However, the degree of corroboration required to support a claimed deduction will vary as respects the business relationship and purpose, the time and place, and the amount of the expense. Thus, oral testimony of the taxpayer together with circumstantial evidence available, may be considered "sufficient evidence" for the purpose of establishing the business purpose required under the new provision. However, oral testimony of the taxpayer plus more specific evidence would be required to be "sufficient evidence" as to the amount of an expense.

Generally, the substantiation requirements of the bill contemplate more detailed recordkeeping than is common today in business expense diaries. However, a clear, contemporaneously kept diary or account book containing information with respect to the date, amount, nature and business purpose of the expense may constitute an adequate record under this provision. Moreover, expenditures merely incidental to entertainment, travel, etc. (such as taxicab fares, tips, and similar payments) will be deductible if they are substantiated by such a diary, account book, or similar record.

The following example illustrates the operation of the requirements of this provision: Taxpayer establishes that he traveled from California to New York on business. He should retain receipts for his transportation and hotel expenses while in New York. However, expenses incidental to that trip such as taxicab fares, tips, business luncheons, etc. could be substantiated by entries in a diary.

Your committee does not intend by this substantiation requirement to deny a taxpayer deductions for entertainment, etc., expenses where he has no records if it can be shown that the failure to produce substantiating records was due to circumstances beyond his control, such as destruction of his records by fire or flood. In such a case, the taxpayer will be permitted to reconstruct the business entertainment, travel, or gift expenses incurred by him in the taxable year.

Under the bill, the Secretary or his delegate may, by regulation, prescribe certain situations in which the substantiation requirements will not be applied. For example, it may be provided that substantiation will not be required for traveling expenses, where such expenses (including the cost of meals and lodging) do not exceed prescribed minimum amounts. This will be of special benefit to employees whose per diem allowance while traveling is within limits established by the Secretary under this provision. Thus, if regulations are

issued under which substantiation will not be required for traveling or entertainment expenses where per diem allowances do not exceed 125 percent of per diem allowed a Government employee in the same locality, it would be sufficient evidence for purposes of the substantiation rule to establish only the amount of the allowance and the fact that the business travel occurred.

6. *Exceptions where disallowance provisions will not apply.*—The bill contains nine exceptions to the general disallowance provision described above under heading 1 or 2. Where an expense falls within one of the enumerated exceptions, the item will continue to be deductible to the same extent as allowed by existing law. However, the new substantiation requirements (discussed under heading 5) will have to be satisfied with respect to any such expense. The exceptions are as follows:

(a) Expenses for food and beverages furnished under circumstances which are of a type generally considered to be conducive to a business discussion. The question as to whether the circumstances are conducive to a business discussion are to be tested by such standards as: First, the surroundings in which the meal or beverage was furnished; second, the taxpayer's trade or business or income-producing activity; and third, the relationship to such trade, business, or activity of the persons to whom the food and beverages were furnished. Under this exception, the general custom of entertaining business guests at meals in restaurants and hotels would not be disallowed if they meet the ordinary and necessary test of existing law. This should leave undisturbed the most significant portion of goodwill entertainment conducted in this country. However, under this exception, it will not be possible to deduct luncheon expenses of a so-called reciprocity luncheon group under which a group of businessmen frequently lunch together and alternate in paying the check (and claiming it as a business expense deduction). This practice is not connected with a trade or business but is a personal or social expenditure which is not deductible under existing law.

(b) Expenses for food and beverages (and facilities used in connection with them) furnished on the business premises of the taxpayer primarily for his employees. This is intended to exclude from the disallowance provision such facilities as a company cafeteria or an executives' dining room. This exception would continue to apply even though guests are occasionally served in the cafeteria or dining room.

(c) Goods, services and facilities to the extent that the entertainment, amusement, or recreation (or use of the facility) is treated on the taxpayer's return with respect to the recipient of the entertainment as compensation paid to an employee and from which income tax is withheld. For example, if the taxpayer permitted an employee to use a yacht for a vacation and treated the expenses for its use as compensation paid to the employee for purposes of the withholding tax and for purposes of the taxpayer's tax return, maintenance and crew costs attributable to such use would be deductible in full because of this exception. On the other hand, where a yacht was used exclusively for business entertaining the salaries paid to the captain and crew, even though they were treated as compensation and withheld on, would not

come within this exception because they are not the recipients of the entertainment. Rather, the deductibility of the salaries would be determined under the general rule of the provision as an expense with respect to an entertainment-type facility.

(d) Expenses paid or incurred by the taxpayer where he pays or incurs the expenses for his employer or a client, customer, etc., and where he is reimbursed by the employer or client, etc. This is designed to prevent the double disallowance of a single expenditure, once to the employee or practitioner, etc., and a second time to the employer or client, etc. This provision will not apply, however, in the case of an employee where the employer treats the amount paid to him as compensation. It also will not apply in the case of a practitioner, etc., unless he accounts to the client, etc., for the expenses incurred. The accounting must represent sufficient substantiation to meet the tests set out under heading No. 5. Thus, if a lawyer enters into a fee arrangement under which his client agrees to reimburse him for expenses (including entertainment expenses) the exception will not apply unless he accounts to his client sufficiently to enable the client to substantiate the expenses as required by the bill.

(e) Expenses incurred for recreation, social, or similar activities (including facilities) primarily for the benefit of employees. The employees referred to in this case are those, other than officers, shareholders, or highly compensated employees. An individual would be considered a shareholder only if he (taking into account holdings of members of his family) holds an interest in the corporation of 10 percent or more. This category is intended to pertain to the usual employee fringe benefit programs, such as expenses of operating a company swimming pool or baseball diamond, as well as the expenses of the annual company picnic or Christmas office party.

(f) Expenses directly related to business meetings of the taxpayer's employees, stockholders, agents, or directors. While this category will apply to business meetings where some social activities are provided, it is not intended to apply to gatherings which are primarily for social purposes rather than for the transaction of the employer's or company's business.

(g) Expenses directly related and necessary to attendance at a business meeting of an organization, such as a trade association, chamber of commerce, real-estate board, etc., described in section 501(c)(6) of the code.

(h) Expenses for goods, services, and facilities made available to the general public by the taxpayer. This pertains to expenses for the entertainment of the general public by means of television, radio, newspapers, and the like. It also permits deductions for expenses for parks, etc., maintained by companies where the general public may attend. Expenses of distributing samples to the general public would also come within this exception.

(i) Expenses for goods or services (including the use of facilities) which are sold by the taxpayer in a bona fide transaction for an adequate and full consideration in money or money's worth. This exception is designed to insure that a taxpayer who sells entertainment to others will be allowed to deduct expenses of producing that entertainment. Thus salaries paid to employees

of nightclubs and amounts paid to performers other than employees will continue to be deductible by the operator. Moreover, since this type of expense is not considered to be "entertainment" the detailed substantiation requirements prescribed in this bill will not apply.

7. *Interest, taxes, casualty losses.*—The restrictions provided by the bill are not to apply with respect to items which are deductible under specific provisions of law which apply both to business and nonbusiness taxpayers. Thus, deduction for interest paid on a loan to acquire an entertainment facility or property taxes paid with respect to it would continue to be allowed as a deduction, whether or not the entertainment facilities meet the tests of the new provision.

8. *Treatment of entertainment-type facilities.*—Under the bill, if deductions with respect to entertainment-type facilities are disallowed, the disallowed portion is to be treated as an asset which is used for personal, living, and family purposes, rather than as an asset used in the trade or business. Under this provision the basis of such an entertainment-type facility will be adjusted for purposes of computing depreciation deductions and determining gain or loss on the sale of such facility in the same manner as other property (for example, a residence) which is regarded as used partly for business and partly for personal purposes. Thus, if a taxpayer has a yacht which is used three-fourths for direct business entertainment purposes, and he ordinarily would be entitled to \$1,000 for depreciation with respect to the yacht (if it were used entirely for business), \$250 of this amount would be disallowed as a depreciation deduction and would be included as a part of the basis of an asset not used in the taxpayer's business.

9. *Meals and lodging while in travel status.*—The bill, as amended by your committee makes clear that the deduction provided for traveling expenses by section 162(a)(2) of present law is not to include expenses for meals and lodging which are lavish or extravagant under the circumstances.

10. *Effective date.*—The amendments made by this provision are to apply with respect to taxable years ending after December 31, 1962, but only in respect of periods after that date.

V. DISTRIBUTIONS IN KIND BY FOREIGN CORPORATIONS

(Sec. 5 of the bill and sec. 301 of the code)

A. *Reasons for provision*

Under present law, when a distribution in kind is made by a corporation to a shareholder which is also a corporation, the amount which is treated as a distribution is the fair market value of the property received or, if lower, the adjusted basis of the property in the hands of the distributing corporation. Where both the distributing corporation and its corporate shareholder are domestic corporations, taking into account the adjusted basis when it is lower than the fair market value of the property may be justified on the grounds that the appreciated property is still owned by a corporation and, in fact, very little has happened. Furthermore, if the distributee corporation sells the property, the same amount of gain will be realized and taxed as if the distributor corporation had sold it. Where the distributing corporation is a foreign corporation, however, the device of distributing

to its U.S. corporate shareholder property which has appreciated in value can be used as a device to permit the U.S. corporation to realize on the earnings and profits of the foreign corporation at minimum U.S. tax. Assume, for example, that an American parent has a 100-percent owned foreign subsidiary. This foreign subsidiary has \$100,000 in accumulated earnings and profits resulting from foreign earnings, all of which enjoyed complete deferral from U.S. tax. Assume further that the foreign subsidiary is in a position to distribute to its American parent either \$50,000 in cash or a property having a fair market value of \$50,000 but an adjusted basis of only \$20,000. Under existing law, the dividend income to the American parent is \$50,000 if the cash is distributed but is only \$20,000 if the property is distributed. Under the amendment provided by this bill, however, the dividend income to the parent is the same amount (\$50,000) whether the cash or the property is distributed. This result is believed appropriate since the increase in value of the parent's assets is the same whether it receives the cash or the property.

B. Comparison of committee amendment with House provision

Your committee has retained the House provision with one modification. It has deleted the subsection in the House bill which, only for purposes of computing the allowable foreign tax credit, treats as the amount of the distribution the adjusted basis of the property which is distributed (where this is less than its fair market value). Your committee believes that since the distribution itself is to be taken into account at its fair market value, it would only be appropriate for purposes of determining the foreign tax credit, allowable with respect to this same distribution, to treat this distribution as sharing in the creditable foreign taxes in proportion to the fair market value of the distribution, rather than in proportion to its adjusted basis as under the House bill. This will maintain the current practice with respect to the valuation of the distribution, for purposes of allowing a foreign tax credit, in the case of those distributions in kind which under existing law already are taxed to the corporate recipients only at their fair market value.

C. General explanation of provision

This provision amends existing law (sec. 301(b)(1)(C)) to provide that where there is a distribution in kind from a foreign corporation and the shareholder is a corporation, then the amount of the distribution for dividend purposes is to be the fair market value of the property distributed, and not its adjusted basis in the hands of the distributor where that is lower.

An exception to the rule described above is provided where the distributing corporation, although a foreign corporation, during the 3 years ending with the close of the corporation's taxable year derived more than 50 percent of its income from sources within the United States. In such cases, to the extent that the income is subject to U.S. tax, the corporation receiving the dividend can continue to apply the rule generally available for domestic corporations. Thus, to the extent the dividend is treated as eligible for the 85-percent dividends received deduction, the amount of distribution will be the adjusted basis of the property to the distributing corporation where this is lower than its fair market value.

Your committee's amendment differs from the House bill in that, in computing the foreign tax credit allowable with respect to the distribution in kind, the distribution is to share in the creditable foreign taxes on the basis of its fair market value rather than in proportion to its adjusted basis, where this is lower. This continues the rule in present law which is that the amount considered to be a dividend also is the amount taken into account for purposes of allowing a foreign tax credit.

The bill also makes appropriate basis adjustments to take into account the changed rules with respect to dividend distributions.

The amendments made by this provision are to apply to distributions made after December 31, 1962.

VI. MUTUAL SAVINGS BANKS, ETC.

(Sec. 6 of bill and secs. 593, 595, and 7701(a) of code)

A. Reasons for provision

Until 1952 mutual savings banks, domestic building and loan associations, and certain cooperative banks (hereinafter referred to as mutual savings institutions) were exempt from Federal income tax. This exemption had initially been based upon the premise that the members' money in the case of these institutions was being used for loans to members, or that the institutions were in effect doing business with themselves and that since the earnings of the institutions belonged to the depositors rather than to them, there could be no profit on which to impose an income tax.

In 1951, however, Congress repealed the exemption of these mutual savings institutions and subjected them to the regular corporate income tax. At the same time, however, these institutions were allowed a special deduction for additions to bad debt reserves which proved to be so large that they have remained virtually tax exempt since 1951. The 1951 legislation provided that deductions could be made for additions to a reserve for bad debts in whatever amount the institution deemed appropriate so long as (1) the amount set aside each year did not exceed the taxable income (before this deduction) of the institution for the year, or (2) its total reserves and surplus did not exceed 12 percent of its deposits or withdrawable accounts at the close of the year.

The President, in his tax message of April 20, 1961, observed that—

Some of the most important types of private savings and lending institutions in the country are accorded tax deductible reserve provisions which substantially reduce or eliminate their Federal tax liability.

He further stated that—

These provisions should be reviewed with the aim of insuring nondiscriminatory treatment.

The Secretary of the Treasury in his appearance before your committee stated:

Under present law, mutual savings banks and savings and loan associations can deduct from their income amounts added to a reserve for bad debts until reserves, surplus, and

undivided profits equal 12 percent of deposits or withdrawable accounts. As a result, during the entire decade, 1952-61, all mutual savings banks and savings and loan associations paid total Federal income taxes of less than \$70 million, while at the same time they retained \$5.5 billion as additions to reserves, surplus, and undivided profits. From an economic and accounting point of view a large part of the untaxed additions to bad debt reserves constitutes net income which, were it earned by competing financial institutions, would be subject to corporate income tax.

Your committee has reviewed the tax treatment of the mutual savings institutions. It agrees with the House that the present bad debt reserve provisions are unduly generous and that they require revision.

B. Comparison of committee amendments with House provision

Your committee has retained the basic House provisions relating to deductible reserves for these mutual savings institutions but has reduced the reserve deduction for stock companies and has made a number of relatively minor modifications in the generally applicable reserve provisions which in large part are designed to restrict the reserves available. In addition, it has provided a new definition of domestic savings and loan associations, has removed certain excise tax exemptions presently available to these institutions, and made another amendment relating to the deduction of dividends paid to depositors.

The House bill amends the special bad debt provisions of existing law which are applicable to these mutual savings institutions to provide that they may add to these reserves for bad debts each year whichever of the following is the greatest:

(1) 60 percent of taxable income for the year computed before a bad-debt deduction,

(2) An amount sufficient to bring the balance of the reserve for losses on qualifying real property loans to 3 percent of such loans outstanding at the close of the taxable year, plus an amount sufficient to bring the balance of the reserve for losses on other loans to a reasonable amount, or

(3) If an institution demonstrates a need for a reserve greater than is permissible under (1) or (2), an amount sufficient to bring the overall balance of its reserves to a "reasonable" amount.

Your committee has amended the 60 percent of taxable income reserve addition referred to in No. (1), above, to provide that the amounts added to the reserve under this provision may not increase the reserve for losses on qualified real property loans to more than 6 percent of these loans. This amount, which is double the 3 percent referred to in No. (2), above, in your committee's estimation should provide an adequate protection against losses. Therefore, the deduction of any amount in excess of this is believed inappropriate.

Your committee also has adopted an amendment to provide that the deduction allowable under any of the three alternatives referred to above is not to be allowed to the extent it would increase the reserve for losses on qualifying real property loans together with the reserve for losses on nonqualifying loans and surplus, undivided profits, and reserves attributable to years beginning both before and after December 31, 1951, to more than 12 percent of total deposits or

withdrawable accounts. This 12-percent limitation is substantially the same as the restriction in existing law and has been added by your committee to give assurance that these mutual savings institutions will in no event receive deductions for building up reserves in excess of those allowable before the enactment of this bill.

The House bill provided that the reserve for losses on qualified real property loans at the end of 1962 was to be established out of existing reserves up to a level of 3 percent of the qualifying loans outstanding at that time. For this purpose only those reserves were to be taken into account which were attributable to years beginning after December 31, 1951, the year when these savings institutions first became taxable institutions. Your committee has concluded, however, that it is appropriate to take into account pre-1952 reserves to the extent necessary to obtain a 3-percent beginning reserve. In this regard it should be noted that Congress when it first made these institutions taxable in 1952 specified that the reserves then set up were to be made with "due regard" to the pre-1952 reserves. Your committee's amendments likewise provide that these reserves are to be taken into account for purposes of establishing the 3-percent reserve. However, recognizing that these amounts are attributable to periods before these institutions were taxable, your committee's amendments provide that these pre-1952 reserves are to be taken into account only in determining the balance in the reserve. Thus, if the institution believes that the reserves it needs are less than this 3 percent then, to the extent pre-1952 reserves were taken into account, these funds may be distributed to depositors or used for other purposes without tax effect. However, in applying the 3-percent limitation (in determining whether deductions are allowable) such amounts will be treated as if they were still in the reserve.

Your committee, recognizing the greater hazards of a new business, concluded that the 3-percent level of reserves, previously referred to, should appropriately be increased to 5 percent with respect to the first \$4 million of loans (a maximum increase in the reserves of \$80,000) during the first 10 years of mutual savings institutions' existence. This amount is not to be available to stock savings and loan associations.

Your committee has also considered the fact that stock savings and loan institutions, although having many of the same characteristics as the mutual savings and loan associations are, nevertheless, commercial enterprises more nearly comparable to banking institutions than are the mutual associations generally. For that reason, although these associations are generally allowed the same treatment as the mutual savings institutions, your committee concluded that it was appropriate to provide a somewhat lower maximum addition to reserves in the case of the stock companies. For that reason, it is provided that 50 percent of taxable income instead of 60 percent is the maximum addition to reserves that such companies may make under alternative No. (1) referred to above.

Your committee also has provided a new definition of domestic building and loan associations. The definition appearing in the House bill in general provided that substantially all of the business of the institution must consist of accepting savings and investing the proceeds in loans secured by residential real property and other loans to the extent authorized to be made by a Federal savings and loan

association under the Home Owners Loan Act. Your committee was concerned with the application of this definition because of the uncertainty as to what might be considered investing substantially all of the proceeds in residential real property. It also doubted the desirability of permitting the tax status of these institutions to turn, in part at least, upon the types of investments allowed them under the Home Owners Loan Act, which has different standards for determining allowable investment. In view of these considerations your committee has provided a more specific definition which, nevertheless, continues to require these institutions to devote most of their proceeds to home loans.

The definition provided by your committee in general provides that 90 percent of the total assets of the institution must be invested in loans secured by an interest in real property (or for certain other closely associated uses). It further provided that of this 90 percent of total assets, at least 80 percent (72 percent of total assets) must be invested in residential real property. Furthermore, 70 percent of this 90 percent (63 percent of total assets) must be invested in residential real property containing four or fewer family units. It is recognized that an institution may under special circumstances not be able to obtain loans on real property, residential real property or 1- to 4-family unit residential real property. Therefore, the new definition provides that cash and Government obligations to a limited extent may also qualify under any of the percentage requirements specified above. It is not intended, however, that cash or Government obligations be used as a means of expanding nonresidential loans beyond the difference between the 72 percent of total assets and the 90 percent of total assets (except to the extent cash and Government bonds are less than 10 percent of total assets) nor is it intended to permit the expansion of other than 1- to 4-unit residential loans beyond the difference between the 63 percent of total assets and the 90 percent of total assets (again except to the extent that the cash and Government obligations are less than 10 percent of total assets). Therefore, although the cash and Government obligations may be taken into account in determining qualification under the 72 percent or 63 percent limitations, this cannot be done in a manner which permits the expansion of the otherwise nonallowable loans above the difference between the 72 percent and 90 percent (namely, 18 percent of total assets) for other than residential loans and cash and government obligations) or the difference between the 63 percent and 90 percent (namely, 27 percent of total assets for other than for 1- to 4-family residential unit loans and cash and Government obligations), except to the extent that the cash and Government obligations are less than 10 percent. Also included are tract loans where the proceeds of the loan will be used for any of the categories specified, interests in such loans and improvements loans which are concerned with such property. In addition, your committee has provided that generally none of the assets of one of these savings institutions may be invested in the stock of any corporation other than that of an instrumentality of the United States or of a State or its political subdivision.

The House bill repealed exemptions granted Federal savings and loan associations from excise taxes on communications, and on transportation of persons. Your committee is in accord with the repeal of these exemptions but in addition has provided for the repeal of

exemptions from documentary stamp taxes provided for these savings institutions. However, it is made clear that the documentary stamp tax on the insurance or transfer of shares of stock is not to apply in the case of shares or certificates representing deposits or withdrawable accounts, which are comparable to bank accounts where no documentary stamp tax is applicable.

The final amendment made by your committee provides that dividends and interest paid by savings institutions which are chartered and supervised as savings and loan or similar associations under Federal or State law are to be deductible to the institution in computing its income subject to tax in the same way as interest on deposits is deductible to commercial banks. This is to be true whether or not the savings institution meets the definition provided by the tax law of a "domestic building and loan association."

C. General explanation of provision

1. *Additions to reserves for losses on loans.*—In the case of mutual savings institutions the bill provides new rules for calculating the deduction allowable for additions to bad-debt reserves, or "reserves for losses on loans" as they are referred to in the bill. Beginning in 1963, these institutions will maintain two accounts to which additions will be made in the future with respect to reserves for bad debts.¹ One of the two accounts is a reserve for "losses on qualifying real property loans," the additions to which can be determined by the taxpayer under rules set forth in the bill. The other is a reserve for "losses on nonqualifying loans."

Additions to this latter account are required to be "reasonable additions," which means that, as in the case of other taxpayers, additions to these reserves will be determined upon the basis of the past experience and other appropriate factors.

In the case of the reserve for losses on qualifying real property loans, the addition to be made each year to this reserve is to be determined by the taxpayer but may not exceed whichever of the following is the largest:

(a) 60 percent of the institution's taxable income for the year computed before this deduction (minus the amount added to the reserve for losses on nonqualifying loans). This may not exceed an amount necessary to increase the balance of the reserve for losses on qualifying real property loans to 6 percent of these loans. Also, in the case of stock savings and loan associations, the deduction, instead of being 60 percent of taxable income, is to be 50 percent of this income;

(b) the amount necessary to increase the balance in the reserve for losses on qualifying real property loans to 3 percent of such loans outstanding at the close of the taxable year. For new mutual (but not stock) companies (in their first 10 years of existence) this 3 percent is increased by 2 percent, but only with respect to loans not in excess of \$4 million (a maximum special reserve addition of \$80,000);

(c) if the institution demonstrates the need for greater reserves than are permitted under (a) or (b) above, an amount which would be permitted to be added to the reserve for losses

¹ They may also have a supplemental reserve which will represent certain reserves built up in the period from 1952 through 1962. This supplemental reserve is explained below.

on qualifying real property loans without regard to the special provision for mutual savings institutions.

Your committee's amendments provide that the total amount added to the reserve for losses on qualifying real property loans (determined under (a), (b), or (c) above) plus the amount added to the reserve for losses on nonqualifying loans may not exceed the amount which brings the combined balance of these reserves and surplus, undivided profits and reserves (whether accumulated before or after December 31, 1951), to an amount equal to 12 percent of total deposits (or withdrawable accounts).

When losses on loans are realized they will be charged to the appropriate account within the general reserve for bad debts. That is, losses on loans with respect to qualifying real property will be charged to the reserve for such loans and losses on nonqualifying loans will be charged to the reserve for losses on such loans.²

The reserves which are required by the bill to be established—that is, the reserve for losses on qualifying real property loans, the reserve for losses on nonqualifying loans, and the supplemental reserve for losses on loans—are required to be treated as bad-debt reserves for all tax purposes (except that no deduction is allowed for any addition to the supplemental reserve). Thus, although these reserves are termed reserves for “loans,” they are reserves for bad debts; and any charge to any such reserve for an item other than a bad debt will result in the inclusion in gross income of an amount equal to such charge.

For purposes of determining annual additions to the reserve for losses on qualifying real property loans, mutual savings institutions are to take into account all loans secured by improved real property (whether such loans are insured or uninsured) except Government bonds, certain corporate obligations and certain loans between banks and related parties. Under this provision, both federally insured FHA and guaranteed VA home loans, as well as conventional loans, may be taken into account in determining the amount of additions to the reserve for losses on qualifying real property loans. Loans on improved real property are intended for this purpose to include loans obtained for the construction of improvements on real property, even though at the time the loan is made no improvements may exist on the property.

The following examples illustrate the operation of the alternative choices for additions to reserves for bad debts:

Example 1: At the close of its taxable year, X, a mutual building association in existence for more than 10 years, has improved real property loans outstanding of \$2,000 and nonqualified loans of \$200. Its taxable income before any addition to a reserve for bad debts is \$50. The balance in its reserve for losses on improved real property loans is \$51 and the balance in its reserve for losses on nonqualifying loans is \$1. (Its experience indicates the need for a reserve for losses on nonqualifying loans of 1 percent of such loans, and a reserve for losses on improved real property loans of 2.5 percent of such loans.)

For this year X would be permitted to add to its reserves \$30 (60 percent times \$50). (Under the 3-percent method only \$10 could have been added, \$1 to the nonqualifying loan reserve and \$9 to the qualifying loan reserve.) Of this amount, \$1 would be added to the

² At the election of the taxpayer, losses on any loan instead of being charged to the reserve referred to above may be charged in whole or in part to the supplemental reserve for losses on loans referred to below.

reserve for losses on nonqualifying loans (making the balance in that account \$2) and \$29 would be added to the reserve for losses on improved real property loans (making the balance in that account \$80). Taxable income for this year would then be \$20.

Example 2: Assume the same facts, except that taxable income before any addition to reserve for bad debts is \$15. X would be permitted to add to its reserves \$10. This is the amount necessary to bring the balance of the reserve for losses on nonqualifying loans to \$2 (1 percent times \$200) plus the amount necessary to bring the balance of the reserve for losses on improved real property loans to \$60 (3 percent times \$2,000). (Under the 60-percent method the addition would have been only \$9.) Taxable income would then be \$5 (\$15 minus \$10).

2. *Treatment of pre-1963 reserves.*—At the present time bad-debt reserves, etc., of mutual savings banks on the average are about 10 percent of their deposits, while similar reserves of domestic building and loan associations average about 8 percent of deposits. This means that existing reserves of these mutual savings institutions in most cases will exceed 3 percent of qualifying real property loans, plus a reasonable reserve for other loans.

The bill makes special provision for the treatment of existing bad-debt reserves of mutual savings institutions. If the entire amount of such reserves (called "pre-1963 reserves" in the bill) were required to be allocated to the reserve for losses on qualifying real property loans and to the reserve for losses on nonqualifying loans, the balances of those reserves would in many cases be so large that many mutual savings institutions would be denied a deduction for additions to bad-debt reserves for many years. In order to mitigate this effect, your committee's bill provides that only a portion of such pre-1963 reserves is to be allocated to the reserve for losses on qualifying real property loans and to the reserve for losses on nonqualifying loans, under the following rules:

(a) First, there is credited to the reserve for nonqualifying loans whatever portion of these pre-1963 reserves is necessary to bring the balance of this reserve to an amount which would be reasonable on the basis of nonqualifying loans outstanding as of December 31, 1962;

(b) Next, there is credited to the reserve for losses on qualifying real property loans whatever remaining portion of the pre-1963 reserves is necessary to bring the balance of this reserve up to 3 percent of loans on improved real property outstanding as of December 31, 1962, or to a greater amount if the experience of the institution as of December 31, 1962, indicates a need for a greater reserve; and

(c) Finally, any remaining pre-1963 reserves are credited to the supplemental reserve for losses on loans.

Amounts credited to the supplemental reserve for losses on loans can be used only to offset losses on loans (if the institution chooses to charge losses to this reserve). Any other use of this reserve will result in the inclusion in gross income of the charge. In determining the amount of these pre-1963 reserves the House bill provided that accumulations in reserves were to be taken into account only for years after December 31, 1951. Your committee's amendments provide that pre-1952 reserves also are to be taken into account in establishing

the 3-percent opening balance in the reserve for qualifying real property loans, but that the amount added to the reserves attributable to this pre-1952 period may be distributed to depositors or otherwise used by the institution so long as this amount continues to be taken into account in determining the balance at any time in this fund.

3. *Distributions to shareholders.*—Some of the savings and loan associations to which this provision is applicable have shares of stock outstanding (which are not withdrawable shares). The bill provides that in the case of distributions to these stockholders, the amounts are to be considered as paid out of the following funds of the institution:

(a) First, out of earnings and profits accumulated in taxable years beginning after December 31, 1951;

(b) Then out of the reserve for losses on qualifying real property loans (but only to the extent the balance in this reserve exceeds the amount which would have been allowed the institution in the absence of the special reserve provision);

(c) Next out of the supplemental reserve for losses on loans; and

(d) Finally, out of other amounts.

Before distributions can be made out of either the reserve for losses on qualifying real property loans or out of the supplemental reserve, the amount required to be charged by the stock institution must be included in its gross income for tax purposes. The amount required to be charged to either of these reserves and included in income is the amount of the distribution to the stockholder "grossed-up" by the appropriate amount of tax. These special rules will insure that any amount distributed to stockholders out of amounts charged to these reserves which was not previously taxed will be subjected to the regular corporate income tax at the time of distribution.

4. *Foreclosures on property securing loans.*—The bill also adds a new provision to the code containing rules to govern the tax consequences of mortgage foreclosures (or other similar proceedings) in which a mutual savings institution takes over property which was security for its loan. Under existing law the foreclosure event is considered a taxable transaction. This has been interpreted to mean that a bad-debt deduction may or may not arise at that time, depending upon the relation of the bid price of the property to the amount of the loan outstanding. Where the foreclosed property is bid in for the amount of the loan a bad debt deduction may not be taken under present law; however, a gain or loss may result at the time of foreclosure if the fair market value of property foreclosed is different from the price at which it was bid in. When the property is subsequently sold by the mutual savings institution, it may realize a further gain or loss on such disposition. Whether the gains and losses at the time of foreclosure and at the time of ultimate disposition are capital or ordinary gains and losses depends on the nature of the activities of the institution at each such time.

The bill seeks to avoid these erratic results by providing that in the future a foreclosure is not to be treated as a taxable event, and that amounts received by the mutual savings institution subsequent to the foreclosure are to be treated as payments on the indebtedness. This would be accomplished under the bill by treating the property received in a foreclosure (or other proceeding) as having the same characteristics as the debt for which it was security. Thus, for bad-

debt (or loss) purposes the act of foreclosure will not create a taxable occasion; however, if the property has depreciated in value, the decline may be charged against the bad-debt reserve as a partially worthless debt. If it continues to decline in value, additional charges may be made against the reserve. When the property is ultimately sold or disposed of, the difference between any amount realized and the original or previously reduced debt, is to be treated as ordinary loss or income and is to be charged, or credited, as the case may be, against the reserve for losses on qualifying real property loans. Because the foreclosed property is to have the same characteristics as the indebtedness, where property is rented by the mutual thrift institution after foreclosure, no depreciation deduction is to be permitted. However, as explained above, if the property actually depreciates in worth (as contrasted to a mere decline in book value), a charge may be made against the reserves.

5. *Definition of domestic building and loan association.*—Under present law “domestic building and loan association” is defined to mean a—

domestic building and loan association, a domestic savings and loan association, and a Federal savings and loan association, substantially all of the business of which is confined to making loans to members.

Problems have arisen with this definition because loans in many cases now are in substance not loans made to members. It is understood that technical conformance has been maintained with the membership requirement of present law by making borrowers of funds members of the institutions. However, questions have arisen as to the substance of such provisions.

As a result, your committee has concluded that the definition of a domestic building and loan association, eligible for the tax treatment described above, should be brought more nearly into conformance with actual practice. At the same time it was deemed desirable to restrict this tax treatment to those primarily engaged in making residential real estate loans, with special emphasis on 1- to 4-family units, and omitting from the definition cases such as those where these institutions have been used for speculative purposes.

In view of these considerations, your committee has redefined a domestic building and loan association to mean a building or savings and loan association which is an insured institution within the meaning of section 401(a) of the National Housing Act or one which is subject by law to supervision and examination by State or Federal authority having supervision over such associations. In addition, however, the bill provides that an institution in either of these groups qualifies only if substantially all of its business consists of accepting savings and investing in loans secured by or for the improvement of real property of the type described below. This restriction will, of course, prevent such a savings institution from carrying on the business of brokering mortgage paper if this represents any substantial part of its business. It is not intended, however, that this prevent necessary borrowings from Government agencies such as HOLC.

A third restriction on qualified domestic building and loan associations requires them to invest at least 90 percent of their assets in—

(a) Cash,

(b) Obligations of the United States or of a State or local government and stock or obligations of a corporate instrumentality of the United States or of a State or local governmental unit,

(c) Loans secured by an interest in real property including so-called improvement loans,

(d) Loans secured by a deposit (or share) of a member, and

(e) Property acquired through default of real property loans.

Of the 90 percent of total assets referred to above, at least 80 percent (72 percent of total assets) must be invested in residential real property loans (including improvement loans for such property and tract loans which will be used for such property) or in cash or Government obligations (referred to in (a) and (b) above). In addition, at least 70 percent of this 90 percent of total assets (63 percent of total assets) must be invested in residential real property representing 1- to 4-family units (or loans made for the improvement of such property or tract loans on such property) or in cash or Government obligations (as referred to in (a) and (b) above). The bill also provides that no more than 18 percent of the total assets of an association may be invested in other than residential real property loans, cash, and Government obligations except to the extent that cash and governmental obligations are less than 10 percent of total assets. Similarly the bill provides that no more than 27 percent of the total assets may be invested in other than 1- to 4-family-unit residential real property loans, cash, and Government obligations, again except to the extent that cash and Government obligations are less than 10 percent of total assets. One further requirement provides that none of the assets of the association may be invested in stock of any corporation other than stock of a corporate instrumentality of the United States, a State or local governmental unit, or stock acquired through defaults.

6. *Repeal of certain excise tax exemptions.*—Under present law, Federal savings and loan associations are exempt from the excise taxes on communications and the excise tax on transportation of persons. These exemptions were granted by the Home Owners' Loan Act of 1933. Your committee's version of the bill repeals these exemptions effective as of December 31, 1962. In addition, the amendments made by your committee delete the exemptions from the documentary stamp taxes on stocks and certificates of indebtedness under existing law in the case of domestic building and loan associations, savings and loans associations, cooperative banks, and homestead associations. The exemption from the stock issuance or transfer taxes is continued, however, in the case of domestic building and loan associations and cooperative banks insofar as these taxes relate to stock representing deposits or withdrawable accounts.

7. *Deduction for dividends paid on deposits.*—Your committee has also provided for a deduction for dividends or interest paid by savings institutions chartered and supervised as savings and loan or similar associations under Federal or State law even though they do not come within the definition of domestic building and loan associations. This deduction is available only in the case of amounts paid to depositors or those having withdrawable accounts.

8. *Effective date.*—The new rules provided by the bill for additions to reserves for bad debts are to apply to taxable years ending after December 31, 1962. However, the bill provides a special rule to deal with fiscal years where a taxpayer has a year which begins in 1962

and ends in 1963. The effect of this special rule is to continue the rules under existing law up to the end of December 1962, and to apply the new rules as of January 1, 1963.

The tax treatment provided for property acquired in mortgage foreclosure proceedings is to apply to transactions occurring after December 31, 1962, in taxable years ending after that date. The new definition of domestic building and loan associations is to be effective for taxable years beginning after the date of the enactment of the bill. The repeal of the exemptions from excise taxes on communications and on transportation of persons in general is made effective as of January 1, 1963.

VII. DISTRIBUTIONS BY FOREIGN TRUSTS

(Sec. 7 of bill and secs. 643, 665, 666, 668, 669, 6047, 6677, and 7701 of code)

A. Reasons for provision

Certain tax avoidance possibilities exist under present law in connection with foreign accumulation trusts created by U.S. citizens or residents. The avoidance device involves the establishment of trusts for the benefit of U.S. beneficiaries by a U.S. grantor (or settlor) in a foreign country where the income of such trust is subject to little or no tax. The trust corpus may consist of foreign securities so that the income can be accumulated in the trust free of any U.S. tax for any number of years. In addition since these trusts are formed in countries which impose little or no tax on such income, no tax at all is likely to be paid. When the trust terminates and distributes the accumulated income and corpus to the U.S. beneficiaries, such distributions may be subject to no U.S. tax, or be subject to tax on only a small portion of the distributions.

Under present law, where a domestic trust is established for the purpose of accumulating income for a period of years the trustee pays a tax currently on the income accumulated at the same rates applicable to individuals. In general, when a beneficiary receives a distribution from the trust, in excess of the currently distributable net income (if the amount exceeds \$2,000), it is taxed to him to the extent it represents income accumulated by the trust in any of the preceding 5 years. The tax on such amounts is payable currently, but is computed as if the beneficiary had received a distribution of this income in each of these 5 prior years in which the income was earned, with a credit being allowed for the taxes paid by the trust with respect to such income.

The above rule, known as the "5-year throwback rule", is also applicable to distributions made by foreign trusts to U.S. beneficiaries. However, it frequently does not result in a tax on the distributions. First of all, it does not in any case apply to any income accumulated for more than 5 years. In addition, there are a number of exceptions making distributions nontaxable to the beneficiaries even where they are attributable to the 5 immediately preceding years. For example, the 5-year throwback rule does not apply to accumulations for the benefit of a minor beneficiary; accumulations distributed to a beneficiary upon reaching a specified age if not more than four such distributions can be made or the distributions are at least 4 years apart; and distributions to a beneficiary where a trust terminates and makes a

final distribution which occurs more than 9 years after the date of the last transfer to the trust. As a result of these exceptions, and the 5-year limitation, it is relatively easy for U.S. grantors or settlors to establish foreign trusts in such a way that they pay little or no tax on trust income and which upon termination make distributions to American beneficiaries with little or no U.S. tax being paid.

In the last Congress, a bill (H.R. 9662) which was passed by the House, but on which action was not completed by the Senate, contained an amendment added by your committee designed to discourage the creation of foreign trusts for the purpose of avoiding U.S. tax. In addition, the Secretary of the Treasury in testimony last year recommended that with respect to existing trusts the law be modified so that distributions to a U.S. beneficiary from a foreign trust would be subject to tax in the year of distribution in an amount equal to the tax which would have been imposed had the income been distributed currently. This is in effect an extension of the existing 5-year throwback rule.

In view of the existing avoidance possibilities with respect to these foreign trusts, your committee agrees with the House that American beneficiaries of foreign trusts created by U.S. grantors, settlors or transferors should be taxed in substantially the same manner as if the income had been distributed to the beneficiary currently as earned (although a "shortcut" method of computation may be elected by the taxpayer in place of this more "exact" method). This provision is not viewed by your committee as imposing a penalty but rather as a method for placing U.S. beneficiaries of foreign accumulation trusts created, or added to, by Americans in substantially the same way as the beneficiaries of domestic trusts distributing their income currently.

B. Comparison of committee amendments with House provision

With the exception of the two relatively minor amendments described below, your committee's bill retains the provision of the House bill without change.

The attention of your committee was called to the fact that under the House bill where there was a foreign trust to which both U.S. persons and foreign persons contributed money or property, a U.S. beneficiary receiving a distribution from such a trust would be taxable on the entire amount of the accumulated income. It is believed that the purpose of the provision was to subject to taxation distributions from foreign trusts only to the extent that the corpus was contributed by U.S. persons. Accordingly, your committee's bill amends the definition of the term "foreign trusts created by a U.S. person", so that it will apply only to the extent that money or property is transferred (directly or indirectly) by a U.S. person, or under the will of a decedent who was a U.S. citizen or resident at the time of his death. Hence, where a foreign trust is created to which U.S. persons and foreign persons both contributed money or property, the U.S. beneficiary will be taxed only to the extent the distribution is attributable to money or property (including earnings thereon) contributed by the U.S. person.

Under the House bill, the new provisions would apply with respect to distributions made in taxable years of trusts beginning after the date of enactment of this bill. In the case of a calendar year foreign

trust, the new rules would not be applicable to distributions made prior to the end of the current year, whereas they may apply sooner to foreign trusts operating on a fiscal year basis. In order to equalize the tax consequences with respect to all foreign trusts, your committee amended the effective date provision to make the new rules applicable with respect to all distributions made after the date of enactment of the bill.

C. General explanation of provision

The bill, as amended by your committee, provides for taxing American beneficiaries on distributions received from foreign trusts which are created by U.S. grantors, settlors, or transferors in substantially the same manner as if the income had been distributed to the beneficiary currently as earned, instead of being accumulated in the trust. The bill, in effect, eliminates the 5-year limitation and all the exceptions applicable to domestic trusts, and provides an unlimited throwback rule with respect to distributions from foreign trusts. However, only distributions of income accumulated after the effective date of the 1954 Code will be subject to the new provisions.

The new provision applies to foreign trusts to the extent money or property has been transferred, directly or indirectly, by U.S. persons or under the will of a decedent who was a U.S. citizen or resident. A foreign trust for this purpose is one the income of which from sources without the United States is not includible in gross income for U.S. tax purposes. The term "U.S. persons" as used here includes U.S. citizens or residents, domestic partnerships and corporations, and estates and trusts.

In the case of these foreign trusts, all of their accumulated income, other than income distributable currently, upon distribution to a U.S. citizen or resident is to be taxed to him. The amounts distributed to the U.S. beneficiary are treated as if they had been distributed in the preceding years in which income was accumulated, but are includible in income of the beneficiary for the current year. However, under the bill the tax on such amounts may be computed, at the election of the beneficiary in either of two ways. One method, referred to here as the "exact" method, is substantially the same as the method provided under present law in the case of distributions subject to the "5-year throwback rule." The other is a "shortcut" method which the beneficiary may elect if he does not desire to go through the more extensive computations required by the exact method.

Under the exact method of computation, the tax on the amounts distributed cannot exceed the aggregate of the taxes that would have been payable if the distributions had actually been made in the prior years. This method requires complete trust and beneficiary records for all past years, so that the distributable net income of the trust can be determined for each year, as well as the years in which trust income was accumulated. The beneficiary's own tax then is recomputed for these years, including in his income the appropriate amount of trust income for each of the years (including his share of any tax paid by the trust). Against the additional tax computed in this manner the beneficiary is allowed a credit for his share of the taxes paid by the trust, including a foreign tax credit for income taxes paid foreign countries. Any remaining tax then is due and payable as a

part of the tax for the current year in which the distribution was received.

The so-called short-cut method in effect averages the tax attributable to the distribution over a number of years, equal to the number in which the income was earned by the trust. This is accomplished by including, for purposes of tentative computations, a fraction of the income received from the trust in the beneficiary's income for the current year and each of the 2 immediately prior years.¹ The fraction of the income included in each of these years is the same as the number of years in which the income was accumulated by the trust. Thus if the accumulated income is attributable to 10 different years (although the trust may have been in existence over longer than a 10-year period, however), then one-tenth of the amount distributed would be included in the income of the current year and one-tenth in each of the 2 prior years. The additional tax is then computed with respect to these 3 years and the average additional tax for the 3 years determined. This average is then multiplied by the number of years to which the trust income relates, namely 10 in the example used here. The tax so computed may be offset by a foreign tax credit for any foreign taxes paid by the trust and any remaining tax liability is due and payable in the same year as the tax on the beneficiary's other income in the year of the distribution.

The bill provides certain exceptions from the two computation methods outlined above. First, if the shortcut method is used and the number of trust years to which the income relates is less than 3, then the average is determined on the basis of any smaller number of years to which the distribution actually relates. Second, if the beneficiary was not yet born, with respect to a year to which part of the trust income which is distributed relates, the so-called exact method of computation is not to be used. Similarly, where the beneficiary was not alive for the full 3-year period in which the shortcut averaging device is applied, then this averaging device is to be computed on the basis of the shorter period in which the beneficiary was in existence. Third, the bill specifies how prior distributions from foreign trusts to the beneficiary are to be treated in making these computations. Where a taxpayer with respect to an earlier distribution has used the shortcut method and subsequently uses the exact method for another distribution, for purposes of this exact computation any income received from the trust in the earlier distribution must be included in his income for any year to which the second distribution relates. However, where in the current distribution the taxpayer is using the so-called shortcut method, he is not required to take into account prior distributions from a foreign trust, whether the exact or shortcut method of taxation was used in the prior computations.

As under present law, the methods of tax computation outlined above are substitutes for including and taxing the entire amount of the distribution in the year actually received. To take advantage of either method the beneficiary at the time of making the election must supply such information with respect to the operation and accounts of the trust for each of the years in which an amount is considered distributed as the Secretary or his delegate may by regulation pre-

¹ The 2 prior years are included for this purpose only to prevent the current year, in which there may be special circumstances, from having too great an influence on the averaging device used.

scribe. This information is necessary in order to give assurance that the computation is made correctly.

So that the Internal Revenue Service will be aware of the existence of foreign trusts created by American grantors, settlors or transferors, the bill provides that the grantor of an inter vivos trust or the fiduciary of an estate in the case of a testamentary trust, or the transferor is to make a return within 90 days after the creation of the foreign trust or the transfer of money or property to it by an American person, setting forth such information with respect to the foreign trust as the Secretary or his delegate prescribes by regulation as necessary to carry out the provisions of the income tax laws. Failure to supply the information, unless it can be shown that this failure is due to reasonable cause, is to result in a civil penalty (in addition to any criminal penalty presently provided by law) equal to 5 percent of the amount transferred to the trust but not to exceed \$1,000. A similar penalty applies with respect to a return which does not show the information required, even though the return itself is filed.

Generally, these provisions relating to foreign trusts are to apply to distributions made after the date of enactment of this bill. The provisions relating to returns with respect to the creation of, or transfers to, a foreign trust, the civil penalties relating to these returns, and the definitions of U.S. persons and foreign estates and trusts are to be effective on the date of enactment of the bill.

VIII. MUTUAL FIRE AND CASUALTY INSURANCE COMPANIES, ETC.

(Sec. 8 of the bill and secs. 821-826, 831, and 832 of code)

A. Reasons for provision

Stock fire and casualty insurance companies have long been taxed at ordinary corporate income tax rates on both investment income and underwriting income. Mutual fire and casualty insurance companies, on the other hand, since 1941 have paid tax under special formulas which do not take into account their underwriting income or loss. Generally, these mutual companies presently are taxed under whichever of two formulas results in the higher tax. Under one formula, they are taxed at ordinary corporate income tax rates on investment income only. Under the other, they pay a tax of 1 percent on their gross investment income plus their premium income after policyholder dividends. Reciprocal underwriters and interinsurers are taxed only on their investment income and they have a vanishing \$50,000 exemption. Mutual companies with total receipts of not more than \$75,000 are tax exempt.

The President recommended that stock and mutual fire and casualty insurance companies be taxed on the same basis. He proposed that mutual companies pay tax on their underwriting profits, as well as on their investment income, substantially in the same manner as stock companies.

This bill to a considerable degree achieves the result sought by the President. Under it, mutual fire and casualty insurance companies are taxed under a modified total income formula. The modifications are required because of the special circumstances of the mutual companies.

While a stock insurance company can pay extraordinary losses not only out of its accumulated profits but out of its paid-in capital, a mutual insurance company can pay extraordinary losses only out of retained underwriting income. As a result, a mutual ordinarily retains a portion of its underwriting income each year for this purpose; the remainder is paid to its policyholders as policy dividends. This accumulated underwriting income constitutes its reserve out of which insurance losses can be paid, and the existence of such reserves is an important protection to the mutual policyholders.

Under the law up to this time, no income taxes have been paid on this retained underwriting income, except (since 1941) to the extent the excess of the alternative 1-percent tax over the tax on investment income in effect taxed part (all, or more than all) of the underwriting income. Similarly, underwriting losses may not reduce the tax on investment income. Under the President's proposal, underwriting gains would have been fully taxed as realized. Under the provisions of this bill, however, these mutual fire and casualty companies will be permitted to set aside a portion of each year's underwriting gain in a special account for protection against losses. This amount will be available to meet certain losses for 5 years, after which most of any remaining portion will be included in taxable income of the sixth year. A small portion, however, will still be retained in the special account to take care of extraordinary losses. Eventually, these companies will pay tax on their total income, but the tax deferral formula of the bill gives recognition to the mutuals' lack of access to the capital market for funds with which to pay losses. Under the bill underwriting losses, other than losses created by the special protection against loss deduction, will reduce the tax on investment income.

Under the bill mutual companies which have substantial underwriting gains will pay larger taxes than under present law. However, the full impact of taxing their underwriting income will be delayed until 1968. Thus, for a 5-year period only a portion of underwriting income of the mutual fire and casualty industry will be exposed to the Federal income tax. Thereafter, most of the amounts in the account which are not used for the payment of losses within 5 years will be taxed, but this will be offset—or more than offset if the company is growing and its underwriting income is increasing—by the portion of the income of the sixth and subsequent years which is set aside in the protection against loss account.

On the other hand, mutual fire and casualty companies having underwriting losses will, for the first time, be permitted to deduct these losses in full. For such companies the tax under the bill will be less than under present law which taxes the investment income of a mutual company at full corporate rates even though there is an underwriting loss. On the other hand, a stock company is taxed only on the net amount after deducting an underwriting loss against investment income. This inequality of treatment should not continue. Under this bill an underwriting loss would, depending on the circumstances, be offset against either investment income or the protection against loss account, or both, and any loss not so absorbed would be carried back (though not to a year before 1963) or carried forward, as in the case of corporations generally.

B. Comparison of committee amendments with House provision

Your committee has approved the basic provisions of the House bill taxing mutual fire and casualty insurance companies on their underwriting profits. Under both the House bill and your committee's bill, a portion of underwriting income is permitted to be set aside for a 5-year period for the purpose of offsetting insurance losses. The remainder will be currently taxed.

However, your committee modified the House bill to eliminate a discrimination in the manner in which losses are to be charged by mutual companies. Under the House bill, a mutual fire or casualty insurance company operating on a "deviated premium" basis (under which, in effect, policyholder dividends are deducted in advance of the policy period and only the net amount is charged for a policy) was permitted to charge all its underwriting losses (other than those created by the protection against loss deduction) directly against investment income. A dividend-paying mutual, on the other hand, even though its net premium at the end of the year (after payment of policyholder dividend) was identical to that charged by the deviating company, would have been compelled to reduce the underwriting loss chargeable to investment income by the amount of the policyholder dividends.

The effect of this discrimination was that in loss years the deviating company could charge larger amounts of underwriting loss to investment income and retain its protection against loss account, while a dividend-paying company was permitted to charge lesser amounts of underwriting loss to investment income and was required to deplete its protection against loss account more rapidly by charging to it not only losses created by the protection against loss deduction but also losses created by the payment of policyholder dividends. Since these dividends are viewed solely as price adjustments in the cost of insurance, your committee feels the tax consequences should be the same regardless of whether the price of the policy is adjusted at the time the policy is sold (by means of a deviated premium) or at the end of the policy period (by means of a policy dividend).

To eliminate this discrimination and to place mutual companies on a basis more comparable to stock companies (which are permitted under existing law to charge underwriting losses created by dividends directly against investment income), your committee's bill permits underwriting losses arising from the payment of policy dividends (price adjustments) to be charged first to investment income with any remaining unused losses then being charged to the protection against loss account.

Some mutual insurance companies specialize in insurance against limited risks such as windstorm, hail, or flood, in relatively small geographical areas. Because their operations cover a small area, few storms or floods may occur in some years and the company will then have relatively large underwriting gains; in other years, storms may cause heavy damage in the area of operations and the company will have relatively large underwriting losses. To compensate for this uneven experience both the House and your committee's bills permit these concentrated risk companies to defer, in the protection against loss account, a greater proportion of underwriting income than is permitted for ordinary companies. This is to protect them against unusually large losses if, and when, such losses occur.

Your committee has amended the House provision relating to the concentrated risk companies in two respects. Both are concerned with the qualification of companies for the additional protection against loss deduction. Under the House bill, a concentrated risk company was one which derived more than 50 percent of its premium income from insuring in one State against losses arising from wind, hail, floods, etc. Your committee believes that a company which has 40 percent of its premium income from such risks assumed in a limited area should also qualify as a concentrated risk company. Accordingly, the percentage test has been reduced to 40 percent. In addition, in recognition that storms and similar hazards are not restricted by State boundaries, your committee has added an alternative area test to the one-State test of the House bill. Under this alternative test, if more than 40 percent of its premium income is from the specified risks arising within a circle having a 200-mile radius (a 400-mile diameter), the company will qualify.

Under existing law, very small mutual companies, that is, companies whose total receipts from all sources (including premiums) do not exceed \$75,000, are exempt from tax. The House bill did not alter this exemption. Your committee, however, has concluded that the \$75,000 limitation on the exemption, which was provided in 1942, is totally inadequate by today's standards. To bring this exemption into line with current conditions, your committee's bill increases the limitation on the small company exemption to \$150,000.

The House bill provided a special tax treatment for mutual companies with total receipts between \$75,000 and \$300,000. Companies in this category would have been treated much as they are under existing law; i.e., these companies would pay tax on their investment income only (however, the alternative 1-percent tax of present law would no longer apply).

Your committee has approved this provision of the House bill, but has amended the limitations. First, the minimum limit has been increased to \$150,000 to coincide with the new limitation on exemption for the very small companies. The maximum limitation has been increased to \$600,000 (from \$300,000 in the House bill). This treatment is justified because these small companies often are of the assessment type and are not required to compute and report their underwriting income on approved forms for State insurance commission purposes. The bill makes it unnecessary for them to compute their underwriting income in the future. Moreover, this amendment will enable these small, often new, companies to maintain sufficient reserves so that they can obtain reinsurance at reasonable rates. Small companies with total receipts between \$600,000 and \$1,200,000 (\$300,000 and \$900,000 in the House bill) will be taxed both on their investment income and on their underwriting income. However, to provide for a gradual transition to the new tax on their underwriting income, like the House bill your committee's bill provides a special deduction of \$6,000 which decreases as total receipts of the company increase above \$600,000. This means that at \$1,200,000 there is no special deduction.

Reciprocal underwriters and interinsurers differ from ordinary mutual insurance companies in that their business is conducted by two entities rather than one. An ordinary mutual insurance company receives all of the premium income from insurance and not only

pays losses but conducts directly the operation and management of the insurance activities. The reciprocal underwriter or interinsurer, on the other hand, pays its insurance losses, but an "attorney-in-fact" performs all, or most, of the insurance functions—writing policies, collecting premiums, settling claims, keeping records, etc.—and pays the related expenses, for a portion of the premium income of the reciprocal. Profits realized by the attorney-in-fact from conducting these insurance operations are taxed as ordinary income. However, if that income were earned by a mutual insurance company which performed these operations itself, under existing law it would constitute underwriting income and would not be taxed. Moreover, under present law reciprocal underwriters and interinsurers are not taxed in the same way as ordinary mutuals since they are not subject to the alternative 1-percent tax and have a special exemption. The House bill taxes reciprocal underwriters and interinsurers under the same rules that apply to ordinary mutuals; but in recognition of their unique form of operation it permits them in effect to combine the underwriting income of the attorney-in-fact with their own for the purpose of offsetting certain losses. This provision has been approved with a change which permits the reciprocal to use the combined underwriting income as the basis for setting aside 25 percent of underwriting income in the protection against loss account; thus, in effect, increasing the amount of its own underwriting income upon which tax may be deferred.

Under present law, factory mutual insurance companies are taxed under the same formulas as other mutuals; that is, they pay tax on investment income only (with no deduction for underwriting losses) or under the alternative 1-percent formula. However, because of the very large premium deposits required of their policyholders (typically up to 10 times the amount of an ordinary premium) the investment income of such companies is very large. As a result in practice they never become subject to the alternative 1-percent tax. As in the case of other mutuals, these companies are not permitted to deduct their underwriting losses. This has been a handicap to these companies in years in which they have losses, because the industrial risks which they insure generally are quite large. The House provision, approved without change by your committee, taxes factory mutual companies as if they were stock companies, thus permitting them to deduct underwriting losses when they occur. However, since a large portion of each premium is in effect a deposit (which may be returned to the policyholder), in computing their underwriting profits these companies are to be permitted to determine their premium income on the basis of their schedules of absorbed premium deposits. The amount so determined will be increased by 2 percent for income tax purposes to offset the advantage of the temporary use of deposits which would ordinarily be viewed as premiums received.

Your committee added two new provisions to the House bill. One of these deals with mutual flood insurance companies. It was brought to the committee's attention that some mutual flood insurance companies (including reciprocal exchanges) operate on a premium deposit system quite similar to that employed by factory mutual fire insurance companies. Because of the similarity of their method of operation, your committee has concluded that these companies should be taxed in the same manner as factory mutual fire insurance com-

panies. Accordingly, your committee has amended the House bill to provide that mutual flood insurance companies are to be taxed under the rules also made applicable by this bill to factory mutual fire insurance companies. Under these rules these flood insurance companies are to determine their underwriting income on the basis of their schedule of premium absorptions. Of course, these companies will also be required to increase the amount of their absorbed premiums by 2 percent of the amount actually absorbed.

The second amendment provides that a mutual company which experienced underwriting losses in each of 5 out of the 6 years immediately preceding 1963 is to be provided a special 5-year carryover of the excess of underwriting losses over underwriting gains during the 6-year period. This exception to the general rule of the bill that underwriting losses may not be carried over from a year prior to 1963 will prevent a company with a long history of unusual loss experience from being penalized in years when it is retaining unusual amounts of underwriting income to restore its reserves to their normal level, particularly when the underwriting losses were not permitted to be taken into account in computing taxable income in the 6-year period. In cases cited to the committee, to which this provision applies, some mutual insurance companies actually paid taxes for the 6-year period in excess of total income for that period.

C. General explanation of provision

Under present law the tax on a mutual fire and casualty insurance company is, in general, the greater of (1) a tax at the ordinary corporation rates on the company's net income from investments, or (2) a tax of 1 percent of its gross income from both investments and premiums less dividends to policyholders. Under the provisions of this bill the 1-percent alternative tax is eliminated, and the tax is computed at the ordinary corporation rates on the company's total income (investment income and underwriting income) less amounts temporarily set aside in a protection against loss account. Underwriting income of these insurance companies is the excess of earned premiums over insurance losses and expenses incurred and dividends paid to policyholders.

There are special provisions for companies with concentrated risks, for small companies, and for reciprocals or interinsurers. The bill also removes the factory mutuals from the treatment accorded mutual casualty companies generally, and treats them as if they were stock companies, with special provisions for determining what portion of their premium deposits is to be viewed as earned premiums.

1. *Ordinary mutual fire and casualty insurance companies.*—Under the bill taxable income of mutual insurance companies will consist of taxable investment income, statutory underwriting income, and certain amounts previously set aside for protection against losses. Statutory underwriting income, as used in the bill, is underwriting income after a special deduction for protection against losses of an amount equal to 1 percent of insurance losses incurred during the year and 25 percent of the ordinary underwriting income.

An amount equal to the special deduction is to be set aside for 5 years in a "protection against loss" account where it can be used only for offsetting losses. After the fifth year, if the amount credited

to the protection against loss account has not been absorbed by losses, the portion attributable to the 1 percent of losses and one-half of the portion attributable to the 25 percent of underwriting income will be withdrawn from the account and included in taxable income. The other one-half of the amount representing the 25 percent of underwriting income is retained in the account for a longer period as a cushion against extraordinary losses.

The bill limits the amount which may be accumulated in this account, however. The amount in this account may not be increased above an amount which at the end of any year is more than 10 percent of the earned premiums less dividends to policyholders for that year. If a greater amount were already in the account at the beginning of the year, the account would not be reduced (because of the ceiling) below this amount.

If in any year there is a loss from underwriting instead of a gain, the part of the loss resulting from the payment of insurance claims and expenses and policy dividends would be offset directly against taxable investment income. Any amount not so offset and other losses (those resulting from the special protection against loss deduction) would be charged against the protection against loss account on a first-in, first-out basis. Losses charged against the account would be applied proportionately to amounts representing the 1 percent of losses incurred and the 25 percent of underwriting income.

If in any year there is an extraordinary underwriting loss—more than the investment income for that year and the entire amount in the protection against loss account—the excess will be treated much like an ordinary net operating loss, to be carried back against the taxable income of the 3 preceding years or carried forward (first against amounts added to the protection against loss account and then against otherwise taxable income) to the succeeding 5 years, as in the case with any corporation.

In computing their taxable income, mutual companies are to be allowed an unlimited deduction for dividends paid to policyholders, just as stock companies may take unlimited deductions for their policy dividends.

Under present law, mutual insurance companies which are not subject to the 1-percent alternative tax are allowed a special exemption of \$3,000, with the tax on taxable incomes between \$3,000 and \$6,000 gradually increasing until the exemption completely vanishes when taxable income reaches \$6,000. The bill increases this special exemption (applicable to the new total of investment and underwriting income) to \$6,000 in the case of mutual companies taxable under the general rules of the bill. There also is a gradually increasing tax on taxable incomes between \$6,000 and \$12,000, so the exemption vanishes when taxable income reaches \$12,000.

2. *Example.*—The computation of taxable income, statutory underwriting gain and the protection against loss account for a 6-year period with successive underwriting gains, may be illustrated as follows, assuming the simplified facts as shown in the following table:

Year	Taxable investment income	Underwriting income	Insurance losses incurred	Additions to protection against loss account
1963.....	\$10	\$12	\$700	\$7+\$3 (\$10)
1964.....	11	16	800	8+ 4 (12)
1965.....	12	12	600	6+ 3 (9)
1966.....	13	20	600	6+ 5 (11)
1967.....	14	24	900	9+ 6 (15)
1968.....	15	20	1,000	10+ 5 (15)

For 1963 the statutory underwriting income would be \$2, the underwriting income of \$12 minus the 1 percent of incurred losses (\$7) and the 25 percent of the underwriting income (\$3) credited to the protection against loss account. The taxable income would be \$12, the sum of the taxable investment income and the statutory underwriting income. For 1964 the statutory underwriting income would be \$4 and the taxable income \$15; for 1965 corresponding figures would be \$3 and \$15; for 1966, \$9 and \$22; and for 1967, \$9 and \$23.

For 1968 the statutory underwriting income would be \$5 (\$20 minus \$10 minus \$5), but there would be included in taxable income an amount equal to the first item added to the protection against loss account in 1963 (\$7), and half of the second item (\$1.5), so that for 1968 the taxable income would be \$28.5, the sum of the taxable investment income (\$15), the statutory underwriting income (\$5), and the \$8.5 withdrawn from the protection against loss account.

At the end of 1968, therefore, the total amount in the protection against loss account would be \$63.5—amounts totaling \$62 added for 1964 and the 4 following years which will be available to offset losses occurring during the next 5 years, and a residual \$1.5 from 1963 to offset any loss which exceeded the entire amount in the account other than that.

If, in the preceding example, for 1966 there had been an underwriting loss of \$30 (excluding the protection against loss deduction), and insurance losses incurred had still been \$600 the deduction added to the protection against loss account would thus have been 1 percent of \$600 or \$6 and the statutory underwriting loss would be \$36. In that case the portion of the loss not resulting from the protection against loss deduction (\$30) would be offset against the taxable investment income of \$13, the taxable income for 1966 thus being zero. The remaining portion of the loss (\$23) would be charged against the protection against loss account, the \$10 added to that account in 1963 and the \$12 added in 1964 being eliminated, and of the 1965 addition there would remain \$5.33 and \$2.67. In that case there would be nothing from the protection against loss account to be included in taxable income for 1968 or 1969.

Under the bill, as passed by the House and approved by your committee, the rules applicable to mutual fire and casualty companies accruing market discount on bonds are changed. Under present law all mutual fire and casualty companies (and life insurance companies) are required to accrue each year a ratable portion of market discount on bonds and pay tax thereon at ordinary income tax rates (Rev. Rul. 60-210; 1960-1 CB 38). Stock fire and casualty insurance companies, on the other hand, are not required to accrue such discount but when the bond is sold or redeemed they are required to pay tax on the

amount of gain resulting from market discount at capital gains rates (if the bond is held for more than 6 months). Since under the general rule of the bill the starting point in computing "mutual insurance company taxable income" is the gross income computed as if the taxpayer were a stock company, the effect is to treat market discount on bonds for mutual companies, other than the small companies taxable on investment income only) as it is treated by the stock companies.

3. *Casualty companies with concentrated windstorm, etc., risks.*—As stated above, most mutual insurance companies will report and pay a tax currently on the underwriting income remaining after transferring to the protection against loss account 25 percent of underwriting income plus 1 percent of incurred losses. With respect to certain insurance companies whose risks are primarily from losses from windstorm, hail, flood, earthquake, or similar natural hazard, and are concentrated in one State, or within 200 miles of any point selected annually by the taxpayer, the bill permits deferral of more than 25 percent of underwriting income. The percentage of underwriting income which can be credited to the account in such a case is determined by dividing the premiums earned on insurance contracts covering the risks in the designated area by total premiums earned by the insurance company. If this does not exceed 40 percent, the regular rule is used. If it does, the normal deduction of 25 percent of underwriting income is increased by the excess percentage points over 40 percent. Thus, under this rule, a company which has 80 percent of its windstorm, etc., risks insured in one State (or in a circle having a 400-mile diameter) would be permitted to transfer 65 percent (the regular 25 percent plus 40 percent) of its underwriting income to the protection against loss account. (However, concentration of risks will not serve to permit a larger percentage of incurred losses to be credited to the protection against loss account.)

The overall limitation on the protection against loss account of 10 percent of premiums less policy dividends for the year is not to apply to the amount of underwriting income in excess of 25 percent which these concentrated risk companies add to their protection against loss account. If it did apply it would defeat the objective of allowing a greater portion of underwriting income to be set aside. In applying the ceiling the concentrated risk company is to be treated as if it had transferred only 25 percent of its underwriting income to the account.

4. *Small companies.*—Under the bill, small mutual fire and casualty insurance companies (those whose total receipts—gross investment income, excluding capital gains, plus premiums—exceed \$150,000 but do not exceed \$600,000) are not taxed on underwriting income. As under present law, these companies will continue to pay tax on investment income only (with no deduction for underwriting losses) but the alternative 1-percent tax will no longer apply. The special exemption of \$3,000, with the "notch" rates applying to taxable incomes between \$3,000 and \$6,000, also will continue in effect.

Despite the treatment for these small companies described above, the bill permits them to elect to be taxed on total income, including underwriting income, in the same manner as other mutual companies, and such an electing company will similarly be allowed to deduct underwriting losses. Presumably the existence, or expectation, of underwriting losses would be the primary reason for making this election. The election, once made, cannot be changed without the consent

of the Treasury Department. On the other hand, a small mutual company which becomes taxable under the general rules because its gross investment income plus premiums exceed \$600,000 in a taxable year, again will be taxed as a small company if its income falls below this level, if one condition is met. If, while it was taxed under the regular formula it was required to credit a portion of its underwriting income to the protection against loss account, this amount must be taken into income and a tax paid on it before the small company treatment will again apply. To provide consistent tax treatment for these small companies, the bill does not permit loss carrybacks or carryovers to be carried to, from, or over a year in which the company was taxable as a small company.

In the case of mutual fire or casualty insurance companies whose total receipts are between \$600,000 and \$1,200,000, the bill provides a special vanishing deduction which is to apply to underwriting income only. For a company whose total receipts are \$600,000, the special deduction will be \$6,000. As total receipts increase, the \$6,000 deduction decreases and finally vanishes when total receipts of the company equal \$1,200,000.

5. *Reciprocal underwriters and interinsurers.*—Under the bill, reciprocal underwriters and interinsurers are in general taxed in the same way as ordinary mutuals, with two important exceptions.

First, reciprocal underwriters and interinsurers may elect to take into account the income of the attorney-in-fact which is attributable to the insurance business of the reciprocal. It accomplishes this by not deducting that part of the fee paid to the attorney-in-fact which is equivalent to the attorney-in-fact's profit from the insurance operation. This election may be made, however, only if the attorney-in-fact is a corporation which keeps its records on the same basis as the reciprocal and certain other requirements are met.

An election by a reciprocal is never to reduce income taxes of the attorney-in-fact. The attorney-in-fact will continue to determine its tax just as it does under present law except that it must identify income and expense items attributable to the insurance business of the reciprocal.

An electing reciprocal will compute its tax liability on the combined income, under your committee's amendments, by applying the formula of this bill to the combined underwriting income. As an offset to the increased tax due to the inclusion of the income of the attorney-in-fact, the reciprocal may take tax credit for the tax paid by the attorney-in-fact with respect to its income from insurance operations. (Under certain circumstances this may result in a refund to the reciprocal.)

If the combined underwriting account of the reciprocal and its attorney-in-fact shows a loss the ordinary rules of the bill for charging it are to apply. Thus, the loss would be charged first to investment income if it is from the payment of claims, policy dividends or expenses, or to the protection against loss account of the reciprocal if it is a loss created by the special loss protection deduction.

The inclusion of the income of the attorney-in-fact in the income of the reciprocal permits the reciprocal to set aside a larger portion of income in the protection against loss account than it otherwise could, since 25 percent of the combined income is thus set aside. Your committee believes this amendment is necessary to give policy-

holders of a reciprocal company much the same protection as that given to the policyholders of an ordinary mutual company. However, a reciprocal, under your committee's amendment, must after 5 years restore to income all of the amount added to the protection against loss account which was attributable to the income of the attorney-in-fact which has not in the interval been absorbed by losses.

The second special feature of the bill relating to reciprocal underwriters or interinsurers permits them to deduct savings credited to individual subscribers' accounts (in the same manner as policyholder dividends paid in cash) if the company is obligated to pay those amounts promptly to the subscriber if he terminates his contract. This is provided because the "pure," or "classical," reciprocal or interinsurer typically credits the account of each policyholder with savings attributable to his contract and because the policyholder has a legal right to receive the amount so credited if he withdraws from the exchange. Because amounts credited to the account of an individual subscriber represent reductions to him in the cost of insurance, the bill provides that for income tax purposes the subscriber must reflect this reduction when the credit is made.

This deduction for credited savings, as stated above, is to be available only in case of so-called "pure" or "classical" reciprocals or interinsurers where the credits, as a matter of actual practice, are paid to policyholder subscribers who terminate their contracts. An ordinary reciprocal which may nominally meet the requirement of the statute would not be entitled to this deduction where savings credited to subscribers are not in fact returned to them when they terminate their policies.

6. *Factory mutual insurance companies.*—The bill amends the law with respect to factory mutual insurance companies in two important respects. First, commencing in 1963, these companies will be treated for tax purposes as if they were stock companies. This means that they will report their underwriting income in full in the year earned, and their underwriting losses after 1962 will be deductible in full.

Secondly, the method of computing premium income of factory mutuals is modified to conform more closely to the actual operation of these companies. This is accomplished by permitting them to determine their premium income on the basis of their schedule of absorbed premium deposits. The amount thus determined is then to be increased under the bill by 2 percent of absorbed premiums for income tax purposes. For example, a factory mutual might require a premium deposit of \$1,000 and its experience indicates it will absorb 12 percent of the premium deposit each year during the term of the policy. Under existing law, in the case of a 3-year policy, the factory mutual would realize earned premiums of \$333.33 each year (one-third of the premium deposit) and would deduct returns to policyholders as if they were dividends. Actually, however, the factory mutual absorbs only 12 percent of the premium deposit, or \$120 each year. Under the bill, this factory mutual will report for income tax purposes \$122.40 (\$120 plus 2 percent of \$120). This bill also provides for an adjustment in the unearned premium account of the factory mutual for returns of unabsorbed premium deposits to policyholders upon termination of their policies. This return of unabsorbed premium deposit is viewed as analogous to a dividend or a payment similar to a dividend.

7. *Mutual marine insurance companies.*—Mutual marine insurance companies have been taxed as stock insurance companies for many years and your committee's bill continues this treatment for them. However, a question has arisen as to whether such a company, if previously taxed as a mutual marine company, should continue to be so taxed. Your committee believes that under existing law a taxpayer which has always filed its returns as a mutual marine company should be treated as such for all years without regard to whether marine premiums still constitute its predominant source of premium income. In order to clarify the law, and foreclose the possibility that a mutual company may be taxed under different sections in different years, in lieu of a definition, your committee's bill provides that any mutual marine insurance company which was taxed as a stock company for a period of at least 5 years may elect to continue to be so taxed. The phrase "whether or not marine insurance is its predominant source of premium income" is intended to make clear that a company which has been taxed as a mutual marine company, and which has always filed its returns as a mutual marine company, may be treated as a stock company for all such years, even though marine insurance is no longer its predominant source of premium income.

8. *Special transitional loss deduction.*—Your committee has added a new provision to the House bill under which mutual insurance companies which have experienced a long and unusual period of underwriting losses will be permitted to take those losses into account in determining their taxable income. Companies qualifying for this treatment are those who have incurred underwriting losses in at least 5 out of the 6 taxable years preceding 1963. Companies which qualify for this treatment may deduct the excess of their underwriting losses over underwriting gains for the 6-year period in the years 1963 through 1967. This 5-year period is the same as the 5-year carry-forward provision of present law which applies in the case of net operating losses. Your committee felt that this treatment is justified because companies with long unfortunate loss experience must of necessity retain additional amounts of underwriting income to rebuild their reserves to a safe level. In the absence of this provision, these companies would be subjected to tax on an unusually high proportion of underwriting income.

9. *Exemption for small mutual insurance companies.*—Your committee also has added a new provision to the House bill which increases the limitation on tax exemption for small mutual insurance companies from \$75,000 to \$150,000. Increasing this limitation will provide complete tax exemption for approximately 160 additional small mutual insurance companies, many of which are of the pure assessment type.

10. *Mutual flood insurance companies.*—Another provision added to the House bill by your committee requires mutual flood insurance companies to be taxed under the stock formula in the same manner as mutual fire insurance companies issuing policies for which the premium deposits are the same regardless of the length of the term for which the policies are issued if the unabsorbed portion of the premium is returned to the insured upon termination of the policy. This same rule (as explained in par. 6, above) applies also to factory mutual insurance companies.

11. *Effective dates.*—The amendments made by this section are to apply with respect to taxable years beginning after December 31, 1962, except that the amendment relating to mutual marine insurance companies is to apply to taxable years beginning after December 31, 1961.

IX. DOMESTIC CORPORATIONS RECEIVING DIVIDENDS FROM FOREIGN CORPORATIONS

(Sec. 9 of the bill and secs. 902 and 78 of code)

A. *Reasons for provision*

The Secretary of the Treasury in his appearance before your committee stated that foreign income received by domestic corporations in the form of dividends—

is, in effect, deducted from taxable profits in computing the U.S. tax, but a good share of it is also allowed as a credit against the U.S. tax liability.

He termed this an unjustified tax advantage and recommended that, as provided in the House bill, it be eliminated.

The problem arises when the foreign tax rate is below the U.S. tax rate and results from the fact that the amount paid in foreign taxes not only is allowed in part as a credit in computing the U.S. tax of the corporation receiving the dividend, but also is in effect allowed as a deduction (since the dividends can only be paid out of income remaining after payment of the foreign tax).

The problem can be illustrated by assuming that a foreign government imposes a 30-percent tax with respect to \$1,000 of income of a corporation. This would leave \$700 of the \$1,000 out of which a dividend could be paid to a U.S. parent corporation. If the applicable U.S. tax rate is 52 percent, the American tax on this \$700 before the allowance of any foreign tax credit would be \$364. On the other hand, if the \$1,000 of income had been earned by a branch of the U.S. corporation, the entire \$1,000 would be subject to U.S. tax before allowance of any foreign tax credit. Thus, in this case the tentative U.S. tax would be \$520, or \$156 more than in the case of the foreign subsidiary.

In the case of the foreign subsidiary, the foreign tax allowed as a credit is limited to the same proportion of the tax which the income included in the American tax base is of the total income.¹ Thus, the allowable credit in the case of the foreign subsidiary is limited to seven-tenths of the \$300 or \$210. As a result the final U.S. tax on the dividend is \$154 (\$364 minus \$210). This U.S. tax of \$154, plus the foreign tax of \$300, results in a total tax of \$454, which is \$66 less than the full \$520 tax which would be paid by a domestic corporation operating in this country, or operating abroad through a branch.² This example is summarized in table 4 below.

¹ This is the result of the decision in *American Chicle Company v. U.S.*, 316 U.S. 450 (1942).

² As indicated above, the U.S. tax before credit in the case of the branch would be \$520. After allowing the \$300 foreign tax credit in this case, the final U.S. tax would be \$220 which, with the \$300 of foreign tax, means a total tax of \$520.

TABLE 4.—*The computation of corporate taxes on foreign income*

	Existing law	Proposed law
	<i>Dollars</i>	<i>Dollars</i>
Profits of subsidiary.....	100.0	100
Foreign tax (assumed rate: 30 percent).....	30.0	30
Dividend to U.S. parent.....	70.0	70
"Gross-up" of dividend.....		30
Tentative U.S. tax at 52 percent.....	36.4	52
Credit for foreign tax paid by subsidiary.....	21.0	30
Net U.S. tax.....	15.4	22
Combined foreign and U.S. tax.....	45.4	52

The size of this tax differential which exists in the case of dividends from foreign subsidiaries at the present time varies with the size of the foreign tax rate. As shown in table 5, the tax differential disappears either when the foreign tax rate equals or exceeds the U.S. tax or when there is no foreign tax imposed at all. The maximum tax differential, given a 52-percent U.S. tax rate, occurs when the foreign tax rate is half that, or 26 percent. The differential at this point is 6.7 percentage points.³ Where dividends are received by a domestic corporation from its foreign subsidiary, which in turn has received its income from another foreign subsidiary, the maximum tax differential (given the 52-percent U.S. tax rate) amounts to 11.93 percentage points.

TABLE 5.—*Rate differential enjoyed with respect to dividends from foreign subsidiaries with various selected foreign income tax rates and present 52-percent U.S. rate*

Income before tax	Foreign tax	Income available for dividend	U.S. tax before credit	Credit against U.S. tax	U.S. tax	Total tax	Rate differential enjoyed by foreign subsidiary
							<i>Percentage points</i>
\$100.....	0	\$100	\$52.00	0	\$52.00	\$52.00	0
\$100.....	\$5	95	49.40	\$4.75	44.65	49.65	2.35
\$100.....	10	90	46.80	9.00	37.80	47.80	4.20
\$100.....	20	80	41.60	16.00	25.60	45.60	6.40
\$100.....	26	74	38.48	19.24	19.24	45.24	6.76
\$100.....	30	70	36.40	21.00	15.40	45.40	6.60
\$100.....	40	60	31.20	24.00	7.20	47.20	4.80
\$100.....	50	50	26.00	25.00	1.00	51.00	1.00
\$100.....	52	48	24.96	24.96	0	52.00	0

Two relatively minor technical corrections recommended by the administration are also included in the House bill. One of these involves the repeal of a subsection (sec. 902(d)) of one of the foreign tax credit provisions, which makes the foreign tax credit available in limited cases with respect to royalty income received from a foreign subsidiary. This royalty income is entitled to this foreign tax credit only where the domestic corporation owns all of the stock of the subsidiary. The provision granting this treatment in the case of royalty income was adopted in 1954 in order to grant relief in a case where, because of currency exchange restrictions, a corporation was prohibited from distributing its earnings. The retention of this provision would have the effect of allowing a foreign tax credit before actual dividend distributions have been made.

³ The tax differential represents the difference between the U.S. and foreign tax rates, multiplied by the income omitted from the U.S. tax base.

Second, the House bill also follows a recommendation of the administration relating to the interrelationship of the foreign tax credit and the intercorporate dividends received deduction. The problem arises here where a foreign corporation derives 50 percent or more of its income from sources within the United States. In such a case a domestic corporation receiving dividends from it is eligible for the 85-percent intercorporate dividends received deduction with respect to the proportion of the income determined to be from sources within the United States. However, all of the remaining income is treated as income from sources without the United States for which a foreign tax credit is available, including the 15-percent amount remaining after the allowance of the intercorporate dividends received deduction which, for that purpose, was treated as income from sources within the United States. The House bill provides that this 15 percent of domestic source income, remaining after the dividend received deduction is allowed, retains its domestic source character rather than being reclassified as foreign source income for purposes of the foreign tax credit.

B. Comparison of committee amendments with House provision

Your committee agrees with the House that, as a result of including only dividend income in the tax base and at the same time allowing a foreign tax credit, the full U.S. tax is not paid on most dividend income received by domestic corporations from foreign corporations. Your committee agrees with the House that in the case of dividend income received from developed countries, there is no reason for this tax differential. Therefore, except in the case of income received from "less developed country corporations" it has provided, as does the House bill, that where a taxpayer elects the foreign tax credit he must increase, or "gross-up," his U.S. tax base by including in it the amount of foreign income paid in taxes to the extent related to the dividend received. Thus, in the example cited in part A, above, the tentative U.S. tax would be computed on the basis of \$1,000, instead of \$700, and then the full \$300 of foreign tax would be allowed as a foreign tax credit in the same way as in the case of branches of U.S. corporations.

In the case of corporations deriving most of their income from less developed countries, however, your committee concluded that it would be inappropriate at this time to raise the effective rate of combined American-foreign tax since this would discourage new investments in such countries. Your committee believes that to discourage such investments at this time would be contrary to our national policy.

The term "less developed country corporation" for purposes of this provision has the same definition as in section 12, but here also is defined to include certain holding companies not included in the definition in section 12. In general terms, a less developed country corporation is a corporation organized under the laws of a less developed country, which is engaged in the active conduct of a trade or business, which derives 80 percent of its gross income from sources within less developed countries, and which has 80 percent in value of its assets invested in a trade or business in a less developed country and certain other assets consistent with the carrying on of this trade or business. Certain shipping and aircraft corporations also qualify. A third category of corporations which for purposes of this one provision also qualify as less developed country corporations consist of foreign hold-

ing companies (wherever incorporated) which own 10 percent or more of the stock in less developed country corporations and which receive 80 percent or more of their gross income from sources within less developed countries and have 80 percent or more in value of their assets invested in the same manner as other less developed country corporations.

Your committee has accepted the other two amendments made by the House bill without change; namely, that relating to the deletion of the provision treating royalty income in certain cases as dividends from a foreign subsidiary and that treating all income eligible for the domestic intercorporate dividends received deduction as domestic rather than foreign income for purposes of the foreign tax credit.

C. General explanation of provision

1. *Provision for "gross-up" except in the case of less developed country corporations.*—Your committee's amendments provide that, except in the case of less developed country corporations, if a domestic corporation elects to take a foreign tax credit (rather than a deduction for foreign taxes), it must include in its gross income an amount equal to the taxes of its subsidiary (or an amount equal to the taxes of its subsidiary's subsidiary) which it is considered, or deemed, to have paid, for purposes of the foreign tax credit provision, with respect to the dividend income received (or treated as having been received under sec. 12 below). Thus, for a domestic corporation to claim a foreign tax credit for foreign taxes paid by its subsidiary which is not a less developed country corporation, or a subsidiary of that subsidiary, it must "gross-up" its dividend income received by the amount of the foreign income, etc., taxes attributable to it.

Your committee's bill also rewrites the rules of present law which determine the portion of the foreign taxes which are treated as being attributable to dividend income received from a 10-percent-owned subsidiary which is not a less developed country corporation and from one which is a less developed country corporation.

In the case of a subsidiary which is *not* a less developed country corporation, all of the foreign income, etc., taxes can be allowed as a credit since in this case the entire earnings before tax are taken into account by the domestic corporation. In the case of dividends received from *less developed country corporations* only the portion of the foreign income, etc., taxes attributable to the accumulated earnings and profits after foreign taxes can be allowed as a credit since only these earnings and profits are taken into income by the domestic corporation. This continues the principles laid down by the Supreme Court in *American Chicle Co. v. United States*, 316 U.S. 450 (1942).

As under present law, if a 10-percent-owned foreign corporation owns 50 percent or more of another foreign corporation, a foreign tax credit is allowed with respect to foreign taxes paid by the second tier foreign corporation to the extent the dividends received by the domestic corporation are attributable to those paid by the second tier corporation. Under your committee's amendments dividends received by a domestic corporation are either "grossed up" or not "grossed up" in such cases on the basis of the status of the first tier foreign corporation. Thus, if the first tier foreign corporation is a less developed country corporation, the status of the second tier foreign corporation in this respect is immaterial (except insofar as

the distributions by it to the first tier corporation aid or hinder the first tier foreign corporation in qualifying as a less developed country corporation). Where there is to be no "gross-up" at the second tier level, the foreign taxes allocated to the dividend are allocated under rules consistent with the principles set forth in the court decision *American Chicle Co. v. United States*.

For purposes of this provision, three different categories of corporations are treated as "less developed country corporations." The first two of these are the same as the definition of a less developed country corporation for purposes of section 12 below. The third category, which essentially is a holding company for one or more less developed country corporations is an additional category that applies only for purposes of this one provision.

A less developed country corporation in the first category is a corporation organized under the laws of a less developed country, which is engaged in the active conduct of a trade or business, derives 80 percent or more of its gross income from sources within less developed countries, and has 80 percent or more of its assets (in terms of value) invested in a manner consistent with carrying on a trade or business in a less developed country. Thus, this 80 percent of its assets must consist of—

- (1) Property used by it in its trade or business in less developed countries;

- (2) Money and bank accounts;

- (3) Stock and obligations (having a maturity of 5 years or more at time of acquisition) of less developed country corporations;

- (4) An obligation of a less developed country;

- (5) Investments required because of restrictions imposed by less developed countries; and

- (6) Certain U.S. property, such as U.S. Government bonds, money, property purchased in the United States for export, etc., which, although having a U.S. situs, for purposes of section 12 below are excluded from the definition of "U.S. property."

The second category of corporation classified as a "less developed country corporation" consists of certain shipping or aircraft companies. These corporations must be foreign corporations 80 percent or more of the gross income of which arises from—

- (1) The use (or hiring or leasing for use) in foreign commerce of aircraft or vessels registered under the laws of a less developed country;

- (2) From the performance of services directly related to these aircraft or vessels;

- (3) From the sale or exchange of such vessels or aircraft;

- (4) Dividends and interest received from foreign corporations which are themselves less developed country corporations under the definition contained in this category and in which the corporation in question has at least a 10-percent stock interest; and

- (5) Gain from the sale or exchange of stock or obligations of foreign corporations which are less developed country corporations.

In addition, to qualify as less developed country corporations, these shipping or aircraft companies must have 80 percent or more of their assets either used for the production of the income described above.

or consisting of property which although having a situs in the United States is not considered as "U.S. property" under the exceptions set forth in section 12.

The third category of corporations qualifies as less developed country corporations only for purposes of this "gross-up" provision. These corporations are foreign corporations (which may or may not be organized under the laws of a less developed country) which have at least a 10-percent stock interest in another foreign corporation which is a less developed country corporation within the meaning of the first category specified above. In addition, the foreign corporation must derive 80 percent of its gross income from sources within less developed countries and 80 percent in value of its assets must be of the type specified in category No. 1, above.

2. *Dividends from U.S. sources.*—The bill amends the rules used in determining whether income is from within or without the United States in the case of a foreign corporation which has received 50 percent or more of its gross income for the 3 prior years from sources within the United States. In such a case, the 85-percent intercorporate dividends received deduction is available with respect to the proportion of its income which its income derived from sources within the United States bears to its income from all sources. However, under present law all of such a corporation's income, to the extent it exceeds the 85-percent deduction allowed for intercorporate dividends received, is treated (for purposes of the foreign tax credit) as income from sources without the United States. Thus, the 15 percent for which no intercorporate dividends received deduction is allowed, although for purposes of the prior computation treated as from sources within the United States, is for this purpose treated as foreign source income. The bill corrects this technical deficiency by providing that the amount treated as foreign source income in such a case is only the remaining income in excess of this 15 percent.

3. *Royalty income eligible for foreign tax credit.*—The bill eliminates the provision of present law (sec. 902(d)) which treats as a distribution (and, therefore, eligible for the foreign tax credit) royalty payments received by a domestic corporation from a 100-percent owned subsidiary engaged in manufacturing, production, or mining.

4. *Effective date.*—The provisions referred to above are applicable to all dividends received by a domestic corporation after December 31, 1964. They also are to apply to *certain* dividends received by the domestic corporation in the period before January 1, 1965, but only in its taxable years beginning after December 31, 1962. (For a calendar year corporation this latter category includes certain dividends received in the calendar years 1963 and 1964.) In the case of dividends received in these years the "gross-up" and other changes made by this provision are to apply only to the extent that the dividends are treated for tax purposes as made out of the accumulated profits of the foreign corporation for taxable years beginning after December 31, 1962. Dividends received by a foreign corporation from its subsidiary before January 1, 1965, which are paid out of the subsidiary's profits from before 1963 are to be treated as paid out of the first foreign corporation's profits from before 1963 if it in turn pays the dividends to the domestic corporation before January 1, 1965.

X. SEPARATE LIMITATIONS ON FOREIGN TAX CREDIT WITH RESPECT TO CERTAIN INTEREST INCOME

(Sec. 10 of the bill and sec. 904(f) of the code)

A. *Reasons for provision*

The Secretary of the Treasury in his appearance before your committee pointed out that last summer Canada revised its tax laws to provide a 57½-percent effective rate of Canadian tax on income going to U.S. corporations operating in branch or subsidiary form in Canada. He stated that this Canadian tax, in excess of the U.S. 52-percent rate, has highlighted a procedure of using the foreign tax credit as an artificial enducement to the outflow of short-term U.S. capital. The Secretary stated that this was harmful to our monetary stability and balance-of-payments position.

Under existing law, a U.S. corporation deriving income from business abroad through a branch or a subsidiary can be expected to have an unused foreign tax credit if the foreign tax rate exceeds the U.S. rate. However, if additional foreign source income, such as interest, can be earned which is subject to a foreign tax rate which is lower than the U.S. rate, then the two types of income can be combined under the existing foreign tax credit rules. In this way the U.S. tax on the investment funds, which the foreign country taxes at a rate at much less than the U.S. rate, can be reduced or completely eliminated by being offset against the excess credit from the tax on the business income. For example, if U.S.-owned business operations are taxed in Canada at a 57½-percent effective rate, this leaves an excess credit of 5½ percentage points over and above the tax which can be credited against the U.S. 52-percent tax. The Canadian rate of tax on interest income, however, is only 15 percent. As a result, the U.S. company involved may transfer to Canada short-term funds, such as bank deposits, which would ordinarily be held in the United States. The excess credit from the business income in this case eliminates the U.S. tax on all, or a part, of the interest income, with the result that the interest income in effect is taxed at only a 15-percent Canadian rate as compared with the 52-percent U.S. rate which would apply if the funds were held here.

The Secretary of the Treasury stated that the existence of this situation has served as an artificial enducement to the movement of U.S. capital abroad. He recommended that the foreign tax credit for certain investment income be computed apart from the foreign tax credit for all other foreign income, in order to end the use of this device. Your committee is in accord with the Secretary on this provision, except that it has limited the separate computation to interest income which is unrelated to the foreign trade or business.

B. *Comparison of committee amendments with House provision*

The House bill does not contain this provision.

C. *General explanation of provision*

Under present law the foreign tax credit which may be taken with respect to any foreign income is limited to the same proportion of the United States tax (computed without the credit) which the taxpayer's taxable income from sources within a foreign country, or all foreign

countries, is of his entire taxable income. This limitation, at the option of the taxpayer, can be applied either separately, i.e., on a per country basis, with respect to the income from each foreign country, or on an aggregate, or overall, basis with respect to all income received from all foreign countries.

Your committee's amendments provide that this limitation on the foreign tax credit is to be applied separately with respect to a certain type of interest income. It also provides that the limitation always is to be applied on a "per country" basis with respect to the specified interest income. Thus, if the taxpayer has been using the overall limitation, this limitation will continue to apply with respect to all income, other than the special interest income, from all foreign countries. However, the limitation will be applied separately for the special interest income derived from each foreign country. If the taxpayer is using the per country limitation, he will be permitted to continue on this basis but will have to apply the limitation separately with respect to the special interest income and other income derived from each country.

The interest income for which the separate computation of the limitation on foreign tax credit is to be made is all interest income, other than interest—

- (1) Derived from any transaction which is directly related to the active conduct of a trade or business in a foreign country or possession (such as interest income on accounts receivable by a foreign business arising from its ordinary business transactions);

- (2) Income derived from the conduct of a banking, financing or similar business; or

- (3) Income received from a corporation in which the taxpayer has at least a 10-percent voting stock interest.

The first exception above includes interest income derived from obligations received where it was necessary to dispose of an active trade or business carried on in a foreign country or U.S. possession or of securities in a foreign subsidiary corporation in which the taxpayer has at least a 10 percent interest.

The bill also provides transitional rules for applying carrybacks of unused credits from years before the separate computation for interest was required to years after such separate computation is required, and also for carryovers from years before such separate computation was required to years after such computation was required. These rules are intended to be applied both where the taxpayer is on a "per country basis" and where he is on an "overall basis." The bill provides that where amounts are carried back to years before this separate computation was required, the new provision can be ignored for the purpose of these carrybacks. Where all of these carrybacks are not used in these prior years, however, and therefore are carried forward to future years, then separate carryforwards are to be provided, determined upon the ratios of the special interest income and other income to total income in the year in which the unused credit arose. Where an unused foreign tax credit is carried forward from a year in which no separate computation was required to a year in which such a separate computation is required, the carryforwards are to be divided between the special interest income and other income in accordance with the ratio of each to the total income in the current year.

This provision is to apply with respect to taxable years beginning after the date of enactment of this bill but only with respect to interest resulting from transactions consummated after April 2, 1962. This date was selected because it represents the date on which the Secretary of the Treasury appeared before your committee and requested action on this provision.

XI. EARNED INCOME FROM SOURCES OUTSIDE THE UNITED STATES

(Sec. 11 of the bill and secs. 911 and 72(f) of the code)

A. Reasons for provision

Under present law an individual citizen of the United States who is a bona fide resident of a foreign country may exclude from his U.S. tax base his entire earned income from sources outside of the United States. In addition, an individual who goes abroad, but does not establish a foreign residence, may exclude from his U.S. tax base his earned income up to \$20,000 a year if he remains abroad for a period of 17 out of 18 consecutive months.

The President recommended that in the case of citizens living abroad in developed countries there be no exclusion for income earned abroad. In the case of less developed countries he would keep the present exclusion of up to \$20,000 a year in the case of those who are abroad 17 out of 18 months, and also provide the same \$20,000 ceiling with respect to those who are bona fide residents of a foreign country.

The House bill provides a ceiling on the exclusion for income earned abroad. However, it does not attempt to distinguish between U.S. citizens residing or present in developed and those in less developed countries. As a result, it retained the 17-out-of-18-month provision of present law without any major change in the presently applicable \$20,000 ceiling. In the case of a bona fide resident of a foreign country the House bill also provides the same \$20,000 limitation for the first 3 years the individual resides abroad. However, if the individual resides abroad for an uninterrupted period of more than 3 consecutive years a higher ceiling of \$35,000 is provided. Thus, during the first 3 years an individual is abroad the exclusion will be the same, whether the individual is a bona fide resident of the foreign country or merely there for 17 out of 18 months. However, in recognition of the fact that those who are abroad for longer periods of time are more dependent on the foreign economy, and less upon the U.S. economy, the higher ceiling of \$35,000 is provided in the case of these longer stays.

A second recommendation of the administration in this area relates to pensions and deferred compensation paid to U.S. citizens, after they have ceased to earn income abroad, but with respect to periods of time during which they did earn income abroad.

In the case of pensions generally, an employee receives back over his period of life expectancy (or in some cases in the first 3 years) the amount he paid toward his pension. The remainder of the pension payments he receives, consisting of contributions by the employer and interest on the funds while they were accumulating, is taxable to him as the pension or annuity payments are received.

In the case of a citizen who has been a bona fide resident of a foreign country, or been in a foreign country for a period of 17 out of 18

months or more, the employer's contributions toward the pension fund with respect to him, during the period the employee was abroad are treated in the same manner as his own contributions and, therefore, are not taxable to him when he draws his pension or annuity upon retirement. This is true even though he may be living in the United States next to someone who has worked for the same employer in the United States and is fully taxable on contributions made by the same employer.

To remove this discrimination the House bill provides that contributions by an employer will, to the extent that they relate to future employment, be fully taxable to the employee when he receives the pension payments reflecting these contributions. Thus, for the future even though employer contributions are attributable to a period when the employee was earning income abroad after 1962, these contributions by the employer will be taxable to him in the same manner as in the case of a domestic worker also receiving a pension. This will be true whether the employee is living in the United States, or abroad, at the time of the receipt of the pension payment.

Also, under the House bill where an individual receives deferred compensation after the end of the taxable year following the year in which the services were performed this compensation is not to be eligible for the exclusion for income earned abroad. The purpose of the exclusion is to provide a special inducement for American citizens or residents to hold employment abroad. However, there does not appear to be any reason to provide this special inducement long after the period in which the employment occurred. Moreover, this will treat deferred compensation under the exclusion the same as qualified pensions.

B. Comparison of committee amendments with House provision

Your committee has retained the House provision with respect to the limitations on the exclusion of income earned abroad with but two relatively minor modifications. Your committee also has accepted the House bill's treatment of contributions to a pension plan and of deferred compensation arrangements without change.

One of the changes made by your committee in the exclusion for income earned abroad is to deny any exclusion to an individual as a "bona fide resident of a foreign country" if the individual: (1) has earned income from sources within that foreign country; (2) has filed a statement with the authorities of that country that he is not a resident of it; and (3) has been held not subject to income tax as a resident of that country. This is intended to prevent an individual from avoiding income tax in the United States and the foreign country by taking inconsistent positions with respect to residence in the two countries.

The second change also relates to the exclusion for income earned abroad by bona fide residents of a foreign country. The attention of your committee was called to the fact that some residents of a foreign country have for a long time received certain fringe benefits, which in the past there was no need to value because of the unlimited exclusion. The type of fringe benefits referred to are noncash compensation, such as provision for a home or a car. It has been suggested that it may take some time to properly value these benefits. In addition, it has been suggested that the inclusion of such fringe benefits

in the U.S. tax base will present an adjustment problem for these individuals. To give such individuals time to properly value these benefits and adjust to their new tax status, your committee's amendments provide that these fringe benefits will be entirely excluded from taxable income for a taxable year ending in 1963, will be excluded to the extent of two-thirds for years ending in 1964, and will be excluded to the extent of one-third for years ending in 1965. Thereafter, these amounts will be taxable to the extent that they, together with any cash (or other) income earned by the individual from foreign sources exceed the \$20,000 or \$35,000 limitation, whichever is applicable.

C. General explanation of provision

1. *Ceiling on earned income exclusion.*—The bill places a ceiling on the amount which may be excluded from income in the case of a citizen of the United States who is a bona fide resident of a foreign country or countries. The bill provides that the total amount which may be excluded with respect to the first 3 years an individual is abroad as a bona fide resident is \$20,000 a year. This is the same ceiling which presently is applicable in the case of citizens or residents of the United States who are abroad for a period of 17 out of 18 months. However, in the case of the U.S. citizen who has been a bona fide resident of a foreign country or countries for more than 3 years, the total amount which may be excluded under the bill in this case (except for the fringe benefits referred to below) is to be \$35,000 per year instead of \$20,000. This higher ceiling is to apply with respect to any portion of a taxable year remaining after the individual has been a bona fide resident of a foreign country or countries for the uninterrupted 3-year period. Where at the time of the passage of this legislation the individual already has been a bona fide resident for 3 years or more, this higher ceiling will, of course, become applicable immediately.

In applying either the \$20,000 or \$35,000 ceiling under community property laws the total community income excludable may not exceed the amount which would be excludable if this income were not community income. Thus, one \$20,000 or \$35,000 ceiling will apply with respect to the husband's earnings abroad even though under community property law, half of this income is the income of the wife. However, if both husband and wife are abroad and earn income, separate ceilings will be applied with respect to the earnings attributable to the services of each.

The \$20,000 or \$35,000 limitation applicable to a bona fide resident of a foreign country is not to apply to certain fringe benefits during a transitional period. The fringe benefits referred to are the right to use property or facilities, such as a home or a car. No part of such compensation received from sources without the United States (unless paid by the U.S. Government) is to be taken into account, and only other earned income in excess of \$20,000 or \$35,000 will be taxed for taxable years ending in 1963. For taxable years ending in 1964, one-third of the value of this type compensation is to be taken into account and for taxable years ending in 1965, two-thirds of the value is to be taken into account. Thereafter, such compensation will be fully taxable, subject to the \$20,000 or \$35,000 limitation, in the same manner as any other compensation.

The bona fide resident rule has also been modified to provide that an individual is not to be treated as a bona fide resident of a foreign

country if he has earned income in the foreign country, has made a statement to the authorities of that country that he is not a resident of it, and has been held not subject as a resident of that country to its income tax. This does not prevent an individual from qualifying under the exclusion for presence in a foreign country or countries for 17 out of 18 months. It also does not deny an individual an exclusion as a bona fide resident if, under wholly consistent positions with respect to residence in the United States and a foreign country, he is held by both countries to be a nonresident.

2. *Deferred compensation.*—Under present law the bona fide resident rule and the 17- out of 18-month rule work somewhat differently in determining the year to which the exclusion relates. The bona fide resident rule at present provides an exclusion without limit for amounts received from sources without the United States which are "attributable" to the period when the U.S. citizen was a bona fide resident of a foreign country. This means that deferred compensation attributable to a period of foreign service is excludable even though received many years after the period of service.

The 17- out of 18-month rule, however, because of the \$20,000 ceiling, has been interpreted as limiting the exclusion which an individual may receive to the proportion of the taxable year, during which the payment was *received*, in which the individual was abroad. Thus, where the individual receives deferred compensation after he has been back in the United States for an entire taxable year, no exclusion is available. Moreover, in this latter case, hardship situations have occurred where an individual, who has returned to the United States early in a year, has received payments attributable to service in the prior year, but because the individual is in the United States most, or all, of the year little, or no, exclusion is available with respect to this income.

The bill eliminates the problems referred to above by attributing the income, for purposes of applying the dollar limitation on the exclusion, to the year in which the service is performed. This means that the exclusion, merely because the individual has returned to the United States before receiving the payment, will not be denied. However, most deferred compensation is made ineligible for the exclusion by providing that no exclusion will be allowed for amounts received more than 1 year after the close of the taxable year in which the services are performed.

3. *Pension income.*—The provision of present law dealing with annuities (sec. 72(f)) provides that in determining what the employee or annuitant paid for an annuity contract, there is to be included contributions of the employer, if, had these contributions been paid to the employee in the first instance, they would not have been taxable to him. This provision generally has the effect of excluding employer contributions to a pension plan from tax (in the year the pension payment is received) where the employee is abroad and qualifies for the exclusion.

The bill nullifies this section by providing that the exclusion for income earned abroad is not to be available in the case of amounts contributed after December 31, 1962, and subsequently received as pensions or annuities or amounts which otherwise would be included in gross income in the case of beneficiaries of tax-exempt trusts (sec. 402(b)), beneficiaries under nonqualified annuities (sec. 403(c)), or

beneficiaries under certain forfeitable contracts purchased by exempt organizations (sec. 403(d)).

The bill also makes it clear that the tax-free status of employer contributions will be continued in the case of contributions made after December 31, 1962, to the extent that they provide pension or annuity credits where these credits are attributable to services performed on or before that date if the pension or annuity plan provisions were in existence on March 12, 1962.

4. *Effective date.*—The changes made by this provision (except for the fringe benefits exclusion) are to apply to amounts received after December 31, 1962, but only to the extent that these amounts are attributable to services performed after that date or services performed on or before that date, where on March 12, 1962, there did not exist a right to receive these amounts.

XII. CONTROLLED FOREIGN CORPORATIONS

(Sec. 12 of bill and secs. 951–972 of code)

A. *Reasons for provision*

Under present law foreign corporations, even though they may be American controlled, are not subject to U.S. tax laws on foreign source income. As a result no U.S. tax is imposed with respect to the foreign source earnings of these corporations where they are controlled by Americans until dividends paid by the foreign corporations are received by their American parent corporations or their other American shareholders. The tax at that time is imposed on the American shareholder with respect to the dividend income received, and if this shareholder is a corporation it is eligible for a foreign tax credit with respect to the taxes paid by the foreign subsidiary. In the case of foreign subsidiaries, therefore, this means that foreign income taxes are paid currently, to the extent of the applicable foreign income tax, and not until distributions are made will an additional U.S. tax be imposed, to the extent the U.S. rate is above that applicable in the foreign country. This latter tax effect has been referred to as “tax deferral.”

The President in his tax message last year questioned the desirability of providing tax deferral with respect to earnings of U.S.-controlled companies except in the case of investments in less developed countries. In this respect he emphasized removing tax deferral in the case of what have been called “tax havens.” Thus he stated:

The undesirability of continuing deferral is underscored where deferral has served as a shelter for tax escape through the unjustifiable use of tax havens such as Switzerland. Recently more and more enterprises organized abroad by American firms have arranged their corporate structures—aided by artificial arrangements between parent and subsidiary regarding intercompany pricing, the transfer of patent licensing rights, the shifting of management fees, and similar practices which maximize the accumulation of profits in the tax haven—so as to exploit the multiplicity of foreign tax systems and international agreements in order to reduce sharply or eliminate completely their tax liabilities both at home and abroad.

In this area the President recommended the:

* * * elimination of the tax haven device anywhere in the world, even in the underdeveloped countries, through the elimination of tax deferral privileges for those forms of activities, such as trading, licensing, insurance, and others, that typically seek out tax haven methods of operation. There is no valid reason to permit their remaining untaxed regardless of the country in which they are located.

The House bill did not go as far as the President recommended. It did not eliminate tax deferral generally, but instead was concerned primarily with what had been referred to as "tax haven" devices. To accomplish this result the House bill in general sought to end tax deferral for income derived by U.S. controlled foreign corporations from insurance abroad of U.S. risks; for certain foreign investment income of these corporations; for their income from foreign sales subsidiaries which are separately incorporated from their manufacturing operations; and income invested in "nonqualified property," that is, generally, earnings not needed in the same trade or business or funds indirectly brought back to the United States without full payment of U.S. tax. In most of the categories described above deferral of the tax was not denied where earnings were reinvested in a less developed country. In addition, under the House bill (sec. 6) a special rule was added which in general provided that in the case of sales between a domestic corporation and a foreign controlled corporation the income arising from the transaction was to be divided between the corporations involved on the basis of payroll, assets, and sales or promotional expenses attributable to the United States or the foreign country or countries.

B. Comparison of committee amendments with House provision

Your committee has substituted a provision for the House bill sections 6 and 13 which differs in several important respects from the House bill sections. However, your committee's amendments, like the House bill, also are designed to end tax deferral on "tax haven" operations by U.S. controlled corporations.

In the area of income arising from insurance of U.S. risks, income from passive investments, and income from sales subsidiary operations, your committee's provision is much the same as the House bill. In these areas among the more significant changes are provision for inclusion of passive investment and sales subsidiary income in the tax base of U.S. shareholders only if it represents 30 instead of 20 percent of gross income, and the expansion of the taxable categories to include service income performed for related persons. Also important are the changes relating to exclusions from the tax base for reinvestments of income. Under your committee's amendments reinvestments which reduce the tax base are limited to reinvestments of dividends and interest (or gains on the sale of investments) and these income items must not only be reinvested in less developed countries but also must be derived from such countries as well. However, the qualifying reinvestments are not limited to those in a corporation in a less developed country in which the taxpayer and no more than four other Americans have an interest of more than 50 percent, as was provided by the House bill.

Your committee's amendments differ considerably from the House provision in that they are no longer concerned with the reinvestment of earnings arising from the active conduct of a trade or business, except to be sure that these earnings are not indirectly brought back to the United States in a manner which avoids the U.S. tax. Thus, there is no requirement that such earnings be reinvested in the same trade or business in which the taxpayer has been engaged in the last 5-year period or before December 31, 1962.

A second area in which your committee's amendments differ from the House provision is in the treatment of patents, copyrights, formulas, and processes, etc., developed or acquired in the United States. Under the House bill tax deferral in the case of controlled foreign corporations having such patents, copyrights, etc., was to be denied and the income either actually or constructively attributable to such items was to be taxed to the U.S. shareholders. Your committee's bill, in a separate section (sec. 16), provides for gains from any such patents, copyrights, etc., to be taxed as ordinary gain in most cases at the time of transfer of the patent or other rights from the domestic corporation to the foreign controlled subsidiary.

A third important change in your committee's amendments is the deletion of the income allocation rule provided by section 6 of the House bill.

Your committee's amendments also differ substantially from the House provision in that they provide two major relief provisions, or "escape valves," which may be used by taxpayers to make section 12 inoperative in their case. One of these is designed to make section 12 inoperative where the overall foreign and U.S. taxes paid with respect to the foreign operations is not substantially below what the U.S. taxes would be on the income. Thus, your committee's amendments provide a schedule of effective foreign tax rates and corresponding percentages of distribution which if complied with make section 12 inoperative. The second major relief provision is the export trade corporation provision. This provides, in general, that where the products sold are those produced or grown in the United States, and where the profit attributable to these operations complies with certain specified limitations, then this "export-trade income" is not to be subject to section 12 if the earnings are reinvested in an export trade business.

Your committee's amendments are described briefly below.

C. General explanation of provision

1. *The general pattern of the provisions.*—The bill provides that certain types of income of controlled foreign corporations, even though undistributed, are to be included in the income of U.S. shareholders in the year the income is earned by the foreign corporation. In these cases the shareholders are permitted to take foreign tax credits to the same extent as if actual distributions had been made. Under the bill only U.S. shareholders are taxed on the undistributed income.¹ The U.S. shareholders to be so taxed must, either actually or constructively, have at least a 10-percent interest in the voting power of all classes of voting stock of a controlled foreign corporation. A

¹ U.S. shareholders are defined in the bill as "U.S. persons" with the 10-percent stockholding. U.S. persons, in general, are U.S. citizens and residents and domestic corporations, partnerships, and estates or trusts.

foreign corporation is a "controlled foreign corporation" for this purpose only if more than 50 percent of the combined voting power of all classes of stock is owned directly or constructively by these U.S. shareholders having a 10 percent or greater stock interest.²

There are two categories of undistributed income which under your committee's amendments are taxed to the U.S. shareholders of controlled foreign corporations. The first of these categories is referred to as income derived from insurance or reinsurance of U.S. risks. The second category is referred to as foreign base company income. This foreign base company income can in turn be broken down into base company personal holding company income, base company sales income, and base company service income. Collectively, the income derived from insurance or reinsurance of U.S. risks and foreign base company income is referred to in the bill as "subpart F income." The amount of this which may be taxed in any year is limited to the earnings and profits of the controlled foreign corporation for the taxable year less deficits not otherwise offset since 1959.

In addition to certain types of undistributed earnings being treated as if they were distributed and taxed to the U.S. shareholders of controlled foreign corporations, the bill also provides that earnings invested in U.S. property (with certain exceptions) are to be taxed to the U.S. shareholders. In general terms, U.S. property is property located in the United States or having a situs in the United States unless used in the foreign trade or business. Earnings invested in U.S. property are treated first as arising out of subpart F income which means that to the extent that subpart F income is taxed to U.S. shareholders, the income of the corporation will not again be taxed to the U.S. shareholders because of investments in U.S. property. Similarly, actual dividend distributions are treated first as being paid out of earnings invested in U.S. property, then out of subpart F income, and only finally, if any balance remains, out of the accumulated earnings and profits of the corporation which have not already been taxed to the shareholders. Only when actual dividends are treated as paid out of this latter category do they represent taxable dividends to the shareholders.

The earnings of a corporation classified as subpart F income or as investments in U.S. property, give rise to taxable income to the U.S. shareholders only for the portion of the earnings represented by the portion of the year in which the corporation was a controlled foreign corporation. Moreover, the shareholders are taxed only on their allocable share of the earnings with the result that any holdings by foreigners or by Americans having less than a 10-percent interest are not taxed to any shareholders under this provision.

2. *Income derived from insurance of U.S. risks.*—Since the passage of the Life Insurance Company Income Tax Act of 1959, which for the first time in many years imposed a tax on underwriting gains of these companies, it is understood that a number of the companies involved have attempted to avoid tax on the gains by reinsuring their policies abroad. In other cases the tax has been avoided by placing the initial policy with a foreign insurance company either controlled by an American insurance company or controlled by other American businesses.

² The 10-percent holding may be on any day of the taxable year of the corporation. A special additional test of control provided in the case of insurance is discussed under the heading of insurance.

To meet this problem the bill provides that where a controlled foreign corporation receives premiums or other consideration for reinsurance or the issuing of insurance or annuity contracts on property in, or residents of, the United States the income attributable to this is to be taxed to the U.S. shareholders as a part of subpart F income. This provision does not apply, however, unless the controlled foreign corporation receives premiums or other consideration for reinsurance or the issuing of insurance or annuity contracts representing U.S. risks which are in excess of 5 percent of their total premiums and other consideration.

The bill also covers the type of situation where the controlled foreign corporation does not hold the policies involving U.S. risks but instead holds other policies which, by arrangement with another corporation, it has received instead of the insurance involving the U.S. risks, while the other corporation holds the policies involving the insurance on property in, or residents of, the United States.

In the case of insurance there also is an alternative definition of a controlled foreign corporation. Under the alternative if U.S. persons hold from 25 to 50 percent of the stock, any income from insurance or reinsurance on U.S. risks is included in income taxed as subpart F income where the U.S. risks represent 75 percent of the gross amount of all premiums and other considerations received with respect to risks held by the company. This alternative rule for control is designed to cover cases where the principal business is the U.S. risks but the control is decreased in order to avoid the application of this provision.

The income subject to tax in the hands of the shareholders in the case of life insurance companies is total gain from operations to the extent attributable to U.S. risks. In effect this represents all (not 50 percent) of the underwriting income as well as net investment income.

3. Foreign base company income.—The second component of the subpart F income which will be taxed to the U.S. shareholders in the case of controlled foreign corporations is foreign base company income. This consists of foreign personal holding company income, foreign base company sales income and foreign base company services income, which are discussed below under paragraph headings *a*, *b*, and *c*. Excluded from this foreign base company income is dividend and interest income from 10-percent-related persons (and gains from the sale or exchange of the underlying investments) which are attributable to certain investments in less developed countries. Also excluded is certain income from shipping. In addition, special rules apply where the foreign base company income represents less than 30 percent or more than 70 percent of the controlled foreign corporation's gross income. A further exception is provided for foreign corporations where it is established to the satisfaction of the Treasury Department that the foreign corporations are not availed of to reduce taxes. These exclusions and special rules are discussed under paragraph heading *d*. below.

a. Foreign personal holding company income.—The income referred to here is income which under other provisions of the code already is defined as "foreign personal holding company income." Generally speaking, this is income which is passive in character. It includes income from dividends, interest, most royalties, annuities, etc. Three modifications made in this definition of "foreign personal holding company income" for purposes of this provision are noted below.

Your committee, while recognizing the need to maintain active American business operations abroad on an equal competitive footing with other operating businesses in the same countries, nevertheless sees no need to maintain the deferral of U.S. tax where the investments are portfolio types of investments, or where the company is merely passively receiving investment income. In such cases there is no competitive problem justifying postponement of the tax until the income is repatriated.

The section adopts the definition of "foreign personal holding company income" appearing elsewhere in the code (sec. 553) with various modifications and adjustments.

First, *all* rental income is included in foreign personal holding company income for purposes of this provision. (Under sec. 553, rent income is only included as foreign personal holding company income if it constitutes less than 50 percent of the gross income of the corporation.)

The second important modification provides that certain income otherwise defined as foreign personal holding company income is not foreign personal holding company income for purposes of this new provision when it arises in connection with certain actual business activities. Specifically, it is provided that rents and royalties received from an unrelated person and derived from the active conduct of a trade or business will not be considered foreign personal holding company income. It is also provided that dividends, interest and gains from the sale or exchange of stock or securities derived in the conduct of a banking, financing or similar business will not be considered foreign personal holding company income. Another exception is made for dividends, interest and gains from the sale of stock or securities derived from the investments made by an insurance company of its unearned premiums or reserves necessary for the proper conduct of its insurance business.

Finally, certain exceptions are made for income received from related parties. Your committee saw no reason for taxing the U.S. shareholders on dividends received by a controlled foreign corporation from a related party where the U.S. shareholder would not have been taxed if he had owned the stock of the related party directly. For this reason, dividends and interest received from a related corporation which is organized under the laws of the same foreign country as the controlled foreign corporation and has a substantial part of its assets used in its trade or business located in that foreign country, are not included in foreign personal holding company income. Rents, royalties, and similar amounts received from a related party (whether or not incorporated in the same jurisdiction) are also excluded from foreign personal holding company income if these amounts are received for the use of property within the country in which the controlled foreign corporation is incorporated. Also excluded from the definition of foreign personal holding company income is interest received by a banking or financial business firm from a related person also engaged in the banking or financing business, if the business of each is predominantly with unrelated persons. This means that the foreign personal holding company income will not arise merely because of normal business transactions between two or more related financial institutions.

b. Foreign base company sales income.—Foreign base company sales income is income derived from the purchase and sale of personal property if the property is either purchased from a related person or sold to a related person. However, this applies only where the property purchased is manufactured, produced, grown, or extracted outside of the country where the controlled foreign corporation is organized and the property also is sold for use, consumption or use outside of that country. The provision also covers similar cases where the controlled foreign corporation does not take title to the property but acts on a fee or commission basis.

The “foreign base company sales income” referred to here means income from the purchase and sale of property, without any appreciable value being added to the product by the selling corporation. This does not, for example, include cases where any significant amount of manufacturing, major assembling, or construction activity is carried on with respect to the product by the selling corporation. On the other hand, activity such as minor assembling, packaging, repackaging or labeling will not be sufficient to exclude the profits from this definition.

The sales income with which your committee is primarily concerned is income of a selling subsidiary (whether acting as principal or agent) which has been separated from manufacturing activities of a related corporation merely to obtain a lower rate of tax for the sales income. This accounts for the fact that this provision is restricted to sales of property, to a related person, or to purchases of property from a related person. Moreover, the fact that a lower rate of tax for such a company is likely to be obtained only through purchases and sales outside of the country in which it is incorporated, accounts for the fact that the provision is made inapplicable to the extent the property is manufactured, produced, grown, or extracted in the country where the corporation is organized or where it is sold for use, consumption, or disposition in that country. Mere passage of title or the place of the sale are not relevant in this connection.

Also included in foreign base company sales income are operations handled through a branch (rather than a corporate subsidiary) operating outside of the country in which the controlled foreign corporation is incorporated, if the combined effect of the tax treatment accorded the branch, by the country of incorporation of the controlled foreign corporation and the country of operation of the branch, is to treat the branch substantially the same as if it were a subsidiary corporation organized in the country in which it carries on its trade or business.

c. Foreign base company services income.—Foreign base company services income is income derived from the performance of technical, managerial, engineering, architectural, scientific, skilled, industrial, commercial, or similar services, but only where they are performed for a related person and are performed outside the country in which the controlled foreign corporation is organized.

As in the case of sales income, the purpose here is to deny tax deferral where a service subsidiary is separated from manufacturing or similar activities of a related corporation and organized in another country primarily to obtain a lower rate of tax for the service income.

d. Exclusions and special rules for foreign base company income.—The three categories of income described above which are called foreign base company income are to be taxed to the U.S. shareholders of a foreign controlled corporation only if this foreign base company

income represents at least 30 percent of the gross income of the corporation. On the other hand, if the foreign base company income exceeds 70 percent of gross income, the entire gross income (reduced by deductions) of the corporation is to be treated as foreign base company income and treated as if it were distributed pro rata to the U.S. shareholders. Thus, where this foreign base company income is relatively minor, the shareholders will not be taxed on any of it; where it is a major factor, they are to be taxed on the entire income of the corporation. Otherwise, only the actual foreign base company income is to be taken into account.

The bill provides that although otherwise classified as foreign base company income, certain categories of income may, nevertheless, not be taxable to the U.S. shareholders of the controlled foreign corporation. The amounts which may not be taxed to these shareholders are dividend and interest income and gains from the sale or exchange of investments, but only if this income or these gains arose from qualified investments in less developed countries and only to the extent that these amounts are reinvested in qualified investments in less developed countries. What constitutes qualified investments in these less developed countries is discussed under paragraph heading (4) below. If a reduction in foreign base company income is granted for an increase in qualified investments in a less developed country and then at a later time these investments are decreased, then to the extent of any foreign base company income previously omitted from the tax base of the U.S. shareholders, there is to be an increase in the income of the controlled foreign corporation taxable to its U.S. shareholders.

This exception for interest and dividend income (and certain gains) from less developed countries is intended to make it possible for a controlled foreign corporation, which is at least in part a holding company, to reinvest dividends and interest obtained from a subsidiary in a less developed country in another subsidiary in a less developed country, without its shareholders being taxed on this income.

Another exception from the application of the foreign base company income is provided for income derived from the use (including the hiring or leasing) of aircraft or vessels used in foreign commerce or services directly related to the use of the aircraft or vessel. This exception was provided by your committee primarily in the interests of national defense. In this regard it was believed desirable to encourage a U.S.-owned maritime fleet and U.S.-owned airlines operating abroad.

A final exception provided from the foreign base company income is for any income received by a controlled foreign corporation, if it is established to the satisfaction of the Treasury Department that with respect to this income the controlled foreign corporation has not effected a substantial reduction of income or similar taxes.

4. *Less developed country corporations.*—As indicated above, interest and dividend income received from 10 percent related persons (and gains on the sale of the underlying investments) may be deducted from the subpart F income which is taxable to the U.S. shareholders of a controlled foreign corporation only if the income was attributable to qualified investments in a less developed country and was reinvested in qualified investments in less developed countries.³ Provision is

³ The bill provides for a reduction in subpart F income to the extent of this dividend and interest income from less developed countries or the increase in investments in these countries, whichever is the lesser.

also made for an increase in the income taxable to the U.S. shareholders whenever there is a decrease in qualified investments in a less developed country, to the extent they were initially attributable to dividends or interest of the type referred to above. The concept of less developed country corporations is also used under section 9 of this bill in determining when the "gross-up" of dividend income is not to be applied. In addition, section 15 of the bill makes use of the concept of less developed country corporations, since the ordinary income treatment provided under that provision in the case of certain corporate liquidations and stock sales does not apply where the corporation involved is a less developed country corporation the stock of which was held for more than 10 years.

Qualified investments in less developed countries under this provision consist of stock of a "less developed country corporation" and obligations of such corporations which at their time of acquisition by the controlled foreign corporation had a maturity of 5 years or more. However, for either the stock or obligations to qualify the controlled foreign corporation must own 10 percent or more of the voting power of all classes of stock of the less developed country corporation. In addition, qualified investments also include obligations of a less developed country.

"Less developed country corporations" consist of two categories. First, they include foreign corporations incorporated in a less developed country, which are engaged in the active conduct of a trade or business, which derive 80 percent or more of their income from sources within less developed countries and which have 80 percent or more (in value) of their assets in property generally used in a trade or business in a less developed country or in certain other specified types of associated property. The specific assets in which this 80 percent of the assets must be invested are—

- (1) Property used by it in its trade or business in less developed countries;

- (2) Money and bank accounts;

- (3) Stock and obligations (having a maturity of 5 years or more at time of acquisition) of less developed country corporations;

- (4) An obligation of a less developed country;

- (5) Investments required because of restrictions imposed by less developed countries;

- (6) Certain U.S. property, such as U.S. Government bonds, money, property purchased in the United States for export, etc., which although having a U.S. situs, are excluded from the definition of "U.S. property." (For a more specific listing of the U.S. property exceptions, see par. (5) below.)

The second category of corporation classified as a less developed country corporation are certain shipping or aircraft companies. These corporations must be foreign corporations (not necessarily incorporated in a less developed country) receiving 80 percent or more of their gross income from:

- (1) The use (or hiring or leasing for use) in foreign commerce of aircraft or vessels registered under the laws of a less developed country;

- (2) From the performance of services directly related to these aircraft or vessels;

(3) From the sale or exchange of such vessels or aircraft;

(4) Dividends and interest received from foreign corporations which are themselves less developed country corporations under the definition contained in this category and in which the corporation in question had at least a 10 percent stock interest; and

(5) Gain from the sale or exchange of stock or obligations of foreign corporations which are less developed country corporations.

In addition, for these shipping or aircraft companies to qualify as less developed country corporations they must have 80 percent or more of their assets invested in assets used for the production of the income described above and in property which although having a situs in the United States is not considered as "U.S. property" (see exceptions listed in par (5) below).

Less developed countries under the bill are defined as foreign countries (other than areas within the Sino-Soviet bloc) or possessions of the United States where the President of the United States has designated such a country or possession as economically less developed.⁴ However, the following countries are in no event to be considered as less developed countries:

Australia	Luxembourg
Austria	Monaco
Belgium	Netherlands
Canada	New Zealand
Denmark	Norway
France	Union of South Africa
Germany (Federal Republic)	San Marino
Hong Kong	Sweden
Italy	Switzerland
Japan	United Kingdom
Liechtenstein	

Once a country has been designated as a less developed country, the President is not to terminate that designation without giving 30 days prior notice to the Senate and House of Representatives of his intention to do so. Moreover, if at the time of acquisition, property was qualified investment in a less developed country, this property is to continue to qualify thereafter even though the country ceases to be a less developed country.

5. *Investment of earnings in U.S. property.*—In addition to the income from insurance of U.S. risks and foreign base company income, U.S. shareholders of controlled foreign corporations also are to be taxed on other earnings of the corporation to the extent of the corporation's investments in U.S. property. For this purpose U.S. property is that acquired after December 31, 1962, which is—

- (1) Tangible property located in the United States;
- (2) Stock of a domestic corporation;
- (3) An obligation of an U.S. person; or
- (4) Any right to use in the United States a patent or copyright, an invention, model, or design whether or not patented, a secret formula or process, or any other similar property right, but only if any of the foregoing is acquired or developed by the controlled foreign corporation for use in the United States.

⁴ Oversea territories, departments, provinces, or possessions for this purpose may be treated as separate countries. Thus, even though the "home" country may be classified as developed, the oversea area may be considered less developed.

Certain exceptions, however, are made to the above categories with the result that the term "U.S. property" does not include—

- (1) Investments in U.S. bonds, money, or bank accounts;
- (2) Property purchased in the United States for export to, or for use in, foreign countries;
- (3) Loans arising in connection with the sale or processing of property where the amount of the loan would be considered ordinary and necessary to carry on the trade or business of both the lending and borrowing corporation had the sale been made between unrelated persons, or in the case of processing, would have been required of the lending corporation had the transaction involving such processing occurred between unrelated persons;
- (4) Aircraft, railroad rolling stock, vessels, motor vehicles, or containers used in the transportation of persons or property in foreign commerce predominantly outside the United States;
- (5) Assets of an insurance company representing reserves attributable to contracts which do not involve U.S. risks; and
- (6) Assets of the controlled corporation equal to the earnings and profits accumulated after December 31, 1962, and taxed as income from sources within the United States, of a foreign corporation engaged in trade or business here.

Generally, earnings brought back to the United States are taxed to the shareholders on the grounds that this is substantially the equivalent of a dividend being paid to them. The exceptions noted above, however, are believed to be normal commercial transactions without intention to permit the funds to remain in the United States indefinitely (except in the case of the last category where full U.S. corporate tax is being paid).

6. *Minimum distribution to domestic corporation.*—A major relief provision under your committee's amendments is that which provides that subpart F income (income from insurance of U.S. risks plus foreign base company income) is not to be taxed to the U.S. corporate shareholders if a schedule of minimum distributions is met. The minimum distribution required varies with the effective foreign tax rate and is as follows:

If the effective foreign tax rate is (percentage)—	The required minimum distribution of earnings and profits after foreign taxes is (percentage)—
Under 10.....	90
10 or over but less than 20.....	80
20 or over but less than 30.....	70
30 or over but less than 40.....	60
40 or over but less than 42.....	50
42 or over but less than 44.....	38
44 or over but less than 46.....	26
46 or over but not more than 47.....	14
Over 47.....	0

The purpose of this provision is to forego any tax on the U.S. shareholders with respect to undistributed income of controlled foreign corporations in those cases where the combined foreign tax and United States (to the extent the latter is paid on the distributed income) is not substantially below the U.S. corporate tax rate. The lower the foreign tax rate is, of course, the greater the distribution must be, and the greater the proportion of the total which must be

subject to U.S. tax, if the aggregate tax is not to be substantially below the U.S. corporate tax rate. Table 2 below shows the combined U.S. and foreign taxes implicit in the schedule set forth in this provision. This is shown both on the assumption that the "gross-up" provision in section 9 applies and that it does not apply.⁵ The table also shows the range of combined taxes in each bracket, assuming the application of both the minimum and the maximum effective foreign tax rate is applied in each bracket. It will be noted that the combined effective tax rates range from 42.4 to 47 percent where the "gross-up" provision applies and from 37.9 to 47 percent where it does not. For the most part, however, the combined tax is around 46 percent where the "gross-up" applies and 44 percent where it does not.

TABLE 2.—Total U.S. and foreign tax burden resulting from minimum distribution schedule applied to \$100 of earnings of a controlled foreign corporation

Assumed effective foreign tax rate	Percent distribution required by schedule	Combined U.S. and foreign tax if dividend is—	
		"Grossed up"	Not "grossed up"
9 percent.....	90	\$47.70	\$44.22
10 percent.....	80	43.60	40.24
19 percent.....	80	45.40	40.38
20 percent.....	70	42.40	37.92
29 percent.....	70	45.10	40.43
30 percent.....	60	43.20	39.24
39 percent.....	60	46.80	43.76
40 percent.....	50	46.00	43.60
41 percent.....	50	46.50	44.25
42 percent.....	38	45.80	44.20
43 percent.....	38	46.42	44.95
44 percent.....	26	46.08	45.16
45 percent.....	26	46.82	46.00
46 percent.....	14	46.84	46.45
47 percent.....	0	47.00	47.00

Taxpayers are permitted to apply the minimum distribution schedule—

- (1) separately for each controlled foreign corporation,
- (2) for each chain of controlled foreign corporations,
- (3) for all controlled foreign corporations, or
- (4) for all controlled foreign corporations other than less developed country corporations.

In addition, taxpayers for purposes of this minimum distribution schedule may treat branches as if they were wholly owned foreign subsidiaries distributing 100 percent of their earnings. For this purpose branches maintained in Puerto Rico or a possession of the United States are taken into account, if they would be controlled foreign corporations if incorporated under the laws of Puerto Rico or the possession, and the gross income of the U.S. shareholder includes income derived from sources within Puerto Rico or the possession.

A taxpayer in computing the minimum distribution may omit income from a foreign corporation if it is established to the satisfaction of the Treasury Department that its earnings were blocked because of

⁵ The method of computing the combined tax can be illustrated by the case of the 10 percent foreign tax, 80 percent distribution and no "gross-up" of the dividend. The foreign tax on the \$100 in this case is \$10, leaving \$90 after foreign tax. Of this amount 80 percent or \$72 is distributed. A 52 percent U.S. tax on this is \$37.44. The credit allowed for foreign taxes paid is \$7.20 ($7\frac{1}{2}\% \times \10), leaving a net U.S. tax of \$30.24. This plus the \$10 foreign tax gives a combined tax of \$40.24.

currency or other restrictions imposed by the laws of a foreign country. The minimum distributions referred to above may be computed if the taxpayers so elect for an affiliated group of corporations (eligible to file a consolidated return) in the same manner as if they were a single U.S. corporation.

The effective foreign tax rate referred to in the minimum distribution is determined by expressing the income, war profits, or excess profits taxes paid or accrued to the foreign countries or possessions of the United States by the foreign corporation (or corporations) involved as a percent of the earnings and profits of the foreign corporation (or corporations) plus the foreign taxes themselves. The earnings and profits referred to here are to be determined according to rules substantially similar to those applicable to domestic corporations. Taxpayers, however, will, by regulations, be permitted to depart from the U.S. rules where their books are kept on a different basis and the variations in computations are not important. A distribution may be treated as being made in a year if paid within 60 days after the end of that year or in such longer period as the Treasury Department by regulations prescribes. In addition, if a U.S. shareholder in making its return applies for the minimum distribution schedule and subsequently it is found that, for reasonable cause, it has not met the minimum schedule, then subsequent distributions may be made by the controlled foreign corporation (in a manner prescribed under regulations) and be treated as if they had been made in the earlier qualifying period.

7. *Export trade corporation.*—A second major relief provision provided by the bill is the exception for “export trade corporations.” The bill provides that foreign base company income (i.e., foreign personal holding company income, base company sales income and base company service income) in the case of export trade corporations is to be reduced by the amount of their foreign base company income which consists of “export trade income.” Thus, the U.S. shareholders of controlled foreign corporations will not be taxed on undistributed income of these corporations (to the extent that it represents foreign base company income) if these controlled foreign corporations are export trade corporations having “export trade income.” However, the exclusion for foreign base company income representing export trade income may not exceed the lesser of—

(1) $1\frac{1}{2}$ times “export promotion expenses,” (attributable to the otherwise excluded income) or

(2) 10 percent of gross receipts of the export trade corporation from the sale, installation, operation, maintenance or use of the property from which it derives the income which otherwise is excluded. (In the case of commissions or fees, this 10 percent is measured on the same basis on which the commissions or fees are based.)

With the limitations it is not expected that the allocation rule in present law (sec. 482) will be needed in many cases involving export trade corporations.

The export trade income which is to be deferred also is limited to the portion of this income which is invested by the export trade corporation in “export trade assets” (or, more specifically, by the portion of the increase in investments in such assets which is attributable to export trade income which constitutes foreign base company income).

Any amount of export trade income where U.S. taxation has been deferred because of such investments, will subsequently be taxed if there is a decrease in export trade assets.

This provision is intended to continue tax deferral in the case of corporations engaged in export trade who are selling abroad products produced, grown, or extracted in the United States. This is intended as an encouragement to export trade. Nevertheless, limitations are imposed to provide that the income attributed to the export trade corporation is in line with the income actually generated by such activity. This is the function of limiting the export trade income to $1\frac{1}{2}$ times export promotion expenses or 10 percent of gross receipts from the property, whichever is the lesser. Also, the provision is intentionally limited to the extent to which the export trade income receiving the special treatment is used for the expansion of the export trade business, itself.

An "export trade corporation" for this purpose is defined as a controlled foreign corporation which derives 90 percent of its gross income (for the prior 3-year period) from sources without the United States and one which derives 75 percent or more of its gross income (for the same 3-year period) from export trade income. However, if 50 percent or more of the gross income of the controlled foreign corporation (for the same 3-year period) is derived from income from agricultural products grown in the United States, this 75-percent requirement is not to apply.

The "export trade income" is an element in the definition of an export trade corporation and also, to the extent included in foreign base company income, represents the maximum amount of subpart F income upon which tax deferral may be granted. Export trade income is net income from—

(1) the sale to an unrelated person (where there is less than 50-percent common control) for use, consumption, or disposition outside the United States of export property. Export property is property manufactured, produced, grown, or extracted in the United States. (In addition to the sale of export trade property, there also is included commissions, fees, etc., from the performance of services with respect to these sales or with respect to the installation or maintenance of export property);

(2) commissions, fees, and other income from commercial, industrial, or other services performed by an unrelated person outside of the United States in connection with patents, copyrights, secret processes and formulas, goodwill, trademarks, trade brands, franchises, etc., acquired or developed and owned by the domestic corporation involved;

(3) commissions, fees, rentals or other income for the use of export property by an unrelated person or attributable to the use of export property in rendering technical, scientific, or engineering services to an unrelated person; and

(4) interest from certain obligations which are export trade assets.

"Export trade assets" are the type of property in which export trade income must be reinvested if its taxation is to be deferred. Export trade assets are—

(1) working capital reasonably necessary for the production of the export trade income;

(2) inventory of export property, i.e., property manufactured, produced, grown, or extracted in the United States, held for use, consumption, or disposition outside of the United States;

(3) facilities located outside of the United States for the storage, handling, transportation, packaging or servicing of export property; or

(4) evidences of indebtedness executed by unrelated persons in connection with the payment for purchases of export property or services.

As indicated previously, the export trade income (to the extent entering into foreign base company income) which may be deferred is limited to $1\frac{1}{2}$ times "export promotion expenses" or 10 percent of gross receipts from the property from which the export trade arises, whichever is the lesser. "Export promotion expenses" are the following expenses paid or incurred in connection with the export trade income—

(1) a reasonable allowance for salaries or other compensation for personal services,

(2) rentals or other payments for the use of property,

(3) a reasonable allowance for the exhaustion, wear and tear of property, and

(4) any other ordinary and necessary expenses to the extent reasonably allocable to the export trade income.

No expense incurred in the United States is to be treated as an export promotion expense unless at least 90 percent of each category of expense is incurred outside the United States.

8. *Other relief provisions.*—In addition to the minimum distribution schedule and export trade corporation provision which may exclude from the tax base of U.S. shareholders undistributed income of controlled foreign corporations, the bill provides two other important relief measures. First, it provides that a U.S. shareholder who is an individual may elect to be taxed upon any undistributed income of a controlled foreign corporation attributed to him as if he were a corporation rather than an individual. If he makes this election this means that he will be subject to a 30-percent tax on the first \$25,000 of undistributed income allocated to him and a 52-percent tax on all income allocated above this level. Against this 52-percent or 30-percent tax rate, credits will be allowed for income and other creditable taxes paid by the controlled foreign corporation to foreign countries in the same manner as if the individual were a domestic corporation.

The purpose of this provision is to avoid what might otherwise be a hardship in taxing a U.S. individual at high bracket rates with respect to earnings in a foreign corporation which he does not receive. This provision gives such individuals assurance that their tax burdens, with respect to these undistributed foreign earnings, will be no heavier than they would have been had they invested in an American corporation doing business abroad.

If an individual has elected with respect to the earnings of a controlled foreign corporation to be treated as if he were a domestic corporation, and then subsequently an actual distribution is made, the bill provides that he then is to be taxed only on the excess of the amount received over the amount of taxes he previously paid with respect to the undistributed income. Therefore, if the individual were to be taxed on \$100 of undistributed income at a 52-percent tax

rate, and then subsequently the \$100 was paid to him as a dividend, he would be taxed at individual income tax rates only on \$48, namely, the excess of the amount distributed to him over the taxes he previously paid, assuming the foreign country involved had no income taxes.

Another relief provision is provided with respect to any undistributed income representing "foreign base company income." The bill provides that such income is not to be taxed to the U.S. shareholder if it is established to the satisfaction of the Secretary of the Treasury or his delegate that the incorporation of the controlled foreign corporation in the particular foreign country involved does not have the effect of substantially reducing income, excess profits or similar taxes.

9. *Treatment provided in the case of Puerto Rico and U.S. possessions.*—The bill provides that a controlled foreign corporation does not include a corporation incorporated in Puerto Rico or a possession of the United States if 80 percent or more of the gross income of the corporation (for the prior 3-year period) is derived from sources within Puerto Rico or a possession of the United States, and if 50 percent or more of the gross income was derived from the active conduct within Puerto Rico or a possession of the United States of specified trades or businesses. The trades or businesses qualifying are the following:

- (1) manufacturing and processing of goods or other tangible personal property,
- (2) the processing of agricultural or horticultural products (including livestock, poultry, or fur-bearing animals),
- (3) the catching of fish (whether or not on the high seas) or extraction of natural resources, or the manufacturing or processing of commodities obtained from such activities, or
- (4) the ownership or operation of hotels.

Your committee has excluded Puerto Rico and U.S. possession corporations from the operation of section 12 in recognition of their special status and our special interest in encouraging investments in such areas. The definition of the excluded corporations parallels (except for the reference to the specific trades or businesses) the provision in existing law which excludes from U.S. tax qualifying businesses carried on in the possessions.

In addition to excluding these Puerto Rican or U.S. possessions corporations from the application of section 12, your committee has also provided that the term "U.S. person" (and, therefore, the term U.S. shareholder) does not include in the case of a corporation organized under the laws of Puerto Rico an individual who is a bona fide resident of Puerto Rico (within the meaning of sec. 933(1)); with respect to a corporation organized under the laws of the Virgin Islands does not include an individual who is a bona fide resident of the Virgin Islands and whose income tax obligation is satisfied by paying tax on income derived from all sources into the treasury of the Virgin Islands and in the case of a corporation organized under the laws of any other possession, does not include a bona fide resident of that possession (qualifying under sec. 932(a) of the code).

The effect of not treating these bona fide residents as U.S. persons is to provide that they do not qualify as U.S. shareholders in determining whether or not more than 50 percent of a foreign corporation is controlled by 10-percent U.S. shareholders.

10. Miscellaneous provisions.—

a. Foreign tax credit.—U.S. shareholders who are taxed on subpart F income, on a decrease in investments in less developed countries, or on the increase of earnings invested in U.S. property, can obtain a foreign tax credit for foreign income, etc., taxes paid by the foreign corporation, if the shareholder is a person to whom such a foreign credit would be allowed in the case of an actual distribution. That means that foreign tax credits will be allowed where the shareholder is a domestic corporation (or an individual electing to be treated as a domestic corporation) holding the stock of a foreign corporation and has at least a 10-percent voting stock interest. Similarly, where a domestic corporation has at least a 10-percent interest in a foreign corporation which in turn has at least a 50-percent voting stock interest in a subsidiary, then a foreign tax credit will be allowed the U.S. shareholder with respect to the earnings of this subsidiary when undistributed earnings of the subsidiary are taxed to the U.S. corporate shareholder. Taxes so allowed as credits will not again be allowed as credits when actual distributions are made.

Where the foreign country imposes a tax directly on dividend distributions, such a tax would not, of course, initially be taken into account when the shareholder at an earlier date was taxed on undistributed earnings of a controlled foreign corporation. These taxes on actual dividend payments, however, will be allowed as credits in the year in which the actual dividends are paid, even though these dividends are not taxable to the domestic corporation receiving them because of an earlier inclusion by it of these amounts in its income. Adjustments are made in the overall and per country limitations to keep these limitations from reducing the creditable taxes in such cases below what could be credited if the income taxed and taxes attributable to this income had been taken into account in the same year. Moreover, if the taxpayer has insufficient U.S. income tax against which to offset such credits in the year of the actual distribution, then refunds are allowed.

b. Adjustments to basis of stock.—It is necessary where amounts not actually distributed to the taxpayer are nevertheless taxed to him, to increase his basis for the stock in the controlled corporation by the amount so taxed to him. However, if subsequently actual distributions are made which do not result in any tax to the shareholder because of the prior tax payment by him, then the basis of the stock needs to again be reduced. The bill makes provision for these adjustments.

c. Other provisions.—The bill provides that earnings and profits of a foreign corporation for purposes of this provision are to be determined according to rules substantially similar to those applicable to domestic corporations under regulations prescribed by the Secretary or his delegate. The bill provides that earnings and profits of a controlled foreign corporation are not to be taxable to the U.S. shareholder when it is established to the satisfaction of the Secretary or his delegate that such earnings are blocked because of currency or other restrictions or limitations imposed by the laws of any foreign country.

11. Effective date.—This provision applies to taxable years of foreign corporations beginning after December 31, 1962, and to taxable years of U.S. shareholders within or with which these taxable years of the foreign corporations end.

XIII. GAIN FROM DISPOSITION OF CERTAIN DEPRECIABLE PROPERTY

(Sec. 13 of bill and secs. 1245, 167(f), 170(e), 453(d) and 613(a) of code)

A. Reasons for provision

Under present law, in the case of depreciable property the taxpayer may write off the cost or other basis of the property over the period of the useful life of the asset in his hands. This cost or other basis can be written off evenly (i.e., in a "straight line" over the asset's life), under the declining balance method, under the sum-of-the-year's digits method, or under any other consistent method which does not during the first two-thirds of the useful life of the property exceed the allowances which would have been allowed under the declining balance method. The depreciation deduction is a deduction against ordinary income. If either the useful life of the asset is too short, or the particular method of depreciation allows too much depreciation in the early years, the decline in value of the asset resulting from these depreciation deductions may exceed the actual decline. Wherever the depreciation deductions reduce the basis of the property faster than the actual decline in its value, then when it is sold there will be a gain. Under present law this gain is taxed as a capital gain, even though the depreciation deductions reduced ordinary income. The taxpayer who has taken excessive depreciation deductions and then sells an asset, therefore, has in effect converted ordinary income into a capital gain.

The President stated that our capital gains concept should not encompass this kind of income. He indicated that this inequity should be eliminated, especially in view of the proposed investment credit for newly acquired property. He states that we should not encourage the further acquisition of such property through tax incentives as long as the loophole remains.

This problem also is of major significance in connection with the recent depreciation liberalization announced by the Treasury Department. Under this new approach, many taxpayers will be permitted to depreciate assets faster for tax purposes than has previously been the case. Therefore, additional ordinary income would be converted into capital gain if this were not dealt with in this provision.

B. Comparison of committee amendments with House provision

Both the House bill and your committee's amendments treat as ordinary income any gain on the sale or other disposition of certain depreciable property to the extent of the depreciation deductions taken. However, this treatment will apply to property subject to the allowance for depreciation which is either (1) personal property or (2) certain other tangible property but not including a building or its structural components. The bill as passed by the House did not apply this treatment to buildings or structural components thereof, and your committee has not changed this feature of the House-passed bill.

The House bill applied to property disposed of after the date of enactment of this bill and provided that the only gain which was to be treated as ordinary income was to be depreciation occurring in 1962 and subsequent years. The bill, as amended by your committee, will only apply to sales, exchanges, or other dispositions occurring

during taxable years beginning after December 31, 1962. However, as under the House bill, in such dispositions, depreciation occurring in 1962 and subsequent years will result in ordinary income.

Your committee concurs with the House in believing that the new treatment of gain on sale will make it possible to be more lenient in determining salvage value. The bill as passed by the House provided that the salvage value for depreciation purposes of an asset may be reduced by up to 10 percent of its cost or other basis, and if this value is less than 10 percent of basis it may be disregarded altogether.

The bill as passed by the House provides that for a period of time after the new ordinary income treatment becomes applicable, taxpayers will have a new election to change their method of depreciation from any declining balance or sum-of-the-years digits method to the straight-line method. This provision has been retained by your committee.

The above description has been in terms of the sale or exchange of a depreciable asset. There are, of course, other methods of disposing of an asset which also are dealt with in this provision. In the case of a gift or a transfer at death no gain is recognized at the time of the disposition of the asset. In the case of a gift, however, the ordinary income potential of the depreciation deductions carries over into the hands of the donee. In the case of gifts to charity, although no ordinary income is recognized at the time of the gift, the charitable contribution is reduced by the amount which would be recognized as ordinary income if the property were sold. Generally, in other cases any gain which under present law would be recognized at the time of the disposition of an asset will be treated as ordinary income to the extent of any depreciation deductions taken. In certain cases, however, in order to prevent tax avoidance the bill provides for the recognition of ordinary income on the disposition of an asset even though gain might not otherwise be recognized. This is true in certain cases where a distribution is made by a corporation or partnership. These provisions have been accepted by your committee.

Your committee has, however, added a new provision providing for an appropriate adjustment in computing the "taxable income from the property" for purposes of the limitation on percentage depletion in the case of mining. This provision is explained below.

C. General explanation of provision

1. *General rule.*—The general rule (in sec. 1245) provides that ordinary income is to be recognized in the case of sales or exchanges to the extent the so-called recomputed basis, or the amount realized in the sale or exchange, whichever is lesser, exceeds the basis of the property in the hands of the person making the sale or exchange. "Recomputed basis" is defined generally as equaling the adjusted basis plus the depreciation deductions previously taken. The excess of the amount realized over the adjusted basis is, of course, the amount presently recognized as capital gain. Since the rule requires that the smaller of these two amounts be treated as ordinary income, this in effect means that the ordinary income in the usual case is to be the gain realized or the sum of the depreciation deductions taken, whichever is the smaller. Where there is a disposition of an asset without a sale or exchange, gain is determined by reference to the fair market value of the asset.

Since this provision is to have prospective application only, in computing depreciation for this purpose only depreciation deductions occurring after December 31, 1961, are to be taken into account. Depreciation deductions for this purpose include not only regular depreciation deductions but also the special initial allowance deduction and any deduction for the amortization of emergency facilities. The special reduction in basis of property provided in connection with the investment credit (sec. 2 of this bill) is not, however, treated as a depreciation deduction for this purpose. Therefore, any gain on sale attributable to this basis adjustment will still result in capital gain (if gain from the property otherwise would be capital gain). The depreciation deductions taken into account are not limited to those taken by the taxpayer, but also include deductions taken by others from whom the taxpayer acquired the property, if the basis of the property was carried over from the transferor. This would not be true where the taxpayer acquired the property from another by reason of the latter's death, since in this case the property receives a new basis at death and this provision does not apply. The general rule is that the depreciation deduction taken into account for each year is the amount allowed or allowable whichever is greater. However, a special rule provides that the depreciation deductions taken into account as to any year will be the amount "allowed" rather than the amount "allowable" if the former is smaller and the taxpayer can establish what the amount was.

The type of property receiving the ordinary income treatment described above is (1) personal property (other than livestock), including intangible personal property, and (2) other property which is tangible, not including a building or its structural components, which is an integral part of certain specified business activities or which constitutes research or storage facilities used in connection with these activities. The activities specified are manufacturing, production, or extraction, or of furnishing transportation, communications, electrical energy, gas, water, or sewage disposal services.

The ordinary income treatment provided by this section will be applied upon the sale of all property the acquisition of which could have resulted in an investment credit (sec. 38 of the code as added by this bill). However, the ordinary income treatment may also apply to the disposition of property even though the acquisition of this specific property did not result in an investment credit. For example, no investment credit may have been allowed upon the acquisition of the property because (1) its expected useful life was less than 4 years; (2) it was to be used outside of the United States; (3) it was to be used by tax-exempt organizations or governmental units; or (4) it was not new when acquired (and was over the \$50,000 limit), etc.

2. Exceptions.—Except as specifically provided in the bill, the ordinary income treatment applies at any time property is disposed of. The bill, however provides six general categories of exceptions to this rule. The first exception is for gifts. As pointed out above, however, the depreciation deductions of the donor must be taken into account by the donee, and may result in ordinary income to him if he sells the property. In the case of depreciable property which is given to a charitable organization, although no income is realized by the donor at the time of the gift, the amount of the charitable contribution deduction he may receive is reduced by the amount which would have

been treated as ordinary income had the property been sold at its fair market value (an amendment adding a new sec. 170(e)).

A second exception to the realization of ordinary income upon the disposition of depreciable personal property is provided in the case of transfers at death (except where the sale has occurred before death and the income is treated as income in respect of a decedent under sec. 691). In this case, however, there is not a carryover of the income potential in the depreciation deductions to the decedent's legatee or heir.

A third category of exceptions to the realization of ordinary income is provided in the case of a series of transactions which generally are tax free and in which the basis is carried over. However, in these transactions where there is any gain recognized, because the exchange is accompanied by "boot" (i.e., money or its equivalent) then to the extent of this gain, ordinary income may be realized (unless the depreciation deductions are smaller). The tax-free transactions referred to relate to those occurring upon the complete liquidation of a subsidiary (sec. 332); in the case of a transfer for stock or securities to a corporation controlled by the transferor (sec. 351); in the case of a transfer by a corporation which is a party to a reorganization of property in pursuance of a plan of a reorganization solely for stock or securities in another corporation also a party to the reorganization (sec. 361); and in the case of reorganizations in certain receivership and bankruptcy proceedings (sec. 371(a) and sec. 374). Also included in the same category are contributions of property to a partnership in exchange for an interest in the partnership, and distributions by a partnership in partial or complete liquidation of an interest (but in this respect see the special partnership treatment described below). Despite the above rule there would be a recognition of ordinary income where there is a contribution of depreciable property to a tax-exempt organization (other than a tax-exempt farm cooperative) in exchange for stock or securities in the exempt organization. Recognition of ordinary income in this case is provided because a disposition of the property by the exempt organization would not ordinarily give rise to the realization of ordinary income with respect to the depreciation deductions.

Another exception is provided in the case of so-called like kind exchanges of property used for production or investment, and for involuntary conversions. In exchanges of these types, the ordinary income realized is not limited to any gain recognized, but also includes gain taking into account the fair market value of nondepreciable or other nonqualifying property acquired in exchange for depreciable property. The realization of ordinary income (to the extent of the depreciation deductions) is necessary in such cases since in the case of property, other than depreciable personal property, there is no opportunity for subsequent recovery of the ordinary income element. A similar exception is provided in the case of the exchange or sale of property in obedience to Federal Communications Commission orders or orders of the Securities and Exchange Commission (secs. 1071 and 1081). In these cases also, the ordinary income realized is not limited to the gain recognized, but also includes any unrecovered depreciation charges with respect to exchanges of depreciable personal property for other types of property.

Special rules are also provided in the case of distributions of depreciable personal property by a partnership to a partner. A distribution of depreciable personal property by a partnership to a partner, to the extent that the distribution accounts for the partner's share of gain attributable to this property, is not to result in ordinary income to the distributee partner at the time of the distribution. However, the ordinary income potential of depreciation deductions taken by the partnership (or by any earlier transferee from whom the partnership acquired property without realization of gain) will be carried over to the distributee partner. When he disposes of this property, the ordinary income potential of these partnership (or pre-partnership) depreciation deductions will be taken into account in a manner substantially the same as that applying where the taxpayer himself took the depreciation deductions. The property distributed is given a "recomputed basis" to the partner equal to the basis of the property in the hands of the partner plus any ordinary income gain on which the partnership would have been taxed had the property been sold by it (at its fair market value) immediately before the distribution.

The rule described above applies only to the extent a partner is considered as receiving his share of the property representing ordinary income gain. An amendment made elsewhere to the code (sec. 751(c)) provides that in other cases the ordinary income element in depreciable property is to be considered as an "unrealized receivable." Thus, to the extent of depreciation deductions taken (or potential gain if smaller) ordinary income will be realized in the case of the sale of a partnership interest, in the case of a distribution to a retiring or deceased partner, and in the case of distributions to a partner where he receives either more or less than his proportionate share of property reflecting this type of gain.

3. *Dispositions resulting in ordinary income where no gain is presently recognized.*—In a series of situations your committee found it necessary to recognize ordinary income even though capital gain in such situations is not recognized under existing law. This was done primarily in those cases where the transferee receives another basis for the property than that of the transferor. This treatment is provided in three types of cases where a distribution is made by a corporation without the payment of a tax at the corporate level on unrealized appreciation in value: namely, where the property is distributed as a dividend (under sec. 311), where the property is distributed in a partial or complete liquidation by a corporation (sec. 336), and where in a plan of complete liquidation a corporation sells the depreciable personal property (and perhaps other assets) and within a 12-month period completes the liquidation of the corporation (sec. 337). Similarly, if the property is first sold by a corporation for installment notes and the gain which would be realized on such sale is delayed because of the installment method of reporting, a distribution of these notes to the shareholders in a liquidation under section 337 (12 months' liquidation) results in the recognition of the same amount of ordinary income to the corporation as would have been realized on a cash sale of such notes. The same rule is applied whenever similar installment notes are distributed by a corporation in a liquidation in which the basis of the property to the receiving shareholder is determined under section 334(b)(2) (purchase of 80 percent of the stock of one corporation by another followed by

the immediate liquidation of the corporation acquired). The other situations where ordinary income may be realized under this provision, although capital gain would not otherwise occur, include the case where a distribution is made by a partnership and the partner gives up, or acquires, more than his proportionate share of this property. Other cases involve the provisions relating to the exchange of "like kind" property, involuntary conversions, sales or exchanges to effectuate FCC policy, and exchanges in obedience to orders of the SEC. In all of these cases where the property received in exchange for depreciable personal property is not itself depreciable personal property, then ordinary income is recognized.

4. *Computation of taxable income for purpose of limitation on percentage depletion deduction.*—The attention of your committee was called to the fact that the House bill worked a hardship on certain mining properties. At the time the depreciation deductions were initially taken they reduced the "taxable income from the (mining) property." Because percentage depletion deductions are limited to 50 percent of the taxpayer's taxable income from the mining property, in many cases this meant smaller deductions for percentage depletion. Under the House bill part of these depreciation deductions were recouped as ordinary income at the time of the sale of the depreciable property but no comparable upward adjustment was made to the taxable income from the mining property for purposes of percentage depletion.

Your committee has removed this discrimination against mining properties by amending the percentage depletion provision of existing law (sec. 613(a)) to provide that for purposes of the limitation restricting the percentage depletion deduction to 50 percent of taxable income, this income, in case of mining, in effect is to be increased by the amount of gain taxed as ordinary income (under sec. 1245) which is allocable to the property. This increase in taxable income, however, is made *only* for purposes of computing taxable income from the property for the 50-percent limitation, and for no other purpose. The amendment is accomplished by reducing the deductions taken into account with respect to the expenses of mining, used in computing the taxable income from the property, by the portion of any gain treated as ordinary income. This avoids any effect on the computation of "gross income from property" (as defined in sec. 613(c)). No change is made in existing law with regard to the treatment of losses resulting from the sale of depreciable personal property used in exploiting a mineral property.

5. *Salvage value.*—The bill also amends the code (a new subsec. (f) in sec. 167) to provide that in computing the basis on which depreciation may be taken for personal property, salvage value may be ignored to the extent of an amount equal to 10 percent of the cost or other basis for the property. Thus, if the expected salvage value equals 8 percent of the basis of the property, the entire basis may be written off in depreciation charges by the taxpayer. If the expected salvage value is 12 percent, all but 2 percent of the basis of the property can be taken into account in computing depreciation charges. The provision applies to depreciable personal property (other than livestock) with a useful life of 3 years or more acquired after the date of enactment.

6. *Change in method of depreciation.*—Your committee recognized that some taxpayers who have been following liberal depreciation policies may desire to follow more conservative policies in order to avoid the possibility of ordinary income treatment at the time of sale, as provided by the bill. Therefore, the bill provides that a taxpayer may elect to change his method of depreciation with respect to depreciable personal property from any declining balance or sum of the years digit method to the straight-line method. The right to make this election will be available on or before the date for filing the return (including extensions of time) for the first taxable year beginning after December 31, 1962.

7. *Effective date.*—This provision is to apply with respect to depreciation attributable to periods after December 31, 1961, and as to dispositions of property during taxable years beginning after December 31, 1962. However, the provision relating to salvage value generally is effective for taxable years beginning after 1961.

XIV. FOREIGN INVESTMENT COMPANIES

(Sec. 14 of the bill and secs. 312(l), 1246 and 1247 of code)

A. *Reasons for provision*

For the small investor who desires to diversify his shareholdings through the use of domestic mutual funds, or regulated investment companies, present law provides that if a series of conditions are met, including the distribution of at least 90 percent of the earnings of the regulated investment company, no tax is imposed on the investment company to the extent it distributes its earnings. Thus, if a domestic company distributes its income currently, present law provides for the imposition of a single, rather than a double, tax, and that one is imposed on the investor rather than the company.

Increasingly in recent years, however, some taxpayers have sought to avoid this tax by investing in foreign investment companies rather than domestic companies. Under present law a foreign investment company usually pays no U.S. income tax, since U.S. tax is imposed only on income derived from sources within the United States and such companies generally have no U.S. securities and, therefore, have no income from U.S. sources. The U.S. shareholders of one of these investment companies are likely to pay a U.S. tax with respect to such investments only when they sell the stock and then, of course, this gain is taxed as a capital gain rather than ordinary income. The U.S. shareholder would, of course, pay tax on any dividend income received from such a company, but most of these companies follow the announced policy of reinvesting all of their income in stocks or bonds in order to prevent the imposition of any such dividend tax by the United States.

The tax avoidance occurring in the case of these foreign investment companies is a matter to which study has been given since 1956. Since that time the seriousness of this problem has increased substantially. The Secretary of the Treasury in his testimony before your committee stated:

There are currently 13 of such companies, most of them Canadian, registered with the Securities and Exchange Commission, having total assets of \$422 million. In addition, there are apparently many more companies not so registered.

It was proposed by the administration that the preferential treatment for investments in these foreign investment companies be eliminated by requiring U.S. shareholders in such companies to pay tax currently on their share of the income derived from the foreign investment company. The provisions included in the House bill achieve much the same result but without attempting to look through the foreign corporation to the American shareholders.

The House bill in general terms provides that American shareholders in these foreign investment companies, when they sell or redeem their stock, are to be taxed at ordinary income rates on their share of any earnings and profits accumulated in the foreign investment company since December 31, 1962, or since the date they acquired the stock, whichever occurred more recently. However, it also provides that this treatment can be avoided at the election of the foreign investment company if it distributes 90 percent of its taxable income other than net long-term capital gains currently and if it informs the U.S. shareholders of their share of any net long-term capital gains. However, for this treatment to apply, the U.S. shareholders must also include in income their share of capital gains whether or not distributed. The distributions of ordinary income in this case, since they are actual distributions, would, of course, in any case be reported for tax purposes by the U.S. shareholders.

B. Comparison of committee amendments with House provision

Your committee has retained the House provision on foreign investment companies with three relatively minor modifications.

Your committee recognized that with the removal of the tax advantages for these corporations in being foreign corporations, many of them may desire to become domestic corporations treated as regulated investment companies. However, under present law when a foreign corporation is a party to a reorganization in which all of its properties are acquired by a domestic corporation, clearance must be obtained from the Internal Revenue Service to the effect that the reorganization is not in pursuance of a plan having as one of its principal purposes the avoidance of Federal income taxes. Failure to obtain such a clearance results in the imposition of capital gains tax on any appreciation of value. Since your committee has allowed a foreign investment company which has been registered with the SEC the right to elect to have its shareholders treated in a manner substantially similar to that accorded to domestic regulated investment companies, it does not believe that there is tax avoidance if such a company is a party to a reorganization in which all of its properties are acquired by a domestic regulated investment company. Moreover, it believes that the conversion of these companies to domestic companies simplifies the operation of the tax laws in the case of their shareholders. For these reasons, it is provided that this clearance from the Internal Revenue Service under section 367 need not be obtained in the case of one of these foreign investment companies registered with the SEC if it is a party to a reorganization in which all of its properties are acquired by a domestic regulated investment company before January 1, 1964. However, this treatment is to be available only if, for the year 1963, the corporation elected to distribute at least 90 percent of its ordinary income to its shareholders and either distribute, or treat as distributed, the excess of its net long-term capital gain over its net short-term capital loss.

The election provided foreign investment companies by the House bill, to distribute most of their ordinary income currently and to require their shareholders to report their share of the company's capital gains (whether distributed or not), provides tax treatment for these foreign investment companies which is substantially similar to that now applicable to domestic regulated investment companies. However, where domestic regulated investment companies have more than 50 percent of their assets invested in securities in foreign corporations, present law permits the foreign tax credit, for which the regulated investment company itself would otherwise be eligible, to be passed on down to the shareholders. Your committee's amendments, in the interest of conforming the treatment for these foreign investment companies to that provided for the domestic regulated investment companies, provides a similar option in their case to pass down through to the shareholders their foreign tax credits.

Your committee has also extended from 30 to 45 days the period of time elapsing after the end of the taxable year before the investment companies must report to their shareholders their share of the undistributed capital gains which they must take into account for tax purposes. Other technical changes are also made.

C. General explanation of provision

As indicated above, the bill provides alternative tax treatment for shareholders of foreign investment companies. Unless an election is made to the contrary, ordinary income treatment, to a limited degree, is provided at the time an investor in a foreign investment company either sells his stock or it is redeemed. However, if the company has elected to distribute most of its taxable income and the shareholders report capital gain, whether or not distributed, then at their election the ordinary income treatment at the time of the sale of the stock is not to apply. These two alternative provisions are discussed below.

1. Ordinary income treatment on sale of stock.—The bill provides that on the sale or exchange of stock in a foreign investment company after December 31, 1962, any gain realized is to be treated as ordinary income, rather than a capital gain, to the extent of the taxpayer's share of the company's earnings and profits accumulated in years beginning after December 31, 1962. For this purpose the taxpayer's share of these earnings and profits is limited to those attributable to his stock which have been accumulated during the period he has held the stock (excluding any earnings taxed to him when the company was a foreign personal holding company or a controlled foreign corporation). Had the company been a domestic company, currently distributing most or all of its earnings, these same earnings would have been taxable to him. Thus, this provision is not designed as a penalty tax, but merely to accord, to the extent practicable, the same tax treatment as that provided for domestic regulated investment companies.

To give assurances that this ordinary income will not escape tax where the shareholder holds the stock until death, the bill provides that the step-up in basis, or increase in value, which would otherwise occur at date of death is not to occur with respect to the amount which would be ordinary income to the decedent had he sold the stock just before death. Thus, when the estate, heir, or legatee sells the stock,

the same amount (assuming the stock has not gone down in value) will still result in ordinary income and will be subject to U.S. tax at that time. However, the estate, heir, or legatee in such a case can treat this as "income in respect of a decedent." Thus, in computing his ordinary income tax he will be allowed a deduction for any estate tax attributable to inclusion in the decedent's estate tax base of the amount taxed as ordinary income.

Without regard to this provision, where a shareholder sells or exchanges stock in one of these foreign investment companies after holding it for not more than 6 months, the gain is short-term capital gain. Since this type of gain is treated much like ordinary income for tax purposes, the bill provides that if stock in a foreign investment company is held for 6 months or less the provision is not to apply.

A foreign investment company, for purposes of this provision, is defined as a foreign corporation, either registered under the Investment Company Act of 1940 as a management or unit investment trust, or any other corporation engaged primarily in the business of investing, reinvesting, or trading in securities where more than 50 percent of the voting stock (and total value of all shares) is held directly or indirectly by U.S. persons. "United States persons," a definition added to the code by the foreign trust provision in this bill (sec. 7), means a citizen or resident of the United States, a domestic partnership, a domestic corporation, and a domestic estate or trust.

To prevent avoidance of this ordinary income tax treatment through the use of tax-free (or partially tax-free) exchanges in which stock in a foreign investment company is exchanged for other stock (in a tax-free incorporation or contribution to capital under sec. 351), the bill provides that the substituted stock in such a case (where its basis is determined by reference to the basis of stock in a foreign investment company) is to be treated substantially as if it were the foreign investment company stock. Thus, upon its sale, any gain to the extent of the appropriate share of the foreign investment company's earnings and profits during the period it and the substituted stock was held is to be treated as ordinary income.

The bill also contains several other provisions similarly designed to prevent the avoidance of the ordinary income treatment through indirect ownership of the foreign investment company stock through certificates in a trust, through stock in a domestic corporation, or through a partnership. In this respect it is provided first that a share of stock in a domestic corporation or a trust certificate is to be treated as foreign investment company stock to the extent it represents such stock. Secondly, it is provided that if a company is a member of an affiliated group (with a 50-percent rather than an 80-percent stock-ownership requirement), then the earnings and profits of the entire group are to be allocated under regulations prescribed by the Treasury Department in a manner to carry out the purposes of the bill. Thus, where a foreign corporation is a holding company in the sense that it holds the stock of one or more foreign investment companies, the shareholders of the holding company will not be permitted to avoid ordinary income on the sale of the foreign holding company stock merely because the earnings and profits of the investment company (or companies) have not been distributed to the holding company. Thirdly, the bill provides that the ordinary income treatment is to apply to redemptions of stock by a foreign investment company which would

otherwise be treated as sale transactions because of section 302(a) (disproportionate buy-out of a shareholder) or because of section 303 (a redemption of stock to pay death taxes). Finally, the bill deals with the sale or exchange of and also certain distributions with respect to partnership interests. The bill provides that if any of the property of the partnership is stock in a foreign investment company and would have resulted in ordinary income had it been sold by the partnership itself, then this amount is to be treated as an inventory item. Thus, the sale of the partnership interest (and distributions in certain cases) will generally result in the incurring of ordinary income treatment with respect to the foreign investment company stock underlying the partnership interest.

The bill provides that the shareholder upon sale of the stock must establish the amount of the accumulated earnings and profits of the foreign investment company and his share of these earnings during the period of his investment. If he does not do so, the entire gain will be treated as ordinary income. This information, of course, is necessary to determine the amount subject to ordinary income tax. In addition, the bill provides that every U.S. person owning 5 percent or more in stock of a foreign investment company is to furnish with respect to such a company such information as the Secretary of the Treasury deems necessary in order to properly enforce the tax provisions applicable to shareholders of these companies.

Your committee's amendments also provide that the clearance of the Internal Revenue Service, required by section 367 of the code, need not be obtained where a foreign investment company registered under the Investment Company Act of 1940 is a party to a reorganization in which all of its properties are acquired before January 1, 1964, by a domestic regulated investment company. However, for this clearance not to be required in such cases the foreign investment company must have elected to distribute most of its income currently (as provided under sec. 1247) for its taxable years beginning after December 31, 1962.

2. Election to distribute income currently.—Foreign investment companies which are registered with the SEC to sell stock in this country can elect to make the provision described above inapplicable under certain conditions. Any such election must be made before December 31, 1962.

For the provision referred to above to be inapplicable the electing foreign investment company must agree with respect to the current and all subsequent years to—

(1) distribute 90 percent of its taxable income to its shareholders. This is exclusive of capital gains.¹ Also, such a corporation can elect to treat as distributed during the year distributions made in the first 2½ months after the end of the year.

(2) designate in written notices mailed to its shareholders their shares of the excess of net long-term capital gains over net short-term capital losses, and the portion, if any, which the corporation has distributed. These notices must be mailed to the shareholders within 45 days after the close of the taxable year.

(3) provide such information as the Treasury Department considers necessary to carry out the purposes of this provision.

¹ For this purpose, as in the case of domestic regulated investment companies, no net operating loss carry-over is allowed and no organizational expense deduction is allowed.

In addition to the corporation's fulfilling these requirements, however, the shareholder (who is a U.S. person), if he is to avoid the ordinary income treatment upon the sale of his stock, also must include in his income for tax purposes the excess of the net long-term capital gain over the net short-term capital loss, which the company in its notice to him designated as being his share of the company's capital gains. If the shareholder does not do so for any year, unless this failure was due to reasonable cause and not to willful neglect, the election provided by this provision will not apply when he sells or otherwise disposes of his stock. Thus, although other shareholders might continue to qualify in such a case, the shareholder who did not report this capital gain income, upon his sale of the stock will have ordinary income (limited as indicated above). It is not made a condition of qualification that the shareholder in such a case report his share of the ordinary income of the corporation. However, since at least 90 percent of his share of this income will actually be distributed to him, it must in fact be reported by him, in the same manner as any other dividend income which he may receive from foreign sources.

The bill provides that qualified shareholders are to include in computing their long-term capital gains both the distributed and the undistributed portions of the excess of net long-term capital gains over net short-term capital gains.

The bill further provides that the capital gains, reported by the shareholders, which are not actually distributed, are to result in a decrease in earnings and profits of the corporation for the shareholders who report them and also that the basis that they had for the foreign investment company stock is to be increased by this amount.

The bill also provides that if a foreign investment company has more than 50 percent of the value of its assets invested in securities of foreign corporations and it is registered under the Investment Company Act, it may elect to itself forego any foreign tax credits and instead pass these credits on to its shareholders on a pro rata basis. In such cases the shareholder takes both the dividends and his share of the taxes into his income and then claims a credit against tentative tax for the foreign taxes, subject to the same limitations as if he had paid them directly.

The election to distribute income currently with respect to the foreign investment company continues until the company fails to comply with the three conditions set forth above, unless the company becomes a foreign personal holding company, or no longer is a foreign investment company.

To prevent the use of the capital gains designating provision as a means of obtaining short-term capital losses which may be short-term capital gains or under certain circumstances ordinary income, merely at the cost of reporting a capital gain under this provision, the bill provides that if the shareholder has held the stock for less than 6 months, then any loss realized on the sale of the stock within that 6-month period is to be treated as if it were a long-term rather than short-term capital loss.

3. Effective date.—The amendments made by this provision apply to taxable years beginning after December 31, 1962.

XV. GAIN FROM CERTAIN SALES OR EXCHANGES OF STOCK IN CERTAIN FOREIGN CORPORATIONS

(Sec. 15 of bill and sec. 1248 of code)

A. Reasons for provision

Under existing law, through an ordinary taxable liquidation or sale or exchange, it is possible to bring earnings accumulated by a foreign corporation back to this country merely by paying a capital gains tax on such earnings included in the gain. Theoretically it is also possible to bring earnings accumulated by a foreign corporation back to the United States without payment of income tax through the use of a tax-free reorganization (under sec. 368) or through the use of a tax-free liquidation (under sec. 332). However, to do so the Commissioner of Internal Revenue must give clearance by determining in advance that the transaction "is not in pursuance of a plan having as one of its principal purposes the avoidance of Federal income taxes." Generally the Commissioner has been unwilling to grant such approval where there is an appreciable amount of earnings and profits accumulated in a foreign corporation.

The bill has as one of its objectives in the foreign income area the imposition of the full U.S. tax when income earned abroad is repatriated. Full U.S. taxation will occur in the case of the ordinary taxable liquidations or sales or exchanges only if the earnings and profits are in effect taxed as dividends (to the extent of any gain) at the time the funds are brought back to the United States. This objective is accomplished by this section of the bill.

B. Comparison of committee amendments with House provision

Your committee has retained the basic structure of the House bill but has made a number of important modifications in it, which are discussed below.

Under the bill as passed by the House, amounts (to the extent of undistributed earnings) received by an individual or corporate stockholder on the sale of the stock (as distinguished from a redemption) were treated as ordinary income and not as dividends. Under your committee's amendments, the appropriate portion of the gain on a sale is also treated as a dividend.

Under the bill as passed by the House, no special treatment was provided for individual shareholders of controlled foreign corporations. They were required to take into their tax base as ordinary income the entire gain in the year recognized. This meant the income might, because of "bunching," be taxed at unusually high rates. Moreover, the individual might be treated much worse than if the corporation had been a domestic corporation subject to the U.S. corporate tax, against which foreign tax credits could be taken, and then the balance distributed and taxed to the individual at capital gains rates. Under your committee's amendments, if the shareholder is an individual his tax (on either a redemption or sale) is to be no greater than that provided under the lower of two ceilings. The first ceiling provides that the individual's tax is to be no greater than if the foreign corporation had been a domestic corporation paying the regular U.S. corporate tax (offset by foreign tax credits allowable to a corporation) which then made a liquidating distribution of the balance to the U.S. share-

holder and this balance was subjected to capital gains tax. In other words, this ceiling would provide a U.S. tax of no more than 52 percent against which foreign tax credits are taken, plus a capital gains tax on the remaining 48 percent at not more than 25 percent. Thus, the aggregate maximum tax could never be more than 64 percent (52 percent plus 25 percent of 48 percent). The second ceiling is an averaging device. It provides that the tax is not to exceed the amount which would have resulted had the earnings and profits been distributed to the shareholder in the years they were earned.

Your committee has also amended the House bill to provide that earnings and profits are not to include profits on sales made during a liquidation if the corporation could have qualified for tax-free sales on liquidation if it had been a domestic corporation.

In addition, your committee has amended the section to provide that it is not to apply to earnings and profits accumulated by a foreign corporation while it was a less developed corporation if the stock sold or exchanged was owned for at least 10 years before the date of sale or exchange by the U.S. shareholder.

Your committee has also amended the House bill to provide that the ordinary income treatment provided by this section is in no case to apply to earnings and profits accumulated in taxable years beginning before January 1, 1963. Under the House bill the ordinary income treatment could apply to earnings and profits accumulated since February 28, 1913.

C. General explanation of provision

The provision as amended by your committee applies to any shareholder who owned 10 percent or more of the total combined voting power of the stock of a foreign corporation at any time during the 5-year period ending on the date of exchange but only if the corporation was a controlled foreign corporation at any time during the period the stock was owned by the shareholder. (The 10-percent ownership is determined under the constructive stock ownership rules in sec. 958(a) as added by this bill.)

The section applies to any sale or exchange or to any surrender of stock to the corporation for redemption in a transaction which would be treated as a sale or exchange under section 302 or section 331 (a buy-out or a total or partial liquidation). If such a sale, exchange or redemption occurs, and there is a gain on the transaction, there is included in the gross income of the person surrendering the stock, as a dividend, the portion of such gain attributable to the earnings and profits of the foreign corporation allocable to the stock surrendered, accumulated while the shareholder held the stock during a period in which the corporation was a controlled foreign corporation, in taxable years beginning after December 31, 1962.

If the shareholder surrendering the stock is a corporation, it is entitled to a credit for foreign taxes paid by the foreign corporation in the same manner and to the same extent as it would be entitled to such credit in the case of any other dividend received from a foreign corporation.

If the shareholder is an individual, the tax to be paid by him shall not be greater than either the "domestic corporation limitation" or the "annual distribution limitation," whichever is the lesser.

The "domestic corporation limitation" is the sum of—

(1) the excess of the U.S. income taxes which would have been paid by the foreign corporation with respect to its income if it had been a domestic corporation over the foreign income taxes actually paid by such corporation, and

(2) the amount of capital gains tax which would have resulted to the shareholder on the surrender of his stock, if the amount actually received by him on such surrender were diminished by the amount described in (1) above.

The "annual distribution limitation" is the amount equal to the aggregate of taxes which would have been attributable to the amount treated as a dividend had it been distributed to the shareholder as a dividend in the year or years in which it was earned.

The earnings and profits for purposes of this section do not include any amount attributable to gains on sales made in the course of a liquidation if these sales would have been treated as tax-free sales on liquidation (under sec. 337(a)) had the foreign corporation been a domestic corporation.

This section does not apply to earnings and profits accumulated by a foreign corporation while it was a less developed country corporation (as defined in sec. 955(c), as added by the bill), if the stock sold or exchanged was owned for at least 10 years by the U.S. persons before the date of the sale or exchange. A transfer of stock by death is viewed as not interrupting the continuous ownership.

This section also provides that any item of gross income of the foreign corporation treated as income derived from sources within the United States is not to be included in the earnings and profits to be taken into account.

This section also contains provisions providing that earnings taxed once under other sections (secs. 951 and 1247) will not be taxed a second time by virtue of this section.

This provision does not apply to distributions to pay death taxes (sec. 303) or to gain realized because of "boot" on a reorganization exchange (sec. 356). It likewise does not apply to any amount which is treated as a dividend, as a gain from the sale of an asset which is not a capital asset, or as a short-term gain under any other section of the code.

This section provides that unless the taxpayer establishes the amount of the earnings and profits of the foreign corporation to be taken into account, the entire gain from the sale or exchange is to be considered a dividend.

This section will apply to sales or exchanges made after December 31, 1962, with regard to earnings and profits accumulated in taxable years beginning after that date.

XVI. SALES AND EXCHANGES OF PATENTS, ETC., TO CERTAIN FOREIGN CORPORATIONS

(Sec. 16 of bill and sec. 1249 of code)

A. Reasons for provision

The House bill in section 13 (now sec. 12 in your committee's amendments) contained a provision which included in the income of 10-percent shareholders of controlled foreign corporations, income of those corporations which arose from patents, copyrights, and exclusive

formulas and processes which have been substantially developed, created, or produced in the United States or acquired from related U.S. persons. The House provision taxed this income to the U.S. shareholders not only when it represented a royalty or similar payment received by the controlled foreign corporation, but also where this corporation itself used the patent, etc. in the manufacture of goods and derived income from the sale of the manufactured articles. In this latter case it would have been necessary to have constructed the income attributable to the patent, etc.

A considerable body of testimony before your committee indicated that it was impractical to attempt to determine this constructive income. Problems also arose, even in the case of royalty payments, in determining how much of the income was due to the patent, copyright, etc., and how much might be due to services rendered in connection with the use of such a patent, etc.

Therefore, your committee has deleted the part of the House provision attributing back to U.S. shareholders income from patents and related rights, and substituted a new provision which merely provides that when a patent, invention, etc., is transferred to a foreign corporation by a U.S. person controlling such corporation, that any gain otherwise recognized is to be ordinary income rather than a capital gain. An exception to this rule is provided where the transfer is to enable the foreign corporation to use the property in its own manufacturing operations. Gain coming under this exception will continue to be treated as capital gain. This amendment applies only in the case of transfers in taxable years beginning after December 31, 1962.

Your committee recognizes that the transfer of U.S. developed patent and similar rights by a U.S. corporation to a controlled foreign corporation causes a diversion of income from U.S. sources. It believes that taxing any gain on such transfer as ordinary income will, however, correct this situation as to such transfers in the future.

B. Comparison of committee amendments with House provision

As indicated above, section 13 of the House bill (sec. 12 under your committee's amendments) would have taxed income attributable to patents, copyrights, and exclusive formulas and processes substantially developed, created or produced in the United States or acquired from related U.S. persons as giving rise to income which, whether distributed or not, was to be taxable to U.S. shareholders of controlled foreign corporations. Your committee has deleted this provision and substituted the new provision which treats gains from the sale of patents, copyrights, etc., as ordinary income rather than capital gain when transferred by a U.S. person to a foreign corporation which it controls.

C. General explanation of provision

Your committee's amendments added a new section to the code providing that gain from the sale or exchange after December 31, 1962, of certain property rights to a foreign corporation by a U.S. person controlling that corporation is to be treated as ordinary income rather than as capital gain. The type of property, the transfer of which will lead to this ordinary income treatment, is—

- (1) a patent,
- (2) an invention,
- (3) a model or design (whether or not patented),

- (4) a copyright,
- (5) a secret formula or process, or
- (6) any other similar property right.

This ordinary income treatment, however, is not to apply in the case of gain realized from the sale or exchange for stock or contribution to capital of such property if it is established to the satisfaction of the Secretary of the Treasury or his delegate that the principal purpose of the transfer was to enable the foreign corporation to use the property in its own manufacturing operations.

For purposes of this provision, a U.S. person will be considered as controlling a foreign corporation if it owns directly or indirectly the stock possessing more than 50 percent of the voting power of all classes of stock entitled to vote. In determining the indirect ownership, certain constructive ownership rules (those in sec. 958) will be applied.

This provision is to apply to taxable years beginning after December 31, 1962.

XVII. TAX TREATMENT OF COOPERATIVES AND PATRONS

(Sec. 17 of the bill and secs. 1381 to 1388 of the code)

A. Reasons for provision

In 1951 Congress passed legislation which, taken together with prior Treasury rulings, it generally was thought insured that earnings of cooperatives would be currently taxable (to the extent they reflected business activity) either to the cooperatives or to the patrons. However, certain court decisions, notably the *Long Poultry Farm* and *B. A. Carpenter* cases, held that noncash allocations of patronage dividends generally were not taxable to the patron, although they were deductible by the cooperative.

The President recommended that what was thought to be the law in 1951 be provided specifically in the statute. Under the recommendation cooperatives would be allowed to deduct amounts allocated in cash or scrip as patronage dividends and patrons would be currently taxable on the patronage dividends allocated to them arising out of business activities.

The House bill adopts an approach which in substance is substantially the same as that recommended by the President. It provides that the cooperative is not required to take patronage dividends paid in money, qualified allocations, or other property, except nonqualified allocations, into account in determining taxable income. A deduction is also provided for the nonqualified allocations when they are redeemed. For the patron, the bill provides that these same amounts (to the extent not attributable to purchases for personal living expenses or capital items) are to be included in income for tax purposes in the year received (or in the case of a nonqualified allocation, when redeemed).

Qualified allocations for this purpose are defined by the House bill as including first, allocations which the patron can redeem in cash at their stated dollar amount at any time in the first 90 days after they are issued and second, qualified allocations which the patron has consented to take into account at their face amount as income (unless the patronage was with respect to personal living expenses or capital

items). In the case of members, consent may be given by being a member of the cooperative if there is a provision in the bylaws requiring all members to agree to take the allocations into account. In the case of nonmembers (and members if the cooperative prefers) this consent can be provided by the patron signing an agreement to do so. (As explained subsequently your committee also provides another manner of obtaining the consent of the patrons.) Your committee agrees with the House that, since in the case of either the 90-day or consent allocation the patrons have constructively received the dividend and reinvested it, it should constitute income to the patron (where the patronage dividend arises from business activity) and should be taxable to him.

The House provision is effective for taxable years beginning after December 31, 1962, in the case of the cooperatives and in the case of patrons is effective with respect to amounts paid by the cooperatives in taxable years of the cooperative beginning after that date. Existing law will continue to apply with respect to allocations (including their redemption after the specified date) issued with respect to patronage in earlier taxable years to which the new provisions do not apply.

B. Comparison of committee amendments with House provision

Your committee has accepted the tax treatment outlined in the House bill for cooperatives and their patrons with two modifications. First, it is provided that at least 20 percent of patronage dividends must be paid in cash for the cooperative to receive any deduction with respect to their patronage dividends. Likewise, a 20-percent cash payment must be made for exempt cooperatives to receive a deduction for distributions out of nonpatronage earnings. Second, a new form of consent is provided, namely, the qualified check, which the cooperative may use.

The House bill provided for withholding on interest, dividends, and patronage dividends at the rate of 20 percent. Your committee's bill has substituted for the withholding provision a reporting system for dividends, interest, and patronage dividends. However, in the case of patronage dividends, withholding also served the purpose of providing the patron with at least enough funds to pay the full first bracket tax on any qualified allocations taxable to him. Your committee believes that it would be unfortunate to require the patrons to report these qualified allocations for tax purposes without being sure that the cooperative made available to the patrons enough cash to pay at least the first bracket income tax. To give assurance that the cooperative provides the patron with at least enough money to pay this first bracket tax, your committee has provided that cooperatives must pay at least 20 percent of their patronage dividends (and in the case of tax-exempt cooperatives other income distributed on a patronage basis) in cash if the cooperatives are to receive any deductions for allocations (and the patrons are to be required to include any such amounts in their income).

Under the House bill a patron could give his consent to being taxed on a noncash patronage dividend (as having been constructively paid to him and then reinvested) either by providing such consent in writing, or by being a member of the cooperative during the period in which its bylaws provided that membership constituted such consent. Your committee, in addition to these two procedures, has provided

that consent may also be supplied by endorsing and cashing a qualified check. The check must indicate, however, that by endorsing and cashing it the patron is consenting to taking the remainder of the patronage dividend into account in computing his taxable income. This may be a convenient way of obtaining consent for some cooperatives, particularly from nonmembers, who it may be difficult for the cooperative to contact directly. For a cooperative to omit a patronage dividend under this procedure in computing its taxable income for the year the patronage occurs, the qualified check must be endorsed and cashed within 90 days after the end of the payment period for the cooperative, namely, within 90 days after 8½ months after the close of the cooperative's taxable year. A qualified check endorsed and cashed after that time will be deductible by the cooperative when the endorsing and cashing occurs, as a redemption at that time of a nonqualified allocation.

C. General explanation of provision

This provision deals both with the tax treatment of cooperatives and the tax treatment of patrons.

1. *Cooperatives covered by provision.*—The tax treatment outlined here applies to the so-called tax-exempt farmers' cooperatives, to other farm cooperatives, to consumer cooperatives, and also to other corporations operating on a cooperative basis. The provision does not, however, apply to exempt mutual ditch, irrigation, or REA cooperatives, to mutual savings banks, building and loan associations, etc., or to mutual insurance companies. It also does not apply to presently taxable organizations which are engaged in furnishing electric energy, or providing telephone service, to persons in rural areas. These will continue to be treated the same as under present law.

2. *Patronage dividends.*—The bill provides that in determining the taxable income of a cooperative there is not to be taken into account patronage dividends which are paid in money, qualified allocations, or other property (except nonqualified allocations).¹ A deduction also is allowed for nonqualified allocations when they are redeemed in cash or other property (except allocations). If there is no taxable income in the year of the redemption against which to take this deduction for redeemed nonqualified allocations, the cooperative may obtain a credit or refund of the tax it paid in the prior year on the earnings represented by the allocations. This gives the cooperative assurance that the deduction for the redeemed patronage dividend will not be wasted.

Under present law patronage dividends paid by taxable cooperatives result in a reduction in the cooperative's taxable income only if they are paid during the taxable year in which the patronage occurred, or within the period in the next year elapsing before the prior year's income tax return is required to be filed (including any extensions of time granted). This is generally a 2½-month period. In the case of exempt farmers' cooperatives, these patronage dividends presently are taken into account as a reduction in taxable income if paid at any time before the 15th day of the 9th month following the close of the year, but there is no requirement that the patronage must have occurred in that year. The bill extends the time period in

¹ For purposes of the internal revenue laws these patronage dividends are treated in the same manner as items of gross income for which deductions were allowed.

which taxable cooperatives can pay patronage dividends, and still take them into account in reducing taxable income, until this 15th day of the 9th month after the end of the year in question. This conforms the treatment to that already accorded exempt cooperatives. This period of time is also made available to both "taxable" and "exempt" cooperatives for payment of the other deductible amounts described below. In addition, exempt cooperatives are now required to pay the patronage dividends within 8½ months after the year when the patronage occurred. In the case of pooling arrangements extending over more than 1 year, the patronage is considered as occurring in the year in which the pool closes.

3. *Qualified allocation.*—Allocations, or more exactly written notices of allocation, must be in the form of capital stock, revolving fund certificates, certificates of indebtedness, or other written notice which indicates to the recipient the dollar amount allocated to him by the cooperative. For the allocation to be a qualified allocation, 20 per cent of the patronage dividend involved must be paid in money (or in a "qualified check" referred to below).² In addition, for the allocation to be qualified one of two other conditions must be met. The patron must either have the opportunity to take down the allocation in cash for a limited period of time, or, in one of three specified forms, must have given his consent to having the allocation treated as constructively distributed to him and reinvested by him in the cooperative. With respect to the first of these requirements, the bill provides that the patron must be able to convert the allocation into cash at any time during at least the first 90 days after the allocation is made. In addition, the patron must receive a written notice of the right of redemption at the same time he is notified of the allocation.

In lieu of the right to convert an allocation into cash, an allocation may be qualified where the patron gives his consent to have it treated as a distribution made to him which he agrees to take into his income for tax purposes (if the patronage arises from business activity). Under your committee's amendments this consent may take any one of three forms. For members of the cooperative this consent may be given merely by becoming, or continuing, as a member after the cooperative has adopted (after the enactment of this bill) a provision in its bylaws providing that membership in the cooperative constitutes such consent. In this case, however, the member (or prospective member) must be furnished with a written notice that the bylaws contain such a provision and must be furnished a copy of this provision. Such a consent cannot be revoked as long as the patron is a member.

A second form of consent, which may be used either for members of the cooperative, nonmembers or both, is a written statement signed by the patron in which he gives the consent referred to above. This form of consent must originally be given by the patron to the cooperative before the end of the year in which the patronage occurs and applies to all patronage in that year and subsequent taxable years until the consent is revoked. A revocation of this consent must be in writing and can be made at any time but becomes effective only for the first of the next year.³

² The 20-percent cash payment is also required in the case of exempt cooperatives for amounts paid on a patronage basis with respect to earnings derived from business done for the United States (or any of its agencies) or from sources other than patronage.

³ In the case of pooling arrangements, a revocation is effective only with respect to new pools.

A third form of consent, provided by your committee's amendments involves the use of a qualified check. This may apply either to members, nonmembers, or both, but applies only if neither of the other two forms of consent had been obtained with respect to a patron. Under this form of consent the cooperative gives the patron a check representing a portion of the patronage dividend.⁴ This check (which also includes a similar instrument redeemable in money) must have clearly imprinted on it a statement that its endorsement and cashing constitutes consent of the patron to include the full stated dollar amount of the allocation, referred to in the check, in his income, to the extent provided by the Federal tax laws. To treat the noncash allocation accompanying the qualified check as a qualified allocation, the check itself must be cashed not later than 90 days after the payment date of the cooperative for patronage dividends (that is, 90 days after September 15 in the case of a calendar year cooperative). This is not intended to deny the cooperative the right, however, to issue the qualified checks substantially before the payment date and require cashing within a 90-day period thereafter. In this manner, if the cooperative wants to, it may require any cashing of the checks before its payment date.

By any of the three forms of consent described above the patron has in effect acknowledged constructive receipt of the entire amount of the patronage dividend and has voluntarily reinvested the amount of the allocation in the cooperative.

If an allocation is not a qualified allocation because one of the conditions set forth above has not been met, it must be included in the income of the cooperative in the year issued, with a deduction being taken for this amount by the cooperative only when the nonqualified allocation is finally redeemed in cash or merchandise. If at that time the cooperative is not able to make use of a deduction, a refund may be obtained with respect to the taxes paid on this amount in the year the allocation was issued.

4. *Additional deduction for "exempt" farmers' cooperative.*—In addition to reducing taxable income for qualifying patronage dividends, the bill, permits the so-called exempt farmers' cooperative, as under present law a deduction for amounts paid out as dividends on its capital stock. Such cooperatives also receive deductions for amounts paid in money, qualified allocations, or other property (except nonqualified allocations) to their patrons on a patronage basis where the earnings involved are derived from business done for or with the U.S. Government or from sources other than patronage (such as investment income).

This deduction is the same as that provided by existing law except that the deduction is limited to qualified allocations and must be paid within 8½ months after the year in which the earnings were derived. Amounts paid in the redemption of nonqualified allocations also are available to these exempt cooperatives as deductions under the bill in the year of the redemption.

5. *Treatment of patron.*—With the exceptions referred to below, under the bill the patron is required to take into income the patronage dividends (and the nonpatronage distributions described above) paid

⁴ The check may also be used as part of a distribution of any amounts paid on a patronage basis with respect to earnings derived from business done with the United States (or any of its agencies) or from sources other than patronage.

in money, qualified allocations, or other property, and the amount he is required to take into his income is the same as that which may be currently deductible or excluded by the cooperative; namely, in the case of qualified allocations, there stated face amount, and in the case of other property (except nonqualified allocations) its fair market value. The patron also is required to take into income any nonqualified allocations which are redeemed. These amounts are taken into the patron's income in the year in which they are received by him, or in the latter case in the year in which the redemption occurs.

Generally, the effect of the treatment specified above for patrons taken together with that also outlined above for cooperatives is to obtain a single current tax with respect to the income of the cooperative, either at the level of the cooperative or at the level of the patron. However, this rule will not apply in the case of patronage dividends paid with respect to purchases of personal, living, or family items, with respect to the patronage dividends even though they are not. In such cases there is to be no inclusion in the income of the patron taken into account by the cooperative. This is in accord with the concept that patronage dividends represent price adjustments. Therefore, the patronage dividends in these cases represent downward price adjustments of personal, living, or family items and should no more lead to taxable income than bargain purchases of such items elsewhere.

An exception to the rule for inclusion of the patronage dividends in income is also made for patronage dividends attributable to purchases of depreciable property or capital assets. In such cases the patron is not required to take the dividend into income since it in effect represents an adjustment in the price paid for these articles and therefore is reflected in their basis. However, the lower basis for the property in the case of depreciable property will mean smaller depreciation deductions or in the case of capital assets (and depreciable assets) will result in a larger gain upon sale.

6. Returns of cooperatives.—Because tax-exempt cooperatives under present law are given until 8½ months after the end of the year to allocate, or pay, patronage dividends, they also have been given the same period of time in which to file their tax returns. This additional time is necessary since whether or not there is an allocation or payment of the dividends, determines the size of the taxable income of the cooperative.

Allowing taxable cooperatives this same time in which to make cash and qualified allocations of patronage dividend distributions, and to redeem nonqualified allocations, has presented the same filing problem in the case of their returns as well. Therefore, the bill provides that the tax return filing date for cooperatives generally is to be 8½ months after the end of their taxable year. However, to prevent an organization allocating relatively little of its income on a patronage basis from obtaining this postponement in the filing date for its return, the bill limits this postponement to those organizations which are either exempt cooperatives or (1) are under an obligation to allocate, or pay, at least 50 percent of their net patronage earnings in patronage dividends or (2) actually allocated, or paid, at least that percentage of their earnings in patronage dividends during the last year in which they had any such earnings.

7. Effective date.—Generally, the bill applies to taxable years of the cooperatives beginning after December 31, 1962. For the patrons

these provisions are to apply with respect to amounts paid by the cooperative during a taxable year which, at the cooperative level, is also subject to the new rules. Existing law continues to apply with respect to patronage dividends paid before the date specified above (or after that date with respect to patronage in a prior year) and also with respect to redemptions of patronage dividends after that date if the scrip involved was actually issued with respect to an earlier period.

XVIII. INCLUSION OF FOREIGN REAL PROPERTY IN BASE FOR ESTATE TAX PURPOSES

(Sec. 18 of bill and secs. 2031, 2033-2038, 2040 and 2041 of the code)

A. Reasons for provision

Under present law real estate situated outside of the United States is excluded from the gross estate and therefore exempt from the estate tax. This is an exception to the general rule that the gross estate of decedents who are citizens or residents of the United States include their entire property wherever situated. The exclusion of real property located outside of the United States from the estate tax base has been specifically provided for in the code since 1934. Before that time the exclusion was granted under an opinion of the Attorney General issued in 1918.

In 1951 Congress adopted legislation providing a credit for estate and inheritance taxes paid to foreign countries. Before that time the exclusion of real property from the estate tax base could be justified on the grounds that the foreign country was likely to impose a tax on real property located within its jurisdiction upon the death of a foreign owner. However, with the provision for the tax credit in 1951, the possibility of double taxation was removed.

The President in his tax program recommended that this exemption be eliminated on the grounds that in recent years this has been a subject of abuse. It was stated that primarily because of this tax advantage, U.S. citizens and residents have been induced to make investments in foreign real estate in countries with either no, or very low, estate or inheritance tax rates.

In view of these considerations the House bill requires the inclusion of real property located outside of the United States in the estate tax base.

B. Comparison of committee amendments with House provision

Your committee has made no change in the House provision other than to advance by 1½ years the effective date of the provision. Thus, under your committee's action the provision will generally become effective for decedents dying on or after January 1, 1963, rather than July 1, 1964. As under the House bill the provision becomes effective for decedents dying after the date of enactment of the bill in the case of property acquired on or after February 1, 1962.

C. General explanation of provision

Under present law, real property situated outside the United States is excluded in determining the value of a decedent's gross estate for estate tax purposes. This section of the bill amends various sections of the code specifically to include such real property in the gross estate of decedents who are citizens or residents of the United States. The

property is included at its fair market value either at the date of death or at the optional valuation date.

In the case of decedents dying after January 1, 1963, the bill provides that all real property located outside of the United States is to be included in the gross estate. However, some real property may also be included in a decedent's gross estate under the bill in the case of those who die after the date of enactment of the bill but before January 1, 1963. For decedents dying in this period, real property located outside of the United States is to be included in the gross estate if it was acquired on or after February 1, 1962, the date the House Committee on Ways and Means announced its action on this provision.

Capital additions or improvements to real property, to the extent they materially increase the value of the property and to the extent they are attributable to construction, reconstruction or erection on or after February 1, 1962, are treated in the same manner as real property acquired after that date. Thus, they are included in the gross estates of decedents dying after the date of enactment of the bill.

XIX. REPORTING OF INTEREST, DIVIDENDS AND PATRONAGE DIVIDENDS OF \$10 OR MORE A YEAR

(Sec. 19 of the bill and secs. 6042, 6044, 6048, 6652 and 6678 of the code)

A. Reasons for provision

The House bill would have provided a 20-percent withholding tax applicable to most interest, dividend and patronage dividend payments. In recognition of the hardship that a universal withholding system would provide, the House bill provided for an annual exemption certificate system for individuals expecting to have no tax liability. In addition, it provided for quarterly refunds of overwithholding to be made to individuals expecting to have tax liability, but with incomes of less than \$5,000 in the case of single persons or \$10,000 in the case of married couples. The refunds in this case were intended to be made on a quarterly basis during the year in which the withholding occurred in order to relieve the hardship with respect to the individuals being overwithheld upon. In addition, under certain circumstances, exemption certificates, intra-annual refunds and credits and offsets would have been available under the House bill in the case of governments, tax-exempt organizations, or corporations.

Your committee has studied at length the system provided by the House bill for withholding on dividends, interest, and patronage dividends. In addition, it has considered numerous alternative withholding provisions. It is convinced after this analysis, however, that the provision in the House bill, as well as the alternatives, are neither simple in operation nor free of substantial hardship for broad groups of taxpayers. Furthermore, it represents a heavy administrative burden for the businesses which would have to perform the withholding and collecting functions for the Government. It also appears that there are numerous tax avoidance possibilities in a system providing exemption certificates and intra-annual refunds. The exemption certificate procedure under the House bill was available only to those who expected to have no tax liability whatsoever (unless the persons involved were under age 18). Thus, many individuals, who

could expect to have a small tax liability, but be faced with substantial overwithholding on dividends and interest, would receive no relief under this exemption certificate system. Such individuals instead would have had to rely upon the quarterly refund system to recoup their overwithholding. Those who filed these claims could expect a delay of at least 3 or 4 weeks and perhaps as much as 3 or 4 months before the withheld amounts were returned. This would deprive them of the use of these funds for living expenses or as sources of investment during the interval. Moreover, the quarterly refund claims which would have had to be made four times a year involved a complex procedure.

While the exemption certificate and quarterly refund procedures of the House bill did not resolve the hardship problems for the shareholder or depositor, they nevertheless presented many compliance problems for the corporate and bank payors of the dividends and interest. Especially difficult from their standpoint would be the processing of the exemption certificates, which not only must be filed each year but also might be subject to change during the year as the individual's expectations with respect to his prospect of having a tax liability changed.

In addition, the House bill would have presented serious administrative problems for the Internal Revenue Service. The use of the exemption certificates, for example, in practice might not have been limited to those who "reasonably expect no tax liability." Moreover, since the individual, when he filed his quarterly refund claim, need submit no proof of the receipt of dividend or interest payments, here also there would seem to be a chance of fraud as well as unintentional mistakes. Nor is it clear that the ordinary recipients of dividends and interest would understand the so-called "gross-up" system which the House bill required them to follow in reporting dividends and most interest on their tax returns.

Despite the shortcomings of a system for withholding on dividends, interest, and patronage dividends, your committee strongly endorses the concept that everyone must pay his full share of the income tax liability. Moreover, it recognizes that the underreporting of dividends and interest on tax returns is a serious problem which needs correction. However, it has concluded that an improved reporting system is preferable to provision for withholding.

Your committee believes that the matching of information returns and tax returns by the Government can provide essentially the same check on dividend and interest reporting as a withholding system, except that the effectiveness of the information returns is not limited to collecting the tax at the first bracket rate. While it may be difficult initially to provide a full matching of information and tax returns, the extended use of automatic data processing, together with the accounting number system provided for in legislation enacted last year, should quite soon make it possible to provide for a full matching of these information and tax returns.

It is recognized that improving the collection of tax with respect to dividend, interest, and patronage dividend payments by an expanded use of information returns may involve some increase in the personnel of the Internal Revenue Service. It is believed, however, that this is preferable to the complications and hardships which would be involved under a withholding system.

As a result, your committee, in lieu of the withholding provisions of the House bill, provides that payors of dividends, interest, and patronage dividends are to report annually to the Federal Government all such payments aggregating \$10 or more per person. In addition, they are to send the recipients of these dividends, interest payments, or patronage dividends an annual statement indicating the total of such payments.

B. Comparison of committee amendments with House provision

As indicated above, the House bill made provision for withholding at a rate of 20 percent with respect to most interest, dividend, and patronage dividend payments. In this system provision was made for the use of exemption certificates for individuals expecting to have no tax liability and a system of quarterly refunds for those having a tax liability but subject to overwithholding. Your committee's amendments in lieu of this provide for the submission by payors of information returns to the Government for interest, dividends, and patronage dividends of \$10 or more per person per year. Essentially the same information must also be submitted by these payors to the recipients of interest, dividends, or patronage dividends. The reporting system provided is described more fully below.

C. General explanation of provision

1. *Reporting requirements.*—The bill provides that dividend, interest or patronage dividend payors who make payments during the year aggregating \$10 or more to any person are to file annual returns with the Internal Revenue Service reporting such payments. (The term "payments" is intended to include not only actual payments in cash or its equivalent but also credits to the account of the payee which he may withdraw at any time without restriction.) The return must show the aggregate amount of the payments to the person involved and give the name and address of the person to whom the payments are made. The bill also provides that nominees, who receive payments of dividends or interest and make payments of \$10 or more to other persons, also are to make a return to the Government with respect to annual payments of \$10 or more per person. This category includes such payments as those made by stockbrokers to individuals where the stock is registered in the street name of the broker. In the case of patronage dividends, only cooperatives to which the new provisions of this bill apply (sec. 17) must file these returns with respect to patronage dividends.

Existing law in the case of dividend payments provides for the submission of information returns by every cooperation "when required by the Secretary or his delegate." Under regulations (sec. 1.6042-1) the Treasury Department has required information return reporting by those making dividend payments during the calendar year of \$10 or more. In the case of interest payments, present law requires the submission of information returns with respect to payments of \$600 or more, as is true in the case of numerous other types of payments made in the course of a trade or business. In addition, present law provides that payments of interest by corporations, regardless of amount, "when required by regulations of the Secretary or his delegate" must be reported to the Internal Revenue Service. In the case of interest, however, the Secretary has not by regulations provided for reporting with respect to payments of less than \$600. In the case of

patronage dividends, present law requires reporting to the Internal Revenue Service with respect to amounts of \$100 or more. It also authorizes the Secretary to require reporting with respect to lesser amounts. The Secretary has not, however, exercised this authority.

Your committee's amendments, in addition to making mandatory the reporting of dividends, interest, and patronage dividends of more than \$10 per year per person, also continue the provisions of present law permitting the Secretary at his discretion to require reporting with respect to smaller amounts.

In addition to the reporting to the Internal Revenue Service, your committee's amendments also require that annual statements be submitted to all recipients of dividend, interest, and patronage dividend payments of more than \$10 a year. These statements must show the amount of the payment reported to the Government and the name and address of the payor. No such statements are required, however, to be furnished to any person if the aggregate of these dividend, interest, or patronage dividend payments is less than \$10 a year.

2. Penalty provisions.—Your committee, in the interest of being sure that the information returns are supplied the Government, and also that the statements are submitted to the dividend, interest, or patronage dividend recipients, has provided civil penalties which apply in the case of noncompliance.

These new penalties apply with respect to the failure to supply the information statements to those receiving \$10 or more a year and also to failures to supply information returns to the Internal Revenue Service with respect to dividend, interest, and patronage dividend payments of \$10 or more a year per person. The penalty provided in these cases, for failing to provide either a statement to the recipient, or an information return to the Government, with respect to each person to whom \$10 or more a year was paid, is \$10 for each statement or return not so filed, but not to exceed \$25,000 for failures to file returns with the Government and \$25,000 for failures to submit statements to payees, with respect to the payor in any calendar year.

Existing penalties (in general \$1 per statement but not more than \$1,000 per payor) will continue to apply with respect to the reporting which the Secretary of the Treasury may require "for payments aggregating less than \$10 a year."

3. Definitions.—In defining dividend, interest, and patronage dividend payments subject to the reporting requirements your committee has followed quite closely the definitions contained in the House bill for purposes of withholding.

Dividends are defined as distributions by a corporation which, for purposes of the Internal Revenue Code, generally are classified as a dividend. The definition of dividends for this purpose also includes payments made by stockbrokers to any person as a substitute for a dividend. This is primarily concerned with payments made by brokers to persons whose stock has been borrowed to cover short sales but who are due "dividend" payments.

Excluded from the definition of dividends for purposes of these reporting requirements are: (1) to the extent provided by regulations, any distribution or payment by a foreign corporation or to a foreign corporation, nonresident alien, or foreign partnership; and (2) undistributed taxable income of small business corporations electing to

have their income taxed to their shareholders. In any case where a payor is unable to determine whether a payment is a dividend, he is to include the entire amount as a dividend for reporting purposes.

Interest for purposes of the reporting requirements is defined as—

(1) interest on evidences of indebtedness (such as bonds, debentures, notes, and certificates) issued by a corporation in registered form. In addition, to the extent provided in regulations, interest on other evidences of indebtedness issued by a corporation of a type offered by corporations to the public;

(2) interest on bank accounts;

(3) interest, or other amounts, paid by mutual savings banks, savings and loan associations, or similar organizations with respect to deposits or similar funds left with such institutions;

(4) interest on amounts held by insurance companies under an agreement to pay interest; and

(5) interest on deposits with stockbrokers and dealers in securities.

For reporting purposes the term "interest" does not include (1) interest on tax-exempt State and local government obligations, (2) to the extent provided by regulations, interest paid by or to foreign corporations, nonresident aliens, or foreign partnerships, and (3) interest on tax-free covenant bonds. These categories for which reporting in the case of interest payments is required to include practically no interest payments by individuals.

In the case of patronage dividends, reporting is to apply to patronage dividends paid in money, qualified allocations or other property except nonqualified allocations, amounts paid by tax-exempt cooperatives with respect to earnings from business done with the U.S. Government or attributable to other than patronage and nonqualified allocations which are redeemed.

The exceptions where the reporting does not apply in the case of patronage dividends include, to the extent provided by regulations, payments made by a foreign corporation, to a foreign corporation, to a nonresident alien or to a foreign partnership. In addition if a cooperative applies to the Secretary or his delegate for exemption from the reporting requirement on the grounds that the cooperative is primarily engaged in selling at retail goods or services of a type generally for personal, living or family use, and the Secretary determines this is true, no reporting shall be required with respect to such cooperative.

4. *Inspection of books.*—Present law (sec. 7605(b)) provides certain procedures which must be followed if the Internal Revenue Service needs to make an additional inspection of a taxpayer's books of account after it has once done so. Under this section, the Secretary or his delegate may not make an additional inspection before (1) an investigation which shows necessity for the additional inspection and (2) notification of the taxpayer in writing that the inspection is necessary. At present there are relatively few cases where it is necessary for the Service to reopen a taxpayer's return which has been audited. However, with the expanded information reporting provided by your committee, it is expected that the Service will follow up discrepancies each year with respect to many taxpayers. There are difficulties in coordinating these inquiries as to discrepancies disclosed by informa-

tion returns with general audits of tax returns selected for examination. Such inquiries will be made as a routine follow-up of machine operations, and in most instances will be carried out independently of regular audit procedures.

Your committee wishes to make it clear that an Internal Revenue Service contact with a taxpayer solely for the purpose of verifying the correct amount of interest, dividends, and patronage dividends to be reported in cases of discrepancy between information returns and a tax return should not be considered as an inspection of a taxpayer's books of account (within the meaning of sec. 7605(b)). Thus, such an inquiry will not require an investigation and notification to the taxpayer in cases in which a prior audit has been conducted, nor will a subsequent audit require the investigation and notification merely because there has previously been an inquiry limited to determining the correct reporting by the taxpayer of items of gross income subject to reporting on information returns by the payors thereof.

XX. INFORMATION WITH RESPECT TO FOREIGN ORGANIZATIONS

(Sec. 20 of the bill and secs. 6038, 6046, and 6678 of the code)

A. Reasons for provision

The administration has asked for the right to obtain more information with respect to operations of Americans abroad. First, with respect to the annual information return, now required of domestic corporations controlling foreign corporations, it was requested that this return also be required of individual citizens or residents of the United States controlling foreign corporations. Second, in addition to the various specified types of information now required to be submitted, it was also requested that the Treasury Department be permitted to require the furnishing of other information which is similar or related in nature to that specified in the existing provision. Third, existing law requires the supplying of this information with respect to a foreign subsidiary, or a subsidiary of such a subsidiary. It was desired that this information also be required of any other controlled foreign corporation. Fourth, it was requested that the definition of "control" be broadened to include most of the constructive ownership rules generally applied elsewhere in the code.

The administration also requested that the information return now required of officers, directors, and significant shareholders of foreign corporations upon the creation, organization, or reorganization of such corporations also be required of persons who are now, or when they become, officers, directors, or important shareholders.

In addition, the administration requested that a civil penalty be provided for those failing to file the returns as to organization, reorganization, etc., of foreign corporations. The penalty in this case is to be \$1,000 unless it can be shown that the failure is due to reasonable cause.

The House bill provided for the submission of this additional information.

B. Comparison of committee amendments with House provision

Your committee has accepted the House provision for expansion of the information to be required with respect to foreign organizations, with four modifications. Two of these relate to the annual information return. First, with respect to the annual information return it has provided a "ceiling" on the penalty which may be imposed in those cases where this information is not supplied. The penalty under present law in general terms provides that failure to supply the required information will result in a decrease of 10 percent in the foreign tax credit allowed to a domestic corporation, plus an additional 5 percent for each additional 3-month period during which the failure to furnish the information continues. Your committee's amendments provide that in no event shall this penalty exceed \$10,000 or the income of the foreign corporation with respect to which the failure occurred, whichever is the greater. Second, in the case of the annual information return, in determining whether or not 50-percent control exists, your committee has narrowed somewhat the constructive ownership rules applied under the House bill.

In the case of the information required with respect to organizations, reorganizations, etc., your committee also has made two amendments. First, it provided that officers or directors who are U.S. citizens need supply information only if there are 5-percent U.S. shareholders, and that the information they submit be only the names and addresses of such shareholders. Second, it has added a provision that no information is to be required to be furnished with respect to a foreign corporation unless that information was required under regulations in effect 90 days prior (30 days prior at the beginning of the first year) to the date on which the U.S. persons become liable to file the return with respect to the information.

C. General explanation of provision

1. *Annual information return.*—In 1960 Congress enacted legislation (Public Law 86-780) providing that domestic corporations must furnish with respect to foreign corporations which they control and also with respect to foreign subsidiaries of any such foreign corporations information specifying—

(1) The name, place, and nature of business of the foreign corporation and country of incorporation;

(2) The accumulated profits of the foreign corporation or subsidiary, including items of income, deduction, and other items taken into account in computing these accumulated profits;

(3) A balance sheet of the foreign corporation or foreign subsidiary;

(4) Transactions between the foreign corporation or foreign subsidiary and (a) other foreign corporations or foreign subsidiaries controlled by the domestic corporation, (b) the domestic corporation or (c) any shareholder owning at least 10 percent of the stock of the domestic corporation; and

(5) A description of the various classes of stock outstanding and name and address and number of shares held by each citizen or resident of the United States and domestic corporation holding 5 percent or more of the stock of the foreign corporation or foreign subsidiary.

Corporations failing to supply any of the information required on the due date receive a 10-percent reduction in their foreign tax credit otherwise available with respect to the income derived from all the foreign corporations or their subsidiaries. If the failure to supply the information continues for more than 90 days, after notification of this failure, then for each 3 months of additional time (or fraction) the reduction in the credit is increased by 5 percent.

The House bill amends this information provision in several respects. First, it requires U.S. citizens or residents, domestic partnerships and domestic estates or trusts as well as domestic corporations controlling the foreign corporations to supply the information specified. Second, "control" is redefined by adding most of the constructive ownership rules of the existing section 318(a). Third, the House bill also extends somewhat the type of foreign corporation with respect to which information must be supplied. Existing law applied to foreign corporations controlled by Americans and subsidiaries which they control. In other words, it applies to two levels of ownership of foreign corporations. The bill extends the requirement to apply to any number of levels of ownership so long as there is control of the corporations involved. Fourth, in addition to the listed types of information, the Treasury Department may also require the furnishing of any other information which is similar or related in nature to that specified.

Your committee has accepted the House amendments with a modification of the constructive ownership rules referred to above and with the addition of a "ceiling" on the penalty provided by present law for the failure to supply the information required. In the case of the constructive ownership rules it has provided that stock owned by a partner, an estate, a trust, or a corporation will not be treated as being owned by the partnership, estate, trust or corporation if this treats a U.S. person as owning stock owned by a person who actually is not a U.S. person. Your committee's amendments also provide that a person is not to be considered as owning his pro rata share of stock held by a corporation if his stock interest is not more than 10 percent.

As indicated above, if a domestic corporation fails to supply information with respect to a subsidiary, it may lose anywhere from 10 to 100 percent of its foreign tax credit, even though only a small proportion, or none, of this credit may be attributable to the subsidiary with respect to which the information is not supplied. Your committee's amendments limit the credit which may be denied in such a case to \$10,000 or the amount of income of the foreign subsidiary with respect to which the failure occurs, whichever is the greater.

2. Information with respect to organization, reorganization, etc.— Present law also requires U.S. citizens or residents who are officers or directors of a foreign corporation within 60 days of its creation, organization or reorganization, and also U.S. persons who within the same 60-day period own 5 percent or more of the value of the stock of the corporation, to supply information with respect to this corporation. The return is required to contain such information as the Secretary of the Treasury or his delegate prescribes by forms or regulation as necessary to carry out the provisions of the income tax laws.

Under existing law it is possible to avoid this information requirement where the U.S. citizen or resident first becomes an officer, direc-

tor, or owner of 5 percent or more of the value of the stock of the corporation after the 60-day period. To prevent this avoidance of the information requirement the bill extends the requirement for supplying the information so that it applies to those U.S. citizens or residents who are officers, directors, or shareholders with more than a 5-percent interest on January 1, 1963, or who acquire such positions after that date. This information also is to be supplied by shareholders whose holdings after that date are increased to 5 percent (or where they acquire an additional 5 percent of the stock of the corporation). This reporting requirement in the case of U.S. citizens or residents who are officers or directors, however, under your committee's amendments applies only if there is a U.S. person who holds 5 percent or more of the stock of the corporation. Moreover, only the names and addresses of the 5-percent shareholders who are U.S. persons are required to be reported.

Your committee has also added an amendment to provide that no information is to be required of a foreign corporation unless that information was required under regulations in effect 90 days (30 days at the beginning of first year) prior to the time the liability to file a return under this provision arises.

The bill also adds a new section to the code providing a civil penalty in the case of any person required to file the return referred to here who fails to do so at the time required, or who files a return which does not show the information required. The penalty in this case is to be \$1,000 unless it is shown that the failure is due to reasonable cause.

3. *Effective dates.*—The amendments with respect to the annual information return apply with respect to annual accounting periods of the foreign corporations beginning after December 31, 1962. The amendments relating to the filing of returns as to organization, reorganization, etc., of foreign corporations takes effect on January 1, 1963.

XXI. CLEARING OF LAND

(Sec. 21 of the bill and sec. 182 of the code)

A. *Reasons for provision*

Under existing law expenses incurred in carrying on a trade or business of farming are deductible in determining taxable income. In 1954 Congress amended the statute to include in the deductible category expenses for soil and water conservation.

This new provision deals with a problem quite similar to that which resulted in the enactment of the soil and water conservation provision. At the present time, expenditures made during the preparatory period in extending a farm may not be deducted since they are not expenses incurred in the business of farming. Examples of expenditures of this nature which, under existing law, must be capitalized are expenditures (including material and labor) incurred in: (1) Clearing brush, trees, and stumps, (2) leveling and conditioning land, and (3) straightening creek beds. Because expenditures for these purposes, when incurred in order to make the land suitable for farming (like expenses for soil conservation), also are closely associated with the trade or business of farming, your committee believes that it would be proper to allow their deduction to a limited extent.

B. Comparison of committee amendment with House provision

There was no comparable provision in the House bill.

C. General explanation of provision

This provision permits taxpayers engaged in the business of farming to deduct, in computing their Federal income tax, expenditures incurred by them in clearing land to make it suitable for farming. Activities included in clearing and preparing land to make it suitable for farming include the clearing of brush, trees, stumps, and boulders, the leveling and conditioning of the land, and the diversion of streams.

Under the bill, deduction of expenditures in any taxable year for these purposes may not exceed \$5,000, or, if lesser, 25 percent of the taxpayer's taxable income from farming. In determining the amount which may be deducted within these limitations, the farmer is permitted to include a reasonable allowance for depreciation with respect to tractors and other items subject to the allowance for depreciation which are ordinarily used by him in his farming activities but which actually may have been used also in the clearing of land.

This provision is to apply for taxable years beginning after December 31, 1962.

XXII. CHARITABLE CONTRIBUTIONS MADE FROM INCOME ATTRIBUTABLE TO SEVERAL TAXABLE YEARS

(Sec. 22 of the bill and sec. 1307 of code)

A. Reasons for provision

In the case of individuals who receive compensation in 1 year for services performed over a period of more than 3 years, or who receive a lump sum of income from an invention or artistic work (or from certain other specified sources) present law provides that the tax on this income is not to be greater than the tax which would have resulted if the bunched income had been received ratably over the period to which it is attributable. The effect of this is to permit income to be averaged for tax purposes in the specified situations.

In applying this provision, the Internal Revenue Service has ruled that deductions based upon adjusted gross income (such as charitable contributions and medical expenses) must be recomputed each time a different amount is taken to represent adjusted gross income in determining tax under the averaging provisions (IR-Mim. 43, 1952-2CB 112). It has come to the attention of your committee that because of this recomputation some individuals who make substantial charitable contributions in years in which they receive "bunched income" are unable to take full advantage of the deduction for such contributions. This occurs because, although the bunched income in effect may be spread over the years to which it is attributable, contributions may be deducted only in the year in which they are made. Thus, while the charitable contribution may have been fully deductible if the individual's adjusted gross income for the year were determined before the spreading, once the spreading provisions are applied adjusted gross income for the year in which the contribution is made must be reduced, thereby limiting the amount of the charitable contribution which may be deducted.

To prevent this wastage of charitable contribution deductions your committee has added to the House bill a provision which permits the individual an election to apply the charitable contribution limitations to the adjusted gross income before the bunched income in effect is spread over the years to which it is attributable.

B. Comparison of committee amendments with House provision

There is no comparable provision in the House bill.

C. General explanation of provision

This provision adds to the statute a special rule for determining the amount of charitable contributions deductible by an individual when his "bunched income" is to be spread under the special "averaging" provisions of the tax law. Under this rule the limitation on charitable contributions (20 or 30 percent of adjusted gross income) made in the year in which the bunched income is received may be applied before the income is spread over the years to which it is attributable. Only the net amount of bunched income remaining after the charitable contribution has been deducted will in effect be spread back over the years to which attributable. If the individual elects to deduct charitable contributions in this manner, he cannot include again any portion of the bunched income in determining the limitation on charitable contributions for the year in which the bunched income is received after the income is spread over the years to which it is attributable.

This provision is to apply with respect to taxable years beginning after December 31, 1962.

XXIII. EFFECTIVE DATE OF SECTION 1371(c) OF THE INTERNAL REVENUE CODE OF 1954

(Sec. 23 of bill and sec. 1371(c) of code)

A. Reasons for provision

Under existing law certain small business corporations may elect to have income taxed directly to their shareholders, thereby eliminating tax at the corporate level. For such an election to be valid, however, the corporation must have no more than 10 shareholders and each shareholder must give his consent to the election.

Previously a problem existed as to the proper method of determining the number of shareholders of a corporation in community property States or where the stock of a corporation was held jointly by husband and wife. In 1959 Congress removed this problem by specifically providing how the number of shareholders was to be determined where husband and wife resided in community property States or where they held stock jointly. Congress provided in such cases that the spouses would be treated as one shareholder (Public Law 86-376, approved September 23, 1959). This provision was made effective with respect to taxable years of small business corporations beginning after December 31, 1959. However, cases have come to the attention of your committee in which small business corporations were prevented from making (or continuing) an election to have their income of 1958 and 1959 taxed to their shareholders because husbands and wives in community property States or who held stock jointly have each been counted as a separate shareholder for those

years. The first year with respect to which such an election could be made was 1958.

Your committee does not believe that the rule enacted by Public Law 86-376 for determining the number of shareholders of a small business corporation should be limited to years after 1959, but should apply to all years for which such an election may be made. This will insure the application of the same rules in applying the 10-shareholder limitation for all years in qualifying a small business corporation for such an election. Accordingly, this provision of the bill makes that rule of Public Law 86-376 apply also to years 1958 and 1959.

B. Comparison of committee amendments with House provision

There is no comparable provision in the House bill.

C. General explanation of provision

This bill provides that with respect to the years 1958 and 1959, in determining the number of shareholders of a small business corporation for purposes of the election provided by subchapter S of the Internal Revenue Code (under which shareholders are taxed directly on the corporate earnings), spouses who hold stock of such a corporation jointly or under the community property laws of a State are to be treated as one shareholder; that is, section 1371(c) of the code will now be applicable to such years.

In order to insure that a small business corporation whose status may be affected by this provision will have an opportunity to qualify for treatment under subchapter S, the bill provides a special 1-year period within which a special election may be made to have the earlier effective date of section 1371(c) apply. For the special election to be valid, however, a corporation must have met the statutory requirements of subchapter S in 1958 and 1959, and must have filed a timely election to be subject to subchapter S for those years. Furthermore, each person who is a shareholder at the time of the special election must give his consent and each person who was a shareholder for any taxable year ending before the year in which the special election is made also must give his consent. Finally, where an election (and the requisite consents) has been made, the statute of limitations for assessing additional tax against the corporation or its shareholders is to remain open, or be opened, for 1 year following the date of the election. Tax assessed or credit or refunds granted within this special period of limitations must relate only to changes resulting directly from the election.

XXIV. CERTAIN LOSSES SUSTAINED IN CONVERTING FROM STREET RAILWAY TO BUS OPERATIONS

(Sec. 24 of the bill)

A. Reasons for provision

Present law provides that business losses incurred in one year can be carried back to the 3 prior years and then, to the extent not absorbed by income in those years, carried forward to the 5 succeeding years after the year in which the losses occurred. For most companies which again earn income such a period is long enough to absorb all of their losses against income.

Rapid transit companies in recent years have had a special problem in connection with the very large losses they have incurred in converting from streetcar to bus operations. Because of the size of these losses, most transit companies have spread their conversion to buses over many years—some over as many as 15 years—so that a sufficient period will be available to absorb the losses against income. However, a situation has come to the attention of your committee in which the conversion from streetcars to buses was completed in an 18-month period. It appears that the conversion was made in such a short period because of fraud on the part of the then existing management. Moreover, evidence is available that the then existing management made this conversion in the 18-month period despite the fact that it was pointed out to them by their financial experts that such losses could not be absorbed within the period of the 5-year carryforward.

After the mismanagement was discovered, the company was reorganized and new officers and a new board of directors elected. However, the conversion from streetcars to buses in the 18-month period could not be undone. As a result of this conversion the company sustained a loss of approximately \$10,200,000. At the end of the 5-year carryforward period about \$5,200,000 of this loss remained unused. While the company has recently been making a small profit, it appears that rate increases may have to be requested if this remaining loss cannot be offset against the income of future years.

Your committee believes that since ordinary prudent, honest management would have spread the conversion over a number of years, a longer carryforward of the unused loss should be permitted. This is a particularly serious problem because of the present inadequacy of our mass transportation system and the fact that a rapid transit system is involved here. Moreover, in this case it is likely that in the long run it will be the users of the transportation who will suffer if the company is not permitted to utilize the benefit of this loss.

B. Comparison of committee amendments with House provision.

There was no comparable provision in the House bill.

C. General explanation of provision

The bill provides that in the case of net operating losses incurred in the calendar years 1953 and 1954, principally as a result of the conversion from streetcar to bus operations, an additional 5 years is to be allowed to offset such losses against income. The bill achieves this result by providing that such losses are to be known as "unused conversion losses" to the extent they still remain unused after the end of the normal 5-year carryforward period. The bill provides that such an unused conversion loss from these 2 years is to be considered a net operating loss sustained in 1959 and therefore available as a net operating loss carryforward to the calendar year 1960 and four subsequent taxable years.

The treatment described above is to apply only for years in which the taxpayer is engaged in the furnishing or sale of transportation on a local electric railroad, trackless trolley system, or bus system. The rates for the transportation in such cases must have been established or approved by a governmental unit, by a public service or public utility commission or similar body.

In the case brought to your committee's attention there is an unused loss of approximately \$5,200,000 from the years 1953 and 1954, and it is estimated, based upon anticipated revenues, that from \$2 to \$3 million of this loss can be offset against income in the additional 5-year period allowed by this bill.

XXV. PENSION PLAN OF LOCAL UNION NO. 435, INTERNATIONAL HOD CARRIERS' BUILDING AND COMMON LABORERS' UNION OF AMERICA

(Sec. 25 of the bill)

A. Reasons for the provision

Under present law, a pension trust is qualified for income tax exemption only if it meets certain requirements relating to coverage of employees and nondiscrimination of contributions or benefits. Where the pension trust is properly qualified, not only is it exempt from Federal taxation with respect to its income, but contributions paid to it by an employer on behalf of his employees are deductible for Federal income tax purposes. Thus, there is considerable incentive for a pension trust to meet the requirements of the Internal Revenue Code and thereby become a qualified trust.

Occasionally, however, it is difficult for a pension trust to achieve qualified status before employer contributions are received by it. This is particularly true in the case of pension plans negotiated under collective-bargaining agreements with many employers, both large and small. Often, considerable time is required to obtain sufficient factual data upon which to insure the actuarial soundness of the plan. Sometimes a formality is not properly performed.

In such cases, where the pension plan operates for some period as a nonqualified plan prior to securing qualification under the Internal Revenue Code, any income it may earn during such period is subject to income tax, thereby reducing amounts which would otherwise serve to provide employee benefits under the plan. In addition, employer contributions are not allowed as deductions unless the employee is given immediate vested rights to the contribution.

Your committee believes these are rather severe consequences, particularly where failure to meet the conditions of the statute for qualification is due to the fact that, because the plan involved many employers, the arrangements could not be worked quickly although it was the initial intention of both the employers and the unions to meet those conditions. If the pension trust has never been operated in a manner which would jeopardize the interest of its beneficiaries, and if, when completed, the pension plan of which the trust is a part conforms with the Internal Revenue Code and has received the approval of the Internal Revenue Service, your committee believes it is just, under such circumstances, to provide that the pension plan be treated as a qualified trust during the intervening period between its inception and the time it actually qualified for tax exemption.

B. Comparison of committee amendments with House provision

There is no comparable provision in the House bill.

C. General explanation of provision

This section of the bill provides that the pension plan of Local Union No. 435, International Hod Carriers' Building and Common Laborers' Union of America, established pursuant to negotiations between the union and the Building Trades Employers' Association of Rochester, which is a qualified trust under section 401(a) of the Internal Revenue Code, is to be treated as having been a qualified trust and to have been exempt from taxation for the period beginning May 1, 1960, and ending April 20, 1961. For this provision to apply however, it must be shown to the satisfaction of the Secretary of the Treasury or his delegate that the trust has not in the period designated been operated in a manner which would jeopardize the interests of its beneficiaries.

Under the bill not only will the income of the pension plan during the specified period be exempt from tax but also contributions made under the plan within such period by employers generally will be deductible by them in determining their Federal income tax liability.

XXVI. CONTINUATION OF PARTNERSHIP YEAR FOR SURVIVING PARTNER IN A TWO-MAN PARTNERSHIP WHERE ONE DIES

(Sec. 26 of bill and sec. 188 of 1939 code)

A. Reasons for provision

The attention of your committee has been called to a case where the partnership provisions of the 1939 Code worked a substantial hardship. The case brought to your committee's attention involves a two-man partnership with a partnership year ending on January 31. The 1939 Code provides that income of partnerships is to be reported by the partners for tax purposes in their year in which, or with which, the partnership year ends. Thus, income from the partnership year ending on January 31, 1946, for example, would be reported by partners on a calendar year basis in their calendar year 1946. However, where one of the partners dies, for example, before the end of December, 1946, the partnership income in that year, which ordinarily would be reported for tax purposes by the partners in 1947, must then be reported by the partners, or their estate, in the calendar year 1946. This can result in a bunching of income, and therefore application of the higher surtax rates, since income of a partner for as long as 23 months may, in this manner, have to be reported in a single year.

At the time of the passage of the 1954 Code, the law was changed to provide that the partnership year was not to close upon the death of a partner but instead was to run to its normal conclusion. In this regard the report of your committee on the 1954 Code stated as follows:

Under present law there has been the contention that the death of a partner closes the partnership year and [in] the bunching of more than a year's income in the decedent's last year. Where the partnership and the partners are on different taxable years, this would have the effect of concentrating as much as 23 months' income in the final return of the deceased partner, that is, the income for the partner-

ship year ending within his taxable year and the income for the taxable year closed by the partner's death.

The problem presented in the case called to your committee's attention occurred before the 1954 Code provision became applicable. Moreover, here the bunching occurs not only with respect to the deceased partner, but with respect to the surviving partner as well, since a partnership was held to no longer exist upon the death of one of two partners.

B. Comparison of committee amendments with House provision

There is no comparable provision in the House bill.

C. General explanation of provision

The bill adds a provision to the 1939 Internal Revenue Code to provide that the death of a partner in a two-man partnership is not to result in the termination of the partnership, or the closing of the taxable year of the partnership with respect to the surviving partner, prior to the time the partnership year would have closed if neither partner had died nor disposed of his interest. Thus, in the case of a partner dying in 1946 where the partnership year does not end until January 31, 1947, the partnership year would continue to that date and the income for such year would be reported by the surviving partner on his tax return for 1947. This provision is to apply only if the surviving partner so elects within 1 year after the date of enactment of this provision.

This amendment applies to taxable years of a partnership beginning after December 31, 1946, to which the Internal Revenue Code of 1939 applies. Generally the 1939 Code applied to partnership taxable year beginning before January 1, 1955. The bill also provides that if refund or credit for an overpayment resulting from the application of this provision is prevented by the operation of any law or rule of law (other than those relating to closing agreements or compromises) the refund or credit of the overpayment may nevertheless be made if the claim is filed within 1 year after the date of enactment of this bill.

XXVII. TREATIES

(Sec. 27 of bill)

Section 7852(d) of the code provides that no provision of the internal revenue title is to apply where its application would be contrary to any treaty obligation of the United States in effect on the date of the enactment of the Internal Revenue Code.

The House bill provided that section 7852(d) of the code was not to apply to any provision contained in this bill and that if any provision in this bill would contravene any existing tax treaty, then the new statutory law was to have precedence over the prior treaty obligation.

Numerous witnesses before your committee have expressed the view that provisions in the bill would be contrary to tax treaty obligations of the United States. Your committee has no desire to abrogate any provision in any treaty. For that reason, it has substituted for the provision in the House bill, language which provides that no provision of this bill is to apply in any case where its appli-

cation would be contrary to any treaty obligation of the United States. The Secretary of the Treasury in his appearance before your committee has indicated that he is in agreement with the adding of this provision.

XXVIII. NEW ELECTION TO FILE SEPARATE RETURNS WHERE CONSOLIDATED RETURN HAD BEEN FILED

The Internal Revenue Code leaves to regulations issued by the Treasury Department requirements as to the filing of consolidated returns by an affiliated group and the requirements for changing from a consolidated return to separate returns. Generally it has been held that a consolidated return once filed must be continued in subsequent years unless there is a significant change in the tax laws. Your committee agrees with the House that enactment of this bill constitutes a significant change in the tax laws and that a new election to file separate returns where a consolidated return has previously been filed should be available for the first taxable year ending after the date of enactment of this bill.

TECHNICAL EXPLANATION OF THE BILL

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TECHNICAL EXPLANATION OF THE BILL

SECTION 1. SHORT TITLE, ETC.

(a) *Short title*.—Section 1(a) of the bill provides that the bill may be cited as the “Revenue Act of 1962.”

(b) *Table of contents*.—Section 1(b) of the bill consists of a table of contents for the bill.

(c) *Amendment of 1954 Code*.—Section 1(c) of the bill provides that, except as otherwise expressly provided, whenever in the bill an amendment or repeal is expressed in terms of an amendment to (or repeal of) a section or other provision, the reference is to be considered to be made to a section or other provision of the Internal Revenue Code of 1954.

SECTION 2. CREDIT FOR INVESTMENT IN CERTAIN DEPRECIABLE PROPERTY

(a) *Allowance of credit*.—Section 2(a) of the bill redesignates section 38 of the code as section 39 and inserts a new section 38 in part IV of subchapter A of chapter 1 (relating to credits against tax).

Subsection (a) of the new section 38 provides that there is to be allowed, as a credit against the tax imposed by chapter 1 of the code, the amount determined under the new subpart B, added by section 2(b) of the bill. Subsection (b) of the new section 38 requires the Secretary of the Treasury or his delegate to prescribe such regulations as may be necessary to carry out the purposes of the new section 38 and the new subpart B.

(b) *Rules for computing credit*.—Section 2(b) of the bill adds a new subpart B to part IV of subchapter A of chapter 1 of the code. The new subpart consists of three sections (secs. 46–48) which are explained below.

SECTION 46. AMOUNT OF CREDIT

(a) *Determination of amount*.—Paragraph (1) of section 46(a) provides in general that the credit allowed for the taxable year is to be an amount equal to 7 percent of the qualified investment as defined in subsection (c) of section 46. Under paragraph (2) of section 46(a) the amount of the credit may not exceed so much of the liability for tax for the taxable year as does not exceed \$25,000 plus 25 percent of so much of such liability as exceeds \$25,000. However, the \$25,000 amount provided by section 46(a)(2) is reduced in the case of certain married individuals filing separate returns (see sec. 46(a)(4)), corporations which are members of affiliated groups (see sec. 46(a)(5)), trusts and estates (see sec. 48(f)(3)), and certain other special types of taxpayers referred to in section 46(d).

Under paragraph (3) of section 46(a), the liability for tax for the taxable year is defined as the tax imposed by chapter 1 (including the 2-percent tax on consolidated taxable income) reduced by the sum

of the credits against the income tax allowed by sections 33, 34, 35, and 37. For purposes of determining the liability for tax, the taxes imposed by sections 531 and 541 (relating, respectively, to the accumulated earnings tax and the personal holding company tax) are not considered taxes imposed by chapter 1. Thus, the liability for tax as defined in section 46(a)(3) and the credit allowable for the taxable year under section 38 are determined before computing any tax imposed by section 531 or 541.

Paragraph (4) of section 46(a) provides generally that, in the case of separate returns filed by a husband and wife, the credit allowed to each may not exceed so much of the liability for tax for the taxable year as does not exceed \$12,500 plus 25 percent of so much of such liability as exceeds \$12,500. However, this reduction in the limitation applies only if the taxpayer's spouse is entitled to an investment credit for the taxable year of such spouse which ends with, or within, the taxpayer's taxable year. Such spouse may be entitled to an investment credit either because of qualified investment made in such taxable year for (whether directly made or whether allocated to such spouse by, for example, a subch. S corporation or a partnership), or because of an unused credit carryback or carryover to, such taxable year.

Paragraph (5) of section 46(a) provides generally that the \$25,000 amount specified in subparagraphs (A) and (B) of section 46(a)(2) is to be reduced for each corporation which is a member of an affiliated group by apportioning \$25,000 among the members of such group in the manner prescribed by regulations of the Secretary of the Treasury or his delegate. An affiliated group within the meaning of section 46(a)(5) is one described in section 1504(a), except that any corporation may be treated as a member of an affiliated group. Thus, an affiliated group for purposes of section 46(a)(5) may include any of the corporations excluded by section 1504(b) from being a member of an affiliated group for purposes of filing a consolidated return. For example, an affiliated group within the meaning of section 46(a)(5) could include a corporation exempt from taxation under section 501 or a foreign corporation.

The application of the limitation provisions of section 46(a) may be illustrated by the following example:

The qualified investment of an unmarried taxpayer is \$2,050,000. His liability for tax for the taxable year is \$185,000. The credit computed without regard to the limitation in section 46(a)(2) is \$143,500 (7 percent of \$2,050,000). The allowable credit for the taxable year is \$65,000 (\$25,000 plus 25 percent of \$160,000).

(b) *Carryback and carryover of unused credits.*—Section 46(b) as passed by the House provided a 5-year carryover for unused credits. Your committee has added a 3-year carryback for unused credits.

Paragraph (1) of section 46(b) provides for a 3-year carryback and a 5-year carryover of any unused credit. Under this provision, if the credit earned during the taxable year exceeds the limitation under section 46(a)(2) for that year (hereinafter referred to as "unused credit year"), the excess (the credit earned but not used to reduce tax for that year) is a carryback to each of the 3 preceding taxable years, and a carryover to each of the 5 succeeding taxable years and, subject to the limitation of paragraph (2) of section 46(b), is to be added to the amount allowable as an investment credit for those

years. Such excess, however, may be a carryback only to taxable years ending after June 30, 1962. The entire amount of the excess (the unused credit for any unused credit year) must be carried first to the earliest of the 8 taxable years to which section 46(b) permits it to be carried. It may then be carried to each of the other 7 taxable years (in order of time) to the extent that, because of the limitation provided in paragraph (2) of section 46(b), it could not be added for a prior taxable year.

Paragraph (2) of section 46(b) provides that the amount of the unused credit from an unused credit year that may be added to the amount allowable as an investment credit for any of the 3 preceding or 5 succeeding taxable years is not to exceed the amount by which the limitation (determined under sec. 46(a)(2)) for such preceding or succeeding taxable year exceeds the sum of (1) the investment credit allowable for such year by reason of investment made in such year, and (2) other allowable unused credits which are attributable to years prior to the taxable year in which the unused credit originated. Thus, before an investment credit carryback or carryover from an unused credit year may be taken into account in any preceding or succeeding taxable year, the credit allowable for such preceding or succeeding taxable year (determined without regard to carrybacks or carryovers of unused credits to that year) will first be applied. Unused credits originating from taxable years prior to the unused credit year will be applied next. To the extent that the investment credit carryback or carryover from an unused credit year cannot be used in a particular preceding or succeeding taxable year because the sum of the credit earned and allowable in that year and the carrybacks and carryovers to that year from taxable years preceding the unused credit year exceed the limitation on allowable credit for such year, the carryback or carryover will be carried forward to the next succeeding taxable year.

Effect of net operating loss carryback

Paragraph (3) of section 46(b) provides that to the extent that an unused credit arises by reason of a net operating loss carryback, subparagraph (A) of section 46(b)(1) will not apply. Although no investment credit carryback of an unused credit will be allowed to the extent that the unused credit arises from the application of a net operating loss carryback, the full amount of the unused credit so arising will be available for use as an investment credit carryover. Thus, assume a taxpayer's credit based on investments in 1965 is \$25,000, and such credit is allowable in full for that year. Subsequently, such taxpayer has a net operating loss that he carries back to 1965 which eliminates the taxpayer's liability for tax for that year. The \$25,000 credit (no longer allowable for the year 1965) is an investment credit carryover that may be carried forward to the 5 succeeding taxable years but is not to be treated as an investment credit carryback.

Taxable years beginning before July 1, 1962

Paragraph (4) of section 46(b) provides a transition rule relating to the amount of an investment credit carryback that may be added under section 46(b)(1) for a taxable year beginning before July 1, 1962, and ending after June 30, 1962. For purposes of determining the amount that may be carried back to such a taxable year, the

amount of the limitation provided by section 46(a)(2) will be considered to be an amount which bears the same ratio to such limitation as the number of days in such year after June 30, 1962, bears to the total number of days in such year.

The application of the carryback and carryover of the unused credit provided for in subsection (b) of section 46 may be illustrated by the following examples:

Example 1.—A new taxpayer's credit based on his investment for the taxable year 1963 amounts to \$120,000, and the limitation under section 46(a)(2) is \$110,000. The taxpayer's unused credit for 1963 amounts to \$10,000 (\$120,000 minus \$110,000), which he may carry forward to 1964 and the 4 succeeding taxable years (there is no carryback because 1963 is the taxpayer's first taxable year). The credit based on his investment for 1964 is \$135,000, and the limitation under section 46(a)(2) is \$120,000. Since the taxpayer is limited to a credit of \$120,000 for 1964, his total unused credits to be carried forward to 1965 amount to \$25,000, \$10,000 from 1963 and \$15,000 from 1964. There is no carryback to 1963 of the \$15,000 unused credit from 1964 because the credit based on investment for 1963 already exceeds the limitation. The credit based on the taxpayer's investment for 1965 is \$135,000, and the limitation under section 46(a)(2) is \$140,000. The taxpayer first applies the \$135,000 for 1965 against the \$140,000 limitation. He next applies any unused credit carried forward from 1963 against the remaining \$5,000 allowable. Since the \$10,000 credit carried forward from 1963 is in excess of the \$5,000 remaining amount allowable for 1965, he has unused credits to carry over to 1966 of \$20,000, \$5,000 from 1963 and \$15,000 from 1964.

Example 2.—X files his tax return on the basis of a calendar year. X's credit based on his investment, and the limitation under section 46(a)(2) for each of the taxable years 1962 through 1968 is as follows:

	Credit	Limitation
1962.....	\$75,000	\$200,000
1963.....	250,000	160,000
1964.....	200,000	210,000
1965.....	210,000	230,000
1966.....	220,000	260,000
1967.....	260,000	220,000
1968.....	270,000	280,000

X's credit for 1962 (for investment in property acquired after June 30, 1962) is allowable in full since it is less than the limitation for that year. His credit for 1963 of \$250,000 is limited by section 46(a)(2) to \$160,000. The unused credit for that year of \$90,000 is an investment credit carryback to 1962, and an investment credit carryover to 1964 through 1968. The amount of the 1963 unused credit that may be added for 1962 is limited to \$25,822 ($\$200,000 \times 184/365$, less \$75,000) by reason of the application of section 46(b)(4). The balance of the 1963 unused credit, \$64,178 (\$90,000 less \$25,822) is carried forward to 1964; \$10,000 of the 1963 unused credit may be added to the amount of the credit allowable in 1964 since the limitation on the credit for 1964 exceeds the credit earned for that year by \$10,000 (\$210,000 less \$200,000). The \$54,178 balance of the 1963 unused credit (\$64,178 less \$10,000) is then carried forward to 1965;

\$20,000 of the 1963 unused credit may be added to 1965 since the limitation on the credit for 1965 exceeds the credit earned for that year by \$20,000 (\$230,000 less \$210,000). The remaining balance of the 1963 unused credit, \$34,178, is carried to 1966 and may be added in full to the amount of the credit allowable in 1966 since the limitation for that year exceeds the credit earned for that year by more than the amount of the carryover. The unused credit from 1967 of \$40,000 (\$260,000 credit earned less \$220,000 limitation on credit) is an investment credit carryback to 1964, 1965, and 1966, and a carryover to 1968 and the 4 succeeding taxable years. None of the 1967 unused credit may be added for 1964 or 1965 because for each of those years the sum of the credit earned and allowable and the additions on account of unused credits from prior unused credit years exceeds the limitation for such years; \$5,822 of the 1967 unused credit may be added for 1966 since the limitation for that year (\$260,000) exceeds by \$5,822 the sum of the credit earned and allowable for that year (\$220,000) and the additions on account of the 1963 unused credit (\$34,178); \$10,000 of the 1967 unused credit may be added for 1968, and the balance (\$24,178) may be carried forward to the 4 succeeding years.

(c) *Qualified investment*.—Paragraph (1) of section 46(c) defines “qualified investment” to mean, with respect to any taxable year, the aggregate of the applicable percentage of the basis of each new section 38 property placed in service by the taxpayer during such taxable year, plus the aggregate of the applicable percentage of the cost of each used section 38 property placed in service by the taxpayer during such taxable year. Under paragraph (2) of section 46(c), the applicable percentage to be applied to the basis (or cost) is (1) 33⅓ percent if the estimated useful life is 4 years or more but less than 6 years, (2) 66⅔ percent if the estimated useful life is 6 years or more but less than 8 years, and (3) 100 percent if the estimated useful life is 8 years or more.

The basis of “new section 38 property” is to be determined under the general rules for determining the basis of property. Thus, the basis of property purchased or constructed would generally be its cost. If property is acquired in a nontaxable exchange to which section 1031 applies by trading in old property and paying a cash difference, the basis of the newly acquired property would be equal to the adjusted basis of the old property, plus the cash paid. However, the basis adjustment required by section 48(g) is to be disregarded for purposes of computing the credit.

The cost of each “used section 38 property” is to be determined in accordance with section 48(c)(3)(B) and with regard to section 48(g). However, the aggregate cost of used section 38 property which may be taken into account in any taxable year in computing qualified investment cannot exceed \$50,000. (See sec. 48(c)(2).)

The credit will apply to new and used property only for the first taxable year such property is placed in service by the taxpayer. The date on which property is placed in service is the first date depreciation would be allowable to the taxpayer if he computed his depreciation deduction on a daily basis. Thus, in determining the date an asset is placed in service, the fact that the taxpayer, in computing his depreciation allowance, uses an assumed timing of additions under one of

the "averaging conventions" is to be disregarded, but only for the purposes of the investment credit.

The estimated useful life of any property is to be determined as of the time such property is placed in service by the taxpayer, and with reference to the useful life in the hands of the taxpayer. Thus, if a taxpayer acquires used section 38 property with a remaining useful life of 3 years in his hands, such property will not qualify regardless of the original estimated useful life to the previous owner. See section 48(d) for the useful life to be used by certain lessees. The estimate of the useful life is to be based on the facts and circumstances known on the date the asset is placed in service.

An estimated useful life must be assigned to each separate property. Thus, if a taxpayer is using a multiple-asset account, he must assign a useful life to each asset in such account for the purpose of computing his qualified investment. If a taxpayer is using a method of depreciation, such as the units of production method, which does not measure useful life in terms of years, he must estimate useful life in years in order to compute his qualified investment.

The provisions of paragraphs (1) and (2) of section 46(c) may be illustrated by the following examples:

Example 1.—Corporation Y acquires and places in service during 1963 the following new and used section 38 assets:

Property	Estimated useful life (years)	Basis or cost
A (new).....	5	\$60,000
B (new).....	10	90,000
C (new).....	6	150,000
D (used).....	4	30,000

Corporation Y's qualified investment for 1963 is \$220,000 determined in the following manner:

Property	Basis or cost times applicable percentage	Qualified investment
A.....	$\$60,000 \times 33\frac{1}{3}$ percent.....	\$20,000
B.....	$\$90,000 \times 100$ percent.....	90,000
C.....	$\$150,000 \times 66\frac{2}{3}$ percent.....	100,000
D.....	$\$30,000 \times 33\frac{1}{3}$ percent.....	10,000
Total.....		220,000

Example 2.—Mr. X, unmarried, owns and operates a business as a sole proprietorship and reports income on a calendar-year basis. He is also a member of the XYZ partnership, which is also on a calendar-year basis. During 1963 Mr. X acquires and places in service in his sole proprietorship a new section 38 property having an estimated useful life of 9 years and a basis of \$25,000. Also during 1963 the XYZ partnership acquires and places in service a new section 38 property having an estimated useful life of 4 years to the partnership and a basis of \$18,000.

X's share of the basis of the new section 38 property acquired by partnership XYZ is \$6,000. X's qualified investment for 1963 is \$27,000, composed of \$25,000 from his sole proprietorship (basis of

\$25,000 times applicable percentage, 100 percent), and \$2,000 attributable to the property of the XYZ partnership (basis of \$6,000 times applicable percentage, 33⅓ percent).

Public utility property

Paragraph (3)(A) of section 46(c) provides that in the case of section 38 property which is public utility property, the amount of the qualified investment is to be three-sevenths of the amount ascertained under section 46(c)(1) with respect to such property.

Paragraph (3)(B) of section 46(c) defines "public utility property" as property used predominantly in the trade or business of the furnishing or sale of (i) electrical energy, water, or sewage disposal services, (ii) gas through a local distribution system, (iii) telephone service, or (iv) telegraph service by means of domestic telegraph operations (as defined in sec. 222(a)(5) of the Communications Act of 1934, as amended; 47 U.S.C., sec. 222(a)(5)), if the rates for such furnishing or sale have been established or approved by a State (as defined in sec. 7701(a)(10) of the code) or political subdivision thereof, by an agency or instrumentality of the United States, or by a public service or public utility commission or other similar body of any State or political subdivision thereof. The term "established or approved" by a State, etc., includes the filing of a schedule of rates with any of the named bodies having the power to approve such rates, even though such body has taken no action on the filed schedule.

If a taxpayer is engaged in one or more regulated activities enumerated in section 46(c)(3)(B) (hereinafter referred to as a utility activity) and is also engaged in a separate trade or business that is not considered a utility activity, property used in the latter trade or business is not subject to the reduction contained in paragraph (3)(A) of section 46(c). If property is used by a taxpayer both in a utility activity and a nonutility activity, the characterization of such property is to be based on the predominant use of such property during the taxable year the property is placed in service. Once property is characterized as public utility property, the fact that in any subsequent year such property is used predominantly in the nonutility business is to be disregarded.

"Public utility property" includes property leased to a taxpayer which uses such property predominantly in a utility activity. Thus, property leased to a taxpayer which uses the property predominantly in a utility activity during a taxable year is to be treated as public utility property for purposes of computing the lessor's credit. "Public utility property" also includes property which is leased to others by a taxpayer where the leasing of such property is part of its utility activity.

Section 38 property which is not public utility property is not subject to the three-sevenths reduction contained in section 46(c)(3)(A). Thus, for example, in the case of property which is used predominantly in international telegraph operations, which is not used predominantly outside the United States, and which otherwise qualifies as section 38 property, the qualified investment is to be determined without reduction by reason of section 46(c)(3)(A).

The provisions of section 46(c)(3) may be illustrated by the following example:

Corporation X is engaged in a trade or business of furnishing telephone services, the rates of which have been established by a public

utility commission. Corporation X is also engaged in a separate nonutility trade or business. During 1963 corporation X acquires and places in service two new section 38 properties, each with a basis of \$30,000 and an estimated useful life of 7 years. One of these properties is used exclusively in the utility activity. The other property is also used at times in the utility activity, but is used in the separate nonutility trade or business more than 50 percent of the time during the taxable year 1963. Corporation X's qualified investment is \$28,571 which includes \$20,000 attributable to nonutility property (\$30,000 basis times applicable percentage, 66⅔ percent) plus \$8,571 attributable to public utility property (three-sevenths times (\$30,000 basis times applicable percentage, 66⅔ percent)).

Certain replacement property

Paragraph (4) of section 46(c) is a new provision added by your committee. This new paragraph provides that, for purposes of section 46(c), if section 38 property is placed in service by the taxpayer to replace property which was destroyed or damaged by fire, storm, shipwreck, or other casualty, or was stolen, the basis (or cost in the case of used property) of such section 38 property which (but for this paragraph) would be taken into account under section 46(c)(1) as qualified investment, shall be reduced by an amount equal to the amount received by the taxpayer as compensation, or otherwise, for such property so destroyed, etc., or by an amount equal to the adjusted basis of such property so destroyed, etc., whichever is the lesser. However, the above rule shall not apply in any case in which the reduction in qualified investment attributable to the substitution required by section 47(a)(1) with respect to the property so destroyed, damaged, or stolen (determined without regard to section 47(a)(4)), is greater than the reduction in basis (or cost) described in the preceding sentence. In order to constitute replacement property, the newly acquired section 38 property need not be placed in service within the same taxable year of the destruction, etc., of the replaced property.

The provisions of paragraph (4) of section 46(c) may be illustrated by the following examples:

Example 1.—On January 1, 1964, corporation X acquires and places in service a new section 38 asset with a basis of \$30,000 and a useful life of 6 years. The qualified investment with respect to such asset is \$20,000 (\$30,000 basis $\times$ 66⅔ percent, applicable percentage). On January 1, 1965, such asset is destroyed by fire. X receives \$23,000 in insurance proceeds as compensation for the destroyed property and on December 15, 1965, purchases for \$35,000 an asset to replace the asset that was destroyed. The adjusted basis of the destroyed asset on January 1, 1965 is \$24,500. The basis of the replacement asset must be reduced for purposes of the new subpart B by \$23,000, since that sum is less than the adjusted basis of the destroyed property on January 1, 1965 (\$24,500), and is greater than the reduction in qualified investment (\$20,000) which would have been required had section 47(a)(1) been applicable. Since section 46(c)(4) applies, section 47(a)(1) does not apply. (See sec. 47(a)(4).)

Example 2.—Assume the same facts as in example 1, except that the insurance proceeds are \$17,000. In such case, no reduction in the basis of the replacement asset is required since the reduction in qualified investment under section 47(a)(1) (\$20,000) is greater than the reduction in basis (\$17,000) which would have been required under

section 46(c)(4). Since section 46(c)(4) is not applicable, the credit attributable to the asset replaced will be recomputed by applying section 47(a)(1).

(d) *Limitations with respect to certain persons.*—Subsection (d) of section 46 limits the applicability of the credit with respect to certain persons. Paragraph (1) of section 46(d) provides that both the qualified investment and the \$25,000 amount specified under subparagraphs (A) and (B) of section 46(a)(2) are to be equal to a ratable share of such items in the case of the following organizations:

(1) mutual savings banks, cooperative banks, and domestic building and loan associations, to which section 593 applies;

(2) regulated investment companies and real estate investment trusts subject to tax under subchapter M; and

(3) cooperative organizations described in section 1381(a).

Under paragraph (2)(A) of section 46(d), in the case of a mutual savings bank, etc., its ratable share of the qualified investment and the \$25,000 amount specified in subparagraphs (A) and (B) of section 46(a)(2) is equal to 50 percent of such items.

Under paragraph (2)(B) of section 46(d), in the case of a regulated investment company or a real estate investment trust, the qualified investment and the \$25,000 amount specified in subparagraphs (A) and (B) of section 46(a)(2) are to be taken into account in the same proportion as its taxable income (as defined in sec. 852(b)(2) or sec. 857(b)(2), respectively) bears to such taxable income computed without regard to the deduction for dividends paid (as defined in sec. 852(b)(2)(D) or 857(b)(2)(C), respectively).

Under paragraph (2)(C) of section 46(d), a cooperative organization described in section 1381(a) is to take into account its qualified investment and the \$25,000 amount specified in subparagraphs (A) and (B) of section 46(a)(2) in the same proportion as its taxable income bears to its taxable income increased by amounts to which section 1382 (b) or (c) applies and similar amounts the tax treatment of which is determined without regard to subchapter T (sec. 1381 and following). Thus, in the case of a taxable year of a cooperative organization beginning before January 1, 1963, the denominator of the proportion for such organization is determined by adding to its taxable income any patronage dividends which are excluded or deducted and any nonpatronage distributions which are deducted under section 522(b)(1). In the case of any taxable year of the organization beginning after December 31, 1962, the denominator is determined by adding to taxable income (in addition to amounts to which sec. 1382 (b) or (c) applies) any amounts of the type described in the preceding sentence which are excluded or deducted without regard to section 1382 (b) or (c) because they are attributable to patronage occurring before 1963.

If any of these special taxpayers to which section 46(d) applies are members of an affiliated group as defined in section 46(a)(5), the \$25,000 amount specified in subparagraphs (A) and (B) of section 46(a)(2) is to be reduced in accordance with section 46(a)(5) before determining the ratable share of such item under section 46(d).

The provisions of section 46(d) may be illustrated by the following example:

The total qualified investment of a regulated investment company is \$150,000, and its investment company taxable income is \$50,000

after taking into account the deduction for dividends paid provided by section 852(b)(2)(D), and \$1 million without regard to such deduction. Such organization's qualified investment would be \$7,500 $\left(\$150,000 \times \frac{\$50,000}{\$1,000,000} \right)$. Similarly, the \$25,000 amount specified in subparagraphs (A) and (B) of section 46(a)(2) would be reduced to \$1,250 $\left(\$25,000 \times \frac{\$50,000}{\$1,000,000} \right)$, and the 25-percent limitation of section 46(a)(2)(B) would apply to the tax liability in excess of \$1,250.

SECTION 47. CERTAIN DISPOSITIONS, ETC., OF SECTION 38 PROPERTY

(a) *In general.*—Section 47 provides, in general, for an adjustment of prior credits (including credit carrybacks and carryovers) and an increase in the tax imposed by chapter 1 if property (1) is disposed of or otherwise ceases to be section 38 property with respect to the taxpayer before the close of the useful life which was taken into account with respect to such property in computing the credit, or (2) becomes public utility property. Subsection (a) of section 47 provides that adjustments due to the application of section 47 and increases in tax resulting from such adjustments are to be determined under regulations prescribed by the Secretary of the Treasury or his delegate.

Early disposition, etc.

Under paragraph (1) of section 47(a), the tax for a taxable year in which property is disposed of or otherwise ceases to be section 38 property before the close of the useful life which was taken into account in computing the credit is to be increased by the amount by which the credits allowed under section 38 for all prior taxable years would have been decreased by reason of adjustments of the credits for such taxable years. Such adjustment is to be made by recomputing qualified investment for the year in which the basis (or cost) of the property that ceases to be section 38 property was included in qualified investment and by recomputing the credit (and credit carrybacks and carryovers) accordingly. Qualified investment is to be recomputed by substituting, in lieu of the estimated useful life of the property that was originally taken into account in applying the applicable percentage, the period beginning with the time such property was placed in service by the taxpayer and ending with the time such property ceased to be section 38 property. This period is hereinafter referred to as the actual period of use. In determining the amount of the aggregate decrease in the credits allowed for all prior taxable years, due regard is to be accorded any previous recomputations of qualified investment, credits, and credit carrybacks and carryovers resulting from a prior application of section 47. Of course, if the actual period of use would have no effect on the appropriate applicable percentage to be applied, no adjustment is necessary. Thus, for example, if the estimated useful life is 10 years, and a disposition occurs resulting in an actual period of use of 8 years, no adjustment results, since the applicable percentage remains 100 percent in either case.

Except as provided in section 47(b), whenever section 38 property is disposed of, such property ceases to be section 38 property with respect to the taxpayer. In general, property will be considered dis-

posed of whenever it is sold, exchanged, transferred, distributed, involuntarily converted, or disposed of by gift. Thus, a cessation will occur when property is contributed to a partnership or to a corporation. (However, see sec. 47(b) for an exception where the contribution of property constitutes a mere change in the form of operating the trade or business.) Generally, the lease of property is not considered to be a disposition for purposes of applying section 47. However, if a taxpayer leases out property which he would ordinarily dispose of by sale or exchange and it appears that a purpose of the lease is to avoid the application of section 47, then such lease will be considered a disposition.

Additional examples of property ceasing to be section 38 property include (1) property (or a portion thereof) which is no longer subject to depreciation with respect to the taxpayer because, for example, it is shifted from a business to a personal use, and (2) property which is used in any taxable year predominantly outside the United States, by a governmental unit, etc. Similarly, property of a partnership (or subch. S corporation or estate or trust) ceases to be section 38 property with respect to the taxpayer (partner, shareholder, or beneficiary) when such taxpayer sells his interest in the partnership (or shares of stock or beneficial interest). Furthermore, when section 38 property is leased, and the lessor elects to treat the lessee as the purchaser of the property under section 48(d), a termination of the lease will result in the application of section 47 with respect to the lessee, unless the property does not cease to be section 38 property with respect to the lessee.

The provisions of section 47(a)(1) may be illustrated by the following example:

Corporation X acquires and places in service a new section 38 asset on January 1, 1963. Such asset has a basis of \$30,000 (determined without regard to sec. 48(g)) and an estimated useful life of 8 years. Assuming this is the only section 38 asset corporation X places in service during its taxable year ending December 31, 1963, X's qualified investment is \$30,000 (\$30,000 basis times applicable percentage, 100 percent). Such investment entitles X to a credit of \$2,100 (7 percent times \$30,000). Corporation X's liability for tax for 1963 is \$100,000, and X reduces its tax liability by the full \$2,100. On January 1, 1968, corporation X sells such asset. There will be added to the taxes imposed by chapter 1 for X's taxable year ended December 31, 1968, \$1,400 which is the aggregate decrease in credits allowed resulting solely from substituting a 5-year life for such asset in computing qualified investment in 1963. The sum of \$1,400 is arrived at by first applying an applicable percentage of $33\frac{1}{3}$ percent to the basis, resulting in an adjusted qualified investment of \$10,000 (\$30,000 basis times $33\frac{1}{3}$ percent, the applicable percentage based on the actual period of use of 5 years). Since the recomputed qualified investment results in an adjusted credit of \$700 (7 percent times \$10,000), the aggregate decrease in credits is \$1,400 (\$2,100 credit allowed minus \$700 adjusted credit).

Property becomes public utility property

Section 47(a)(2) provides that the credit is to be adjusted if during any taxable year any property previously taken into account in determining qualified investment as nonutility property becomes

public utility property. Property becomes public utility property if in any 1 taxable year the property is used predominantly in a trade or business described in section 46(c)(3)(B) by the taxpayer or by a person leasing such property from the taxpayer. Once such property becomes public utility property in the hands of the taxpayer, the fact that in any subsequent year such property is used by such taxpayer predominantly in a nonutility activity is to be disregarded. (See sec. 46(c)(3)(B) for the definition of public utility property.)

In such a case, the tax liability for the taxable year in which the property becomes public utility property is to be increased by the amount that the credits allowed under section 38 for all prior taxable years is decreased by the adjustment. The adjustment is to be made by treating the property as public utility property beginning with the year the property was placed in service, but with due regard to the use of the property as nonutility property before such change in use. For purposes of the adjustment, it is assumed that the property will continue to be used as section 38 public utility property for the estimated useful life of the property which was taken into account in computing the credit in the year the property was placed in service.

If property becomes public utility property before the close of the useful life which was taken into account in computing the credit under section 38, the proper applicable percentage to be used in recomputing qualified investment is determined by adding (1) the applicable percentage (either 0, 33 $\frac{1}{3}$, or 66 $\frac{2}{3}$ percent) earned by the property as nonpublic utility property prior to the change in use, and (2) three-sevenths times the difference between the applicable percentage originally taken into account in computing the credit in the year the taxpayer placed the property in service and the applicable percentage determined in (1). Thus, if property with an original estimated useful life of 10 years is used predominantly as public utility property after use as nonutility property for 5 years, the applicable percentage to be used in recomputing qualified investment is 61.9 percent. This percentage is arrived at by adding 33 $\frac{1}{3}$ percent (the applicable percentage earned by the property as nonpublic utility property) plus three-sevenths of 66 $\frac{2}{3}$ percent (100 percent original applicable percentage, less 33 $\frac{1}{3}$ percent, applicable percentage earned as nonutility property).

If property becomes public utility property and section 47(a)(2) applies, and if such property is subsequently disposed of or used in a manner causing section 47(a)(1) to apply, proper adjustment for the fact that section 47(a)(2) has previously applied is to be made in applying section 47(a)(1).

Carrybacks and carryovers adjusted

Section 47(a)(3) provides that carrybacks and carryovers of unused credits under section 46(b) are to be adjusted by reason of a disposition or other cessation described in section 47(a)(1), or by reason of a change in use described in section 47(a)(2). Thus, even if the recomputation of qualified investment required by section 47(a)(1) does not result in a decrease in the credits allowed, credit carrybacks and carryovers are to be adjusted.

The provisions of section 47(a)(3) may be illustrated by the following example:

In 1963, corporation X, a new taxpayer, acquired and placed in service a number of section 38 assets. One of these was asset A which

has a basis of \$300,000 and an estimated useful life of 8 years. X's qualified investment and liability for tax for such year were \$2,300,000 and \$525,000 respectively. In 1963, X's tentative credit was \$161,000 (7 percent times \$2,300,000), but because of the limitation contained in section 46(a)(2) the credit allowed for such year was \$150,000 (\$25,000 plus 25 percent of \$500,000). Therefore, an \$11,000 credit carryover was available for 1964 and succeeding years. On January 1, 1970, X trades in asset A in exchange for a new asset. Under these facts, corporation X must adjust its credit for 1963 by recomputing the qualified investment attributable to asset A. The original qualified investment with respect to asset A was \$300,000 (\$300,000 basis times applicable percentage, 100 percent); the recomputed qualified investment is \$200,000 (\$300,000 basis times applicable percentage, 66⅔ percent based on the actual period of use of asset A). Therefore, the total recomputed qualified investment is \$2,200,000 (\$2,300,000 minus \$100,000). In this case, the adjustment of the credit for 1963 will not affect the credit allowed in 1963 but will reduce the credit allowable as a carryover to 1964 and succeeding years. This is because in recomputing the credit, X's credit is reduced to \$154,000 (7 percent times \$2,200,000). Since X's adjusted credit is still in excess of the limitation of \$150,000 for 1963, there is no decrease in credits allowed in 1963, and hence no increase in X's liability for tax for 1970 attributable to credits allowed in 1963. Thus, only the \$11,000 unused credit carryover from 1963 is affected by the recomputation. Such carryover as adjusted is \$4,000 (\$154,000 adjusted credit for 1963 minus \$150,000 credit used in 1963). To the extent more than \$4,000 of the original carryover from 1963 has been used by the taxpayer as a credit against tax for 1964 or any succeeding year, such credits shall be adjusted and the decrease attributable thereto will be added to X's 1970 tax.

Property destroyed by casualty, etc.

Paragraph (4) of section 47(a) was added to the bill by your committee. Paragraph (4) provides an exception to section 47(a)(1). If (1) any property is disposed of, or otherwise ceases to be section 38 property with respect to the taxpayer, on account of its destruction or damage by fire, storm, shipwreck, or other casualty, or by reason of its theft, and (2) section 38 property is placed in service by the taxpayer to replace the property described in (1), and (3) the reduction in basis (or cost) of the replacement property resulting from the application of the first sentence of section 46(c)(4) is greater than the reduction in qualified investment which (but for this paragraph) would be made by reason of the substitution required by section 47(a)(1) with respect to the destroyed, etc., property, then, no increase in tax shall be made under section 47(a)(1) and no adjustment in unused credit carryovers will be made under section 47(a)(3). (See the discussion of sec. 46(c)(4) in this report for examples which illustrate the application of this provision.)

(b) *Section not to apply in certain cases.*—Subsection (b) of section 47 provides additional exceptions to the adjustments required by section 47(a).

The first exception provides that section 47(a) will have no application to the transfer of property which arises by reason of an individual taxpayer's death. Thus, on the death of an individual tax-

payer, the transfer of the decedent's property interests to his personal representative or heirs will be disregarded. Nor will section 47(a) apply to the transfer of a deceased taxpayer's interest held in joint tenancy (either as a joint tenant, or a tenant by the entirety) to the surviving owners of the property. The effect of this provision is that all properties held by a decedent at the time of his death for which the credit has been granted will be deemed held by the decedent for the useful life estimated by the decedent in computing his credits.

Another exception provided by subsection (b) of section 47 is that section 47(a) will not apply to the transfer of property to the acquiring corporation in a transaction to which section 381(a) applies. (See sec. 381(c)(23) for the treatment to be accorded the acquiring corporation with respect to the credits of the acquired corporation, including the sec. 47 adjustments with respect to dispositions by the acquiring corporation of property transferred by the acquired corporation.)

In addition, subsection (b) of section 47 provides, in effect, a suspension of the application of section 47(a) where there has been a mere change in the form of conducting a trade or business so long as (1) the property is retained in such trade or business as section 38 property, and (2) the taxpayer retains a substantial interest in such trade or business. On the occurrence of any event which results in a failure to meet either of the conditions described above, the property will be deemed to cease to be section 38 property when such event occurs. Thus, in determining whether the property ceases to be section 38 property before the close of its estimated useful life, the period the property was held as section 38 property before the mere change in form of conducting the trade or business will be tacked on to the period beginning with the change in form and ending with the occurrence of the event which results in a failure to meet either of the conditions specified in the first sentence of this paragraph.

The phrase "a mere change in the form of conducting the trade or business" (whether through incorporation, the formation of a partnership, or otherwise) applies only to cases where the properties of a trade or business are transferred. Thus, the transfer of section 38 assets to a newly formed corporation in a transaction to which section 351 applies will not fall within the scope of the exception unless the transaction involves the transfer of the trade or business in which such assets were used.

The determination of whether the taxpayer has retained a substantial interest in the trade or business is to be made immediately after the change in form of conducting the business, as well as after each time the taxpayer disposes of a portion of his interest in the new enterprise. However, in any case where a taxpayer's interest in the business of the new enterprise remains constant in relation to his former interest, the taxpayer will be considered as having retained a substantial interest in the trade or business. Thus, where a taxpayer owns a 5-percent interest in a partnership, and after the incorporation of that partnership the taxpayer retains a 5-percent interest in the corporation, the taxpayer will be considered as having retained a substantial interest in the trade or business as of the date of the change in form.

The provisions of section 47(b) may be illustrated by the following examples:

Example 1.—On July 1, 1962, the XYZ partnership acquires and places in service asset A, a new section 38 asset, with a basis of \$30,000

and an estimated useful life of 8 years. One-third of the basis of such asset is taken into account by each of the three partners of the XYZ partnership in computing their individual credits. On January 1, 1964, the XYZ partnership transfers all of its assets to the XYZ corporation, a newly formed corporation, in exchange for all of the stock of XYZ corporation. Such stock is then transferred pro rata to the partners. The XYZ corporation continues to operate the same trade or business formerly conducted as a partnership. On September 1, 1970, the XYZ corporation sells asset A. Assuming all the partners have continuously retained a substantial interest in the XYZ corporation and asset A was used in the business as a section 38 asset until September 1, 1970, no adjustment is required under section 47 since the total holding period of asset A for each partner exceeds 8 years (18 months while used by the XYZ partnership and 80 months while used by the XYZ corporation or a total of 8 years and 2 months).

Example 2.—On January 1, 1963, the X corporation acquires and places in service a new section 38 property (with an estimated useful life of 6 years) which it takes into account in computing a credit. Such property is used in X's manufacturing business. X corporation is also engaged in a separate personal service business. In 1964, the X corporation transfers the assets of the manufacturing business (including the sec. 38 property upon which the X corporation took a credit) to a newly formed corporation, the Y corporation. X corporation then transfers to its shareholders all of the stock of the Y corporation. Since the X corporation does not retain a substantial interest in the manufacturing business, section 47(a) will apply to the transfer of the assets to Y corporation.

(c) *Special rule.*—Subsection (c) of section 47 provides a special rule for treating the increase in tax resulting from the adjustment of the credit. In general, such increase in tax will be treated as a tax imposed by chapter 1. However, it will not be so treated for purposes of determining the amount of the credits under section 33 (relating to tax of foreign countries and possessions of the United States), section 34 (relating to dividends received by individuals), section 35 (relating to partially tax-exempt interest received by individuals), section 37 (relating to retirement income), and section 38 (relating to investment in certain depreciable property). Thus, the increase in tax is not to be taken into account in determining a taxpayer's liability for tax as defined in section 46(a)(3), and hence will have no effect on the limitation contained in section 46(a)(2). However, all adjustments to credit carryovers to the current taxable year resulting from a cessation or change in use during such taxable year are to be taken into account in determining the amount of credit carryovers which may be used for such year.

SECTION 48. DEFINITIONS; SPECIAL RULES

(a) *Section 38 property.*—Section 48 contains various definitions and special rules necessary to the application of the investment credit. Section 48(a) defines the type of property investment which will qualify for the credit.

In general

The term "section 38 property" is defined by section 48(a)(1) as property which is tangible personal property, or which is other tangible property (not including a building and its structural com-

ponents) but only if such other property is used as an integral part of manufacturing, production, or extraction, or of furnishing transportation, communications, electrical energy, gas, water, or sewage disposal services, or is a research or storage facility used in connection with any of the foregoing activities. The property described above, however, must be property with respect to which depreciation (or amortization in lieu of depreciation) is allowable, and such property must have a useful life of 4 years or more (determined as of the time such property is placed in service). (See the discussion of useful life in this report under sec. 46(c), relating to qualified investment.)

If an asset is in part subject to an allowance for depreciation and in part nondepreciable, only the proportionate part of the asset which is subject to depreciation will qualify as section 38 property. Thus, if an asset is used 80 percent of the time in a trade or business and is used 20 percent of the time for personal purposes, only 80 percent of such property will qualify as section 38 property subject to depreciation. Further, property does not qualify to the extent it is treated as property which is used for personal, living, and family purposes under section 274 (relating to disallowance of certain entertainment, etc., expenses).

Property may qualify as section 38 property if amortization is allowable with respect to such property in lieu of depreciation. Amortization in lieu of depreciation is allowable, for example, if a lessee makes improvements on leased property which have a longer estimated useful life than the remaining term of the lease and amortizes the cost of such improvements over the remaining term of the lease.

Tangible personal property may qualify as section 38 property irrespective of whether it is used as an integral part of manufacturing, production, or extraction or of the furnishing of transportation, communications, electrical energy, gas, water, or sewage disposal services. Local law definitions will not be controlling for purposes of determining the meaning of the term "tangible personal property." For purposes of section 48, the term "tangible personal property" includes any tangible property except land, and improvements thereto, such as buildings or other inherently permanent structures thereon (including items which are structural components of such buildings or structures). Assets accessory to the operation of a business, such as machinery, printing presses, transportation or office equipment, refrigerators, individual air-conditioning units, grocery counters, testing equipment, display racks and shelves, etc., generally constitute tangible personal property for purposes of section 48, even though such assets may be termed fixtures under local law. Further, assets in the nature of machinery will be considered "tangible personal property" for purposes of section 48 whether they are placed within or without a building or other structure. Thus, for example, a gasoline pump, or a hydraulic car lift, although not within any structure, will nevertheless be considered "tangible personal property." Intangible property, such as patents and copyrights, does not qualify as section 38 property.

Buildings and structural components thereof are not eligible for the credit. The term "building" is to be given its commonly accepted meaning, that is, a structure or edifice enclosing a space within its walls, and usually covered by a roof. It is the basic structure of an improvement to land the purpose of which is, for example, to provide shelter or housing or to provide working, office, display, or sales space.

The term would include, for example, the basic structure used as a factory, office building, warehouse, theater, railway or bus station, gymnasium, or clubhouse. The term "structural components" of a building includes such parts of the building as central air-conditioning and heating systems, plumbing, and electric wiring and lighting fixtures, relating to the operation and maintenance of the building.

In addition to tangible personal property, other tangible property (not including a building and its structural components) used as an integral part of the manufacturing, production, or extraction process or as an integral part of a system of furnishing transportation, communications, electrical energy, gas, water, or sewage disposal services may qualify for the credit. Property is to be considered as being used as an integral part of a system of furnishing transportation, communications, electrical energy, gas, water, or sewage disposal services only if such property is used by one engaged in the trade or business of furnishing such services. Thus, if a manufacturing firm constructs an airstrip for use by airplanes operated for the convenience of its officers and employees, such airstrip would not qualify as section 38 property since the manufacturing firm is not engaged in the transportation business.

The terms "manufacturing," "production," "extraction," and the businesses of furnishing "transportation," "communications," "electrical energy," "gas," "water," or "sewage disposal" services are to be given their commonly accepted meaning. Thus, for example, manufacturing or production includes the construction, reconstruction, or making of property from or with scrap, salvage, or junk material, as well as from new or raw material, (1) by processing, manipulating, refining, or changing the form of an article, or (2) by combining or assembling two or more articles, and includes the cultivation of the soil and the raising of livestock and other farm produce. Section 38 property would include, for example, property used as an integral part of the extraction, processing, refining, and fabrication of minerals or mineral products; the growing, raising, processing, and packing or packaging of foodstuffs; the operation of sawmills and the production of lumber and lumber products and other building materials; and the manufacture, treatment, and packaging of textiles, paper, leather goods, glass, etc. Examples of transportation businesses would be railroads and airlines. Examples of communications businesses would include businesses furnishing telephone and telegraph services or radio or television broadcasting stations.

In order to qualify for the credit, property (other than tangible personal property and research or storage facilities used in connection with the specified activities) must be used as an integral part of one or more of the specified activities. Thus, for example, section 38 property would ordinarily not include such assets as pavements, parking areas, advertising displays, outdoor lighting facilities, or swimming pools which, although used as a part of the overall business operation, are not used directly in the specified activities. Specific examples of qualifying property which normally would be used as an integral part of one of the specified activities are blast furnaces, oil and gas pipelines, and railroad tracks and signals. Fences will qualify as section 38 property where used as an integral part of a specified activity as, for example, where used in connection with the raising of livestock.

Research or storage facilities (other than buildings) are eligible for the credit if used in connection with any of the specified activities, although such property is not an integral part of the activity. Examples of such facilities include wind tunnels and test stands.

Property used outside the United States

Subparagraph (A) of section 48(a)(2) provides that, subject to certain exceptions contained in subparagraph (B) of that section, the term "section 38 property" does not include property used predominantly outside the United States (as defined in sec. 7701(a)(9)). The term "predominantly outside the United States" means that the property must be physically located outside the United States more than 50 percent of the time during any one taxable year. Thus, if property is originally placed in service in the United States and a credit is received on such property, but such property is thereafter in any one year used predominantly outside the United States, such property ceases to be section 38 property with respect to the taxpayer who obtained the credit, regardless of the fact that the property is later returned to the United States. Furthermore, if property is originally placed in service by the taxpayer outside the United States and is used predominantly outside the United States during the taxable year originally placed in service, such property cannot qualify as section 38 property with respect to such taxpayer.

Subparagraph (B)(i) of section 48(a)(2) provides that any aircraft which is registered by the Administrator of the Federal Aviation Agency and which is operated, whether on a scheduled or nonscheduled basis, to and from the United States may be section 38 property even though it is used predominantly outside the United States. The term "to and from" the United States is not intended to exclude an aircraft which makes flights from one point in a foreign country to another such point, as long as such aircraft returns to the United States with some degree of frequency.

Subparagraph (B)(ii) provides that rolling stock of a domestic railroad corporation subject to part I of the Interstate Commerce Act which is used within and without the United States does not lose its eligibility for the credit even though it is used predominantly outside the United States. For the purposes of subparagraph (B)(ii) the term "rolling stock" means locomotives, freight and passenger train cars, floating equipment, and miscellaneous transportation equipment on wheels, the expenditures for which are chargeable to the equipment investment accounts in the uniform system of accounts for railroad companies prescribed by the Interstate Commerce Commission.

Subparagraph (B)(iii) provides that any vessel which is documented under the laws of the United States and which is operated in the foreign or domestic commerce of the United States may qualify as section 38 property.

Subparagraph (B)(iv) provides that any motor vehicle of a U.S. person (as defined in sec. 7701(a)(30)) which is operated to and from the United States with some degree of frequency may be section 38 property even though predominantly used outside the United States.

Subparagraph (B)(v) provides that any container of a U.S. person which is used in the transportation of property to and from the United States may be section 38 property even though used predominantly outside the United States.

Subparagraph (B)(vi) provides that property (other than vessels or aircraft) of a U.S. person which is used for the purposes of exploring for, developing, removing, or transporting resources from the outer Continental Shelf of the United States (within the meaning of sec. 2 of the Outer Continental Shelf Lands Act, as amended and supplemented; 43 U.S.C., sec. 1331) may be section 38 property. Thus, for example, the credit may be allowed for offshore drilling equipment.

Property used for lodging

The first sentence of paragraph (3) of section 48(a) provides that the term "section 38 property" does not include property which is used predominantly to furnish lodging or is used predominantly in connection with the furnishing of lodging. Thus, if property is used predominantly to furnish lodging in the year it is placed in service, it does not qualify as section 38 property. If property on which a credit has been allowed is used predominantly to furnish lodging in any subsequent year, such property will cease to be section 38 property. Property which is generally considered to be used to furnish lodging includes beds and other furniture and fixtures used in the accommodations for lodging.

The second sentence of section 48(a)(3) provides two exceptions to the rule excluding from the credit property used for lodging or in connection with the furnishing of lodging. Subparagraph (A) of such second sentence provides that nonlodging commercial facilities which are available to persons not using the lodging facilities on the same basis that they are available to persons using the lodging facilities may qualify for the credit. For example, tangible personal property used in a restaurant or pharmacy may qualify as section 38 property notwithstanding the fact that the restaurant or pharmacy is operated in connection with lodging facilities such as an apartment house. However, the furniture and fixtures, rugs, draperies, etc., used, for example, in the lobby of an apartment house would be excluded since they are furnished in connection with the furnishing of lodging and since the lobby of an apartment house is not a nonlodging commercial facility.

Subparagraph (B) of the second sentence of section 48(a)(3) provides that property used by a hotel or motel in connection with the trade or business of furnishing lodging may qualify for the credit where the predominant portion of the accommodations is used by transients. Thus, if more than half of the rooms used to accommodate guests of a hotel or motel are normally used on a transient basis, the property used in such hotel or motel may qualify for the credit even though it is used in connection with furnishing lodging. Conversely, if less than half of the accommodations are normally used on a transient basis, none of the property used in the hotel or motel may qualify for the credit except for property used in connection with a nonlodging commercial facility.

Property used by tax-exempt organizations

Paragraph (4) of section 48(a) provides that property used by an organization (other than a cooperative described in sec. 521) which is exempt from the tax imposed by chapter 1 of the code shall be treated as section 38 property only if such property is used predominantly in an unrelated trade or business the income of which is subject to tax under section 511. The term "property used by" an

organization exempt from tax includes property leased to such an organization, as well as property leased by such an organization to another person. Thus, if property does not qualify under section 48(a)(4) because it is leased to an organization exempt from tax, no credit is allowable to the lessor with respect to such property.

Property used by governmental units

Paragraph (5) of section 48(a) also excludes from the term "section 38 property" property used by the United States, any State (as defined in sec. 7701(a)(10) of the code) or political subdivision thereof, any international organization (as defined in sec. 7701(a)(18) of the code), or any agency or instrumentality of any of the foregoing.

Livestock

Paragraph (6) of section 48(a) which was added by your committee provides that livestock will not be treated as section 38 property. The term "livestock" includes horses, cattle, poultry, and fur-bearing animals, irrespective of the use to which they are put or the purpose for which they are held.

(b) *New section 38 property.*—Subsection (b) of section 48 provides that, for purposes of the credit, "new section 38 property" means only section 38 property, the construction, reconstruction, or erection of which is completed by the taxpayer after June 30, 1962, or acquired by the taxpayer after that date, provided the original use of such property commences with the taxpayer and commences after such date. In the case of property constructed, reconstructed, or erected by the taxpayer, there is to be taken into account in determining the basis of such property only that portion of the basis which is properly attributable to construction, reconstruction, or erection after June 30, 1962. The principles applicable under section 167(c) of the code are to be applied under section 48(b) in determining, for example, when the property is acquired by the taxpayer, whether the original use of the property commences with the taxpayer, and the portion of the basis of property completed after June 30, 1962, which is attributable to construction, reconstruction, or erection after that date.

(c) *Used section 38 property.*—Paragraph (1) of section 48(c) defines the term "used section 38 property" as section 38 property acquired by purchase after June 30, 1962, which is not new section 38 property.

Used section 38 property does not include property which, after its acquisition by the taxpayer, is used by a person who used such property before such acquisition. This rule also applies where the property after acquisition by the taxpayer is used by a person who is related to a person who used the property before acquisition. Such person will be considered as related if the relationship is one described in section 179(d)(2) (A) or (B) (as, for example, where the parties are members of an affiliated group, as defined in sec. 48(c)(3)(C)). Thus, if property were sold under a sale and leaseback arrangement, such property in the hands of the purchaser-lessor would not be used section 38 property since the property, after its acquisition, is being used by the same person who used it before the acquisition. Similarly, where a taxpayer has been leasing property, and subsequently purchases such property (whether or not the lease contained a purchase option feature), such property is not used section 38 property with respect to such taxpayer, since it is being used by the person who used

such property before its acquisition. In addition, if property owned by a lessor is sold subject to a lease or is sold upon the termination of a lease, the property will not qualify as used section 38 property with respect to the purchaser, if thereafter the property is used by a lessee who used the property before the acquisition. For purposes of applying the rule contained in section 48(c)(1), property will be considered used by a person only if a substantial use is made. Thus, property would not be disqualified as used section 38 property merely because a person using the property after acquisition had also made some casual use of it before acquisition.

Dollar limitation

Under subparagraph (A) of section 48(c)(2), the cost of used section 38 property which may be taken into account under section 46(c)(1)(B) in computing qualified investment for any taxable year is not to exceed \$50,000. If the total cost of used section 38 property placed in service during the taxable year exceeds \$50,000, the taxpayer must select the particular assets he wishes to be taken into account in computing qualified investment (but not to exceed an aggregate cost of \$50,000). The selection of the specific assets to be taken into account is to be made at the time and in the manner prescribed by regulations. Such selection may be changed only in the manner and to the extent provided by the regulations. Thus, if a taxpayer has a cost of used section 38 property of \$25,000 acquired in connection with the operation of a sole proprietorship, \$30,000 allocated to him from a subchapter S corporation, and \$20,000 which is his share of the cost of used section 38 property acquired by a partnership of which he is a member, he may select from the total of \$75,000 the particular assets which he wishes to take into account for purposes of computing qualified investment. If the assets selected all have useful lives of between 4 and 6 years, the maximum qualified investment in used section 38 property will be \$16,667. If the assets selected all have useful lives in excess of 8 years, qualified investment in used section 38 property would be \$50,000.

Subparagraph (B) of section 48(c)(2) provides that in the case of a husband or wife filing a separate return, the cost of used section 38 property that may be taken into account is not to exceed \$25,000. If this subparagraph applies, and such cost exceeds \$25,000, the husband or wife may select, under regulations prescribed by the Secretary of the Treasury or his delegate, the assets to be taken into account, but only to the extent of an aggregate cost of \$25,000. Subparagraph (B) shall apply, however, only if the spouse of the taxpayer has purchased (or has been allocated) used section 38 property which may be taken into account in qualified investment for the taxable year of such spouse which ends within or with the taxpayer's taxable year. Thus, if both husband and wife have purchased (or have been allocated) any used section 38 assets for the taxable year (as described above) and they file separate returns, the maximum cost of used section 38 property which may be taken into account by each is \$25,000; but if only one spouse has purchased (or has been allocated) any used section 38 assets, such spouse may take into account \$50,000 of the cost of used section 38 property.

Subparagraph (C) of section 48(c)(2) provides that in the case of an affiliated group, the \$50,000 limitation is to be reduced for each

member of the group by apportioning the \$50,000 limitation among the members of the affiliated group in accordance with their respective amounts of used section 38 property which may be taken into account. The phrase, "their respective amounts of used section 38 property which may be taken into account", has reference to the total cost of used section 38 property without regard to the \$50,000 limitation or the applicable percentages to be applied in computing qualified investment. An affiliated group is one defined in section 1504(a) except that the phrase "more than 50 percent" is to be substituted for the phrase "at least 80 percent" each place it appears in section 1504 (a), and all corporations are to be treated as includible corporations. Thus, even if a corporation is excluded under section 1504(b) from being a member of an affiliated group for purposes of filing a consolidated return, it nevertheless will be treated as an includible corporation for purposes of section 48(c).

Subparagraph (D) of section 48(c)(2) provides that, in the case of partnerships, the limitation on the amount of used section 38 property which may be taken into account is to apply both with respect to the partnership and with respect to each partner. Thus, a partnership will be limited to used section 38 property having a cost of \$50,000 regardless of the number of partners.

If the aggregate cost of used section 38 property purchased by the partnership during a taxable year exceeds \$50,000, the partnership, under regulations prescribed by the Secretary of the Treasury or his delegate, is to select the properties, the cost of which is to be taken into account by the partners. Each partner will then combine his share of the cost of the used section 38 property selected by the partnership with the cost of any other used section 38 property to which he may be entitled. This combined amount may not exceed \$50,000 (or \$25,000 in the case of certain married individuals under section 48(c)(2)(B)). If such amount exceeds \$50,000, the taxpayer will then select the properties to which the applicable percentages are to be applied in computing his qualified investment.

Definitions

Subparagraph (A) of section 48(c)(3) provides that the principles of section 179(d)(2) of the code are to be applied in determining whether the property has been acquired by purchase. Thus, for example, used section 38 property is not acquired by purchase if it is acquired from a person whose relationship to the person acquiring it would result in the disallowance of a loss under section 267 or 707(b) (except that in applying sec. 267 (b) and (c), the family of an individual includes only his spouse, ancestors, and lineal descendants, and not his brothers and sisters). Furthermore, the term "purchase" does not include the acquisition of property by one member of an affiliated group (as defined in sec. 48(c)(3)(C)) from another member of the same affiliated group, or the acquisition of property the basis of which is determined in whole or in part by reference to the adjusted basis in the hands of person from whom acquired, or under 1014(a) (relating to property acquired from a decedent).

Subparagraph (B) of section 48(c)(3) provides that the cost of used section 38 property does not include so much of the basis of such property as is determined by reference to the adjusted basis of other property held at any time by the person acquiring such property. Thus, for example, if the basis of used section 38 property acquired is

determined under section 1031 (relating to certain nontaxable exchanges), the preceding rule applies. In addition, if property is disposed of (other than by reason of its destruction or damage by fire, storm, shipwreck, or other casualty, or its theft) and used section 38 property which is similar or related in service or use is acquired as a replacement therefor (whether before or after the disposition), in a transaction to which the preceding rule does not apply, the cost of the used section 38 property acquired is the basis of such property, reduced by the adjusted basis of the property replaced. In such a case, if the basis of the replacement asset is \$2,000 and the adjusted basis of the replaced asset is \$1,200 at the time of its disposition, the cost of used section 38 property would be \$800. Notwithstanding the rules described in this paragraph, the cost of used section 38 property is not to be reduced by the adjusted basis of any property disposed of if by reason of section 47 the disposition of such property gives rise to an increase of tax or a reduction of unused credit carrybacks or carryovers. The cost of used section 38 property acquired as a replacement for property which is destroyed or damaged by fire, storm, shipwreck, or other casualty, or which is stolen, shall be determined under section 46(c)(4).

(d) *Certain leased property.*—Subsection (d) of section 48 provides that in certain cases where property is leased, the lessor may elect to treat the lessee as having acquired such property. This rule applies only with respect to property which is new section 38 property in the hands of the lessor. Thus, for example, the election may not be made with respect to property owned by an organization exempt from tax unless the property is used predominantly in an unrelated trade or business, the income of which is subject to tax under section 511.

In addition, the election may be made only with respect to the first lessee of such new section 38 property, and only if such property would constitute new section 38 property if such lessee had actually acquired the property. Thus, for example, the election cannot be made if the first lessee uses the property predominantly outside the United States.

Also, for purposes of determining whether such property would constitute new section 38 property if purchased by the lessee, the original use of the property will be deemed to commence with the first lessee if he is the first person to use such property for its intended function. Thus, the fact that the lessor may have, for example, tested, stored, or attempted to lease the property to other persons will not preclude the lessee from being deemed the original user as long as neither the lessor nor any other person has physically used the property for its intended function before its use by the lessee. Moreover, in determining whether the property qualifies as new section 38 property to the lessee and in determining the amount of his qualified investment with respect to such property, the estimated useful life of the property to the lessee will be deemed to be the estimated useful life in the hands of the lessor. The election is not available if the lessor is a person referred to in section 46(d); i.e., a mutual savings bank, cooperative bank, or domestic building and loan association to which section 593 applies; a regulated investment company or real estate investment trust subject to taxation under subchapter M; or a cooperative organization described in section 1381(a).

If the election is made, the lessee will be treated for all purposes of subpart B as though he had acquired the property. Thus, if the leased

property is disposed of by the lessee, or if it otherwise ceases to be section 38 property to him, such property will be subject to the provisions of section 47 applicable to such cessations. Also, if the first lessee of property is treated as having acquired such property, the lessor is thereafter precluded from obtaining a credit as to such property. The election under section 48(d) will be made at such time, in such manner, and subject to such conditions as may be provided in regulations prescribed by the Secretary of the Treasury or his delegate.

In any case in which the lessee is treated as having acquired the property, the lessee's investment is deemed to be equal to the fair market value of the property if such property is constructed by the lessor or by a corporation which controls or is controlled by the lessor within the meaning of section 368(c). In any other case the lessee's investment is the basis of the property in the hands of the lessor.

A new sentence has been added to the provisions of section 48(d) as contained in the House bill. This sentence provides that if a lessor makes the election under section 48(d) in respect of any property, then under regulations prescribed by the Secretary of the Treasury or his delegate, section 48(g) shall not apply with respect to such property, and the deductions otherwise allowable to the lessee for amounts paid to the lessor under the lease will be adjusted in a manner consistent with the provisions of section 48(g). Thus, rather than the lessor being required to reduce the basis of the property in respect of which he has elected to treat the lessee as a purchaser, the lessee will be required to reduce the amount of his deductions for rental payments (over a period of time, as provided by regulations) by an amount equal to the credit (determined without regard to the limitation contained in sec. 46(a)(2)).

If, because of a credit or unused credit, a lessee's rental deductions have been reduced, and such credit or unused credit is later reduced because of the application of section 47(a), then an adjustment to the lessee's rental deductions shall be made (in a manner consistent with sec. 48(g)(2) and under regulations prescribed by the Secretary of the Treasury or his delegate) to the extent of the prior diminution of rental deductions attributable to such credit or unused credit.

The provisions of section 48(d) may be illustrated by the following example:

X corporation is engaged in the business of manufacturing and leasing new and reconditioned equipment which in its hands has an estimated useful life of 8 years. After December 31, 1962, X corporation constructs machine No. 1, having a fair market value of \$15,000 and a cost of \$10,000, and reconditions machine No. 2 at a cost of \$5,000. Y corporation leases both machines from X immediately after their construction and reconditioning and before X has made any other use of such machines. As to machine No. 1, if X elects to treat the property as being acquired by Y, such machine will have a basis of \$15,000 in Y's hands, and an estimated useful life of 8 years, for purposes of determining qualified investment (assuming the property otherwise qualifies as new sec. 38 property in Y's hands). Y's rental deductions will be reduced (in the manner prescribed by regulations) by an aggregate amount equal to the credit attributable to such property, \$1,050 (7 percent times basis of \$15,000). The election is not available with respect to machine No. 2, since a reconditioned machine would not constitute new section 38 property if the lessee had purchased it. In such a case, while X corporation cannot make

the election to let the Y corporation take the credit, X corporation would be entitled to a credit based on its expenditure of \$5,000 as an investment in new section 38 property, the reconstruction of which is completed after December 31, 1962.

(e) *Subchapter S corporations.*—Subsection (e) of section 48 provides for the application of the credit in the case of an electing small business corporation under subchapter S. The qualified investment of the subchapter S corporation is allocated pro rata among the persons who are shareholders on the last day of the corporation's taxable year. The qualified investment is ascertained at the corporate level, and thus the aggregate cost of used section 38 property that may be allocated to the shareholders is limited to \$50,000. If the cost of used section 38 property purchased by the subchapter S corporation exceeds \$50,000 in any one taxable year, the corporation is to select, under regulations prescribed by the Secretary of the Treasury or his delegate, the properties the cost of which may be taken into account by its shareholders.

Any person to whom an investment is apportioned under subsection (e) of section 48 is to be treated as the taxpayer with respect to such investment, and such investment will not (by reason of such apportionment) lose its character in his hands as an investment in either new or used section 38 property. Thus, each shareholder will take into account, in determining his own qualified investment, his allocated share of the corporation's qualified investment in new section 38 property. He will also take into account his allocated share of the corporation's investment in used section 38 property. Of course, since only \$50,000 cost of used section 38 property may be taken into account, if a shareholder's combined cost of used section 38 property exceeds \$50,000, he must select the properties to be taken into account in computing his qualified investment.

If a shareholder includes in his qualified investment any portion of the basis or cost of property acquired by the subchapter S corporation and the corporation subsequently disposes of such property, or if the shareholder disposes of his stock in such corporation, the shareholder will be subject to the provisions of section 47 with respect to such property.

(f) *Estates and trusts.*—Subsection (f) of section 48 provides rules for applying the investment credit to estates and trusts. Paragraph (1) of section 48(f) provides that the qualified investment for any taxable year is to be apportioned between the estate or trust and the beneficiaries on the basis of the income of the estate or trust allocable to each. The qualified investment is ascertained at the trust or estate level, and thus the aggregate cost of used section 38 property that may be apportioned between the estate or trust and the beneficiaries is limited to \$50,000. If the cost of used section 38 property purchased by the estate or trust exceeds \$50,000 in any one taxable year, the estate or trust is to select, under regulations prescribed by the Secretary of the Treasury or his delegate, the properties the cost of which may be taken into account.

Paragraph (2) of section 48(f) provides that any beneficiary to whom the investment is apportioned is to be treated as the taxpayer with respect to such investment, and such investment will not (by reason of such apportionment) lose its character as an investment in either new or used section 38 property. If the combined cost of used section 38 property available from all sources to any beneficiary

exceeds \$50,000, such beneficiary must select the properties the cost of which is to be taken into account in computing his qualified investment. The term "beneficiaries" as used in section 48(f) includes heirs, legatees, and devisees.

Paragraph (3) of section 48(f) provides that the \$25,000 amount specified under subparagraphs (A) and (B) of section 46(a)(2) applicable to such estate or trust is to be reduced to an amount which bears the same ratio to \$25,000 as the amount of the qualified investment allocated to the estate or trust under paragraph (1) of section 48(f) bears to the entire amount of the qualified investment. Thus, in a case where the qualified investment of the estate or trust is \$1 million, and \$250,000 of such amount is allocated to the estate or trust because 25 percent of the income is allocable to the estate or trust, the \$25,000 amount in the case of such estate or trust is reduced to \$6,250.

(g) *Adjustments to basis of property.*—Subsection (g) of section 48 was added to the bill by your committee. Paragraph (1) of section 48(g) provides the general rule that the basis of any section 38 property shall (for purposes of subtitle A, relating to income tax, other than for purposes of new subpart B of pt. IV of subch. A of ch. 1) be reduced by an amount equal to 7 percent of the qualified investment of such property as determined under section 46(c). Thus, an adjustment to basis must be made even though the limitation under section 46(a)(2) reduces the amount of the credit the taxpayer may take into account. Such reduction in basis shall be made before any depreciation deductions are computed. It shall also be taken into account for purposes of determining gain or loss on the sale or disposition of the property, and for any other purpose for which the determination of basis is relevant, except that such adjustment shall be disregarded for purposes of computing (or recomputing) the credit under section 38. No adjustment to basis shall be made in the case of property with respect to which an election under section 48(d) (election of lessor to treat lessee as having acquired the property) has been made. (See sec. 48(d).) If the cost of used section 38 property for any taxable year exceeds \$50,000, the basis of only those assets selected to be taken into account under section 46(c)(1)(B) shall be adjusted.

Paragraph (2) of section 48(g) provides that if the tax under chapter 1 of the code is increased for any taxable year under paragraphs (1) or (2) of section 47(a) (relating to certain dispositions, etc., of sec. 38 property) or an adjustment in carrybacks or carryovers is made under paragraph (3) of such section, the basis of the property described in section 47(a) (1) or (2) shall be increased by an amount equal to the portion of the increase in tax and adjustments to carrybacks or carryovers attributable to such property. Whenever the preceding sentence applies, the increase in the basis of the property shall be made immediately before the event causing the application of section 47(a) (1) or (2). Thus, the adjustment will be taken into account for purposes of determining gain or loss on a disposition of the property. (In the case of property subject to an election under section 48(d), see sec. 48(d).)

The provisions of paragraphs (1) and (2) of section 48(g) may be illustrated by the following example:

Corporation X acquires and places in service a new section 38 asset on January 1, 1964, the first day of its first taxable year. Such asset has a basis of \$60,000 and an estimated useful life of 10 years. Cor-

poration X's credit is \$4,200 (7 percent times \$60,000, qualified investment), but since X's liability for tax (as defined in sec. 46(a)(3)) is only \$4,000, X can only take into account \$4,000 of its credit. X will have an unused credit carryover of \$200. However, X must reduce the \$60,000 basis of its section 38 asset by the full \$4,200 credit. The basis of such section 38 asset for purposes of computing a depreciation allowance for the year ending December 31, 1964, is \$55,800 (\$60,000 basis less \$4,200 credit determined without regard to the limitation of sec. 46(a)(2)). On June 30, 1965, corporation X sells such asset. There will be added to the taxes imposed by chapter 1 for X's taxable year ending December 31, 1965, \$4,000 (the aggregate decrease in the credits allowed resulting solely from substituting a 1½-year life for such asset in recomputing qualified investment for 1964). The unused credit carryover to 1965 is reduced from \$200 to zero. (See sec. 47(a)(3).) The basis of such asset immediately prior to the sale on June 30 shall be increased by \$4,200 (\$4,000, the increase in tax, plus \$200, the adjustment in carryovers, attributable to the property).

(c) *Deduction for unused credit.*—Subsection (c) of section 2 of the bill was added by your committee. It adds new section 181 to part VI of subchapter B of chapter 1 (relating to itemized deductions for individuals and corporations). Section 181 provides that if the amount of the credit earned (after taking into account any reductions in credit and credit carryovers resulting from the application of sec. 47(a)) exceeds the limitation provided by section 46(a)(2) for any taxable year, and if any portion of such excess credit has not, after the application of section 46(b) (relating to a 3-year carryback and a 5-year carryover of unused credits), been allowed to the taxpayer as a credit under section 38 for any taxable year, then an amount equal to such portion shall be allowed to the taxpayer as a deduction for the first taxable year following the last taxable year in which such portion could under section 46(b) have been allowed as a credit. In the case of property with respect to which an election under section 48(d) has been made, the lessee of such property is the taxpayer and will be entitled to such deduction.

However, if a taxpayer dies or ceases to exist prior to the first taxable year following the normal expiration of an unused credit carryover (5 years), an amount equal to the unused credit, or an amount equal to the proper portion thereof, shall, under regulations prescribed by the Secretary of the Treasury or his delegate, be allowed to the taxpayer as a deduction for the taxable year in which such death or cessation occurs. The preceding rule shall not apply to a corporate acquisition to which new paragraph (23) of section 381(c) applies. A "proper portion" of the unused credit carryover means that a deduction shall be allowed only to the extent that the reduction in basis under section 48(g) (or reduction in lease payments under sec. 48(d)) has caused a diminution of prior depreciation allowances (or rental payments).

The provisions of section 181 may be illustrated by the following examples:

Example 1.—Y corporation's credit based on its investment for the calendar year ending December 31, 1964, its first taxable year, amounts to \$100,000, and the limitation under section 46(a)(2) is \$60,000. Y's unused credit for 1964 is \$40,000 (\$100,000 minus

\$60,000), which it may carry forward to 1965, and the 4 succeeding taxable years. However, because of successive net operating losses through 1969, Y is unable to use any portion of the \$40,000 as a credit against tax; nor has the \$40,000 unused credit carryover been adjusted under section 47(a)(3). For the taxable year ending December 31, 1970, Y, in computing its taxable income, may take a deduction for \$40,000 under the new section 181.

Example 2.—Corporation X acquires and places in service a new section 38 asset, asset A, on January 1, 1964, the first day of its first taxable year. Asset A has an estimated useful life of 4 years. The credit with respect to such asset is \$50,000, but because of the limitation based on tax, only \$30,000 is taken into account as a credit in 1964. X has an unused credit carryover of \$20,000 which may be carried forward through 1969. Because of substantial purchases of section 38 property in 1965, 1966, 1967, and 1968, X is unable to use any portion of the \$20,000 credit carryover as a credit against tax. By 1968, asset A has been fully depreciated. On December 31, 1968, X distributes all of its assets in complete liquidation and dissolves. The transaction is not one to which section 381(c) applies, and section 48(g)(2) does not apply to the transfer of asset A. For the taxable year ending December 31, 1968, X, in computing its taxable income, may take a deduction for \$20,000 under section 181.

(d) *Certain corporate acquisitions.*—Subsection (d) of section 2 of the bill, which corresponds to subsection (c) of section 2 of the bill as passed by the House, provides an amendment to section 381(c) of the 1954 Code (relating to the carryover of tax attributes in the case of certain corporate acquisitions) by adding paragraph (23) thereto. Section 381(c)(23) provides that the acquiring corporation is to take into account (to the extent proper to carry out the purposes of sec. 381 and sec. 38, and under such regulations as may be prescribed by the Secretary of the Treasury or his delegate) the items required to be taken into account for purposes of section 38 in respect of the distributor or transferor corporation. Thus, for example, the regulations under section 381(c)(23) will provide rules for the carryover of any unused credit carryovers of the distributor or transferor corporation, for the application of new section 181, and for the application of section 47 to dispositions by the acquiring corporation of property acquired from the distributor or transferor corporation.

(e) *Statutes of limitations and interest relating to investment credit carrybacks.*—Subsection (e) of section 2 of the bill, which was added to the bill by your committee, amends certain provisions of the code relating to statutes of limitations and interest. These amendments were made necessary by the adoption of the provision allowing a 3-year carryback of any unused investment credit.

Paragraph (1) of section 2(e) of the bill amends section 6501, relating to limitations on assessment and collection, to provide that in the case of a deficiency attributable to the application of an investment credit carryback, the deficiency may be assessed at any time before the expiration of the period within which a deficiency may be assessed for the taxable year in which the unused investment credit arose (i.e., the unused credit year) which results in such carryback. This provision in effect suspends the statute of limitations on the assessment of a deficiency on account of the disallowance of an erroneous or improper investment credit carryback until the expiration of

the statutory period of limitation on assessments attributable to the taxable year from which the investment credit carryback arose.

Paragraph (2) of section 2(e) of the bill amends subsection (d) of section 6511, relating to limitations on credit or refund, by adding a new paragraph (4) thereto, entitled "Special period of limitation with respect to investment credit carrybacks." Subparagraph (A) of new paragraph (4) provides that a claim for credit or refund relating to an investment credit carryback may be filed at any time before the 15th day of the 40th month (or 39th month, in the case of a corporation) following the end of the taxable year of the unused investment credit which gave rise to the carryback, or within the period prescribed in section 6511(c) in respect of such year (relating to special rules applicable in case of extension of time by agreement), whichever expires later. Subparagraph (A) of new paragraph (4) also provides that in the case of such a claim, the amount of the credit or refund may exceed the portion of the tax paid within the period provided in section 6511 (b)(2) or (c), depending on whichever is applicable, to the extent of the amount of the overpayment which is attributable to the carryback.

Subparagraph (B) of new paragraph (4) of section 6511(d) provides rules for the application of the special period of limitation with respect to the investment credit carryback. Subparagraph (B) provides that if the allowance of a credit or refund of an overpayment of tax attributable to an investment credit carryback is otherwise prevented by operation of any law or rule of law other than section 7122, relating to compromises, such credit or refund may be allowed or made, if a claim therefore is filed within the period provided in section 6511(d)(4) (A). In the case of any such claim for credit or refund, the determination by any court, including the Tax Court, in any proceeding in which the decision of the court has become final, shall not be conclusive with respect to the investment credit, and the effect of such credit, to the extent that such credit is affected by a carryback which was not an issue in such proceedings.

Paragraph (3) of section 2(e) of the bill amends subsection (e) of section 6601 (relating to interest on underpayment, nonpayment, or extensions of time for payment of tax) to provide that if the credit allowed by section 38 for any taxable year is increased by reason of an investment credit carryback, the increase shall not affect the computation of interest under section 6601 for the period ending with the last day of the taxable year in which the investment credit carryback arises (the unused credit year).

Paragraph (4) of section 2(e) of the bill amends subsection (f) of section 6611, relating to interest on overpayments, to provide that for purposes of the payment of interest on an overpayment of tax resulting from an investment credit carryback, such overpayment will be deemed not to have been made prior to the close of the taxable year in which the investment credit carryback arises. Thus, if an unused investment credit for the calendar year 1968 is carried back to 1965, and an overpayment of tax for the year 1965 results, no interest will be allowed or paid in respect of such overpayment for any period prior to December 31, 1968.

(f) *Technical amendment.*—Subsection (f) of section 2 of the bill, which was added by your committee, amends section 1016(a) of the 1954 Code, relating to adjustments to basis, by adding a new para-

graph 19 thereto. Under the new section 1016(a)(19), an adjustment must be made to the basis of property which is or has been section 38 property, to the extent provided in section 48(g).

(g) *Clerical amendments.*—Subsection (g) of section 2 of the bill, provides a clerical amendment to part IV of of subchapter A and part VI of subchapter B of chapter 1 of the 1954 Code.

(h) *Effective date.*—Subsection (h) of section 2 of the bill provides that the amendments made by section 2 of the bill are to apply with respect to taxable years ending after June 30, 1962.

SECTION 3. APPEARANCES, ETC., WITH RESPECT TO LEGISLATION

Except for the addition by your committee of a provision relating to stockholders and employees, this section is identical to section 3 of the bill as passed by the House. Subsection (a) of section 3 amends section 162 (relating to trade or business expenses) by redesignating subsection (e) as subsection (f) and by inserting after subsection (d) a new subsection (e) relating to appearances, etc., with respect to legislation.

Paragraph (1) of the new subsection (e) provides that the deduction allowed by subsection (a) of section 162 is to include all of the following ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business: (1) expenses in direct connection with appearances before, submission of statements to, or sending communications to, the committees, or individual members, of Federal, State, or local legislative bodies with respect to legislation or proposed legislation of direct interest to the taxpayer, (2) expenses in direct connection with communication of information between the taxpayer and an organization of which he is a member with respect to legislation or proposed legislation of direct interest to the taxpayer and to such organization, (3) that portion of dues with respect to any organization of which the taxpayer is a member which is attributable to the expenses of the activities above described in this paragraph which are carried on by such organization, and (4) expenses in direct connection with communication of information between the taxpayer and an employee or stockholder with respect to legislation or proposed legislation of direct interest to the taxpayer. Paragraph (1) also provides that the expenses referred to therein are to include, but not be limited to, the cost of preparing testimony and traveling expenses described in subsection (a)(2) of section 162.

Paragraph (2) of the new subsection (e) provides that the provisions of paragraph (1) are not to be construed as allowing the deduction of any amount paid or incurred (whether by way of contribution, gift, or otherwise)—

(1) for participation in, or intervention in, any political campaign on behalf of any candidate for public office, or

(2) in connection with any attempt to influence the general public, or segments thereof, with respect to legislative matters, elections, or referendums.

Subsection (b) of this section of the bill provides that the amendments made by subsection (a) are to apply to taxable years beginning after December 31, 1962.

SECTION 4. DISALLOWANCE OF CERTAIN ENTERTAINMENT, ETC., EXPENSES

(a) *Denial of deduction.*—Subsection (a) of section 4 of the bill adds to part IX of subchapter B of chapter 1 of the code (relating to items not deductible in computing taxable income) a new section 274.

SECTION 274. DISALLOWANCE OF CERTAIN ENTERTAINMENT, ETC., EXPENSES

Section 274 provides generally that certain expenses deductible in full under present law will be partially or completely disallowed for purposes of chapter 1 of subtitle A. Since section 274 is a disallowance provision exclusively, no expense would become deductible by reason of its enactment. In other words, the tests for deductibility under provisions of existing law (such as secs. 162, 165, 167, and 212) must first be met before the provisions of section 274 become operative. In addition, subsection (d) (relating to substantiation) of the new section 274 must be applied before determining the extent to which an expense or other item is disallowed under subsection (a), (b), or (c) of section 274.

(a) *Entertainment, amusement, or recreation.*—

Activity.—Paragraph (1)(A) of subsection (a) of new section 274 provides that no deduction otherwise allowable under chapter 1 of the 1954 Code is to be allowed for any item with respect to an activity which is of a type generally considered to constitute entertainment, amusement, or recreation, unless the taxpayer establishes that the item was directly related to or associated with the active conduct of his trade or business. Such deduction in no event is to exceed the portion of such item directly related to or associated with the active conduct of the taxpayer's trade or business.

Examples of "entertainment, amusement, or recreation" are entertaining guests at nightclubs, country clubs, theaters, football games, and prizefights, and on hunting, fishing, vacation, and similar trips. In addition, "entertainment" includes satisfying the personal, living, or family needs of any individual (which would otherwise constitute a business expense to the taxpayer) such as the furnishing of food and beverages, a hotel suite, or an automobile. By referring to an activity which "is of a type generally considered to constitute" entertainment, amusement, or recreation, the subsection provides an objective test for determining whether an activity is to be treated under this new provision.

Facilities.—Paragraph (1)(B) of subsection (a) of new section 274 provides that no deduction otherwise allowable under chapter 1 of the code is to be allowed for any item with respect to a facility used in connection with an activity generally considered to constitute entertainment, amusement, or recreation, unless the taxpayer establishes that the facility was used primarily for the furtherance of his trade or business, and that the item was directly related to or associated with the active conduct of his trade or business. Such deduction in no event is to exceed the portion of such item directly related to or associated with the active conduct of the taxpayer's trade or business. The same tests for determining whether an item is directly related to

or associated with the active conduct of a trade or business apply as in the case of an item under paragraph (1)(A).

The term "facility" includes any item of personal or real property owned or rented by the taxpayer, such as a yacht, hunting lodge, fishing camp, swimming pool, tennis court, bowling alley, automobile, airplane, apartment, hotel suite, dining room, and cafeteria. In addition to the items more commonly regarded as "expenses" for entertaining, discussed above, paragraph (1)(B) also relates to other items, such as depreciation and losses realized on certain sales.

Under paragraph (1)(B), in addition to the requirement that the item be directly related to or associated with the active conduct of the taxpayer's trade or business, the facility must be used primarily for the furtherance of the taxpayer's trade or business. Thus, if a facility is used more than one-half for business entertaining, so that more than one-half of the entertainment expense with respect to such facility would be deductible as a business expense under present law, that portion is still to be deductible to the extent it meets the test of being directly related to or associated with the active conduct of the taxpayer's trade or business. If less than one-half of such entertainment expense would be deductible under present law, no deduction is to be allowed.

Paragraph (2) of subsection (a) of new section 274 prescribes two special rules for purposes of applying paragraph (1). All dues and fees paid to any social, athletic, or sporting club or organization will be treated as items with respect to a facility used for entertaining. Thus, only if the taxpayer uses a country club to which he belongs primarily for the furtherance of his business will a deduction be allowed for dues or fees paid to such club, and then only to the extent that such use is directly related to or associated with the active conduct of his business. In addition, in applying paragraph (1) an activity described in section 212 (relating to expenses for the production of income) is to be treated as a trade or business.

(b) *Gifts*.—Subsection (b)(1) of new section 274 is the same as passed by the House except that your committee has added three exceptions to the term "gift." Generally, subsection (b)(1) disallows all expenses for gifts to individuals in excess of a cumulative total of \$25 per year per recipient. The reference to "indirect" gifts in this subsection includes situations where the gift is intended for the eventual use or benefit of an individual but is made initially to his corporation or to some member of his family. The term "gift", for purposes of section 274, has, in general, the same meaning as it does under section 102 of the code (relating to the exclusion of gifts and inheritances from gross income).

Any item which is excludable from gross income under a provision of chapter 1 of the code other than section 102 is not a "gift" within the meaning of subsection (b)(1). To illustrate the applicability of subsection (b)(1), a payment by an employer to a deceased employee's widow which is excludable from her income by reason of the gift exclusion provision, section 102, will not be deductible by the employer in excess of \$25, whereas the treatment by an employer of a payment to a deceased employee's widow which is not a gift but which constitutes an employee's death benefit excludable by the recipient under section 101(b) of the code will not be affected by this provision. As another example, amounts paid to an individual as a scholarship

which are excludable from the individual's gross income under section 117 of the code are not "gifts" within the meaning of this subsection. Similarly, those prizes and awards which are excludable from a recipient's gross income under section 74(b) of the code are not "gifts" within the meaning of this subsection.

Subparagraph (A) sets forth the first exception to the term "gift" added by your committee. It provides that the term "gift" does not include an item which cost the taxpayer not more than \$4 on which the name of the taxpayer is clearly and permanently imprinted and which is one of a number of identical items distributed generally by the taxpayer. Thus, the deductibility of the cost of any such item will not be affected by section 274(b) and the taxpayer will not have to take such items into account in connection with the \$25 limitation in such section.

The second exception, in subparagraph (B), excludes from the term "gift" any sign, display rack, or other promotional material to be used on the business premises of the recipient. Such items are sometimes referred to as "point-of-purchase" advertising materials.

Subparagraph (C) contains the third exception to the term "gift" added by your committee. It provides that "gift" does not include an item of tangible personal property, such as a watch, which costs the taxpayer not more than \$100 and which the taxpayer awarded to an employee because of his length of service or for his safety achievement. This exception relates only to deductibility by the employer. It is not intended to have any effect in determining whether the employee who receives the award is to be taxed on its value.

Since the question in subsection (b)(1) is what portion of the taxpayer's expense will be disallowed, the \$25 amount necessarily relates to the taxpayer's cost rather than to the value of the property to the donee. However, certain incidental costs, such as packaging, insurance, and mailing or other delivery, will be disregarded in determining whether the \$25 limit has been exceeded.

There is a possibility of overlapping application of subsections (a) and (b), since some items can reasonably be classified both as gifts and as entertainment. Different rules under section 274 apply depending on the classification of the item. As described in greater detail below, the express authority given to the Secretary of the Treasury or his delegate to prescribe regulations will be used to solve these problems of classification so as to clarify and make more certain the application of section 274.

Subsection (b)(2) prescribes two special rules for applying subsection (b)(1). Under subsection (b)(2)(A), in the case of a gift by a partnership (including a gift made by a partner with respect to the business of the partnership), the \$25 limitation will be applied at the partnership level, as well as at the level of the individual partner. Thus, deductions for gifts made with respect to partnership business will not exceed \$25 per recipient, regardless of the number of partners.

Under subsection (b)(2)(B), a husband and wife are for purposes of subsection (b)(1) treated as one "taxpayer". Thus, in the case of a gift by a husband and wife, the spouses will be treated as one donor. However, since "taxpayer" in subsection (b)(1) refers only to the donor of a gift, this special rule does not pertain to gifts, for example, made by an individual to a husband and wife who are partners in a business.

(c) *Traveling.*—This is a new subsection adopted by your committee. Under present law if a taxpayer travels to a destination and while at such destination engages in both business activities (or activities described in section 212) and personal activities, traveling expenses to and from such destination are deductible only if the trip is related primarily to the taxpayer's trade or business. If the primary purpose is business the entire amount of such traveling expenses is deductible. If the trip is primarily personal in nature no part of the traveling expenses to and from the destination is deductible even though the taxpayer engages in business activities while at such destination. However, expenses while at the destination which are properly allocable to the taxpayer's trade or business are deductible even though the traveling expenses to and from the destination are not deductible.

The new subsection (c) which your committee has added to section 274 provides that in the case of any individual who is traveling away from home in pursuit of a trade or business or in pursuit of an activity described in section 212, no deduction shall be allowed under section 162 or section 212 for that portion of the expenses of such travel otherwise allowable under such section which, under regulations prescribed by the Secretary of the Treasury or his delegate, is not allocable to such trade or business or to such activity. Under this provision a taxpayer must meet two tests before he becomes entitled to deduct traveling expenses. First, the expenditure must be deductible under the rules of section 162 or 212. If it is not deductible under those sections the taxpayer gets no deduction and no reference to the rules of section 274(c) is necessary. However, if an expenditure is deductible under section 162 or 212 then the expenditure must be subjected to the allocation rules of section 274(c) to determine the extent to which the expenditure is ultimately deductible.

To avoid the application of section 274(c) in cases where the possibilities of abuse are relatively small your committee's amendment provides that the provision shall not apply to the expenses of any travel away from home which does not exceed 1 week or where the portion of the time away from home which is not attributable to the pursuit of the taxpayer's trade or business or an activity described in section 212 is less than 25 percent of the total time away from home on such travel.

The operation of subsection (c) may be illustrated by the following examples:

Example 1.—Taxpayer A flew from New York to London where he conducted business for 2 days. A then flew to Stockholm for a 14-day vacation after which he flew back to New York from Stockholm. The trip took 18 days, 2 of which were attributable to the flight to London and return. A would not have made the trip except for the business he had to conduct in London. Under present law A could deduct the entire cost attributable to transportation and food to and from London and the food and lodging during the 2 days spent on business in London. The traveling expenses attributable to the vacation part of his trip including transportation, food, and lodging would not be deductible under present law. Such personal expenditures would also not be deductible under section 274(c) in the bill. In addition under such section, since the travel away from home exceeded a week and the time devoted to personal activities was not less than 25 percent of the total time away from home, it is contem-

plated that the regulations will provide that fourteen-eighteenths (14 days devoted to personal activities out of a total of 18 days away from home on the trip) of the costs attributable to transportation and food to and from London are to be disallowed. The deductibility of cost of the food and lodging during the 2 days spent on business in London would be determined under section 162(a)(2), as amended by the bill.

Example 2.—Taxpayer B flew from New York to Paris where he conducted business for 1 day. He spent the next 2 days sightseeing in Paris and then flew back to New York. The entire trip, including 2 days flying to and from Paris, took 5 days. B would not have made the trip except for the business he had to conduct in Paris. Under present law B can deduct the entire cost of his transportation and food to and from Paris, and the food and lodging attributable to the 1 business day in Paris but not the food and lodging attributable to the 2 days spent on sightseeing. Since the trip did not exceed 1 week, the allocation rules of section 274(c) would not apply.

Example 3.—Taxpayer C flew from New York to Brussels where he spent 14 days on business and 5 days on personal matters and then flew back to New York. The entire trip, including 2 flying days, took 21 days. C would not have made the trip except for the business he had to transact in Brussels. Under present law C could deduct the entire cost attributable to transportation and food to and from Brussels and the food and lodging during the 14 days spent on business but not the food and lodging attributable to the 5 days spent on personal matters. Although the trip exceeded a week the time away from home attributable to nonbusiness activities (5 days out of 21) was less than 25 percent of the total time away from home during the trip. Therefore the allocation rule of section 274(c) does not apply.

(d) *Substantiation required.*—This subsection, except for a clerical change, is identical to subsection (c) of section 274 of the bill as passed by the House. It imposes another limitation on traveling expenses deductible under section 162(a)(2) or 212, on items with respect to activities described in subsection (a) as entertainment, amusement, or recreation, or with respect to facilities used in connection therewith (whether or not excepted from the application of subsec. (a) of sec. 274 by subsec. (e)), and on expenses for gifts. Subsection (d) overrules with respect to the described expenditures the case of *Cohan v. Commissioner*, 39 F. 2d 540 (C.A. 2d 1930). That case held that where evidence indicates that a taxpayer has incurred deductible travel or entertainment expenses but their exact amount cannot be determined, the court must make “as close an approximation as it can” and not disallow the deduction entirely. Under subsection (d) approximations of the type which under the *Cohan* doctrine have been sufficient to entitle the taxpayer to a deduction will no longer have that effect. In other words, if the taxpayer fails to substantiate an item as required by subsection (d) and the regulations thereunder, the item will be completely disallowed.

Subsection (d) provides that no deduction is to be allowed for the above-described items unless the taxpayer substantiates by adequate records or by sufficient evidence corroborating his own statement the following: the amount of such expense or other item; the time and place of the travel, entertainment, amusement, recreation, or use of the facility, or the date and description of the gift; the business purpose

of the expense or other item; and the business relationship to the taxpayer of the persons entertained, using the facility, or receiving the gift. The taxpayer's records or corroborating evidence, must pertain to separate expenses or other items of deduction, not to aggregate amounts.

Generally, a clear, contemporaneously kept diary, account book, or similar record containing the information specified in subsection (d) will be an adequate record within the meaning of this subsection. However, receipts, canceled checks, paid bills, stubs, or other similar records may be required in certain cases, as, for example, to substantiate the amount expended for lodging and transportation while traveling on business. Thus, the taxpayer may be required to preserve hotel bills or transportation receipts to substantiate such items by adequate records. In order to avoid hardship, a reasonable reconstruction of expenditures will be accepted in those cases where the absence of records is due to circumstances beyond the taxpayer's control, such as destruction by fire, flood, or other casualty.

Where the taxpayer fails to maintain adequate records with respect to any of the described aspects of an expense, that aspect must be substantiated by the taxpayer's own statement corroborated by sufficient evidence. The taxpayer's own uncorroborated statement will not constitute substantiation with respect to any such aspect. The evidence required may vary with respect to each aspect of an item claimed as a deduction. Thus, circumstantial evidence, such as the nature of the business activities of the taxpayer and of the person entertained, may be sufficient to corroborate the taxpayer's statement regarding business purpose and business relationship, whereas more direct evidence, such as the testimony of witnesses, will be required to substantiate amount, time, place, date, and description.

Under subsection (d), the Secretary of the Treasury or his delegate is authorized to provide by regulations that some or all of the requirements of subsection (d) are not to apply in the case of an expense which does not exceed an amount determined under such regulations. Thus, the regulations could provide that a fixed scale of allowance for mileage or per diem in lieu of subsistence, based upon reasonable business practices, will be acceptable in lieu of detailed substantiation. Similarly, the regulations could prescribe an exception for *de-minimis* expenses.

(e) *Exceptions to application of subsection (a).*—Subsection (e) of the new section 274 is identical to subsection (d) of the bill as passed by the House except for clerical changes and an amendment to paragraph (6) discussed below. Subsection (e) contains nine exceptions to the general rule of section 274(a). These exceptions are to the disallowance provision of subsection (a) exclusively. The fact that an item is not covered by one of the nine exceptions does not mean that *ipso facto* it will be disallowed under subsection (a). It is to be emphasized that the new section 274(e) in no way changes existing law with respect to the disallowance of expenses by reason of failure to meet the "ordinary and necessary" test in section 162 or 212 of the code. Furthermore, the substantiation requirements of subsection (d) also must be fulfilled with respect to the items covered by these exceptions.

Paragraph (1) excepts from the disallowance prescribed in subsection (a)(1) expenses for food and beverages furnished under circum-

stances which are of a type generally considered to be conducive to a business discussion, taking into account the surroundings in which furnished, the taxpayer's trade, business, or income-producing activity, the relationship to such trade, business, or activity of the persons to whom the food and beverages are furnished, and any other relevant facts. There is no requirement in this exception that business actually be discussed. Thus, if the described circumstances are established, and if the amounts are deductible under section 162 or 212 and are substantiated as required under section 274(d), the expenses for food and beverages will be deductible without reference to the "directly related to or associated with" tests of subsection (a)(1). Of course, "trade or business" is not restricted to commercial activities but includes other activities such as teaching, the practice of law or medicine, etc.

Paragraph (2) relates to food and beverages furnished on the taxpayer's business premises. By reason of this exception, no expense for food and beverages furnished on the business premises primarily to employees of the taxpayer will be disallowed under section 274(a). In addition, expenses for food and beverages furnished to nonemployee business guests will be deductible if furnished in a dining room which is primarily for the taxpayer's employees and is located on the taxpayer's business premises. Paragraph (2) also excepts from disallowance expenses for facilities to the extent they are used in connection with furnishing the above-described food and beverages. The exception provided by paragraph (2) applies to both the typical company cafeteria and meals furnished to employees because their presence on the job at all times is essential.

The exception in paragraph (3) applies to expenses for goods, services and facilities to the extent that the expense is properly treated by the taxpayer, with respect to the recipient of the entertainment, amusement, or recreation, as compensation paid to an employee on the taxpayer's income tax return and as "wages" for purposes of withholding. Thus, a taxpayer rewarding a key employee with a vacation trip would not be disallowed the expenses under section 274(a) if the taxpayer treated the expenses as wages for withholding purposes and deducted them on his income tax return as compensation paid to the key employee. Salary paid to the captain of a yacht used for business entertaining does not come within this exception.

If an expense properly constitutes a dividend to a shareholder, or if it constitutes unreasonable compensation to an officer or employee, the exception in paragraph (3) will not prevent its disallowance.

Paragraph (4) excepts from disallowance with respect to the taxpayer certain expenses paid or incurred by the taxpayer in connection with the performances by him of services for another person (whether or not such other person is the taxpayer's employer) for which the taxpayer is reimbursed by such other person under a reimbursement or other allowance arrangement. This exception prevents the double disallowance of a single expenditure, once with respect to the person who actually bears the expense and benefits from it and once with respect to the person who pays the expense on behalf of the first person and is reimbursed therefor. However, two qualifications are provided which insure that a described expense will be disallowed at one level. If the services are performed by a taxpayer, who is an employee, for his

employer, and if the employer treats the expense as compensation paid to the employee and it falls within the scope of the subsection (e)(3) exception, the subsection (e)(4) exception does not apply. If the services are performed by the taxpayer for a person who is not the taxpayer's employer, the subsection (e)(4) exception does not apply unless the taxpayer accounts to such other person by means of records or other sufficient evidence which would satisfy the substantiation requirement of subsection (d). The term "reimbursement or other expense allowance arrangement" is derived from section 62(2)(A) of the code and has the same meaning in section 274(e) (without regard to whether the taxpayer is the employee of the person for whom services are performed) as it does in that section.

Paragraph (5) provides an exception for expenses for recreational, social, or similar activities which are primarily for the benefit of the employees of the taxpayer. This exception applies to the usual employee fringe benefit programs. For example, the expenses of operating a company bowling alley or swimming pool which is available to all employees generally will be deductible. Similarly, the costs of the office Christmas party or summer outing generally will be deductible.

In order to exclude from this exception benefits primarily for executives and owners of closely held businesses, the exception applies only with respect to activities which are primarily for employees other than employees who are officers, shareholders or other owners who own a 10 percent or greater interest in the business, or highly compensated employees. In determining whether an employee owns a 10 percent or greater interest in the business, the employee is to be treated as owning any interest owned by a member of his family (within the meaning of sec. 267(c)(4)).

Paragraph (6) provides an exception for expenses incurred by a taxpayer which are directly related to business meetings of his employees, stockholders, agents, or directors. This paragraph is substantially the same as paragraph (6) of subsection (d) of section 274 in the bill as passed by the House except that whereas the bill as passed by the House was limited to meetings of employees and stockholders, your committee's amendment also includes meetings of agents and directors of the taxpayer. This exception pertains only to meetings which are principally for the discussion of business. To illustrate, a meeting of employees for the principal purpose of introducing them to and instructing them with respect to a new procedure for conducting the employer's business would be considered a business meeting. Similarly, a regular annual meeting of stockholders for the election of directors and discussion of corporate affairs would be considered a business meeting. A convention of employees for the principal purpose of rewarding them for their outstanding performance of services for their employer would not be considered a business meeting. However, such a convention might come within the scope of paragraph (3) or (5).

Paragraph (7) pertains to expenses directly related and necessary to attendance at business meetings or conventions of exempt section 501(c)(6) organizations. It is similar to the exception in paragraph (6), except that it relates only to attendance at meetings, or conventions of business leagues, chambers of commerce, real estate boards, or boards of trade which are exempt from tax under section 501(a).

Paragraph (8) pertains to goods and services (including the use of facilities) which are made available by the taxpayer to the general public. By reason of this exception, expenses for entertainment of the general public by means of television, radio, newspapers, and the like will continue to be deductible under section 162. Similarly, a deduction may still be claimed under section 162 for the expense of maintaining private parks, golf courses, and similar facilities, to the extent that they are available for public use. For example, if a corporation maintained a swimming pool for the use of its executive officers and their guests, but during the summer months made the pool available for a period of time each week to the children participating in the local public recreation program, the portion of the expenses relating to such public use of the pool would come within this exception.

Paragraph (9) is designed to insure that no expense will be disallowed under subsection (a) if it is for goods or services which are sold by the taxpayer in a bona fide transaction for an adequate and full consideration in money or money's worth. Thus, the cost of producing nightclub entertainment for sale to customers will not be disallowed. Similarly, the cost of operating a pleasure cruise ship as a business will not be disallowed.

The last sentence in subsection (e) makes it clear that the "expenses" to which paragraphs (1) through (9) relate include such items as depreciation and losses.

(f) *Interest, taxes, casualty losses, etc.*—This subsection, except for a clerical change, is identical to subsection (e) of new section 274 of the bill as passed by the House. Subsection (f) excepts from the provisions of section 274 items which would constitute allowable deductions for an individual taxpayer regardless of whether he was engaged in any trade or business. Examples of such items are interest, taxes such as real property taxes, and casualty losses. Thus, if a taxpayer owned a fishing camp, he could still deduct mortgage interest and real property taxes in full even if its use was not primarily for the furtherance of the taxpayer's trade or business.

(g) *Treatment of entertainment, etc., type facility.*—This subsection, except for a clerical change, is identical to subsection (f) of new section 274 of the bill as passed by the House. This subsection prescribes the treatment to be accorded facilities coming within the purview of subsection (a)(1)(B), for purposes of chapter 1 generally. To the extent that expenses and other items with respect to a facility are disallowed under subsection (a), that portion of the facility is to be accorded the treatment provided under present law to an asset used exclusively for personal, living, and family purposes. Thus, the portion of a facility so treated will not be subject to depreciation, and losses incurred on the sale of such portion will not be deductible.

(h) *Regulatory authority.*—This subsection, except for a clerical change, is identical to subsection (g) of new section 274 of the bill as passed by the House. Subsection (h) authorizes the Secretary of the Treasury or his delegate to prescribe such regulations as he deems necessary to carry out the purposes of section 274. For example, under this authorization rules will be prescribed for determining whether subsection (a) or subsection (b) applies to an expenditure to which both subsections might be considered to apply. Items are to be given the character ascribed to them by the public generally and without regard to the revenue consequences of the characterization.

In addition, the Secretary of the Treasury or his delegate is required to prescribe rules for determining whether section 274 (a) or (b) applies with respect to an expenditure which could also be described as falling solely within the purview of some other section. This overlap problem will be resolved by ascribing to the expenditure a character which carries out the purposes of section 274. If the item confers a personal benefit in the form of entertainment, amusement, recreation, or a personal, living, or family need of the individual it will be treated as a section 274 item.

The problem of the overlap of subsections (a) and (b) of section 274 can be illustrated by a case where a taxpayer provides one of his customers with tickets to an amusement event. Here both the entertainment and gift provisions might apply. Under the regulations the entertainment provision always will apply with respect to such theater tickets regardless of whether the taxpayer accompanies the customer to the theater or sends him the tickets. On the other hand, gifts of a chattel such as a book or a toy will be classified as a gift, coming within the purview of subsection (b), even though the use of the item results in the entertainment of the recipient. Packaged food and beverages will be treated as gifts, while food and beverages consumed at meals will be considered entertainment.

The problem of properly characterizing an expenditure for purposes of determining whether section 274 is applicable, or whether the expenditure is to be treated solely under some other section, can be illustrated by a case where a taxpayer distributes to each of his customers a valuable gift which is inscribed with the taxpayer's name. Expenditures for such items might be characterized as advertising expenses or as expenses for gifts. Under the regulations, expenditures for such items will be characterized as gifts.

SECTION 4. DISALLOWANCE OF CERTAIN ENTERTAINMENT, ETC., EXPENSES (Continued)

(b) *Traveling expenses*.—The House bill amended section 162(a)(2) of the 1954 Code (relating to traveling expenses while away from home) by striking out the existing provision under which the "entire" amount expended for meals and lodging is included in the allowable deduction and would have substituted therefor a provision under which there is to be included a "reasonable" allowance expended for meals and lodging. In lieu of the House provision your committee's amendment provides that the allowable deduction is to include amounts expended for meals and lodging other than amounts which are lavish or extravagant under the circumstances.

(c) *Effective date*.—The House bill provided that the amendments made by section 4 are to apply with respect to taxable years ending after June 30, 1962, but only with respect to periods after such date. Your committee's action makes this provision effective with respect to taxable years ending after December 31, 1962, but only with respect to periods after such date.

SECTION 5. AMOUNT OF DISTRIBUTION WHERE CERTAIN FOREIGN CORPORATIONS DISTRIBUTE PROPERTY IN KIND

(a) *Amount distributed.*—Subsection (a) of section 5 of the bill amends section 301(b)(1) (relating to amount distributed to corporate distributees) of the 1954 Code by adding at the end thereof a new subparagraph (C). The general rule in new subparagraph (C) provides that for purposes of section 301 the amount of a distribution of property (other than money) received by a corporate shareholder from a foreign corporation will be the fair market value of such property.

An exception to the general rule is provided in cases where a dividends received deduction is allowable under section 245 with respect to such a distribution. In such a case, to the extent the distribution of such property is out of earnings and profits described in section 245(a) (1) and (2), the amount to be taken into account (for purposes of sec. 301 of the code) with respect to property other than money is the sum, determined under regulations prescribed by the Secretary of the Treasury or his delegate, of the amounts computed under subparagraphs (C)(i) and (C)(ii). The amount under subparagraph (C)(i) is that proportion of the lesser of—

(1) the fair market value of such property, or

(2) the adjusted basis (in the hands of the distributing corporation immediately before the distribution) of such property,

which is properly attributable to gross income from sources within the United States. The amount under subparagraph (C)(ii) is that proportion of the fair market value of such property which is properly attributable to gross income from sources without the United States.

The application of subparagraph (C) may be illustrated by the following example involving corporation X, a domestic corporation which owns 100 percent of the outstanding stock of corporation Y, a foreign corporation. Corporation Y, which makes its return on the basis of the calendar year, has earnings and profits of \$200,000 for 1963 and derives 60 percent of its gross income from sources within the United States during 1963. For an uninterrupted period of 36 months ending with the close of 1963, corporation Y has been engaged in trade or business within the United States and has derived 50 percent or more of its gross income from sources within the United States. Assume that the only distribution made by corporation Y during 1963 is a distribution of property which has a fair market value of \$100,000 and an adjusted basis (in the hands of the distributing corporation immediately before the distribution) of \$40,000. The amount of the distribution of such property as determined under section 301(b)(1)(C) is \$64,000, computed as follows:

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|--|-----------|
| (1) Amount computed under section 301(b)(1)(C)(i): That proportion of the adjusted basis of such property (since it is less than the fair market value) which is properly attributable to gross income from sources within the United States, that is, adjusted basis multiplied by the ratio which gross income from sources within the United States bears to gross income from all sources. $\$40,000 \times 60$ percent..... | \$24, 000 |
| (2) Amount computed under section 301(b)(1)(C)(ii): That proportion of the fair market value of such property which is properly attributable to gross income from sources without the United States, that is, fair market value multiplied by the ratio which gross income from sources without the United States bears to gross income from all sources. $\$100,000 \times 40$ percent..... | 40, 000 |
| (3) Amount of distribution of property for purposes of section 301.. | 64, 000 |

(b) *Basis*.—Subsection (b) of section 5 of the bill amends section 301(d) of the code (relating to basis of property) by adding a new paragraph (3). The new paragraph (3) provides that where the amount of a distribution of property other than money is determined in accordance with the provisions of subparagraph (C) of section 301(b)(1), the basis of such property shall be the amount of the property distribution. Thus, in the above example the property distributed would have a basis in the hands of corporation X, the distributee, of \$64,000, the amount of the distribution.

(c) *Dividends received from certain foreign corporations*.—Paragraph (1) of subsection (c) of section 5 of the bill amends section 245 of the 1954 Code (relating to dividends received from certain foreign corporations) by adding a new subsection (b). The new subsection (b) provides that for purposes of computing the dividends received deduction under section 245(a) the amount of any distribution of property other than money shall be determined under section 301(b)(1)(B). Under section 301(b)(1)(B) the amount of a distribution of property to a corporate shareholder is the lesser of (1) the fair market value of such property, or (2) the adjusted basis of such property (in the hands of the distributing corporation immediately before the distribution). Thus, for purposes of section 245, the amount of the dividend in the above example would be \$40,000, rather than \$64,000, and the amount allowed as a deduction under section 245 would be \$20,400 ($\$40,000 \times 60$ percent $\times 85$ percent).

Paragraph (2) of subsection (c) of section 5 of the bill amends section 245 of the 1954 Code so as to designate the existing text as subsection (a) of section 245.

Subsection (d) of section 5 of the House bill, which provides that the section 301(b)(1)(B) amount of a distribution of property other than money is to be used in computing the credit for foreign taxes under section 902, has been deleted. Therefore, the section 301(b)(1)(C) amount will be used in this respect.

(d) *Effective date*.—Subsection (d) of section 5 of the bill, identical with subsection (e) of such section of the bill as passed by the House, provides that the amendments made by section 5 of the bill shall apply to distributions made after December 31, 1962.

SECTION 6. MUTUAL SAVINGS BANKS, ETC.

(a) *In general*.—Subsection (a) of section 6 of the bill as reported, which corresponds to section 8 of the bill as passed by the House, amends section 593 of the 1954 Code to provide a new method for

calculating the deduction for additions to bad debt reserves allowable to the mutual savings banks, domestic building and loan associations, and cooperative banks, referred to in section 593(a) (all of which are hereinafter referred to as mutual savings institutions).

SECTION 593. RESERVES FOR LOSSES ON LOANS

(a) *Organizations to which section applies.*—Subsection (a) of section 593, as amended by the bill, provides that section 593 is to apply to any mutual savings bank not having capital stock represented by shares, domestic building and loan association, or cooperative bank without capital stock organized and operated for mutual purposes and without profit. This description of the organizations to which the amended section 593 applies is substantially the same as that contained in section 593 of existing law, and no substantive change is made by this change in description. As is noted below, however, section 7701(a)(19) (definition of domestic building and loan association) was amended by section 8(c) of the bill as passed by the House, and section 6(c) of the bill as reported by your committee further amends such section.

(b) *Additions to reserves for bad debts.*—Subsection (b)(1) prescribes the method for determining the reasonable addition for the taxable year to the reserve for bad debts under section 166(c), and also specifies the reserves to which such additions shall be made. Such reasonable addition is the sum of two amounts—(1) the amount added to the reserve for losses on nonqualifying loans, and (2) the amount added to the reserve for losses on qualifying real property loans.

The first amount is that determined under section 166(c) to be a reasonable addition to the reserve for losses on nonqualifying loans. Nonqualifying loans are defined in subsection (e)(2), and (with certain exceptions) are loans other than loans secured by an interest in improved real property.

The second amount is the amount determined by the taxpayer to be a reasonable addition to the reserve for losses on qualifying real property loans. Qualifying real property loans are defined in subsection (e)(1) and (with certain exceptions) are loans secured by an interest in improved real property. Under the bill as passed by the House, the amount of the reasonable addition to the reserve for losses on such loans could not exceed the amount determined under one of three different methods described in paragraphs (2), (3), and (4) of subsection (b), whichever method produced the largest amount.

Your committee has amended subsection (b)(1) to provide that the amount of the addition for a taxable year to the reserve for losses on qualifying real property loans, when added to the amount of the addition to the reserve for losses on nonqualifying loans, shall in no case be greater than the amount by which 12 percent of the total deposits or withdrawable accounts of depositors of the taxpayer at the close of such year exceeds the sum of its surplus, undivided profits, and reserves at the beginning of such year (taking into account any portion thereof attributable to the period before the first taxable year beginning after December 31, 1951).

Percentage of taxable income method

This method is described in subsection (b)(2). Under the bill as passed by the House the amount of the reasonable addition to the reserve for losses on qualifying real property loans for a taxable year was limited to the excess of an amount equal to 60 percent of the taxable income for such year over the amount determined under section 166(c) to be a reasonable addition to the reserve for losses on non-qualifying loans. For purposes of this method, taxable income is determined without regard to any deduction under section 166(c) for any additions to the reserves for bad debts, and also by excluding from gross income any amount included therein by reason of subsection (f) (relating to the treatment of certain distributions of property to stockholders by a domestic building and loan association).

Your committee has made two amendments to subsection (b)(2). The first amends subparagraph (A) of subsection (b)(2) to provide that the amount computed under that subparagraph shall be an amount equal to 50 percent of taxable income for the taxable year (rather than 60 percent) in the case of a taxpayer which is a domestic building and loan association having capital stock with respect to which any distribution of property (as defined in sec. 317(a)) is not allowable as a deduction under section 591. In the case of a mutual savings institution other than one described in the preceding sentence the percentage figure remains at 60 percent.

Your committee's second amendment to subsection (b)(2) provides that the amount of the addition determined thereunder shall not exceed such amount as is necessary to increase the balance (as of the close of the taxable year) of the reserve for losses on qualifying real property loans to 6 percent of such loans outstanding at such time.

Percentage of real property loans method

Under this method, which is described in subsection (b)(3) and which has been amended by your committee to provide a special deduction for certain new companies, the amount of the reasonable addition to the reserve for losses on qualifying real property loans is limited to the amount necessary to increase the balance (as of the close of the taxable year) of such reserve to an amount equal to the amount described in subparagraph (A) or equal to the sum of two amounts which are described in subparagraphs (A) and (B) of such subsection. The first amount, which applies in the case of all mutual savings institutions, is an amount equal to 3 percent of qualifying real property loans outstanding at the close of the taxable year. The second amount applies only to a mutual savings institution which is a "new company" and which does not have capital stock with respect to which distributions of property (as defined in sec. 317(a)) are not allowable as a deduction under section 591. In the case of such an institution, such second amount is equal to (i) 2 percent of such loans outstanding, or 2 percent of \$4 million, whichever is the lesser, reduced (but not below zero) by (ii) the amount, if any, of the balance (as of the close of the year) of the taxpayer's supplemental reserve for losses on loans. For purposes of computing such second amount, a mutual savings institution qualifies as a "new company" for any taxable year only if such taxable year begins not more than 10 years after the first day on which it (or any predecessor) was authorized to do business as an organization described in section 593(a).

Experience method

Under this method, described in subsection (b)(4), the amount of the reasonable addition to the reserve for qualifying real property loans is limited to the amount determined under section 166(c) (without regard to sec. 593(b)) to be a reasonable addition to such reserve.

(c) *Treatment of reserves for bad debts.*—Subsection (c)(1) of section 593 as amended provides that each mutual savings institution which uses the reserve method of accounting for bad debts is to establish and maintain a reserve for losses on qualifying real property loans, a reserve for losses on nonqualifying loans, and a supplemental reserve for losses on loans. Except as provided in the last sentence of paragraph (5) of this subsection, which is a new paragraph added by your committee, such reserves are to be treated for all purposes as reserves for bad debts. Thus, although these reserves are termed reserves for “losses,” they are reserves for bad debts; and any charge to any such reserve for an item other than a bad debt will result in the inclusion in gross income of an amount equal to such charge. As is indicated below, however, any portion of the reserve for losses on qualifying real property loans which represents amounts allocated thereto pursuant to subsection (c)(5) shall not be treated as a reserve for bad debts for any purpose other than the determination of the amount deductible under subsection (b).

Allocation of pre-1963 reserves

Paragraphs (2) and (3) of subsection (c) prescribe rules governing the method of allocating pre-1963 reserves among the three reserves described above. The term “pre-1963 reserves” is defined by paragraph (4) to mean the net amount, determined as of the close of December 31, 1962 (after applying the provisions of subsec. (d)(1) relating to taxable years beginning in 1962 and ending in 1963), accumulated in the reserve for bad debts pursuant to section 166(c) (or the corresponding provisions of prior revenue laws), whether or not determined with reference to section 593, for taxable years beginning after December 31, 1951.

Paragraph (2) of subsection (c) provides that such pre-1963 reserves shall, as of the close of December 31, 1962, be allocated to, and constitute the opening balances of, the reserve for losses on nonqualifying loans, the reserve for losses on qualifying real property loans, and the supplemental reserve for losses on loans.

Paragraph (3) of subsection (c) provides that the pre-1963 reserves shall be allocated first to the reserve for losses on nonqualifying loans to the extent that such reserve is not increased above the amount which would constitute a reasonable addition under section 166(c) for a period in which such nonqualifying loans increased from zero to the amount thereof outstanding at the close of December 31, 1962. Thus, the pre-1963 reserves will be allocated to the reserve for losses on nonqualifying loans in an amount not in excess of the maximum amount (determined without regard to any annual limitation which might be imposed under sec. 166(c) on building such reserve to its full amount) which could have been added, as of the close of 1962, to such reserve under subsection (b)(1)(A) if the balance of such reserve immediately prior to such addition had been zero. The remaining portion of the pre-1963 reserves is then allocated to the reserve for

losses on qualifying real property loans to the extent such reserve is not increased above the larger of two amounts. The first amount is the amount which would be determined under paragraph (3)(A) of subsection (b) as being necessary to increase the balance of the reserve from zero to 3 percent of qualifying real property loans outstanding at the close of December 31, 1962. The second amount is the amount which would be determined under section 166(c) (without regard to sec. 593) to be a reasonable addition to the reserve for losses on qualifying real property loans for a period in which such loans increased from zero to the amount thereof outstanding at the close of December 31, 1962. Any remaining balance of the pre-1963 reserves is allocated to the supplemental reserve for losses on loans.

Paragraph (5) of subsection (c) is a new provision which your committee has added to the bill. This paragraph provides that if, after the allocation of pre-1963 reserves to the reserves for losses on non-qualifying loans and for losses on qualifying real property loans, the opening balance of the reserve for losses on qualifying real property loans is less than the maximum amount prescribed by paragraph (3)(B), then, for purposes of subsection (c), the term "pre-1963 reserves" shall also include so much of the taxpayer's "pre-1952 surplus" as does not exceed the amount by which such opening balance is less than the amount described in such paragraph (3)(B). As used in the preceding sentence the term "pre-1952 surplus" refers to the taxpayer's surplus, undivided profits, and bad debt reserves determined as of December 31, 1962, and attributable to the period before the first taxable year beginning after December 31, 1951, but does not include any portion thereof attributable to interest which would have been excludable from gross income under section 22(b)(4) of the Internal Revenue Code of 1939 (relating to interest on governmental obligations) or the corresponding provisions of prior revenue laws.

Paragraph (5) also provides that, notwithstanding the second sentence of paragraph (1) (which requires that the three reserves established pursuant to subsec. (c) shall be treated as reserves for bad debts), any portion of the pre-1952 surplus included in the reserve for losses on qualifying real property loans shall not be treated as a reserve for bad debts for any purpose other than determining the amount of the addition to the reserve for losses on qualifying real property loans, and for such purpose such portion shall be treated as remaining in such reserve. Thus, such portion of the pre-1952 surplus as is included in the reserve for losses on qualifying real property loans as of the close of December 31, 1962, shall be deemed to be included in the balance of such reserve as of the close of each taxable year to which the amended section 593 applies, but only for the limited purpose of determining the maximum permissible addition to such reserve under subsection (b). For all other purposes such portion of the pre-1952 surplus will retain the character that it has under existing law. The effect of your committee's addition of paragraph (5) to subsection (c) is to place an institution which accumulated most of its reserves and surplus prior to 1952 on the same basis, for purposes of computing future additions to reserves, as an institution which accumulated most of its reserves after 1951.

Subsection (c)(6), which is identical to subsection (c)(5) of section 593 in the bill as passed by the House, provides that any debt becoming worthless or partially worthless in respect of a qualifying real

property loan shall be charged to the reserve for losses on such loans, and any debt becoming worthless or partially worthless in respect of a nonqualifying loan shall be charged to the reserve for losses on nonqualifying loans; except that any such debt may, at the election of the taxpayer, be charged in whole or in part to the supplemental reserve for losses on loans.

(d) *Taxable years beginning in 1962 and ending in 1963.*— Subsection (d) of the amended section 593 contains provisions for the computation of taxable income in the case of a taxable year which is a fiscal year beginning in 1962 and ending in 1963. With certain exceptions, the general effective date provision in section 6(g)(1) of the bill makes the amended section 593 applicable with respect to taxable years ending after December 31, 1962. However, subsection (d) makes section 593 take effect with respect to fiscal year taxpayers as of January 1, 1963. Subsection (d) apportions taxable income for the entire taxable year (determined without regard to any deduction under sec. 166(c)) between the part of the taxable year which falls in 1962 and the part which falls in 1963. Such taxable income is allocated to each part year on the basis of the ratio which the number of days in each such part year bears to the number of days in the entire taxable year. The portion of such taxable income allocable to the part of the year occurring before January 1, 1963, is then reduced under subsection (d)(1) by an amount equal to the deduction which would have been allowable under section 166(c) for an addition to the reserve for bad debts as if such part year constituted a taxable year and as if section 593, as in effect before the amendments made by section 6 of the bill, applied. The portion of such taxable income allocable to the part of the taxable year occurring after December 31, 1962, is reduced, under subsection (d)(2), by an amount equal to the deduction for an addition to a reserve for bad debts which would be allowed under section 166(c) (taking into account the amendments made by sec. 6 of the bill) if such part year constituted a taxable year. The amounts of taxable income thus obtained for each part year are then added to obtain the taxable income for the entire taxable year.

The amount of the deduction allowable for the pre-1963 part year to a mutual savings institution under subsection (d)(1) is limited, by reason of section 593(2) of existing law, to the amount by which 12 percent of the total deposits or withdrawable accounts of its depositors at the close of such part year (Dec. 31, 1962) exceeds the sum of its surplus, undivided profits, and reserves at the beginning of the taxable year. In addition, by reason of section 593(1) of existing law, the deduction allowable under subsection (d)(1) for the pre-1963 part year to a mutual savings institution cannot exceed the amount of its taxable income (determined without regard to any deduction under sec. 166) allocable to the pre-1963 part year. Although the amount of the deduction allowable for the pre-1963 part year under subsection (d)(1) cannot be determined until the close of the entire taxable year (by reason of the taxable income limitation and because the amount must be reflected on the institution's regular books of account), this amount is added to the institution's pre-1963 reserves. The pre-1963 reserves are then allocated under the rules of subsection (c), as of the close of December 31, 1962, by reference to the amount of nonqualifying loans and qualifying real property loans outstanding at that time.

The deduction referred to in subsection (d)(2) for the post-1962 part year is determined under subsection (b) and is equal to the sum of the amount of an addition to the reserve for losses on nonqualifying loans plus the amount of an addition to the reserve for qualifying real property loans. The amount of the addition to the reserve for nonqualifying loans is computed by reference to the amount of such loans outstanding at the close of the taxable year in relation to the balance in the reserve for such loans at that time. The amount of the addition to the reserve for qualifying real property loans, if determined under the percentage of taxable income method, would be equal to the excess of an amount equal to 60 percent (or 50 percent, as the case may be) of the taxable income (determined under subsec. (b)(2)) which is allocable to the post-1962 part year over the amount of the reasonable addition to the reserve for nonqualifying loans. If the addition to the reserve for qualifying real property loans is determined under the percentage of real property loans method or the experience method, it would be computed by reference to the amount of such loans outstanding at the close of the taxable year in relation to the balance in the reserve for such loans at that time.

(e) *Loans defined.*—Subsection (e) of the amended section 593 defines, for purposes of that section, the terms “qualifying real property loans”, “nonqualifying loans”, and “loans”.

The term “loan” is defined to mean debt, as the term “debt” is used in section 166. Since subsection (e) of section 166 is made inapplicable by section 582(a) in the case of a mutual savings institution, the term “loan” includes a debt evidenced by a security as defined in section 165(g)(2)(C). For purposes of subsection (e), a taxpayer will be considered to have made a loan to the extent of his participation in the loan, whether the loan was made by him or by another person.

Under paragraph (1) of subsection (e), a “qualifying real property loan” is defined to mean any loan of the taxpayer which is secured by an interest in improved real property unless such loan is described in subparagraph (A), (B), (C), or (D) of such paragraph. The loans described in these subparagraphs are: (A) any loan evidenced by a security (as defined in sec. 165(g)(2)(C)); (B) any loan, whether or not evidenced by a security as defined in section 165(g)(2)(C), the primary obligor on which is a government or political subdivision or instrumentality thereof, a bank as defined in section 581, or another member of the same affiliated group; (C) any loan to the extent secured by a deposit in or share of the taxpayer; and (D) any loan which, within a 60-day period beginning in one taxable year of the creditor and ending in its next taxable year, is made or acquired and then repaid or disposed of, unless the transactions by which such loan was made or acquired and then repaid or disposed of, are established by the taxpayer to be for bona fide business purposes.

The term “affiliated group” is defined as having the meaning assigned to such term by section 1504(a) of existing law; except that (1) the phrase “more than 50%” shall be substituted for the phrase “at least 80%” each place it appears in section 1504(a), and (2) all corporations shall be treated as includible corporations (without any exclusion under sec. 1504(b)).

Paragraph (2) of subsection (e) defines the term “nonqualifying loan” as any loan of the taxpayer which is not a qualifying real property loan as defined by the bill. Thus, a loan which is, for example,

evidenced by a security as defined in section 165(g)(2)(C), is treated as a nonqualifying loan irrespective of the fact that it may be secured by improved real property.

(f) *Distributions to shareholders.*—Subsection (f) of the amended section 593 prescribes rules governing certain distributions of property (as defined in sec. 317(a)) by a domestic building and loan association to a shareholder with respect to its stock, if such distribution is not allowable as a deduction under section 591. The term “distribution” is defined to include any distribution in redemption of stock or in partial or complete liquidation of the association, as well as dividend distributions as defined in section 316(a).

Paragraph (1) of subsection (f) provides, in general, that a distribution with respect to its capital stock is to be treated as made, first, out of the association's earnings and profits accumulated in taxable years beginning after December 31, 1951 (to the extent thereof); second, out of the reserve for losses on qualifying real property loans, to the extent the additions to such reserve exceed the additions which would have been allowed under the experience method described in subsection (b)(4); third, out of the supplemental reserve for losses on loans (to the extent thereof); and, finally, out of such other accounts as may be proper. The foregoing order of charging applies to all subsection (f) distributions other than those in redemption of stock or in partial or complete liquidation of the association. In these latter situations the distribution is treated as made, first, out of the reserve for losses on qualifying real property loans to the extent the additions to such reserve exceed the additions which would have been allowed under the experience method described in subsection (b)(4); second, out of the supplemental reserve (to the extent thereof); third, out of earnings and profits accumulated in taxable years beginning after December 31, 1951 (to the extent thereof); and, finally, out of other appropriate accounts. In determining the portion of the reserve for losses on qualifying real property loans out of which a distribution described in subsection (f)(1) is treated as made, the word “additions,” as used in subparagraph (B) of subsection (f)(1), includes both the additions made to such reserve under subsection (b)(1)(B) and the amount of the pre-1963 reserves allocated thereto pursuant to subsection (c)(3). In computing the amount of the additions which would have been allowed under the experience method, the amount of the pre-1963 reserves initially allocated, and the subsequent additions, to the reserve for losses on qualifying real property loans shall be computed solely by reference to the experience method.

Paragraph (2) of subsection (f) provides that, if a distribution described in paragraph (1) is treated as having been made out of the reserve for losses on qualifying real property loans or out of the supplemental reserve for losses on loans, the amount charged against such reserve shall be the amount which, when reduced by the amount of Federal income tax attributable to the inclusion of such amount in gross income, is equal to the amount of such distribution. Any amount so charged against such reserve shall be included in the gross income of the distributor association. Since the amount so included in gross income is also included in earnings and profits, the effect of subsection (f) is to treat such amount as having been first transferred from the reserves to earnings and profits and then charged to earnings and profits. Thus, this rule will normally insure that there will be

earnings and profits sufficient to make distributions which are in reality dividends taxable as such, even though the association has previously deducted, in computing its earnings and profits, the amount of additions to its bad debt reserves. However, apart from the consequences which flow from the fact that earnings and profits will be created by such charges to the reserves, income tax consequences to stockholders are not otherwise affected by subsection (f).

Paragraph (3) of subsection (f) provides special rules. Subparagraph (A) provides that, for purposes of treating a distribution as having been made out of the reserve for losses on qualifying real property loans, additions to such reserve for the taxable year in which the distribution occurs shall be taken into account. Thus, the amount of such reserve will be augmented by the addition to such reserve computed under subsection (b) before the reserve is reduced by reason of treating a distribution as having been made out of the reserve. Subparagraph (B) provides that, for purposes of computing (under sec. 593, as amended by the bill) the amount of a reasonable addition to the reserve for losses on qualifying real property loans for any taxable year, any amount charged during any year to such reserve pursuant to the provisions of paragraph (2) of subsection (f) shall not be taken into account. Thus, the amount by which such reserve is reduced by reason of distributions to stockholders cannot serve as the basis for subsequent deductible additions to such reserve.

SECTION 6. MUTUAL SAVINGS BANKS, ETC. (Continued)

(b) *Foreclosure on property securing loans.*—Subsection (b) of section 6 adds a new section 595 to the code. The section applies only to a creditor which is a mutual savings institution described in the amended section 593(a).

Nonrecognition of gain or loss as a result of foreclosure

Subsection (a) of the new section 595 provides that in the case of a creditor which is an organization described in section 593(a), no gain or loss shall be recognized, and no debt shall be considered as becoming worthless or partially worthless, as the result of such organization having bid in at foreclosure, or having otherwise reduced to ownership or possession by agreement or process of law, any property which was security for the payment of any indebtedness.

Character of property

Subsection (b) of the new section 595 provides that, for purposes of sections 166 (relating to the deduction for bad debts) and 1221 (relating to the definition of a capital asset), any property acquired in a transaction with respect to which gain or loss was not recognized to the creditor by reason of subsection (a) shall be considered as property having the same characteristics as the indebtedness for which such property was security. The subsection further provides that any amount realized by such creditor with respect to such property shall be treated (for purposes of ch. 1 of the code) as a payment on account of such indebtedness, and that any loss with respect to such property shall be treated as a bad debt to which the provisions of section 166 apply.

Basis

Subsection (c) of the new section 595 provides that the basis of any property acquired in a transaction to which subsection (a) applies shall be the basis of the indebtedness for which such property was security, determined as of the date of the acquisition of such property, properly increased for any costs of acquisition.

Regulatory authority

Subsection (d) of the new section 595 provides that the Secretary of the Treasury or his delegate shall prescribe such regulations as he may deem necessary to carry out the purposes of this section.

(c) *Definition of a domestic building and loan association.*—Subsection (c) of section 6 amends section 7701(a)(19) of the code to provide a new definition of the term “domestic building and loan association.” As amended by your committee, paragraph (19) of section 7701(a) defines this term to mean any domestic building and loan association, domestic savings and loan association, or Federal savings and loan association, which meets each of the requirements prescribed by subparagraphs (A) through (E) of such paragraph. For purposes of convenience, such associations are hereinafter referred to as “domestic savings associations.”

Subparagraph (A) of paragraph (19) provides that the domestic savings association must be either an insured institution within the meaning of section 401(a) of the National Housing Act (12 U.S.C., sec. 1724(a)), or subject by law to supervision or examination by State or Federal authority having supervision over such associations. The “insured institutions” referred to are those the accounts of which are insured by the Federal Savings and Loan Insurance Corporation.

Subparagraph (B) thereof requires that substantially all the business of the domestic savings association consist of acquiring the savings of the public and investing in loans described in subparagraph (C). Thus, even though such an association otherwise meets the asset requirements imposed by subparagraphs (C), (D), (E), and (F) of paragraph (19), it will nevertheless not qualify as a domestic building and loan association if more than an insubstantial portion of its business consists of, for example, mortgage or insurance brokerage activities.

Subparagraph (C) of paragraph (19) requires that at least 90 percent of the amount of the total assets of a domestic savings association must consist of (i) cash (including time or demand deposits with, or withdrawable accounts in, other financial institutions), (ii) obligations of the United States or of a State or political subdivision thereof, and stock or obligations of a corporation which is an instrumentality of the United States, or of a State or political subdivision thereof, (iii) loans secured by an interest in real property and loans made for the improvement of real property, (iv) loans secured by a deposit or share of a member of such association, and (v) property acquired through the liquidation of defaulted loans which are secured by an interest in real property or which are made for the improvement of such property. In determining whether the percentage requirements imposed by paragraph (19) are met, the amount of each item included in the amount of total assets of a domestic savings association shall be measured by the adjusted basis of such item, as determined under section 1011 (relating to the adjusted basis

for determining gain or loss), or by such other method as is in accordance with sound accounting principles.

Subparagraph (D) of paragraph (19) provides that, of the assets which are taken into account by the taxpayer under subparagraph (C) as assets constituting the 90 percent of total assets, at least 80 percent of such 90 percent must consist of (1) cash and governmental obligations described in clauses (i) and (ii) of subparagraph (C), and (2) loans secured by an interest in real property which is (or, from the proceeds of the loan, will become) residential real property, or of loans which are made for the improvement of such residential real property. Subparagraph (D) further provides that at least 70 percent of such 90 percent must consist of (1) cash and governmental obligations described in clauses (i) and (ii) of subparagraph (C), and (2) loans secured by an interest in real property which is (or, from the proceeds of the loan, will become) residential real property containing four or fewer family units, or of loans made for the improvement of residential real property containing four or fewer family units.

Subparagraph (E) of paragraph (19) provides that not more than 18 percent of the total assets of the taxpayer may consist of assets other than those described in clause (i) of subparagraph (D) (cash, certain Government obligations, and loans secured by an interest in improved residential real property); and not more than 27 percent of the total assets of the taxpayer may consist of assets other than those described in clause (ii) of subparagraph (D) (cash, certain Government obligations, and loans secured by one- to four-family residential real property). However, the 18- and 27-percent limitations contained in this subparagraph shall be increased by the number, if any, of percentage points (including any fraction of a percentage point) by which 10 percent exceeds the percentage of the total assets consisting of assets described in clauses (i) and (ii) of subparagraph (C) (cash and certain governmental obligations). Thus, a mutual savings institution may not have more than 18 percent of its total assets in commercial loans, nor more than 27 percent of its total assets in commercial loans and loans secured by apartment buildings, except to the extent its cash and governmental obligations constitute less than 10 percent of its assets.

Subparagraph (F) of paragraph (19) provides that none of the assets of a domestic savings association may be invested in the stock of any corporation, other than stock of a corporation which is an instrumentality of the United States or of a State or political subdivision thereof, stock acquired through the liquidation of a defaulted loan which was secured by an interest in real property or made for the improvement of real property, or stock representing a withdrawable account in another financial institution.

(d) *Clerical amendments.*—Subsection (d) of section 6 contains clerical amendments.

(e) *Repeal of exemption from certain excise taxes.*—Under section 5(h) of the Home Owner's Loan Act of 1933 (48 Stat. 132; 12 U.S.C., sec. 1464(h)), Federal savings and loan associations are exempted from Federal taxes other than payroll taxes and income, war profits, and excess profits taxes, the legal incidence of which would fall upon such associations. Thus, under existing law Federal savings and loan associations are not subject to the excise taxes which sections 4251 and 4261 of the code impose, respectively, on communications and the transportation of persons. Subsection (d) of this section of the

bill as passed by the House eliminated the exemption which section 5(h) of the Home Owner's Loan Act accorded those associations with respect to the taxes imposed by sections 4251 and 4261. Paragraph (1) of subsection (e) of this section of the bill, as reported by your committee, amends section 5(h) of the Home Owner's Loan Act so as to eliminate entirely the exemption from Federal taxes which that section now provides in the case of Federal savings and loan associations.

Under section 4382(a)(2) of the code, capital stock and certificates of indebtedness issued by domestic building and loan associations (as defined in sec. 7701(a)(19)) and cooperative banks are exempt from the documentary stamp taxes imposed by chapter 34 of the code. Your committee has added a new paragraph (2) to section 6(e) of the bill which eliminates this exemption insofar as it extends (i) to all certificates of indebtedness (as defined in sec. 4381(a)) issued by a domestic building and loan association or cooperative bank, and (ii) to shares or certificates of stock issued by such a domestic building and loan association or cooperative bank with respect to which any distribution of property (as defined in sec. 317(a)) is not allowable as a deduction under section 591. Thus, your committee's amendment of section 4382(a)(2) continues the exemption which that section provides in the case of shares or certificates of stock issued by such associations or banks and representing deposits or withdrawable accounts, as well as the exemption which it provides in the case of all shares or certificates of stock and certificates of indebtedness issued by mutual ditch or irrigation companies. As used in section 6(e)(2) of the bill, the term "domestic building and loan association" includes homestead associations which qualify under the amended definition of domestic building and loan associations contained in section 6(c) of the bill.

(f) *Deduction for dividends or interest paid on deposits.*—Subsection (f) of section 6 of the bill, which has been added by your committee, amends section 591 of existing law by providing that—in addition to mutual savings banks, cooperative banks, and domestic building and loan associations—savings institutions chartered and supervised as savings and loan associations or similar associations under Federal or State law shall be allowed as a deduction in computing taxable income amounts paid to, or credited to the accounts of, depositors or holders of accounts as dividends or interest on their deposits or withdrawable accounts, if such amounts paid or credited are withdrawable on demand subject only to customary notice of intention to withdraw. Thus, even though an association chartered and supervised as a savings and loan or similar association under Federal or State law may not qualify as a domestic building and loan association as defined in section 7701(a)(19), as amended, your committee's amendment will insure the deductibility of dividends or interest paid on such withdrawable accounts or deposits.

(g) *Effective dates.*—Subsection (g) of section 6 of the bill provides effective dates for subsections (a), (b), (c), and (e) of section 6 of the bill.

Paragraph (1) of section 6(g) of the bill provides that the amendments made by section 6(a) of the bill (which amends sec. 593 of existing law) shall apply to taxable years ending after December 31, 1962, except that section 593(f) of the code shall apply to distributions made after December 31, 1962, in taxable years ending after such date.

Paragraph (2) of section 6(g) of the bill provides that the amendments made by section 6(b) of the bill (which adds a new sec. 595) shall apply to transactions described in section 595(a) of the code occurring after December 31, 1962, in taxable years ending after such date.

Paragraph (3) of section 6(g) of the bill provides that the amendment made by section 6(c) of the bill (which amends section 7701(a) (19) of existing law) shall apply to taxable years beginning after the date of the enactment of the bill.

Paragraph (4) of section 6(g) of the bill, as amended by your committee, provides that subsection (e) of the bill shall become effective on January 1, 1963, except that, in the case of the tax imposed by section 4251 of the code, subsection (e) shall apply only with respect to amounts paid pursuant to bills rendered after December 31, 1962; and, in the case of the tax imposed by section 4261 of the code, subsection (e) shall apply only with respect to transportation beginning after December 31, 1962.

SECTION 7. DISTRIBUTIONS BY FOREIGN TRUSTS

This section is the same as section 9 of the bill as passed by the House, with two exceptions. First, your committee has changed the definition of the term "foreign trust created by a U.S. person" so that a foreign trust will come within the definition only to the extent of money or property (including accumulated earnings therefrom) transferred to the trust by a U.S. person or under the will of a U.S. citizen or resident. Second, a change has also been made in the effective date provision to provide that the amendments made by the bill shall apply to distributions made after the date of enactment of the bill.

(a) *Definitions.*—Section 7(a) of the bill amends section 643 of the 1954 Code (definitions relating to the income of estates and trusts) in the following respects:

Modification of distributable net income.—Section 7(a)(1) of the bill amends section 643(a) (relating to modifications taken into account in computing distributable net income) in two respects. First, a new subparagraph (B) is added to section 643(a)(6) to provide that the gross income of a foreign trust from sources within the United States is to be determined without regard to section 894 (relating to income exempt under treaty). A further amendment is made to section 643(a)(6) by the addition of a new subparagraph (C). The new section 643(a)(6)(C) provides that section 643(a)(3) (relating to capital gains and losses) is not to apply to a "foreign trust created by a U.S. person," as defined in section 643(d). In lieu of the rules provided by section 643(a)(3), the new subparagraph (C) provides that there is to be included in distributable net income gains from the sale or exchange of capital assets, reduced by losses from such sales or exchanges to the extent such losses do not exceed gains from such sales or exchanges. The new subparagraph (C) also provides that the deduction under section 1202 (relating to deduction for excess of capital gains over capital losses) is not to be taken into account. Existing section 643(a)(3) will continue to apply to trusts other than foreign trusts created by U.S. persons.

Foreign trusts created by U.S. persons

Section 7(a)(2) of the bill adds a new subsection (d) to section 643 of the 1954 Code. The new section 643(d) provides that, for purposes of part I of subchapter J (relating to estates, trusts, and beneficiaries), the term "foreign trust created by a U.S. person" means the portion of a foreign trust (as defined in sec. 7701(a)(31)) attributable to money or property transferred to it directly or indirectly by a U.S. person (as defined in sec. 7701(a)(30)), or under the will of a decedent who at the date of his death was a U.S. citizen or resident, and including all accumulated earnings, profits, or gains attributable to such money or property. A foreign trust, created by a person who is not a U.S. person, to which a U.S. person transfers money or property would under this definition be in part a foreign trust created by a U.S. person.

(b), (c), and (d) *Modification of throwback.*—Subsections (b) through (d) of section 7 of the bill make various amendments designed to modify the so-called throwback provisions of the code in their application to certain foreign trusts.

Existing law

Under existing law the so-called throwback provisions of subchapter J operate substantially as follows: When a beneficiary receives as a distribution an amount in excess of current distributable net income, and the distribution exceeds \$2,000, it is called an accumulation distribution. The beneficiary is taxed on this amount to the extent there was undistributed net income of the trust in any of the preceding 5 years, the undistributed net income of such prior years being taken into account in inverse order. Undistributed net income consists of undistributed distributable net income for a taxable year, minus the taxes on the trust attributable to such undistributed amount. The beneficiary is also required to include in gross income an appropriate portion of the U.S. income taxes, if any, imposed on the trust with respect to the undistributed net income, but he receives a tax credit based on the taxes the trust would not have had to pay if the undistributed distributable net income had actually been paid to the beneficiary.

Although under section 668(a) the beneficiary is taxable currently on the entire distribution, as well as on the taxes on the trust allocable to that amount, the tax attributable to the distribution cannot exceed the tax he would have paid had the distribution been paid to him on the last day of each of the preceding taxable years to the extent the undistributed net income of each of those years is considered absorbed by the distribution. The taxes deemed distributed to him are similarly spread back.

Under existing law, however, as noted, the throwback rule does not operate with respect to distributions made out of accumulations for taxable years before the fifth year preceding the taxable year. In addition, there are certain exceptions to what may be taken into account in determining whether there has been an accumulation distribution, e.g., a distribution out of accumulations for a minor, or a final distribution of the trust made to a beneficiary more than 9 years after the date of the last transfer to the trust.

Modification of accumulation distribution

Section 7(b)(1) of the bill amends section 665(b) (relating to the definition of accumulation distribution) to limit the application of

such definition to trusts other than foreign trusts created by U.S. persons. A new section 665(c), added by section 7(b)(2) of the bill, provides a definition of accumulation distribution for foreign trusts created by U.S. persons. Under this new definition, a distribution in excess of current distributable net income constitutes an accumulation distribution whether or not the distribution exceeds \$2,000. In addition, there are no exceptions to what is taken into account in determining whether there has been an accumulation distribution. Thus, any distribution in excess of current distributable net income will, under the new section 665(c), be an accumulation distribution.

The last sentence of section 665(c) provides that any amount paid to a U.S. person which is from a payor who is not a U.S. person, and which is derived directly or indirectly from a foreign trust created by a U.S. person, is to be deemed in the year of payment to have been directly paid by the foreign trust. Thus, if a nonresident alien receives a distribution from a foreign trust created by a U.S. person and he then pays the amount of the distribution over to a U.S. person, the payment of such amount to the U.S. person represents an accumulation distribution to the U.S. person from such trust, to the extent that the amount received would have been an accumulation distribution had the trust paid the amount directly to the U.S. person. An example of a payment indirectly derived by a nonresident alien from such a foreign trust would be where the trust distributes to a foreign trust which was not created by a U.S. person, and which latter foreign trust makes a distribution to the nonresident alien. In this case, the payment over to a U.S. person is considered to have been made from the initial and not from the intervening trust. The same result would obtain if the intervening trust were a foreign trust created by a U.S. person. However, even if a payment is made to a U.S. person by a person who is not a U.S. person and who directly or indirectly derived the amount paid from a foreign trust created by a U.S. person, the receipt of the amount by the U.S. person is not considered the receipt of an accumulation distribution from a trust if the amount is received under circumstances indicating lack of intent on the part of the parties to circumvent the purposes of section 7 of the bill.

Other modifications of the throwback rule

The restriction of the throwback rule to the 5 preceding taxable years of the trust is removed by section 7(c)(2) of the bill for foreign trusts created by a U.S. person. However, this unlimited throwback will operate only for years governed by the 1954 Code.

Section 7(d) of the bill adds a new sentence to section 668(a) (relating to amounts treated as received in prior taxable years). In the case of a U.S. person who is a beneficiary of a foreign trust created by a U.S. person, this sentence conditions the availability of the limitation on tax provided by section 668(a) on a beneficiary's meeting the information requirements of new section 669(b), added by section 7(e) of the bill.

The provisions of subchapter J which remain unchanged by the bill will continue to apply as under existing law. Thus, the credit allowed to a beneficiary by section 668(b) for U.S. income taxes paid by the trust, and the credit against tax for taxes imposed by foreign countries will continue to be available.

(e) *Limitation on tax.*—Section 7(e) of the bill adds a new section 669 to subpart D of part 1 of subchapter J of chapter 1 (relating to treatment of excess distributions by trusts).

SECTION 669. SPECIAL RULES APPLICABLE TO CERTAIN FOREIGN TRUSTS

Section 669 provides that a beneficiary who is a U.S. person and who satisfies certain additional requirements may elect between two methods of computing the limitation on tax attributable to an accumulation distribution received from a foreign trust created by a U.S. person. These two methods are in addition to the method available to the beneficiary of computing his tax in the ordinary way by including in income the entire amount of an accumulation distribution when it is paid, credited, or required to be distributed. The additional requirements referred to which must be satisfied by the beneficiary are those provided in section 669(b), relating to the furnishing of certain information by the beneficiary with respect to the operation and accounts of the trust. Information may be required to be furnished for each taxable year of the trust on the last day of which an amount is deemed distributed by the trust under section 666(a). The nature and extent of the information required is to be determined by regulations prescribed by the Secretary of the Treasury or his delegate.

First method of limiting tax

As noted above, section 669(a) provides for an election by the beneficiary as between two methods of computing the limitation on tax attributable to the receipt of an accumulation distribution. The first method is the one provided by existing law, and which is now contained in the next to the last sentence of section 668(a). However, section 669(a)(2)(B) provides that this method may not be elected if the beneficiary was not alive on the last day of each preceding taxable year of the trust with respect to which a distribution is deemed made under section 666(a). Thus, if a portion of an amount received as an accumulation distribution was accumulated by the trust during years when the beneficiary was unborn, the beneficiary is not permitted to elect the limitation on tax provided by section 669(a)(1)(A).

Second method of limiting tax

The second method of limiting tax is provided by section 669(a)(1)(B). Under this method the beneficiary's gross income for the taxable year in which the accumulation distribution is paid, credited, or required to be distributed to him (determined without regard to the inclusion in income required by section 668(a) of any amount other than pursuant to section 669(a)(1)(B)) and for each of his 2 taxable years immediately preceding such year is recomputed solely for purposes of determining the limitation on the beneficiary's tax for the current year. The income for each of such 3 years is recomputed by adding thereto an amount determined by dividing the amount required to be included in income under section 668(a) by the number of preceding taxable years of the trust on the last day of each of which an amount is deemed under section 666(a) to have been distributed. There is then computed the increase in tax for each of such 3 years attributable to the increased amount of gross income. The aggregate of the increases in tax for such 3 years is divided by 3 to arrive at an

average increase in tax for such 3 years. This average increase in tax, multiplied by the number of preceding taxable years of the trust from the income of which the distribution is made, is the limitation on the beneficiary's tax liability (before the application of any credit for taxes paid by the trust allowed by sec. 668(b)) with respect to the accumulation distribution.

The computation made under the alternate election provided by section 669(a)(1)(B) is modified in two cases. When an accumulation distribution is deemed under section 666(a) to have been distributed on the last day of less than 3 taxable years of the trust, the taxable years of the beneficiary for which a recomputation is made under section 669(a)(1)(B) is limited to the number of years to which section 666(a) applies, commencing with the most recent taxable year of the beneficiary. Also, no recomputation of gross income is to be made for a beneficiary for a taxable year for which he was not alive on the last day thereof; and if the beneficiary has no preceding taxable year, the recomputation of gross income is made on the basis of his taxable year without regard to the inclusion in income required by section 668(a) of any amount other than pursuant to section 669(a)(1)(B).

The application of the preceding paragraph may be illustrated by the following examples: Assume that a foreign trust created by a U.S. person accumulates \$3,000 of income for one year and \$7,000 for a second year and then distributes the accumulated income on January 1, 1965, to a beneficiary who is a U.S. person. The limitation on tax computed under section 669(a)(1)(B) would be determined by recomputing the beneficiary's gross income for 1964 and 1965 by adding \$5,000 to each year. If the same distribution were made to an infant who was born in 1965, the limitation on tax would be computed by adding \$5,000 to his gross income for such year. The resulting increase in tax would be multiplied by 2 to arrive at the limitation on the increase in his tax for 1965 attributable to such distribution.

Effect of prior election

Section 669(a)(3) provides special rules which have application when a beneficiary who is a U.S. person receives a second or succeeding accumulation distribution from a foreign trust created by a U.S. person.

If a beneficiary has elected the limitation on tax provided by section 669(a)(1)(B) (the second method described herein) with respect to an accumulation distribution, and with respect to a subsequent accumulation distribution he desires to elect the limitation on tax provided by section 669(a)(1)(A) (the method provided by existing law), for purposes of computing the limitation on tax with respect to the subsequent accumulation distribution the income of any year with respect to which an amount is deemed distributed to a beneficiary under section 666(a) is to include amounts previously deemed distributed to such beneficiary for such year as a result of an accumulation distribution with respect to which an election under section 669(a)(1)(B) was made. The result of this rule is to require that for the purposes of computing the limitation on tax under section 669(a)(1)(A) with respect to an accumulation distribution, all previous elections are considered to have been made under section 669(a)(1)(A).

A special rule is also provided by section 669(a)(3) regardless of the limitation on tax elected with respect to a prior accumulation distribution when, with respect to a subsequent accumulation distribution, the limitation on tax provided by section 669(a)(1)(B) is elected by the beneficiary. When this occurs the number of preceding taxable years of the trust with respect to which an amount is deemed distributed to a beneficiary under section 666(a) is to be determined without regard to any such year with respect to which an amount was previously deemed distributed to such beneficiary.

(f) *Requirement of information return.*—Section 7(f) of the bill amends subpart B of part III of subchapter A of chapter 61 (relating to information concerning transactions with other persons) by adding a new section 6047.

SECTION 6047. RETURNS AS TO CREATION OF OR TRANSFERS TO CERTAIN FOREIGN TRUSTS

Section 6047 provides for the filing of an information return on or before the 90th day after the creation of any foreign trust by a U.S. person or after the transfer of any money or property to a foreign trust by a U.S. person. The return is to be in such form and is to set forth, in respect of the foreign trust, such information as the Secretary of the Treasury or his delegate prescribes by regulation as necessary for carrying out the provisions of the income tax laws. The return is required to be filed by the grantor in the case of an inter vivos trust, the fiduciary of an estate in the case of a testamentary trust, or by the transferor to a foreign trust, as the case may be.

(g) *Penalty for failure to file return.*—Section 7(g) of the bill amends subchapter B of chapter 68 (relating to assessable penalties) by adding a new section 6677.

SECTION 6677. FAILURE TO FILE INFORMATION RETURNS WITH RESPECT TO CERTAIN FOREIGN TRUSTS

Section 6677(a) provides that, in addition to any criminal penalty provided by law (such as the penalty provided by sec. 7203 for willful failure to file a return), any person required to file a return under section 6047 who fails to file such return at the time provided in such section, or who files a return which does not show the information required pursuant to such section, is to pay a penalty equal to 5 percent of the amount transferred to a trust, but not more than \$1,000, unless it is shown that such failure is due to reasonable cause.

Section 6677(b) provides that the assessment or collection of any penalty imposed by section 6677(a) is not to be subject to the deficiency procedures provided by subchapter B of chapter 63 of the code.

(h) *Definitions.*—Section 7(h) of the bill amends section 7701(a) (relating to definitions) by adding paragraphs (30) and (31). Paragraph (30) defines the term "U.S. person" to mean an individual who is a citizen or resident of the United States; a domestic partnership; a domestic corporation; and any estate or trust (other than a foreign estate or foreign trust, within the meaning of sec. 7701(a)(31)). Paragraph (31) defines the terms "foreign estate" and "foreign trust" to mean an estate or trust, as the case may be, the income of which from sources without the United States is not includible in gross income under subtitle A of the code (relating to income taxes).

(i) *Technical amendments.*—Section 7(i) of the bill amends the tables of sections where necessary to reflect the addition of the new sections added by the bill.

(j) *Effective date.*—The amendments made by section 7 of the bill (other than by subsecs. (f), (g), and (h)) are to apply with respect to distributions made after the date of the enactment of the bill. The amendments made by subsections (f), (g), and (h) will take effect on such date of enactment.

SECTION 8. MUTUAL INSURANCE COMPANIES (OTHER THAN LIFE, MARINE, AND CERTAIN FIRE OR FLOOD INSURANCE COMPANIES), ETC.

(a) *Imposition of tax.*—Subsection (a) of section 8 of the bill, which corresponds to subsection (a) of section 10 of the bill as passed by the House, amends the heading and table of sections for part II of subchapter L of chapter 1 of the 1954 Code to conform them to the substantive changes made by the bill. In addition, subsection (a) in effect strikes out existing section 821 of the code and substitutes a new section 821, relating to the tax on mutual insurance companies to which part II applies.

SECTION 821. TAX ON MUTUAL INSURANCE COMPANIES TO WHICH PART II APPLIES

(a) *Imposition of tax.*—Subsection (a) of the new section 821 provides the general rule for taxing mutual insurance companies (including interinsurers and reciprocal underwriters). The tax will not apply to a mutual life insurance company, or to a mutual marine or mutual fire or flood insurance company subject to the tax imposed by section 831 of the 1954 Code. In addition, the tax will not apply if the alternative tax imposed by the new section 821(c) (relating to alternative tax for certain small companies) applies. Also, under subsection (d) of section 8 of the bill as amended by your committee, mutual insurance companies (other than life or marine) whose gross receipts (not including capital gains) for the taxable year do not exceed \$150,000 will be exempt from tax under section 501(c)(15) of the 1954 Code.

The tax imposed by the new section 821(a) applies to each taxable year beginning after December 31, 1962. The tax is to consist of—

(1) a normal tax—

(A) in the case of taxable years beginning before July 1, 1963, of 30 percent of the mutual insurance company taxable income, or 60 percent of the amount by which such taxable income exceeds \$6,000, whichever is the lesser; and

(B) in the case of taxable years beginning after June 30, 1963, of 25 percent of the mutual insurance company taxable income, or 50 percent of the amount by which such taxable income exceeds \$6,000, whichever is the lesser; plus

(2) a surtax of 22 percent of the mutual insurance company taxable income (computed without regard to the deduction provided in section 242 for partially tax-exempt interest) in excess of \$25,000.

Under existing law a mutual insurance company which is subject to the tax on investment income only is exempt from tax if its mutual

insurance company taxable income does not exceed \$3,000. Similarly, existing law provides special notch relief if such a company has mutual insurance company taxable income between \$3,000 and \$6,000. Under the bill, companies having mutual insurance company taxable income (as defined in the new sec. 821(b)) which does not exceed \$6,000 will be exempt from tax, and the special notch provision will apply if the company has mutual insurance company taxable income between \$6,000 and \$12,000.

(b) *Mutual insurance company taxable income defined.*—Subsection (b) of the new section 821 defines the term “mutual insurance company taxable income” for purposes of part II of subchapter L. Under this definition, mutual insurance company taxable income means the amount by which—

(1) the sum of—

(A) the taxable investment income (as defined in sec. 822(a)(1)),

(B) the statutory underwriting income (as defined in sec. 823(a)(1)), and

(C) the amounts required by section 824(d) to be subtracted from the protection against loss account, exceeds

(2) the sum of—

(A) the investment loss (as defined in sec. 822(a)(2)), if any,

(B) the statutory underwriting loss (as defined in sec. 823(a)(2)), if any, and

(C) the unused loss deduction provided by section 825(a).

If for any taxable year the amount determined under paragraph (2) of the new section 821(b) exceeds the amount determined under paragraph (1) of the new section 821(b), the mutual insurance company taxable income shall be zero.

(c) *Alternative tax for certain small companies.*—Paragraph (1) of the new section 821(c) provides an alternative tax which is in lieu of the tax imposed by section 821(a) for taxable years beginning after December 31, 1962. Except as provided in section 821(c)(3)(B), this tax applies in the case of every mutual insurance company described in section 821(c)(3)(A) and consists of—

(1) a normal tax—

(A) in the case of taxable years beginning before July 1, 1963, of 30 percent of the taxable investment income, or 60 percent of the amount by which such taxable income exceeds \$3,000, whichever is the lesser; and

(B) in the case of taxable years beginning after June 30, 1963, of 25 percent of the taxable investment income, or 50 percent of the amount by which such taxable income exceeds \$3,000, whichever is the lesser; plus

(2) a surtax of 22 percent of the taxable investment income (computed without regard to the deduction provided in sec. 242 for partially tax-exempt interest) in excess of \$25,000.

Thus, paragraph (1) of the new section 821(c) provides, in effect, that certain small mutual insurance companies shall be taxed at regular corporate rates on taxable investment income only. Under the bill, such companies will continue to be taxed the same as under present law, except that the alternative 1-percent tax will not apply. Accordingly, if such a company has taxable investment income of less than \$3,000, it is not subject to tax, and if the taxable investment income

is between \$3,000 and \$6,000, it is entitled to special notch relief. Unless such a company makes an election to be taxed under section 821(a), its underwriting gains or losses will not be taken into account for purposes of determining its tax liability.

Paragraph (2) of the new section 821(c), like section 821(c) of existing law, provides a special tax reduction for companies subject to tax under section 821. Your committee's amendments, however, provide for larger dollar amounts. Thus, if the gross amount received during the taxable year from the items described in section 822(b) (other than par. (1)(D) thereof) and premiums (including deposits and assessments) is over \$150,000 but less than \$250,000, the tax otherwise computed under paragraph (1) of section 821(c) is reduced to an amount which bears the same proportion to such tax as the excess over \$150,000 bears to \$100,000. Under the bill as passed by the House, if the gross amount received during the taxable year from items described in section 822(b) (other than par. (1)(D) thereof) and premiums (including deposits and assessments) was over \$75,000 but less than \$125,000, the tax otherwise computed under paragraph (1) of section 821(c) was reduced to an amount which bore the same proportion to such tax as the excess over \$75,000 bore to \$50,000. However, this special relief provision is to apply only to companies which are subject to the tax imposed by the new section 821(c) and is not to apply in the case of companies which are subject to the tax imposed by the new section 821(a).

Subparagraph (A) of the new section 821(c)(3) provides that, except as provided by section 821(c)(3)(B), every mutual insurance company (other than a life insurance company and other than a fire or flood or marine insurance company subject to the tax imposed by sec. 831) is to be subject to the tax imposed by section 821(c) if the gross amount received during the taxable year from the items described in section 822(b) (other than par. (1)(D) thereof) and premiums (including deposits and assessments) exceeds \$150,000 but does not exceed \$600,000. The \$150,000 and \$600,000 are amounts increased by your committee's amendments from amounts of \$75,000 and \$300,000, respectively, in the bill as passed by the House.

Subparagraph (B) of the new section 821(c)(3) provides that a mutual insurance company described in section 821(c)(3)(A) shall not be subject to the alternative tax imposed by section 821(c)(1) for the taxable year if there is in effect for the taxable year an election made by such company under section 821(d) to be taxable under section 821(a), or if there is any amount in the protection against loss account of such company at the beginning of the taxable year. Where the alternative tax treatment for certain small companies does not apply by reason of there being an amount in the protection against loss account at the beginning of the taxable year, the bill provides that an election may be made to subtract such amount from the protection against loss account as of the close of the preceding taxable year. (See sec. 824(d)(5).)

(d) *Election to include statutory underwriting income or loss.*—Paragraph (1) of the new section 821(d) provides that any mutual insurance company which is subject to the tax imposed by section 821(c) may elect to be subject to the tax imposed by section 821(a). Paragraph (2) provides that if the company makes such an election it shall be subject to the tax imposed by section 821(a) for the first taxable year for which the election is made and for all taxable years thereafter

unless the Secretary of the Treasury or his delegate consents to a revocation of such election. Under the bill, it is not intended to permit such companies an annual election to be taxed either under subsection (a) or (c) of the new section 821. However, there may be some situations where because of a substantial change in the character of the taxpayer's operations there would be an undue burden or material hardship if such taxpayer were not permitted to revoke its prior election. Under such circumstances, the bill provides that the election may be revoked with the consent of the Secretary of the Treasury or his delegate. If, however, for any taxable year for which the election would otherwise apply, the gross amount received by the company during the taxable year from the items described in section 822(b) (other than par. (1)(D) thereof) and premiums (including deposits and assessments) does not exceed \$150,000, such election will terminate automatically. Thus, if for any taxable year after such a termination such a company has gross receipts from such sources of over \$150,000 but not more than \$600,000, it shall be subject to tax under section 821(c) unless it makes a new election to be taxed under section 821(a).

(e) *No U.S. insurance business.*—Subsection (e) of the new section 821 is identical with section 821(d) of existing law and provides that foreign mutual insurance companies (other than a life insurance company and other than a fire, flood, or marine insurance company subject to the tax imposed by sec. 831) not carrying on an insurance business within the United States are not to be subject to tax under part II of subchapter L but shall be taxable as other foreign corporations. (See sec. 881 of the code.)

(f) *Special transitional underwriting loss.*—Paragraph (1) of this subsection, for which there is no corresponding provision in the bill as passed by the House, provides a special transitional rule for determining the mutual insurance company taxable income of every mutual insurance company which has been subject to the tax imposed by this section (as in effect before enactment of this subsection) for the 6 taxable years immediately preceding January 1, 1963, and which has incurred an underwriting loss for at least 5 of such 6 taxable years.

Paragraph (2) of the new section 821(f) provides, for purposes of this part, that the mutual insurance company taxable income for the taxable year of a company described in paragraph (1) shall be the mutual insurance company taxable income for the taxable year (determined without regard to this subsection) reduced by the amount by which—

(A) the sum of the underwriting losses of such company for the 6 taxable years prior to January 1, 1963, reduced by the underwriting gain during such years, exceeds

(B) the total amount by which the mutual insurance company taxable income was reduced by reason of this subsection in prior taxable years.

Paragraph (3) of the new section 821(f) provides that for purposes of this subsection the term "underwriting loss" means the statutory underwriting loss, computed without any deduction under section 824(a), and that the term "underwriting gain" means statutory underwriting income, computed without any deduction under section 823(c) or any deduction under section 824(a).

Paragraph (4) of the new section 821(f) provides that this subsection shall only apply with respect to taxable years beginning after Decem-

ber 31, 1962, and before January 1, 1968, for which the taxpayer is subject to the tax imposed by section 821(a).

(g) *Cross-references*.—Subsection (g) of the new section 821, corresponding to subsection (f) of the bill as passed by the House, contains cross-references to section 501(c)(15) of the code (relating to exemption from tax of certain mutual insurance companies) and section 1201(a) (relating to alternative tax in case of capital gains).

SECTION 8. MUTUAL INSURANCE COMPANIES (OTHER THAN LIFE, MARINE, AND CERTAIN FIRE OR FLOOD INSURANCE COMPANIES), ETC. (Continued)

(b) *Taxable investment income*.—Subsection (b) of section 8 of the bill, which corresponds to subsection (b) of section 10 of the bill as passed by the House, contains technical amendments to sections 822 and 823 of the code. These amendments, in effect, retain the existing substantive provisions of section 822 but change the designation of the excess of gross investment income (as defined in sec. 822(b)) over gross investment deductions (as provided in sec. 822(c)) from “mutual insurance company taxable income” to “taxable investment income.”

Subsection (b)(1) of section 8 of the bill changes the heading of section 822 to refer to taxable investment income and amends section 822(a) to define the terms “taxable investment income” and “investment loss” for purposes of part II of subchapter L. The investment loss is the excess of gross investment deductions over gross investment income.

Subsection (b)(2) of section 8 of the bill amends section 822(c) of the code (relating to deductions) and section 822(e) of the code (relating to foreign mutual insurance companies) by striking out the term “mutual insurance company taxable income” each place it appears and inserting in lieu thereof the term “taxable investment income”. This amendment conforms to the amendment to section 822(a).

Subsection (b)(3) of section 8 of the bill amends section 822(c)(7) of the code (relating to special deductions) and provides that for purposes of paragraph (7) of section 822(c), in applying section 246(b) (relating to limitation on aggregate amount of deductions for dividends received), the reference in section 246(b) to “taxable income” is to be treated as a reference to “taxable investment income.”

Subsection (b)(4) of section 8 of the bill redesignates section 823 of the code (relating to other definitions) as subsection (f) of the new section 822.

(c) *Statutory underwriting income or loss*.—Subsection (c) of section 8 of the bill, which corresponds to subsection (c) of section 10 of the bill as passed by the House, adds (after sec. 822(f), as redesignated by subsec. (b)(4) of sec. 8 of the bill) a new section 823, relating to determination of statutory underwriting income or loss, and a new section 824, relating to adjustments to provide protection against losses.

SECTION 823. DETERMINATION OF STATUTORY UNDERWRITING INCOME OR LOSS

(a) *In general*.—Paragraph (1) of the new section 823(a) defines the term “statutory underwriting income” for purposes of part II

of subchapter L. Under this definition, statutory underwriting income is the amount by which—

(1) the gross income which would be taken into account in computing taxable income under section 832 if the taxpayer were subject to the tax imposed by section 831, reduced by the gross investment income (as determined under sec. 822(b)), exceeds

(2) the sum of—

(A) the deductions which would be taken into account in computing taxable income if the taxpayer were subject to the tax imposed by section 831, reduced by the deductions provided in section 822(c) (relating to deductions in computing taxable investment income), plus

(B) the deductions provided in subsection (c) of the new section 823 (relating to special deduction for small company having gross amount of less than \$1,200,000) and in section 824(a) (relating to deduction to provide protection against losses).

Thus, generally, the income of a company subject to tax under section 821(a) will be derived from the income as computed if it were subject to tax under section 831. For example, under existing law, mutual fire and casualty insurance companies must annually accrue all market discount attributable to the taxable year on bonds or securities which they hold. (See sec. 822(d)(2).) For purposes of computing taxable investment income this rule will continue to apply. However, since in computing statutory underwriting income, taxable investment income is subtracted from income determined as if the company were subject to tax under section 831, and since market discount is not required to be annually accrued by companies subject to the tax imposed by section 831, the effect is to understate what would otherwise be the statutory underwriting income by an amount equal to the amount of such accrual. Accordingly, the net effect under the bill, is that mutual fire and casualty insurance companies subject to the tax imposed under section 821(a) will treat market discount in the same manner as such item is presently treated in the case of a company subject to tax under section 831. In the case of a company subject to tax under section 831, any income attributable to market discount is subject to capital gains treatment at such time as the bond is sold or redeemed.

Paragraph (2) of the new section 823(a) provides that, for purposes of part II of subchapter L, the term “statutory underwriting loss” means the amount by which the amount referred to in paragraph (1)(B) of the new section 823(a) exceeds the amount referred to in paragraph (1)(A) of the new section 823(a).

Paragraphs (1) and (2) of the new section 823(a) provide, in effect, that for purposes of determining statutory underwriting income or loss for the taxable year a mutual insurance company subject to the tax imposed by section 821(a) must first take into account the same gross income and deduction items (except as modified by sec. 823(b)) as a taxpayer subject to tax under section 831 would take into account for purposes of determining its taxable income under section 832. These items are then reduced to the extent that they include amounts which are included in determining taxable investment income under section 822(a). In addition, the taxpayer is allowed a deduction for

the amount determined under section 824(a) (relating to deduction to provide protection against losses) and, in the case of a company having gross receipts of less than \$1,200,000, an additional deduction equal to the amount determined under section 823(c)(1), after the application of the limitation provided in section 823(c)(2).

(b) *Modifications.*—Subsection (b) of the new section 823 provides certain modifications to the general rule for determining statutory underwriting income or loss contained in section 823(a). Paragraph (1) of section 823(b) provides that for purposes of applying section 823(a), the deduction for net operating losses provided by section 172 is not to be allowed. (However, a company is allowed an unused loss deduction under the provisions of sec. 825.) Paragraph (2) of the new section 823(b) provides a special rule which applies in the case of an interinsurer or reciprocal underwriter which is subject to the tax imposed by section 821(a). This rule provides that if such a company, before the 16th day of the 3d month following the close of the taxable year, credits the individual account of each of its subscribers with an amount, representing savings to subscribers for the taxable year, which it would be obligated to pay promptly to such subscriber if he terminated his contract at the close of the company's taxable year, then—

(1) there is to be allowed as a deduction the increase for the taxable year in savings credited to subscriber accounts, or

(2) there is to be included as an item of gross income the decrease for the taxable year in savings credited to subscriber accounts.

Any amount representing savings credited to his account for the taxable year is to be treated by the subscriber as a dividend paid or declared for purposes of his taxable income. Thus, the amount of any savings credited to a subscriber within the meaning of this section shall be taken into account by him in computing his income to the extent that the cost of the insurance with respect to which the savings are credited constitutes a business expense.

(c) *Special deduction for small company having gross amount of less than \$1,200,000.*—Subsection (c) of the new section 823 is identical to the bill as passed by the House, except for the increase in the gross amount provided by your committee's bill and relates to the special deduction for certain small companies having gross receipts of less than \$1,200,000. Paragraph (1) of the new section 823(c) provides that if the gross amount received during the taxable year from the items described in section 822(b) (other than par. (1)(D) thereof) and net premiums (including deposits and assessments) is less than \$1,200,000, then, subject to the limitation provided in paragraph (2) of the new section 823(c) there shall be allowed an additional deduction for purposes of determining statutory underwriting income or loss (under subsec. (a) of the new sec. 823) for the taxable year. This additional deduction is \$6,000; except that if the gross amount exceeds \$600,000, the additional deduction is limited to an amount equal to 1 percent of the amount by which \$1,200,000 exceeds such gross amount. The special deduction provided by paragraph (1) does not apply if the taxpayer is either subject to the tax imposed by section 821(c) (relating to alternative tax for certain small companies) or has gross amounts of \$1,200,000 or more.

Paragraph (2) of the new section 823(c) provides that the amount of the deduction allowed under paragraph (1) of the new section 823(c) is not to exceed the statutory underwriting income (as defined in sec. 823(a)(1)) for the taxable year, computed without regard to the deduction under paragraph (1) or the deduction allowed under section 824(a) (relating to deduction for protection against losses).

Example: The application of section 823(c) may be illustrated by the following example:

Company M, a mutual insurance company subject to the tax imposed by section 821(a), has the following items for the taxable year 1963:

Gross amount for purposes of sec. 823(c)(1)-----	\$800, 000
Gross investment income (including capital gains)-----	150, 000
Capital gains-----	100, 000
Gross income under sec. 832-----	900, 000
Deductions under sec. 822(c)-----	142, 000
Deductions under sec. 832 (as modified by sec. 823(b))-----	866, 000

Under the provisions of section 823(c), company M's special small company deduction for the taxable year 1963 would be \$4,000, computed as follows:

(1) Gross amount for purposes of sec. 823(c)(1)-----	\$800, 000
(2) Amount by which \$1,200,000 exceeds item (1) (\$1,200,000 minus \$800,000)-----	400, 000
(3) 1 percent of item (2), not to exceed \$6,000-----	4, 000
(4) Gross income under sec. 832, reduced by gross investment income (\$900,000 minus \$150,000)-----	\$750, 000
(5) Deductions under sec. 832 (as modified by sec. 823 (b)), reduced by deductions under sec. 822(c) (\$866,000 minus \$142,000)-----	724, 000
(6) Limitation on deduction under sec. 823(c)(1) (excess, if any, of item (4) over item (5))-----	26, 000
(7) Deduction under sec. 823(c)(1) (item (3) or item (6), whichever is the lesser)-----	4, 000

SECTION 824. ADJUSTMENTS TO PROVIDE PROTECTION AGAINST LOSSES

(a) *Allowance of deduction.*—Paragraph (1) of the new section 824(a) provides that for purposes of determining the statutory underwriting income or loss (as defined in sec. 823(a)) for any taxable year there is to be allowed as a deduction to provide protection against losses the sum of—

(1) 1 percent of the losses incurred during the taxable year (as determined under sec. 832(b)(5)); plus

(2) 25 percent of the underwriting gain for the taxable year; plus

(3) if the concentrated windstorm, etc., premium percentage for the taxable year (as defined in par. (2) of the new sec. 824(a)) exceeds 40 percent, the amount determined by applying so much of the concentrated windstorm, etc., premium percentage as exceeds 40 percent to the underwriting gain for the taxable year.

This paragraph is the same as the corresponding provision under the bill as passed by the House, except that under your committee's amendments the excess of the premium percentage over 40 percent, instead of 50 percent, is used in determining that part of the protection against loss deduction provided by subparagraph (C).

For purposes of paragraph (1) of the new section 824(a), the term "underwriting gain" means the statutory underwriting income com-

puted under section 823(a) without regard to the deduction provided by paragraph (1) of the new section 824(a).

Subparagraph (C) of the new section 824(a)(1) permits an additional deduction for protection against losses in the case of certain companies having concentrated windstorm, etc., risks. For example, assume that for the taxable year 1963, W, a mutual insurance company subject to the tax imposed by section 821(a), has an underwriting gain (for purposes of sec. 824(a)) of \$100. Assume further that W's concentrated windstorm, etc., premium percentage (as determined under sec. 824(a)(2)) for the taxable year is 70 percent, and losses incurred during the taxable year are \$1,000. Under the provisions of section 824(a), W's deduction for protection against losses for 1963 would be \$65. Of this amount, \$10 (1 percent of losses incurred, or 1 percent of \$1,000) is due to the application of section 824(a)(1)(A), \$25 (25 percent of underwriting gain, or 25 percent of \$100) is due to the application of section 824(a)(1)(B), and \$30—the amount determined by multiplying the underwriting gain by so much of the concentrated windstorm, etc., premium percentage as exceeds 40 percent, or 30 percent (70 percent minus 40 percent) times \$100—is due to the application of section 824(a)(1)(C).

Paragraph (2) of the new section 824(a) defines the term "concentrated windstorm, etc., premium percentage." This definition is changed from that of the bill as passed by the House only by the addition in the bill as reported of a provision for losses arising within a 200-mile radius of any point selected by the taxpayer. Thus, for any taxable year the percentage is obtained by dividing—

(1) the amount of the premiums earned on insurance contracts during the taxable year (as defined in sec. 832(b)(4)), to the extent attributable to insurance against losses arising either in any one State or within 200 miles of any fixed point selected by the taxpayer from windstorm, hail, flood, earthquake, or similar hazards, by

(2) the total amount of the premiums earned on insurance contracts during the taxable year (as defined in sec. 832(b)(4)). The taxpayer may annually select, within the period of limitation allowed, any geographical area permitted by this paragraph. For example, a company located in Springfield, Ill., may in one year use as the numerator of the fraction the amount of premiums attributable to special insurance risks located within the State of Illinois; in the second year the amount of premiums attributable to such insurance risks located within 200 miles of Peoria; and in the third year the amount of premiums attributable to such insurance risks located within 200 miles of Cedar Rapids, Iowa. For purposes of this paragraph, the term "similar hazards" includes tornadoes, cyclones, and similar natural phenomena but does not include insurance against fires, explosions, or riots. In the case of a company which issues contracts insuring against a combination of risks, some of which are included under this paragraph and some of which are not included under this paragraph, a reasonable allocation of the premiums earned for the taxable year with respect to such contracts will be made for purposes of determining such company's concentrated windstorm, etc., premium percentage for the taxable year.

(b) *Protection against loss account.*—Subsection (b) of the new section 824 requires every insurance company subject to the tax imposed by section 821(a) for any taxable year to establish and maintain a

protection against loss account. This account is to be established for taxable years beginning after December 31, 1962, and the beginning or opening balance of such account is to be zero.

(c) *Additions to account.*—Subsection (c) of the new section 824 relates to the amount which is to be added to the protection against loss account for each taxable year for which the taxpayer is subject to the tax under section 821(a). Subsection (c) of the new section 824 provides that the amount to be added to the protection against loss account is to be an amount equal to the deduction for protection against losses provided by section 824(a)(1).

(d) *Subtractions.*—Paragraphs (1), (4), and (5) of the new section 824(d) sets forth the amounts which are to be subtracted from the protection against loss account. The amount which is required to be subtracted under section 824(d) is taken into account under section 821(b)(1)(C) for purposes of determining mutual insurance company taxable income. Except for the amendments described below, the subtractions required under your committee's bill are identical with those provided in the bill as passed by the House.

Paragraph (1) of the new section 824(d) provides that, after making the additions required by section 824(c) for the taxable year, there shall be subtracted from the protection against loss account—

(A) first, an amount equal to the excess (if any) of the protection against loss deduction allowed under section 824(a) for the taxable year over the underwriting gain (as defined in sec. 824(a)(1)) for the taxable year,

(B) then, the amount (if any) by which—

(i) the sum of the investment loss for such year and the statutory underwriting loss (reduced by the amount referred to in subpar. (A)) for such year, exceeds

(ii) the sum of the statutory underwriting income and the taxable investment income for such taxable year,

(C) next (in the order in which the losses occurred), amounts equal to the unused loss carryovers to such taxable year,

(D) next, any amount remaining which was added to the account for the fifth preceding taxable year, minus one-half of underwriting gain remaining in the account for such taxable year which was added under subsection (a)(1)(B), and

(E) finally, the amount by which the total amount in the account exceeds whichever of the following is the greater:

(i) 10 percent of premiums earned on insurance contracts during the taxable year (as defined in sec. 832(b)(4)) less dividends to policyholders (as defined in sec. 832(c)(11)), or

(ii) the total amount in the account at the close of the preceding taxable year.

Under the bill as passed by the House, subparagraph (A) of the new section 824(d)(1) provided that the first subtraction from the protection against loss account was to have been made for so much of the statutory underwriting loss as was generated either by the deduction for dividends to policyholders (as defined in sec. 832(c)(11)) or by the deduction provided in section 824(a) for protection against losses. Thus, under the bill as passed by the House, any underwriting loss which was attributable to the payment of policy dividends could not be applied against taxable investment income unless the balance in the protection against loss account had first been reduced to zero.

Your committee has amended subparagraphs (A) and (B) to provide in effect that any portion of the statutory underwriting loss which is attributable to the deduction for dividends to policyholders may first be applied against taxable investment income. Under your committee's amendments, however, no portion of the statutory underwriting loss which is attributable to the deduction for protection against losses provided in section 824(a) may be applied against taxable investment income since it is applied against the balance in the protection against loss account.

Under subparagraph (B) of the new section 824(d)(1), the statutory underwriting loss is subtracted from the protection against loss account but only to the extent that such loss exceeds the taxable investment income and the amount determined under subparagraph (A) for the taxable year. The adjustment for the amount subtracted under subparagraph (A) is required by reason of your committee's amendment to subparagraph (A), and prevents the same item from being subtracted from the protection against loss account more than once. In addition, subparagraph (B) provides that where there is an investment loss for the taxable year such loss must first be applied against statutory underwriting income and then any remaining amount must be applied against any balance in the protection against loss account. Or, if there is both a statutory underwriting loss after the reduction referred to in subparagraph (A) and an investment loss, the sum of these losses must be so applied. Only then may any remaining amount give rise to an unused loss.

Subparagraph (D) of the new section 824(d)(1) provides for the subtraction of certain amounts added to the protection against loss account for any taxable year under section 824(c) if such amounts remain in the account for 5 taxable years. Under subparagraph (D) of the new section 824(d), the entire amount remaining in the account from the fifth preceding taxable year which was added by reason of section 824(a)(1)(A) (relating to deduction for 1 percent of losses incurred during the taxable year) or section 824(a)(1)(C) (relating to additional deduction for certain companies having concentrated wind-storm, etc., risks) is to be subtracted from the protection against loss account. There is also to be subtracted under subparagraph (D) of the new section 824(d)(1) an amount representing one-half of the amount remaining in the account with respect to such fifth preceding taxable year which was added by reason of section 824(a)(1)(B) (relating to deduction for 25 percent of underwriting gain for the taxable year). (For a special rule with respect to a reciprocal making the election provided in sec. 826(a), see sec. 826(d).)

Subparagraph (E) of the new section 824(d)(1) provides (taking into account the priority rule in sec. 824(d)(3)(B)), in effect, a ceiling on the amount which can be added to and remain in the protection against loss account for the taxable year for which the amount is added. Subparagraph (E) provides that if the total amount in the account (as determined under sec. 824(d)(2)) exceeds the greater of (1) 10 percent of premiums earned on insurance contracts during the taxable year (as defined in sec. 832(b)(4)) less dividends to policyholders (as defined in sec. 832(c)(11)), or (2) the total amount in the account at the close of the preceding taxable year, then the amount of such excess shall be subtracted from the protection against loss account.

Paragraph (2) of the new section 824(d) contains rules for determining the ceiling on the protection against loss account. It provides

that for purposes of paragraph (1)(E) of the new section 824(d), the total amount in the account is to be determined—

(1) after the application of section 824(d) without regard to paragraph (1)(E) thereof, and

(2) without regard to amounts remaining in the account which were added, with respect to all taxable years, under section 824(a)(1)(C) (relating to additional deduction to provide protection against losses for certain companies having concentrated windstorm, etc., risks).

Under paragraph (2) of the new section 824(d), for purposes of determining the ceiling on the protection against loss account in the case of a company having concentrated windstorm, etc., risks, any amount added to the account by reason of the application of section 824(a)(1)(C) is not to be taken into account.

Paragraph (3) of the new section 824(d) provides rules relating to the priority in which the subtractions from the protection against loss account are to be made. Under paragraph (3)(A) of the new section 824(d) the amounts required to be subtracted from the protection against loss account under section 824(d)(1) (A), (B), and (C), are to be made—

(1) first (on a first-in, first-out basis) from amounts in the account with respect to the 5 preceding taxable years and the taxable year, and

(2) then from amounts in the account with respect to earlier years.

Under paragraph (3)(B) of the new section 824(d), the amounts required to be subtracted from the protection against loss account under section 824(d)(1)(E) are to be subtracted only from amounts in the account with respect to the taxable year.

Under paragraph (3)(C) of the new section 824(d), if the amount to be subtracted from the total amounts in the account with respect to any taxable year is less than such total, the amount required to be subtracted from the protection against loss account under section 824(d)(1) (A), (B), (C), and (E) is to be subtracted from each of the amounts referred to in section 824(a)(1) in the account with respect to such year in the proportion which each bears to the total amount in the account with respect to such year. For example, assume that for the taxable year 1966, N, a mutual insurance company subject to the tax imposed by section 821(a), is required to subtract \$60 from its protection against loss account under section 824(d)(1) (other than under subpar. (E)). Assume that the total amount in the account for 1963 (the first preceding taxable year for which additions to the account were made) is \$100. Assume further that of this \$100 balance, \$30 is due to the application of section 824(a)(1)(A), \$50 is due to the application of section 824(a)(1)(B), and \$20 is due to the application of section 824(a)(1)(C). Under paragraph (3)(C) of the new section 824(d), since the amount to be subtracted from the balance in the account with respect to 1963 is less than such balance, the amount to be subtracted from each of the amounts in the account with respect to such taxable year shall be in the proportion which each bears to such total. Accordingly, the amount in the account by reason of the application of section 824(a)(1)(A) shall be reduced by \$18 ($30/100 \times \60). The amount in the account with respect to the application of section 824(a)(1)(B) shall be reduced by \$30

($50/100 \times \$60$). The amount in the account with respect to the application of section 824(a)(1)(C) shall be reduced by \$12 ($20/100 \times \60).

Paragraph (4) of the new section 824(d) provides that if the taxpayer is not subject to tax under part II of subchapter L for any taxable year, the entire amount in the protection against loss account at the close of the preceding taxable year is to be subtracted from the account in such preceding taxable year and included in mutual insurance company taxable income (as defined in sec. 821(b)) for such preceding taxable year.

Paragraph (5) of the new section 824(d) provides that for any taxable year for which the company is subject to the tax imposed by section 821(a), it may elect to subtract from its protection against loss account any amount which, except for the application of this election, would be in such account as of the close of such taxable year. The amount elected to be subtracted from the protection against loss account is to be included in mutual insurance company taxable income (as defined in sec. 821(b)) for the taxable year. The election must be made after the close of the taxable year for which it is to apply and not later than the time prescribed by law for filing the return (including extensions thereof) for the taxable year following such taxable year, and in such manner and form as the Secretary of the Treasury or his delegate may by regulations prescribe. The election is to apply only with respect to the taxable year for which it is made and once such an election has been made it may not subsequently be revoked.

Examples.—The application of new section 824(d) may be illustrated by the following examples:

Example 1.—For the taxable year 1969, X, a mutual insurance company subject to the tax imposed by section 821(a), has taxable investment income of 25 and a statutory underwriting loss of 22 (including a protection against loss deduction of 7 which is entirely attributable to the application of sec. 824(a)(1)(A)). The following table shows the protection against loss account of X before and after the application of section 824(d) for the taxable year 1969:

	1963	1964	1965	1966	1967	1968	1969
Protection against loss account: Balance remaining in account with respect to each taxable year (before application of sec. 824(d)).....	3	1	1	1	2	1	7
Balance remaining in account with respect to each taxable year (after application of sec. 824(d)).....	3	0	0	0	0	0	6

Under the provisions of section 824(d)(1)(A), for the taxable year 1969, X would subtract 7 from its protection against loss account (the amount by which the protection against loss deduction allowed under sec. 824(a) for the taxable year exceeds the underwriting gain for the taxable year, or 7 minus 0). Under the provisions of section 824(d)(3)(A), since the subtractions are to be made with respect to amounts in the account for the 5 preceding taxable years and the taxable year on a first-in, first-out basis, X would first apply the amount to be subtracted to the amount in the account with

respect to 1964, 1965, 1966, 1967, and 1968, in that order. This would reduce the total amount in the account with respect to such taxable years by 6, and the balance in the account with respect to each of the taxable years 1964 through 1968 would be reduced to zero. The remaining amount required to be subtracted under section 824(d)(1)(A), 1 (7 minus 6), would then be subtracted from the amount added to the account for the taxable year, 7 (an amount equal to the protection against loss deduction for the taxable year 1969), leaving a balance of 6 (7 minus 1) in the account with respect to 1969. No proration of the subtraction from the amount in the account for 1969 is required under section 824(d)(3)(C) since the entire amount added to the account in 1969 was added by reason of section 824(a)(1)(A).

Example 2.—Assume the facts are the same as in example 1, except that X has taxable investment income of 7 (instead of 25) for the taxable year 1969. After the application of section 824(d) for the taxable year 1969, the results would be as follows:

Protection against loss account

	1963	1964	1965	1966	1967	1968	1969
Balance remaining in account with respect to each taxable year (after application of sec. 824(d))-----	1	0	0	0	0	0	0

Under the provisions of section 824(d)(1), for the taxable year 1969, X would subtract 15 from its protection against loss account. Of this amount, 7 would be attributable to the application of section 824(d)(1)(A) (i.e., the amount by which the protection against loss deduction allowed under sec. 824(a) for the taxable year exceeds the underwriting gain for the taxable year, or 7 minus 0), and 8 would be attributable to the application of section 824(d)(1)(B) (i.e., the amount by which the statutory underwriting loss for the taxable year, reduced by the amount determined under sec. 824(d)(1)(A), exceeds the taxable investment income for the taxable year, or the amount by which 15 (22 minus 7) exceeds 7). Under section 824(d)(3)(A)(i), this subtraction would be made (on a first-in, first-out basis) from amounts in the account with respect to 1964, 1965, 1966, 1967, 1968, and 1969, in that order. This would reduce the total amount in the account with respect to such taxable years by 13, and the balance in the account with respect to each of the taxable years 1964 through 1969 would be reduced to zero. Under the provisions of section 824(d)(3)(A)(ii), the remaining amount required to be subtracted under section 824(d)(A), 2 (15 minus 13), would then be subtracted from the amount in the account with respect to 1963 (i.e., the amount representing one-half of the amount added by reason of sec. 824(a)(1)(B) which was not required to be subtracted from the protection against loss account under sec. 824(d)(1)(D) in 1968). Thus, the amount in the account with respect to 1963 would be reduced to 1 (3 minus 2).

Example 3.—Assume that Y, a mutual insurance company subject to tax under section 821(a), has a protection against loss account

which reflects the following items for the taxable years 1963 through 1968:

Additions to protection against loss account

	1963	1964	1965	1966	1967	1968
Additions:						
1 percent of losses incurred.....	15	20	60	60	60	60
25 percent of underwriting gain.....	60	20	40	50	45	45
Additional deduction for concentrated risks.....	0	0	5	5	0	0
Total.....	75	40	105	115	105	105

Y, in computing mutual insurance company taxable income for 1968, is required to subtract from the account with respect to 1963 the entire amount of the 1 percent of losses incurred added for 1963 (15) and one-half of the underwriting gain (30) added for such year. Upon taking into account these subtractions, the balance in the protection against loss account with respect to 1963 is 30 (the one-half remaining in the account after the application of par. (1)(D) of sec. 824(d)).

Assume further, that for the taxable year 1969, Y has taxable investment income of 50, underwriting gain of 80, resulting because of incurred losses of 4,000, expenses of 1,000, and premiums earned less dividends to policyholders of 5,080. Under section 824(a), the protection against loss deduction for 1969 is 60. After applying section 824(c), but before applying section 824(d) for 1969, the protection against loss account as of the close of 1969 (after subtracting in 1968 the 45 amount with respect to 1963) would be as follows:

Protection against loss account

	1963	1964	1965	1966	1967	1968	1969
Additions:							
1 percent of loss incurred.....	0	20	60	60	60	60	40
25 percent of underwriting gain.....	30	20	40	50	45	45	20
Additional deduction for concentrated risks.....	0	0	5	5	0	0	0
Total with respect to taxable year....	30	40	105	115	105	105	60
Total (as of end of each year before 1969 subtractions).....	30	70	175	290	395	500	560

After making the addition to the protection against loss account for 1969 and obtaining the results shown in the table above, Y is required to make the subtractions for 1969 from the account. These subtractions may be summarized as follows:

Subtractions under section 824(d) for 1969

Taxable year with respect to which amount is subtracted	1963	1964	1965	1966	1967	1968	1969
Par. (1)(A) subtraction.....	0	0	0	0	0	0	0
Par. (1)(B) subtraction.....	0	0	0	0	0	0	0
Par. (1)(C) subtraction.....	0	0	0	0	0	0	0
Par. (1)(D) subtraction.....	0	130	0	0	0	0	0
Par. (1)(E) subtraction.....	0	0	0	0	0	0	12
Pars. (4) and (5) subtraction.....	0	0	0	0	0	0	0

¹ 20 represents the amount added for 1964 with reference to incurred losses; 10 represents one-half of the amount added for 1964 with reference to underwriting gain.

After determining the subtractions with respect to years before 1969, the next step is to determine whether any subtraction is required for the taxable year 1969 under section 824(d)(1)(E). Since the total balance in the account after the application of section 824(d) (other than par. (1)(E) thereof), 520 (560 minus 30, and excluding 10 added to the account by reason of the additional deduction for protection against losses for concentrated windstorm, etc., companies provided by sec. 824(a)(1)(C)), exceeds 10 percent of premiums earned on insurance contracts during the taxable year less dividends to policyholders, 508 (10 percent of 5,080), Y would be subject to the ceiling on the protection against loss account for the taxable year 1969 and would be required to subtract 12 (the excess of 520 over 508) from the account under section 824(d)(1)(E). Under the provisions of section 824(d)(3)(B) this subtraction would be made only from amounts in the account with respect to the taxable year 1969. Under the provisions of section 824(d)(3)(C), however, since the amount to be subtracted, 12, is less than the total amount added to the account for the taxable year, 60 (40 plus 20), the subtractions under section 824(d)(1)(E) would be applied ratably against each of the amounts added to the account for the taxable year. Thus, the amount remaining in the account with respect to section 824(a)(1)(A) for the taxable year 1969, would be 32 (40 minus $40/60 \times 12$, or 40 minus 8), and the amount remaining in the account with respect to section 824(a)(1)(B) for the taxable year 1969, would be 16 (20 minus $20/60 \times 12$, or 20 minus 4).

Based on these facts, Y's mutual insurance company taxable income for 1969 would be 112 (the sum of taxable investment income of 50, plus statutory underwriting income of 20 (underwriting gain minus protection against loss deduction, or 80 minus 60), plus subtractions from the protection against loss account under sec. 824(d) of 42).

SECTION 825. UNUSED LOSS DEDUCTION

(a) *Amount of deduction.*—Subsection (a) of the new section 825 provides that, for purposes of part II of subchapter L, the unused loss deduction (used in the determination of mutual insurance company taxable income under sec. 821(b)) shall be an amount equal to the unused loss carryovers and carrybacks to the taxable year.

(b) *Unused loss defined.*—Subsection (b) of the new section 825 defines the term "unused loss," for purposes of part II of subchapter L, as the amount by which—

(1) the sum of the statutory underwriting loss (as defined in sec. 823(a)(2)) and the investment loss (as defined in sec. 822(a)(2)), exceeds—

(2) the sum of—

(A) the taxable investment income (as defined in sec. 822(a)(1)),

(B) the statutory underwriting income (as defined in sec. 823(a)(1)), and

(C) the amounts required to be subtracted from the protection against loss account under section 824(d).

If the sum of the items under (1) does not exceed the sum of items under (2), the unused loss is zero.

(c) *Loss year defined.*—Subsection (c) of the new section 825 defines as the loss year, for purposes of part II of subchapter L, any taxable year in which a company subject to the tax imposed by section 821(a) has an unused loss which is more than zero.

(d) *Years to which carried.*—Subsection (d) provides that the unused loss for any loss year is to be an unused loss carryback to each of the 3 taxable years preceding the loss year and an unused loss carryover to each of the 5 taxable years following the loss year. (For certain taxable years to or from which an unused loss may not be carried, see section 825(g).)

(e) *Amount of carrybacks and carryovers.*—Subsection (e) of the new section 825 provides that for any loss year, the entire amount of the unused loss, determined under the provisions of section 825(b), shall be carried to the earliest of taxable years to which such loss may be carried under section 825(d) (subject to the limitations of sec. 825(g)). The amount of the unused loss carried to each of the other taxable year (permitted under section 825(d)), following the earliest taxable year shall be the excess of such loss over the sum of the offsets for each taxable year preceding the taxable year to which the loss is carried.

(f) *Offset defined.*—Subsection (f) of the new section 825 defines the term “offset,” for purposes of section 824(e) and provides that the taxable year to which an unused loss is carried is to be referred to as the “offset year.” “Offset” is defined as the mutual insurance company taxable income for the offset year in the case of an unused loss carryback from the loss year to the offset year. In the case of an unused loss carryover from the loss year to the offset year, the offset is the sum of the amount required to be subtracted from the protection against loss account under section 824(d)(1)(C) for the offset year and the mutual insurance company taxable income for the offset year. For purposes of computing the offset, the mutual insurance company taxable income for the offset year (as defined in sec. 821(b)) shall be determined without regard to any loss carryback or carryover to the offset year from the loss year, or any year thereafter.

Example: The application of section 825 may be illustrated by the following example:

For the taxable year 1967, F, a mutual insurance company subject to the tax imposed by section 821(a), has the following items:

Taxable investment income.....	1
Underwriting loss.....	59
Addition to protection against loss account.....	8
Statutory underwriting loss.....	67

As explained below, the subtractions from protection against loss account are as follows:

Amount subtracted from amounts in account with respect to taxable years 1963 through 1966.....	18
Amount subtracted from amounts in account with respect to taxable year 1967.....	8
Total subtractions from protection against loss account under sec. 824(d).....	26

The application of section 825 in this case may be illustrated by the facts and results shown in the following table and explained below:

	Taxable year—					
	1963	1964	1965	1966	1967	1968
Protection against loss account:						
Addition to account during taxable year.....	6	2	3	7	8	7
Subtraction from account during taxable year.....	0	0	0	0	8	7
Protection against loss account (at end of year).....	6	2	3	7	0	0
Protection against loss account (at end of taxable year 1968).....	0	0	0	0	0	0
Unused loss.....	0	0	0	0	40	0
Unused loss carryback.....	0	40	35	25	0	0
Unused loss carryover.....	0	0	0	0	0	18
Unused loss deduction.....	0	40	35	25	0	18
Mutual insurance company taxable income (computed without regard to unused loss).....	13	5	10	7	0	2
Mutual insurance company taxable income (computed with regard to unused loss).....	13	0	0	0	0	0
Offset for year.....	0	5	10	7	0	9
Offset total.....	0	5	15	22	0	31

1967: Under the provisions of section 825(b), F's unused loss for 1967 is 40, the amount by which the sum of the statutory underwriting loss and the investment loss, 67 (67 plus 0), exceeds the sum of the taxable investment income, the statutory underwriting income, and the amounts required to be subtracted from the protection against loss account under section 824(d) for the taxable year, 27 (the sum of 1, 0, and 26, respectively).

1967 carryback to 1964: Under the provisions of section 825(e), the entire unused loss for 1967 of 40 is carried back to 1964, the earliest year to which the loss may be carried under section 825(d). Since there are no other amounts carried to 1964, the unused loss deduction for 1964 is 40. Thus, after taking the unused loss deduction into account, the mutual insurance company taxable income for 1964 is zero, and the offset for 1964 is 5 (the mutual insurance company taxable income for 1964 determined without regard to the unused loss carryback from 1967 or any year thereafter).

1967 carryback to 1965: The portion of the unused loss for 1967 which is carried back to 1965 is 35 (40 minus 5, the offset for 1964). After taking the underwriting loss deduction into account, the mutual insurance company taxable income for 1965 is zero. The offset for 1965 is 10, the mutual insurance company taxable income for 1965 determined without regard to any unused loss carryback or carryover from 1967 or any year thereafter.

1967 carryback to 1966: The portion of the unused loss for 1967 which is carried back to 1966 is 25. This amount is the excess of the underwriting loss for 1967 of 40 over the sum of the offset for 1965 (5) and the offset for 1966 (10). Thus, as a result of the unused loss for 1967, the mutual insurance company taxable income for 1966 is reduced to zero. The offset for 1966 is 7.

1967 carryover to 1968: Under the provisions of section 825(d), the portion of the unused loss for 1967 which is carried forward to 1968 is 18 (40 minus the sum of 10, 5, and 7, the offsets for 1964, 1965, and 1966, respectively). Under section 825(f)(2), this amount is first applied against any amounts in the protection against loss account at the end of 1968, and is then applied against the mutual insurance company taxable income for 1968. Thus, assuming that there are

no other subtractions from its protection against loss account under section 824(d) for 1968, F's protection against loss account of 7 is reduced to zero by reason of the subtraction under section 824(d)(1)(C). The remaining portion of the unused loss for 1967 which is carried to 1968, 11 (18 minus 7, the amount of the unused loss carryover to 1968 which is subtracted from the protection against loss account under sec. 824(d)(1)(C)), is then applied against the mutual insurance company taxable income for 1968. Thus, after the application of the unused loss deduction for 1968, the mutual insurance company taxable income for 1968 is zero. The offset for 1968 is 9, the sum of the amount required to be subtracted from the protection against loss account under section 824(d)(1)(C) for 1968 (7), plus the mutual insurance company taxable income for 1968, determined without regard to the unused loss carryover from 1967 or any unused loss carry-back from 1967 or any year thereafter (2). The remaining 9 of the unused loss for 1967 (40 minus the sum of 10, 5, 7, and 9, the offsets for 1964, 1965, 1966, and 1968, respectively), is carried forward to 1969, and to the extent not used in that year or any year thereafter, may be carried forward to 1970, 1971, and 1972, in that order.

(g) *Limitations*.—Subsection (g) of the new section 825 provides that, for purposes of part II of subchapter L, an unused loss (as defined in sec. 825(b)) may not be carried—

(1) to or from any taxable year beginning before January 1, 1963;

(2) to or from any taxable year for which the insurance company is not subject to tax imposed by section 821(a); nor

(3) to any taxable year if, between the loss year and such taxable year, there is an intervening taxable year for which the insurance company was not subject to the tax imposed by section 821(a).

Examples.—The application of section 825(g) may be illustrated by the following:

Example 1.—For the taxable year 1963, M, a mutual insurance company subject to tax imposed by section 821(a), has an unused loss (as defined in sec. 825(b)) of \$65,000. The loss may not be carried back to any taxable year beginning before 1963. However, the loss may be carried forward to each of the 5 taxable years following 1963 provided that for each of such succeeding taxable years M is subject to the tax imposed by section 821(a).

Example 2.—Assume the facts are the same as in example 1, except that for the taxable year 1964, the gross amount received by M from the items described in section 822(b) (other than par. (1)(D) thereof) and premiums (including deposits and assessments) exceeds \$150,000 but does not exceed \$600,000. If M does not make the election under section 821(d) (relating to election to be taxed under sec. 821(a) for 1964), the loss will not be allowed as an unused loss carryover since, by reason of section 825(g)(3), the unused loss may not be carried to any taxable year if, between the loss year and such taxable year, there is an intervening taxable year for which the insurance company was not subject to the tax imposed by section 821(a), and by reason of section 825(g)(1), the unused loss may not be carried to any taxable year beginning before 1963.

SECTION 826. ELECTION BY RECIPROCAL

(a) *In general.*—Subsection (a) of the new section 826 provides that, except as provided in section 826(c), any insurance company which is an interinsurer or reciprocal underwriter (referred to in sec. 826 as a “reciprocal”) subject to the tax imposed by section 821(a), may elect to be subject to the limitation provided in subsection (b) of the new section 826. Such election shall be made, under regulations prescribed by the Secretary of the Treasury or his delegate, not later than the time prescribed by law (including extensions thereof) for filing the return for the year for which such election is first to apply. The election is to apply for the taxable year for which made and for all succeeding taxable years and may not be revoked without the consent of the Secretary of the Treasury or his delegate. The effect of such election is to increase the income of the reciprocal by the income of its attorney-in-fact attributable to the reciprocal for purposes of computing the taxes imposed by section 821(a) and to allow such reciprocal a credit for the taxes paid by the attorney-in-fact with respect to the income attributed to the reciprocal.

(b) *Limitation.*—Subsection (b) of the new section 826 provides that a reciprocal making the election provided under section 826(a) shall limit the deduction for amounts paid or incurred in the taxable year to the attorney-in-fact to such amounts as are deductible by the attorney-in-fact in respect of the income received by the attorney-in-fact from the reciprocal. In no case may such deduction of the reciprocal be increased by the deductions of the attorney-in-fact allocable to the income received from the reciprocal.

(c) *Exception.*—Section 826(c) provides that no election under section 826(a) may be made by a reciprocal unless its attorney-in-fact—

(1) is a corporation subject to the taxes imposed by section 11 (b) and (c) of subtitle A;

(2) consents to make available such information as may be required during the period in which an election made under subsection (a) is in effect;

(3) reports income received from the reciprocal and deductions allocable thereto under the same method of accounting used by the reciprocal in reporting deductions for amounts paid or incurred to the attorney-in-fact; and

(4) files its return on a calendar-year basis.

(d) *Special rule.*—Under the bill as passed by the House, the limitation under section 826(b) would not have been taken into account by any reciprocal electing under section 826(a) either for purposes of computing the protection against loss deduction provided in section 824(a) or for purposes of computing the addition to the protection against loss account provided in section 824(c). Thus, in effect, a reciprocal making the election would not have included any of the income of the attorney-in-fact in computing its protection against loss deduction. Your committee has amended this section to provide that the protection against loss deduction, and the amount added to the protection against loss account, for the taxable year, may be increased to reflect any amounts attributable to the consolidation permitted under this subsection. However, your committee has provided a special rule that in applying section 824(d)(1)(D) any amount which was added to the protection against loss account by

reason of such an election shall be treated as having been added by reason of section 824(a)(1)(A). The effect of this special rule is that no portion of the amount added to the protection against loss account by reason of the election under section 826(a) (i.e., the amount by which 25 percent of consolidated underwriting income exceeds 25 percent of underwriting income determined prior to consolidation), may be deferred for more than 5 years.

(e) *Credit*.—Subsection (e) of the new section 826 provides that any reciprocal electing to be subject to the limitation provided in subsection (b) shall be credited with the tax paid by its attorney-in-fact with respect to the income of the reciprocal in such taxable year.

(f) *Surtax exemption denied*.—Subsection (f) of the new section 826 provides that any tax imposed upon the increase in the income of the reciprocal attributable to the limitation under subsection (b) shall be computed without regard to the \$25,000 surtax exemption provided in section 821(a)(2).

(g) *Adjustment for refund*.—Subsection (g) of the new section 826 provides that if for any taxable year an attorney-in-fact is allowed a credit or refund for taxes paid with respect to which a reciprocal was allowed a credit or refund as a result of the application of subsection (e) of the new section 826, the taxes of the reciprocal for the year in which such credit or refund is allowed shall be properly adjusted under regulations prescribed by the Secretary of the Treasury or his delegate. This adjustment prevents the reciprocal and the attorney-in-fact from obtaining a credit or refund with respect to the same tax.

For example, assume that a reciprocal has elected in 1963 to be subject to the limitation provided in section 826(b) and such election is still in effect in taxable year 1966. Assume further that in taxable year 1969 its attorney-in-fact receives a refund or credit with respect to taxable year 1966. In such case, the taxes of the reciprocal in taxable year 1969 shall be properly adjusted under regulations prescribed by the Secretary of the Treasury or his delegate.

(h) *Taxes of attorney-in-fact unaffected*.—Subsection (h) of the new section 826 provides that nothing in section 826 shall either increase or decrease the taxes imposed by chapter 1 on the income of the attorney-in-fact.

Example.—The application of section 826 may be illustrated by the following example:

For the taxable year 1963, R, a reciprocal underwriter subject to the taxes imposed by section 821(a), has the following items (determined before applying any election under sec. 826):

Gross income under sec. 832.....	\$578
Gross investment income.....	50
Deductions under sec. 832 (as modified by sec. 823(b)):	
Deduction for amounts paid by R to attorney-in-fact A.....	\$100
All other deductions.....	500
Total deductions under sec. 832.....	600
Deductions under sec. 822(c).....	40
Incurred losses.....	400
Protection against loss deduction.....	4
Underwriting gain.....	0
Mutual insurance company taxable income.....	0
Unused loss.....	22
Credit or refund for taxes paid.....	0

Assume that the deductions of attorney-in-fact A allocable to the income received by A from R are 60 and the tax paid by A allocable to the income received from R is 16. If R elects to be subject to the limitation provided in section 826(b), the results for 1963 would be as follows:

Gross income under sec. 832.....	578
Gross investment income.....	50
Deductions under sec. 832 (as modified by sec. 823(b)):	
Deduction for amounts paid by R to attorney-in-fact A.....	60
All other deductions.....	500
Total deductions under sec. 832.....	560
Deductions under sec. 822(c).....	40
Incurred losses.....	400
Protection against loss deduction.....	6
Underwriting gain.....	8
Mutual insurance company taxable income.....	12
Unused loss.....	0
Credit or refund for taxes paid.....	16

Under the provisions of section 826(b), R's deduction for amounts paid or incurred to the attorney-in-fact in the taxable year 1963 would be limited to the deductions of A allocable to the income received by A from R. Thus, R's deductions under section 832 (as modified by sec. 823(b)) for 1963 would be 60 (the deductions of A which are allocable to the income received by A from R). As a result of making the election under section 826(a) for the taxable year 1963, R's underwriting gain would be 8, and its statutory underwriting income would be 2 (the underwriting gain of 8 minus the protection against loss deduction of 6—of which 4 represents the amount determined under sec. 824(a)(1)(A) and 2 represents the amount determined under sec. 824(a)(1)(B)—or 8 minus 6). Accordingly, R's mutual insurance company taxable income for 1963 would be 12. This amount consists of the taxable investment income of 10 (gross investment income minus deductions under sec. 822(c), or 50 minus 40) plus the statutory underwriting income of 2. Since all of R's mutual insurance company taxable income of 12 is attributable to the limitation under section 826(b), the entire amount is subject to the surtax under section 821(a) (2) without regard to the \$25,000 surtax exemption. The credit of 16, representing that part of the taxes paid by A which is allocable to the income received by A from R, may be applied by R against its taxes with respect to its mutual insurance company taxable income of 12 for 1963, and R would be entitled to a refund of any excess of the amount of such credit over its tax liability for 1963.

Under the provisions of section 826(d), no portion of the amount added to such account in 1963 by reason of the election under section 826(a), 2 (25 percent of the amount by which the consolidated underwriting gain exceeds 25 percent of the underwriting gain determined without regard to the election under sec. 826(a), or the amount by which 25 percent of 8 exceeds 25 percent of 0), may be permitted to continue to remain in the protection against loss accounts beyond the taxable year 1968.

(d) *Exemption from tax.*—The bill as reported by your committee adds an amendment to section 501(c)(15) (relating to exemption from tax of certain mutual insurance companies) by striking out "\$75,000" and inserting in lieu thereof "\$150,000". Thus, the \$75,000 exemption

for certain mutual insurance companies under existing law is increased to \$150,000, in accordance with the changes made in section 821 by your committee.

SECTION 8. MUTUAL INSURANCE COMPANIES (OTHER THAN LIFE, MARINE, AND CERTAIN FIRE OR FLOOD INSURANCE COMPANIES), ETC. (Continued)

(e) *Mutual fire insurance companies operating on basis of premium deposits.*—Subsection (e) of section 8 of the bill, which corresponds to subsection (d) of section 10 of the bill as passed by the House, amends section 831(a) of the 1954 Code to include mutual fire insurance companies operating on the basis of premium deposits among the companies which are subject to the tax imposed by part III of subchapter L of chapter 1 of the code. Your committee's amendment adds mutual flood insurance companies to this group.

(1) *Application of section 831(a).*—Subsection (e)(1) of section 8 of the bill amends section 831(a) of the code (which imposes a tax on certain mutual marine and mutual fire insurance companies and on stock insurance companies which are not life insurance companies) to provide that, for taxable years beginning after December 31, 1962, mutual fire or flood insurance companies operating on the basis of premium deposits are to be subject to tax under part III of subchapter L. Under existing law, mutual fire insurance companies operating on the basis of premium deposits (the so-called factory mutual insurance companies) are taxed in the same manner as any other mutual insurance company (other than a life or marine or fire insurance company issuing perpetual policies); thus, these companies are subject to the tax imposed by section 821. (See *Philadelphia Manufacturers Mutual Insurance Company v. Commissioner* (1959), 33 T.C. 490, aff'd (C.A. 3d 1960) 284 F.2d 296.) Under the bill, every mutual fire or flood insurance company whose principal business is the issuance of policies for which the premium deposits are the same, regardless of the length of the term for which the policies are written, will be subject to the tax imposed by section 831(a) if the unabsorbed portion of such premium deposits not required for losses, expenses, or establishment of reserves is returned or credited to the policyholder on cancellation or expiration of the policy. For purposes of this subsection, in the case of a mutual flood insurance company, the premium deposits will be considered to be the same if the payment of a premium increases the total insurance under the policy in an amount equal to the amount of such premium, and the omission of any annual premium does not result in the reduction or suspension of coverage under the policy.

(2) *Treatment of unabsorbed premium deposits.*—Subsection (e)(2) of section 8 of the bill amends section 832(b)(4) of the code (relating to definition of premiums earned) to provide that for purposes of determining the premiums earned on insurance contracts during the taxable year in the case of a mutual fire or flood insurance company operating on the basis of premium deposits, the term "unearned premiums" means (with respect to the policies described in sec. 831(a)(3)(B)) the amount of unabsorbed premium deposits which the company would be obligated to return to its policyholders at the close of the company's taxable year if all of such policies were terminated at such

time. This paragraph further provides that for purposes of determining the amount which such company would be obligated to return to its policyholders at the close of any taxable year, the company must use its own schedule of unabsorbed premium deposit returns then in effect.

(3) *Conforming amendments.*—Subparagraph (e)(3) of section 8 of the bill amends section 832(b)(1)(C) of the code (relating to definition of gross income) to conform to the amendment to section 831(a).

(4) *Adjustment of premium deposit.*—Subparagraph (e)(4) of section 8 of the bill amends section 832(c)(11) of the code (relating to deduction for dividends to policyholders) to provide that the term “dividends and similar distributions” includes amounts returned or credited to policyholders on cancellation or expiration of factory mutual policies described in the new section 831(a)(3)(B).

(5) *Additional item of income.*—Subparagraph (e)(5) of section 8 of the bill amends section 832(b)(1) of the code (relating to the definition of gross income) to provide that, in the case of a mutual fire or flood insurance company operating on the basis of premium deposits, gross income includes an amount which is equal to 2 percent of premiums earned on insurance contracts during the taxable year with respect to policies described in section 831(a)(3)(B) after deduction of premium deposits returned or credited during the same taxable year. The term “premiums earned on insurance contracts during the taxable year”, for purposes of this section, means the absorbed premiums for the taxable year determined in accordance with the schedule of unabsorbed premium deposits in effect at the end of the taxable year.

(f) *Election of certain mutual companies to be taxed on total income.*—Subsection (f) of section 8 of the bill, which corresponds to subsection (e) of section 10 of the bill as passed by the House, amends section 831 of the code (relating to tax on insurance companies (other than life or mutual), mutual marine insurance companies, and mutual fire insurance companies issuing perpetual policies) by redesignating subsection (c) as subsection (d) and adding a new subsection (c). The new section 831(c) provides that any mutual insurance company engaged in writing marine, fire, and casualty insurance which for any 5-year period beginning after December 31, 1941, and ending before January 1, 1962, was subject to the tax imposed by section 831 (or the tax imposed by corresponding provisions of prior law) may elect to be subject to the tax imposed by section 831, whether or not marine insurance is its predominant source of premium income. If such election is made, the electing company shall be subject to the tax imposed by section 831, for years beginning after December 31, 1961, rather than subject to the tax imposed by section 821. Such election shall not be revoked except with the consent of the Secretary of the Treasury or his delegate.

(g) *Technical amendments, etc.*—This subsection, which corresponds to subsection (f) of the bill as passed by the House, makes certain technical changes to provisions of the 1954 Code outside of parts II or III of subchapter L to conform those provisions to the changes in subchapter L made by section 8 of the bill.

(1) *Credit for foreign taxes.*—Subsection (g)(1) amends section 841 of the code (providing for the allowance to an insurance company of the foreign tax credit provided in sec. 901) so as to define the term “taxable income,” as used in section 904, to mean the mutual insurance company taxable income (as defined in sec. 821(b)) in the case of the

tax imposed by section 821(a), and the taxable investment income (as defined in sec. 822(a)(1)) in the case of the tax imposed by section 821(c).

(2) *Adjustments to basis for depreciation sustained.*—Subsection (g)(2) amends section 1016(a)(3) of the code (relating to adjustments to basis for depreciation, etc., sustained) to provide, in effect, that any exhaustion, wear and tear, obsolescence, amortization, and depreciation, to the extent sustained (and to the extent sec. 1016(a)(2) does not apply), on property held in respect of any period since February 28, 1913, by a person subject to tax under part II of subchapter L (or the corresponding provisions of prior income tax laws), must be taken into account in determining the adjusted basis of such property.

(3) *Alternative tax on capital gains.*—Subsection (g)(3) amends section 1201(a) of the code (relating to alternative tax on capital gains) to conform to the amendment to section 821.

(4) *Clerical amendments.*—Subsection (g)(4) makes clerical conforming changes.

(h) *Effective date.*—Subsection (h) of section 8 of the bill provides that the amendments made by section 8 of the bill (other than by subsec. (f)) shall apply only with respect to taxable years beginning after December 31, 1962. Section 831(c) of the code, as added by subsection (f) of section 8, is applicable for taxable years beginning after December 31, 1961.

SECTION 9. DOMESTIC CORPORATIONS RECEIVING DIVIDENDS FROM FOREIGN CORPORATIONS

Section 9 of the bill, corresponding to section 11 of the bill as passed by the House, deals with the method to be used for determining the amount of foreign income tax deemed to have been paid by domestic corporations with respect to dividends received from foreign corporations for purposes of allowance of a foreign tax credit under section 902 of the code. Section 9 of the bill revises section 902 of the code, and requires (under a new sec. 78) the inclusion of certain taxes deemed paid in income as a dividend from corporations other than certain less developed country corporations (the bill as passed by the House applied such rule to dividends from all foreign corporations). The new section 902 omits the present subsection (d), which provides a special rule for allowance of a foreign tax credit with respect to royalty or compensation payments made by certain wholly owned foreign subsidiaries to domestic parents in lieu of dividends. Section 9 also changes the source of income rule of section 861(a)(2)(B) with respect to dividend income received from a foreign corporation which derived income from sources within the United States and for which a dividends received deduction was allowed under section 245.

(a) *Entire amount of foreign tax to be taken into account.*—Subsection (a) of the new section 9 revises section 902. Paragraph (1) of subsections (a) and (b) of section 902 as revised, and subparagraph (A) of subsection (c)(1), provide a new formula for determining the amount of foreign income tax deemed to have been paid by a domestic corporation with respect to dividends received from a foreign corporation other than a less developed country corporation. Paragraph (2) of subsections (a) and (b), and subparagraph (B) of subsection (c)(1),

of section 902 as revised continue existing law for determining the amount of foreign income tax deemed to have been paid by a domestic corporation with respect to dividends from less developed country corporations. Subsections (b)(1) and (c)(1)(A) apply only if subsection (a)(1) applies, and subsections (b)(2) and (c)(1)(B) apply only if subsection (a)(2) applies. The first clause of section 902(c)(1) of existing law defines accumulated profits as gains, profits, or income reduced by the amount of taxes with respect thereto. Under subsection (c)(1)(A) of section 902 as revised, however, accumulated profits are defined as gains, profits, or income computed without reduction by the amount of the income, war profits, and excess profits taxes imposed by a foreign country or possession of the United States on or with respect to such profits or income. Taxes imposed by the United States will, however, continue to reduce such accumulated profits.

The redefinition of accumulated profits increases the amount of taxes to be taken into account in applying the proportions provided in section 902 (a)(1) and (b)(1) of the code. Under existing law, a credit is allowed to a domestic corporation for all or a part of the foreign taxes paid on or with respect to the accumulated profits of the foreign corporation making a distribution. However, by the existing definition, accumulated profits are total profits less taxes thereon. The Supreme Court, in *American Chicle Co. v. United States*, 316 U.S. 450 (1942), has held that the amount of tax paid on or with respect to a foreign corporation's accumulated profits is the same proportion of total taxes on profits as accumulated profits is of total profits. Thus, if a corporation had total profits of \$100, foreign taxes of \$40, and therefore accumulated profits of \$60, the amount of taxes paid on or with respect to accumulated profits would be \$24 ($\$40 \times \$60 / \100). If the accumulated profits of \$60 were paid as a dividend, no more than \$24 could be allowed as a credit as deemed paid under section 902 of existing law.

As amended, the section 902(c)(1)(A) definition will permit the taking into account of a stated proportion of total taxes under section 902(a)(1) and 902(b)(1). For such purpose it is no longer necessary to apply the *American Chicle* rule. Since accumulated profits would be total profits without reduction for taxes paid thereon, the amount of taxes paid on or with respect to accumulated profits would, in the above example, be \$40 rather than \$24.

Subsections (a)(1) and (b)(1) of section 902 as revised provide for the use of the proportion which distributed dividends bear to the accumulated profits in excess of foreign taxes. The result is to continue under such subsections the use of the ratios under existing law, but because of section 902(c)(1)(A) the amount against which the ratios operate is increased.

The application of these changes in a section 902(a)(1) computation may be illustrated by the following example involving corporation P, a domestic corporation which owns 100 percent of the voting stock of corporation FC, a foreign corporation not a less developed country corporation. It is assumed that all transactions have taken place within, and are related to, the same taxable year.

Example 1

(i) Gains, profits, and income of corporation FC-----	\$100
(ii) Foreign tax paid by corporation FC with respect to such gains, profits, and income-----	30
(iii) Accumulated profits of corporation FC computed without reduction for foreign taxes (sec. 902(c))-----	100
(iv) Accumulated profits of corporation FC reduced by foreign taxes (sec. 902(a))-----	70
(v) Dividends paid by corporation FC to corporation P-----	35
(vi) Corporation P is deemed to have paid the same proportion of the total tax paid by corporation FC as dividends, determined without regard to section 78, bear to accumulated profits in excess of taxes: $\$30 \times$ $35/70$ -----	15

Example 1 will apply to all dividends received by a domestic corporation after December 31, 1964, from a foreign corporation (not a less developed country corporation), regardless of the year in which the profits from which such dividends were paid were accumulated. Example 1 will also apply with respect to dividends received by a domestic corporation from such a foreign corporation in its taxable years beginning after December 31, 1962, so long as the dividends from the foreign corporation are attributable to accumulated profits of the foreign corporation for its taxable years beginning after December 31, 1962. However, for periods before January 1, 1965, the *American Chicle* rule and the present section 902(a) treatment will continue to apply where the dividends from such a foreign corporation are attributable to accumulated profits for taxable years beginning before January 1, 1963. Following the established rule, a foreign corporation is considered to be making a distribution first from its accumulated profits for its current taxable year and then from its accumulated profits of its immediately preceding year, etc.

The following example illustrates the above rules where a dividend is distributed out of both accumulated profits for taxable years beginning after December 31, 1962, and accumulated profits for taxable years beginning before January 1, 1963. The facts are the same as in example 1 except for the noted differences:

Example 2

(i) Gains, profits, and income of corporation FC in 1963-----	\$100
(ii) Foreign tax paid by corporation FC with respect thereto-----	40
(iii) 1962 accumulated profits and foreign tax: Accumulated profits (existing sec. 902(c))-----	60
Foreign tax-----	40
(iv) Dividends paid by corporation FC to corporation P in 1963 and the year to which such dividends are attributable: 1963-----	\$60
1962-----	30
	90
(v) Corporation P is deemed to have paid a foreign tax with respect to the 1963 accumulated profits of corporation FC computed in the same manner as in example 1 ($\$40 \times 60/60$)-----	40
(vi) Corporation P is deemed to have paid a foreign tax with respect to the 1962 accumulated profits of corporation FC in the same manner as existing rules ($\$40 \times 60/100 \times 30/60$)-----	12
(vii) Total foreign tax corporation P is deemed to have paid ((v) + (vi))---	52

The new subsections (a)(1), (b)(1), and (c)(1)(A), when applied to dividends received after December 31, 1964, will not be affected by the fact that there may have been in an earlier year a partial distribution of accumulated profits to which the *Chicle* rule applied. For example, if a wholly owned foreign subsidiary (not a less developed country corporation) of a domestic corporation had total profits of \$100, upon which foreign taxes of \$40 had been paid, accumulated

profits under existing law would be \$60. Under the *Chicle* rule the taxes paid with respect to the accumulated profits would be \$24 ($\$40 \times \$60/100$). Upon a distribution of one-half (\$30) of such accumulated profits the domestic parent would be entitled under existing section 902(a) to a maximum credit of \$12. However, if at any time after 1964, the subsidiary distributes another dividend, \$30, with respect to the accumulated profits of such earlier year, and taxes deemed paid, determined in accordance with new section 902(a)(1), will be the same proportion of total taxes as the dividend bears to accumulated profits in excess of foreign taxes. Thus, the total tax of \$40 would be multiplied by the fraction 30/60 and the parent would be entitled under section 902(a), as amended, to a credit of \$20. No account is to be taken of the foreign tax of \$8 which, because of the *Chicle* rule, was not taken into account in the earlier dividend year.

If a dividend from a foreign corporation (not a less developed country corporation) is distributed out of its accumulated profits for a taxable year beginning after 1962, and such accumulated profits are composed in whole or in part of dividends which were received from accumulated profits of a foreign subsidiary of the foreign corporation accumulated in taxable years beginning after 1962, both subsections (a)(1) and (b)(1) applies. After 1964 the new subsections (a)(1) and (b)(1) of section 902 will apply whether the distributions are from accumulated profits of the foreign corporation and its foreign subsidiary for their taxable years beginning after 1962 or before 1963. The computation involving these rules may be illustrated by the following example involving corporation P, a domestic corporation which owns 100 percent of the voting stock of foreign corporation FC (not a less developed country corporation) which in turn owns 100 percent of the voting stock of foreign subsidiary FS. It is assumed that all transactions have taken place and are related to the taxable year 1963.

Example 3

(A) Application of section 902(b)(1) to determine tax deemed to be paid by corporation FS:

(i) Gains, profits, and income of corporation FS	\$100
(ii) Foreign tax paid by corporation FS with respect to such gains, profits, and income	20
(iii) Accumulated profits in excess of taxes of corporation FS: \$100 less \$20	80
(iv) Dividends paid by corporation FS to corporation FC	40
(v) Corporation FS foreign tax which is deemed paid by corporation FC: $\$20 \times 40/80$	10

(B) Application of amended section 902(a)(1) to determine tax deemed to be paid by corporation P:

(i) Gains, profits, and income of corporation FC:	
Business profits	\$100
Dividends from corporation FS	40
	140
(ii) Foreign tax paid by corporation FC with respect to its gains, profits, and income	40
(iii) Accumulated profits in excess of taxes paid by corporation FC: \$140 less \$40	100
(iv) Dividend paid by corporation FC to corporation P	80
(v) Foreign tax paid (\$40) and deemed paid (\$10) by corporation FC	50
(vi) Foreign taxes paid and deemed paid by corporation FC which are deemed paid by corporation P: $\$50 \times 80/100$	40

Where a dividend from a foreign corporation (not a less developed country corporation) before 1965 is attributable to its accumulated profits for a taxable year beginning after 1962, but which profits are composed in part of a dividend received by such foreign corporation from the accumulated profits of its foreign subsidiary for a taxable year or years of the subsidiary beginning before 1963, for purposes of computing the foreign tax credit a pro rata amount of the dividend received from the foreign corporation will be deemed to consist of accumulated profits of its foreign subsidiary attributable to the period before 1963. Existing law will apply to that portion of the foreign tax paid or accrued or deemed paid by the foreign corporation with respect to such pro rata amount of the dividend considered attributable to the accumulated profits of its subsidiary for taxable years before 1963 and the amendment made by section 9 of the bill will apply to the balance of such tax.

The new subsections (a)(1), (b)(1), and (c)(1)(A) apply to the extent that a domestic corporation receives dividends from the accumulated profits of a foreign corporation for a taxable year for which it is not a less developed country corporation, and shall apply although such accumulated profits include dividends from accumulated profits of another foreign corporation for a taxable year for which such other foreign corporation is a less developed country corporation. Such provisions do not apply if the dividend is from accumulated profits of a corporation for a taxable year for which it is a less developed country corporation even though such accumulated profits includes dividends from accumulated profits of another foreign corporation for a taxable year for which such other corporation is not a less developed country corporation.

The new subsection (d) of section 902 as revised defines a less developed country corporation for the purpose of section 902 as a foreign corporation—

(1) which, for its taxable year, is a less developed country corporation under section 955(c) (1) or (2), or

(2) which owns at least 10 percent of all classes of stock entitled to vote of a less developed country corporation under section 955(c)(1), derives at least 80 percent of its gross income for its taxable year from sources within less developed countries under section 955(c)(1)(A), and at least 80 percent in value of its assets on each day of such year consists of property described in section 955(c)(1)(B).

A foreign corporation which is a less developed country corporation for its first taxable year beginning after December 31, 1962, is to be treated as such for each of its prior taxable years. Thus, if, after December 31, 1964, a domestic corporation receives a dividend from a foreign corporation from its accumulated profits for a taxable year beginning before December 31, 1962, the rules of existing law apply if such foreign corporation is a less developed country corporation for its first taxable year beginning after December 31, 1962, without regard to its earlier status.

(b) *Inclusion in gross income of amount equal to taxes deemed paid.*— Subsection (b) of section 9 of the bill amends part II of subchapter B of chapter 1 (relating to items specifically included in income) by adding at the end thereof a new section 78. Section 78 requires a domestic corporation to include in gross income as a dividend an amount equal

to the taxes deemed, as a result of section 902 (a)(1), (b)(1), and (c)(1)(A) of the code, as added by subsection (a) of section 9 of the bill, or as a result of section 960(a)(1)(C) (relating to taxes paid by foreign corporation), as added by section 12 of the bill, to have been paid by the domestic corporation, if the domestic corporation chooses the benefits of the foreign tax credit. Section 78 does not apply where the taxes attributable to a particular distribution are computed under present law. Thus, in the preceding example 1 corporation P will include \$15 in gross income as a dividend. In example 2 corporation P will include only \$40 in gross income since \$12 of foreign tax deemed to be paid by corporation P is computed under existing rules. In example 3 corporation P will include \$40 in gross income.

The amount included in gross income by operation of section 78 is treated as a dividend in the same manner as a dividend actually received by the domestic corporation from a foreign corporation. For example, a section 78 dividend is included in gross income under section 61(a)(7); is personal holding company income for purposes of section 543(a)(1); and may be a portion of accumulated taxable income for purposes of section 535. However, a section 78 dividend is not a dividend for purposes of section 245 of the code (relating to deduction for dividends received from certain foreign corporations).

(c) *Determination of source of dividends received from certain foreign corporations.*—Subsection (c) of section 9 of the bill amends section 861(a)(2)(B) of the code by striking out “to the extent exceeding the amount of the deduction allowable under section 245 in respect of such dividends” and inserting in lieu thereof “to the extent exceeding the amount which is 100/85ths of the amount of the deduction allowable under section 245 in respect of such dividends.” This restores the rule contained in section 119(a)(2)(B) of the 1939 Code, as added by the Revenue Act of 1951. The effect of the change is to establish a closer correlation between the operation of sections 245 and 861(a)(2)(B) than existing law provides.

Under present section 861(a)(2)(B), the excess of the amount of a dividend taken into account in determining the dividends received deduction under section 245 over the amount allowed as a deduction, is determined to be income from sources without the United States for purposes of the foreign tax credit provisions. As a result, 15 percent of that portion of the dividend considered as derived from sources within the United States within the meaning of section 245 is treated as income from sources within the United States for purposes of that section, but, conversely, is treated as income from sources without the United States under section 861(a)(2)(B) for foreign tax credit purposes. Subsection (c) removes this inconsistency by treating as income from sources without the United States for foreign tax credit purposes only the amount of the dividend in excess of one hundred eighty-fifths of the dividends received deduction.

(d) *Technical amendments.*—Subsection (d) of section 9 of the bill conforms the table of sections for part II of subchapter B of chapter 1 of the code to the addition of the new section 78 and adds a cross-reference to section 901 of the code. In addition it makes technical changes in section 535(b)(1) and 545(b)(1) to prevent the amendments made by section 9 of the bill from changing “accumulated taxable income” for purposes of the accumulated earnings tax and “undistributed personal holding company income” for purposes of the

personal holding company tax and to offset the effects of section 78 whereby these incomes are increased by reason of the taxes deemed to have been paid under section 902 (a)(1), (b)(1), and (c)(1)(A). These technical changes will allow as a deduction the taxes deemed to have been paid under section 902 (a)(1), (b)(1), and (c)(1)(A).

(e) *Effective date.*—Subsection (e) of section 9 of the bill provides that the amendments made by section 9 are to be applicable to dividends which are received by domestic corporate taxpayers in their taxable years beginning after December 31, 1962, but only to the extent that such distributions are made out of the accumulated profits of foreign corporations for their taxable years beginning after December 31, 1962. However, the amendments made by section 9 of the bill will be applicable to all dividends received by domestic corporate taxpayers from foreign corporations after December 31, 1964, regardless of the year to which the accumulated profits are attributable.

If, before 1965, the distribution from a foreign corporation for its taxable year beginning after December 31, 1962, is out of profits which are attributable to a distribution received by such foreign corporation from its foreign subsidiary, the effectiveness of the amendments depends on the taxable year to which the subsidiary's distribution is attributable. If the distribution is out of the subsidiary's accumulated profits for taxable years beginning after December 31, 1962, the amendments will be applicable. However, if the distribution is attributable to the subsidiary's accumulated profits for taxable years beginning before January 1, 1963, the present law will continue in effect.

The amendments are not applicable to a domestic corporation receiving a distribution from a foreign corporation prior to January 1, 1965, unless such distribution (1) is made out of profits of a foreign corporation accumulated in a taxable year beginning after December 31, 1962, and (2) is received by the domestic corporation in a taxable year beginning after December 31, 1962. Therefore, if for example, a foreign corporation is on a calendar-year basis and it makes a distribution on November 15, 1963, out of its accumulated profits for 1963 to a domestic corporation whose taxable year began on December 1, 1962, the present law would be applicable.

SECTION 10. SEPARATE LIMITATION ON FOREIGN TAX CREDIT WITH RESPECT TO CERTAIN INTEREST INCOME

Section 10 of the bill, for which there is no corresponding provision in the bill as passed by the House, amends section 904 (relating to limitations on the foreign tax credit) by redesignating subsection (f) as subsection (g) and by inserting after subsection (e) a new subsection (f) relating to special rules in case of certain interest income.

Existing law

Under section 904(a) of existing law a taxpayer may elect between two alternative limitations on the amount of the foreign tax credit:

- (1) The per country limitation limits the credit for tax paid or accrued to any one foreign country (or U.S. possession) to the proportion of U.S. tax before credit which taxable income from sources within such country (or possession) bears to the entire taxable income;

(2) The overall limitation limits the total credit for taxes paid or accrued to all foreign countries or U.S. possessions to the proportion of U.S. tax before credit which taxable income from all sources without the United States bears to the entire taxable income.

Separate limitation for interest income.—Paragraph (1) of new subsection (f) requires a taxpayer to apply subsection (a) of section 904 (and the related rules of subsecs. (c), (d), and (e)) with respect to interest described in paragraph (2) separately from all other income.

Paragraph (2) defines the interest income to which paragraph (1) applies as taxable income from interest other than interest—

(A) derived from transactions directly related to the active conduct of a trade or business in a foreign country or U.S. possession,

(B) derived in the conduct of a banking, financing, or similar business, or

(C) received from a corporation in which the taxpayer owns at least 10 percent of the voting stock.

Paragraph (3) provides that the overall limitation does not apply to interest described in paragraph (2) and that the Secretary of the Treasury or his delegate shall by regulations prescribe the manner of application of the foreign tax credit carrybacks and carryovers where the taxpayer elects the overall limitation as to other income.

Paragraph (4) provides transitional rules for foreign tax credit carrybacks and carryovers. Under subparagraph (A), carrybacks of taxes paid or accrued in taxable years beginning after the date of enactment of the bill carried to taxable years beginning on or before such date are determined without regard to new subsection (f). Where such taxes are carried back to taxable years beginning on or before such date of enactment and are partially deemed paid or accrued in such taxable years, the excess, if any, when carried forward is deemed paid or accrued in a taxable year beginning after the date of enactment, with respect to—

(i) interest (described in par. (2)) in the ratio that taxes paid or accrued with respect to such interest to a foreign country or possession in the year in which the tax was actually paid or accrued (in excess of the applicable limitation for such year) bears to the total tax paid or accrued to such country or possession in such year (in excess of the applicable limitation for such year); and

(ii) other income in the ratio that taxes paid or accrued with respect to such other income to a foreign country or possession in the year in which the tax was actually paid or accrued (in excess of the applicable limitation for such year) bears to the total taxes paid or accrued to such country or possession for such year (in excess of the applicable limitation for such year).

Under subparagraph (B) taxes, paid or accrued in a taxable year beginning on or before the date of enactment, are when carried forward deemed paid or accrued in a taxable year beginning after such date with respect to—

(i) interest (described in par. (2)) in the ratio that taxes paid or accrued to a foreign country or possession in the later year with respect to such interest bears to the total taxes paid or accrued in such year to such country or possession; and

(ii) other income in the ratio that taxes paid or accrued to a foreign country or possession in the later year with respect to such other income bears to the total taxes paid or accrued in such year to such country or possession.

If the taxpayer uses the overall limitation provided in section 902 (a)(2) with respect to income other than the interest income to which paragraph (2) applies, the computation under subparagraphs (A) and (B) of paragraph (4) will, under the provisions of paragraph (3), be computed, with respect to such other income, on the basis of the overall limitation.

Example 1.—Corporation M, to which the per country limitation applies, has for the taxable year 1963 \$50,000 of taxable income described in paragraph (2) from sources within country X, \$100,000 of other taxable income from sources within that country, and \$150,000 of taxable income (none of which is interest income) from sources within country Y. M has no other income (or losses) from sources without the United States in 1963 and has total taxable income from all sources (including countries X and Y) of \$2 million. It pays or accrues income tax for 1963 to country X of \$15,000 with respect to income described in paragraph (2), and \$60,000 with respect to other income, and it pays or accrues \$75,000 income tax to country Y. M's U.S. tax (before credit) is \$1,040,000. M's country X foreign tax credit limitation with respect to interest described in paragraph (2), is $\$1,040,000 \times \frac{\$50,000}{\$2,000,000}$, or \$26,000, so that the full amount of the \$15,000 of country X tax is allowed as a credit for 1963. M's country X limitation on credit for taxes with respect to other income is $\$1,040,000 \times \frac{\$100,000}{\$2,000,000}$, or \$52,000 so that \$52,000 of the \$60,000 of country X tax with respect to such other income is allowed as a credit for 1963. M's country Y limitation, $\$1,040,000 \times \frac{\$150,000}{\$2,000,000}$, or \$78,000, is unaffected by the new subsection (f) since M has no taxable income described in paragraph (2) from sources within country Y. M's total foreign tax credit is therefore \$142,000 (\$15,000 + \$52,000 + \$75,000).

Example 2.—Assume the same facts as in example 1 except that M has elected the overall limitation. The limitation on the credit for foreign tax paid or accrued to country X with respect to the income described in paragraph (2) is $\$1,040,000 \times \frac{\$50,000}{\$2,000,000}$, or \$26,000, the same as in example 1, and would not change even if M also had taxable income described in paragraph (2) from sources within some other foreign country, since the overall limitation is unavailable with respect to income described in paragraph (2). M's overall limitation with respect to foreign tax on all other income is $\$1,040,000 \times \frac{\$100,000 + \$150,000}{\$2,000,000}$, or \$130,000, so that of the \$135,000 (\$60,000 + \$75,000) foreign taxes paid or accrued with respect to income other than income described in paragraph (2), \$130,000 is allowed as a credit. M's total credit is therefore \$145,000 (\$130,000 + \$15,000).

Example 3.—Corporation O, which does not elect the overall limitation, paid or accrued to country X for the taxable year 1962

\$100 of foreign tax in excess of the section 904 limitation. Corporation O has no income from sources within any other country. For 1963, O pays or accrues to country X \$20 in tax on income described in paragraph (2) and \$80 in tax on other income. The section 904 limitation for 1963 is \$50 with respect to income described in paragraph (2) and \$80 with respect to other income. With respect to the \$100 carryover from 1962, corporation O is deemed to have paid or accrued in 1963 \$20, i.e., $\frac{\$20}{\$100} \times \$100$. The remaining \$80 of the carryover may be carried to 1964, and assuming the same amount of taxes are paid or accrued in 1964 as in 1963 and the same limitations are applicable, O is deemed to have paid or accrued in 1964 \$16, i.e., $\frac{\$20}{\$100} \times \$80$.

Example 4.—Assume the same facts as in example 3 except that the limitation under section 904 for 1962 exceeds the tax paid or accrued for that year by \$10, and the limitation for 1964 with respect to income other than that described in paragraph (2) is \$50. Under these facts, the excess of the \$80 tax paid or accrued for 1964 with respect to other income over the limitation of \$50, or \$30, is carried back first to 1962, and \$10 will be deemed paid or accrued for that year. The remaining \$20 is carried to 1963, but no amount will be deemed paid or accrued in 1963 since the tax being carried back was paid or accrued with respect to income other than that described in paragraph (2) and the limitation for 1963 with respect to such income does not exceed the tax actually paid or accrued for such year with respect to such income.

Example 5.—Assume the same facts as in example 4 except that the limitation for 1964 with respect to income described in paragraph (2) is \$10. The excess of the \$20 tax paid or accrued for 1964 with respect to income described in paragraph (2) over the limitation of \$10, or \$10, is aggregated with the excess tax of \$30 paid in 1964 with respect to other income, making a total of \$40. Of this aggregate amount, \$10 will be deemed paid or accrued in 1962 as in example 4. Of the remaining \$30, $\$7.50 \left(\frac{\$10}{\$40} \times \$30 \right)$ will be deemed paid or accrued in 1963 with respect to interest income described in paragraph (2). No amount will be deemed paid or accrued in 1963 with respect to other income because the limitation for that year with respect to other income (\$80) does not exceed the tax actually paid or accrued for that year with respect to such other income (\$80).

Effective date.—The new subsection applies with respect to taxable years beginning after the date of enactment of the bill but only with respect to interest resulting from transactions consummated after April 2, 1962.

SECTION 11. EARNED INCOME FROM SOURCES WITHOUT THE UNITED STATES

This section is the same as section 12 of the bill as passed by the House except for the addition of a presumption in certain circumstances with respect to bona fide residence and a temporary exemption for certain noncash remuneration.

(a) *Limitation on amount and type of income excluded.*—Subsection (a) of section 11 of the bill amends section 911 of the 1954 Code. This amendment retains the provisions of section 911 which require, under certain circumstances, the exclusion of earned income from gross income of an individual who has been a bona fide resident, or is physically present, in a foreign country. However, under the amendment there will be dollar limitations on the amounts which may be excluded under section 911 by any individual. The amendment also imposes a requirement as to time of receipt and, for some purposes, attributes amounts received to the taxable year in which the services to which the amounts are attributable were performed. The amendment also provides that no amount received as a pension or annuity is excludable under section 911. Your committee has added amendments which provide a presumption in certain circumstances with respect to bona fide residence and a temporary exemption for certain noncash remuneration.

SECTION 911. EARNED INCOME FROM SOURCES WITHOUT THE UNITED STATES

(a) *General rule.*—Subsection (a) of section 911, as amended by section 11 of the bill, is the same as existing law in that it provides that in the case of an individual citizen of the United States—

(1) who has been a bona fide resident of a foreign country or countries for an uninterrupted period which includes an entire taxable year, or

(2) who during any period of 18 consecutive months is present in a foreign country or countries during at least 510 full days in such period,

amounts received from sources without the United States (except amounts paid by the United States or any agency thereof) which constitute earned income attributable to services performed during the uninterrupted period or during an 18-month period, whichever applies, may be excluded from gross income. However, the amended section 911(a) contains a new provision to the effect that the amount excluded under that provision will be computed by applying special rules contained in subsection (c). The new provision referring to the special rules in subsection (c) is in lieu of the unlimited exclusion provided by existing law with respect to bona fide foreign residence, and the \$20,000 limitation with respect to physical presence in a foreign country provided by existing law. Subsection (a) also retains the provision of existing law that no deductions (other than the deductions allowed by sec. 151, relating to personal exemptions) will be allowed to the extent such deductions are properly allocable to or chargeable against amounts excluded from gross income under such subsection.

(b) *Definition of earned income.*—Subsection (b) of the amended section 911 continues, without change, the existing definition of “earned income.”

(c) *Special rules.*—Subsection (c) of section 911, as amended by the bill, provides rules for purposes of computing the amount excludable from gross income of an individual under section 911(a).

Paragraph (1) of section 911(c) contains the limitations on the amount excludable under section 911(a). It provides, as a general rule, that the amount excluded for any taxable year is not to exceed

an amount which is to be computed on a daily basis at an annual rate of \$20,000. However, the annual rate is to be \$35,000 in the case of an individual who qualifies as a bona fide resident of a foreign country or countries under section 911(a)(1), but only with respect to taxable years (or a portion of a taxable year) occurring immediately after such individual has been a bona fide foreign resident for any uninterrupted period of 3 consecutive years (36 consecutive months). The amount excludable accrues on a daily basis throughout the taxable year. The number of days to be used in making the computation on a daily basis is the number of days in the taxable year for which the exclusion is claimed.

The manner of computing the amount excludable under section 911(a) on a daily basis at the prescribed annual rates may be illustrated by the following example:

Example.—A, a U.S. citizen, who files his returns on a calendar year basis, is privately employed, and is a bona fide resident of France for the period April 1, 1963, through June 30, 1968. The amounts excludable from his gross income for the various calendar years under the provisions of section 911(a) which are computed by applying the special rules contained in section 911(c) are not to exceed the following amounts: For the year 1963, \$15,068.49 ($275/365 \times \$20,000$); for the year 1964, \$20,000 ($366/366 \times \$20,000$); for the year 1965, \$20,000 ($365/365 \times \$20,000$); for the year 1966, \$31,301.37 ($90/365 \times \$20,000$ plus $275/365 \times \$35,000$); for the year 1967, \$35,000; and, for the year 1968, \$17,404.37 ($182/366 \times \$35,000$).

An individual who, on January 1, 1963, has been a bona fide foreign resident for an uninterrupted period in excess of 3 consecutive years is immediately entitled to the benefits of the annual rate of \$35,000. An individual who returns and takes up residence in the United States is, upon resuming bona fide foreign residence, only entitled to the benefits of the annual rate of \$20,000 until such individual completes another uninterrupted period of 3 consecutive years of bona fide foreign residence.

Paragraph (2) of section 911(c) provides that, for purposes of applying the limitation in paragraph (1), amounts received are to be considered received in the taxable year in which the services to which the amounts are attributable are performed. For example, amounts received during the taxable year 1965 attributable to services performed during the taxable year 1964 will, for purposes of applying the limitation in section 911(c)(1), be considered received in the taxable year 1964. Thus, if I (to whom the \$20,000 limitation applies) receives \$16,000 in 1964 and \$7,000 in 1965, both amounts being attributable to his 1964 services, \$3,000 of the \$7,000 received in 1965 would be includible in his gross income for 1965.

Paragraph (3) of section 911(c) provides in effect that in applying the rules of paragraph (1), the amount excludable under section 911(a) is to be neither increased nor decreased solely by operation of community property law.

The application of the rule contained in section 911(c)(3) may be illustrated by the following examples:

Example 1.—H, a U.S. citizen, qualifies under section 911(a) and receives \$40,000 during a taxable year for services performed abroad during such taxable year. He has been abroad for less than 3 consecutive years. W, the wife of H, earns no income of her

own and continues to live in a community property State in the United States. The marital domicile also continues in such State. H and W file a joint return. The aggregate amount excludable from gross income under section 911 is \$20,000. If H and W had filed separate returns, the aggregate amount excludable under section 911 would be \$20,000.

Example 2.—The facts are the same as in example 1, except that W also resides abroad. Whether H and W file their returns separately or jointly, the aggregate amount excludable under section 911 is \$20,000. If W also qualifies under section 911(a) and receives \$10,000 during the taxable year for services she performed abroad during such taxable year, the aggregate amount excludable under section 911 is \$30,000 (whether a joint return or separate returns are filed).

Similarly, in a noncommunity property jurisdiction, if H and W both qualify under section 911(a) and receive \$40,000 and \$10,000, respectively, for services performed abroad during the taxable year, the aggregate amount excludable under section 911 is \$30,000.

Paragraph (4) of section 911(c) establishes a requirement as to time of receipt by providing that no amount received after the close of the taxable year following the taxable year in which the services to which the amounts are attributable are performed may be excluded under section 911(a). For example, an amount received on or before the close of the taxable year 1965 which is attributable to services performed during the taxable year 1964 will satisfy the requirement as to receipt of section 911(c)(4). However, an amount received after the close of the taxable year 1965 which is attributable to services performed during the taxable year 1964 will not satisfy the requirement as to receipt of section 911(c)(4) and, therefore, will in no event be excludable under section 911(a).

Subparagraph (A) of section 911(c)(5) provides that no amount received as a pension or annuity may be excluded under section 911(a). The result is the same whether the recipient of such pension or annuity is a resident or a nonresident of the United States. Subparagraph (B) provides that no amount included in gross income by reason of section 402(b) (relating to taxability of beneficiary of nonexempt trust), section 403(c) (relating to taxability of beneficiary under a non-qualified annuity), or section 403(d) (relating to taxability of beneficiary under certain forfeitable contracts purchased by exempt organizations) may be excluded under section 911(a). Thus, amounts contributed by an employer to certain plans which do not qualify under section 401 and in which an individual has nonforfeitable rights, must be included in such individual's gross income currently. The amounts of such contributions are not excludable under section 911(a).

Your committee has added a new paragraph (6) to section 911(c) which provides that a statement by an individual who has earned income from sources within a foreign country that he is not a resident of such country, if he is held not subject as a resident of that country to the income tax of that country by its authorities with respect to such earnings, shall be conclusive evidence that he is not a bona fide resident of that country for purposes of section 911(a)(1).

Your committee has also added a new paragraph (7) to section 911(c) which provides that if an individual receives compensation from sources without the United States (except from the United

States or any agency thereof) in the form of a right to use property or facilities, the limitation under section 911(c)(1) applicable with respect to such individual, (A) for a taxable year ending in 1963, shall be increased by an amount equal to the amount of such compensation so received during such year; (B) for a taxable year ending in 1964, shall be increased by an amount equal to two-thirds of such compensation so received during such year; and (C) for a taxable year ending in 1965, shall be increased by an amount equal to one-third of such compensation so received during such year.

Example 1.—X, a U.S. citizen who files his returns for the calendar year, qualifies under section 911(a) and has been abroad for less than 3 consecutive years. During the taxable years ending December 31, 1963, 1964, 1965, and 1966, X receives compensation in the form of a right to use a residence, such use having a fair market value of \$6,000 per year. Under the provisions of section 911(c)(7), the applicable limitation under section 911(c)(1) will be increased in the following amounts:

Taxable year ending:	Amount
Dec. 31, 1963-----	\$6, 000
Dec. 31, 1964-----	4, 000
Dec. 31, 1965-----	2, 000
Dec. 31, 1966-----	0

Example 2.—The facts are the same as in example 10 except that X returns and takes up residence in the United States on July 1, 1965. X will be entitled to increase the applicable limitation under section 911(c)(1) for the taxable year ending December 31, 1965, in an amount limited to one-half of \$2,000, or \$1,000.

(b) *Computation of employees' contributions.*—Existing section 72(f)(2) of the code provides that, in the case of employees' annuities, employees' contributions include amounts contributed by the employer if such amounts would have been exempt from tax had they been paid to the employee directly. Existing law continues to apply to amounts contributed on or before December 31, 1962, for services performed on or before such date.

Subsection (b) of section 11 of the bill amends paragraph (2) of section 72(f) of the code by providing, in general, that such paragraph is not to apply to amounts which were contributed by the employer after December 31, 1962, and which would have been exempt from tax by reason of section 911 had they been paid to the employee directly. However, the preceding sentence does not apply to amounts which were contributed by the employer to provide pension or annuity credits, to the extent such credits are attributable to services performed before January 1, 1963, and are provided pursuant to pension or annuity plan provisions in existence on March 12, 1962, and on that date applicable to such services. Thus, in effect, the first sentence of the amendment contained in section 11(b) of the bill provides that an employee's basis will not be increased by reason of foreign service contributions made by an employer after December 31, 1962, and which would have been exempt from tax by reason of section 911 had they been paid to the employee directly. However, existing law would continue to apply to contributions made after December 31, 1962, to provide benefits attributable to services performed before January 1, 1963, to the extent that (1) such benefits are provided by a plan which is in existence on March 12, 1962, and (2) such con-

tributions are required to provide the benefits set forth in the plan on March 12, 1962. Thus, certain amounts attributable to services performed before January 1, 1963, and contributed after December 31, 1962, to fund current or past service credits may be added to an employee's basis. However, to the extent benefits are initially provided after March 12, 1962, or to the extent existing benefits are increased after such date, amounts attributable to the new or increased benefits may not be added to an employee's basis even though the new or increased benefits are attributable to services performed before January 1, 1963.

(c) *Effective date.*—Subsection (c) of section 11 of the bill contains the effective date provisions applicable to the amendments to sections 911 and 72(f) of the code.

Paragraph (1) of section 11(c) of the bill provides that, except as provided in paragraph (2), the amendments made by section 11 of the bill are to apply to taxable years ending after December 31, 1962. Paragraph (2) provides that, with respect to the changes in section 911 of the code, the amendment made by section 11(a) of the bill is to apply only with respect to amounts received after December 31, 1962, and which are attributable either, as provided in subparagraph (A), to services performed after such date, or, as provided in subparagraph (B), to services performed on or before such date, but only if on March 12, 1962, there existed no right (whether forfeitable or nonforfeitable) to receive such amounts. Thus, in effect, the effective date provision, with respect to the amendment to section 911, applies existing law to amounts received after December 31, 1962, which are attributable to services performed before January 1, 1963, if on March 12, 1962, a right existed (whether forfeitable or nonforfeitable) to receive such amounts. On the other hand, if amounts are received after December 31, 1962, which are attributable to services performed before January 1, 1963, to which the recipient did not have a right in existence on March 12, 1962, section 911, as amended by section 11 of the bill, will apply to such amounts. In the event a right to receive an amount attributable to services performed before January 1, 1963, existed as of March 12, 1962, and thereafter such amount is increased, section 911, as amended by section 11 of the bill, will apply to such increase.

The application of the provisions of section 11(c)(2) of the bill may be illustrated by the following examples:

Example 1.—A, a U.S. citizen who files his returns on a calendar-year basis, is privately employed and a bona fide resident of Italy for the period January 1, 1961, through December 31, 1963. He is compensated at a rate of \$25,000 per year and receives such compensation in the year it is earned. The amounts excludable from gross income for the various calendar years and the applicable provisions of section 911 of the code are as follows: for the years 1961 and 1962, \$25,000 under section 911 before amendment by section 11 of the bill; for the year 1963, \$20,000 under section 911, as amended by the bill.

Example 2.—A, the taxpayer described in example 1, receives on May 1, 1963, \$5,000 as a supplementary salary payment for services performed during the taxable year 1962. Such amount is received pursuant to an agreement in existence on March 12, 1962. Under section 11(c)(2)(B) of the bill, such amount will be subject to section 911 of the code before amendment. The entire supplementary salary

payment will be excludable from gross income under section 911(a)(1) (before amendment).

Example 3.—The facts are the same as in example 2, except that no right to receive the \$5,000 supplementary salary payment is in existence on March 12, 1962. Under section 11(c)(2)(B) of the bill, such amount is to be subject to the provisions of section 911, as amended by the bill. Under section 911, as amended, the amount excludable is to be computed under section 911(c). Under section 911(c)(2), the supplementary salary payment is to be considered received in 1962. Under section 911(c)(1), that portion of the amount received which, when added to other qualifying amounts received during the taxable year 1962, does not exceed an amount computed on a daily basis at an annual rate of \$20,000 will be excludable. Since, under the facts set forth in example 1, A received excludable amounts in excess of \$20,000 during the taxable year 1962, no part of the supplementary salary payment is to be excludable from gross income.

SECTION 12. CONTROLLED FOREIGN CORPORATIONS

(a) *Tax on United States shareholders.*—Subsection (a) of section 12 of the bill, corresponding to section 13 of the bill as passed by the House, adds a new subpart F (secs. 951–964) and a new subpart G (secs. 970–972) to part III of subchapter N of the Internal Revenue Code of 1954.

SECTION 951. AMOUNTS INCLUDED IN GROSS INCOME OF UNITED STATES PERSONS

(a) *Amounts included.*—Subsection (a) provides that, if a foreign corporation is a controlled foreign corporation for an uninterrupted period of 30 days or more during its taxable year, then any United States person who is a United States shareholder (as defined in subsection (b)) and who owns (within the meaning of section 958(a)) stock in such corporation, on the last day of such taxable year on which it was a controlled foreign corporation must include in gross income for his taxable year (in which or with which ends the taxable year of the controlled foreign corporation) the sum of (except as provided by section 963, relating to the receipt of minimum distributions):

(1) his pro rata share of the corporation's subpart F income for its taxable year, and his pro rata share of the corporation's previously excluded subpart F income withdrawn from investment in less developed countries for such year; and

(2) his pro rata share of the corporation's increase in earnings invested in United States property for its taxable year which is not excluded from gross income under section 959(a)(2).

The pro rata shares are included in the income of the United States shareholder even though there may be intervening entities in a chain between the controlled foreign corporation and such shareholder. The pro rata share to be included by the United States shareholder (if the corporation is a controlled foreign corporation for its entire taxable year) is that amount which would have been distributed with respect to the ownership interest of such person if the corporation had distributed the total amount of its subpart F income, the total of its previously excluded subpart F income withdrawn from investment in

less developed country corporations, and the total of the increase in its earnings invested in United States property on the last day of its taxable year. If the corporation is a controlled foreign corporation for only part of its taxable year, paragraphs (2), (3), and (4) of section 951(a) provide that the pro rata share is that which would have been distributed (on the last day of the corporation's taxable year on which it was a controlled foreign corporation) if the controlled foreign corporation had distributed pro rata an amount which bears to such total amount the same ratio that the part of the year during which the corporation was a controlled foreign corporation bears to the entire taxable year.

Example (1).—X, a United States shareholder, wholly owns throughout 1965 Y, a controlled foreign corporation, which has \$50 of subpart F income, \$50 of previously excluded subpart F income withdrawn from investment in less developed countries, and \$100 of earnings and profits for its taxable year 1965. Both X and Y use a calendar year as their taxable year. X, for taxable year 1965, must include \$100 (\$50 + \$50) in gross income as if such amount had been distributed on December 31, 1965.

Example (2).—X and T, United States shareholders with the calendar year as a taxable year, each acquire on July 1, 1963, 30 percent of the voting stock of Y, a foreign corporation (having only one class of stock) which became, as of that day, a controlled foreign corporation. Y has no subpart F income or previously excluded subpart F income withdrawn from investment in less developed countries, has \$100 of earnings and profits, and has a \$100 increase in earnings invested in United States property, for its 1963 taxable year (also a calendar year). For their 1963 taxable year, X and T each must include in gross income \$15, the amount which would have been distributed with respect to their stock if Y had distributed pro rata $\frac{1}{2}$ of \$100, or \$50 on December 31, 1963.

An increase in earnings invested in United States property is included in gross income only to the extent that it exceeds the subpart F income for the current taxable year and previous taxable years, but only if such subpart F income (here used to include subpart F income previously excluded because of qualified investment in less developed countries but now withdrawn from such investment) has not already been so used as an offset or has not been actually distributed in a previous taxable year. Distributions from subpart F income and from amounts taxed under section 951(a)(1)(B) as increases in earnings invested in United States property are excluded from gross income under section 959. Rules for allocation of distributions to subpart F income, increases in earnings invested in United States property, or other earnings and profits are made under the rules of section 959(c).

In a case in which stock of a controlled foreign corporation is transferred by any person to a United States shareholder during a taxable year, if the transferor receives a distribution with respect to such stock, the acquiring shareholder, under section 951(a)(2)(B), may reduce the amount he would otherwise be required to include in gross income under section 951(a)(1)(A)(i) by the amount of such dividend. The corresponding provision of the bill as passed by the House applied only to transfers among United States persons. Section 951(a)(2)(B) also provides a limitation (not contained in the bill as passed by the House) that the reduction is only to the extent the

amount of the distribution with respect to stock by the corporation does not exceed the distribution which would have been distributed with respect to such stock if the corporation had distributed an amount which bears the same ratio to subpart F income of the corporation for the taxable year as the part of such year during which such shareholder did not own (within the meaning of section 958(a)) such stock bears to the entire year. The exclusion applies only where the dividend is paid to a person outside the chain of ownership described in section 958(a)(2) since otherwise the United States person is a United States shareholder both before and after the transfer.

Example (1).—Assume that A, a United States shareholder, owns 20 percent of the one class of stock in Z, a controlled foreign corporation, and that on July 1, 1963, immediately after receiving a \$12 dividend, A transfers the stock to B, a United States shareholder. A, B, and Z use the calendar year as the taxable year. Z's entire earnings and profits for 1963 consists of \$100 all of which is subpart F income. A must include in gross income the \$12 dividend. B must include in his gross income for 1963, \$10, computed as follows:

(a) The amount distributed by the controlled foreign corporation ($\$12 \div 20$ percent)-----	\$60
(b) Limitation on the distribution ($\$100 \times \frac{1}{2}$)-----	50
(c) Limitation on the reduction (20 percent of \$50)-----	10
(d) Amount included in gross income under section 951(a)(1)(A)(i) (\$20 minus \$10)-----	10

Example (2).—A, a United States shareholder, owns all the one class of stock of Y, a foreign corporation, which in turn owns all the one class of stock in Z which for its taxable year has \$100 subpart F income. A, Y, and Z, each uses the calendar year as the taxable year. On July 1, Z distributes \$100 to Y. A must include in gross income \$100 of Z's subpart F income, unreduced under section 951(a)(2)(B) by the distribution by Z since A is the owner of the Z stock within the meaning of section 958(a) for the entire year.

Example (3).—The facts are the same as in example (2) except that A acquired the stock in Y from B (not in the chain of ownership described in section 958(a)(2)) on July 1, and that Z, immediately before the transfer, distributed \$50 to B. Under section 951(a)(2)(B) the \$100 otherwise required to be included in X's gross income is reduced by \$50.

(b) *United States shareholder defined.*—Subsection (b) defines "United States shareholder" with respect to any foreign corporation to mean a United States person (as defined in section 957(d)) who owns under section 958(a), or is considered as owning under section 958(b), 10 percent or more of the total combined voting power of all classes of stock entitled to vote of such foreign corporation. Only a United States shareholder as thus defined is taxable under section 951 or is taken into account in determining whether there exists the United States ownership of a foreign corporation required to constitute it a controlled foreign corporation. The bill as passed by the House, in determining whether a corporation is a controlled foreign corporation, took into account any U.S. person who under the provisions corresponding to section 958(b) owned stock in the foreign corporation even though such person owned (under section 958(b)) less than 10 percent of the total combined voting power of all classes of stock entitled to vote in the corporation. Also, once a foreign corporation was classed as a controlled foreign corporation, the bill as

passed by the House taxed a United States person who owned 10 percent of the value of the stock in the corporation, notwithstanding that his stock entailed no voting power.

Example.—H owns (under section 958(a)) 5 percent of the one class of stock of X, a controlled foreign corporation, and his wife, W, owns (under section 958(a)) 10 percent of the stock of such corporation. Under the rules of section 958(b), H is considered to own 15 percent of the stock of X and will be required to include in gross income amounts attributable to his 5 percent interest as determined under section 958(a). W will be required to include in gross income amounts attributable to her 10 percent of the stock of such corporation.

(c) *Coordination with election of a foreign investment company to distribute income.*—Subsection (c) provides that a United States person who, for his taxable year, is a qualified shareholder, within the meaning of section 1247(c), of a foreign investment company with respect to which an election under section 1247 is in effect is not required to include in gross income under subsection (a) for such year any income of such company. The corresponding provision of the bill as passed by the House applied only to subpart F income.

(d) *Coordination with foreign personal holding company provisions.*—Subsection (d) provides that a United States shareholder who, for a taxable year, is subject to tax under section 551(b) (relating to foreign personal holding company income included in gross income of United States shareholders) on income of a controlled foreign corporation is not required to include in gross income, for such taxable year, any amount under subsection (a) with respect to such company. The corresponding provision of the bill as passed by the House (sec. 13(b)(1)) amended section 551(b) to provide that the amount of undistributed foreign personal holding company income otherwise required under section 551(b) to be included in gross income of a United States person is reduced by his proportionate share of undistributed foreign personal holding company income included in gross income under section 951(a) for the taxable year as his proportionate share of subpart F income of such controlled foreign corporation.

SECTION 952. SUBPART F INCOME DEFINED

Section 952 defines the two types of income of a controlled foreign corporation which constitute "subpart F income" and may be includible in the gross income of United States shareholders under section 951(a)(1)(A).

(a) *In general.*—Paragraph (1) of section 952(a) provides that the subpart F income of a controlled foreign corporation, for purposes of section 951(a)(1)(A), is the sum of (1) the income of the controlled foreign corporation derived from insurance of United States risks as determined under section 953; and (2) the foreign base company income of a controlled foreign corporation, as determined under section 954. The provision in the bill as passed by the House which included in subpart F income the income of the controlled foreign corporation from United States patents, copyrights, and exclusive formulas and processes has been deleted from subpart F; but see section 16 of the bill as reported by your committee for provisions relating to the transfer of such rights to a controlled foreign corporation.

(b) *Exclusion of United States income.*—Subsection (b) excludes, from subpart F income, amounts includible in gross income under chapter 1 of the code (other than the new subpart F) where the controlled foreign corporation is engaged in trade or business in the United States and such income is treated as income from sources within the United States. This subsection will not permit an exclusion from subpart F income in the case of United States source income of a controlled foreign corporation having no permanent establishment in the United States in situations (involving tax treaties) in which such permanent establishment is a requisite to imposition of United States tax, since in such a situation no amount will have been included in gross income for purposes of this section.

(c) *Limitation.*—Section 952(c), corresponding to section 952 (a)(3) of the bill as passed by the House, provides that the subpart F income of a controlled foreign corporation for any taxable year of such corporation may not exceed the earnings and profits of the controlled foreign corporation for that year but with a reduction not provided for by the bill as passed by the House. The reduction is the amount (if any) by which—

(1) the sum of the deficits in earnings and profits for prior taxable years beginning after December 31, 1959 (reduced by any earnings and profits for taxable years beginning after December 31, 1959, and before January 1, 1963), exceeds

(2) an amount equal to the earnings and profits described in section 959(c)(3) accumulated for taxable years beginning after December 31, 1962, determined as of the close of the preceding taxable year.

For such purpose a deficit for a prior taxable year is taken into account only to the extent it has not been taken into account for any preceding taxable year.

Example (1).—M, a controlled foreign corporation, has subpart F income for taxable year 1963, before applying subsection (c), of \$100. Deductions not allocable to such income exceed gross income (other than gross income giving rise to subpart F income) by \$25 with the result that earnings and profits for the year are \$100 minus \$25, or \$75. M's subpart F income for 1963 as limited by subsection (c) is \$75.

Example (2).—In 1963 a controlled foreign corporation has earnings and profits of \$90,000, consisting of \$40,000 of subpart F income and \$50,000 of other income. For taxable year 1964, the corporation has a deficit in earnings and profits of \$400,000. In 1965 it has earnings and profits of \$380,000, consisting of subpart F income of \$300,000 and other income of \$80,000. It makes no distributions during 1963, 1964, or 1965. Under subsection (c), the limitation for 1965 is \$30,000 computed as follows:

Earnings and profits for 1965	-----	\$380, 000
Reduced by deficit for 1964	-----	\$400, 000
Less:		
Earnings and profits described in sec. 959(c)(3) accumulated as of close of 1964 (without reduction by the 1964 deficit)	-----	50, 000
		<u>350, 000</u>
Limitation under subsection (c)	-----	30, 000

(d) *Special rule in case of indirect ownership.*—Subsection (d) provides a special rule that, for purposes of the limitation in subsection (c), the earnings and profits of a controlled foreign corporation for a taxable year are reduced not only by the deficits of such controlled foreign corporation as provided in subsection (c), but also by the deficits of certain other foreign corporations. The special rule is that if a United States shareholder owns (within the meaning of section 958(a)) stock of a foreign corporation and by reason of such ownership owns (within the meaning of such section) stock of any other foreign corporation, and any of such foreign corporations has a deficit in earnings and profits for the taxable year, then earnings and profits of each such foreign corporation which is a controlled foreign corporation is, with respect to such shareholder, reduced to take account of such deficit in such manner as the Secretary of the Treasury or his delegate may prescribe by regulations.

SECTION 953. INCOME FROM INSURANCE OF UNITED STATES RISKS

Section 953, corresponding to section 952(b) of the bill as passed by the House, defines the term “income derived from insurance of United States risks” referred to in section 952(a)(1) as one item included in subpart F income.

(a) *General rule.*—Subsection (a) provides that income derived from the insurance of United States risks is that income which would (subject to certain modifications) be taxed under subchapter L of chapter 1 if the controlled foreign corporation were a domestic insurance corporation. Such income is included in subpart F income, however, only if attributable to the reinsurance or the issuing of any insurance or annuity contract (A) in connection with property in or liability arising out of activity in, or in connection with the lives or health of, residents of the United States, or (B) in connection with risks which are not included in subparagraph (A) because of an arrangement whereby another corporation receives a substantially equal amount of premiums or other consideration in respect of reinsurance or the issuing of any insurance or annuity contract in connection with property in or liability arising out of activity in, or in connection with the lives or health of, residents of the United States. The definition is the same as that in the bill as passed by the House except for changes which are clerical and which make clear that the contract must be in connection with property in or liability arising out of activity in the United States or in connection with the life or health of residents of the United States. Your committee has added a new sentence at the end of subsection (a) which provides that section 953 applies only in the case of a controlled foreign corporation which receives, during any taxable year, premiums or other consideration in respect of contracts described above in excess of 5 percent of the total premiums and other consideration received during the taxable year in respect of all reinsurance and issuing of insurance and annuity contracts.

(b) *Special rules.*—Subsection (b), which is the same, except for conforming changes, as section 952(b)(2) of the bill as passed by the House, provides special rules which modify the application of subchapter L for purposes of subsection (a).

Under paragraph (1), respecting the application of part I of subchapter L, life insurance company taxable income is defined solely as

the gain from operations under section 809(b) despite the provisions of section 802(b).

Under paragraph (2), the taxable income of all insurance companies other than life insurance companies, that is, both mutual and stock insurance companies which are ordinarily subject to the provisions of part II or part III of subchapter L, respectively, is to be determined under part III of subchapter L.

Paragraph (3) disallows certain deductions from income for purposes of this subsection. These deductions are:

- (A) Section 809(d)(4) (operations loss deduction),
- (B) Section 809(d)(5) (certain nonparticipating contracts),
- (C) Section 809(d)(6) (group life, accident, and health insurance),
- (D) Section 809(d)(10) (small business deduction),
- (E) Section 817(b) (gain on property held on December 31, 1958, and certain substituted property acquired after 1958), and
- (F) Section 832(b)(5) (certain capital losses).

Under paragraph (4) "gross amount" (in section 809(c)(1)), net decrease in reserves (in section 809(c)(2)), "increases in certain reserves" (defined in section 809(d)(2)), and premiums earned (defined in section 832(b)(4)) are taken into account only to the extent in respect of any reinsurance or the issuing of any insurance or annuity contract described in subsection (a)(1) of section 953.

Under paragraph (5), all other items of income, that is items other than those taken into account under paragraph (4), as well as all items of expenses, losses, and deductions shall be properly allocated under regulations prescribed by the Secretary of the Treasury or his delegate.

SECTION 954. FOREIGN BASE COMPANY INCOME

(a) *Foreign base company income.*—Subsection (a), corresponding to section 952(e) of the bill as passed by the House, defines foreign base company income as the sum of three items, each reduced by deductions properly allocable to such items: (1) foreign personal holding company income, (2) foreign base company sales income, and (3) foreign base company services income. The bill as passed by the House contained no provision corresponding to item (3).

(b) *Exclusions and special rules.*—Paragraph (1) provides an exclusion from foreign base company income for (A) dividends and interest received during the taxable year from investments which at the time of receipt are qualified investments in less developed countries, or (B) gains from the sale or exchange during the taxable year of investments which at the time of sale or exchange are qualified investments in less developed countries to the extent that gains from such sales or exchanges exceed the losses from such sales or exchanges. The preceding exclusion is limited to the increase for the taxable year in qualified investments in less developed countries. The bill as passed by the House contained a provision for the reduction of foreign base company income by the amount of any increase in qualified investments in less developed countries, with different terms of qualification discussed under section 955(b).

Example.—O, a controlled foreign corporation, has for taxable year 1965 subpart F income of \$100 which includes \$50 of foreign

base company income of which \$40 consists of dividends from qualified investments in less developed countries. O's increase for the taxable year in qualified investments in less developed countries is \$30. O may exclude from foreign base company income \$30 under section 954(b)(1) and will, accordingly, include in gross income foreign base company income of only \$20.

Paragraph (2) of section 954(b) provides that foreign base company income does not include income derived from, or in connection with, the use (or hiring or leasing for use) of any aircraft or vessel in foreign commerce, or the performance of services directly related to the use of any such aircraft or vessel.

Paragraph (3), corresponding to paragraph (6) of section 952(e) of the bill as passed by the House, provides that, if the foreign base company income for the taxable year is less than 30 percent of gross income, no part of the income is to be treated as foreign base company income, but if foreign base company income for the taxable year exceeds 70 percent of gross income, the entire gross income is, subject to the provisions of paragraphs (1), (2), (4), and (5) of section 954(b), to be treated as foreign base company income. The corresponding percentages in the bill as passed by the House were 20 percent and 80 percent, respectively. The reduction of subpart F income provided by subpart G (Export Trade Corporations) does not affect the determinations of the 30 and 70 percent lines.

Paragraph (4) provides that foreign base company income does not include any item of income with respect to which it is established to the satisfaction of the Secretary of the Treasury or his delegate that the creation or organization of the controlled foreign corporation receiving such item under the laws of the country in which it is incorporated does not have the effect of substantial reduction of income, war profits, or excess profits taxes or similar taxes.

The determination of whether the creation or organization of a controlled foreign corporation has the effect of substantially reducing income, war profits, excess profits taxes or similar taxes depends upon all the facts and circumstances including the effective rate of tax and the extent to which it has been reduced.

Paragraph (5), corresponding to section 952(e)(7) of the bill as passed by the House, provides that the foreign personal holding company income, the foreign base company sales income, and the foreign base company services income are reduced, under regulations prescribed by the Secretary of the Treasury or his delegate, so as to take into account deductions (including taxes) properly allocable to such income.

(c) *Foreign personal holding company income.*—Subsection (c) is similar to section 952(e) of the bill as passed by the House, and defines foreign personal holding company income, for purposes of section 954(a)(1), as foreign personal holding company income (as defined in section 553) with the modifications and adjustments provided in paragraphs (2), (3), and (4) of section 954(c).

Paragraph (2) provides that all rents are included in foreign personal holding company income without regard to whether or not such rents constitute 50 percent or more of gross income. Section 553 already achieves such a result as to royalties.

Paragraph (3) excludes from personal holding company income (A) rents and royalties derived in the active conduct of a trade or business, (B) or dividends, interest and gains from the sale or exchange of stock

or securities derived in the conduct of a banking, financing, or similar business, or derived from the investments by an insurance company of its unearned premiums or reserves ordinary and necessary for the proper conduct of its insurance business. The exclusion applies, however, only to amounts received from a person other than a related person.

Paragraph (4) excludes certain income received from related persons:

(A) dividends and interest from a related person which (i) is organized under the laws of the same foreign country under the laws of which the controlled foreign corporation is created or organized and (ii) has a substantial part of its assets used in its trade or business located in such same foreign country;

(B) interest received in the conduct of a banking, financing, or similar business from a related person engaged in the same type of business provided the business of the payor and the recipient are predominantly with persons other than related persons; and

(C) rents, royalties, and similar amounts received from a related person for the use of, or privilege of using, property within the country under the laws of which the controlled foreign corporation is created or organized.

(d) *Foreign base company sales income*.—Paragraph (1) of subsection (d) corresponds to section 952(e)(2) of the bill as passed by the House and defines foreign base company sales income as income (whether in the form of profits, commissions, fees, or otherwise) derived in connection with:

(1) the purchase of personal property from a related person and its sale to any person,

(2) the sale of personal property to any person on behalf of a related person,

(3) the purchase of personal property from any person and its sale to a related person, or

(4) the purchase of personal property from any person on behalf of a related person,

where (A) the property which is purchased (or in the case of property sold on behalf of a related person, the property which is sold) is manufactured, produced, grown, or extracted outside the country under the laws of which the controlled foreign corporation is created or organized, and (B) the property is sold for use, consumption, or disposition outside such foreign country, or, in the case of property purchased on behalf of a related person, is purchased for use, consumption, or disposition outside such foreign country.

The definition does not apply to income of a controlled foreign corporation from the sale of a product which it manufactures. In a case in which a controlled foreign corporation purchases parts or materials which it then transforms or incorporates into a final product, income from the sale of the final product would not be foreign base company sales income if the corporation substantially transforms the parts or materials, so that, in effect, the final product is not the property purchased. Manufacturing and construction activities (and production, processing, or assembling activities which are substantial in nature) would generally involve substantial transformation of purchased parts or materials.

Where the definition of foreign base company sales income depends on whether property is sold for use, consumption, or disposition out-

side the country under the laws of which the controlled foreign corporation is created or organized, a destination test applies. Generally property will be considered to be used, consumed, or disposed of in the country to which it is delivered unless circumstances indicate that the property is to be exported after it is so delivered.

Paragraph (2) of section 954(d) provides that in situations in which the carrying on of activities by a controlled foreign corporation through a branch or similar establishment outside the country of incorporation of the controlled foreign corporation has substantially the same effect as if such branch or similar establishment were a wholly owned subsidiary corporation deriving such income, then, under regulations prescribed by the Secretary of the Treasury or his delegate, the income attributable to the carrying on of such activities of such branch or similar establishment shall be treated as income derived by a wholly owned subsidiary of the controlled foreign corporation and shall constitute foreign base company sales income of the controlled foreign corporation. Determinations, such as those required under section 954 (b)(3) and (d)(1) (A) and (B), as to such branch income shall be made as though such branch were a separate controlled foreign corporation.

Paragraph (3), corresponding to the last sentence of section 952(e)(2) of the bill as passed by the House, provides that a person is a related person with respect to a controlled foreign corporation, if such a person is—

(A) an individual, trust, or estate which controls such corporation;

(B) a corporation which controls, or is controlled by, the controlled foreign corporation;

(C) a corporation which is controlled by the same person or persons which control the controlled foreign corporation.

For purposes of such paragraph, control means the ownership, directly or indirectly, of stock (determined under section 958) possessing more than 50 percent of the total combined voting power of all classes of stock entitled to vote.

The bill as passed by the House provided in section 952(e)(2) that foreign base company income included foreign base company sales income if, for the taxable year, such income was equal to at least 20 percent of the gross income of the foreign corporation. Your committee's amendment provides no comparable limitation with respect to foreign base company sales income but, as discussed above, it provides in section 954(a)(2) a 30-percent limitation which is applicable to total foreign base company income.

(e) *Foreign base company services income.*—Subsection (e) defines foreign base company services income as that income (whether in the form of compensation, commissions, fees, or otherwise) derived in connection with technical, managerial, engineering, architectural, scientific, skilled, industrial, commercial, or like services which are performed—

(1) for or on behalf of a related person, and

(2) outside the country under the laws of which the controlled foreign corporation is created or organized.

Such rule, however, does not apply to income derived from services which are directly related to the sale or exchange of property manufactured, produced, grown, or extracted by the controlled foreign corporation and which are performed before the sale or exchange, or

derived from services directly related to an offer or effort to sell or exchange such property.

(f) *Increase in qualified investments in less developed countries.*—Subsection (f) provides the rule for determining the increase for a taxable year in qualified investments in less developed countries. This amount constitutes a limitation on the exclusion of dividends, interest, and gains from qualified investments in less developed countries and requires, in effect, that such dividends, interest, and gains be reinvested in qualified investments in less developed countries. The increase for a taxable year is the amount by which a controlled foreign corporation's qualified investment in less developed countries at the close of its taxable year exceeds such investments at the close of the preceding taxable year.

SECTION 955. WITHDRAWAL OF PREVIOUSLY EXCLUDED SUBPART F INCOME FROM QUALIFIED INVESTMENT

(a) *In general.*—Subsection (a) provides rules relating to previously excluded subpart F income withdrawn from investment in less developed countries which is includible in gross income of a United States shareholder under section 951(a)(1)(A)(ii).

Paragraphs (1) and (2) of section 955(a) define the amount of subpart F income withdrawn from investment in less developed countries and set forth the limitations on including such amount in gross income. The amount withdrawn is an amount equal to the decrease in qualified investments in less developed countries for the taxable year provided such decrease does not exceed the sum of the amounts excluded from foreign base company income under section 954(b)(1) for all prior taxable years reduced by the sum of amounts of previously excluded subpart F income withdrawn from investments in less developed countries for all prior taxable years. Further, such decrease must be reduced by the amount (if any) by which losses exceed gains on dispositions of qualified investments in less developed countries and, after application of such losses, such decrease may not exceed the sum of earnings and profits for the current year and all prior taxable years beginning after December 31, 1962.

Example (1).—X, a United States shareholder and sole owner of M, a controlled foreign corporation, determines the amount includible in gross income under section 951(a)(1)(A)(ii) for the taxable year as follows:

(1) Decrease in qualified investments in less developed countries for the taxable year.....	50	
(2) Excess of losses over gains on dispositions of qualified investments in less developed countries during the taxable year.....	10	
(3) Earnings and profits for the current taxable year and all prior taxable years beginning after December 31, 1962.....	45	
(4) Section 955(a)(1) (A) and (B) limitation: Amounts excluded from foreign base company income under section 954(b)(1) for all prior taxable years.....	75	
Less: amounts of previously excluded subpart F income withdrawn from qualified investments in less developed countries for all prior taxable years.....	25	50
(5) Amount includible in gross income under section 951(a)(1)(A)(ii) for the taxable year (item 1 reduced by item 2 to the extent not in excess of the lesser of items 3 or 4).....		40

Example (2).—The facts are the same as in example (1) except that earnings and profits for the current taxable year and all prior taxable years are 35 instead of 45. The amount includible in gross income under section 951(a)(1)(A)(ii) for the taxable year is 35 (item 1 reduced by item 2 and limited by item 3 to the extent not in excess of item 4).

Example (3).—The facts are the same as in example (1) except the section 955(a)(1) (A) and (B) limitation (item 4) is 30 instead of 50. The amount includible in gross income under section 951(a)(1) (A)(ii) for the taxable year is 30 (item 1 reduced by item 2 limited by item 4 and not in excess of item 3).

Paragraph (3) provides that a United States shareholder's pro rata share of the amount of previously excluded subpart F income of a controlled foreign corporation withdrawn from investment in less developed countries for a taxable year is his pro rata share of the amount determined under paragraph (1).

(b) *Qualified investments in less developed countries.*—Subsection (b) defines qualified investments in less developed countries as property which is—

(A) stock of a less developed country corporation but only if the controlled foreign corporation owns 10 percent or more of the total combined voting power of such less developed country corporation;

(B) an obligation of a less developed country corporation which at the time of its acquisition by the controlled foreign corporation has a maturity of 5 years or more, but only if the controlled foreign corporation owns 10 percent or more of the total combined voting power of all classes of stock of such less developed country corporation; or

(C) an obligation of a less developed country.

For purposes of this section, an obligation of a less developed country includes, wherever appropriate, obligations issued or guaranteed by the government of a less developed country or a political subdivision thereof and obligations of an agency, instrumentality or other "alter ego" of a government of a less developed country. Because of the variety of legal forms that may be involved, the provision refers only to the essential condition that a less developed country be financially committed in the obligation.

Paragraph (2) provides that property which would be a qualified investment in less developed countries but for the fact that the foreign country, after the property was acquired, ceased to be a less developed country shall be treated as a qualified investment in less developed countries.

Paragraph (3) provides that a controlled foreign corporation may, under regulations prescribed by the Secretary of the Treasury or his delegate, elect to treat qualified investments in a less developed country as acquired during the taxable year although actually acquired during the following taxable year or on or before such day after the close of the following taxable year as such regulations may prescribe.

Paragraph (4) provides that the amount taken into account with respect to property described in paragraph (1) or (2) shall be its adjusted basis, reduced by any liability to which such property is subject.

(c) *Less developed country corporations.*—Subsection (c) defines a less developed country corporation as a foreign corporation which is created or organized under the laws of a less developed country and which during the taxable year is engaged in the active conduct of one or more trades or businesses and—

(A) at least 80 percent of whose gross income for such year is derived from sources within less developed countries, and

(B) at least 80 percent in the value of whose assets on each day of the taxable year consists of—

(i) property used in such trades or businesses and located in less developed countries,

(ii) money, and deposits with persons carrying on the banking business,

(iii) stock, and obligations which, at the time of their acquisition, have at least a 5-year maturity, of any other less developed country corporation,

(iv) obligations of a less developed country,

(v) an investment required because of restrictions imposed by a less developed country, and

(vi) property described in section 956(b)(2) relating to exceptions from the term United States property.

For purposes of section 955(c)(1)(A), whether income is derived from sources within less developed countries shall be determined under regulations prescribed by the Secretary of the Treasury or his delegate.

The source rules prescribed under such regulations, to be used in determining whether income is derived from sources within one foreign country or another, need not be analagous to the rules used in determining whether or not income is derived from sources within the United States.

Paragraph (2) provides that the term “less developed country corporation” also includes a foreign corporation 80 percent or more of the assets of which on each day of the taxable year consists of assets used, or held for use, for or in connection with production of income described below and property described in section 956(b)(2), relating to exceptions from the term United States property, and 80 percent or more of the gross income of which consists of:

(A) gross income derived from, or in connection with, the using (or hiring or leasing for use) in foreign commerce of aircraft or vessels registered under the laws of a less developed country, or from, or in connection with, the performance of services directly related to use of such aircraft or vessels, or from the sale or exchange of such aircraft or vessels, or

(B) dividends and interest received from foreign corporations which are less developed country corporations within the meaning of this paragraph and 10 percent or more of the total combined voting power of all classes of stock of which are owned by the foreign corporation, and gain from the sale or exchange of stock or obligations of foreign corporations which are such less developed country corporations.

The 80-percent gross income requirement can be satisfied by a combination of the amounts described in subparagraphs (A) and (B).

Paragraph (3), which is identical to section 953(b)(5) of the bill as passed by the House, except for one new rule, defines less developed country. Except for certain countries and areas specified in the paragraph which may not be designated as less developed countries,

the designation of which countries are less developed is left to Executive order. The new rule is that termination of a designation of a country as a less developed country may not be made until 30 days after notice by the President to the Senate and the House of Representatives of his intention to make the termination.

SECTION 956. INVESTMENT OF EARNINGS IN UNITED STATES PROPERTY

Section 956 provides rules for determining the amount includible in gross income under section 951(a)(1)(B) as a United States shareholder's pro rata share of the controlled foreign corporation's increase in earnings invested in United States property. A similar provision of the bill as passed by the House, section 953, applied to investments in nonqualified property which included not only United States property but also property other than that ordinary and necessary for the active conduct of an existing trade or business and other than certain investments in corporations incorporated in less developed countries and actively carrying on a trade or business almost wholly within such countries.

(a) *Determination of the amount of the investment.*—Paragraph (1) of section 956(a) provides that the amount of earnings of a controlled foreign corporation invested in United States property at the end of any taxable year is the aggregate amount of such property held at the close of the taxable year, to the extent such amount would have constituted a dividend if it had been distributed. For such purpose, however, earnings and profits does not include amounts attributable to previously excluded subpart F income withdrawn from less developed countries during the taxable year.

Paragraph (2) of section 956(a) provides that the increase for any taxable year of a United States shareholder's pro rata share of the earnings of a controlled foreign corporation invested in United States property is the amount determined by subtracting, from his pro rata share of the amount determined under paragraph (1) for the close of the taxable year, his pro rata share of the amount determined under paragraph (1) for the close of the preceding taxable year, reduced by amounts distributed during such preceding taxable year to which section 959(c)(1) applies, that is, reduced by distributed amounts which have been excluded from gross income because they are earnings and profits previously taxed as increases in earnings invested in United States property. Such determination is made on the basis of stock owned under section 958(a) on the last day during the taxable year on which the foreign corporation is a controlled foreign corporation.

Example.—X is a United States shareholder and 100-percent owner of controlled foreign corporation M. M's investment in United States property determined under section 956(a)(1) at the close of the taxable year 1964 was \$150 and its accumulated earnings and profits at the beginning of the taxable year 1965 was \$175, \$100 of which were described in section 959(c)(1), \$50 of which were described in section 959(c)(2), and \$25 of which were described in section 959(c)(3). During the taxable year 1965, M had earnings and profits of \$50, \$35 of which were subpart F income and M withdrew \$10 of previously excluded subpart F income from qualified investments in less developed countries. M distributed \$50 to which section 959(c)(1) applies during the preceding taxable year 1964. The total United States prop-

erty held by M at the close of the taxable year 1965 is \$250. X determines the amount includible in his gross income under section 951(a)(1)(B) as follows:

(1) Amount of United States property held at the close of the taxable year 1965.....	\$250
(2) Amount of item (1) which would have constituted a dividend if distributed (item (1) to extent not in excess of earnings and profits at December 31, 1965 of \$225).....	225
(3) Determination of pro rata increase in investment in United States property for the taxable year 1965:	
Amount determined under section 956(a)(1) at close of taxable year 1965.....	\$225
Amount determined under section 956(a)(1) at close of preceding taxable year, reduced by amounts paid to which section 959(c)(1) applies during such preceding taxable year (\$150 minus \$50).....	100
	125
(4) Amount includible in gross income under section 951(a)(1)(B):	
Pro rata increase in investment in United States property.....	125
Less: Previously taxed subpart F income (\$50 in prior years and \$35 in current year) and previously excluded subpart F income withdrawn from qualified investments (\$10).....	95
	30

Paragraph (3) of section 956(a) provides that the amount taken into account under paragraphs (1) or (2) with respect to any property is to be its adjusted basis, reduced by any liability to which the property is subject.

(b) *United States property defined.*—Paragraph (1) of subsection 956(b) provides the general rule that United States property means property acquired after December 31, 1962, which is tangible property located in the United States; stock of a domestic corporation; an obligation of a United States person; any right to the use in the United States of a patent or copyright, an invention, model, or design (whether or not patented), a secret formula or process, or any similar property right, which is acquired or developed by the controlled foreign corporation for use in the United States.

Paragraph (2) excepts property from United States property if it is referred to in subparagraphs (A) through (F). Subparagraph (A) refers to obligations of the United States, money, or deposits with persons carrying on the banking business. Subparagraph (B) refers to property located in the United States purchased in the United States for export to, or for use in, foreign countries. Subparagraph (C) refers to any obligation of a United States person arising in connection with the sale or processing of property, if the amount of such obligation outstanding at no time during the taxable year exceeds the amount which would be ordinary and necessary to carry on the trade or business of both the other party to such sale or processing transaction and the United States person had such transaction been made between unrelated persons.

Subparagraph (D) refers to aircraft, railroad rolling stock, vessels, motor vehicles, or containers, used in the transportation of persons or property in foreign commerce and used predominantly outside the United States. Subparagraph (E) refers to insurance company assets equivalent to the unearned premiums or reserves ordinary and necessary for the proper conduct of its insurance business with respect to

contracts not described in section 953(a)(1). Subparagraph (F) refers to an amount of assets of the controlled foreign corporation equal to the earnings and profits accumulated after December 31, 1962, and excluded from gross income under section 952(b), relating to the exclusion of certain United States income.

(c) *Pledges and guarantees.*—Subsection (c) provides that a controlled foreign corporation, under regulations by the Secretary of the Treasury or his delegate, is considered to hold an obligation of a United States person if it is a pledgor or guarantor of such obligation.

SECTION 957. CONTROLLED FOREIGN CORPORATIONS;
UNITED STATES PERSONS

(a) *Controlled foreign corporations defined.*—Subsection (a), corresponding to section 954(a) of the bill as passed by the House, defines controlled foreign corporation for purposes of the new subpart F, as a foreign corporation of which more than 50 percent of the total combined voting power of all classes of stock entitled to vote is owned by United States shareholders (defined in section 951(b) to include only United States persons owning or considered as owning 10 percent or more of such stock) on any day during the taxable year of the corporation. In this connection, constructive rules of ownership provided in section 958 apply. The bill as passed by the House, to determine whether ownership of more than 50 percent exists in the United States, took account of any stock interest (even if less than 10 percent) owned by a United States person.

(b) *Special rule for insurance.*—Subsection (b), corresponding to section 954(b) of the bill as passed by the House, provides a special definition of controlled foreign corporations solely for the purpose of including the income derived from insurance of United States risks, referred to in section 953(a), in the gross income of a United States shareholder. Under the special definition “controlled foreign corporation” includes not only a foreign corporation satisfying subsection (a) but also one of which more than 25 percent of the total combined voting power of all classes of stock is owned under section 958 by United States shareholders, on any day during the taxable year of a corporation, if the gross amount of premiums or other consideration in respect of any reinsurance or issuing of insurance or annuity contracts described in section 953(a)(1), exceeds 75 percent of the gross amount of all premiums or other consideration in respect of all risks. Only the subpart F income consisting of income from insurance of United States risks is required to be included in the gross income of a United States person owning stock in a corporation satisfying subsection (b) but not subsection (a).

(c) *Corporations organized in United States possessions.*—Subsection (c) excepts from the definition of “controlled foreign corporation” a corporation created or organized in Puerto Rico or a United States possession. In order to qualify for the exception, the corporation must derive at least 80 percent of its gross income for the 3-year period immediately preceding the close of the taxable year (or for such part of such period immediately before the end of such taxable year as may be applicable) from sources within Puerto Rico or a United States possession. In addition, 50 percent of its gross income for such period (or part thereof) must be derived from the active conduct within Puerto Rico or a United States possession of certain specified trades or

businesses. The statutory language for this requirement is adapted from Puerto Rican economic incentive law and does not necessarily indicate that the activities described constitute substantial transformation for purposes of the foreign base company sales income rule. The trades or businesses constituting manufacturing or processing referred to in section 957(c)(2) will include, for example, the manufacture in the Commonwealth of Puerto Rico of tabulating cards, paper tablets or pads, facial tissues, and paper napkins from jumbo rolls of paper; the manufacture of such household products as liquid starch by mixing large quantities of the ingredients which are used to produce liquid starch; or the manufacture of fruit nectar juices and drinks from fruit concentrates.

Subsection (c) in effect leaves the corporations covered there subject to the rules of existing law. In order to insure that such corporations will not be availed of for tax haven activities, however, the Secretary of the Treasury or his delegate is given the power under the last sentence of section 957(c) to prescribe regulations as to whether the source of income is in the Commonwealth of Puerto Rico or a United States possession, or whether income is derived from the active conduct of a described trade or business in such Commonwealth or United States possession. However, such regulations will not change existing law governing the source of income which is derived from the "manufacture or processing" of goods, wares, merchandise or other tangible personal property in the Commonwealth of Puerto Rico.

(d) *U.S. person defined.*—Subsection (d), for which there was no corresponding provision in the House bill, provides that, for purposes of subpart F, the term "United States person" has the meaning assigned to it in section 7701(a)(30) except that—

(1) with respect to a corporation organized under the laws of Puerto Rico, such term does not include an individual who is a resident of Puerto Rico, if a dividend received by him during the taxable year from such corporation would, for purposes of section 933(1), be treated as income derived from sources within Puerto Rico,

(2) with respect to a corporation organized under the laws of the Virgin Islands, such term does not include an individual who is a resident of the Virgin Islands and whose income tax obligation under subtitle A for the taxable year is satisfied pursuant to section 28(a) of the Revised Organic Act of the Virgin Islands, approved July 22, 1954 (48 U.S.C. 1642), by paying tax on income derived from all sources into the treasury of the Virgin Islands, and

(3) with respect to a corporation organized under the laws of any other possession of the United States, such term does not include an individual who is a resident of any such other possession and whose income derived from sources within possessions of the United States is not, by reason of section 931(a), includible in gross income under subtitle A for the taxable year.

The effect of paragraphs (1), (2), and (3), above, is to exclude individuals who qualify thereunder in determining whether a foreign corporation incorporated in Puerto Rico, the Virgin Islands, or another possession of the United States, as the case may be, is a controlled foreign corporation by reason of the ownership of more than 50 percent of its stock by United States shareholders (i.e., shareholders who are

United States persons) each of whom owns 10 percent or more of the stock of such foreign corporation. This determination of whether a foreign corporation is a controlled foreign corporation is made not only for purposes of subpart F, but also for purposes of section 1248 of the code, as added by section 15 of the bill, as reported by your committee. The application of sections 931(a) and 933(1) of the code and of section 28 of the Revised Organic Act of the Virgin Islands is not affected by the bill.

SECTION 958. RULES FOR DETERMINING STOCK OWNERSHIP

Section 958 is the same as section 955 of the bill as passed by the House except for conforming and clarifying changes and the addition of certain modifications to the constructive ownership rules of section 318(a) of the Code for purposes of this section.

Section 958 provides, in subsection (a), a limited rule of stock ownership for determining the amount taxable to a United States shareholder, and, in subsection (b), a broader set of constructive rules of ownership for determining whether the requisite ownership by United States shareholders exists so as to make a corporation a controlled foreign corporation or a United States shareholder has the requisite ownership to be liable for tax under section 951(a).

(a) *In general.*—For purposes of subpart F (other than sections 955(a)(1) (A) and (B), 955(c)(2)(A)(ii), and 960(a)(1)), a United States shareholder owns the stock which he owns directly in a foreign corporation and also that which he owns through certain foreign entities as follows: stock owned, directly or indirectly, by or for a foreign corporation, foreign partnership, or a foreign trust or foreign estate (within the meaning of section 7701(a)(31)) is considered as proportionately owned by the shareholders, partners, or beneficiaries. Stock owned by such a foreign entity with the application of such rule is considered as actually owned by such foreign entity for again applying the rule. The rule in effect gives rise to a chain of ownership and, since the rule operates only on stock owned by a foreign entity, attribution under the rule stops with the first United States shareholder in the chain of ownership running from the controlled foreign corporation to such person. For example, W, a domestic corporation, owns 80 percent of the one class of stock of X, a foreign corporation, which in turn owns 80 percent of the one class of stock of Y, another foreign corporation, which in turn owns 90 percent of the one class of stock in Z. Under the rule, X is considered as owning 80 percent of the 90 percent which Y owns in Z, or 72 percent. 80 percent of such 72 percent, or 57.6 percent of the stock in Z, is considered as owned by W. Since W is a domestic corporation which is a United States shareholder, W is the person taxed even though W is wholly owned by U, another domestic corporation. If Z has \$100 of subpart F income, then W is required to include \$57.60 in gross income under section 951(a).

Paragraph (3) of subsection (a) provides, for the sole purpose of taxing United States shareholders on a foreign mutual insurance company's income derived from insurance of United States risks, that that term "stock" includes any certificate entitling the holder to voting power in the corporation.

(b) *Other provisions.*—Subsection (b) provides constructive rules of ownership based, with certain specified exceptions, on section 318. The principle to be followed in applying such rules is that they are to

be applied so that the effect is to subject a United States shareholder to the requirement of section 951(a), to treat a person as a related person under section 954(d)(3) with respect to a controlled foreign corporation, or to make a corporation a controlled foreign corporation under section 957.

The specified exceptions to the rules of section 318 are as follows:

(1) No attribution of ownership from a nonresident alien individual (other than a foreign estate or trust) to a citizen or resident of the United States can occur under section 318 (a)(1)(A);

(2) In considering stock owned by a partnership, estate, trust, or corporation, as owned by the partners, beneficiaries, or shareholders, a partnership, estate, trust, or corporation which owns more than 50 percent of the total combined voting power of all classes of stock entitled to vote, is to be considered as owning all the voting power of all such classes of stock;

(3) Stock of a partner, beneficiary, or shareholder which is attributed to the partnership, estate, trust, or corporation will not be attributed to another partner, beneficiary, or shareholder;

(4) In applying the rule which requires ownership of 50 percent of the stock of a corporation before stock owned by such corporation can be attributed to its stockholders, the bill as passed by the House substituted a zero limitation for the 50-percent limitation; your committee's amendment provides that a 10-percent limitation will be substituted for the 50-percent limitation in the application of clause (i) of section 318(a)(2)(C);

(5) Your committee has also added a provision that the rule that stock owned by or for a partner or a beneficiary or a shareholder of an estate or trust or corporation shall be considered as owned by the partnership, estate, or trust or corporation will not be applied so as to consider a United States person as owning stock which is owned by a person who is not a United States person, nor will a corporation be considered as owning stock owned by or for a 50 percent or more shareholder where the effect is to consider a United States person as owning stock which is owned by a person who is not a United States person.

Example (1).—M, N, and O, all United States persons, each own 20 percent of the stock in X, a foreign corporation having only one class of stock, which in turn owns 60 percent of the stock in Y, also a foreign corporation having only one class of stock. For the purpose of attributing the stock owned by X in Y to M, N, and O, X is considered as owning all of the stock of Y with the result that M, N, and O are considered as each owning 20 percent of the stock of Y.

Example (2).—A, an owner of 50 percent of the one class of stock in Y, owns 8 percent of the one class of stock in Z, a controlled foreign corporation; B (not related to A), the owner of the other 50 percent of the stock in Y, owns 45 percent of the one class of stock of Z. A is considered as owning no part of the stock in Z which is owned by B. Thus, A does not own 10 percent or more of the stock of Z so as to be required under section 951(a) to include in gross income any amount of income of Z.

Example (3).—M, N, and O, all United States persons, each own 30 percent of the stock in X, a foreign corporation having only one class of stock, which in turn owns 40 percent of the stock in Y, also a

foreign corporation having only one class of stock. Under the provisions of section 958(b)(4), M, N, and O are each considered as owning 12 percent of the stock of Y.

SECTION 959. EXCLUSION FROM GROSS INCOME OF PREVIOUSLY TAXED EARNINGS AND PROFITS

Section 959, except for conforming changes, is the same as section 956 of the bill as passed by the House.

(a) *Exclusion from gross income of United States persons.*—Subsection (a) provides that earnings and profits of a foreign corporation attributable to amounts once included in gross income under section 951(a) are not again included in gross income when actually distributed. The exclusion is applicable whether the income included in gross income under section 951 was required to be included by reason of direct ownership of stock in a controlled foreign corporation or ownership through a chain of ownership described in section 958(a). Further, the exclusion applies with respect to the United States shareholder who owned stock in a foreign corporation at the time it was included in gross income under section 951(a), or with respect to a successor in interest who can at the time of the actual distribution provide such proof as the Secretary of the Treasury or his delegate by regulations require that he holds the interest of the United States shareholder who previously included in gross income the earnings and profits being distributed.

Example.—On December 31, 1963, X, a United States shareholder, owns 20 shares of the 100 shares of the only class of stock in Z, a controlled foreign corporation, and by reason of such ownership includes \$20 in gross income under section 951 (his proportionate share of Z's \$100 of subpart F income which constituted Z's entire earnings and profits for its 1963 taxable year). On January 31, 1964, X transfers 9 shares of his stock in Z to Y. On June 1, 1964, X receives an \$11, and Y a \$9, distribution from Z. Neither the \$11 received by X nor the \$9 received by Y is includible in gross income.

Subsection (a) in conjunction with section 951(a)(1)(B) also prevents including in gross income under section 951(a)(1)(B) any increase in earnings invested in United States property to the extent such increase can be considered as attributable income taxable under section 951(a)(1)(A). Subpart F income thus provides an offset to prevent the inclusion in gross income of amounts otherwise includible as an increase in earnings invested in United States property. For example, Z, a controlled foreign corporation wholly owned by X, a domestic corporation, has \$40 subpart F income, and a \$50 increase in earnings invested in United States property; X includes in gross income only \$10 of the \$50 because \$40 of such \$50 is offset by the \$40 of subpart F income included in X's gross income.

(b) *Exclusion from gross income of certain foreign subsidiaries.*—Subsection (b) provides that, for purposes of section 951(a), income of a controlled foreign corporation once included in gross income of a United States shareholder is not, when distributed to another controlled foreign corporation, included in any of such other foreign corporation's income which must be taxed to such United States shareholder or his successor in interest. For example, X, a domestic corporation, wholly owns Y, a controlled foreign corporation which in turn wholly owns Z, another controlled foreign corporation. In 1970,

Y has no income except that which is received from Z, which has \$100 of income which X is required to include in gross income under section 951. Such \$100, although paid to Y as a dividend in 1970, is not included in the income of Y which must be included in the gross income of X, even though such a dividend would ordinarily constitute subpart F income. The same result follows whether the dividend is paid in 1970 or a later year so long as under the rules of subsection (c) it is allocated to earnings and profits under paragraphs (1) and (2) which were once included in X's gross income under section 951.

(c) *Allocation of distributions.*—Subsection (c) provides rules for the allocation of distributions to earnings and profits. Amounts included in gross income of a shareholder under section 951(a) do not constitute distributions for purposes of reducing the earnings and profits of the controlled foreign corporation. Accordingly, when the controlled foreign corporation makes an actual distribution, thereby reducing its earnings and profits, it is necessary at the shareholder level to identify whether the distribution is from earnings and profits attributable to amounts already included in gross income of the shareholder under section 951(a) (in which case the distribution is not taxable as a dividend) or is from earnings and profits which are attributable to amounts not so taxed (in which case the distribution is taxable as a dividend). Under subsection (c), earnings and profits attributable to amounts once taxed (described in paragraphs (1) and (2)) are to be considered to be distributed until they are exhausted (first from the current year and next from past years). Subsequent distributions, after the earnings and profits described in paragraphs (1) and (2) have been received by a shareholder, are taxable as dividends to the extent of the remaining earnings and profits.

A shareholder is not taxable on a distribution which is out of earnings and profits described in paragraph (1) (relating to earnings invested in United States property) or paragraph (2) (relating to subpart F income). The separate classification of earnings and profits under paragraphs (1) and (2) is for purposes of computing a United States shareholder's pro rata share of the increase in earnings in United States property under section 956. For purposes of section 956(a)(2)(A), the amount of earnings invested in United States property for a taxable year is reduced by earnings so invested which were actually distributed. For this purpose, paragraph (1) of section 959(c) provides that earnings and profits attributable to investment in United States property are the first earnings and profits considered as distributed to a shareholder.

In this connection, although amounts taxed once under section 951(a)(1)(A) may offset amounts representing an increase in earnings in United States property under section 951(a)(1)(B) (so as to avoid taxing the same earnings twice) such offset does not affect the amount of earnings and profits attributable to amounts representing the increase in earnings in United States property for purposes of paragraph (1). The amount of earnings and profits under paragraph (1) includes earnings and profits attributable to amounts includible in gross income under section 951(a)(1)(B) as well as earnings and profits attributable to amounts which would have been included under such section except for the availability of the offset by reason of the inclusion of amounts under section 951(a)(1)(A). Earnings and profits attributable to amounts included in income under section 951(a)(1)(A), but used to offset an increase in earnings invested in United States property are

not, however, included in paragraph (2) since they are already included in paragraph (1). Thus, there is no duplication in the amounts attributable to paragraphs (1) and (2), and, from the standpoint of the shareholder, the amount of earnings and profits allocable to him under paragraphs (1) and (2) is always equal to the amount of income he has been taxable on under section 951(a) (and for which he has not received an actual distribution).

Example.—M, a controlled foreign corporation, is organized on January 1, 1963, and is solely owned by X, a United States shareholder. Both M and X use the calendar year as a taxable year. M's earnings and profits for 1963 are \$200, \$100 of which is subpart F income. (M's income included \$25 excluded under section 954(b)(1) as dividends, interest, and gains invested in qualified investments in less developed countries.) M's total United States property at the end of 1963 is \$50 and M makes a distribution during 1963 of \$20. The division of M's earnings and profits account at December 31, 1963, for the purpose of determining the tax on X, is as follows:

Sec. 959(c)(1) amounts (\$50 increase in U.S. property less \$20 distribution).....	\$30
Sec. 959(c)(2) amounts (\$100 subpart F income less \$50 used as offset to increase in investment in U.S. property and reclassified as a sec. 959(c)(1) amount).....	50
Sec. 959(c)(3) amounts (the remaining earnings and profits after reduction for sec. 959(c)(1) and (2) amounts—\$200 minus \$20 (actual distribution) minus \$30 (U.S. property) minus \$50 (subpart F income)).....	100
Total earnings and profits at Dec. 31, 1963.....	180

X is required to include \$100 in gross income under section 951(a)(1)(A)(i) and he would have been required to include \$50 in gross income under section 951(a)(1)(B) but for section 959(a)(2) which allows the offset of previously taxed subpart F income (whether in the current year or in prior years) against increases in investments in United States property. X may exclude the \$20 distribution from gross income under section 959(a)(1) since under section 959(c) such distribution is considered to be out of amounts described in section 959(c)(1).

In 1964, M's earnings and profits are \$300, \$75 of which is subpart F income. M has no change in investments in United States property and withdraws \$15 of previously excluded subpart F income from qualified investments in less developed countries. M makes a distribution of \$250 during 1964.

M's earnings and profits account, at December 31, 1964, for purposes of section 959(c) is as follows:

Sec. 959(c)(1) amounts (\$30 accumulation from prior years less distributions but not in excess of total current and accumulated sec. 959(c)(1) amounts or \$30).....	0
Sec. 959(c)(2) amounts (\$50 accumulation from prior years plus current subpart F income of \$75 and withdrawals of previously excluded subpart F income from qualified investments of \$15 less distributions but not in excess of total current and accumulated sec. 959(c)(2) amounts or \$140).....	0
Sec. 959(c)(3) amounts (\$100 accumulation from prior years, plus current earnings and profits not classified under sec. 959(c)(1) or (2) of \$225, less withdrawals of previously excluded subpart F income from qualified investments of \$15, less distributions not out of sec. 959(c)(1) and (2) amounts of \$80).....	\$230
Total earnings and profits at Dec. 31, 1964.....	230

X is required to include \$75 in gross income under section 951(a)(1)(A)(i) and \$15 under section 951(a)(1)(A)(ii). X may exclude \$170 of the \$250 distribution from gross income under the provisions of section 959(a)(1); \$80 is includible in gross income as a dividend.

(d) *Distributions excluded from gross income not to be treated as dividends.*—Except for deeming foreign taxes paid by foreign corporations as being paid by a domestic corporation in special cases discussed below, a distribution excluded from gross income under section 959 is treated as a distribution which is not a dividend.

SECTION 960. SPECIAL RULES FOR FOREIGN TAX CREDIT

A domestic corporation owning stock in a controlled foreign corporation is required to include in its gross income, under the provisions of subpart F, income of such foreign corporation, whether or not the foreign corporation is one or more links removed in a chain of ownership. Therefore, section 902 (relating to credit for corporate stockholder in foreign corporation) which depends on actual distributions would not operate to give the domestic corporation a credit for foreign taxes paid by the controlled foreign corporation. Section 960 provides rules, consistent with section 902, for treating foreign taxes paid by controlled foreign corporations on income which is included in the gross income of domestic corporations under section 951(a) as having been paid by such domestic corporations. Section 960 corresponds to section 957 of the bill as passed by the House.

(a) *Taxes paid by a foreign corporation.*—Subsection (a) applies to a domestic corporation which includes in gross income under section 951(a) an amount attributable to earnings and profits of a foreign corporation at least 10 percent of the voting stock of which is directly owned by such domestic corporation, or of a foreign corporation at least 50 percent of the voting stock of which is owned by a foreign corporation at least 10 percent of the voting stock of which in turn is directly owned by the domestic corporation. If the directly owned corporation is a less developed country corporation as defined in section 902(d), then the domestic corporation is deemed to have paid the same proportion of the income, war profits, and excess profits taxes paid (or deemed paid) by the controlled foreign corporation to a foreign country or possession of the United States for the taxable year which the amount of the earnings and profits of the foreign corporation so included in gross income of the domestic corporation bears to the sum of the entire earnings and profits of such foreign corporation for such taxable year and the total amount of such income, war profits, and excess profits taxes paid by such foreign corporation.

Example 1.—X, a domestic corporation, wholly owns Y, a foreign corporation, which is a less developed country corporation, which in turn wholly owns Z, another foreign corporation. X, Y, and Z each

use the calendar year as a taxable year. For 1963, X is deemed to have paid taxes actually paid by Y and Z as follows:

	X	Y	Z
Earnings and profits plus foreign taxes.....		100	100
Earnings and profits.....		60	80
Foreign taxes.....		40	20
Subpart F income.....		30	50
Gross income under sec. 951 (30+50).....	80.00		
Foreign taxes deemed paid by X under sec. 960 (a):			
$\left(\frac{30}{100} \times 40\right)$	12.00		
$\left(\frac{50}{100} \times 20\right)$	10.00		

If the directly owned corporation is not a less developed country corporation, then the domestic corporation is deemed to have paid the same proportion of the total income, war profits, and excess profits taxes paid by the controlled foreign corporation to a foreign country or possession of the United States for its taxable year which the amount of the earnings and profits of the foreign corporation included in gross income of the domestic corporation bears to the entire earnings and profits of such foreign corporation for such taxable year. The taxes so deemed paid by the domestic corporation under section 960(a)(1)(C) if the directly owned corporation is not a less developed country corporation are included in the gross income of the domestic corporation under section 78 of the code (as added by sec. 9 of the bill).

Example (2).—X, a domestic corporation, wholly owns Y, a foreign corporation not a less developed country corporation, which in turn wholly owns Z, another foreign corporation. X, Y, and Z each use the calendar year as a taxable year. For 1963, X is deemed to have paid taxes actually paid by Y and Z as follows:

	X	Y	Z
Earnings and profits.....			
Foreign taxes.....		60	80
Subpart F income.....		40	20
Gross income under sec. 951 (30+50).....		30	50
Gross income under sec. 951 (30+50).....	80.00		
Foreign taxes deemed paid by X under sec. 960(a)(1)(C) and included in gross income under sec. 78:			
$\left(\frac{30}{60} \times 40\right)$	20.00		
$\left(\frac{50}{80} \times 20\right)$	12.50		

If a domestic corporation receives a distribution any part of which is excluded from gross income under section 959, the foreign taxes which are deemed to have been paid under section 960(a) are not again deemed paid under section 902. Other foreign taxes which are not deemed paid under section 960 because paid, for instance, by a first-tier corporation, through which profits of a second-tier corporation are distributed (after having been taxed for a prior year under section 951 to a United States shareholder which is a corporation), will still be deemed paid under section 902 when an actual distribution is made. A distribution of such profits, although excluded under section 959(a), is treated by the domestic corporation as a dividend

solely for taking into account under section 902 such foreign taxes as were not deemed paid under section 960.

Example (3).—Suppose that the \$50 of subpart F income of Z taxed to X in 1963 in examples (1) and (2) above was in 1970 distributed to Y who received no other income for such year, and that Y paid a tax of \$20 for 1970 and distributed the remaining \$30 to X before the end of 1970. In such case, although such \$30 is excluded from gross income under section 959(a), it is treated as a dividend under section 902 so that for 1970, X is deemed to have paid \$12 in foreign taxes under example (1), or \$20, under example (2).

If income of a first-tier foreign corporation required to be included in the gross income of a domestic corporation under section 951(a) includes a dividend from a second-tier foreign corporation to the first-tier corporation, then section 902(b) applies to foreign taxes paid by the second-tier corporation and not already allowed as a credit in order to deem them paid by the first-tier foreign corporation so that under section 960(a) they will be deemed paid by the domestic corporation.

Example (4).—M, a domestic corporation, wholly owns N, a controlled foreign corporation, which is a less developed country corporation, which in turn wholly owns O, also a controlled foreign corporation but which has no income required to be included in any United States shareholder's gross income. For taxable year 1970, O pays \$40 in foreign taxes. O pays to N as a dividend its total earnings and profits of \$60 for such taxable year, which dividend is N's only income and which in N's hands is foreign base company income required to be included in M's gross income under section 951(a). N has no deductions and pays no foreign taxes. Applying section 902(b) N is deemed to have paid \$24 in foreign taxes and M is in turn deemed to have paid \$24 under section 960. If N were not a less developed country corporation, N and in turn M, would be deemed to have paid \$40.

(b) *Special rules for foreign tax credit on receipt of previously taxed earnings and profits.*—Where a taxpayer receives a distribution which is excluded from income under section 959 because it was once taxed as income included in gross income of a United States shareholder under section 951(a), the section 904 limitation is increased in the year of actual distribution so that a credit will be allowed for foreign taxes imposed on the income distributed after it was included in gross income under section 951. The taxpayer, however, must have either chosen the foreign tax credit in the taxable year in which such income was included in gross income under section 951(a), or have paid or accrued in such year no income, war profits, or excess profits taxes to any foreign country or possession of the United States. He must also choose the foreign tax credit in the year of the receipt of the excluded distribution.

The amount of the increase in the section 904 limitation is an amount equal to the increase in such limitation which occurred in the taxable year of the inclusion of the income under section 951(a) solely by reason of such inclusion. Such amount is then reduced by the foreign taxes which were allowed as a credit in such year of the inclusion but which would not have been allowable but for such inclusion. The increase in the section 904 limitation may not exceed the income, war profits, or excess profits taxes paid, or deemed paid, or

accrued with respect to the distribution in the taxable year such distribution is received.

Under paragraph (3) of section 960(b), a taxpayer who chose to take a foreign tax credit in the taxable year in which he was required to include income in gross income under section 951(a), but does not choose to take a foreign tax credit in the taxable year in which such income is actually received, may not deduct under section 164 any income, war profits, or excess profits taxes paid or accrued on such income.

Under paragraph (4) of section 960(b), if the increase in limitation exceeds the U.S. tax for the taxable year, the excess is deemed an overpayment of tax for such year.

SECTION 961. ADJUSTMENTS TO BASIS OF STOCK IN CONTROLLED FOREIGN CORPORATION AND OF OTHER PROPERTY

Section 961 is the same as section 958 of the bill as passed by the House except for the changes made necessary by the addition of section 962, relating to an election by individuals to be subject to tax at corporate rates.

(a) *Increase in basis.*—Subsection (a) provides that the basis of a United States shareholder's stock in a controlled foreign corporation, and of property by reason of which he is treated as owning such stock in determining the amount which he must include in gross income under section 951, is increased by the amount included in gross income under section 951. Your committee has added a provision to subsection (a) that in the case of a United States shareholder who has made an election under section 962 for the taxable year, the increase in basis shall not exceed an amount equal to the amount of tax paid under chapter 1 with respect to the amounts required to be included in his gross income under section 951(a).

Example (1).—X, who owns stock in corporation M with a basis of \$1,000, includes \$50 of M's income in gross income as required under section 951(a). The basis of X's stock in M is increased to \$1,050.

Example (2).—The facts are the same as in example (1) except that X is also required under section 951(a) to include in gross income \$60 of the income of corporation N, a controlled foreign corporation wholly owned by M. In such case the basis of X's stock in M is increased to \$1,110.

Example (3).—Y, an individual United States shareholder who owns stock in corporation O with a basis of \$1,000, and who would have included \$70 in gross income under section 951(a), makes an election under section 962, and pays \$15 in U.S. tax under chapter 1 of the code. The basis of Y's stock in corporation O is increased to \$1,015.

(b) *Reduction in basis.*—Subsection (b) provides that the basis of stock or other property with respect to which a United States shareholder receives an amount which is excluded from gross income under section 959(a) is reduced by such amount. Your committee has added a provision to subsection (b) that in the case of a United States shareholder who has made an election under section 962 for any prior taxable year, the reduction in basis shall not exceed an amount equal to the

amount received which is excluded from gross income under section 959(a), relating to the exclusion of previously taxed earnings and profits, after the application of section 962(d), relating to actual distributions of earnings and profits attributable to amounts with respect to which an election was made under section 962. Thus, if X, in example (2) above, received a distribution of \$110 which was excluded from gross income under section 959(a) as the income previously taxed in such example, the basis of X's stock in Y would be reduced again to \$1,000. If Y, in example (3) above, received a distribution of \$70, his basis in the stock of corporation O would be reduced by \$15, that is, the amount excluded from gross income under section 959(a) after the application of section 962(d).

Subsection (b)(2) provides that to the extent that an amount excluded from gross income under section 959(a) exceeds the adjusted basis of stock or other property with respect to which it is received, such excess shall be treated as gain from the sale or exchange of the property.

SECTION 962. ELECTION BY INDIVIDUALS TO BE SUBJECT TO TAX AT CORPORATE RATES

Section 962 provides an election for an individual United States shareholder to be subject to tax at corporate rates instead of individual rates with respect to amounts included in his gross income under section 951(a).

(a) *General rule.*—Subsection (a) provides that in the case of a United States shareholder who is an individual and who elects to have the provisions of section 962 apply for the taxable year, the tax imposed under chapter 1 of the Code on amounts included in gross income under section 951(a), relating to amounts included in gross income of United States shareholders, shall be an amount equal to the tax which would be imposed under section 11 of the Code, relating to tax imposed on corporations, if such amounts were received by a domestic corporation. Subsection (a) further provides that, for purposes of applying the provisions of section 960, relating to foreign tax credit, the amounts included in gross income under section 951(a) with respect to which an election is made under section 962, shall be treated as if they were received by a domestic corporation.

Example.—X, an individual and sole shareholder of controlled foreign corporation M (not a less developed country corporation), is required to include \$70,000 (the entire earnings and profits of M Corporation for the taxable year) in gross income under section 951(a) and makes an election under section 962 to be subject to tax at corporate rates. (M Corporation is the only controlled foreign corporation in which X is a United States shareholder.) Both X and M use the calendar year as a taxable year. M Corporation paid \$30,000 of foreign tax in connection with earning the \$70,000 of income referred to above. The limitation on tax under section 962(a) is equal to the

corporate tax less any foreign tax credit to which a corporation would be entitled. Thus, the tax would be computed as follows:

Income included in gross income under sec. 951(a) with respect to which election under sec. 962 is made.....	\$70, 000
Foreign tax deemed paid under sec. 960(a) (included in gross income under new sec. 78) $(\frac{\$70,000}{\$70,000} \times \$30,000)$	30, 000
Taxable income under sec. 11 of code.....	100, 000
Tax at 52 percent.....	52, 000
Less tax attributable to surtax exemption.....	5, 500
Tax.....	46, 500
Less foreign tax credit.....	30, 000
U.S. tax liability (limitation under sec. 962(a)).....	16, 500

(b) *Election*.—Subsection (b) provides that an election to have the provisions of section 962 apply for any taxable year shall be made by a United States shareholder at such time and in such manner as the Secretary of the Treasury or his delegate shall prescribe by regulations and that an election made for any taxable year may not be revoked except with the consent of the Secretary of the Treasury or his delegate.

(c) *Surtax exemption*.—Subsection (c) provides that, for purposes of applying subsection (a)(1), the surtax exemption provided by section 11(c) of the Code shall not exceed an amount which bears the same ratio to \$25,000 as the amounts included in a United States shareholder's gross income under section 951(a) for the taxable year bears to his pro rata share of the earnings and profits for the taxable year of all controlled foreign corporations with respect to which he included any amount in gross income under section 951(a).

Example.—X, an individual United States shareholder owning 60 percent of controlled foreign corporations N and O, makes an election under section 962 for the taxable year and includes in gross income for such year under section 951(a) \$20,000 with respect to corporation N and \$10,000 with respect to corporation O. Corporation M has \$100,000 and corporation N has \$50,000 earnings and profits for the taxable year. X's surtax exemption is computed as follows:

$$\frac{20,000 + 10,000}{60,000 + 30,000} \times 25,000 = 8,333.33$$

(d) *Special rules for actual distributions*.—Paragraph (1) of section 962(d) provides that the earnings and profits of a foreign corporation attributable to amounts which were included in the gross income of a United States shareholder under section 951(a) and with respect to which an election under section 962 applied shall, when such earnings and profits are distributed, notwithstanding the provisions of section 959(a)(1), relating to the exclusion from gross income of actual distributions of previously taxed earnings and profits, be included in gross income to the extent that such earnings and profits so distributed exceed the amount of tax paid on the amounts to which such election applied.

Example.—X, an individual and sole shareholder of controlled foreign corporation M (not a less developed country corporation), was required to include \$70,000 (the entire earnings and profits of M Corporation for the taxable year) in gross income under section 951(a) for the taxable year 1963, and \$30,000 (the amount of foreign taxes

paid by M Corporation for such year), and made an election under section 962 to be subject to tax at corporate rates. X paid \$16,500 in U.S. tax on such amount with the application of section 962(a). In 1964, X received an actual distribution of the \$35,000 from M Corporation. Notwithstanding the provisions of section 959(a)(1), X is required to include \$26,750 in gross income for the taxable year 1964 (\$35,000 minus \$8,250).

SECTION 963. RECEIPT OF MINIMUM DISTRIBUTIONS BY
DOMESTIC CORPORATIONS

This section provides that if a given percentage, termed a minimum distribution, of the earnings and profits of a controlled foreign corporation is received by a domestic corporate shareholder of such foreign corporation, the domestic corporation may elect to exclude from its gross income for such taxable year the amount of subpart F income of such foreign corporation otherwise includible in gross income of the domestic corporation under section 951(a)(1)(A)(i). In addition to the elective treatment accorded domestic corporate shareholders with respect to subpart F income of controlled foreign corporations in which stock is owned directly, domestic corporate shareholders may elect with respect to foreign corporations in a chain of corporations or with respect to all controlled foreign corporations in which the domestic corporate shareholder owns stock directly or stock owned indirectly through interests in foreign corporations, foreign partnerships, foreign trusts or foreign estates. The required minimum distribution of earnings and profits by a foreign corporation is inversely proportional to the effective foreign tax rate of the controlled foreign corporation with respect to which an election is made, or the consolidated earnings and profits and consolidated effective foreign tax rate of a chain of foreign corporations, or a group of controlled foreign corporations, with respect to which an election is made. Thus, as the effective foreign tax rate increases, the required minimum distribution of earnings and profits decreases. The inverse proportion is intended to result in a distribution which will give rise to sufficient United States tax to make the overall taxes of the recipient roughly approximate the United States rate.

(a) *General rule.*—Subsection (a) of section 963 sets forth the general rule that subpart F income of a controlled foreign corporation will not be included in the gross income of a United States shareholder, as defined in section 951(b), if (1) the United States shareholder is a domestic corporation; (2) the domestic corporate shareholder (A) receives a minimum distribution, as defined in section 963(b), of the earnings and profits for the taxable year from a controlled foreign corporation in which stock is owned directly, within the meaning of section 958(a)(1)(A); or, (B) to the extent the domestic corporate shareholder elects, receives a minimum distribution with respect to the consolidated earnings and profits for the taxable year of foreign corporations in a chain of corporations as described in section 963(c)(2); or, (C) the domestic corporate shareholder receives a minimum distribution, as defined in section 963(b), with respect to a group of foreign corporations as described in section 963(c)(3); and (3) the domestic corporate shareholder consents to all the regulations prescribed by the Secretary of the Treasury or his delegate under section 963 prior

to the last day prescribed by section 6072 for filing its income tax return. The exclusion from gross income under this section is limited to subpart F income of controlled foreign corporations, as defined in section 952, which would otherwise be includible in gross income under section 951(a)(1)(A)(i). This section (which is concerned with current earnings and profits) does not apply to previously excluded subpart F income withdrawn from investment in less developed country corporations includible in gross income under section 951(a)(1)(A)(ii) or increase in earnings invested in United States property includible in gross income under section 951(a)(1)(B) (both of which are measured by current and certain accumulated earnings and profits).

(b) *Minimum distributions.*—Subsection (b) of section 963 establishes a schedule of required minimum distributions of earnings and profits as a percentage of total earnings and profits. If a domestic corporate shareholder elects to apply this section to a single controlled foreign corporation as provided in subsection (a)(1), the required minimum distribution is determined by the effective foreign tax rate, determined in accordance with the provisions of subsection (d), of the controlled foreign corporation. Thus, if the controlled foreign corporation was subject to an effective foreign tax rate of 15 percent, for this elective section to apply, the controlled foreign corporation would be required to distribute, as a dividend, an amount equal to 80 percent of its earnings and profits for the taxable year of the foreign corporation ending with or within the taxable year of the electing domestic corporate shareholder. If a domestic corporate shareholder elects to apply this section to a chain of foreign corporations as provided in subsection (a)(2), the required minimum distribution is determined as a percentage of the consolidated earnings and profits of foreign corporations in the chain, to the extent elected, and the effective foreign tax rate is determined, in accordance with the provisions of subsection (d)(2), for all foreign corporations for which the election is applicable. In like manner, if a domestic corporate shareholder elects to have this section apply to all controlled foreign corporations as provided in subsection (a)(3), the required minimum distribution of earnings and profits for the taxable year is determined as a percentage of the consolidated earnings and profits of all such controlled foreign corporations, and all foreign corporations through which, within the meaning of section 958(a)(2), the domestic corporate shareholder is considered to own stock in a controlled foreign corporation, and the effective foreign tax rate is determined, in accordance with the provisions of subsection (d)(2), for all foreign corporations for which the election is applicable.

(c) *Amounts to which section applies.*—Subsection (c) of section 963 describes the controlled foreign corporation, or combination of controlled foreign corporations, in a corporate organization for which a minimum distribution of earnings and profits for a taxable year will permit a domestic corporate shareholder to elect to exclude from gross income the subpart F income of such controlled foreign corporation or corporations. Paragraphs (1), (2), (3), and (4) of section 963(c) provide for alternative applications of this section of the bill.

Paragraph (1) of section 963(c) provides that subsection (a) may apply in the case of a controlled foreign corporation in which a domestic corporate shareholder owns stock directly. Thus, application of section 963 may be limited to a single first-tier controlled

foreign corporation, to two or more first-tier controlled foreign corporations, or to all first-tier controlled foreign corporations in which a domestic corporation is a United States shareholder.

Paragraph (2) of section 963(c) provides that subsection (a) may apply to a controlled foreign corporation in which a domestic corporation owns stock directly and to a controlled foreign corporation in which the domestic corporation, within the meaning of section 958(a)(2), is considered to be the owner of stock through a foreign corporation, foreign partnership, or a foreign trust or foreign estate. However, if a domestic corporate shareholder elects with respect to a controlled foreign corporation below the first tier of foreign corporations, the earnings and profits of each foreign corporation through which the domestic corporate shareholder is considered to be the owner of stock in the controlled foreign corporation must be taken into account in determining if a required minimum distribution of consolidated earnings and profits had been made, whether or not such intermediate foreign corporations are controlled foreign corporations.

Paragraph (3) of section 963(c) provides that subsection (a) may apply to all controlled foreign corporations in which the domestic shareholder owns stock directly or is considered to own stock within the meaning of section 958(a)(2). Consistent with paragraph (2), the earnings and profits of all foreign corporations through which the domestic corporate shareholder is considered to own stock in controlled foreign corporations is taken into account in determining if a required minimum distribution had been made whether or not such intermediate foreign corporation is a controlled foreign corporation.

Subparagraph (A) of section 963(c)(4) provides for the exception of earnings and profits of certain less developed country corporations in determining if the required minimum distribution of subsection (b) has been made. The less developed country corporations which may be excluded are all such less developed country corporations other than those through which the United States shareholder is considered to own stock of other foreign corporations which are not less developed country corporations. If the election is made all less developed country corporations described in the preceding sentence must be excluded from the determination.

Subparagraph (B) of section 963(c)(4) provides that foreign branches of a domestic corporate shareholder may, at the election of such shareholder, be treated, under regulations prescribed by the Secretary of the Treasury or his delegate, as 100-percent owned controlled foreign corporations, which, for purposes of this section, will be considered to have distributed to the electing domestic corporate shareholder all of the earnings and profits attributable to such foreign branches. For purposes of this subparagraph, a branch of a domestic corporation will be considered a foreign branch if it is located in a foreign country or in the Commonwealth of Puerto Rico or a possession of the United States. However, a branch located in Puerto Rico or a possession of the United States will be taken into account under subparagraph (B) only if (1) such branch would be considered a controlled foreign corporation, if it were incorporated under the laws of Puerto Rico or such possession of the United States, as the case may be, and (2) the gross income of the electing domestic corporate shareholder, for the year of election, includes gross income derived from sources within Puerto Rico and possessions of the United States. Except as provided in the preced-

ing sentence, an election to have subparagraph (B) apply may be made by a domestic corporation only with respect to all its foreign branches.

Generally speaking, a foreign branch is a permanent organization maintained in a foreign country to engage in the active conduct of a trade or business. The income of a branch is that produced by the business activities separately conducted by it.

Subparagraph (C) of section 963(c)(4) provides that, if a domestic corporate shareholder which is a United States shareholder so elects, the consolidated earnings and profits of controlled foreign corporations as provided in subsection (a)(3) shall not include any amount with respect to the earnings and profits of any controlled foreign corporation if it is established to the satisfaction of the Secretary of the Treasury or his delegate that the earnings and profits of such controlled foreign corporation could not have been distributed to United States shareholders who own stock, directly or through foreign corporations, foreign partnerships, or foreign estates or trusts, in such controlled foreign corporation because of currency or other restrictions or limitations imposed under the laws of any foreign country.

The application of the provisions of section 963(c) may be illustrated by the following example:

Example.—Domestic corporation M owns 5 percent of the voting stock of foreign corporation A, and 100 percent of the voting stock of foreign corporations B and C respectively. Foreign corporation C owns 100 percent of the voting stock of foreign corporation D, which owns 50 percent of the voting stock of foreign corporation E. The voting stock of foreign corporation F is owned 50 percent by foreign corporation E and 30 percent by foreign corporation B. None of the foreign corporations are less developed country corporations as defined in section 955(c). Assume that all corporations use the calendar year as a taxable year. Corporations A and E are not controlled foreign corporations.

Under section 963(a)(1), corporation M may elect to determine if a minimum distribution of earnings and profits has been made with respect to the earnings and profits of corporation B, corporation C, or both corporations B and C; and thereby exclude from gross income subpart F income of corporation B, corporation C, or both corporations B and C, as the case may be, if a minimum distribution had been received. Corporation M would be required to include in gross income its pro rata share of the subpart F income of controlled foreign corporations D and F.

In the alternative, corporation M may elect under section 963(a)(2) to consolidate the earnings and profits of corporations C and D, or corporations B, C, D, E, and F; and, if the required minimum distribution is received from corporation C with respect to the consolidated earnings and profits of corporations C and D, or from corporations B and C with respect to the consolidated earnings and profits of corporations B, C, D, E, and F, corporation M may exclude from gross income subpart F income of corporations C and D or corporations B, C, D, and F, as the case may be.

As another alternative, corporation M may elect under section 963(a)(3) to determine if a minimum distribution of earnings and profits has been made with respect to the earnings and profits of corporations B, C, D, E, and F. If the required minimum distribution is received from corporations B and C with respect to the consolidated earnings

and profits of corporations B, C, D, E, and F, corporation M may exclude from gross income subpart F income of corporations B, C, D, and F.

(d) *Effective foreign tax rate.*—Subsection (d) of section 963 defines the term “effective foreign tax rate” as used in section 963(b).

Paragraph (1) of section 963(d) establishes the rule for determining the effective foreign tax rate of a single controlled foreign corporation in determining if a minimum distribution has been received by a domestic corporate shareholder as required in the case of a distribution from a controlled foreign corporation to which section 963(a)(1) applies. In such a case, the effective foreign tax rate is the percentage that income, war profits, or excess profits taxes paid or accrued to foreign countries by the controlled foreign corporation on or with respect to the earnings and profits of such corporation for the taxable year of such corporation ending in or with the taxable year of the electing domestic corporate shareholder, bears to the sum of the earnings and profits of such corporation for such period and the income, war profits, and excess profits taxes paid or accrued with respect to such earnings and profits. For example, if a controlled foreign corporation had profits before foreign income taxes of \$100,000, and paid foreign income taxes of \$20,000, the effective tax rate would be 20 percent ($\$20,000/\$100,000$). In cases where the amount of foreign income taxes payable by the corporation varies depending upon whether or not profits are distributed by the foreign corporation, the effective foreign tax rate is determined without regard to distributions made by the controlled foreign corporation. For example, assume foreign corporation A is incorporated in country X and derives all its income from within country X. Assume also, that country X levies an income tax of 50 percent on undistributed profits and 15 percent on distributed profits. Assume further that corporation A derived before tax income of \$100,000, distributed \$50,000, and paid foreign income tax of \$32,500 (50 percent of \$50,000 undistributed income and 15 percent of \$50,000 distributed income). Although corporation A only paid an effective tax rate of 32½ percent, it will be deemed to have paid an effective foreign tax rate of 50 percent for purposes of section 963. If country X had levied a tax of 25 percent on undistributed profits and an additional 15-percent withholding tax on distributed profits, although the foreign tax paid would have been the same, \$32,500 or 32½ percent, the effective foreign tax rate will be deemed to be 25 percent for purposes of section 963.

Paragraph (2) of section 963(d) establishes the rule for determining the effective foreign tax rate if the earnings and profits of two or more foreign corporations are consolidated under section 963(a)(2) or (3). In such cases, the effective foreign tax rate is the percentage that income, war profits, or excess profits taxes paid or accrued to any foreign country by the foreign corporations whose earnings and profits are consolidated with respect to the total earnings and profits of such corporations for taxable years of such corporations ending in or with the taxable year of the electing domestic corporate shareholder, bears to the sum of the earnings and profits of such corporations for such periods and the income, war profits, and excess profits taxes paid or accrued with respect to such earnings and profits to any foreign country.

(e) *Special rules.*—Paragraph (1) of section 963(e) provides that distributions made by a foreign corporation in the first 60 days of any taxable year shall be treated as having been paid from the earnings and profits of the preceding taxable year or years of the foreign corporation. In addition, the Secretary of the Treasury or his delegate may by regulations provide a period in excess of 60 days in lieu of such 60-day period.

Paragraph (2) of section 963(e) permits a domestic corporate shareholder of a controlled foreign corporation who elects the provisions of this section to treat the receipt of a subsequent distribution with respect to the foreign corporation or foreign corporations to which the election applies as having been made for, and received in, the taxable year of the United States shareholder for which the domestic corporate shareholder applied the provisions of this section of the bill. For example, if a domestic shareholder received a distribution of 50 percent of the earnings and profits of controlled foreign corporation A for taxable year 1963 (the required minimum distribution of earnings and profits if the effective foreign tax rate was 40 percent), and it was determined in 1965 that the effective foreign tax rate was 30 percent, subsequent distributions equal to an additional 10 percent of 1963 earnings and profits (the required minimum distribution of earnings and profits is 60 percent if the effective foreign tax rate is 30 percent) may, if made at a time and in a manner prescribed by the Secretary of the Treasury or his delegate, be treated, for purposes of chapter 1, as having been made by the foreign corporation in taxable year 1963 and as having been received by the electing domestic corporate shareholder in its taxable year with or in which the 1963 taxable year of the controlled foreign corporation ended. The distribution will result in additional tax owing in 1963 and interest will be payable on that additional tax for the time it has been owing.

Paragraph (3) of section 963(e) provides that an affiliated group of corporations which are eligible to make a consolidated return under section 1501 for the taxable year may elect to be treated as a single United States shareholder for purposes of section 963.

The application of this provision of your committee bill may be illustrated by the following example involving domestic corporations M and N and foreign corporations A and B. Corporation A is a wholly owned subsidiary of corporation M and corporation B is a wholly owned subsidiary of corporation N. Corporation A had earnings and profits for taxable year 1963 of \$100, none of which was subpart F income, after payment of foreign income tax of \$120 (an effective foreign tax rate of 55 percent). Corporation B had earnings and profits for taxable year 1963 of \$100, all of which was subpart F income, after payment of foreign income tax of \$15 (an effective foreign tax rate of 13 percent). Corporation M received a distribution of \$40 from corporation A and corporation N received a distribution of \$60 from corporation B. Corporations M and N file a consolidated return with respect to income tax imposed by chapter 1. Corporations M and N elected, under the provisions of section 963(e)(3), to be treated as a single United States person for purposes of determining if a minimum distribution of the consolidated earnings and profits of corporations A and B had been received. Since the consolidated effective foreign tax rate of corporations A and B was 40 percent (the percentage that foreign tax paid (\$135) bears to the sum of earnings and profits (\$200), and foreign taxes paid (\$135)), and corpo-

rations M and N, treated as a single shareholder, received 50 percent of the consolidated earnings and profits of corporations A and B (\$100 distributed out of consolidated earnings and profits of \$200), the subpart F income of corporation B is excluded from the consolidated gross income of corporations M and N.

(f) *Regulations*.—Subsection (f) of section 963 provides that the Secretary of the Treasury or his delegate shall prescribe such regulations as the Secretary of the Treasury may deem necessary to carry out the provisions of this section of the bill. Such regulations may include, among other provisions, the establishment of special rules for the determination of the amount of foreign tax credit allowable an electing domestic corporate shareholder in the case of distributions with respect to the earnings and profits of two or more foreign corporations.

Thus, special rules for the determination of the amount of foreign tax credit allowable an electing domestic corporate shareholder (including an affiliated group of corporations electing to be treated as a single U.S. shareholder) in the case of distributions with respect to the earnings and profits of a chain of foreign corporations or of brother-sister controlled foreign corporations, may be established under regulations prescribed by the Secretary of the Treasury or his delegate. The application of the provisions of this subsection may be illustrated by the following examples:

Example (1).—Assume domestic corporation M owns 100 percent of the stock of controlled foreign corporation A, which owns 100 percent of the stock of controlled foreign corporation B. All corporations use the calendar year as a taxable year. In 1963 corporation A had earnings and profits of \$75 after payment of foreign income tax of \$75 (a 50-percent rate). Corporation B, for taxable year 1963, had earnings and profits of \$120 after payment of foreign income tax of \$30 (a 20-percent rate). The consolidated effective foreign tax rate of corporations A and B was 35 percent (total tax paid over consolidated earnings and profits plus total tax paid—105/300) and required a minimum distribution of 60 percent of the consolidated earnings and profits of corporations A and B—\$117 ($195 \times 60\%$). Corporation M received a distribution of \$117 from corporation A, which amount was includible in gross income as a dividend. Corporation M elects to consolidate under section 963(c)(2). Corporation M's tax liability under this chapter is determined as follows:

Amount includible in gross income as a dividend.....	\$117. 00
Amount included in gross income under sec. 78 (foreign tax paid with respect to \$117 based upon the consolidated effective foreign tax rate of corporations A and B ($117/195 \times 105$)).....	63. 00
Total amount included in gross income.....	180. 00
Tentative U.S. tax (at 52-percent rate).....	93. 60
Foreign tax credit based upon consolidated effective foreign tax rate of 35 percent ($117/195 \times 105$).....	63. 00
Net U.S. tax.....	30. 60

Example (2).—Domestic corporation M owns 100 percent of the stock of foreign corporations A and B. All corporations use the calendar year as a taxable year. In 1963 corporation A had earnings and profits of \$80 after payment of foreign income tax of \$120 (a 60-percent rate). Corporation B, for taxable year 1963, had earnings and profits of \$100 with respect to which no foreign income tax had

been paid. The consolidated effective foreign tax rate of corporations A and B was 40 percent (total tax paid over consolidated earnings and profits plus total tax paid—120/300) and required a minimum distribution of \$90 ($\180×50 percent). Corporation M received a distribution of \$80 from corporation A and \$10 from corporation B, which amounts were includible in gross income as a dividend. Corporation M elects to consolidate under section 963(c)(3). Corporation M's tax liability under this chapter is determined as follows:

Amount includible in gross income as a dividend.....	\$90
Amount included in gross income under sec. 78 (foreign tax paid with respect to \$90 based upon the consolidated effective foreign tax rate of corporations A and B ($90/180 \times 120$)).....	60
Total amount included in gross income.....	150
Tentative U.S. tax (at 52-percent rate).....	78
Foreign tax credit based upon consolidated effective foreign tax rate of 40 percent ($90/180 \times 120$).....	60
Net U.S. tax.....	18

SECTION 964. MISCELLANEOUS PROVISIONS

Section 964 provides the regulatory authority necessary for the administration of subpart F and subpart G.

(a) *Earnings and profits*.—Under subsection (a), the earnings and profits of a foreign corporation and the deficit in earnings and profits for a taxable year shall be determined according to rules substantially similar to those applicable to domestic corporations under regulations prescribed by the Secretary of the Treasury or his delegate.

(b) *Blocked foreign income*.—Subsection (b) provides that under regulations prescribed by the Secretary of the Treasury or his delegate no part of earnings and profits shall be included in earnings and profits under sections 952, 955, and 956, if it is established to the satisfaction of the Secretary of the Treasury or his delegate that such part could not be distributed by the controlled foreign corporation to United States shareholders because of currency restrictions or limitations imposed under the laws of a foreign country. Such rule applies in either a case where the United States shareholder directly owns (see sec. 958(a)(1)(A)) the stock, or in case he indirectly owns (see sec. 958(a)(1)(B)) the stock and the restrictions apply at some point in the chain of ownership.

(c) *Records and accounts of United States shareholders*.—Subsection (c) provides that the Secretary of the Treasury or his delegate may by regulations require a United States shareholder or a person who has been a United States shareholder to maintain such records and accounts as such regulations prescribe as necessary to carry out the provisions of subpart F and subpart G. Such regulations may provide that the maintenance and furnishing of such records and accounts by one person may satisfy the requirement as to all United States shareholders otherwise required to furnish records and accounts with respect to a controlled foreign corporation.

SUBPART G.—EXPORT TRADE CORPORATIONS

This subpart, for which there is no corresponding provision in the bill as passed by the House, provides generally that the export trade income, as defined in section 971(b), constituting foreign base company income of a controlled foreign corporation which is an export trade corporation, as defined in section 971(a), shall reduce the subpart F income of such corporation to the extent of such corporation's increase in investment in export trade assets, as defined in section 971(c). Limitations on this reduction are provided in section 970(a), based on the relationship of the export trade income to export promotion expenses or on the gross receipts from export trade income of the corporation. Section 970(b) provides for an inclusion in gross income of amounts by which subpart F income was previously reduced to the extent of a decrease in investment in export trade assets. Section 972 provides for the consolidation of groups of export trade corporations. Nothing in the new subpart G affects the authority of the Secretary of the Treasury or his delegate to apply the provisions of section 482 relating to allocation of income and deductions among taxpayers.

SEC. 970. REDUCTION OF SUBPART F INCOME OF EXPORT TRADE CORPORATIONS

(a) *Export trade income constituting foreign base company income.*— Subsection (a) of section 970 provides that the subpart F income of a controlled foreign corporation, as defined in section 957, which for the taxable year is an export trade corporation, as defined in section 971(a), shall be reduced by an amount equal to so much of the export trade income, as defined in section 971(b), of such corporation for such year as constitutes foreign base company income, as defined in section 954. However, the amount by which subpart F income is reduced is limited to the lesser of (1) an amount provided in subparagraph (A) of section 970(a)(1); (2) an amount provided in subparagraph (B) of section 970(a)(1); or (3) an amount provided in paragraph (2) of section 970(a). Paragraph (1) of section 970(a) also provides that subpart F income of a controlled foreign corporation is to be determined without regard to subpart G. Thus, the amount of foreign base company income of a controlled foreign corporation, for purposes of section 954(b)(3), is determined without regard to the amount by which subpart F income is reduced under section 970.

Subparagraph (A) of section 970 provides that the amount by which subpart F income may be reduced under section 970 may not exceed an amount equal to $1\frac{1}{2}$ times so much of the export promotion expenses, as defined in section 971(d), of the export trade corporation for the year as is properly allocable to the export trade income of such corporation which constitutes foreign base company income for such year.

Subparagraph (B) of section 970(a)(1) provides, as an alternative limitation, that the amount by which subpart F income may be reduced under section 970 may not exceed an amount equal to 10 percent of so much of the gross receipts for the taxable year accruing to the export trade corporation from the sale, installation, operation, maintenance, or use of property in respect of which the export trade corporation derived export trade income which is properly allocable

to export trade income which constituted foreign base company income for such year. If the gross receipts attributable to the sale, installation, operation, maintenance, or use of export property arises from commissions, fees, or other compensation received by an export trade corporation for its services, the amount upon which the 10-percent limitation applies is the amount upon which the commission, fee, or other compensation is computed.

The allocations with respect to export trade income which constitute foreign base company income under subparagraphs (A) and (B) shall be made under regulations prescribed by the Secretary of the Treasury or his delegate.

In addition to the alternative limitations provided in paragraph (1) of section 970(a), paragraph (2) of section 970(a) establishes an overall limitation that provides that the reduction under paragraph (1) for any taxable year shall not exceed an amount which bears the same ratio to the increase in the investments in export trade assets of an export trade corporation for its taxable year as the export trade income which constitutes foreign base company income of the export trade corporation for the taxable year bears to the entire export trade income of such corporation for such year.

The application of the provisions of this subsection may be illustrated by the following examples:

Example (1).—Corporation A, a 100-percent owned subsidiary of domestic corporation M, purchased products manufactured by corporation M in the United States from corporation M and resold such products to unrelated persons for use outside the foreign country in which corporation A was incorporated. For taxable year 1963, the entire operations of corporation A consisted of this activity. In such year, it purchased goods from corporation M for \$1,000 and sold the goods for \$2,000. Corporation A derived gross income of \$1,000, incurred export promotion expenses of \$300 with respect to such sales, paid foreign income taxes of \$50, and derived export trade income of \$650, all of which constituted foreign base company income. Corporation A, in 1963, had an increase in investment in export trade assets of \$100. The limitation on the amount by which subpart F income is reduced with respect to export trade income which constitutes foreign base company income as provided in section 970(a), is \$100, the lesser of (1) the export trade income which constitutes foreign base company income (\$650); (2) $1\frac{1}{2}$ times the export promotion expenses properly allocable to export trade income which constitutes foreign base company income (\$450 (150 percent of \$300)); (3) 10 percent of gross receipts from the sale of property from which corporation A derived export trade income which is properly allocable to export trade income which constitutes foreign base company income (\$200 (10 percent of \$2,000)); or (4) the increase in investment in export trade assets (\$100). Corporation M would include \$550 of subpart F income of corporation A in gross income in accordance with the provisions of section 951(a)(1)(A)(i).

Example (2).—Controlled foreign corporation A, a 100-percent owned subsidiary of domestic corporation M, in taxable year 1965 had net income of \$100 and qualified as an export trade corporation. Corporation A derived export trade income of \$75, of which \$60 was foreign base company income. The remaining \$25 of net income, which was not export trade income, was subpart F income. The

\$60 of export trade income which constituted foreign base company income was less than $1\frac{1}{2}$ times the export promotion expenses of \$100 of corporation A for the taxable year properly allocable to such income and less than 10 percent of gross receipts of \$1,000 from the sale, installation, operation, maintenance, or use of property in respect of which corporation A derived export trade income which constituted foreign base company income. The total increase in investment in export trade assets was \$40. Corporation M is required to include \$53 subpart F income of corporation A in gross income for taxable year 1963, which amount is computed as follows:

- | | |
|--|------|
| (i) Tentative subpart F income of corporation A (\$60 which is also export trade income plus \$25 which is not export trade income)----- | \$85 |
| (ii) Amount by which subpart F income is reduced under sec. 970(a): | |
| (a) Export trade income which reduces subpart F income before application of the sec. 970(a)(2) limitation (item (1), (2), or (3), whichever is the lesser): | |
| (1) Export trade income which is foreign base company income----- | \$60 |
| (2) 150 percent of export promotion expenses properly allocable to the amount described in (1) (sec. 970(a)(1)(A))----- | 150 |
| (3) 10 percent of gross receipts from the sale of property from which the amount described in (1) was derived (sec. 970(a)(2)(B))----- | 100 |
| (b) Section 970(a)(2) limitation: | |
| The percentage of the increase in investment in export trade assets which export trade income which constitutes foreign base company income bears to total export trade income | |
| $\$40 \times \frac{\$60}{\$75} =$ ----- | 32 |
| Amount of export trade income which reduces subpart F income (item (a) or (b) whichever is lesser)----- | 32 |
| (iii) Subpart F income includible in gross income of corporation M (item (i) minus item (ii))----- | 53 |

(b) *Inclusion of certain previously excluded amounts.*—Subsection (b) of section 970 provides that each United States shareholder, as defined in section 951(b), who is a shareholder in a controlled foreign corporation that was an export trade corporation in any prior taxable year, must include in his gross income, under section 951(a)(1)(A)(ii), as an amount to which section 955 applies, an amount equal to his pro rata share of the decrease in investments in export trade assets of the controlled foreign corporation for such year. The United States shareholder's pro rata share of a decrease is includible in gross income under section 970(b), however, only to the extent of—

(1) the excess of the United States shareholder's pro rata share of the sum of the reductions for all previous years in subpart F income by reason of section 970(a) and section 972 (relating to the treatment of two or more corporations as a single corporation), over

(2) all inclusions in his gross income under section 951(a)(1)(A)(ii) with the application of section 970(b) for all previous years.

Example.—Assume that for 1963 Z, a controlled foreign corporation, having \$100 in export trade income of which \$40 is subpart F income, has an increase in investment in export trade assets of \$100 and reduces its subpart F income by \$40 under section 970(a) (with the application of the sec. 970(a)(2) overall limitation which is also \$40).

Assume that for 1964 Z has a \$50 decrease in investment in export trade assets. Y, a United States shareholder, who wholly owns Z, must include \$40 in gross income under subsection (b) as his pro rata share of the decrease in investments in export trade assets.

(c) *Investments in export trade assets.*—Subsection (c) of section 970 establishes the rules for determining if, for a taxable year of a controlled foreign corporation, there has been an increase in investments in export trade assets for purposes of section 970(a), or a decrease in investments in export trade assets for purposes of section 970(b).

Paragraph (1) of section 970(c) provides that the amount taken into account with respect to any export trade asset will be its adjusted basis, reduced by any liability to which the asset is subject.

Paragraph (2) of section 970(c) provides that the amount of increase in investments in export trade assets of a controlled foreign corporation for any taxable year, for purposes of section 970(a), is the amount by which the amount of such investments at the close of the taxable year exceeds the amount of such investments at the close of the preceding taxable year.

Paragraph (3) of section 970(c) provides that the amount of decrease in investments in export trade assets of a controlled foreign corporation for any taxable year, for purposes of section 970(b), is the amount by which the amount of such investments at the close of the preceding taxable year, reduced by an amount equal to the amount of the net loss sustained during the taxable year with respect to export trade assets, exceeds the amount of such investments at the close of the taxable year.

Paragraph (4) of section 970(c) provides that a United States shareholder of an export trade corporation may, under regulations prescribed by the Secretary of the Treasury or his delegate, make the determinations under paragraphs (2) and (3) of section 970(c) as of the close of the 75th day after the close of the years referred to in such paragraphs in lieu of on the last day of such years. It is also provided that such an election made for any taxable year shall apply to such year and to all succeeding taxable years unless the Secretary of the Treasury or his delegate consents to the revocation of such election.

SECTION 971. DEFINITIONS

Section 971 defines the terms export trade corporation, export trade income, export trade assets, export promotion expenses, export property, and unrelated person for purposes of subpart G of subchapter N of chapter 1.

(a) *Export trade corporation.*—Subsection (a) of section 971 defines the term “export trade corporation” for purposes of subpart G.

Paragraph (1) of section 971(a) establishes the general rule that a controlled foreign corporation, as defined in section 957, is an export trade corporation if for the three calendar year period immediately preceding the close of the taxable year of such corporation, the corporation (1) derived 90 percent or more of its gross income from sources without the United States, as determined in accordance with the provisions of sections 861 through 863, and (2) 75 percent or more of the gross income of such corporation constituted income in respect of which the controlled foreign corporation derived export trade income, as defined in section 971(b). However, for taxable years of a controlled foreign corporation ending less than three calendar years after

taxable years of such corporation beginning after December 31, 1962, 90 percent or more of the gross income of such corporation must be derived from sources without the United States, and 75 percent or more of the gross income of such corporation must have constituted income in respect of which the controlled foreign corporation derived export trade income, for taxable years of the corporation beginning after December 31, 1962.

Paragraph (2) of section 971(a) provides a special rule in the case of controlled foreign corporations if 50 percent or more of the gross income of such a corporation, for the period specified in section 971(a)(1)(A), constituted income in respect of which the controlled foreign corporation derived export trade income in respect of agricultural products grown in the United States. In such cases, a controlled foreign corporation is considered an export trade corporation without regard to the fact 75 percent or more of the gross income of such corporation does not constitute income in respect of which the controlled foreign corporation derived export trade income.

(b) *Export trade income*.—Subsection (b) of section 971 defines the term “export trade income” for purposes of subpart G.

Paragraph (1) of section 971(b) includes within the definition of export trade income, net income of a controlled foreign corporation derived from the sale of export property, as defined in section 971(e), by the controlled foreign corporation to an unrelated person, as defined in section 971(f), for use, consumption, or disposition outside the United States. The export trade income derived from the sale of export property may consist of other than foreign base company sales income, as defined in section 954(d). For example, goods may be purchased by the export trade corporation from an unrelated person and sold to an unrelated person, or if purchased from a related person, the goods may be sold to an unrelated person for use, consumption, or disposition within the country in which the export trade corporation is incorporated. In addition to net income derived from the purchase and resale of property manufactured, produced, grown, or extracted in the United States, export trade income includes net income from commissions, fees, compensation, or other income of a controlled foreign corporation (1) derived from the performance of commercial, industrial, financial, technical, scientific, managerial, engineering, architectural, skilled, or other services in connection with the sale of export property to an unrelated person for use, consumption, or disposition outside the United States or (2) derived in connection with the installation or maintenance of such property.

Paragraph (2) of section 971(b) includes within the definition of export trade income, net income of a controlled foreign corporation derived from commercial, industrial, financial, technical, scientific, managerial, engineering, architectural, skilled, or other services performed by the controlled foreign corporation in connection with the use by an unrelated person outside the United States of patents, copyrights, secret processes and formulas, goodwill, trademarks, trade brands, franchises, and other like property acquired or developed and owned by the United States manufacturer, producer, grower, or extractor of export property, but only if the controlled foreign corporation derived export trade income (as defined in sec. 971(b)(1)) from the sale of such property.

Paragraph (3) of section 971(b) includes within the definition of export trade income, net income of a controlled foreign corporation

derived from the furnishing of technical, scientific, or engineering services to unrelated persons to the extent income from such services is attributable to the use of export property in the rendition of the services. If income from the rendition of technical, scientific, or engineering services is not solely attributable to the use of export property, and the amount attributable to export property cannot be established by reference to transactions between unrelated persons, the amount of export trade income will be deemed to be that percentage of total gross income received by the controlled foreign corporation from such services as the cost of the export property consumed in the rendition of such services, including a reasonable allowance for depreciation, bears to the total cost attributable to such service income. For example, assume a machine produced in the United States was sold to a customer in Germany. Controlled foreign corporation A contracted to furnish technical services to the German user with respect to the United States manufactured machine and a similar machine manufactured in Germany. The entire commission allocable to servicing the United States manufactured machine would be export trade income. If corporation A used replacement parts manufactured in the United States in servicing the German manufactured machine, corporation A would derive export trade income in the percentage of the commission allocable to servicing the German machine as the cost of the United States replacement parts used in furnishing the service bears to total cost and expenses of furnishing the services.

Paragraph (4) of section 971(b) includes within the definition of export trade income, interest income received by a controlled foreign corporation on evidences of indebtedness executed by unrelated persons in connection with payment for purchases of export property for use, consumption, or disposition outside the United States, or in connection with the payment for services described in sections 971(b) (2) and (3).

(c) *Export trade assets*.—Subsection (c) of section 971 defines the term “export trade assets” for purposes of subpart G to include (1) working capital reasonably necessary for the production of export trade income; (2) inventory of export property held for use, consumption, or disposition outside the United States; (3) facilities located outside the United States for the storage, handling, transportation, packaging, or servicing of export property; and (4) evidences of indebtedness executed by unrelated persons in connection with payment for purchases of export property for use, consumption, or disposition outside the United States, or in connection with services described in section 971(b) (2) and (3). For purposes of paragraph (2) of section 971(c), inventory of an export trade corporation will constitute export property held for use, consumption, or disposition outside the United States, even if such property is in the United States pending shipment. For purposes of paragraph (3) of section 971(c) a facility used for the manufacture or production of property will not be considered to be used for the purpose of handling export property, even though export property may be used or consumed in production or become a component part of a manufactured article.

(d) *Export promotion expenses*.—Subsection (d) of section 971 defines the term “export promotion expenses,” as used in section 970(a)(1), to include all ordinary and necessary expenses paid or in-

curring by a controlled foreign corporation which are reasonably allocable to the receipt or production of export trade income. Expenses so allocable include, but are not limited to, a reasonable allowance for salaries or other compensation for personal services actually rendered for the purpose of producing export trade income, rentals or other payments for the use of property actually used for the purpose of producing export trade income, and a reasonable allowance for the exhaustion, wear, and tear of property actually used for the purpose of producing export trade income. However, no expense incurred within the United States will be treated as an export promotion expense unless at least 90 percent of all salaries incurred for the production of export trade income, 90 percent of rents and other payments for the use of property used for producing export trade income, 90 percent of depreciation allowances on property used in the production of export trade income, and 90 percent of all other ordinary and necessary expenses reasonably allocable to the production of export trade income, are paid or incurred outside the United States. For this purpose, salary expenses will be considered paid or incurred at the place where the employment is performed, and rents, depreciation and other expenses related to property will be considered incurred at the place where the property is located.

(e) *Export property*.—Subsection (e) of section 971 defines the term “export property” for purposes of subpart G to include any property manufactured, produced, grown, or extracted in the United States, or any interest in such property.

(f) *Unrelated person*.—Subsection (f) of section 971 defines the term “unrelated person” for purposes of subpart G to mean a person other than a related person as defined in section 954(d)(3).

SEC. 972. CONSOLIDATION OF GROUP OF EXPORT TRADE CORPORATIONS

Section 972 provides that a United States shareholder, as defined in section 951(b), of a controlled foreign corporation which is an export trade corporation, may, under regulations prescribed by the Secretary of the Treasury or his delegate, treat as a single controlled foreign corporation, for purposes of subparts F and G of subchapter N, (1) such controlled foreign corporation, (2) all controlled foreign corporations which are export trade corporations if 80 percent or more of the total combined voting power of all classes of stock entitled to vote of which is owned by such controlled foreign corporation, and (3) all controlled foreign corporations which are export trade corporations if 80 percent or more of the total combined voting power of all classes of stock entitled to vote of which is owned by controlled foreign corporations described in item (2).

(b) *Technical and clerical amendments*.—Subsection (b) of section 12 of the bill makes conforming changes.

(c) *Effective date*.—Subsection (c) of section 12 of the bill provides that the amendments made by section 12 are to apply with respect to taxable years of foreign corporations beginning after December 31, 1962, and to taxable years of United States shareholders in which or with which such taxable years of such corporations end.

SECTION 13. GAIN FROM DISPOSITIONS OF CERTAIN DEPRECIABLE PROPERTY

(a) *In general.*—Paragraph (1) of section 13(a) of the bill adds a new section 1245 to the 1954 Code. In general, the new section provides for the inclusion in gross income (as ordinary income) of the gain from the disposition of certain depreciable property, to the extent of depreciation deductions taken in periods after December 31, 1961, which are reflected in the adjusted basis of such property.

SECTION 1245. GAIN FROM DISPOSITIONS OF CERTAIN DEPRECIABLE PROPERTY

(a) *General rule.*—Paragraph (1) of section 1245(a) provides the general rule that if “section 1245 property” is disposed of, the amount by which the lower of “recomputed basis” or the amount realized (or the fair market value in transactions in which no amount is realized) exceeds the adjusted basis of the property is to be treated as gain from the sale or exchange of property which is neither a capital asset nor property described in section 1231. The term “disposed of” includes any transfer or involuntary conversion. The bill as passed by the House provided that paragraph (1) applies only to dispositions after the enactment of the Revenue Act of 1962. The bill as reported by your committee provides that paragraph (1) applies only to dispositions during taxable years beginning after December 31, 1962.

Paragraph (2) of section 1245(a), under the bill as passed by the House, defined “recomputed basis” as the adjusted basis of the property recomputed by adding thereto all adjustments, for taxable years beginning after December 31, 1961, reflected in such adjusted basis on account of deductions for depreciation, or for amortization under section 168, whether in respect of the same or other property and whether allowed or allowable to the taxpayer or any other person. Your committee amendments provide that such adjustments shall be added thereto for all periods after December 31, 1961. For example, if a taxpayer, who reports his income on the basis of a fiscal year ending November 30, purchases section 1245 property on January 1, 1962, at a cost of \$10,000 and the taxpayer takes depreciation deductions of \$2,000 (the amount allowable) before making a gift of the property to his son on October 31, 1962, the son’s adjusted basis in the property for purposes of determining gain would, under the provisions of sections 1015 (relating to the basis of property acquired by gift) and 1016 (relating to adjustments to basis), be the same as his father’s adjusted basis (\$8,000), and the recomputed basis of the property in the son’s hands would be \$10,000 since the \$2,000 of depreciation deductions taken by the father are reflected in the son’s basis in the property. Thus, if the son later sells the property, during a taxable year of the son beginning after December 31, 1962, for \$10,000, he would have \$2,000 of gain to which section 1245(a) applies. Moreover, if the son himself takes \$1,000 in depreciation deductions (the amount allowable) with respect to the property and then sells it for \$10,000, he would have \$3,000 of gain to which section 1245(a) applies.

While recomputed basis is determined with respect to adjustments to basis for deductions for depreciation (and for amortization under sec. 168) which were either allowed or allowable, if the taxpayer can

establish by adequate records or other sufficient evidence that the amount allowed for any taxable year was less than the amount allowable, the amount to be added for such taxable year is the amount allowed. For example, assume that in the year 1967 it becomes necessary to determine the recomputed basis of property, the adjusted basis of which reflects an adjustment of \$1,000 with respect to depreciation deductions allowable for the calendar year 1962. If the taxpayer can establish by adequate records or other sufficient evidence that he had been allowed a deduction of only \$800 for 1962, then in determining the recomputed basis, the amount added to adjusted basis with respect to the \$1,000 adjustment to basis for 1962 will be only \$800.

Paragraph (1) of section 1245(a) further provides that gain is to be recognized notwithstanding any other provision of subtitle A of the 1954 Code. Thus, other nonrecognition sections of the code are overridden by the new section. For example, the gain under such paragraph (1) would be recognized to a corporation in the case of a distribution of section 1245 property by it to a shareholder, notwithstanding the provisions of section 311(a) or 336. Likewise, gain under such paragraph (1) would be recognized to a corporation on a sale or exchange of such property, notwithstanding the provisions of section 337. The operation of section 1245 may, however, be affected by the taxpayer's method of accounting. For example, the gain from a disposition to which section 1245 applies may be reported by the taxpayer under the installment method if such method is otherwise available under section 453 of the code. For another example, section 1245 does not require recognition of gain or loss upon normal retirement of an asset in a multiple asset account as long as the taxpayer's method of accounting, in accordance with Treasury regulations, does not require recognition of such gain or loss and clearly reflects income.

In the case of a disposition of section 1245 property in which an amount is realized (a sale, exchange, or involuntary conversion), the gain to which section 1245(a) applies is the amount by which the amount realized or the recomputed basis, whichever is lower, exceeds the adjusted basis of the property. In the case of any other disposition, the gain to which section 1245(a) applies is the amount by which the fair market value of the property on the date of disposition or its recomputed basis, whichever is lower, exceeds its adjusted basis. For example, if section 1245 property has an adjusted basis of \$2,000 and a recomputed basis of \$3,300 and is sold for \$2,900, the gain to which section 1245(a) applies is \$900 (\$2,900 minus \$2,000). If the property is sold for \$3,700, the gain is \$1,700, of which \$1,300 (\$3,300 minus \$2,000) is gain to which section 1245(a) applies. If, on the other hand, the property is distributed by a corporation to a stockholder in a distribution to which section 1245(a) applies and at a time when the fair market value of the property is \$3,100, the gain recognized to the corporation upon such disposition is \$1,100 (\$3,100 minus \$2,000); if the fair market value is \$3,800 at the time of such disposition, the gain to which section 1245(a) applies is \$1,300 (\$3,300 minus \$2,000).

Paragraph (3) of section 1245(a) defines "section 1245 property." Section 1245 property is any property (other than livestock) of a type described in subparagraph (A) or (B) of such paragraph (3) which is or has been property of a character subject to the allowance for de-

preciation provided in section 167. Even though the property may not be subject to the allowance for depreciation in the hands of the taxpayer, such property is nevertheless subject to the provisions of section 1245(a) if the property was subject to the allowance for depreciation in the hands of any prior holder, and if such depreciation is taken into account in determining the adjusted basis of the property in the hands of the taxpayer.

The definition of "section 1245 property" is similar in certain respects to the definition of "section 38 property" contained in section 48(a) (relating to the investment credit). However, section 1245 property is a broader concept than section 38 property, since (for example) the definition of section 1245 property is not subject to the minimum useful life provision in section 48(a)(1) or to the other limitation and exclusion provisions in paragraphs (2) through (5) of section 48(a). Moreover, the term "personal property" in subparagraph (A) of section 1245(a)(3) is intended to include not only "tangible personal property" referred to in section 48(a)(1)(A) but also intangible personal property.

Subparagraph (B) of section 1245(a)(3) describes other property (not including a building or its structural components) if such other property is tangible and has an adjusted basis in which there are reflected adjustments for depreciation or amortization under section 168 which would be taken into account in determining recomputed basis for a period in which such property (or other property) either (i) was used as an integral part of manufacturing, production, or extraction, or of furnishing transportation, communications, electrical energy, gas, water, or sewage disposal services, or (ii) constituted research or storage facilities used in connection with any such activities. The language in clauses (i) and (ii) in section 1245(a)(3)(B) is intended to have the same meaning as when used in clauses (i) and (ii) in section 48(a)(1)(B) (relating to the definition of sec. 38 property subject to the investment credit). Even though the property is not used by the taxpayer as an integral part of an activity specified in clause (i), or does not constitute research or storage facilities within the meaning of clause (ii), such property in certain circumstances may, nevertheless, be section 1245 property under subparagraph (B). An illustration of such a circumstance is when the adjusted basis of such property in the hands of the taxpayer reflects adjustments for depreciation with respect to such property taken for periods after December 31, 1961, at a time when such property was used as an integral part of manufacturing by the taxpayer or another taxpayer. Another illustration is when the adjusted basis of such property in the hands of the taxpayer reflects adjustments for depreciation with respect to *other* property (as, for example, in the case of a like kind exchange under sec. 1031) taken for periods after December 31, 1961, at a time when such other property was used as an integral part of manufacturing by the taxpayer.

(b) *Exceptions and limitations.*—Subsection (b) of section 1245 sets forth certain exceptions and limitations to the general rule provided in subsection (a). Paragraph (1) provides that subsection (a) will not apply to a disposition by gift. Paragraph (2) provides that, except as provided in section 691, subsection (a) will not apply to a transfer at death.

Paragraph (3) of section 1245(b) provides that if the basis of property in the hands of a transferee is determined by reference to its basis

in the hands of the transferor by reason of the application of certain sections of the code providing for nonrecognition treatment, then the amount of gain taken into account by the transferor under subsection (a)(1) is to be limited to the amount of gain recognized by the transferor under these sections (determined without regard to sec. 1245). These nonrecognition provisions are: Section 332 (relating to distributions in liquidation of an 80 percent or more controlled subsidiary corporation); section 351 (relating to transfers to a corporation controlled by the transferor); section 361 (relating to exchanges pursuant to certain corporate reorganizations); section 371(a) (relating to exchanges pursuant to certain receivership and bankruptcy proceedings); section 374(a) (relating to exchanges pursuant to certain railroad reorganizations); section 721 (relating to transfers to a partnership in exchange for a partnership interest); and section 731 (relating to distributions by a partnership to a partner). For example, assume that a taxpayer transfers section 1245 property to a corporation in exchange for cash of \$1,000, and stock in the corporation worth \$9,000, in a transaction qualifying under section 351. The property has a fair market value of \$10,000, a recomputed basis of \$8,000, and an adjusted basis of \$4,000. Since under section 351(b) gain in the amount of \$1,000 would be recognized to the transferor without regard to the new section 1245, subsection (b)(3) limits the gain taken into account by the transferor under section 1245(a) to \$1,000. The basis of the property in the hands of the corporation under section 362(a) (relating to basis to corporations of property acquired by issuance of stock, etc.) will be \$5,000, that is, the adjusted basis of the property in the hands of the transferor (\$4,000) increased by the gain recognized to the transferor on the transfer (\$1,000). If the corporation later sells the property for \$10,000 without having taken any deductions with respect to the property, the gain recognized to the corporation under subsection (a) will be \$3,000, the excess of recomputed basis (\$8,000) over adjusted basis (\$5,000).

Since the limitation provided in subsection (b)(3) upon the gain recognized under subsection (a) is confined to instances of "carryover basis," in the case of the liquidation of an 80 percent or more controlled subsidiary the limitation is not applicable if the basis of the property in the hands of the parent corporation is determined under section 334(b)(2). Subsection (b)(3) does not apply to a disposition of property to an organization (other than a cooperative described in sec. 521) exempt from taxation under chapter 1 of the code, but no implication is intended as to whether a transfer to such an exempt organization could or could not qualify for nonrecognition under the sections of the code set forth in subsection (b)(3).

Paragraph (4) of section 1245(b) provides that if property is disposed of and gain (determined without regard to sec. 1245) is not recognized in whole or in part under section 1031 (relating to like kind exchanges) or 1033 (relating to involuntary conversions), then the amount of gain taken into account under section 1245(a) is not to exceed the sum of the amount of gain recognized on such disposition (determined without regard to sec. 1245) plus the fair market value of property acquired which is not section 1245 property and which is not otherwise taken into account in determining the gain under section 1031 or 1033. For example, assume that a taxpayer owns section 1245 property with an adjusted basis of \$100,000 and a recomputed basis of

\$116,000. The property is destroyed by fire and the taxpayer receives \$117,000 of insurance proceeds. He uses \$105,000 of the proceeds to purchase property similar or related in service or use to the property destroyed in an acquisition qualifying under section 1033(a)(3)(A), and he uses \$9,000 of the proceeds to purchase stock in the acquisition of control of a corporation owning property similar or related in service or use to the converted property, which acquisition also qualifies under section 1033(a)(3)(A). The taxpayer properly elects under section 1033(a)(3)(A) and the regulations thereunder to limit recognition of gain to the amount by which the amount realized from the conversion exceeds the cost of the stock and other property acquired to replace the converted property. Since \$3,000 of the gain is recognized (without regard to sec. 1245) under section 1033(a)(3) (that is, \$117,000 minus \$114,000), and since the stock purchased for \$9,000 is not depreciable property and was not taken into account in determining the gain under section 1033, the amount of gain to be taken into account under section 1245(a) may not exceed \$12,000. Thus, section 1245(a) applies to \$12,000 of the \$16,000 gain.

Paragraph (5) of section 1245(b) empowers the Secretary of the Treasury or his delegate to prescribe regulations setting forth rules consistent with paragraphs (3) and (4) in the case of transactions described in section 1071 (relating to gain from sale or exchange to effectuate policies of FCC) or section 1081 (relating to nonrecognition of gain or loss on exchanges or distributions in obedience to orders of SEC).

Paragraph (6)(A) provides that, for purposes of section 1245, the basis of section 1245 property distributed by a partnership to a partner will be deemed to be determined by reference to the adjusted basis of such property to the partnership. Paragraph (6)(B) provides that, for purposes of computing the recomputed basis of such property, the amount of the adjustments added back for periods before the distribution is the amount of gain to which section 1245(a) would have applied if such property had been sold by the partnership immediately before the distribution, reduced by the amount of such gain which resulted from the application of section 751(b). Thus, since the basis of section 1245 property distributed by a partnership to a partner is deemed to be a carryover basis, any subsequent disposition of the property which requires a computation of the recomputed basis would have to take into account adjustments to basis for depreciation deductions taken before the distribution. However, such adjustments are fixed at an amount equal to the gain to which section 1245(a) would have applied if the partnership had sold the property instead of distributing it, assuming no gain upon distribution arose out of the application of section 751(b).

The application of this provision is illustrated as follows: A, B, and C are equal partners in a partnership whose assets consist of three pieces of section 1245 property, assets X, Y, and Z, each with a fair market value of \$100,000. Asset X has an adjusted basis of \$60,000 and a recomputed basis of \$85,000; asset Y has an adjusted basis of \$85,000 and a recomputed basis of \$110,000; and asset Z has an adjusted basis of \$95,000 and a recomputed basis of \$100,000. Asset Y is distributed to B in complete liquidation of his partnership interest. B's basis in his partnership interest is \$75,000, and under section 732 this basis is allocated to asset Y. If B later sells asset Y for \$103,000 at a time when the adjusted basis is still \$75,000 and

if B has not taken any depreciation deductions with respect to asset Y since the distribution, the gain to which section 1245(a) applies would be \$15,000, since the recomputed basis of the property is only \$90,000, that is, the adjusted basis of the property (\$75,000) increased by the amount of gain (\$15,000) which would have been recognized to the partnership if the asset had been sold for its fair market value at the time of distribution (\$100,000 minus \$85,000).

(c) *Adjustments to basis.*—Subsection (c) of section 1245 provides that the Secretary of the Treasury or his delegate is to prescribe such regulations as he may deem necessary to provide for adjustments to the basis of property to reflect gain to which section 1245(a) applies. This provision is necessary to prevent the same amount from being subjected to taxation more than once. For example, under existing law if a corporation distributes section 1245 property to a corporate shareholder, generally the amount of the distribution and the basis of the property in the hands of the corporate distributee is the fair market value of the property or its adjusted basis in the hands of the distributing corporation, whichever is lower. Under section 1245, however, the distribution may result in gain being recognized to the distributing corporation and unless the distributee is permitted to increase its carryover basis by the amount of the gain recognized to the distributor, the same gain may be subjected to tax when the distributee later sells the property. Therefore, under regulations prescribed by the Secretary of the Treasury or his delegate, adjustment will be made to the basis of the distributed property to reflect the gain recognized to the distributing corporation.

(d) *Application of section.*—Subsection (d) of section 1245 provides that the section is to apply notwithstanding any other provision of subtitle A of the code. Thus, section 1245 overrides any nonrecognition provision of subtitle A or any "income characterizing" provision. For example, the gain to which section 1245(a) applies might otherwise be considered as gain from the sale or exchange of a capital asset under section 1231 (relating to property used in the trade or business and involuntary conversions). Since section 1245 overrides section 1231, the gain to which section 1245(a) applies will be treated as ordinary income, and only the remaining gain, if any, from the property may be considered as gain from the sale or exchange of a capital asset if section 1231 is applicable. For example, assume that a taxpayer sells for \$130 section 1245 property with an adjusted basis of \$40 and a recomputed basis of \$100. The excess of the recomputed basis over adjusted basis, or \$60, will be treated as gain under section 1245(a). The excess of the selling price over recomputed basis, or \$30, may be considered under section 1231 as gain from the sale of a capital asset.

Subsection (d) is not intended to prevent gain not recognized under section 1245 from being considered as gain under another provision of the code. For example, assume that a taxpayer purchases section 1245 property for \$1,000 and for periods before December 31, 1961, he takes deductions of \$500 under section 168 (relating to amortization of emergency facilities). Assume that if section 168 had not applied the taxpayer would instead have taken depreciation deductions of \$300. For periods after December 31, 1961, the taxpayer takes additional deductions under section 168 of \$400. Under these facts, if the property is then sold for \$800, section 1245(a) would recognize gain to the extent of the \$400 in deductions taken in periods after

December 31, 1961, but would not recognize gain to the extent of the deductions taken in prior periods. Nothing in subsection (d) prevents \$200 of the remaining gain from being taxed under section 1238 (relating to amortization in excess of depreciation).

SECTION 13. GAIN FROM DISPOSITIONS OF CERTAIN DEPRECIABLE PROPERTY (Continued)

(b) *Change in method of depreciation.*—Subsection (b) of section 13 of the bill amends subsection (e) of section 167 of the 1954 Code (relating to depreciation). Paragraph (1) of section 167(e) is the same in substance as existing section 167(e). Under paragraph (2), which is new, the bill as passed by the House provided that any taxpayer may, within such period after the date of the enactment of the Revenue Act of 1962 and in such manner as the Secretary of the Treasury or his delegate shall by regulations prescribe, elect to change his method of depreciation in respect of section 1245 property from any declining balance or sum of the years-digits method to the straight-line method. Your committee's amendment provides that the taxpayer may make the election with respect to taxable years beginning after December 31, 1962, on or before the last day prescribed by law (including extensions thereof) for filing his return for such first taxable year.

(c) *Salvage value of personal property.*—Subsection (c)(1) of section 13 of the bill adds a new subsection (f) to section 167 of the code (relating to depreciation) and redesignates subsections (f), (g), and (h) of section 167 as subsections (g), (h), and (i), respectively.

Paragraph (1) of section 167(f) provides the general rule that, under regulations prescribed by the Secretary of the Treasury or his delegate, a taxpayer may, for purposes of computing the allowance for depreciation with respect to personal property, reduce the amount taken into account as salvage value by an amount which does not exceed 10 percent of the basis of such property (as determined under sec. 167(g) as of the time as of which such salvage value is required to be determined). For example, a taxpayer purchases depreciable personal property on January 1, 1963, for \$10,000. The estimated useful life of the property is 10 years and the estimated salvage value is \$500. The taxpayer uses the straight-line method of depreciation. Under present law the taxpayer would take depreciation deductions of \$950 in each of the 10 years of the useful life of the property. However, under section 167(f) the taxpayer may reduce salvage value, for purposes of computing the allowable depreciation deduction, by 10 percent of \$10,000. Since this amount, \$1,000, is greater than the estimated salvage value, \$500, the salvage value may be reduced to zero and the taxpayer may deduct \$1,000 in each year of the useful life of the property. In the above case, if the taxpayer had taken into account salvage value of only \$700 but the estimated salvage value had actually been \$1,500, the Internal Revenue Service could not adjust the amount used by the taxpayer since the reduction of salvage value by 8 percent of basis would be within the privilege granted by the new section 167(f).

Paragraph (2) of section 167(f) defines "personal property" as depreciable personal property (other than livestock) with a useful life of 3 years or more acquired after the date of the enactment of the Revenue Act of 1962.

(d) *Special rule for charitable contributions of section 1245 property.*—Subsection (d) of section 13 of the bill adds a new subsection (e) to section 170 of the code (relating to deductions for charitable contributions). Under the new subsection, the amount of a charitable contribution of section 1245 property will be reduced by the amount which would have been treated as gain to which section 1245(a) applied if the property had been sold at its fair market value instead of contributed to the charity. For example, a taxpayer owns depreciable property with an adjusted basis of \$10,000, a recomputed basis of \$14,000, and a fair market value of \$17,000. If the property were sold for \$17,000, gain of \$4,000 under section 1245(a) would result. Assume that the taxpayer contributes the property to a qualifying charitable organization. Under the new section 170(e) the amount of the charitable contribution would be \$13,000 (\$17,000 minus \$4,000).

(e) *Computation of taxable income for purposes of limitation on percentage depletion deduction.*—Subsection (e) of section 13 of the bill, which has no corresponding provision in the bill as passed by the House, inserts a new sentence after the second sentence in section 613(a), relating to the general rule for computing percentage depletion. The new sentence, which does not affect the computation of the gross income from the property under the first sentence of section 613(a), provides that the allowable deductions taken into account with respect to expenses of mining in computing taxable income from the property shall, for purposes of the 50-percent limitation contained in the second sentence of section 613(a), be decreased by the gain recognized under section 1245(a) which is properly allocable to the property.

(f) *Technical amendments.*—This subsection of the bill is identical to subsection (e) of the bill as passed by the House. Paragraph (1) of section 13(f) of the bill amends section 751(c) of the code to provide that, for purposes of section 751 (relating to unrealized receivables and inventory items), section 731 (relating to extent of gain or loss on distribution), section 736 (relating to payments to a retiring partner or a deceased partner's successor in interest), and section 741 (relating to recognition and character of gain or loss on sale or exchange), the term "unrealized receivables" will include section 1245 property, but only to the extent of the amount which would be treated as gain to which section 1245(a) applied if the property were sold by the partnership at its fair market value. Thus, the rules provided in section 751 with respect to unrealized receivables will also apply with respect to section 1245 property, to the extent of the potential section 1245(a) gain. For example, if a partner sold his interest in a partnership to a third party, the portion of the amount realized on such sale allocable to the partner's share of the potential section 1245(a) gain on the section 1245 property of the partnership will be recognized to the partner.

Paragraph (2) of section 13(f) of the bill amends section 301 (b) and (d) of the code (relating to the amount distributed and basis in a corporate distribution of property) by striking out "subsection (b) or (c) of section 311" and inserting in lieu thereof "subsection (b) or (c) of section 311 or under section 1245(a)."

Paragraph (3) of section 13(f) of the bill amends section 312(c)(3) (relating to adjustments to earnings and profits) by striking out

“subsection (b) or (c) of section 311” and inserting in lieu thereof “subsection (b) or (c) of section 311 or under section 1245(a).”

Paragraph (4) of section 13(f) of the bill adds a new paragraph (12) to section 341(e) (relating to collapsible corporations). New paragraph (12) provides that, for purposes of section 341(e), the determination of whether gain from the sale or exchange of property would be considered as gain from the sale or exchange of property which is neither a capital asset nor property described in section 1231(b) is to be made without regard to the application of section 1245(a).

Paragraph (5)(A) of section 13(f) of the bill adds a new sentence at the end of section 453(d)(4)(A), relating to distribution of installment obligations in complete liquidations of subsidiaries under section 332. Section 453(d)(4)(A) provides that if an installment obligation is distributed by one corporation to another corporation and if under section 332 no gain or loss is recognized to the recipient corporation with respect to the receipt of such obligation, then no gain or loss with respect to the distribution of such obligation is recognized to the distributing corporation. The new sentence provides that if section 334(b)(2) (relating to the basis of property received in certain liquidations to which sec. 332 applies) applies in respect of property received by the distributee corporation, then the rule of existing law is not to apply to the extent that under paragraph (1) of section 453(d) gain to the distributing corporation would be considered as gain to which section 1245(a) applies. For example, assume that corporation X sells section 1245 property and returns its income therefrom on the installment method under section 453. Corporation Y then buys all the outstanding stock of X and within 2 years after the purchase X adopts a plan of complete liquidation. If an installment obligation received by X upon the sale of the section 1245 property is distributed to Y in the liquidation, gain will be recognized to X under paragraph (1) of section 453(d) to the extent that the excess of the fair market value of the obligation over its basis constitutes gain to which section 1245(a) applies.

Paragraph (5)(B) of section 13(f) of the bill adds a new sentence at the end of section 453(d)(4)(B), relating to distribution of installment obligations in liquidations to which section 337 applies. Section 453(d)(4)(B) provides that if an installment obligation is distributed by a corporation in the course of a liquidation and if under section 337 no gain or loss would have been recognized to the corporation if the corporation had sold or exchanged such obligation on the day of the distribution, then no gain or loss is recognized to the corporation by reason of the distribution. The new sentence provides that the preceding rule is not to apply to the extent that under paragraph (1) of section 453(d) gain to the distributing corporation would be considered as gain to which section 1245(a) applies. For example, assume that corporation X, which makes its return on the basis of the fiscal year ending June 30, adopts a plan of complete liquidation on March 15. On June 15, X sells section 1245 property and returns its income therefrom on the installment method under section 453. On October 15, X distributes all of its property (including an installment obligation received in respect of the sale) in complete liquidation. Gain will be recognized to X under paragraph (1) of section 453(d) to the extent that the excess of the fair market value of the installment

obligation over its basis constitutes gain to which section 1245(a) applies.

(g) *Effective dates.*—Subsection (g) corresponds to subsection (f) of the bill as passed by the House which provided that the amendments made by this section of the bill shall apply to taxable years beginning after December 31, 1961, and ending after the date of the enactment of the bill. Your committee's amendment provides that the amendments made by this section shall apply to taxable years beginning after December 31, 1962, except that subsection (c) of this section shall apply to taxable years beginning after December 31, 1961, and ending after the date of enactment of the bill.

SECTION 14. FOREIGN INVESTMENT COMPANIES

(a) *Treatment of sale of stock of foreign investment companies.*—Section 14(a) of the bill adds to the code a new section 1246 (relating to gain on foreign investment company stock) and a new section 1247 (relating to election by foreign investment companies to distribute income currently). Section 1246 provides for the inclusion as ordinary income of certain gains from the sale or exchange of stock in a foreign investment company. However, section 1246 will not apply to the qualified shareholders of a registered foreign investment company which elects, under section 1247, to distribute its income currently.

This section is substantially similar to section 15 of the bill as passed by the House. However, your committee has made certain clarifying changes and has added a provision permitting a foreign investment company which elects to distribute its income currently to make a further election, if more than 50 percent of the value of its assets consists of stock or securities in foreign corporations, to allow its shareholders to treat as paid by them their proportionate shares of the foreign taxes paid by the investment company. Your committee has also added a provision allowing registered foreign investment companies the opportunity to reincorporate tax free in the United States without obtaining a ruling from the Commissioner under section 367.

SECTION 1246. GAIN ON FOREIGN INVESTMENT COMPANY STOCK

(a) *Treatment of gain as ordinary income.*—Under subsection (a)(1) of section 1246, the bill as passed by the House provided that any gain from the sale or exchange after December 31, 1962, of stock to which the subsection applies is to be treated as gain from the sale or exchange of property which is not a capital asset, but only to the extent of the taxpayer's ratable share of the earnings and profits of the company accumulated for taxable years beginning after December 31, 1962. Your committee has amended this provision to make it clear that any gain upon a distribution which, under section 302 or 331, is treated as a sale or exchange of stock shall be given the same treatment. Any additional gain or any loss on the sale or exchange of such stock will remain unaffected by these provisions. Subsection (a)(1) applies to stock in a foreign corporation which was a foreign investment company at any time during the period during which the taxpayer held such stock. Thus subsection (a)(1) applies whether or not the foreign corporation is within the definition of a foreign

investment company at the time of the sale or exchange. However, since under section 14(c) of the bill, section 1246 applies only with respect to taxable years beginning after December 31, 1962, the corporation must have been a foreign investment company while the taxpayer held the stock at some time during such a taxable year.

Subsection (a)(2) of the new section 1246 provides that the taxpayer's ratable share of the accumulated earnings and profits is to be determined under regulations prescribed by the Secretary of the Treasury or his delegate. Such determination is to include only the taxpayer's ratable share of the earnings and profits of the foreign corporation accumulated for the period during which the taxpayer held stock in such foreign corporation (excluding any portion of such period occurring in a taxable year of the corporation beginning before January 1, 1963). The bill provides that such determination will exclude the taxpayer's share of undistributed earnings and profits which previously had been taxed to him under section 951 (relating to amounts included in gross income of U.S. persons, added by sec. 12 of the bill) or under section 551 (relating to foreign personal holding company income taxed to U.S. shareholders). Under the bill as amended by your committee only such earnings and profits attributable to any amount previously included in the gross income of such taxpayer under section 951 will be excluded, and then only to the extent that such inclusion under section 951 did not result in an exclusion of any other amount from gross income under section 959. The amount of the accumulated earnings and profits for any period is determined after applying the rules of the code that distributions are treated as made out of the most recently accumulated earnings and profits.

Subsection (a)(3) of the new section 1246 requires the taxpayer to establish the amount of the accumulated earnings and profits of the foreign corporation and his ratable share of such amount. He must establish this information for the period during which he held such stock, including whatever holding period is required by other subsections of section 1246. Failure to establish this information will result in all the gain from the sale or exchange of such stock being considered as gain from the sale or exchange of property which is not a capital asset.

Subsection (a)(4) of the new section 1246 provides that section 1246 is not to apply where the holding period of the stock as of the date of the sale or exchange is 6 months or less.

(b) *Definition of foreign investment company.*—The definition of foreign investment company in subsection (b) of section 1246 has been amended by your committee. The House bill defined a foreign investment company as any foreign corporation which satisfied one of two alternative tests. Your committee bill provides that either of these two tests must be satisfied for any taxable year beginning after December 31, 1962, in order for a foreign corporation to be a foreign investment company. The first test is met if the foreign corporation is registered under the Investment Company Act of 1940, as amended (15 U.S.C. 80a-1 to 80b-2), either as a management company or as a unit investment trust. Under the Investment Company Act of 1940, an investment company organized or created under the laws of a foreign country is required to register with the Securities and Exchange Commission in order to make a public offering of its securities in the United States. The act defines an investment company, in

general, as any issuer of securities which is or holds itself out as being engaged primarily in the business of investing, reinvesting, or trading in securities. Under the second test provided by the new section 1246(b), a foreign corporation, even though it does not make a public offering of its securities and does not register under the act, is a foreign investment company if it satisfies two conditions. The first condition under the House bill was that the foreign corporation must be engaged (or holding itself out as being engaged) primarily in the business of investing, reinvesting, or trading in securities (within the meaning of sec. 3(a)(1) of the act). The bill as amended by your committee provides that section 3(a)(1) of the act would be limited by paragraphs (2) through (10) (except par. (6)(C)) and paragraphs (12) through (15) of section 3(c) of such act for purposes of determining if the first condition is satisfied. The effect of your committee's amendment is to exclude from foreign investment company treatment certain foreign corporations such as, for example, brokers, banks, and small loan companies. Under the second condition, the first condition must be satisfied at a time when more than 50 percent of the total combined voting power of all classes of stock entitled to vote or more than 50 percent of the total value of shares of all classes of stock, was held directly or indirectly (within the meaning of sec. 958(a) of the code, added by sec. 12 of the bill), by U.S. persons (as defined in sec. 7701(a)(30) of the code, added by sec. 7(h) of the bill). Under the Investment Company Act of 1940, the term "security" is defined broadly and includes among others, stock, treasury stock, bond, debenture, any evidence of indebtedness, certificate of interest or participation in any profit-sharing agreement, collateral-trust certificate, certificate of deposit for a security, or a fractional undivided interest in oil, gas, or other mineral rights.

(c) *Stock having transferred or substituted basis.*—Subsection (c) of new section 1246 provides that stock in a foreign corporation, the basis of which (in the hands of the taxpayer selling or exchanging such stock) is determined by reference to the basis (in such taxpayer's hands or any other person's hands) of stock in a foreign investment company, will to the extent provided in regulations prescribed by the Secretary of the Treasury or his delegate be treated as stock of a foreign investment company. The stock which is so treated will be considered under section 1223 (relating to holding period of property) to be held by the taxpayer throughout the period during which the foreign investment company stock was held in addition to the period during which the stock in the foreign corporation is held. Transactions to which subsection (c) applies include the following:

A person owning stock in a foreign investment company transfers such stock to foreign corporation F which he controls in exchange for stock of corporation F in a transaction to which section 351 applies. Clearance under section 367 is obtained. The stock of corporation F received in exchange for the foreign investment company stock will be considered stock of a foreign investment company. If the stock of corporation F is later transferred by gift, the donee will also treat such stock as stock of the foreign investment company and the holding period of the donee will include the period during which the donor held the stock in the foreign investment company and corporation F.

(d) *Rules relating to entities holding foreign investment stock.*—Subsection (d) of the new section 1246 provides that to the extent

provided in regulations prescribed by the Secretary of the Treasury or his delegate, trust certificates of a trust to which section 677 (relating to income for benefit of grantor) applies, and stock in a domestic corporation, will be treated as stock of a foreign investment company to the extent that such trust or corporation has an investment in stock in a foreign investment company. As a result of this provision the taxpayer is deemed to be holding stock of the foreign investment company. The trust certificates or stock are to be treated under section 1223 as held by the taxpayer throughout the holding period for which the trust or domestic corporation held stock in a foreign investment company, but limited to the period during which the taxpayer held such trust certificates or stock in the domestic corporation. Such stock is deemed to be held by him in the same proportion that the actual investment in stock in a foreign investment company by the trust or domestic corporation bears to the total assets of such trust or domestic corporation. For example, if a domestic corporation has an investment of \$20,000 in stock of a foreign investment company and total assets of \$100,000, the proportion of the domestic corporation's investment is 20 percent. Therefore, 20 percent of each share of stock in such corporation will be deemed to be foreign investment stock and 20 percent of the gain, if any, resulting from the sale or exchange thereof, will be subjected to section 1246 treatment.

(e) *Rules relating to stock acquired from a decedent.*—Paragraph (1) of subsection (e) sets forth the manner for computing the basis of stock in a foreign investment company which is acquired from a decedent dying after December 31, 1962, and treats the holding period by the heir or successor in the manner provided for in subsection (c). Under paragraph (1) of subsection (e) the stock's basis determined under section 1014 will be reduced by the decedent's ratable share of the company's earnings and profits accumulated in taxable years beginning after December 31, 1962. For example, if the stock had an adjusted basis of \$100, a fair market value of \$150 on the date of the decedent's death, and \$30 was the decedent's ratable share of the accumulated earnings and profits during the period he held such stock after December 31, 1962, the person acquiring the stock from the decedent would have a basis of \$120 (\$150—\$30). In no case is the basis determined under section 1014 to be reduced below the adjusted basis of the stock in the hands of the decedent immediately before his death, regardless of the decedent's ratable share of such earnings. Thus, in the above example, the basis could not be reduced below \$100.

The stock so acquired from a decedent shall be treated as if it were held throughout the holding period of the decedent in addition to the holding period of the person acquiring the stock. Thus, in effect, the holding period of the decedent is tacked onto that of the person acquiring the stock. If, in the example illustrated in the preceding paragraph, the stock were sold immediately after acquisition at its fair market value of \$150, the gain of \$30 (\$150—\$120) would be treated as gain from the sale of property which is not a capital asset. If, after acquisition the stock further increased in value, upon a sale or exchange, \$30 plus the portion of the gain which is equal to the taxpayer's ratable share of the accumulated earnings and profits of the corporation for the period during which he held such stock would be treated in the same manner.

In the event the decedent's executor decides to determine the gross estate under section 2032 (relating to alternate valuation), for purposes of section 1246(e), the date the stock is so valued will be considered the date of the decedent's death. Therefore, the basis determined at such later date will be reduced by the decedent's ratable share of the earnings and profits accumulated during the period preceding the date of his death and the earnings and profits accumulated during the period between such date and the date of alternate valuation.

Paragraph (2) of section 1246(e) provides that if foreign investment company stock acquired from a decedent is sold or exchanged at a gain which gain is subject to ordinary income treatment under subsection (a) of section 1246, the taxpayer, under regulations prescribed by the Secretary of the Treasury or his delegate, is to be allowed a deduction from gross income, for the taxable year of the sale or exchange, equal to that portion of the decedent's estate tax deemed paid which is attributable to the excess of (A) the value at which such stock was taken into account for purposes of determining the value of the decedent's gross estate, over (B) the value at which it would have been so taken into account if such value had been reduced by the amount representing the reduction in basis described in paragraph (1). The value determined in (B) is actually the taxpayer's basis of the stock as determined under section 1246(e)(1). The provision of paragraph (1) may be illustrated by the following example:

Example

The gross estate of a decedent dying in 1963 was \$125,000, which included foreign investment company stock valued at \$5,000. Assuming deductions of \$10,000 and an exemption of \$60,000, the taxable estate amounted to \$55,000. The estate tax paid on this amount is \$8,250. Assuming that the decedent's share of earnings and profits accumulated after December 31, 1962, was \$500 the heir's basis for such stock determined under section 1246(e)(1) would be \$4,500. If the heir sold such stock in 1963, he is allowed to deduct the following amount from his 1963 gross income:

Estate tax actually paid (on taxable estate of \$55,000).....	\$8, 250
Less: Estate tax computed by reducing the gross estate by \$500 (tax on taxable estate of \$54,500).....	8, 125

Amount deducted from the heir's gross income..... 125

If in 1963, the heir had sold only one-half of the stock, then only \$62.50 (one-half of \$125) could have been deducted from his gross income.

(f) *Information with respect to certain foreign investment companies.*— Subsection (f) of section 1246 requires certain U.S. shareholders of a foreign investment company to furnish with respect to such company such information as the Secretary of the Treasury or his delegate shall by regulations prescribe. The requirement is applicable only to those U.S. persons who on the last day of the taxable year of a foreign investment company beginning after December 31, 1962, own 5 per cent or more in value of the stock of such company.

(g) *Nonapplication of section 367 in certain cases.*—Your committee has redesignated subsection (g) of section 1246 in the bill as passed by the House as subsection (h) and has added a new subsection (g) which has no corresponding provision in the bill as passed by the House. The new subsection (g) provides that if a registered foreign investment company described in subsection (b)(1) has made an effective election

to distribute income currently under section 1247 with respect to taxable years beginning after December 31, 1962, then section 367 will not apply in respect of such foreign investment company if the company is a party to a reorganization (within the meaning of sec. 368) in which all of its properties are acquired before January 1, 1964, by a domestic corporation which is a regulated investment company under section 851 for its first taxable year ending after the reorganization.

(h) *Cross-reference.*—Subsection (h) of section 1246, which corresponds to subsection (g) in the bill as passed by the House, is a cross-reference to section 312(l) of the code (relating to effect on earnings and profits of foreign investment companies) which is added by section 14(b)(1) of the bill.

SECTION 1247. ELECTION BY FOREIGN INVESTMENT COMPANIES TO
DISTRIBUTE INCOME CURRENTLY

Section 1247, which is added to the code by section 14(a) of the bill, provides that section 1246 will not apply to the shareholders of a registered foreign investment company if such company makes the election provided for by section 1247, and if the shareholders include in their income their pro rata share of the excess of the net long-term capital gain over the net short-term capital loss of the company for each taxable year.

(a) *Election by foreign investment company.*—Section 1247(a)(1) provides that if a foreign investment company of the type defined in section 1246(b)(1) (relating to registered foreign investment companies) makes the election provided by section 1247, section 1246 will not apply with respect to its qualified shareholders during any taxable year of the company to which the election is effective. Such election must be made on or before December 31, 1962, in the manner provided in regulations prescribed by the Secretary of the Treasury or his delegate. The election commits the company to fulfill the requirements provided in subparagraphs (A), (B), and (C) of subsection (a)(1) for each taxable year beginning after December 31, 1962.

Under subparagraph (A), the company elects to distribute to its shareholders during each taxable year at least 90 percent of its taxable income for such year. For this purpose, taxable income is the amount determined as if such company were a domestic corporation but with the adjustments provided in subparagraph (A) of paragraph (2).

Under subparagraph (B), the bill provided that the company elects to designate, in a written notice mailed to its shareholders at any time before 30 days after the close of its taxable year, the pro rata amount of the excess of the net long-term capital gain over the net short-term capital loss and the portion thereof which is being distributed. The bill as amended by your committee provides that the written notice shall be mailed at any time before 45 days after the close of such taxable year. Such determinations are to be made as if such company were a domestic corporation.

Under subparagraph (C), the company elects to provide such information as the Secretary of the Treasury or his delegate deems necessary to carry out the purposes of section 1247.

Paragraph (2)(A) of subsection (a) provides special rules for computing taxable income under paragraph (1)(A).

Subparagraph (A) states that such taxable income will be determined without regard to—

- (i) the excess of the net long-term capital gain over net short-term capital loss for the taxable year,
- (ii) the net operating loss deduction under section 172, and
- (iii) the deductions provided in part VIII of subchapter B (relating to special deductions for corporations), other than the deduction provided in section 248 (relating to organizational expenses).

Paragraph (2)(B) provides that in determining the amount of the distribution made under paragraph (1)(A), a distribution made after the close of the taxable year but on or before the 15th day of the third month of the next taxable year will be treated by the company (but not by its shareholders) as distributed during the earlier year to the extent elected by the company on or before the 15th day of such third month. Such election is to be made in accordance with regulations prescribed by the Secretary of the Treasury or his delegate.

Subparagraph (C) of paragraph (2) provides that for purposes of making the computations under paragraph (1)(B), any capital loss under section 1212 incurred prior to the first effective year of the election will not be carried forward to the period for which the election is effective.

(b) *Years to which election applies.*—Subsection (b) of the new section 1247 provides that the election is to terminate starting with the first day of the first taxable year in which—

- (1) the company fails (unless it is shown that such failure is due to reasonable cause and not due to willful neglect) at any time to comply with any of the requirements set forth in subsection (a)(1),
- (2) the company is a foreign personal holding company, or
- (3) the company is not a registered foreign investment company as described in section 1246(b)(1).

It is recognized that some registered foreign investment companies may experience difficulties in ascertaining the extent to which distributions which they receive on investments in stocks of other foreign corporations represent income to them under the standards of the Internal Revenue Code; for example, this may be true with respect to distributions from foreign mining companies. The bill provides in section 1247(b)(1) that the company will not be disqualified under section 1247 if its failure to distribute 90 percent of its income is due to reasonable cause and not due to willful neglect. If in determining its income, the company relies in good faith upon estimates and opinions of independent certified public accountants or other experts which are also used for purposes of its financial statements filed with the Securities and Exchange Commission under the Investment Company Act of 1940, such reliance would constitute reasonable cause for this purpose.

(c) *Qualified shareholders.*—Paragraph (1) of subsection (c) of section 1247 defines a “qualified shareholder” to mean a shareholder who is a U.S. person (as defined in sec. 7701(a)(30), added by sec. 7(h) of the bill) other than a shareholder described in paragraph (2).

Paragraph (2) provides that a U.S. person is not to be treated as a qualified shareholder for his taxable year if for such taxable year (or for any prior taxable year) he fails to include (in computing his long-term capital gains in his return for such taxable year) the amount designated by the company as his pro rata share of the undistributed

portion of the excess of the net long-term capital gain over the net short-term capital loss of the company for the company's taxable year ending within or with the shareholder's taxable year. Once a taxpayer fails to comply with the provisions of this paragraph in determining his status as a qualified shareholder, he loses the benefits of a qualified shareholder for the duration of the election and section 1246 will apply when he sells or exchanges the stock of the foreign investment company at a gain. However, if a taxpayer can show that the failure to include his share of the undistributed capital gains in his return was due to reasonable cause and not due to willful neglect, he will continue to be treated as a qualified shareholder.

(d) *Treatment of distributed and undistributed capital gains by qualified shareholders.*—Your committee has redesignated subsection (d) (relating to adjustments) of the new section 1247 as subsection (e) and has substituted a new subsection (d) which has no corresponding provision in the bill as passed by the House. The new subsection (d) provides rules for the treatment at the shareholder level of the distributed and undistributed portions of certain capital gains of a foreign investment company. Such capital gains are the excess of the net long-term capital gain over the net short-term capital loss for each taxable year of a foreign investment company with respect to which an election pursuant to subsection (a) is in effect. These rules for the treatment of such gains apply only to shareholders of such company who are qualified shareholders within the meaning of subsection (c).

Paragraph (1) of subsection (d) provides that every qualified shareholder of such company shall include his pro rata share of the distributed portion of such capital gains of such company in computing his long-term capital gains for his taxable year in which such distributed portion is received. Rules of existing law will continue to apply with respect to the receipt of such amounts by shareholders who are not qualified shareholders within the meaning of subsection (c). Accordingly, an unqualified shareholder would treat his pro rata share of the distributed portion of such capital gains as dividend income taxable at ordinary income rates.

Paragraph (2) of subsection (d) provides that every qualified shareholder of such company, in computing his long-term capital gains for his taxable year in which or with which the taxable year of the company ends, shall include his pro rata share of the undistributed portion of such capital gains for the taxable year of the company.

(e) *Adjustments.*—Subsection (e) of the new section 1247, which corresponds to subsection (d) in the bill as passed by the House, provides that proper adjustment, under regulations prescribed by the Secretary of the Treasury or his delegate, shall be made to reflect the inclusion in gross income of a qualified shareholder of his pro rata share of the undistributed portion of such capital gains under subsection (d)(2).

Under paragraph (1), the bill as passed by the House provided that such adjustment shall be made to the earnings and profits of the electing foreign investment company. The bill as reported provides in addition that such adjustment shall be made to a qualified shareholder's ratable share of such earnings and profits.

Paragraph (2), provides that adjustment shall also be made to the adjusted basis of stock held by qualified shareholders of the company.

(f) *Election by foreign investment company with respect to foreign tax credit.*—Subsection (f) of the new section 1247, for which there is no corresponding provision in the bill as passed by the House, provides that certain foreign investment companies may elect to be treated as conduits for the purposes of income, war profits, and excess profits taxes described in section 901(b)(1) which such companies pay to foreign countries and possessions of the United States. If such an election is made, the qualified shareholders may apply their proportionate shares of such foreign taxes either as a credit under section 901 or as a deduction under section 164(a) to the same extent as if they had paid such foreign taxes. The election may be made by a foreign investment company for any taxable year with respect to which an election pursuant to subsection (a) is in effect, if more than 50 percent of the value of the company's total assets at the close of such taxable year consists of stock or securities in foreign corporations. The conduit treatment provided in this subsection is not available with respect to taxes deemed to have been paid under section 902 (relating to the credit allowed to corporate shareholders of a foreign corporation for taxes paid by such foreign corporation).

If a foreign investment company for a taxable year elects the conduit treatment for foreign taxes under subsection (f), the determination of whether the election under subsection (a) is in effect for such taxable year is made in accordance with the rules provided in paragraph (1) of subsection (f). Under these rules, taxable income of the foreign investment company is computed without any deductions for income, war profits, or excess profits taxes (which are described in sec. 901(b)(1)) paid to foreign countries or possessions of the United States and the amount of such taxes are treated as distributed to shareholders for purposes of satisfying the requirement in subsection (a)(1)(A) that at least 90 percent of taxable income be distributed.

Under paragraph (2) of subsection (f), each qualified shareholder of the foreign investment company making the election under this subsection is required to include in his gross income and treat as paid by him his proportionate share of foreign taxes described in subsection (f)(1)(A), which were paid by the foreign investment company. For purposes of applying the foreign tax credit, the qualified shareholder shall treat his proportionate share of such taxes as having been paid to the country in which the foreign investment company is incorporated.

(g) *Notice to shareholders.*—Subsection (g) of section 1247, for which there is no corresponding provision in the bill as passed by the House, provides that the amounts to be treated by a qualified shareholder, for purposes of subsection (f)(2), as his proportionate share of taxes described in subsection (f)(1)(A) paid by the foreign investment company shall not exceed the amounts designated by the foreign investment company in a written notice mailed to its shareholders not later than 45 days after the close of its taxable year.

(h) *Manner of making election and notifying shareholders.*—This subsection, which has no corresponding provision in the bill as passed by the House, provides that the election by the foreign investment company to make the foreign tax credit available to its shareholders under subsection (f) and the notice to its shareholders of the designation of certain amounts under subsection (g) shall be made in the manner provided in regulations to be prescribed by the Secretary of the Treasury or his delegate.

(i) *Loss on sale or exchange of certain stock held less than 6 months.*—Subsection (i) which is identical to subsection (e) of section 1247 of the bill as passed by the House, provides that if a share of stock is held by a qualified shareholder for less than 6 months and if he treats any amount designated under section 1247(a)(1)(B) as long-term capital gain with respect to such shares, then any loss on the sale or exchange of such share (to the extent of the amount so treated as long-term capital gain) shall be treated as loss from the sale or exchange of a capital asset held for more than 6 months. For example, on December 20, 1963, A purchases a share of stock in corporation F, an electing foreign investment company, for \$50. Corporation F (which is on a calendar-year basis) designates A's share of its long-term capital gains for the year 1963 as being \$5. No distribution with respect to capital gains is made. A, therefore, includes \$5 in computing his long-term capital gains in his return for 1963. On January 10, 1964, A sells such share for \$49. Since A has a basis of \$55 (the \$50 original cost plus the \$5 capital gain included in income but not distributed) the sale results in a loss of \$6. Subsection (e) treats \$5 of this loss as a long-term capital loss.

SECTION 14. FOREIGN INVESTMENT COMPANIES (Continued)

(b) *Conforming amendments.*—Paragraph (1) of section 14(b) of the bill amends section 312 of the 1954 Code (relating to effect on earnings and profits) by adding after subsection (k) thereof a new subsection (l).

Paragraph (1) of subsection (l) provides that upon the sale or exchange of stock in a foreign investment company by a shareholder who is a U.S. person, if such foreign investment company is a member of an affiliated group (as defined in par. (2)), then the accumulated earnings and profits of all member companies are to be allocated under regulations prescribed by the Secretary of the Treasury or his delegate, in such a manner as to carry out the purposes of section 1246.

Paragraph (2) of subsection (l) defines the term "affiliated group" for purposes of subsection (l)(1) to have the same meaning as such term has in section 1504(a) except that (A) "more than 50 percent" is substituted for "80 percent or more" wherever appearing in section 1504(a), and (B) all corporations are treated as includible corporations without regard to section 1504(b).

Paragraph (3) of new subsection (l) provides a rule governing the reduction in the earnings and profits of a foreign investment company as a result of amounts distributed by a foreign investment company in a partial liquidation or in redemptions to which section 302(a) or 303 applies. The portion of the distribution which is chargeable to earnings and profits shall be an amount which is not in excess of the redeemed stock's ratable share of the earnings and profits of the company accumulated after February 28, 1913. The effect of this provision is to allocate to each share of stock (whether or not redeemed) an equal amount of the company's accumulated earnings and profits at the time of the redemption. Paragraph (3) of subsection (l) applies only to such distributions made after December 31, 1962. The application of subsection (l)(3) of section 312 may be illustrated by the following example: Corporation F, a foreign investment company, has

accumulated earnings and profits of \$10,000 on December 31, 1963, on which date corporation F redeems shareholder A's stock for cash in the amount of \$4,000. A is a 20-percent shareholder. Under the amendment the earnings and profits of the corporation are reduced by only \$2,000 (20 percent of \$10,000).

Paragraph (2) of section 14(b) of the bill amends section 751(d)(2) of the code (relating to inventory items of a partnership which have appreciated substantially in value) by adding new subparagraphs (C) and (D) which provide treatment for the sale or exchange of an interest in a partnership which holds stock in a foreign investment company. The amendment treats foreign investment company stock as an inventory item of the partnership under subsection (d)(2) of section 751. If an interest in a partnership, holding stock in a foreign investment company, is sold or exchanged, and if section 1246(a) would apply to the gain on the sale or exchange of such stock were such stock sold or exchanged by the partnership, the amount received for such interest which is attributable to the inventory items under section 751(d)(2) (including foreign investment company stock) will be taxed at ordinary income rates, provided under section 751(d)(1) the substantial appreciation tests for inventory items of the partnership are satisfied.

Paragraph (3) of section 14(b) of the bill amends section 1223 of the code (relating to holding period of property) by redesignating paragraph (10) as paragraph (11) and adding a new paragraph (10). Paragraph (10) requires a taxpayer in determining the period for which he held certain trust certificates to which section 1246(d) applies (relating to entities holding foreign investment company stock), or the period for which he held stock to which such section applies, to include the period for which the trust or corporation held the stock of foreign investment companies.

(c) *Effective date.*—Subsection (c) of section 14 of the bill provides that the amendments made by section 14 are to apply with respect to taxable years beginning after December 31, 1962.

SECTION 15. GAIN FROM CERTAIN SALES OR EXCHANGES OF STOCK IN CERTAIN FOREIGN CORPORATIONS

(a) *Treatment of gain from the redemption, cancellation, or sale of stock in certain foreign corporations.*—Subsection (a) of section 15 of the bill, corresponding to section 16 of the bill as passed by the House, amends part IV of subchapter P of chapter 1 (relating to special rules for determining capital gains and losses) by adding after section 1247 (as added by sec. 14 of the bill) a new section 1248.

SECTION 1248. GAIN FROM CERTAIN SALES OR EXCHANGES OF STOCK IN CERTAIN FOREIGN CORPORATIONS

Section 1248 provides that gain recognized on the sale or exchange of stock by a U.S. person owning 10 percent or more of the voting stock of a foreign corporation shall be included in gross income of such person as a dividend to the extent of the earnings and profits of the foreign corporation attributable to the period the stock sold or exchanged was held by such person while the foreign corporation was a controlled foreign corporation. Section 1248 also provides a limita-

tion on the amount of tax payable by a U.S. person who is an individual, as defined in section 7701(a)(30)(A) (added by sec. 7 of the bill), and special rules for determining earnings and profits of a foreign corporation for purposes of this section.

(a) *General rule.*—Subsection (a) of section 1248 provides two prerequisites to the application of the section. First, a U.S. person, as defined in section 7701(a)(30), must sell or exchange stock in a foreign corporation. For this purpose, distributions under section 302, relating to distributions in redemption of stock, or section 331, relating to complete or partial liquidations of a corporation, are treated as exchanges. Second, a U.S. person must have owned within the meaning of section 958 (added by sec. 12 of the bill), 10 percent or more of the total combined voting power of all class of stock entitled to vote of the foreign corporation at any time during the 5-year period ending on the date of sale or exchange, and the foreign corporation must have been a controlled foreign corporation, as defined in section 957 (added by sec. 12 of the bill), on such date. If these conditions are satisfied, section 1248(a) requires that if a gain is recognized by the U.S. person on the sale or exchange of the stock of the foreign corporation, such amount of the gain as does not exceed the U.S. person's proportionate share of the earnings and profits of the foreign corporation attributable (under regulations prescribed by the Secretary of the Treasury or his delegate) to the stock sold or exchanged which were (1) accumulated in taxable years of the foreign corporation beginning after December 31, 1962, (2) during the period or periods the stock sold or exchanged was held by such person, and (3) while such foreign corporation was a controlled foreign corporation, shall be included in gross income of the U.S. person as a dividend. Section 1248 will not apply to exchanges in which gain is not recognized, for example, exchanges described in sections 332, 351, 354, 355, or 361 of the code, if before such exchange, as prescribed in section 367, it has been established to the satisfaction of the Secretary of the Treasury or his delegate that such exchange is not in pursuance of a plan having as one of its principal purposes the avoidance of Federal income taxes.

To the extent gain is included in gross income as a dividend, the pertinent rules of subpart A of part III of subchapter N, relating to foreign tax credits, apply. Thus, foreign-tax credits for amounts allowed under section 901(b) with respect to taxes paid, and section 902 with respect to taxes deemed to be paid, are allowable if the U.S. person chooses to have the benefits of such sections. That part of the gain in excess of the amount included in gross income as a dividend under section 1248 is treated as provided by the code without regard to new section 1248 and there is no foreign tax credit with respect to taxes paid by the foreign corporation as to the portion of the gain that is not a dividend.

The bill as passed by the House would have treated as a dividend gain attributable to earnings and profits of foreign corporations accumulated after February 28, 1913, and in taxable years of such corporations ending on or before December 31, 1962, or gain attributable to earnings and profits of foreign corporations for periods during which a U.S. person was a shareholder in a foreign corporation at a time

when the foreign corporation was not a controlled foreign corporation. The bill as passed by the House contained no provision for the allowance of a foreign tax credit in the case of the sale or exchange, other than in redemption or liquidation, of stock in a controlled foreign corporation.

The application of this subsection may be illustrated by the following examples:

Example 1.—A, an individual U.S. person, is, and always has been, the sole shareholder of foreign corporation X. X was organized on January 1, 1961, and had earnings and profits of \$100 in the taxable year ending December 31, 1961, \$200 in taxable year 1962, and \$50 in taxable year 1963. A sold all his stock, a capital asset, in corporation X on December 31, 1963, and realized a gain of \$400. Fifty dollars of the total gain (A's share of the earnings and profits of X for taxable year 1963) is includible in gross income of A as a dividend and \$350 is includible in gross income of A as gain from the sale or exchange of a capital asset held for more than 6 months.

Example 2.—Assume the same facts as in example 1, except that A sold one-half of his shares in corporation X on December 31, 1963, rather than his entire stock interest, and realized a gain of \$150. Twenty-five dollars of the total gain is includible in gross income of A as a dividend and the remaining \$125 of gain is includible in gross income of A as gain from the sale or exchange of a capital asset held for more than 6 months.

Example 3.—U.S. person A, a domestic corporation, on January 1, 1963, owned 35 shares of stock in corporation X, a foreign corporation which was not a less developed country corporation. The remaining shares of X stock were held by U.S. individual B, 10 shares, and foreign corporation M, 55 shares. On January 1, 1964, A purchased 10 shares of corporation X stock from M and on January 1, 1965, A purchased 10 shares of corporation X stock from B. Corporation X had earnings and profits of \$100 in each of the years 1963, 1964, and 1965 after payment of foreign income tax of \$25 in each such year (20-percent rate). A sold all its stock in corporation X, 55 shares, on December 31, 1965, and realized a total gain of \$500. Of the total gain, \$100 (45 percent of the earnings and profits of 1964 and 55 percent of the earnings and profits of 1965 (corporation X was not a controlled foreign corporation in 1963)) is includible in gross income of A as a dividend and \$400 is includible in gross income of A as gain from the sale or exchange of a capital asset held for more than 6 months. A, being a domestic corporation and owning at least 10 percent of the voting stock of foreign corporation X, could choose the foreign tax credit benefits of the code. Therefore, since foreign corporation X had paid a foreign income tax of 25 percent on the amount includible in income as a dividend, the inclusion of an amount under section 1248 would result in a net additional Federal income tax of 32 percent (assuming an effective U.S. tax rate of 52 percent) of the grossed-up amount included in gross income, a tax result equivalent to that which would have followed a distribution of earnings and profits to A by the controlled foreign corporation. The

amount of tax payable under this chapter would be computed as follows:

Amount includible in gross income as a dividend	\$100. 00
Amount included in gross income under sec. 78:	
1965: $\$25 \times 55/100$	\$13. 75
1964: $\$25 \times 45/100$	11. 25
Total foreign tax paid with respect to \$100	25. 00
Total amount included in gross income	125. 00
Tentative U.S. tax (at 52 percent rate)	65. 00
Foreign tax credit (sec. 902)	25. 00
Net U.S. tax	40. 00

Example 4.—Assume the same facts as in example 3 except that A sold 30 shares of corporation X stock, rather than 55 shares, upon which A realized a total gain of \$300. The shares sold represented 10 shares purchased from B on January 1, 1965, 10 shares purchased from corporation M on January 1, 1964, and 10 shares owned by A on January 1, 1963. Of the total gain, \$50 (20 percent of the earnings and profits of 1964 (\$20) and 30 percent of the earnings and profits of 1965 (\$30)) is includible in gross income of A as a dividend, and \$250 is includible as gain from the sale or exchange of a capital asset held for more than 6 months.

(b) *Limitation of tax applicable to individuals.*—Subsection (b) of section 1248, for which there is no corresponding provision in the bill as passed by the House, provides for a limitation of Federal income tax resulting from the inclusion in gross income of an individual U.S. person of an amount as a dividend under the provisions of section 1248(a).

Paragraph (1) of section 1248(b) provides that the tax attributable to an amount included in the gross income of a U.S. person in accordance with the provisions of section 1248(a) shall not be greater than an amount described in paragraph (2) or paragraph (3), whichever is lesser.

Paragraph (2) of section 1248(b) applies if the stock sold or exchanged, including distributions treated as exchanges under sections 302 or 331, is a capital asset, within the meaning of section 1221, and such stock has been held by the U.S. person for more than 6 months. If these conditions are met, the limitations of tax applicable to an amount includible in gross income of an individual U.S. person under section 1248(a) is an amount equal to the sum of the amounts determined under subparagraphs (A) and (B) of section 1248(b)(2), if such amount is less than the amount determined under paragraph (3) of section 1248(b).

Subparagraph (A) of section 1248(b)(2) provides for an amount equal to a pro rata share of the excess of an amount determined under the provisions of clause (i) over an amount determined under the provisions of clause (ii).

Clause (i) of section 1248(b)(2)(A) provides for an amount equal to the taxes that would have been paid by the foreign corporation had it been taxed under chapter 1 as a domestic corporation for the period or periods the stock sold or exchanged was held by the

U.S. person while the foreign corporation was a controlled foreign corporation in taxable years beginning after December 31, 1962. In determining the amount of Federal income tax the foreign corporation would have paid as a domestic corporation, the nature and amount of income of the foreign corporation will be determined under the provisions of the code as it relates to domestic corporations. Thus, gain on the sale of a capital asset held for more than 6 months is considered long-term capital gain, so much of taxable income as does not exceed \$25,000 is exempt from surtax, etc. However, no deduction or credit will be allowable from gross income for income, war profits, or excess profits taxes paid by the foreign corporation. Income, deductions, credits, or allowances will be taken into account only for the period or periods the stock sold or exchanged was held by the U.S. person in taxable years beginning after December 31, 1962, while the foreign corporation was a controlled foreign corporation, adjusted for distributions and amounts previously included in gross income of a U.S. shareholder under section 951.

Clause (ii) of section 1248(b)(2)(A) provides for an amount equal to the income, war profits, or excess profits taxes paid by the foreign corporation with respect to income included in gross income under section 1248(a).

Subparagraph (B) of section 1248(b)(2) provides for an amount equal to a tax that would result by including in gross income of the individual U.S. person, as gain from the sale or exchange of a capital asset, an amount equal to the amount included in gross income in accordance with the provisions of section 1248(a), reduced by the amount determined under subparagraph (A) of section 1248(b)(2).

The application of section 1248(b)(2) may be illustrated by the following example involving individual U.S. person A who owns 100 percent of the stock of foreign corporation X. A purchased the stock of corporation X on January 1, 1963, and sold the stock on December 31, 1963. Corporation X files its income tax returns on a calendar year basis. For taxable year 1963, the entire income of corporation X was derived from the purchase and sale of property held for sale to customers in the ordinary course of trade or business. The profit or loss statement of corporation X is summarized as follows:

1963	
Gross receipts.....	\$300, 000
Cost of goods sold.....	125, 000
Gross income.....	175, 000
Rent, salaries, utilities, etc.....	75, 000
Taxable income.....	100, 000
Foreign income tax (10 percent).....	10, 000
Earnings and profits.....	90, 000

A realized \$120,000 gain on the sale of the stock and was required, under the provisions of section 1248(a), to include \$90,000 in gross income as a dividend and \$30,000 as long-term capital gain. Without the application of section 1248(b), the tax attributable to the inclusion of \$90,000 in gross income of A as a dividend was \$63,000, an effective

tax rate of 70 percent. The limitation of section 1248(b)(2) would be computed as follows:

(i) An amount determined under section 1248(b)(2)(A):	
(a) An amount determined under clause (i) of section 1248(b)(2)(A): Taxable income of corporation X under chapter 1 of the code, \$100,000, upon which corporation X would have paid Federal income tax of	\$46, 500
(b) An amount determined under clause (ii) of section 1248(b)(2)(A): Income tax paid by corporation X	10, 000
(c) The amount determined under subparagraph (A) is the excess of the amount determined under clause (i) over the amount determined under clause (ii) ((a) minus (b))	\$36, 500
(ii) An amount determined under section 1248(b)(2)(B):	
(a) The amount included in gross income under section 1248(a)	\$90, 000
(b) The amount determined under subparagraph (A) of section 1248(b)(2)	36, 500
(c) The amount treated as long-term capital gain for purposes of subparagraph (B) ((a) minus (b)) ..	53, 500
(d) Tax that would have resulted from including \$53,500 in gross income as a long-term capital gain (25 percent of \$53,500)	13, 375
(iii) The limitation of tax attributable to the inclusion of \$90,000 in gross income as a dividend under section 1248(b)(2) is (item (i) plus (ii))	49, 875

Paragraph (3) of section 1248(b) provides for an alternative limitation of tax applicable to an amount includible in gross income of an individual U.S. person under section 1248(a) equal to the aggregate additional Federal income tax which would have been paid by the individual U.S. person had he included in gross income as a dividend his pro rata share of the undistributed earnings and profits of the foreign corporation for the period or periods the stock sold or exchanged was held by such person while such foreign corporation was a controlled foreign corporation in taxable years of the foreign corporation beginning after December 31, 1962.

(c) *Special rules.*—Subsection (c) of section 1248 provides that certain amounts included in earnings and profits of a foreign corporation, determined in accordance with rules substantially similar to those applicable to domestic corporations, will be excluded from earnings and profits of the foreign corporation for purposes of section 1248.

Paragraph (1) of section 1248(c) correlates section 1248 with section 951 (added by sec. 12 of the bill) by reducing the amount of gain considered a dividend under subsection (a) by the U.S. person's proportionate share of earnings and profits of the foreign corporation, attributable to the stock sold or exchanged, which had been previously included in the gross income of the U.S. person by the application of subpart F of part III of subchapter N. However, such amounts previously included in the gross income of the U.S. person under section 951 are reduced by amounts, attributable to the stock sold or exchanged, subsequently distributed by the foreign corporation and excluded from gross income of the U.S. person under section 959.

The application of this paragraph may be illustrated by the following example involving U.S. corporation A which owns 100 percent of the stock of foreign corporation X. A purchased the stock on January 1, 1964, for \$100 and sold the stock on January 1, 1966, for \$115. For the year 1964, corporation X had earnings and profits, all of which was subpart F income, of \$10, which was included in the gross income of A under section 951. Corporation X had no earnings and profits for the year 1965, but made a \$5 distribution out of 1964 earnings and profits which was excludable from gross income of A under section 959. For the year 1966, A is required to include \$10 in gross income as a long-term capital gain, which amount is computed as follows:

(i) Amount of gain:	
(a) Amount realized.....	\$115
(b) Adjusted basis:	
Cost.....	\$100
Increase by amount included in gross income under section 951 (sec. 961(a)).....	10
	110
Reduced by amount excluded from gross income under section 959 (sec. 961(b)).....	5
	Adjusted basis.....
	105
(c) Amount of gain ((a) minus (b)).....	10
(ii) Amount of gain includible in gross income of A as a dividend (sec. 1248(a)):	
(a) A's proportionate share of earnings and profits accumulated during the period the stock sold was held by A (\$10 of earnings and profits for 1964, reduced by \$5 distributed in 1965).....	\$5
(b) A's proportionate share of earnings and profits previously included in the gross income of A under section 951 (\$10) reduced by distributions excluded from the gross income of A under sec. 959, (\$5).....	5
(c) Amount includible in gross income as a dividend ((a) minus (b)).....	0
(iii) Amount of gain from the sale of a capital asset held for more than 6 months (item (i) minus item (ii)).....	10

Paragraph (2) of section 1248(c), for which there is no corresponding provision in the bill as passed by the House, provides that if a foreign corporation realizes gain from the sale or exchange of property in pursuance of a plan of complete liquidation in a taxable year beginning after December 31, 1962, and if section 337(a) would apply if such corporation had been a domestic corporation, the earnings and profits attributable, under regulations prescribed by the Secretary of the Treasury or his delegate, to any net gain from the sale or exchange of property, as defined in section 337(b), will be excluded from earnings and profits of the foreign corporation for purposes of section 1248.

The application of paragraph (2) of section 1248(c) may be illustrated by an example involving foreign corporation X, wholly owned by U.S. person A. Corporation X, reporting its income on a calendar-year basis, adopted a plan of complete liquidation on January 1, 1963. During 1963, it sold all of its assets to M, and realized a gain of \$300. The earnings and profits of corporation X for taxable year 1963 were \$400, \$100 attributable to operations and \$300 attributable to the sale of all of its assets to M. Corporation X was completely liquidated

on December 31, 1963, at which time all of its assets were distributed to A. A realized a gain of \$500 on the exchange. Corporation X was not a collapsible corporation and section 332 did not apply to the liquidation; \$100 of earnings and profits attributable to 1963 operations is includible in the gross income of A as a dividend under the provisions of section 1248(a), and \$400 is includible in gross income of A as gain from the exchange of a capital asset.

Paragraph (3) of section 1248(c), for which there is no corresponding provision in the bill as passed by the House, provides for the exclusion from earnings and profits of a foreign corporation, for purposes of section 1248, of earnings and profits accumulated while the foreign corporation was a less developed country corporation, as defined in section 955(c), if the requirements of subparagraphs (A) and (B) are met.

Subparagraph (A) of section 1248(c)(3) provides that the foreign corporation whose stock is sold or exchanged must have qualified (1) as a less developed country corporation, as defined in section 955(c)(1) (added by sec. 13 of the bill), for all taxable years of such corporation beginning after December 31, 1962, for which the country under the laws of which the foreign corporation was created or organized was designated a less developed country under section 955(c)(3) (added by sec. 12 of your committee bill) or (2) as a less developed country corporation, as defined in section 955(c)(2), for all taxable years of such corporation beginning after December 31, 1962, for which the country under the laws of which the aircraft or vessels described in section 955(c)(2) were registered were designated less developed countries under section 955(c)(3).

The application of subparagraph (A) of section 1248(c)(3) may be illustrated by the following examples:

Example 1.—A, a U.S. person, acquired 100 percent of the stock of M, a foreign corporation incorporated under the laws of country X, on January 1, 1951, and sold the stock on December 31, 1965. Corporation M, a calendar year taxpayer, had earnings and profits of \$100 in each of its taxable years 1951 through 1965. A realized a gain of \$1,900 on the sale of corporation M stock. Country X was designated a less developed country for the year 1963, and corporation M qualified as a less developed country corporation for its 1963 taxable year. A is required to include \$200 in gross income as a dividend under the provisions of section 1248(a) (\$100 attributable to earnings and profits of taxable year 1964 and \$100 attributable to earnings and profits of taxable year 1965). \$1,700 of the total gain from the sale of M stock is includible in gross income as long-term capital gain. If foreign corporation X had been designated a less developed country for taxable years 1963 and 1964, but corporation M qualified as a less developed country corporation only for taxable year 1963, \$300 of the gain would be includible in gross income of A as a dividend (all post-1962 earnings and profits) and \$1,600 would be includible in gross income as long-term capital gain.

Example 2.—A, a U.S. person, owns 100 percent of the stock of foreign corporation M. Corporation M owns 100 percent of the stock of foreign corporation N. Corporation N's only asset in taxable year 1963 is a vessel registered under the laws of foreign country X. Foreign country X was designated a less developed country for taxable year 1963 and corporation N qualified as a less developed country corporation in that year. Corporation M's only income for 1963 was

dividend income from corporation N and corporation N stock constituted the only asset of corporation M for taxable year 1963. Corporation M also qualified as a less developed country corporation for taxable year 1963. Corporation N sold its vessel on December 31, 1963, and purchased a replacement on January 1, 1965. Corporations M and N were not less developed country corporations for taxable year 1964 because Corporation N could not meet the income requirements of section 955(c)(2)(A) for such taxable year. Corporation N registered the vessel acquired January 1, 1965, in foreign country Y which was designated a less developed country for taxable year 1965. Corporations M and N qualified as less developed country corporations for taxable year 1965. A sold the stock in corporation M on December 31, 1965. The earnings and profits of corporation M accumulated in taxable years 1963 and 1965, are excluded from earnings and profits for purposes of section 1248 due to the fact the vessels from which the gross income described in section 955(c)(2) was derived were registered in less developed countries for all taxable years in which corporation N owned the vessels.

Subparagraph (B) of section 1248(c)(3) provides that a U.S. person who sells stock in a foreign corporation described in section 1248(c)(3)(A) must have owned the stock sold or exchanged for a continuous period of at least 10 years ending with the date of sale or exchange. If stock in a foreign corporation is sold by a U.S. person, other than a domestic corporation, such U.S. person must have owned the stock for the entire 10-year period. However, for purposes of subparagraph (B), the holding period of a U.S. person who is an individual, estate, or trust who acquired the stock sold or exchanged by reason of the death of an individual, shall be deemed to include the period the stock was held by the deceased individual, and by any other predecessor in interest if between such individual, estate, or trust, and such other predecessor in interest there was no transfer other than by reason of the death of an individual. If (1) the stock in a foreign corporation is sold by a U.S. person which is a domestic corporation, and (2) more than 50 percent of the total combined voting power of all classes of stock entitled to vote of the domestic corporation was owned at any time during the 10-year period ending on the date of sale or exchange by U.S. persons who were individuals, estates, or trusts, then section 1248(c)(3) will apply only if the same such U.S. persons owned more than 50 percent of the total combined voting power of all classes of stock entitled to vote of the domestic corporation at all times during the remainder of the 10-year period ending on the date of sale or exchange of the stock. However, only U.S. persons, other than domestic corporations, who own, within the meaning of section 958(a), or are considered as owning, by applying the rules of ownership of section 958(b), 10 percent or more of the stock in the domestic corporation which sells the stock in the foreign corporation will be taken into account in determining if 50 percent or more of the stock of the domestic corporation was owned at any time within the 10-year period ending on the date of sale or exchange by individuals, estates, or trusts, and if so held, has been held continuously by the same U.S. persons for the uninterrupted period ending with the date of sale or exchange.

Paragraph (4) of section 1248(c), for which there is no corresponding provision in the bill as passed by the House, provides that the earnings and profits of a foreign corporation, for purposes of section 1248, shall

be determined without regard to any item includible in gross income of the foreign corporation under chapter 1 of the code as income derived from sources within the United States for the period or periods the foreign corporation was engaged in trade or business in the United States. This paragraph will not permit an exclusion in the case of U.S. source income of a controlled foreign corporation having no permanent establishment in the United States in situations (involving tax treaties) in which such permanent establishment is a requisite to imposition of U.S. tax, since in such a situation no amount will have been included in gross income for purposes of this paragraph.

Paragraph (5) of section 1248(c), for which there is no corresponding provision in the bill as passed by the House, correlates section 1248 with section 1247 by providing that the earnings and profits of the foreign corporation, for purposes of section 1248, shall exclude earnings and profits of the foreign corporation for any taxable year of such corporation with respect to which an election under section 1247(a) (added by sec. 14 of the bill) was in effect and for which the U.S. person whose stock is sold or exchanged was a qualified shareholder, as defined in section 1247(c) (added by sec. 14 of the bill).

The application of this paragraph may be illustrated by the following examples:

Example 1.—U.S. person X acquired 10 percent of the stock of foreign corporation A on January 1, 1962, and sold such stock on December 31, 1964. Corporation A, a calendar year taxpayer, was both a controlled foreign corporation, as defined in section 957, and a foreign investment company, as defined in section 1246(b)(1), but was not a foreign personal holding company, as defined in section 552, for taxable years 1962, 1963, and 1964. Corporation A had dividend income of \$1,000 and an excess of net long-term capital gain over net short-term capital loss of \$500 in each such taxable year (1962, 1963, and 1964). Corporation A made an election in accordance with the provisions of section 1247(a) with respect to taxable years 1963 and 1964 and distributed \$900 to its shareholders in both such taxable years. X, by including \$140 in gross income (\$90 as a dividend and \$50 as long-term capital gain) in taxable years 1963 and 1964, was a qualified shareholder, as defined in section 1247(c), for both such years. X realized a gain of \$270 on the sale of his stock. Section 1246 does not apply to the sale; but section 1248(a) does apply. However, as applied to the facts of this case, section 1248(c)(5) provides that the earnings and profits, for purposes of section 1248, for taxable years 1963 and 1964 are zero and the entire gain, \$270, is includible in gross income of X as long-term capital gain from the sale of a capital asset.

Example 2.—Assume the same facts as in example 1 above except that corporation A was not a foreign investment company as defined in section 1246(b)(1) for taxable year 1964 and X did not include in gross income any amount with respect to the income of corporation A in taxable year 1964. X's ratable share of the earnings and profits of corporation A, as provided by section 1246(a)(1), is includible in gross income of X as gain from the sale of property which is not a capital asset, and section 1248 does not apply because of subsection (d)(3)(B) of section 1248.

(d) *Exceptions.*—Subsection (d) of section 1248, which corresponds to paragraphs (4), (5), and (6) of section 1248(c) of the bill as passed by the House, provides that gain on the sale or exchange of stock in

a foreign corporation shall not be includible in the gross income of the U.S. person if paragraph (1), (2), or (3) applies.

Paragraph (1) provides that section 1248 does not apply to a distribution of property to a U.S. person by a foreign corporation in redemption of part or all of the stock of such corporation to which section 303, relating to distributions in redemption of stock to pay death taxes, applies.

Paragraph (2) provides that section 1248 does not apply to gain recognized because of the receipt of additional consideration on exchanges to which section 356 applies.

Paragraph (3) provides that the amount includible in gross income as a dividend under section 1248(a) shall not include any amount treated as a dividend, as gain from the sale of an asset which is not a capital asset, or as gain from the sale of an asset held for not more than 6 months, under any other provision of the code.

(e) *Taxpayer to establish earnings and profits.*—Subsection (e) of section 1248 is the same as section 1248(d) of the bill as passed by the House, except for conforming and clarifying changes and the addition of a rule applicable to individuals whose Federal income tax is limited under the provisions of section 1248(b)(2).

Subsection (e) of section 1248 provides that the U.S. person selling or exchanging stock in a foreign corporation must establish the amount of earnings and profits of the foreign corporation to be taken into account under subsection (a), and the amount of foreign tax paid by the foreign corporation to be taken into account under subsection (b)(2). If the U.S. person does not establish the amount of earnings and profits to be taken into account, his entire gain will be treated as a dividend under subsection (a). If the U.S. person does not establish the amount of foreign taxes to be taken into account under subsection (b)(2), the limitation of tax of subsection (b)(2) shall not apply.

(b) *Clerical amendment.*—This subsection makes an addition to the table of contents of part IV of subchapter P of chapter 1.

(c) *Effective date.*—This subsection provides that the amendments made by section 15 shall apply with respect to sales or exchanges occurring after December 31, 1962. The bill as passed by the House provided that the amendments made by this section would apply with respect to sales or exchanges occurring after the date of the enactment of the bill.

SECTION 16. SALES AND EXCHANGES OF PATENTS, ETC., TO CERTAIN FOREIGN CORPORATIONS

Section 16 of the bill, for which there is no corresponding provision in the bill as passed by the House, adds a new section 1249 to part IV of subchapter P of chapter 1 (relating to special rules for determining capital gains and losses).

(a) *Treatment of gain as ordinary income.*—Under existing law certain exchanges described in sections 351 and 361 by a taxpayer of a patent or like property to a foreign corporation which the taxpayer controls may result in nonrecognition of gain if, before the exchange, under section 367 it has been established to the satisfaction of the Secretary of the Treasury or his delegate that the exchange is not in pursuance of a plan having as one of its principal purposes the avoidance of Federal income taxes. However, if the taxpayer fails to

establish that the exchange is not in pursuance of such a plan, or if a transfer by a taxpayer to a foreign corporation which he controls is an exchange other than one described in section 351 or 361, or is a sale, the gain recognized may constitute capital gain.

Subsection (a) of the new section 1249 applies to gain recognized from the sale or exchange after December 31, 1962, of a patent, invention, model, or design (whether or not patented), copyright, secret formula or process, or any similar property right by a U.S. person (as defined in sec. 7701(a)(30)) to a foreign corporation which such person controls. If such gain (but for the new subsection) would be capital gain from the sale or exchange of a capital asset or of property described in section 1231, then it is to be considered as gain from the sale or exchange of property which is neither a capital asset nor property described in section 1231.

Subsection (b) defines control to mean, with respect to a foreign corporation, ownership, directly or indirectly, of stock possessing more than 50 percent of the total combined voting power of all classes of stock entitled to vote. The ownership rules of section 958 apply in determining whether control exists.

Subsection (c) provides that subsection (a) does not apply to gain realized from the sale or exchange for stock or contribution to capital of property where it is established to the satisfaction of the Secretary of the Treasury or his delegate that the principal purpose of the transfer is to enable the foreign corporation to use such property in its own manufacturing operations.

(b) *Clerical amendment.*—Subsection (b) of section 16 of the bill makes conforming changes to the table of sections for part IV.

(c) *Effective date.*—Subsection (c) of section 16 of the bill provides that section 1249 applies to taxable years beginning after December 31, 1962.

SECTION 17. TAX TREATMENT OF COOPERATIVES AND PATRONS

(a) *In general.*—Subsection (a) of section 17 of the bill amends the Internal Revenue Code of 1954 by adding to chapter 1 a new subchapter T (relating to cooperatives and their patrons) consisting of part I, tax treatment of cooperatives, part II, tax treatment by patrons of patronage dividends, and part III, definitions and special rules.

PART I—TAX TREATMENT OF COOPERATIVES

Part I of subchapter T consists of section 1381, organizations to which such part applies, section 1382, taxable income of cooperatives, and section 1383, computation of tax where cooperative redeems non-qualified written notices of allocation.

SECTION 1381. ORGANIZATIONS TO WHICH PART APPLIES

(a) *In general.*—Subsection (a) of section 1381 provides that part I of subchapter T is to apply to any organization which is exempt from tax under section 521 (relating to exemption of farmers' cooperatives) and to any corporation operating on a cooperative basis. Part I is not applicable, however, to any organization (1) which is exempt from income taxes (other than an exempt farmers' cooperative described in

sec. 521); (2) which is subject to the provisions of part II of subchapter H (relating to mutual savings banks, etc.); (3) which is subject to the provisions of subchapter L (relating to insurance companies); or (4) which is engaged in furnishing electric energy, or providing telephone service, to persons in rural areas. Thus, part I of the new subchapter T does not apply to any cooperative exempt from tax under section 501. Nor does it apply to a cooperative which generates or transmits electricity for use by persons living in rural areas.

(b) *Tax on certain farmers' cooperatives.*—Subsection (b) of section 1381 provides that the farmers' cooperatives described in section 521 are subject to corporate income taxes. This is the same provision as the provision presently contained in section 522.

SECTION 1382. TAXABLE INCOME OF COOPERATIVES

(a) *Gross income.*—Subsection (a) of section 1382 provides that, except as provided in section 1382(b), all cooperatives to which part I of the new subchapter T applies must compute gross income without any adjustment (as a reduction in gross receipts, an increase in cost of goods sold, or otherwise) for amounts allocated or distributed to patrons out of net earnings.

(b) *Patronage dividends.*—Subsection (b)(1), applicable to both taxable and exempt cooperatives, provides that in determining the taxable income of a cooperative there are not to be taken into account certain patronage dividends paid in money, qualified written notices of allocation, or other property (other than nonqualified written notices of allocation). Under this subsection, the patronage dividends which are not to be taken into account in computing taxable income for a taxable year are those which are paid during the payment period for that taxable year (as defined in sec. 1382(d)) with respect to patronage occurring during such taxable year. For this purpose, under section 1382(d) a patronage dividend shall be treated as paid in money during the payment period to the extent it is paid by a qualified check (as defined in sec. 1388(c)(4)) issued during the payment period and endorsed and cashed on or before the 90th day after the close of the payment period.

Under subsection (b)(2), also applicable to both taxable and exempt cooperatives, certain amounts paid in money or other property (except written notices of allocation) in redemption of nonqualified written notices of allocation are not to be taken into account in determining the taxable income of a cooperative. The amounts described in subsection (b)(2) which are not to be taken into account for a taxable year are those which are paid during the payment period for that taxable year in redemption of nonqualified written notices of allocation which were paid as patronage dividends during the payment period for the taxable year during which the patronage occurred.

Subsection (b) also provides that amounts described in such subsection which are not taken into account in determining taxable income are to be treated for purposes of the 1954 Code in the same manner as items of gross income and corresponding deductions therefrom. Thus, for example, in determining the amount omitted from gross income for purposes of section 6501(e) (relating to period of limitations where there are omissions from gross income), amounts paid as patronage dividends (though not required to be taken into

account in determining taxable income) are to be treated as amounts properly includible in gross income.

(c) *Deduction for nonpatronage distributions, etc.*—In the case of a farmers' cooperative which is exempt under section 521, certain deductions (in addition to other deductions allowed under ch. 1) are allowed under subsection (c) of the new section 1382. Subsection (c)(1) allows a deduction for dividends paid by such a cooperative during the taxable year on its capital stock. This deduction is the same in substance as that currently allowed under section 522(b)(1)(A).

Subsection (c)(2)(A) allows a deduction for amounts paid (or treated as paid under sec. 1382(d)) during the payment period for a taxable year, on a patronage basis, out of earnings of that taxable year derived either from business done for the United States or from sources other than patronage. A deduction is allowed by subsection (c)(2)(A), however, only for amounts paid in money, qualified written notices of allocation, or other property (except nonqualified written notices of allocation). For purposes of the deduction allowed by subsection (c)(2)(A), amounts are considered as paid on a patronage basis if they are paid in proportion, insofar as is practicable, to the amount of business done by or for patrons during the period to which such amounts are attributable.

In addition to the deductions allowed by subsections (c)(1) and (c)(2)(A), a deduction is allowed under subsection (c)(2)(B) for amounts paid in money or other property (except written notices of allocation) in redemption of a nonqualified written notice of allocation which was previously paid during the payment period for a taxable year on a patronage basis to a patron out of earnings derived during that taxable year either from business done for the United States or from sources other than patronage. A deduction under subsection (c)(2)(B) will be allowed for a taxable year only for amounts paid during the payment period for that taxable year.

For purposes of the new subchapter T, a written notice of allocation is considered paid when it is issued to the patron. Amounts paid in redemption of a nonqualified written notice of allocation which are in excess of the stated dollar amount of such written notice of allocation and which in effect constitute interest may be deducted by the cooperative as interest. These excess amounts will be treated by the distributee as interest and not as a patronage dividend.

(d) *Payment period for each taxable year.*—Subsection (d) of section 1382 contains the definition of the "payment period for each taxable year." It provides that the payment period for any taxable year is the period beginning with the 1st day of such taxable year and ending with the 15th day of the 9th month following the close of such year. Thus, a cooperative has 8½ months after the close of a taxable year in which to pay patronage dividends out of the net earnings from patronage occurring during that taxable year. Any patronage dividend which it pays after that time must be taken into account by the cooperative in computing its taxable income; and the cooperative will be allowed no subsequent adjustment for any amount it pays in redemption of a written notice of allocation which was paid as a part of such patronage dividend. The same general rules apply with respect to nonpatronage distributions made on a patronage basis. Subsection (d) also provides that, for purposes of section 1382 (b)(1) and (c)(2)(A), a qualified check shall be treated as an amount paid in money during the payment period for a taxable year if it is issued during such

payment period and is endorsed and cashed on or before the 90th day after the close of such payment period.

(e) *Products marketed under pooling arrangements.*—Subsection (e) of section 1382 provides a special rule for determining, for purposes of section 1382(b), when the patronage is considered to have occurred in the case of a pooling arrangement for the marketing of products. Under this rule, the patronage will (to the extent provided in regulations prescribed by the Secretary of the Treasury or his delegate) be treated as occurring during the taxable year in which the pool closes. For example, farmer A delivers to the X cooperative 100 bushels of wheat on August 15, 1963, at which time he receives a “per bushel” advance. On October 15, 1963, he receives an additional “per bushel” payment. The pool sells some of its wheat in 1963 and the rest in January of 1964. The pool is closed on February 15, 1964. For purposes of section 1382(b), A’s patronage is considered as occurring in 1964.

Section 1382 has no effect on, and is not intended to change, existing rules with respect to the time at which items are taken into account in computing the cooperative’s gross income. For example, a tobacco stabilization cooperative may be required by the Commodity Credit Corporation to apply a portion of its proceeds from the sale of tobacco against loans on other crop years. In a letter to the Department of Agriculture dated October 11, 1955, the Internal Revenue Service held that this portion of the proceeds was not includible in the cooperative’s gross income until the cooperative had an unrestricted right to such portion. Section 1382 will in no way change this holding. Under section 1382(f), the Secretary of the Treasury or his delegate may provide by regulations that, in such a case, the patronage to which this portion of the proceeds relates is to be considered to have occurred during the taxable year when the cooperative first had an unrestricted right to such portion. This will permit the cooperative to pay these proceeds out as patronage dividends during the payment period for such later year. If the conditions of section 1382(b) are met, such patronage dividends need not be taken into account in determining the taxable income of the cooperative for such later year. Section 1382(f) permits the Secretary of the Treasury or his delegate to provide similar rules as to when patronage is considered to have occurred in other cases when earnings are includible in the gross income of a cooperative for a taxable year after the patronage occurred.

SECTION 1383. COMPUTATION OF TAX WHERE COOPERATIVE REDEEMS NONQUALIFIED WRITTEN NOTICES OF ALLOCATION

Section 1383 provides a special rule for computing a cooperative’s tax for a year when it redeems nonqualified written notices of allocation.

(a) *General rule.*—Section 1383(a) provides that if, for a taxable year, a cooperative is allowed a deduction under section 1382 (b)(2) or (c)(2)(B) for amounts it pays in redemption of nonqualified written notices of allocation, then its tax for that year shall be whichever of the following is the smaller:

- (1) The tax for the taxable year computed with the deduction for the amounts paid in redemption of the nonqualified written notices of allocation, or

(2) An amount equal to—

(A) the tax for the taxable year computed without such deduction, minus

(B) the decrease in tax under chapter 1 for the prior taxable year (or years) which would result solely from treating such nonqualified written notices of allocation as qualified written notices of allocation.

(b) *Special rules.*—Section 1383(b) provides three special rules applying to the alternative tax computations based on the decrease in tax for the prior taxable years. Under section 1383(b)(1), if the decrease in tax for the prior taxable year (or years) exceeds the tax for the current year (computed without any deduction for amounts paid in redemption of nonqualified written notices of allocation), the excess is to be considered to be a payment of tax on the last day prescribed by law for the payment of tax for the current taxable year, and is to be refunded or credited in the same manner as if it were an overpayment for the current taxable year.

Section 1383(b)(2) provides that, for purposes of computing the decrease in tax for the prior taxable year, the nonqualified written notices of allocation which are treated as qualified written notices of allocation are to be considered to have a stated dollar amount equal to the amount paid in redemption of such written notices of allocation to the extent such amount is allowable as a deduction under section 1382 (b)(2) or (c)(2)(B).

Section 1383(b)(3) provides that if the alternative tax computation provided by section 1383(a)(2) is used, then the deduction otherwise allowable for the current year by reason of the redemption of nonqualified written notices of allocation is not to be allowed for any purpose under the 1954 Code.

The application of section 1383 may be illustrated by the following example:

The X cooperative (which reports its income on a calendar year basis) pays patronage dividends of \$100 in nonqualified written notices of allocation on February 1, 1964, with respect to patronage occurring in 1963. Since the patronage dividends were paid in nonqualified written notices of allocation, the X cooperative must include the \$100 in gross income and is not allowed a deduction for that amount for 1963. On December 1, 1966, the X cooperative redeems these nonqualified written notices of allocation for \$50. Section 1382(b)(2) permits, in effect, the X cooperative to deduct that \$50 from gross income in determining its taxable income for 1966. However, if the X cooperative otherwise has a loss for 1966 and, therefore, owes no tax for that year, it may make the computation under the alternative method provided in section 1383(a)(2). Under this alternative, it would be permitted a credit or refund of the decrease in tax for 1963 which results from recomputing the 1963 tax liability as if patronage dividends of \$50 had been paid for 1963 in qualified written notices of allocation. If this alternative is used, the X cooperative cannot then use the \$50 deduction otherwise allowable for 1966 to increase its net operating loss carryback or carryforward. If the X cooperative also redeems on December 1, 1966, nonqualified written notices of allocation which were paid as patronage dividends on February 1, 1965, with respect to patronage occurring in 1964, it would be allowed a credit or refund for the decrease in tax for 1964. It could not, however, apply one method for computing the tax with

respect to the redemption in 1966 of the nonqualified written notices of allocation paid in 1964 and the other method with respect to the redemption in 1966 of the nonqualified written notices of allocation paid in 1965.

PART II—TAX TREATMENT BY PATRONS OF PATRONAGE DIVIDENDS

Part II of subchapter T, consisting of section 1385, deals with the patron's tax treatment of patronage dividends and amounts paid by an exempt farmers' cooperative from nonpatronage earnings.

SECTION 1385. AMOUNTS INCLUDIBLE IN PATRON'S GROSS INCOME

(a) *General rule.*—Subsection (a)(1) requires the patron to include in gross income the amount of any patronage dividend (other than one described in sec. 1385(b)) received during the taxable year from a taxable or an exempt cooperative to which part I of subchapter T applies, if paid in money, a qualified written notice of allocation, or other property (except a nonqualified written notice of allocation). Subsection (a)(2) requires inclusion in the gross income of the patron of distributions (other than those paid in nonqualified written notices of allocation) paid on a patronage basis by a farmers' cooperative exempt under section 521 with respect to earnings derived either from business done for the United States or from sources other than patronage. The patron must include patronage dividends in gross income for the taxable year during which they are received, even though the adjustment in computing taxable income of the cooperative was made for its preceding taxable year because they were paid during the payment period for such preceding taxable year. Patronage dividends are includible in the patron's gross income under section 1385 even if the cooperative is not permitted any adjustment for such patronage dividends because they were not paid during the payment period for the taxable year in which the patronage occurred.

(b) *Exclusion from gross income.*—Subsection (b)(1) of section 1385 excludes from gross income a patronage dividend, or an amount received on the redemption, sale, or other disposition of a nonqualified written notice of allocation which was previously paid as a patronage dividend, which is properly taken into account as an adjustment to basis of property. For example, if a patronage dividend is attributable to the purchase of a capital asset or property used in a trade or business, such patronage dividend will not be included in the distributee's gross income but will reduce the basis of such asset or property. Subsection (b)(2) provides that a patronage dividend, or an amount received on the redemption, sale, or other disposition of a nonqualified written notice of allocation which was previously paid as a patronage dividend, which is paid to a patron with respect to the purchase of a personal, rather than a business, expense item, is not includible in gross income. These provisions are to be applied under regulations prescribed by the Secretary of the Treasury or his delegate.

(c) *Treatment of certain nonqualified written notices of allocation.*—Subsection (c)(1) of section 1385 describes the kind of nonqualified written notices of allocation to which section 1385(c) applies. This subsection applies to a nonqualified written notice of allocation which was paid as a patronage dividend by a taxable or an exempt coopera-

tive, and to a nonqualified written notice of allocation which was paid on a patronage basis by a farmers' cooperative exempt under section 521 out of earnings derived either from business done for the United States or from sources other than patronage.

Subsection (c)(2)(A) of section 1385 provides that such a nonqualified written notice of allocation is to have a zero basis in the hands of the patron to whom it was paid. Subsection (c)(2)(B) of section 1385 provides that the basis of a nonqualified written notice of allocation described in subsection (c)(1) acquired from a decedent is to be its basis in the hands of the decedent. Any amount which the beneficiary is required to report as ordinary income on the redemption, sale, or other disposition of such written notice of allocation is income in respect of a decedent under section 691 of the code. Subsection (c)(2)(C) provides that any gain on the redemption, sale, or other disposition of a nonqualified written notice of allocation described in subsection (c)(1) is to be ordinary income to the extent that its stated dollar amount exceeds its basis. This is true whether such gain is realized by the patron who received the nonqualified written notice of allocation or any subsequent holder. For example, farmer A receives a patronage dividend paid in the form of a nonqualified written notice of allocation which is attributable to the sale of his crop to the X cooperative. The stated dollar amount of the nonqualified written notice of allocation is \$100. The basis of the written notice of allocation in the hands of farmer A is zero and he must report any amount up to \$100 received by him on its redemption, sale, or other disposition as ordinary income. If farmer A gives the written notice of allocation to his son B, B takes farmer A's (the donor's) basis which is zero, and any gain up to \$100 which B later realizes on its redemption, sale, or other disposition is ordinary income. Similarly, if A dies before realizing any gain on the nonqualified written notice of allocation, B, his legatee, has a zero basis for such written notice of allocation and any gain up to \$100 which he then realizes on its redemption, sale, or other disposition is also ordinary income. Any amounts realized on the redemption, sale, or other disposition of such nonqualified written notice of allocation in excess of \$100 will be treated under the applicable provisions of the code. These provisions in section 1385(c)(2)(C) are not intended to reflect in any way on how gain on the redemption, sale, or other disposition of a written notice of allocation would be treated under existing law.

PART III—DEFINITIONS; SPECIAL RULES

Part III of subchapter T, consisting of section 1388, defines "patronage dividend," "written notice of allocation," "qualified written notice of allocation," "qualified check," and "nonqualified written notice of allocation," and provides special rules for determining amounts paid or received.

SECTION 1388. DEFINITIONS; SPECIAL RULES

(a) *Patronage dividend*.—Under subsection (a) of section 1388, the term "patronage dividend" means an amount paid to a patron by a cooperative to which part I of subchapter T applies (1) on the basis of quantity or value of business done with or for such patron, (2) under an obligation to pay such amount, which obligation existed before the

cooperative received the amount, and (3) which is determined by reference to the net earnings of the cooperative from business done with or for its patrons. It is made clear that there are not to be included as patronage dividends any amounts which are out of earnings other than from business done with or for patrons, or any amounts paid to patrons which are attributable to the patronage of other patrons to whom no amounts are paid, or to whom smaller amounts are paid, with respect to substantially identical transactions. Thus, if a cooperative does not pay any patronage dividends to nonmembers, any portion of the amounts paid to members which is out of net earnings from patronage with nonmembers, and which would have been paid to the nonmembers if all patrons were treated alike, is not a patronage dividend.

(b) *Written notice of allocation.*—The term “written notice of allocation” is defined in subsection (b) of section 1388 to mean any capital stock, revolving fund certificate, retain certificate, certificate of indebtedness, letter of advice, or other written notice, which discloses to the recipient the stated dollar amount allocated to him, and the portion thereof, if any, which constitutes a patronage dividend.

This definition is applicable both to written notices of allocation paid as patronage dividends and to written notices of allocation paid with respect to nonpatronage earnings or earnings from business done for the United States.

(c) *Qualified written notice of allocation.*—Subsection (c)(1) of section 1388 contains the definition of “qualified written notice of allocation”. Subsection (c)(1)(A) provides, in the case of both taxable and exempt cooperatives, that the term “qualified written notice of allocation” includes a written notice of allocation which the patron may redeem in cash, at its stated dollar amount, at any time within a period beginning on the date such written notice of allocation is paid and ending not earlier than 90 days from such date. The patron must be notified by the cooperative, in writing, at the time he receives the written notice of allocation, of this right of redemption. It is intended that this notice must be given separately to each patron and not in the form of a notice in a newspaper or posted at the cooperative’s headquarters. If the patron does not exercise his option to redeem the written notice of allocation, he must, nevertheless, take it into account, at its stated dollar amount, in the manner provided in section 1385(a).

Subsection (c)(1)(B) of section 1388, also applicable to both taxable and exempt cooperatives, provides that the term “qualified written notice of allocation” also includes a written notice of allocation which the patron has consented to take into account at its stated dollar amount in the manner provided in section 1385(a). This consent must be made in the manner provided in subsection (c)(2) of section 1388.

Subsection (c)(1) provides, however, that a written notice of allocation is not “qualified” unless at least 20 percent of the patronage dividend, or the payment with respect to nonpatronage earnings or earnings from business done for the United States, of which it is a part, is paid in money or by qualified check (as defined in sec. 1388(c)(4)). Thus, even though the patron has consented to take the face amount of a written notice of allocation paid as part of a patronage dividend into account as provided in section 1385(a), or

such allocation is redeemable for cash at any time within a period of at least 90 days, such written notice of allocation will not be qualified unless at least 20 percent of the patronage dividend is paid in money or by qualified check.

Subsection (c)(2) of section 1388 provides the three different ways in which the consent to take written notices of allocation into account as provided in section 1385(a) may be made. The first way is to make such consent in writing. (This does not include a consent made by endorsing and cashing a qualified check which is described in subsection (c)(2)(C).) The written consent must be made by the patron before the close of the cooperative's taxable year during which the patronage to which the written notice of allocation is attributable occurred. Such consent is, under subsection (c)(3)(A)(i), effective with respect to all patronage occurring during the taxable year of the cooperative in which such consent is made and, unless revoked as provided in subsection (c)(3)(B)(i), all subsequent taxable years. Subsection (c)(3)(B)(i) provides that such a consent may be revoked by the patron at any time. The revocation must be in writing and filed with the cooperative. Thus, any such written consent which is, by its terms, irrevocable is not a consent that would qualify a written notice of allocation under subsection (c)(1)(B). A revocation is only effective with respect to patronage occurring after the close of the cooperative's taxable year during which the revocation is filed with it. In the case of a patron participating in a pooling arrangement described in section 1382(e), a written consent may be made at any time before the close of the cooperative's taxable year during which the pool closes. Any subsequent revocation filed by the patron, however, would not be effective with respect to that pool.

Subsection (c)(2)(B) describes another way the consent can be given by a patron who is a member (or prospective member) of the cooperative. In this case, the consent may be made by the patron by obtaining or retaining membership in the cooperative after—

(A) the cooperative has adopted a bylaw providing that membership in the cooperative constitutes such consent, and

(B) he has received a written notification and copy of such bylaw.

The bylaw described in (A) must be adopted by the cooperative after the date of enactment of this bill (the Revenue Act of 1962) and must contain a clear statement that membership in the cooperative constitutes the prescribed consent. The following is an example of a bylaw provision which would meet this requirement:

Each person who hereafter applies for and is accepted to membership in this cooperative and each member of this cooperative on the effective date of this bylaw who continues as a member after such date shall, by such act alone, consent that the amount of any distributions with respect to his patronage occurring after -----, which are made in written notices of allocation (as defined in 26 U.S.C. 1388) and which are received by him from the cooperative, will be taken into account by him at their stated dollar amounts in the manner provided in 26 U.S.C. 1385(a) in the taxable year in which such written notices of allocation are received by him.

Before a patron shall be considered to have consented under this second alternative, he must receive the written notification and the copy of the bylaw, as provided in (B) above. In the case of a new member, he must receive the notification and the copy of the bylaw before he becomes a member. The written notification must inform the patron that this bylaw has been adopted and of its significance. It is intended that the notification and copy of the bylaw must be given to each individual separately and not in the form of a notice in a newspaper or posted at the cooperative's headquarters.

Under subsection (c)(3)(A)(ii) of section 1388, this alternative consent will be effective with respect to all patronage of the member-patron occurring after he receives the notification and copy of the bylaw provision. In the case of a pooling arrangement described in section 1382(e), the consent will only be effective with respect to the member's actual patronage occurring after he receives the notification and copy of the bylaw and shall not be effective with respect to any of his patronage under the pool before this time. Subsection (c)(3)(B)(ii) provides that this alternative consent will not apply to any patronage of the patron after he ceases to be a member of the cooperative or after the bylaw provision is repealed by the cooperative. In the case of a pooling arrangement, this refers to the time when the patronage actually occurred. Thus, if the patron resigns his membership in the cooperative during the period a pool is in operation, he will not be considered to have consented with respect to any of his patronage under the pool after the date of his resignation.

Subsection (c)(2)(C) describes the third way that a patron may consent to take a written notice of allocation into account as provided in section 1385(a). Under this alternative, the consent may be given by endorsing and cashing a qualified check (as defined in subsec. (c)(4)) which is paid as part of the same patronage dividend, or the same distribution with respect to nonpatronage earnings, as is the written notice of allocation.

Subsection (c)(4) defines a qualified check to mean only a check, or other instrument redeemable in money, (1) which is paid as a part of a patronage dividend, or as a part of a payment described in section 1382(c)(2)(A), to a patron who has not already given consent in the manner provided in subsection (c)(2) (A) or (B) with respect to such patronage dividend or such payment, and (2) on which there is clearly imprinted a statement that the endorsement and cashing of the check (or other instrument) constitutes the consent of the payee to take into account, as provided in the Federal income tax laws, the stated dollar amount of any written notices of allocation which are paid as a part of the patronage dividend or payment of which such check (or other instrument) is also a part. The term "qualified check" does not include a check or other instrument which is paid as part of a patronage dividend or payment which does not include a written notice of allocation (other than one described in sec. 1388(c)(1)(A)). Thus a check which is paid as part of a patronage dividend is not a "qualified check" (even though it has the above-described statement imprinted on it) if the remaining portion of such patronage dividend is paid in cash or if the only written notices of allocation included in the distribution are redeemable allocations which are considered qualified under section 1388(c)(1)(A). Under this definition, it is not necessary that a qualified check be in the form of an ordinary check which is payable through.

the banking system. It may, for example, be in the form of an instrument which may be redeemed by the cooperative for money.

In order to constitute consent, a qualified check must be cashed by the payee on or before the 90th day after the close of the payment period for the taxable year of the cooperative for which the patronage dividend, or the distribution with respect to nonpatronage earnings, is paid. Thus, in the case of a cooperative on a calendar year basis, which pays patronage dividends for 1963 in qualified checks and written notices of allocation, only those patrons who cash their qualified checks on or before December 14, 1964, shall be considered to have consented under subsection (c)(2)(C) with respect to the written notices of allocation. For purposes of determining whether or not the cooperative is required to take the amount of a qualified check into account in computing its taxable income under section 1382 (b)(1) or (c)(2)(A), section 1382(d) provides that those qualified checks which are issued during the payment period for the taxable year and which are endorsed and cashed on or before the 90th day after the close of such period shall be treated as amounts paid in money during such payment period. Thus, in the above example, if the qualified checks were issued on or before September 15, 1964, then the amount of those checks which are cashed on or before December 14, 1964, shall be treated, for purposes of section 1382(b)(1), as patronage dividends paid in money during the payment period for 1963.

Under the above example, in the case of a patron who has not cashed his qualified check by December 14, 1964, there is no consent and both the written notice of allocation and the qualified check constitute nonqualified written notices of allocation. Therefore, as of that date, the patron is not required to include any amount in gross income, and the cooperative is allowed no deduction, with respect to either the qualified check or the written notice of allocation. If the payee cashes his check on January 2, 1965, he shall treat the amount received for tax purposes as an amount received on January 2, 1965, in redemption of a nonqualified written notice of allocation. Likewise, the cooperative shall treat the amount of the check as an amount paid on January 2, 1965, in redemption of a nonqualified written notice of allocation. The written notice of allocation itself will be treated in the same manner as any other nonqualified written notice of allocation; that is, nothing will be includible in the gross income of the patron and no deduction will be allowed the cooperative until the written notice of allocation is redeemed.

Since the term "qualified check" includes only checks or other instruments issued to patrons who have not otherwise consented with respect to the distribution of which the check or other instrument is a part, the endorsing and cashing of a check which contains a statement that this constitutes consent by a patron of a cooperative shall have no effect as a consent if such patron is already considered as having consented by reason of subsection (c)(2) (A) or (B) with respect to the distribution of which such check is a part.

Endorsing and cashing a qualified check shall be considered a consent only with respect to the written notices of allocation which are paid as part of the same distribution as is the qualified check.

(d) *Nonqualified written notice of allocation.*—Subsection (d) of section 1388 defines "nonqualified written notice of allocation" to mean (1) a written notice of allocation which is not described in subsection (c) and (2) a qualified check which is not cashed on or before

the close of the 90th day after the close of the payment period for the taxable year (of the cooperative) for which the distribution of which it is a part is paid.

(e) *Determination of amount paid or received.*—Subsection (e) of section 1388 provides that, for purposes of the new subchapter T, in determining amounts paid or received: (1) Property, other than a written notice of allocation, is to be taken into account at its fair market value, and (2) a qualified written notice of allocation is to be taken into account at its stated dollar amount. Thus, if a cooperative pays part of its patronage dividends in qualified written notices of allocation, and the requirements of section 1382 are met, the cooperative will not be required to take the stated dollar amounts of such written notices of allocation into account in determining its taxable income. Conversely, the patron receiving a qualified written notice of allocation must take it into account, as provided in section 1385(a), at its stated dollar amount. If a cooperative pays a patronage dividend in nonqualified written notices of allocation, it is required to include the stated dollar amount thereof in gross income and is allowed no deduction (and the patrons are not required to include such amount in gross income) at the time such written notices of allocation are paid (or received).

SECTION 17. TAX TREATMENT OF COOPERATIVES AND PATRONS (Continued)

(b) *Technical amendments.*—Subsection (b) of section 17 of the bill makes certain technical amendments to reflect the provisions of the new subchapter T.

Paragraph (1) amends section 521(a) (relating to exemption of farmers' cooperatives from tax) to insert references to part I of the new subchapter T.

Paragraph (2) repeals section 522 (relating to tax on farmers' cooperatives exempt under sec. 521).

Paragraph (3) amends section 6072(d) (relating to time for filing income tax returns of exempt cooperative associations) to extend the time for filing income tax returns of certain taxable cooperatives. Under this amendment, these cooperatives need not file returns for a taxable year until the 15th day of the 9th month following the close of such taxable year. Under existing law, these nonexempt cooperatives must file returns for a taxable year on or before the 15th day of the 3d month following the close of such taxable year. The taxable cooperatives which may take advantage of this filing date provision are those described in section 1381(a)(2) which either (1) are under an obligation to pay patronage dividends in an amount equal to 50 percent or more of net earnings from business done with or for patrons, or (2) actually paid patronage dividends in such an amount out of net earnings from business done with or for patrons during the most recent taxable year for which they had such net earnings. Under existing law, exempt farmers' cooperatives are not required to file returns for a taxable year until the 15th day of the 9th month following the close of such taxable year, and this rule is not changed.

(c) *Effective dates.*—Subsection (c) of section 17 of the bill prescribes the effective dates for subsections (a) and (b).

Paragraph (1) of subsection (c) provides that, in the case of cooperatives, the amendments made by subsections (a) and (b) will, ex-

cept as provided in paragraph (3), apply to taxable years of organizations described in section 1381(a) beginning after December 31, 1962.

Paragraph (2) of subsection (c) provides that, in the case of patrons, section 1385 will, except as provided in paragraph (3), apply with respect to any amount received from any organization described in section 1381(a), to the extent that such amount is paid by such organization in a taxable year of such organization beginning after December 31, 1962.

Paragraph (3) of subsection (c) provides that, in the case of any money, written notices of allocation, or other property, paid by any organization described in section 1381(a)—

(A) before the first day of the first taxable year of such organization beginning after December 31, 1962, or

(B) on or after such first day with respect to patronage occurring before such first day,

the tax treatment of such money, written notices of allocation, or other property (including the tax treatment of gain or loss on the redemption, sale, or other disposition of such written notices of allocation) by any cooperative or patron is to be made under the 1954 Code without regard to the new subchapter T. For example, if a cooperative pays a patronage dividend during its taxable year beginning January 1, 1963, out of net earnings for its taxable year ending on December 31, 1962, the tax treatment of such a patronage dividend (including the determination of when it is considered paid) would be determined under existing law. Furthermore, the provisions of section 1382 (b)(2) and (c)(2)(B) (relating to deduction for amounts paid in redemption of certain nonqualified written notices of allocation) and section 1383 (relating to computation of tax where a cooperative redeems nonqualified written notices of allocation) are not applicable to amounts paid in redemption of a written notice of allocation which was paid (whether before or after January 1, 1963) with respect to patronage occurring before such date.

SECTION 18. INCLUSION OF FOREIGN REAL PROPERTY IN GROSS ESTATE

This section of the bill is the same as section 18 of the bill as passed by the House, except that the special provisions discussed below in subsection (b), which under the bill as passed by the House were applicable in the case of decedents dying after the date of enactment and before July 1, 1964, are changed by your committee so as to be applicable in the case of decedents dying after the date of enactment and before January 1, 1963.

(a) *Amendments to include foreign real property.*—Subsection (a) of section 18 of the bill amends sections 2031(a), 2033, 2034, 2035(a), 2036(a), 2037(a), 2038(a), 2040, and 2041(a) of the 1954 Code by striking from each section the language which requires the exclusion from the gross estate of real property situated outside of the United States. The result of these amendments, subject to the effective date provisions of subsection (b) of section 18, is to include in the gross estate of decedents who are citizens or residents of the United States, the fair market value of their interest in real property which is situated outside of the United States. Under existing law real

property situated outside of the United States is excluded in determining the value of the gross estate.

(b) *Effective date.*—Subsection (b) of section 18 provides that the amendments which repeal the exclusion for real property situated outside of the United States are effective with respect to the estates of decedents dying after the date of the enactment of the bill. However, special provisions apply in the case of decedents dying after such date of enactment and before January 1, 1963.

Under one of these provisions, the value of real property situated outside of the United States is not included in the gross estate of the decedent under section 2033, 2034, 2035(a), 2036(a), 2037(a), or 2038(a) to the extent the decedent's interest in it was acquired before February 1, 1962. Under another of these special provisions, the value of real property situated outside the United States is excluded from the gross estate of a decedent who dies after the date of the enactment of the bill and before January 1, 1963, to the extent the property or interest therein was either held by the decedent and the surviving tenant in a joint tenancy or tenancy by the entirety before February 1, 1962, or, even though the joint tenancy or tenancy by the entirety was created on or after February 1, 1962, to the extent the property or interest therein was acquired by the decedent before February 1, 1962. Under still another of these special provisions, in the case of decedents dying after the date of the enactment of the bill and before January 1, 1963, the value of real property situated outside the United States is excluded from the gross estate to the extent that before February 1, 1962, it was subject to a general power of appointment possessed by the decedent.

For purposes of applying these three special provisions, the real property, interests therein, and general powers of appointment to which these special provisions apply, which are acquired by the decedent after January 31, 1962, by gift within the meaning of section 2511, or from a prior decedent by devise or inheritance, or by reason of death, form of ownership, or other conditions (including the exercise or nonexercise of a power of appointment), are treated as acquired before February 1, 1962, if the donor or prior decedent acquired the property, his interest therein, or a power of appointment (whether or not a general power) in respect thereof, before that date. For example, assume that A, who bought foreign real property on December 1, 1961, dies on March 1, 1962, and by will leaves the property to B who dies after the date of the enactment of the bill and before January 1, 1963. In this example B will be treated as having acquired the property before February 1, 1962, since A, the prior decedent from whom B acquired the property, had acquired it before February 1, 1962.

For purposes of the amendments made by section 18(b) of the bill, substantial capital additions and improvements to real property made after January 31, 1962, are to be treated as separate properties. Capital additions or improvements to either commercial or residential property which do not materially increase the value of the property are to be disregarded.

SECTION 19. REPORTING OF INTEREST, DIVIDEND, AND PATRONAGE DIVIDEND PAYMENTS OF \$10 OR MORE DURING A YEAR

Section 19 of the bill as passed by the House provided a system for the withholding of tax at the source on interest, dividends, and patronage dividends. Your committee has struck out those provisions and has inserted provisions which would require annual information reporting of certain dividend, interest, or patronage dividend payments. Such reporting is to be required with respect to payments to any person when they aggregate \$10 or more in amount to such person in any calendar year. In addition, your committee has added provisions requiring that payers of interest, dividends, or patronage dividends furnish to the recipients of these amounts annual statements showing the amounts paid to them as reported on the information returns filed with the Government. New penalty provisions are provided by your committee for failure to file information returns with respect to payments of interest, dividends, or patronage dividends and for failure to furnish to a recipient of such payments an annual statement of such payments.

(a) *Returns regarding payment of dividends and corporate earnings and profits.*—Subsection (a) of the new section 19 completely revises section 6042 of the 1954 Code (relating to returns regarding corporate dividends, earnings, and profits). Under existing section 6042 of the code the Secretary of the Treasury or his delegate has discretionary authority to require corporations to make information returns, with respect to their payments of dividends, showing the name and address of, the number of shares owned by, and the amount of dividends paid to, each shareholder. In addition, the Secretary of the Treasury or his delegate may require corporations to furnish other specified information, such as statements of accumulated earnings and profits, the names and addresses of shareholders who would be entitled to such earnings and profits if they were distributed, and the amounts that would be payable to each.

SECTION 6042. RETURNS REGARDING PAYMENT OF DIVIDENDS AND CORPORATE EARNINGS AND PROFITS

(a) *Requirement of reporting.*—Subsection (a)(1) of the new section 6042 requires every person making payments of dividends aggregating \$10 or more to any other person during any calendar year to file an information return with respect to such payments. In addition, such new subsection requires persons receiving payments of dividends in the capacity of nominee to report payments by them aggregating \$10 or more during any calendar year to any other person with respect to the dividends so received. Thus, if an individual has his stock registered in the name of his stockbroker, the stockbroker must file an information return showing the name and address of the individual and the amount of dividends he received and paid over to, or credited to the account of, such individual during the calendar year if they amount to \$10 or more. The return to be filed under section 6042(a)(1) is to be made according to the forms or regulations prescribed by the Secretary of the Treasury or his delegate and is

to set forth the name and address of the person to whom the payments were made and the aggregate amount of such payments.

Section 6042 only requires reporting with respect to dividends paid by one "person" to another "person." For purposes of this section (and secs. 6044, as amended by the bill, and 6048, as added by the bill) the term "person" has the meaning assigned to it by section 7701(a)(1) of the code. Under that section the term "person" does not include the United States, a State, a foreign government, a political subdivision of a State or foreign government, or an international organization. Therefore, dividends (and patronage dividends and interest) paid by or to one of these entities need not be reported. The person required to report under subsection (a)(1) is the person on whose capital stock the dividends are paid. The term "payment" includes constructive payment. Thus, dividends which are credited to the account of a shareholder by a mutual fund must be reported by the fund if they aggregate \$10 or more during the calendar year. The term "nominee" does not include a partner acting with respect to property of a partnership of which he is a member or a person who, acting in the capacity of trustee, holds record title to trust property. The general rules discussed in this paragraph are also applicable with respect to the new reporting requirements for interest and patronage dividends.

Subsection (a)(2) of the new section 6042 gives the Secretary of the Treasury or his delegate discretion to require information returns to be filed with respect to dividend payments aggregating less than \$10 during a calendar year.

(b) *Dividend defined.*—Subsection (b)(1) of the new section 6042 defines the term "dividend" for purposes of section 6042 to mean: (A) any distribution by a corporation which is a dividend as defined in section 316 of the code; and (B) any payment made by a stockbroker to any person as a substitute for a dividend (as so defined). Reporting is required whether a dividend is paid in cash or in other property. A dividend paid by an insurance company to a policyholder, other than a dividend upon the capital stock of such insurance company, is not a dividend within the meaning of section 6042(b)(1).

Subsection (b)(2) of the new section 6042 provides that the term "dividend," for purposes of section 6042, does not include: (A) to the extent provided in regulations prescribed by the Secretary of the Treasury or his delegate, any distribution or payment (i) by a foreign corporation, or (ii) to a foreign corporation, a nonresident alien, or a partnership not engaged in trade or business in the United States and composed in whole or in part of nonresident aliens; or (B) any amount described in section 1373 of the code (relating to undistributed taxable income of electing small business corporations).

Subsection (b)(3) provides that if the person making any payment described in subsection (a)(1) is unable to determine the portion of the payment which is a dividend or is paid with respect to a dividend, the total amount of the payment is to be treated as a dividend for purposes of information reporting required by subsection (a)(1). Thus, if a corporation is unable to determine what portion of its distributions to its shareholders during the calendar year is paid out of earnings and profits, the total amount of the distributions must be treated as a dividend.

(c) *Statements to be furnished to persons with respect to whom information is furnished.*—Subsection (c) of the new section 6042 requires every person making a return under subsection (a)(1) of section 6042 to furnish to each person whose name is set forth in such return a written statement showing (1) the name and address of the person making the return, and (2) the aggregate amount paid to the person as shown on the return. Such written statement is to be furnished to the person on or before January 31 of the year following the calendar year for which the return was made. However, no statement is required to be furnished to any person under this subsection if the aggregate amount of payments to the person as shown on the return made under subsection (a)(1) is less than \$10.

(d) *Statements to be furnished by corporations to Secretary.*—Subsection (d) of the new section 6042 provides that every corporation shall, when required by the Secretary of the Treasury or his delegate—

(1) furnish to the Secretary of the Treasury or his delegate a statement stating the name and address of each shareholder, and the number of shares owned by each shareholder;

(2) furnish to the Secretary of the Treasury or his delegate a statement of such facts as will enable him to determine the portion of the earnings and profits of the corporation (including gains, profits, and income not taxed) accumulated during such periods as the Secretary of the Treasury or his delegate may specify, which have been distributed or ordered to be distributed, respectively, to its shareholders during such taxable years as the Secretary of the Treasury or his delegate may specify; and

(3) furnish to the Secretary of the Treasury or his delegate a statement of its accumulated earnings and profits and the names and addresses of the individuals or shareholders who would be entitled to such accumulated earnings and profits if divided or distributed, and of the amounts that would be payable to each.

These provisions are substantially the same as provisions contained in the present section 6042.

SECTION 19. REPORTING OF INTEREST, DIVIDEND, AND PATRONAGE DIVIDEND PAYMENTS OF \$10 OR MORE DURING A YEAR (Continued)

(b) *Returns regarding payments of patronage dividends.*—Subsection (b) of the new section 19 amends section 6044 of the 1954 Code, to revise the provisions relating to information returns which must be filed by cooperatives.

Under existing law, a cooperative must file an information return with respect to patronage dividends which it pays to a patron during a calendar year if the aggregate is \$100 or more. Existing law also gives the Secretary of the Treasury or his delegate authority to require such information returns with regard to all patronage dividends regardless of amounts. The revised section 6044 requires reporting with respect to all payments of \$10 or more during the calendar year and, in addition, reflects the provisions of the new subchapter T of chapter 1 (relating to the tax treatment of cooperatives and patrons) which is added to the code by section 17 of the bill.

SECTION 6044. RETURNS REGARDING PATRONAGE DIVIDENDS

(a) *Requirement of reporting.*—Subsection (a)(1) provides that, except as otherwise provided in section 6044, every cooperative to which part I of subchapter T of chapter 1 applies, which makes payments of amounts described in subsection (b) aggregating \$10 or more to any person during any calendar year, is to file an information return with respect to such payments. Such return is to be made according to the forms or regulations prescribed by the Secretary of the Treasury or his delegate and is to set forth the aggregate amount of the payments and the name and address of the person to whom paid.

Subsection (a)(2) provides that the Secretary of the Treasury or his delegate may require information returns regarding payments of amounts described in subsection (b) where such payments aggregate less than \$10 to any person during any calendar year.

(b) *Amounts subject to reporting.*—Subsection (b)(1) provides that the amounts with respect to which reporting is required by subsection (a) are (except as otherwise provided by sec. 6044): (A) Patronage dividends paid in cash, qualified written notices of allocation, or other property (except nonqualified written notices of allocation); (B) in the case of an exempt farmers' cooperative, amounts described in section 1382(c)(2)(A) (relating to amounts paid with respect to nonpatronage earnings) which are paid in money, qualified written notices of allocation, or other property (except nonqualified written notices of allocation); (C) amounts described in section 1382(b)(2) paid in redemption of nonqualified written notices of allocation which were previously paid as patronage dividends; and (D) amounts described in section 1382(c)(2)(B) paid by an exempt farmers' cooperative in redemption of nonqualified written notices of allocation previously paid with respect to nonpatronage earnings. The cooperative is required to report these amounts even though it must pay tax with respect to them because they were not paid within the prescribed time limits.

Subsection (b)(2) provides that information reporting shall not be required, to the extent provided in regulations prescribed by the Secretary of the Treasury or his delegate, with respect to any payment (A) by a foreign corporation, or (B) to a foreign corporation, a nonresident alien, or a partnership not engaged in trade or business in the United States and composed in whole or in part of nonresident aliens.

(c) *Exemption for certain consumer cooperatives.*—Subsection (c) of the new section 6044 provides that a cooperative which the Secretary of the Treasury or his delegate determines is primarily engaged in selling at retail goods or services of a type that are generally for personal, living, or family use is to be granted exemption from the requirements of information reporting imposed by subsection (a) upon application for such exemption to the Secretary of the Treasury or his delegate. The application for exemption is to be made in accordance with regulations prescribed by the Secretary of the Treasury or his delegate.

(d) *Determination of amount paid.*—Subsection (d) provides that for purposes of section 6044, in determining the amount of any payment, property (other than a written notice of allocation) is to be taken into account at its fair market value, and a qualified written notice of allocation is to be taken into account at its stated dollar amount.

(e) *Statements to be furnished to persons with respect to whom information is furnished.*—Subsection (e) provides that every cooperative making a return under subsection (a)(1) shall furnish to each person whose name is set forth in such return a written statement showing (1) the name and address of the cooperative making the return, and (2) the aggregate amount of payments to the person as shown on the return. This written statement is to be furnished to the person on or before January 31 of the year following the calendar year for which the return under subsection (a)(1) was made. However, no statement is required to be furnished to any person under this subsection if the aggregate amount of payments to the person as shown on the return made under subsection (a)(1) is less than \$10.

SECTION 19. REPORTING OF INTEREST, DIVIDEND, AND PATRONAGE DIVIDEND PAYMENTS OF \$10 OR MORE DURING A YEAR (Continued)

(c) *Returns regarding payments of interest.*—Subsection (c) of the new section 19 amends subpart B of part III of subchapter A of chapter 61 of the code (relating to information concerning transactions with other persons) by adding a new section 6048 to such subpart B.

SECTION 6048. RETURNS REGARDING PAYMENTS OF INTEREST

(a) *Requirement of reporting.*—Paragraph (1) of new section 6048(a) requires every person making payments of interest (as defined in subsec. (b)) aggregating \$10 or more to any other person during any calendar year to report such payments. In addition, paragraph (1) requires persons receiving payments of interest (as defined in subsec. (b)) in the capacity of nominee to report payments by them aggregating \$10 or more during any calendar year to any other person with respect to such interest so received. The return to be filed under paragraph (1) is to be made according to the forms or regulations prescribed by the Secretary of the Treasury or his delegate and is to set forth the name and address of the person to whom the payments were made and the aggregate amount of such payments.

Paragraphs (2) and (3) restate, in general, provisions of existing law (sec. 6041(c)). Paragraph (2) provides that, when required by the Secretary of the Treasury or his delegate, every person who makes payments of interest (as defined in subsec. (b)) aggregating less than \$10 to any other person during any calendar year is to make a return setting forth the aggregate amount of such payments and the name and address of the person to whom paid. Under existing law the Secretary of the Treasury or his delegate has discretionary authority to require every corporation making payments of interest, regardless of amounts, to report the amounts so paid. Paragraph (2) limits the discretionary authority of the Secretary of the Treasury or his delegate to require information returns, with respect to payments of interest defined in subsection (b), to such payments to another person aggregating less than \$10 during a calendar year. Payments aggregating \$10 or more during the year must be reported under subsection (a)(1).

Paragraph (3) provides that, when required by the Secretary of the Treasury or his delegate, every corporation making payments, regardless of amounts, of interest other than interest as defined in subsection

(b), is to make a return according to the forms or regulations prescribed by the Secretary of the Treasury or his delegate, setting forth the amount paid and the name and address of the recipient of each such payment.

(b) *Interest defined.*—Subsection (b)(1) of the new section 6048 defines the term “interest” for purposes of subsections (a) (1) and (2) of such section to mean:

(A) Interest on evidences of indebtedness (including bonds, debentures, notes, and certificates) issued by a corporation in registered form, and to the extent provided in regulations prescribed by the Secretary of the Treasury or his delegate, interest on other evidences of indebtedness issued by a corporation of a type offered by corporations to the public. For this purpose, an instrument is in registered form if its transfer must be effected by the surrender of the old instrument and either the reissuance of the old instrument by the corporation to the new holder or the issuance by the corporation of a new instrument to the new holder. If an instrument can be transferred by endorsement it is not in registered form even though a list is maintained by the corporation of such instruments issued by it.

As used in subsection (b)(1) the term “of a type offered by corporations to the public” refers to a type of instrument. In determining whether a particular instrument comes within the scope of the term it is immaterial whether the particular instrument (or any instrument of the issue of which it is a part) actually was offered to the public so long as it is of a type which is offered by corporations to the public. Therefore, in a case where an entire issue is offered by a corporation only to its shareholders, the instruments come within the scope of the term if they are of a type offered by corporations to the public. The term does not have reference to instruments of a type offered by corporations only to other corporations. Coupon bonds issued by a corporation are an example of an evidence of indebtedness with respect to which the Secretary of the Treasury or his delegate may require information reporting under subsections (a) (1) and (2).

(B) Interest on deposits with persons carrying on the banking business. This includes interest paid or credited by any individual or organization carrying on the banking business.

(C) Amounts (whether or not designated as interest) paid or credited by a mutual savings bank, savings and loan association, building and loan association, cooperative bank, homestead association, credit union, or similar organization, in respect of deposits, investment certificates, or withdrawable or repurchasable shares. This includes interest paid with respect to face amount certificates.

(D) Interest on amounts held by an insurance company under an agreement to pay interest thereon. This subparagraph includes interest paid with respect to policy dividends held by an insurance company, and interest on the proceeds of an insurance policy held by an insurer under an agreement to pay interest thereon. This paragraph does not apply to amounts which represent the so-called “interest element” in the case of annuity or installment payments under a life insurance or endowment contract.

(E) Interest on deposits with stockbrokers and dealers in securities. This subparagraph includes interest on deposits with

stockbrokers, bondbrokers, and other persons engaged in the business of dealing in securities.

Subsection (b)(2) provides that, for purposes of subsection (a) (1) and (2), the term "interest" does not include:

(A) Interest on obligations described in section 103(a) (1) or (3) of the code (relating to obligations of a State, etc.);

(B) To the extent provided in regulations prescribed by the Secretary of the Treasury or his delegate, any amount paid by or to a foreign corporation, a nonresident alien, or a partnership not engaged in trade or business in the United States and composed in whole or in part of nonresident aliens; and

(C) Any amount on which the person making payment is required to deduct and withhold a tax under section 1451 (relating to tax-free covenant bonds) or would be so required but for section 1451(d) (relating to benefit of personal exemptions). Thus, the payment of interest on a tax-free covenant bond issued before January 1, 1934, is not required to be reported under subsection (a) (1) and (2). The fact that the person entitled to receive such interest files with the payer a signed notice in writing, as provided in section 1451(d) of the 1954 Code, claiming benefit of the deduction for personal exemptions provided in section 151 of the code, thereby relieving the payer of the duty to withhold a tax under section 1451(a), does not abrogate the exception provided by this subparagraph.

(c) *Statements to be furnished to persons with respect to whom information is furnished.*—Subsection (c) of the new section 6042 requires every person making a return under subsection (a)(1) to furnish to each person whose name is set forth in such return a written statement showing (1) the name and address of the person making the return, and (2) the aggregate amount paid to the person as shown on the return. Such written statement is to be furnished to the person on or before January 31 of the year following the calendar year for which the return under subsection (a)(1) was made. However, no statement is required to be furnished to any person under this subsection if the aggregate amount of payments to the person as shown on the return made under subsection (a)(1) is less than \$10.

SECTION 19. REPORTING OF INTEREST, DIVIDEND, AND PATRONAGE DIVIDEND PAYMENTS OF \$10 OR MORE DURING A YEAR (Continued)

(d) *Penalties for failure to file information returns.*—Subsection (d) of section 19 of the bill amends section 6652 of the 1954 Code (relating to failure to file information returns) to provide a new civil penalty for failure to file an information return with respect to payments aggregating \$10 or more, respectively, of dividends, interest, or patronage dividends as required by the amendments made to the code by subsections (a), (b), and (c) of the new section 19, and to reflect the other amendments with respect to information reporting made by such subsections.

SECTION 6652. FAILURE TO FILE CERTAIN INFORMATION RETURNS

(a) *Returns relating to payments of dividends, interest, and patronage dividends.*—Subsection (a) provides a new penalty of \$10 per statement for each failure to file a statement of the aggregate amount of payments to another person, as required by section 6042(a)(1) (relating to payments of dividends aggregating \$10 or more), section 6044(a)(1) (relating to payments of patronage dividends aggregating \$10 or more), or section 6048(a)(1) (relating to payments of interest aggregating \$10 or more), on the date prescribed therefor (determined with regard to any extension of time for filing). No penalty is to be imposed, however, with respect to a failure to file a statement, if it is shown by the payer that the failure was due to reasonable cause and not to willful neglect. The penalty is to be paid, upon notice and demand by the Secretary of the Treasury or his delegate and in the same manner as tax, by the person failing to so file the statement. The total amount imposed on the delinquent person for all such failures during any calendar year shall not exceed \$25,000.

(b) *Other returns.*—Subsection (b) retains the penalty provided under existing section 6652 for failures to file information returns not covered by the new \$10 penalty in subsection (a). Subsection (b) provides a penalty of \$1 for each failure to file a statement, at the proper time, of a payment to another person required under authority of section 6041 (relating to certain information at source), section 6042(a)(2) (relating to payments of dividends aggregating less than \$10), section 6044(a)(2) (relating to payments of patronage dividends aggregating less than \$10), section 6048(a)(2) (relating to payments of interest aggregating less than \$10), section 6048(a)(3) (relating to other payments of interest by corporations), or section 6051(d) (relating to information returns with respect to income tax withheld). The penalty is to be imposed, with respect to each failure, unless it is shown that the failure was due to reasonable cause and not to willful neglect. The penalty is to be paid, upon notice and demand by the Secretary of the Treasury or his delegate and in the same manner as tax, by the person failing to so file the statement. The total amount imposed on the delinquent person for all such failures during the calendar year shall not exceed \$1,000.

SECTION 19. REPORTING OF INTEREST, DIVIDEND, AND PATRONAGE DIVIDEND PAYMENTS OF \$10 OR MORE DURING A YEAR (Continued)

(e) *Penalty for failure to furnish statements to persons with respect to whom returns are filed.*—Subsection (e) of the new section 19 amends subchapter B of chapter 68 (relating to assessable penalties) by adding to such subchapter a new section 6678 to provide civil penalties for failure to furnish statements to persons to whom dividends, patronage dividends, or interest are paid as required by the amendments made to the code by subsections (a), (b), and (c) of the new section 19.

SECTION 6678. FAILURE TO FURNISH CERTAIN STATEMENTS

Section 6678 provides a penalty of \$10 for each failure to furnish a statement under section 6042(c), 6044(e), or 6048(c) on the date

prescribed therefor to a person with respect to whom an information return has been made under section 6042(a)(1), 6044(a)(1), or 6048(a)(1), respectively. The penalty is to be imposed unless it is shown that such failure was due to reasonable cause and not to willful neglect. The penalty is to be paid, upon notice and demand by the Secretary of the Treasury or his delegate and in the same manner as tax, by the person failing to so furnish the statement. The total amount imposed on the delinquent person for all such failures during any calendar year shall not exceed \$25,000.

(f) *Technical amendments.*—Subsection (f) of the new section 19 amends section 6041 of the code, relating to information at source, to reflect the amendments made to the code by subsections (a), (b), and (c) of the new section 19.

Paragraph (1) amends section 6041(a) of the code (relating to information returns with respect to payments of \$600 or more) in order to exclude from the application of such section payments of dividends, patronage dividends, and interest aggregating, respectively, \$10 or more during any calendar year to another person, and to exclude from such application other payments of dividends, patronage dividends, and interest with respect to which the Secretary of the Treasury or his delegate requires information returns under the authority of sections 6042(a)(2), 6044(a)(2), 6045, 6048(a)(2), and 6048(a)(3) as amended, or added to the code, by your committee's amendment.

Paragraph (2) further amends section 6041 of the code by striking out subsection (c) thereof (relating to payments of interest by corporations) since the provisions of such subsection are contained in the new section 6048 added to the code by subsection (c) of section 19 of the bill.

(g) *Clerical amendments.*—Subsection (g) of section 19 of the bill makes certain clerical amendments to the code to reflect the other amendments made to such code by section 19 of the bill.

(h) *Effective date.*—Subsection (h) of section 19 of the bill provides effective dates for the application of the provisions of such section 19 with respect to payments of dividends, interest, and patronage dividends.

Paragraph (1) provides that, except as provided in paragraph (2), the provisions of section 19 of the bill are to apply with respect to payments of dividends and interest on or after January 1, 1963.

Paragraph (2) provides that the provisions of section 19 of the bill are to apply with respect to payments of amounts described in section 6044(b) of the code (relating to returns regarding patronage dividends) on or after January 1, 1963, with respect to patronage occurring on or after the first day of the first taxable year of the cooperative beginning on or after January 1, 1963.

SECTION 20. INFORMATION WITH RESPECT TO CERTAIN FOREIGN ENTITIES

This section is the same as section 20 of the bill as passed by the House except for certain changes in the constructive ownership rules and in the penalty provision under section 6038 of the code, as amended by the bill (relating to information to be furnished with respect to certain foreign corporations), and except for certain changes in section

6046 of the code, as amended by the bill (relating to information as to the organization or reorganization of foreign corporations and as to acquisitions of their stock). The changes in section 6046 are, in general, as follows: (1) Officers or directors need not file returns unless there are one or more U.S. persons owning 5 percent or more in value of the stock of their foreign corporation; (2) the information required of officers and directors is limited to the names and addresses of U.S. persons who are 5 percent or more shareholders; and (3) information need not be furnished unless such information was required under regulations in effect 90 days prior to the date on which a person becomes liable to file a return.

(a) *Information to be furnished by individuals, domestic corporations, etc., with respect to certain foreign corporations.*—Subsection (a) of section 20 of the bill amends section 6038 of the 1954 Code. Section 6038(a)(1) requires every U.S. person to furnish the information required by such section with respect to any foreign corporation which such person controls (as defined in sec. 6038(d), as amended by the bill). Under existing law, the obligation to furnish information is imposed only on domestic corporations and only with respect to controlled foreign corporations and foreign subsidiaries of such controlled foreign corporations.

The requirements as to the information to be furnished are not changed except that (1) because of the redefinition of "control" including the addition of most of the constructive ownership rules of section 318(a) of the 1954 Code, there will be an increase in the number of persons whose transactions with controlled corporations must be reported, and (2) the Secretary of the Treasury or his delegate is authorized to require the furnishing of any other information which is similar or related in nature to that specified in paragraph (1) of section 6038(a) as amended by the bill.

Under the amendment made by section 20(a) of the bill, the period for which information is to be furnished under section 6038(a)(2) is modified to provide that, in all cases, such period is that ending with or within the U.S. person's taxable year. The amendment does not change the period with respect to a first-tier foreign corporation. However, with respect to a foreign subsidiary of such corporation, the period is changed from that ending with or within the first-tier corporation's annual accounting period to that ending with or within the U.S. person's taxable year. Thus, the effect of the amendment will be to obtain information which is more current from the subsidiary.

Section 6038(a)(3), as amended by the bill, is the same as existing law. It provides that no information will be required to be furnished under section 6038(a) with respect to any foreign corporation for any annual accounting period unless such information was required to be furnished under regulations in effect on the first day of such annual accounting period.

Section 6038(b), which sets forth the penalty for failure to file the required information within the prescribed time, is amended to provide that the reduction in foreign taxes paid or deemed paid now provided by section 6038(b) will occur in applying section 901 as well as section 902, although it will not occur under both sections with respect to the same tax. In addition, the reduction is to apply in respect of taxes deemed paid under section 960 of the code (added by sec. 12(a) of

the bill). Also, the penalty provided by section 6038(b), as amended by the bill, is extended to other than corporate taxpayers. Your committee has added a limitation on the penalty provided by section 6038(b) to the effect that the amount of the reduction in foreign tax credit under section 6038(b)(1) for each failure to furnish information with respect to a foreign corporation required under section 6038(a)(1) will not exceed the greater of (1) \$10,000, or (2) the income of the foreign corporation for its annual accounting period with respect to which the failure occurs.

The reduction in foreign taxes paid or deemed paid for failure to file the required information within the prescribed time is not to apply, however, in computing accumulated profits in excess of income, war profits, and excess profits taxes under section 902 (a) and (b) of the code (relating to foreign tax credit for a corporate stockholder of a foreign corporation) or under section 960(a) of the code (added by sec. 12(a) of the bill).

Section 6038(c), as amended by the bill, provides that where two or more persons are required to furnish information with respect to the same controlled foreign corporation for the same period, the Secretary of the Treasury or his delegate may prescribe that such information will be required only from one person. To the extent practicable, the Secretary's determination is to be based on actual ownership of stock (as distinguished from constructive ownership).

Section 6038(d) defines "control" as the possession of more than 50 percent of the combined voting power, or of the value, of all classes of stock. A person in control of a corporation which, in turn, owns more than 50 percent of the combined voting power, or of the value, of all classes of stock of another corporation is also treated as in control of such other corporation. Thus, for example, in the case of a chain of corporations consisting of corporation M, owning 51 percent of the voting stock in corporation N, owning, in turn, 51 percent of the voting stock in corporation O, owning, in turn, 51 percent of the voting stock in corporation P; corporation P is controlled by corporation M. The bill as passed by the House provided that the rules of section 318(a) apply in determining stock ownership, except that the rule which requires ownership of 50 percent of the stock of a corporation before stock owned by such corporation is attributed to its stockholders applies without regard to the 50-percent limitation. The constructive ownership rules apply in determining control of domestic and foreign corporations but not in determining, under section 6038(a)(1)(D)(iii), whether a transaction is with a corporation 10 percent or more of the value of any class of stock of which is owned by a U.S. person.

With respect to their application under section 6038, the bill, as amended by your committee, makes the following changes in the rules of section 318(a) as modified by the bill as passed by the House:

- (1) The rules that stock owned by or for a partner or a beneficiary of an estate or trust shall be considered as owned by the partnership, estate, or trust will not be applied so as to consider a U.S. person as owning stock owned by a person who is not a U.S. person, nor will a corporation be considered as owning stock owned by or for a 50 percent or more shareholder where the effect is to consider a U.S. person as owning stock which is owned by a person who is not a U.S. person.

(2) The rule that requires ownership of 50 percent (the bill as passed by the House removed this limitation) of the stock of a corporation before stock owned by such corporation is attributed to its stockholders has been modified by substituting the phrase "10 percent" for the phrase "50 percent."

(3) The rule that attributes to a corporation stock owned by or for persons owning the stock of such corporation will not apply.

The amended section 6038(d) defines the "annual accounting period" of a foreign corporation as the annual period on the basis of which such corporation regularly computes its income in keeping its books.

Section 6038(e) provides cross-references to sections 7203 and 7701(a)(30), respectively, for provisions relating to penalties for violations of section 6038, and for the definition of the term "U.S. person."

(b) *Information as to organization or reorganization of foreign corporations and as to acquisitions of their stock.*—Subsection (b) of section 20 of the bill amends section 6046 of the 1954 Code.

Paragraph (1) of section 6046(a), as amended by the bill as passed by the House, required an information return from each U.S. citizen or resident who, on January 1, 1963, was an officer or director of a foreign corporation or who became such an officer or director at any time after that date. In lieu of this provision, the bill, as amended by your committee, requires an information return from each U.S. citizen or resident who is on January 1, 1963, an officer or director of a foreign corporation, 5 percent or more in value of the stock of which is owned by a U.S. person, or who becomes such an officer or director at any time after such date.

Paragraph (2) of section 6046(a) requires each U.S. person to file an information return under any of the following circumstances:

(1) He owns 5 percent or more in value of the stock of a foreign corporation on January 1, 1963.

(2) He owns stock of a foreign corporation on January 1, 1963, which has a value of less than 5 percent of the value of the stock of such corporation, or owns no stock on January 1, 1963, and thereafter acquires stock which, when added to the stock held on January 1, 1963, if any, has a value equal to 5 percent or more of the value of the stock of such foreign corporation.

(3) He acquires an additional 5 percent or more in value of the stock of a foreign corporation.

Paragraph (3) of section 6046(a) requires each person who becomes a U.S. person after January 1, 1963, while owning 5 percent or more in value of the stock of a foreign corporation to file an information return.

Example.—A, a U.S. person, who on January 1, 1963, owns 2 percent in value of the stock of foreign corporation M, is not required to file an information return under section 6046. However, when he acquires, on April 1, 1963, an additional block of stock consisting of 4 percent in value of the stock of such corporation, he is required by subparagraph (A) of section 6046(a)(2) to make an information return with respect to corporation M. If, on December 31, 1964, he acquires a 6-percent block of stock in addition to that already owned, he is required to file a return under subparagraph (B) of section 6046(a)(2). He is not required to report when, on May 1, 1965, he acquires an

additional 3-percent block of stock, but he is required to report under subparagraph (B) when, on November 30, 1965, he acquires a 4-percent block of stock because the last two blocks of stock total more than 5 percent.

Subsection (b) of section 6046, as amended by the bill as passed by the House, was the same as existing law. It provided that the information returns required by subsection (a) of section 6046 shall be in such form and shall set forth, in respect of the foreign corporation, such information as the Secretary of the Treasury or his delegate prescribes by forms or regulations as necessary for carrying out the provisions of the income tax laws. Your committee has added a provision which limits the information which may be required of persons described in subsection (a)(1) to the names and addresses of persons described in subsection (a)(2).

Subsection (c) of section 6046 is amended by omitting the definition of "U.S. shareholder". The term "U.S. person", as used in sections 6038 and 6046, as amended by the bill, has the same substantive meaning as the term "U.S. shareholder" in existing section 6046.

Subsection (d) of section 6046, as amended by the bill, provides a limitation on the time for filing a return required by subsection (a) of such section. Such return must be filed on or before the 90th day after the day on which, under any provision of section 6046(a), the U.S. citizen, resident, or person becomes liable to file such return.

Your committee has redesignated subsection (e) of section 6046 (as amended by the bill as passed by the House) as subsection (f) and added a new subsection (e) which provides that no information shall be required to be furnished under section 6046 with respect to any foreign corporation, if the liability of the U.S. citizen, resident, or person to file a return under subsection (a) arises on or after January 1, 1963, and before March 1, 1963, unless such information was required to be furnished under regulations which have been in effect since January 1, 1963 (but only if such regulations were prescribed before December 1, 1962); or, if the liability of the U.S. citizen, resident, or person to file a return under subsection (a) arises on or after March 1, 1963, unless such information was required to be furnished under regulations which have been in effect for at least 90 days.

Subsection (f) of section 6046, as amended by the bill, is a cross-reference to section 7203, relating to willful failure to file a return, supply information, or pay tax.

(c) *Civil penalty for failure to file return.*—Subsection (c) of section 20 of the bill amends subchapter B of chapter 68 (relating to assessable penalties) by adding new section 6679.

Subsection (a) of section 6679, similar in purpose to section 6677 (relating to failure to file information returns with respect to certain foreign trusts) as added by section 7(g) of the bill, provides that in addition to any criminal penalty provided by law, any person required to file a return under section 6046 who fails to file such return at the time provided in section 6046, or who files a return which does not show the information required pursuant to such section, must pay a penalty of \$1,000, unless it is shown that such failure is due to reasonable cause.

Subsection (b) of section 6679 provides that subchapter B of chapter 63 (relating to deficiency procedure for income, estate, and gift taxes) is inapplicable in respect of the assessment or collection of any penalty imposed by subsection (a).

(d) *Technical amendments.*—Subsection (d) of section 20 of the bill contains technical amendments adding a cross-reference to section 318 of the code and conforming the appropriate table of sections to the change in the heading of section 6046.

(e) *Effective date.*—Under subsection (e) of section 20 of the bill, section 6038 of the code as amended by the bill is to apply with respect to annual accounting periods of foreign corporations beginning after December 31, 1962, and section 6046 of the code as amended by the bill is to take effect on January 1, 1963. Under subsection (e)(1), existing section 6038 will continue to apply in respect of a foreign corporation or foreign subsidiary whose annual accounting period begins before January 1, 1963. For example, assume that D, a domestic corporation, has a taxable year beginning July 1, 1963, and ending June 30, 1964. F, a foreign corporation controlled by D, has an annual accounting period beginning January 1, 1963, and ending December 31, 1963. FS, a foreign subsidiary of F, has an annual accounting period beginning April 1, 1962, and ending March 31, 1963. Under the effective date provision, information with respect to FS's annual accounting period beginning April 1, 1962, and ending March 31, 1963, is to be furnished under existing law, and information with respect to F's annual accounting period beginning January 1, 1963, and ending December 31, 1963, is to be furnished under section 6038 as amended by the bill.

SECTION 21. EXPENDITURES BY FARMERS FOR CLEARING LAND

Section 21 of the bill, which is a new section added to the bill as passed by the House, amends the Internal Revenue Code of 1954 by adding a new section 182, relating to the tax treatment of expenditures by farmers for clearing land.

Subsection (a) of section 182 permits farmers to elect to treat as deductible expenses, rather than as nondeductible improvements to property, expenditures for clearing land if such expenditures are for the purpose of making the land suitable for use in farming.

Subsection (b) of section 182 limits the deduction under subsection (a) for any taxable year to \$5,000, or to 25 percent of the taxable income derived from farming during the taxable year, whichever amount is the lesser. For purposes of such 25-percent limitation, the term "taxable income derived from farming" means the gross income of the taxpayer derived from farming during the taxable year, that is, the gross income of the taxpayer from the production of crops, fruits, or other agricultural products or from livestock, reduced by the allowable deductions which are attributable to the business of farming other than the deduction allowed by section 182. Thus, all of the ordinary and necessary expenses paid or incurred in the business of farming, including amounts allowed as deductions by sections 175 and 180 for soil and water conservation expenditures and for lime and fertilizer expenditures, respectively, but not including the amount allowed as a deduction by section 182 for expenditures for clearing land, should be deducted from gross income derived from farming in computing the taxable income derived from farming for purposes of applying the 25-percent limitation on the amount deductible as an expenditure for clearing farm land.

The term "clearing of land" is defined in subsection (c)(1) of section 182 to include, but is not limited to, the eradication of trees, stumps, and brush, the treatment or moving of earth, and the diversion of streams and watercourses. Your committee's amendment has application only in respect of expenditures paid or incurred in the clearing of land for the purpose of making such land suitable for use in farming. The term "land suitable for use in farming" means land which as a result of the clearing of land, as described above, is suitable for use by the taxpayer or his tenant for the production of crops, fruits, or other agricultural products or for the sustenance of livestock.

Subsection (d)(1) of section 182 provides that the expenditures to which section 182(a) applies do not include expenditures for the purchase, construction, installation, or improvement of structures, appliances, or facilities which are of a character which is subject to the allowance for depreciation. In addition, such expenditures do not include any expense which is deductible under any other section of the code.

Subsection (d)(2) of section 182 provides that expenditures to which section 182(a) applies shall include a reasonable allowance for depreciation with respect to property which is used in the clearing of land for the purpose of making such land suitable for use in farming and which if used in a trade or business, would be property subject to the allowance for depreciation. Under present law such depreciation must be capitalized. Such subsection (d)(2) further provides that to the extent an amount representing a reasonable allowance for depreciation with respect to property used in clearing land is treated as an expenditure to which subsection (a) applies, such expenditure shall, for purposes of chapter 1 of the 1954 Code, be treated as amount allowed under section 167 for depreciation of such property. Under this provision, proper adjustment to the basis of such property would be made under section 1016(a) of the 1954 Code.

Subsection (e) of section 182 provides that the taxpayer shall make the election to deduct his expenditures for clearing his land within the time prescribed by law (including extensions thereof) for filing his return for any taxable year in which he pays or incurs such expenditures, and that such election shall be made in such manner as the Secretary of the Treasury or his delegate may by regulations prescribe. Once the election is made for any taxable year such election may not be revoked without the consent of the Secretary of the Treasury or his delegate.

SECTION 22. CHARITABLE CONTRIBUTIONS MADE FROM INCOME ATTRIBUTABLE TO SEVERAL TAXABLE YEARS

Section 22 of the bill, which is a new section added to the bill as passed by the House, amends section 1307 of the Internal Revenue Code of 1954 by adding a new subsection (e) thereto. Section 1307 relates to rules applicable to part I of subchapter Q of such code which part relates to income attributable to several taxable years.

Part I of subchapter Q provides a limitation with respect to the tax imposed on certain amounts received or accrued by an individual taxpayer during a taxable year. The tax attributable to any such amount for the taxable year in which it is received or accrued is, in general, not to be greater than the aggregate increases in taxes which would have resulted if the amount had been included in the taxpayer's

income, on an allocated basis, over the period specified in the applicable section of such part I.

It is the present position of the Internal Revenue Service that in computing tax in accordance with part I of subchapter Q the adjusted gross income for the taxable year in which the amount was received or accrued shall be computed without regard to that portion of such amount which is allocated to other taxable years. (See, Internal Revenue Mimeograph 43, 1952-2 C.B. 112.) The amounts allowable as deductions under section 170, relating to charitable, etc., contributions and gifts, and under section 213, relating to medical, dental, etc., expenses, are based upon percentages of adjusted gross income. The computation of adjusted gross income without including that portion of the amount received or accrued which is allocated to other taxable years results in a determination of adjusted gross income which is less than would be the case if adjusted gross income for the taxable year in which the amount was received or accrued were computed without regard to part I of subchapter Q. A lower adjusted gross income figure for the taxable year decreases the allowable deduction for charitable contributions and increases the allowable medical deduction.

New subsection (e) provides that an individual who receives or accrues in a taxable year an amount to which part I of subchapter Q applies may elect (in such manner and at such time as the Secretary of the Treasury or his delegate prescribes by regulations) to apply the provisions of subsection (e) in computing his tax liability under such part. If the taxpayer so elects, the amount received or accrued shall be reduced, for the purposes of computing his tax liability under such part I with respect to such amount, by an amount (1) which bears the same ratio to the amount of his allowable charitable deduction for the taxable year in which the amount was received or accrued (computed without regard to pt. I of subch. Q) as (2) the amount received or accrued during the taxable year to which part I applies bears to the adjusted gross income for such year (computed without regard to pt. I of subch. Q).

The last sentence of new subsection (e) provides that no portion of the amount received or accrued to which part I of subchapter Q applies shall (for purposes of computing the limitation on tax under such part) be taken into account for purposes of computing the limitation under section 170(b)(1) of the code for the taxable year in which the amount to which such part applies is received or accrued.

Example.—Assume the following facts with respect to individual I (who elects to have the new subsection (e) apply) for the taxable year 1963:

(1) Amount received or accrued to which pt. I of subch. Q applies.....	\$12, 000
(2) Adjusted gross income (determined without regard to pt. I of subch. Q).....	16, 000
(3) Deductible charitable contributions (determined without regard to pt. I of subch. Q).....	1, 600

Assume further that, for purposes of computing the limitation on tax under part I of subchapter Q, the \$12,000 amount is to be prorated in equal amounts to the taxable years 1960, 1961, 1962, and 1963.

Under the first sentence of the new subsection (e), for purposes of computing the tax liability of the taxpayer under part I, the \$12,000 is reduced by \$1,200 (that portion of the \$1,600 deductible charitable contributions which \$12,000 is of \$16,000). The remainder, \$10,800,

is then prorated at the rate of \$2,700 per year to 1960, 1961, 1962, and 1963.

Under the last sentence of the new subsection (e), for purposes of computing the limitation on tax under part I, the \$12,000 amount is not to be taken into account for 1963 for purposes of computing the limitation under section 170(b)(1) on the amount deductible for charitable contributions during 1963. Thus, for this purpose, the adjusted gross income is to be treated as being \$4,000 (the amount remaining after excluding \$12,000 from \$16,000).

SECTION 23. EFFECTIVE DATE OF SECTION 1371(c) OF THE INTERNAL REVENUE CODE OF 1954

Section 23 of the bill, which is a new section added to the bill as passed by the House, relates to the effective date of section 1371(c) of the Internal Revenue Code of 1954.

(a) *In general.*—Subsection (a) of section 23 of the bill provides that section 1371(c) of the code, which was added by section 2(a) of the Act of September 23, 1959 (Public Law 86-376), shall (notwithstanding the provisions of the first sentence of sec. 2(d) of such Act) also apply to taxable years beginning after December 31, 1957, and before January 1, 1960. Section 1371(c) provides that stock which is community property of a husband and wife (or the income from which is community income) under the applicable community property law of a State, or is held by a husband and wife as joint tenants, tenants by the entirety, or tenants in common, shall be treated as owned by one shareholder. The first sentence of section 2(d) of Public Law 86-376 provides that section 1371(c) is to apply to taxable years beginning after December 31, 1959. Under your committee amendment, if the provisions of subsections (b) and (c) of section 23 of the bill are met, section 1371(c) will now be applicable for all taxable years for which a corporation may elect to be taxed as an electing small business corporation under subchapter S (secs. 1371-1377) of the code.

The enactment of this new effective date for section 1371(c) does not relax or otherwise change the requirements of any of the provisions of subchapter S. Thus, in order to be eligible to be treated as an electing small business corporation for years beginning after December 31, 1957, and before January 1, 1960, a "small business corporation" must have filed a timely election for such year in accordance with section 1372 and in the manner prescribed by the Secretary of the Treasury or his delegate by regulations. Such election must have been valid in all respects except that by reason of counting a husband and wife owning stock of a corporation in the specified joint forms or as community property as two shareholders, the corporation failed to meet the requirement that a small business corporation must have 10 or fewer shareholders. Furthermore, shareholder consents to such elections must have been filed in the prescribed time and manner. However, the Commissioner has announced that he will consider, upon request, the granting of extensions of time for the filing of consents in certain cases under section 1.9100-1 of the Income Tax Regulations.

If all the requirements, except the 10-or-fewer-shareholder requirement, had been met for taxable years beginning after December 31, 1957, and before January 1, 1960, and the effect of applying the new effective date of section 1371(c) is to reduce the number of shareholders

to 10 or fewer, the election shall be treated as a valid election, and the corporation shall be treated as an electing small business corporation for the year of the election and all succeeding years (unless, even though sec. 1371(c) is applicable, the election has been terminated for any reason) if the corporation and the shareholders meet the requirements of subsections (b) and (c) of section 23 of the bill. The earlier effective date provided in subsection (a) is also available in those situations where the initial election was valid, but where a termination in a subsequent taxable year beginning before January 1, 1960, is attributable solely to the fact that, by counting a husband and wife owning stock in joint form or as community property as two shareholders, the corporation had more than 10 shareholders and thus failed to meet the definition of a small business corporation. In such a case, if the corporation and shareholders elect and consent as provided in subsections (b) and (c) of section 23 of the bill, such termination shall be disregarded, and such corporation shall be treated as an electing small business corporation for the year of the termination and all succeeding years (unless, even though sec. 1371(c) is applicable, the election has been terminated for any reason).

(b) *Election and consent by corporations; consent by shareholders.*—Subsection (b) of section 23 of the bill prescribes rules which must be complied with if the earlier effective date provided in subsection (a) is to apply with respect to any electing small business corporation and its shareholders.

Subsection (b)(1) provides that the earlier effective date for section 1371(c) shall not apply unless the corporation elects, within 1 year after the date of the enactment of the bill, to have the earlier effective date apply and consents to the application of subsection (c) (relating to tolling of statutes of limitations). Both the election to have the provisions of subsection (a) apply and the consent to the application of subsection (c) are to be made in such manner as the Secretary of the Treasury or his delegate prescribes by regulations.

Under subsection (b)(2), each shareholder of the corporation must consent to the corporation's election, and must also consent to the application of subsection (c), within 1 year after the date of the enactment of the bill. These consents, which must be filed in such manner and at such time as the Secretary of the Treasury or his delegate prescribes by regulations, are required of each person who is a shareholder of the corporation on the date the corporation makes the election under subsection (b)(1), and of each person who was a shareholder of the corporation at any time during any taxable year of the corporation beginning after December 31, 1957, and ending before the date of such election. It is contemplated that the election and consent by the corporation under subsection (b)(1) and the consents by its shareholders under subsection (b)(2) will be filed together.

(c) *Tolling of statutes of limitations.*—Subsection (c) of section 23 of the bill provides for a tolling of the statutes of limitations with respect to (1) the assessment of deficiencies, and (2) the credit or refund of overpayments, which are attributable to the application of the earlier effective date provided in subsection (a).

Subsection (c)(1) provides that if the assessment of any deficiency against the corporation making such election, or against any shareholder of such corporation who consents to such election, for any taxable year is prevented, at any time on or before the expiration of 1

year after the date of such election, by the operation of any law or rule of law, assessment of such deficiency may, nevertheless, be made, to the extent such deficiency is attributable to the application of subsection (a), at any time on or before the expiration of such 1-year period.

Subsection (c)(2) provides that if credit or refund of any overpayment of tax by the corporation making such election, or by any shareholder of such corporation who consents to such election, for any taxable year is prevented, at any time on or before the expiration of 1 year after the date of such election, by the operation of any law or rule of law, credit or refund of such overpayment may, nevertheless, be allowed or made, to the extent such overpayment is attributable to the application of subsection (a), if claim therefor is filed on or before the expiration of such 1-year period.

SECTION 24. CERTAIN LOSSES SUSTAINED IN CONVERTING FROM STREET RAILWAY TO BUS OPERATIONS

Section 24 of the bill, which is a new section added to the bill as passed by the House, relates to certain losses sustained in converting from street railway to bus operations.

(a) *In general.*—Subsection (a) of section 24 of the bill provides that if a corporation has a net operating loss for the taxable year ending December 31, 1953, or the taxable year ending December 31, 1954, principally as the result of conversion from street railway to bus operations with respect to part or all of the company's operations, then its unused conversion loss (as defined in subsec. (b)) will be subject to the treatment provided in subsection (c).

(b) *Unused conversion loss defined.*—Subsection (b) of section 24 of the bill defines an "unused conversion loss" as the aggregate of the net operating losses for the taxable years ending December 31, 1953 and 1954, reduced to the extent that they have been used as net operating loss carryovers or carrybacks to reduce taxable income for any taxable year beginning before January 1, 1960.

(c) *Treatment of unused conversion loss.*—Subsection (c) of section 24 of the bill provides that if a taxpayer has an unused conversion loss, it shall be treated by such taxpayer as a net operating loss for the taxable year ending December 31, 1959, in determining the amount of the net operating loss carryover from such taxable year to each of the 5 taxable years following such taxable year. Subsection (c) applies, however, only for years in which the taxpayer is engaged in the furnishing or sale of transportation (as defined in sec. 1503(c)(1)(A) of the 1954 Code).

(d) *Regulations.*—Subsection (d) of section 24 of the bill authorizes the Secretary of the Treasury or his delegate to prescribe by regulation such rules as may be necessary to carry out the purposes of this section.

SECTION 25. PENSION PLAN OF LOCAL UNION NO. 435,
INTERNATIONAL HOD CARRIERS' BUILDING AND
COMMON LABORERS' UNION OF AMERICA

Section 25 of the bill, which is a new section added to the bill as passed by the House, provides that the pension plan of Local Union No. 435 of the International Hod Carriers' Building and Common Laborers' Union of America, which was negotiated to take effect May 1, 1960, pursuant to an agreement between such union and the Building Trades Employers Association of Rochester, N.Y., shall be held and considered to have been a qualified trust under section 401(a) of the Internal Revenue Code of 1954, and to have been exempt from taxation under section 501(a) of such code, for the period beginning May 1, 1960, and ending April 20, 1961, but only if it is shown to the satisfaction of the Secretary of the Treasury or his delegate that the trust has not in this period been operated in a manner which would jeopardize the interests of its beneficiaries.

SECTION 26. CONTINUATION OF A PARTNERSHIP YEAR
FOR SURVIVING PARTNER IN A TWO-MAN PARTNER-
SHIP WHERE ONE DIES

(a) *Close of taxable year of two-man partnership when one partner dies.*—Paragraph (1) of subsection (a) of section 26 of the bill is a clerical amendment the effect of which is to designate the text of section 188 of the Internal Revenue Code of 1939 as subsection (a) of section 188.

Paragraph (2) of subsection (a) of section 26 of the bill amends section 188 of the Internal Revenue Code of 1939 (relating to different taxable years of partner and partnership) by adding a new subsection (b). The new subsection (b) provides that for purposes of chapter 1 of the 1939 Code, if the surviving partner so elects within 1 year after the date of enactment of this bill, the death of one of the partners of a partnership consisting of two members shall not result in the termination of the partnership or in the closing of the taxable year of the partnership with respect to the surviving partner prior to the time the partnership year would have closed if neither partner had died or disposed of his interest.

(b) *Effective date, etc.*—Subsection (b) of section 26 of the bill provides that the amendments made by section 26 of the bill are to apply with respect to taxable years of a partnership beginning after December 31, 1946, to which the Internal Revenue Code of 1939 applies. Subsection (b) further provides that if refund or credit of any overpayment resulting from the application of the amendment made by new section 188(b) (including interest, additions to the tax, and additional amounts), is prevented on the date of enactment of this bill, or within 1 year from such date, by the operation of any law or rule of law (other than sec. 3760 of the Internal Revenue Code of 1939 or sec. 7121 of the Internal Revenue Code of 1954, relating to closing agreements, and other than sec. 3761 of the Internal Revenue Code of 1939 or sec. 7122 of the Internal Revenue Code of 1954, relating to

compromises), such refund or credit or such overpayment, may, nevertheless, be made or allowed if claim therefor is filed within 1 year after the date of enactment of this bill. Furthermore, no interest shall be allowed or paid on any overpayment resulting from the enactment of this section.

SECTION 27. TREATIES

Section 7852(d) of the 1954 Code provides that no provision of the 1954 Code shall apply in any case where its application would be contrary to any treaty obligation of the United States in effect on August 16, 1954. The bill as passed by the House provided that section 7852(d) would not apply in respect of any amendment made by the bill, thus providing that in the event there was any conflict with any treaty provision (whether or not such provision was in effect on August 16, 1954) the provisions of the bill would govern. Your committee has stricken this provision and substituted for it an amendment providing that no provision of the bill shall apply in any case where its application would be contrary to any treaty obligation of the United States.

CHANGES IN EXISTING LAW

In the opinion of the committee, it is necessary, in order to expedite the business of the Senate, to dispense with the requirements of subsection 4 of rule XXIX of the Standing Rules of the Senate (relating to the showing of changes in existing law made by the bill, as reported).

INDIVIDUAL VIEWS OF SENATORS HARRY F. BYRD, ALBERT GORE, JOHN J. WILLIAMS, AND CARL T. CURTIS ON SECTION 2 OF H.R. 10650

We oppose section 2 of the 1962 revenue bill (H.R. 10650) which would give a 7-percent tax credit to segments of business for investment in new machinery and equipment.

Our opposition to this section of the bill is based on firm convictions after full consideration of views expressed by competent witnesses in exhaustive hearings, and those expressed in voluminous correspondence from the general public.

We have given closest possible study to statements in behalf of the administration's recommendations made before the Senate Finance Committee which, in some respects, are at variance with provisions now in the section.

Before adopting the "investment credit" (sec. 2) provisions as reported, the Senate must consider the fact that the Internal Revenue Service on July 11, 1962, substantially revised its regulations to accelerate regular depreciation.

Our position is in accord with views of a vast number of citizens, including those representing industry, business, labor, and agriculture throughout the Nation, who have testified and counseled for rejection of the provisions of section 2.

Hearings on the pending bill were held over a period of 4 months, and a substantial portion of the testimony taken was directed to section 2. Generally, our conclusions may be summarized, but the detail must be considered, too.

In summary, we oppose "investment credit" as it would be provided by section 2 for numerous reasons including the facts that—

- (1) It would be a subsidy in the nature of a windfall to be given to businesses which comply with a Government policy.

- (2) It would be discriminatory in its application among various businesses, even among those similar in kind.

- (3) Its value and its need as a stimulant to so-called "economic growth" are both questionable and doubtful.

- (4) Its continuing cost would be heavy and it would increase the Federal deficit in the current fiscal year.

WOULD INCREASE DEFICIT

There was a Federal deficit of \$6.3 billion in fiscal year 1962 which ended June 30. There will be another deficit in the current fiscal year which started July 1. The "investment credit" provisions in H.R. 10650 would increase the 1963 deficit by \$630 million (net).

The staff of the Joint Committee on Internal Revenue Taxation, using officially budgeted expenditures, estimates that—

- (1) The Federal deficit in the current fiscal year 1963 will be more than \$3.9 billion, excluding the effect of this bill.

(2) This Federal deficit would be increased by a total of more than \$1 billion if H.R. 10650, as passed by the House of Representatives, were enacted; and

(3) The Federal deficit estimate would have to be increased by a total of \$630 million (net) if the bill, as reported by the Senate Finance Committee, were enacted.

If H.R. 10650—in either the House or the Senate committee version—were enacted, a substantial portion of the estimated increase in the Federal deficit would be directly attributable to the effect of the “investment credit” provisions alone. The Joint Committee staff estimates that—

(1) Under the House-passed version of the “investment credit” provisions, revenue in fiscal year 1963 would be reduced by \$1.3 billion; and

(2) Under the Senate committee version of the “investment credit” provisions, revenue in fiscal year 1963 would be reduced by \$650 million (gross).

If the “investment credit” provisions of section 2 remain in this bill and the measure is enacted, they will become permanent in the law. For this reason it is appropriate for the Senate at this time to examine the long-range budgetary effects.

When this is done, the enormity of the revenue loss becomes even more clear, and the budgetary effect becomes even more significant. Extending application of the “investment credit” provisions over an 11-year period (1962–72), the Joint Committee staff finds that—

(1) Business tax liabilities would be reduced during that period by \$21 billion under the House-passed version; and

(2) Business tax liabilities would be reduced during that period by \$15.6 billion under the Senate committee version.

Revenue loss resulting from application of the new depreciation guidelines made effective by the Treasury Department on July 11, 1962, would be in addition to revenue loss resulting from the “investment credit” provisions in this bill if they were enacted.

The Treasury has estimated that in their first year of operation the recent revisions in Internal Revenue Service rules on depreciation will result in a reduction in business tax liabilities of \$1.5 billion. Estimates for subsequent years have not been made.

WRONG IN PRINCIPLE

The “investment credit” proposed in section 2 of this bill is wrong in principle. It would be discriminatory in its application. It would do harm to our tax structure. It would not achieve so-called “growth” in investment. It is not needed under existing conditions.

Under terms of the bill, those complying with the “investment credit” provisions would be entitled to a tax credit which could be offset directly against income tax liability. Coupled with depreciation, “investment credit” would return to the investor more than he paid for the asset.

It should be made clear for the record and the information of the Senate that the tax “credit” would not be included in taxable income. If a corporate tax rate of about 50 percent were assumed, an “investment credit” of \$7 would be equal to \$14 of additional income before taxes in the year.

Under existing law and Internal Revenue Service regulations the cost of *plant*, machinery, and equipment generally may be depreciated 100 percent over specified periods; and depreciation has been accelerated under the new rules now in force.

Under the current administration proposal and House bill provisions "investment credit" for new machinery and equipment would be in addition to 100-percent depreciation. Under the Senate committee version of the bill the "investment credit" would be in addition to 93-percent depreciation.

The administration proposed an 8-percent "investment credit" (with public utilities excluded) on new machinery and equipment in addition to 100-percent depreciation. The effect of this would be to give investors generally 116 percent of what they paid for the asset.

The House bill generally would give a 7-percent "investment credit" for new machinery and equipment, with a 3-percent "credit" for public utilities, in addition to 100-percent depreciation. This would allow investors up to 114 percent of what they paid for the asset.

The Senate committee bill generally would give a 7-percent "investment credit" for new machinery and equipment, with 3 percent for public utilities, in addition to 93 and 97 percent depreciation respectively. This would allow investors up to 107 percent of what they paid for the asset.

Evidence given in hearings on this bill clearly shows that "investment credit" is both wrong in principle and unnecessary. Numerous witnesses, including those representing four major segments of the economy, opposed the principle involved.

In view of the testimony in the published record on this proposal, it is difficult to understand the persistence of the "investment credit" advocates. Leaders of industry, business, labor, and agriculture all have appeared before the Senate Finance Committee to oppose it.

Stanley H. Ruttenberg, research director, AFL-CIO, urged the committee to "delete this provision from the bill," because those he represented thought:

It is a multibillion-dollar windfall that will not really contribute anything to our national goals and will not relieve our balance-of-payments problems as it is claimed.

Walter Slowinski, appearing in behalf of the U.S. Chamber of Commerce, with respect to the "investment credit" provisions, said:

The chamber again recommends against the adoption of this novel and untried preferential tax credit subsidy for business. It is also unnecessarily complex, and it will be difficult to administer.

Harold H. Scaff, chairman, Tax Committee, National Association of Manufacturers, said "investment credit"—

would simply provide reduction in effective tax rates for taxpayers who use their income and other funds as the Government thinks is best for the economy at a particular time.

There has been a tendency to promote and discuss the investment tax credit apart from the price which it would exact in terms of other changes in the tax law. Even without the exaction of such a price, we would oppose the credit

for the reasons set forth in the appendix attached hereto. Very simply, we believe that tax reductions should be afforded by direct means. We would take this position even if, in our opinion, all of the other provisions of H.R. 10650 constituted sound tax policy.

Charles B. Shuman, president, American Farm Bureau Federation, took the position that—

these provisions are both unsound and likely to have a number of undesirable effects. It would be far better to liberalize the treatment of depreciation and work toward a general reduction in income tax rates.

The proposed investment credit is a selective form of tax relief—in reality a subsidy. * * * The result would be to give some taxpayers a competitive advantage at the expense of others.

Although the Farmers Union did not send a representative to testify directly before the Finance Committee, a communication signed by James G. Patton, president, National Farmers Union, published in the congressional record of March 29, 1962 (p. 4984), said:

Urge your influence to delete provision giving huge private corporations operating at less than full capacity over \$1½ billion and private electrical power monopoly over \$100 million in tax subsidies which would result in the flight of capital overseas and further aggravate the dollar crisis.

The “investment credit” proposal would be discriminatory in obvious respects. It would discriminate against companies which were recently modernized, against poorer companies, and against companies needing new buildings with or without new machinery and equipment.

The very fact that “investment credit” would give special tax reduction only to those companies able and willing to invest in new machinery and equipment means that those who for any reason were unable to make such investments would be subjected to discrimination.

Struggling small companies unable to provide the funds for qualifying investments would not be eligible for the “credit,” but their more prosperous competitors could reap a windfall from the Federal Government through special tax treatment.

None of the proposals—administration, House bill, or Senate committee bill—would give “investment credit” for new buildings or structural components. It is difficult to imagine installing expensive modern machinery and equipment in an old, outmoded building.

INEFFECTIVE AND QUESTIONABLE

Plans for new facilities contemplated by advocates of the “credit” are formulated far in advance. Many of those who would benefit from the proposal would have developed their improvements without the incentive of “investment credit.”

In such cases the “credit” would be of questionable value as a stimulant to “economic growth.” On the other hand, the proposal offers neither incentive nor immediate means of expansion for companies which are hard pressed for capital.

A recent McGraw-Hill survey developed the consensus that this "investment credit" proposal would increase 1962 investments by only about \$300 million, or 1 percent. This raises the question of the effectiveness of section 2 as a stimulant for increased investment.

Witnesses before the Finance Committee also raised the question as to the effectiveness of "investment credit" in this respect. For example, Augustus W. Kelley, representing the Proprietary Association, said:

The theory of the tax incentive in our opinion is based on the false premise that business investments are motivated substantially by tax considerations. In our industry, and we believe it is typical of others, the decision whether or not to invest in new machinery and equipment is based primarily on pure business consideration. Simply stated, we are not going to spend \$1 just because the Government gives us 7 cents.

Otis H. Ellis, speaking for the National Jobbers Council, said:

This tax credit will not be enough to induce a single jobber to buy one item more than what he would otherwise have purchased.

The McGraw-Hill survey, previously referred to, indicates that without the "investment credit" business investments in plant and equipment this year may be expected to reach some \$38 billion. This would be \$1 billion more than the previous record set in 1957.

If \$38 billion is spent in new plant and equipment this year, it will exceed such investments of last year by \$3.5 billion or 11 percent; and the same survey finds reason to expect continuing high level of investment for the period of 1963-65.

We believe the sound way to achieve a reduction in taxes is first to cut unnecessary Federal expenditures as a means of putting the Nation on a sound financial basis.

We do not believe that tax reductions should be discriminatory by favoring some taxpayers over others in the manner inherent in the "investment credit" proposal or otherwise.

We believe that revisions in the Federal revenue structure should not create new discriminatory and artificial distinctions among taxpayers such as this proposal would establish in the law.

We believe our attention should be directed toward reducing rather than increasing such inequities.

HARRY F. BYRD.
ALBERT GORE.
JOHN J. WILLIAMS.
CARL T. CURTIS.

ADDITIONAL VIEWS OF SENATOR EUGENE J. McCARTHY ON H.R. 10650

In my opinion, neither section 2 of this bill, on the investment credit, or section 12, on controlled foreign corporations, provides an adequate solution to what are admittedly two important problems, and neither of these two sections is defensible in terms of equity or of administrative simplicity which should characterize our tax system.

INVESTMENT CREDIT

The tax credit for "qualified investment" is designed to stimulate what has been termed "a sluggish economy." I have no argument with the fact that our economy would profit from modernization of plant and equipment and from the expansion of certain productive facilities—even though we have substantial underutilization of productive capacity in many areas—but I question whether a selective and hence discriminatory tax credit is the cure for the Nation's investment maladies or economic problems. In my opinion, comprehensive business tax relief in the form of a general reduction in the corporation income tax, together with an across-the-board reduction in personal income tax rates, will better meet these needs by freeing money both for new investment and for consumption without binding business decisions to Government decisions and without creating the problem of distinguishing between qualified investment and nonqualified investment.

The investment credit as it stands in this bill today is but a pale representation of the original administration proposal. In his testimony before the Committee on Ways and Means in May 1961, Secretary Dillon said:

* * * the purpose of the investment credit is not to provide general tax reduction for recipients of profit income. Rather it is to stimulate investment in the most efficient manner. The credit, therefore, should be focused on investment which would not have been undertaken without this inducement, and which will be most responsive to the stimulus which it provides.

Originally the administration recommended a 15-percent tax credit, most of which would have been available only for plant and equipment expenditures in excess of current depreciation allowances. A 6-percent credit was provided for certain investment below the level of these allowances, and a 10-percent credit on the first \$5,000 of investment was provided whether it was more or less than depreciation allowances. The credit was not to be limited to tangible personal property, but also was to be available for most buildings and their structural components as well. The credit also was not to exceed

30 percent of a firm's tax liability. A 5-year carryforward of unused tax credits was provided.

The investment credit which passed the House in March of this year contained the following major changes: (1) A tax credit of 7 percent was granted on all new investment in eligible property, regardless of current depreciation allowances; (2) public utilities, excluded from any credit under the administration plan, were allowed a 3-percent credit; (3) the full credit was made available for assets with a useful life of 8 years or more and scaled down for assets with a useful life of 4 to 8 years; (4) the credit was limited to \$25,000 plus 25 percent of a company's tax liability over this amount; (5) the property eligible for the credit excluded buildings and structural components as well as certain other property.

The Senate Finance Committee has made further changes, adding a 3-year carryback for unused tax credits, changing the effective date of the credit from January 1, 1962, to July 1, 1962, and stipulating that the depreciable base of property eligible for the credit shall be reduced by the amount of the credit.

The result of most of these changes has been to reduce the impact of the investment credit. Section 2 is now little more than a tax-relief measure, but the relief is restricted in its application to certain firms investing in certain types of property.

What is wrong with the investment credit provided in this section? In the first place it is highly selective as to the type of investment which may qualify and as to the time when this investment must have been made. Individual air-conditioning units qualify but central air-conditioning systems do not; transient hotels qualify but residential hotels do not; cattle fences qualify but the cattle themselves do not. How are we to make sense out of a provision which substitutes the Federal Government's wisdom for that of the private sector in ascertaining what type of investment is required for the economic health of individual business enterprises? Not only does the section differentiate between types of assets, but it also makes an arbitrary determination, based on the expected life of the asset, as to how much, if any, credit will be allowed.

Furthermore, the credit discriminates between investment undertaken before and after July 1, 1962, in effect rewarding those business concerns which have for one reason or another failed to modernize and to expand prior to the effective date of this section. How can we justify a plan which announces to one group of businesses that they invested too early and are, therefore, not eligible for the 7-percent credit while telling another that they have waited until the proper time, that they have waited until the Government can step in with a special inducement for technological developments?

Secondly, the credit would be granted for qualified investment irrespective of the plans or obligations of a particular business. This is most obvious in the case of public utilities but applies also to any firm which has faith in the dynamism of the American economy and in the stability of our political and social institutions. Many businessmen have commented that the tax credit would have slight, if any, effect on their investment plans. Considered in this light, section 2 is, in a sense, a windfall which would benefit some of our industrial giants, leaving smaller and depressed businesses in the same cash-shy position as before. In the final analysis new investment is

dependent not upon a taxsaving of perhaps 1 or 2 percent of a company's estimated income tax, but upon the company's expectations of profits through the marketing of its goods or services. Businessmen invest because they have reason to believe that they will sell. Most business witnesses indicated preference for accelerated depreciation, together with straight tax reduction.

The Treasury's new depreciation schedule which went into effect in July of this year is a step in the right direction and, in my opinion, should be carried even further.

There is near unanimity among leaders of both labor and management that the investment credit is unsound and ill-suited to the problem which it seeks to solve.

CONTROLLED FOREIGN CORPORATIONS

Provisions of this bill for taxation of controlled foreign corporations threaten to upset established business practices both at home and abroad at a time when economic conditions throughout the world are changing rapidly and when nations are attempting to reevaluate and redefine their trade positions. Testimony before the Finance Committee indicated that the competitive position of many American firms operating in foreign countries may be seriously jeopardized because of the uncertainty and because of the penalties in this section.

Many American corporations have established subsidiaries abroad in order to take advantage of business opportunities in an expanding international economy. Subsidiaries have been set up to protect old markets and to penetrate new ones. These actions have increased the domestic business of the companies, have created jobs for U.S. workers, and in the case of most firms have resulted in a dollar return to the United States from the oversea business in excess of the amount invested abroad.

Many changes have been made in this section of the bill since the administration's initial recommendation of last year. The original proposal was to eliminate tax deferral for all controlled foreign corporations except operating subsidiaries in developed countries.

The House-passed bill eliminated deferral for the so-called foreign-base company income of tax havens unless it was reinvested in less-developed countries, and for operating subsidiaries unless their income was reinvested in the same business outside of the United States or in a less-developed country. Now the Finance Committee has adopted amendments which would leave the tax deferral for manufacturing subsidiaries intact while continuing tax deferral for foreign-base company income only if it is earned, as well as reinvested, in less-developed countries. The committee also voted to include income from services within the definition of foreign-base company income and to permit deferral if certain minimum distributions are made to U.S. shareholders, according to a formula which takes into account the effective tax rate of the foreign country in which the subsidiary is located. Finally, tax deferral has been continued for companies which qualify as export trade corporations.

In addition to these fundamental changes, there have been a number of other modifications. The definition of controlled foreign corporations affected by section 12 has changed; the tax treatment of patents sold or transferred to foreign subsidiaries has changed; cor-

porations organized in Puerto Rico or possessions of the United States have been exempted; greater recognition of the losses of foreign subsidiaries has been provided; and there have been many other changes.

These changes improved the bill, but are of limited good and do not eliminate the basic difficulties which would result from the passage of this section.

Many American firms would suffer in trying to compete with foreign competitors which enjoy the tax advantages while locating where they will. Companies with contractual commitments or indebtedness abroad would face an uncertain future, as would companies which can sell abroad only through sales subsidiaries because their volume is insufficient to justify expenses of establishing and operating a plant. This section would, in fact, serve as an invitation to foreign countries to increase their taxes on American subsidiaries, as such taxes can be credited against the U.S. taxes.

In a broader sense, the controlled foreign corporations provision erects a barrier to the achievement of vital national objectives, namely the expansion of trade and an improvement in our balance-of-payments position. We cannot promote either of these related objectives through a restrictive policy which, in the hope of correcting tax abuses, slashes with a broad sword at America's oversea subsidiaries.

In addition, section 12 raises certain constitutional questions. Can the United States tax a corporation's income to the shareholder before it is realized by the latter? Does the bill discriminate between different classes of shareholders in contravention of the fifth amendment? Would the United States be acting in violation of treaty obligations with foreign nations?

There are controlled corporations which have been established in foreign countries primarily, if not solely, for purposes of tax avoidance here in the United States. It is also true that some of these subsidiaries probably serve no real purpose as far as the interests of the United States are concerned. We should not throw the baby out with the bath water but should reconsider the means by which we undertake to correct abuses.

The fact that this section as originally proposed by the Treasury has been changed drastically in the House and Senate suggests strongly that this approach to oversea income is far too complex in its administration, far too selective in its application, and far too uncertain in its effects.

WITHHOLDING

The Senate Finance Committee eliminated the section which imposed withholding tax on interest and dividend income. This section had been proposed as a means of collecting a substantial portion of the estimated \$850 million per year of taxes on interest and dividend income which, either because of ignorance of the law or dishonesty, is not paid. On the proposition that every person should pay his just taxes there can be no disagreement. The proposition, on the other hand, that to achieve this objective we should shift the burden of collection from the Government to the private sector of the economy and create unprecedented administrative complexities is, I believe, open to serious challenge.

Withholding on wages cannot be compared directly with withholding on interest and dividends. The former is imposed on the principal source of income for the vast majority of Americans. In most cases

an individual derives his wages or salary from a single source rather than from several sources as in the case of many taxpayers who receive interest and dividends. Even though our law provides for withholding from zero to 18 percent on wages and salaries, according to income and exemptions claimed, there has been overwithholding on as many as 40 million returns in a single year. In the case of interest and dividends, where a flat 20 percent would be withheld, we could expect overwithholding, in proportion to the number of returns with taxable income from these sources, to be considerably higher than overwithholding on wages and salaries. The quarterly refund and exemption certificate procedures included in the House bill would not alleviate the hardship and inconvenience created for many taxpaying citizens and institutions, and would, of course, complicate still further an already difficult administrative task.

One of the time-honored criteria of a good tax system is administrative simplicity and ease of compliance. The proposed withholding tax, with its exceptions and complications, would burden payors, recipients, and the Government itself. The collection of withholding on interest payments would be especially difficult because of the large number of small accounts, but similar difficulty exists with reference to dividend payments. Estimating tax liability and determining the exempt or nonexempt status of each interest and dividend recipient, knowing when an individual's status may change and adjusting his records accordingly, learning which types of payments are exempt, applying credits for individuals, governmental units, and tax-exempt organizations—these are among the many problems which would arise. Plans to apply the withholding tax more selectively, either by exempting persons with annual incomes of \$5,000 or less or by exempting payments of \$10 or less per year on any one account, would introduce additional complexities.

It appears that attempts to introduce equity into withholding only complicate its administration, while attempts to ease administrative problems would only result in serious inequities.

There is good reason, I believe, to expect much improved compliance in the future with existing tax laws, partly because of a public information program on the part of business and Government. Automatic data processing will soon be in operation and should help the Government to enforce tax laws while standing as a modern, mechanical reminder to taxpayers of their obligations. Section 19 of this bill now requires interest and dividend payors to report to the Government all payments of \$10 or more during the year and to furnish each such recipient with a statement of his aggregate amount of payments. The Federal Government has required that every person who files a tax return be assigned an identification number which shall appear on all of his tax documents. Perhaps the Internal Revenue Service may even devise an improved tax form which would give greater prominence to interest and dividend income.

Together, all of these should add up to much improved reporting of interest and dividends and improved collections. Certainly for the sake of the taxpayer, businessmen, and the Internal Revenue Service, these methods should be tried more thoroughly. Only if these efforts and methods prove inadequate after fair and full trial, should withholding methods be applied.

EUGENE J. MCCARTHY.

DISSENTING VIEWS OF SENATORS FRANK CARLSON,
WALLACE F. BENNETT, JOHN MARSHALL BUTLER,
CARL T. CURTIS, AND THRUSTON B. MORTON ON
SECTION 11—FOREIGN SOURCE INCOME, H.R. 10650,
AS AMENDED BY SENATE FINANCE COMMITTEE

The provisions for the taxation of foreign source income as set forth in sections 11 and 15 of H.R. 10650 as reported to the Senate are truly amazing. Eleven volumes of hearings by the Committee on Finance have been published since April 2, 1962. They include the testimony of 200 witnesses and statements by 300 additional taxpayers. In spite of virtually unanimous opposition by witnesses from industry, agriculture, the accounting and legal professions, and distinguished academicians and economists, these amendments are now before the Senate. The enactment of these provisions will produce no appreciable revenue, will have an ultimate adverse effect on our balance of payments, will discourage U.S. foreign investments, will hamper our export trade, and will invite retaliation and generate friction with our friends and allies. If the provisions of these sections are enacted into law, normal trade relations will be seriously disturbed.

There is a serious question as to the constitutionality of the basic concept of taxing the earnings of foreign subsidiaries which have not been constructively received by U.S. taxpayers.

Section 11 proposes that a tax be imposed on increase in net worth which has long been held unconstitutional. If such a theory is accepted as proper, there is no reason why every stockholder would not be assessed a tax on the increase in the value of his security during any given period of time, whether such an increase has been a taxable gain or not.

Section 11 completely disregards corporate legal entities, legitimate in purpose or otherwise. It disregards the spirit, if not the letter, of existing tax treaties and conventions which have taken years to negotiate by both Republican and Democrat administrations. It provides for a tax on imputed income. If a U.S. domestic taxpayer has not received funds to pay this tax, it must be paid by reducing the availability of funds for employment or investment in this country.

It encourages U.S. direct investment in foreign securities rather than in U.S. owned and operated foreign subsidiaries. Clearly such investments will reduce America's competitive position in world markets and in all likelihood will have an additional adverse effect on our short and long term balance of payments position.

It imposes an unfair competitive burden on foreign subsidiaries of U.S. corporations, since no foreign government imposes similar taxes on local competitive enterprises. It establishes undue hardships resulting from differences in accounting practices employed by foreign versus U.S. companies. Section 11 provides that the accounting

practices applicable to domestic corporations shall govern the determination of foreign source income on which a tax is to be levied. Necessarily, in most instances this will require the maintenance of two sets of books and accounts—one to meet the needs of the foreign operation and the second to determine U.S. tax liabilities. This procedure will impose unwarranted costs on many small enterprises. Furthermore, if a subsidiary has a substantial foreign minority interest, the entire cost of duplicate records will have to be borne by the domestic, parent corporation, thus reducing its income and tax liability to the Federal Government. It would create a powerful incentive to the governments of foreign countries to levy special taxes on the income of subsidiaries of U.S. companies.

Necessarily the determination of subpart F "income" includes the conversion of foreign earnings into dollars at the existing rate of exchange which may be favorable or unfavorable at the time. If a tax is paid to the Federal Government by the U.S. parent corporation and at a subsequent date the exchange rate between the dollar and the foreign currency is changed, there is no recourse by the U.S. parent corporation for the unjust enrichment to the U.S. Government.

Furthermore, the language contains unprecedented delegation to the Secretary of the Treasury or his delegate to prescribe by regulation concepts which should be embodied in substantive legislation itself. The delegations leave so much to administrative fiat that they represent an abdication of congressional authority over taxation. By their terms, they warn business that the tax burden is subject to change by administrative decree. This fact alone inhibits orderly planning and makes the risks of capital investment abroad very uncertain.

There is also the possibility that in some instances American interests in foreign operations will be transferred to foreign firms because of their inability to finance the payment of these additional taxes. Such an eventuality would greatly weaken the U.S. competitive position in world markets.

Section 15 "Sales and Exchange of Patents to Certain Foreign Corporations" as reported to the Senate once again abandons long established practices and discriminates against American corporations doing business abroad. It would tax the sale and exchange of capital assets in a different manner than they are taxed in domestic transactions. Since the proponents of this legislation have stressed the need for neutrality of taxation on foreign and domestic activities, these discriminatory provisions clearly show that neutrality is not provided in this proposed legislation.

The enactment of these provisions will be bewildering to American business and to the Internal Revenue Service itself. They will foster serious litigation and demand court interpretation before the true meaning of the language reported by the committee can be applied to actual business transactions.

THE ADMINISTRATION'S OBJECTIVES

President Kennedy first presented his tax recommendations to the Congress on April 20, 1961. They included basic changes in the concepts for the taxation of foreign source income. His message suggested that existing law which does not tax the unrepatriated earnings of foreign subsidiaries had played an important role in

recent years but that it should now be abandoned. The President stated that:

Changing economic conditions at home and abroad, the desire to achieve greater equity in taxation, and the strains which have developed in our balance of payments position in the last few years, compel us to examine critically certain features of our tax system which, in conjunction with the tax system of other countries, consistently favor U.S. private investment abroad compared with investment in our own economy.

* * * Many American investors properly made use of this deferral in the conduct of their foreign investment. Though changing conditions now make continuance of the privilege undesirable, such change of policy implies no criticism of the investors who so utilize this privilege.¹

It should be noted that the President clearly stated that he did not regard the so-called principle of deferral as an improper practice or a form of tax evasion. However, there is an implication that so-called deferral represents a privilege, and is a relatively new concept in our tax laws and perhaps was enacted in order to promote the aims of the European recovery program under the Marshall plan. This is not a fact, as the basic concepts of taxation applicable to foreign-source income have been included in the Internal Revenue Code since its inception in 1913. Furthermore, they are found in the tax laws of every other country.

Secretary Dillon, in his appearance before the House Ways and Means Committee, in May 1961, advocated the elimination of deferral in developed countries as he believed such action would further several desirable objectives. They included the improvement of our balance-of-payment position, increased U.S. tax revenues, the achievement of "tax neutrality," which, in turn, he suggested, would result in additional domestic employment by the promotion of added exports and encouragement for additional investment in the less-developed countries of the world.

Extensive hearings were conducted by the Ways and Means Committee, and representatives of every sector of the business community appeared in opposition to this marked change in the concept of taxation. Their testimony clearly showed that the operation of foreign subsidiaries promoted our exports, and that the balance-of-payments position had been favorably affected by the existence of direct foreign U.S. investments. In fact, Secretary Dillon conceded that after a period of approximately 17 years, our balance-of-payments position would be damaged by discouraging any further direct U.S. foreign investment as the administration recommended. When such changes are proposed, there must be compelling and convincing reasons.

U.S. direct foreign investments total more than \$50 billion. They constitute one of the Nation's most valued assets. If, as a result of the enactment of this measure, foreign investments by American firms are discouraged, the economy of this country will be adversely affected.

The testimony presented before the House Ways and Means Committee clearly showed that over the 15-year period ending in 1960,

¹ President's 1961 Tax Recommendations, hearings before the Committee on Ways and Means, House of Representatives, 87th Cong., 1st sess., vol. 1, p. 8.

receipts from direct investment exceeded current outflows by nearly \$10 billion. Certainly this data does not support the contention that foreign direct investments adversely affect our balance of payments.

The testimony also showed that the taxes levied on the remittance of dividends to U.S. parent corporations on their direct overseas investments have been a substantial source of income to our Government. The witnesses who appeared showed that it was impossible to accomplish "tax neutrality" in the sense advanced by the administration. True neutrality must respect the business facts of life and insure that competition may take place on a basis of neutrality in the marketplace.

The Congress of the United States cannot determine the tax laws that will be applicable in other countries, not only with respect to their own nationals but to those of other countries as well.

Furthermore, the hearings before the Ways and Means Committee clearly showed that there was no basis to support the contention that by restricting investments overseas, additional investment would occur in the United States—thus providing employment opportunities for our people and increased exports. On the contrary, the testimony indicated that virtually every U.S. firm would prefer to operate entirely within the jurisdiction of the United States, and export its production to world markets. However, a multitude of reasons have necessitated the establishment of foreign operations if the United States is to enjoy its share of participation in foreign markets. U.S. firms are confronted with a choice of either abandoning these markets or of establishing appropriate facilities to meet the competition already present or which is expected to be established to penetrate such markets.

The concepts originally advanced by the administration in 1961, with modifications to meet the more obvious discriminations, are the basis for H.R. 10650 as reported by the Committee on Finance. While this measure is still supported as a means of providing what the administration chooses to call "tax neutrality," it is quite apparent that no enactment by the Congress could achieve this result.

Our citizens should be in a position to compete in any country of the world with the nationals of other developed nations. Such competition may take the form of exports from the United States, licensing of patents and processes to a foreign firm, or the operation of manufacturing and distribution facilities in foreign countries. The decision as to the best combination of business activities must be determined on the basis of all of the factors involved in a given market as well as whether firms established in other nations are free to make what, to them, appears the most desirable economic choice. It is a disservice to place American firms in a position where their freedom to compete is restricted.

Contrary to the views advanced by the administration, American business does not go abroad because of a more favorable tax climate, but because on the basis of business judgment, it appears that a profit can be achieved by establishing a foreign operation. Business is rarely confronted with a choice of exporting or operating abroad. It is rather the choice of whether to abandon a market entirely or to seek a competitive position therein. In spite of the refutation of the arguments advanced by the administration, the House of Representatives passed H.R. 10650.

The preponderance of the evidence presented to the House Ways and Means Committee and to the Committee on Finance clearly shows that none of the objectives the administration is seeking to achieve would be furthered through the enactment of its proposals with respect to the taxation of foreign-source income.

HEARINGS BY THE COMMITTEE ON FINANCE

Section 13 of H.R. 10650, as passed by the House of Representatives, did not completely eliminate the administration's so-called tax-deferral privilege. Accordingly when the Committee on Finance started its hearings on April 2, the administration once again urged that its original proposals for complete deferral be accomplished by amendments to H.R. 10650. Secretary Dillion stated that:

H.R. 10650, as passed by the House of Representatives, apart from tax havens, deals only peripherally with tax deferral for foreign income, another important tax preference now accorded foreign, as compared with domestic, corporate income. It responds to the President's recommendation in this area only insofar as it specifies that the undistributed foreign income of U.S. subsidiaries operating abroad will be subject to U.S. tax, as it is earned, unless it is reinvested in substantially the same trade or business already conducted by the firm in question, or in a less-developed country.

By not treating the tax-deferral issue fully and directly, the bill still retains a substantial tax advantage for investment abroad rather than at home. The privilege of deferring U.S. taxes until income is repatriated as dividends should simply be eliminated for our subsidiaries in advanced industrial countries, as the President has requested. The deferral privilege should be retained, for income earned in less-developed countries, in line with our general foreign policy objectives.²

The Secretary endeavored to develop the need for this legislation. He stressed that it would serve two purposes: The first, an improvement of our balance-of-payments position, and second, it would contribute to Federal revenues. However, as the hearings proceeded, several major inconsistencies in the administration's position were developed.

The testimony which had been presented before the House Committee on Ways and Means clearly established that U.S. direct investments had generated a return flow of capital over the past 15 years that was a major factor in preventing a serious balance-of-payments crisis. Nevertheless, Secretary Dillon advanced a new concept by conceding that while the overall balance of payments on all U.S. direct investments abroad was favorable, the return flow on new investments was insufficient in comparison with the current outflow. He testified as follows:

Now, certainly, we agree that if the investment is profitable, if it works well over the long term, it should begin to return funds back home and should return enough to offset

² Revenue Act of 1962, Hearings Before the Committee on Finance, U.S. Senate, 87th Cong., 2d sess., on H.R. 10650, pt. I, p. 99.

the outflow, and should be an asset. That is why we believe in foreign investment, and it should be made in years when you have substantial surpluses, and it should be there to help you in years when you have deficits in your balance of payments. * * *

Now, many of the statements that were made last summer before the Ways and Means Committee, which were made after our original presentation, did make it appear that this investment was profitable for balance-of-payments purposes sooner than we think is the case. But the big problem there was that they always compare, every time that I have seen it, the income that is received from investments that have been made over the past 10, 15, or 20 years, with the immediate dollar that goes overseas, and actually that is not a relevant comparison.

At the moment, the facts are that we have a total investment overseas of about \$50 billion, and we are getting a net return out of the investment—compared to the net against the new investment that has gone overseas—a net return of about \$200 million, and that is much too small at this time.

We think this is a time when we should be getting some net benefits in our balance of payments from our investments overseas.³

A number of observations are in order with respect to these statements. The formation of the European Economic Community has built a common external tariff barrier around a rapidly expanding market. This has forced U.S. firms to establish new operations within the Community. This single fact accounts for the large outflows to Western Europe during recent years. A single transaction involving the purchase of a foreign interest in the subsidiary of a U.S. firm accounted for a very large portion of the total outflow to Western Europe during 1960. It is idle to suggest that any new investment could possibly generate a return comparable to the investment itself within a few years after its establishment.

It appears strange that the administration would jeopardize the long-term benefits in order to provide a temporary correction of the short-term imbalance. The mere fact that the Secretary of the Treasury concedes that within a comparatively few years, new investments will make substantial contributions to our balance of payments, makes his position untenable. If the \$50 billion of foreign investments overseas were not in existence, our present balance-of-payments problem would be acute. If the policies of taxation advanced by this administration had been adopted by the Congress a few years ago, this national asset would not be in existence. Should the Congress follow the Secretary's proposal, it will certainly not continue to grow and provide a greater positive factor in our overall balance-of-payments picture.

It appears likely at this time that for many years to come, perhaps for a generation, there will be a continuing need for foreign assistance and the military support of our allies to prevent further Communist aggression. In this context, the long-term needs of our economy extend far beyond the period that would be benefited by an immediate

³ Ibid., pp. 447-448.

improvement in our balance of payments. However, the inconsistency in the Secretary's position with respect to the effectiveness of his proposal to eliminate tax deferral as a means toward the correction of an adverse balance of payments is shown in his statement before the committee on April 2. He said:

* * * Insofar as taxation is concerned, our foreign subsidiaries at most would feel the effect of elimination of the deferral privilege only through a reduction in retained earnings. If this portion of the retained earnings is needed in the business, the parent can pay the U.S. tax or supply the additional needed capital in other ways.⁴

If the U.S. parent pays the tax from domestic sources, there will be no effect on our balance-of-payments position. But capital which would otherwise be available to expand domestic investment in the private sector of our economy would be diverted to the public sector. Clearly the improvement of our balance-of-payments position cannot justify the enactment of section 11 with the many serious consequences to our overall world trading position it would entail.

The Secretary of the Treasury in his first appearance before the Committee on Finance on April 2 continued to stress the need to enact legislation to provide additional revenues. Yet the real impact of the administration proposals with respect to the taxation of foreign source income is revealed in the following colloquy between Senator Carlson of Kansas and the Secretary of the Treasury:

Senator CARLSON. I know you expressed your concern about our balance of payments. Is it not reasonable to assume that this legislation we are considering today is most important in our balance of payments rather than in the collection of taxes?

Secretary DILLON. I think that of the two elements involved here in the foreign field, that the most important one probably—it is difficult to say which is the most important one—but vitally important is, first, the balance of payments, as you say; and the other thing that is vitally important is the general principle of tax equity, with respect to the abuse of these foreign tax havens which has become a scandalous thing. It is not that everybody who uses them should be stigmatized that way, but they have been very seriously abused, and that is the second major reason they should be prohibited.

The third reason only is the extra revenue that will be obtained for the Government from that. I do not think it is tremendous compared to our overall revenues.⁵

It has long been the accepted view that the primary concern of the Congress in levying taxes is to provide funds for the operation of the Federal Government. If a complex measure which will impose burdens on most business enterprises with oversea activities and which will also complicate our international relations will not make a tremendous contribution to our overall revenues, it is strange that the administration would seek to secure the enactment of such provisions under these circumstances.

⁴ Ibid., p. 102.

⁵ Ibid., p. 449.

In short, the hearings before the Committee on Finance developed the same philosophy and facts as had been presented a year before to the House Committee on Ways and Means. No convincing evidence was presented to substantiate the view that the administration's proposals could either ultimately improve our balance-of-payments position or contribute substantially to the Federal revenue. Nevertheless, the administration has continued to seek approval of a new concept to impose a tax on the unremitted earnings of foreign corporations to American shareholders.

In order to secure the acceptance of this principle, the amendments incorporated in the present version of section 11 do not deal with tax deferral as stringently as section 13 of the bill which passed the House of Representatives. The administration has abandoned its efforts to seek the complete elimination of tax deferral as proposed by the Secretary of the Treasury on April 2. It is now prepared to accept a measure which permits deferral on operations conducted within a given country and even on a portion of what were considered base company earnings such as sales and management activities. Clearly, the issue before the Senate is not the correction of our balance-of-payments position nor the provision of revenues, but rather the acceptance or rejection of an unsound and unwise principle of taxation, which if adopted in the pending bill will establish a precedent for the extension of such a principle into countless other areas. This measure could have no significant impact on either our revenue nor our balance-of-payments position. It cannot promote exports nor contribute to the attainment of any of the objectives outlined by the administration in its original message on taxation to the Congress in 1961. On the contrary, the uncertainty and confusion which even the discussion of these proposals has engendered, deterred some worthy foreign investments. Insofar as direct foreign investments support exports, the continued efforts to secure the enactment of this legislation are a disservice to our citizens whether they be investors or employees seeking broader opportunities. Our farmers and miners, whose economic position is directly effected by the strength of our overall efforts in world markets also have a vital stake in this matter. It is apparent that many of our citizens are confused with respect to the impact of the proposed legislation on our domestic economy. Nevertheless, the testimony from every sector of the business community clearly shows that if these concepts are enacted into law, the welfare of our own citizens who may not realize they have a stake in direct foreign investments will be adversely effected.

COMPLEXITIES OF SECTION 11

The language proposed by the Committee on Finance in section 11 "Controlled Foreign Corporations" is unnecessarily complex and confusing. The attempt to impute an amount to be included in the gross income of U.S. shareholders based on the earnings of controlled foreign corporations necessarily presents difficulties that repeated amendments have been unable to clarify. The Congress under the Constitution is responsible for the enactment of legislation which clearly defines the tax obligations of our citizens. The substantive determination of tax liabilities should not be delegated to the executive branch of the Government.

Section 11 provides that many substantive matters are to be determined by the Secretary of the Treasury or his delegate. The number of instances in which the Congress would abdicate its constitutional responsibilities by this delegation of power suggests that the concepts underlying this proposed new section of the Internal Revenue Code have not been clearly defined and perhaps can never be so defined. The requirement that the determination of the earnings of controlled foreign corporations follow the concepts of the U.S. tax laws is unrealistic, since these corporations operate under the laws of other nations and the tax credits, the rules for depreciation, and numerous other basic concepts differ widely from the U.S. law and the rules and regulations for its implementation prescribed by the Secretary of the Treasury. Furthermore, earnings are computed in foreign currencies and the apportionment of the U.S. parent corporation's share of such earnings requires their conversion into dollars at an arbitrary value. The language in the proposed amendment does not provide for the return to the taxpayer of any taxes that were paid on unrepatriated earnings that subsequently could not be realized in equivalent dollars because of currency devaluation or other factors operative after the assessment of the U.S. tax. The language in section 964, subsection b, "Blocked Foreign Income," provides:

(b) **BLOCKED FOREIGN INCOME.**—Under regulations prescribed by the Secretary or his delegate, no part of the earnings and profits of a controlled foreign corporation for any taxable year shall be included in earnings and profits for purposes of Sections 952, 955 and 956, if it is established to the satisfaction of the Secretary or his delegate that such part could not have been distributed by the controlled foreign corporation to United States shareholders who own (within the meaning of section 958(a)) stock of such controlled foreign corporation because of currency or other restrictions or limitations imposed under the laws of any foreign country.⁶

However, it fails to grant relief for taxes paid prior to the time that earnings could not be transferred. Furthermore, the assessment of a tax unrepatriated earnings insures that the U.S. Government derived revenue even though such earnings are based on accounting procedures which anticipate levels of activity for future income which may not be attained.

The burden of maintaining the records and accounts provided in subsection C of section 964 will impose additional costs on domestic parent corporations, as in almost every instance it will be necessary to maintain duplicate sets of records and accounts—one, to conform with the accounting procedures of the foreign country in which the operation takes place, and the second, for the computation of U.S. tax liabilities.

These activities do not contribute to the productivity and growth of our economy. They are a luxury that we cannot afford at this critical juncture in world history.

The committee received testimony on behalf of a distinguished group of New York attorneys who are specialists in matters involving taxation.

⁶ H.R. 10650, 87th Cong., 2d sess., sec. 964, subsec. b.

Mr. Robert J. McDonald, a member of the group testified that:

We believe, however, that the present bill does not effectively distinguish between avoidance devices and legitimate business operations conducted outside of the United States.

Further, we believe the foreign income provisions are unworkable, are unduly penal in their impact on the foreign business of the U.S. persons, and may have many consequences that are clearly adverse to the interests of the United States.

The foreign income provisions are unworkable because they are so complex that they cannot reasonably be understood or administered, and because their application depends upon detailed historical and current information that will often be impossible or impractical to obtain.

They are unduly harsh and, in many cases, penal in effect in imposing burdens of taxation and of administrative compliance that are much more extensive than in the case of domestic operations, particularly in their impact on the individual foreign investor. Moreover, no opportunity is provided to adjust legitimate business arrangements established in reliance upon existing law and, indeed, at the urging of our Government.

These provisions would have numerous consequences that are clearly undesirable and often unintended. The substantially favor foreign competitors who are not subject to similar burdens, even though the committee report notes that one of its guiding policies is to avoid weakening the competitive power of American business abroad.

Now, in determining the pro rata share of a corporation's increase in earnings invested in nonqualified property, not only must there be a determination of the earnings and profits for the year and the earnings and profits accumulated since December 31, 1962, but there must also be a review of the financing business needs and underlying nature of the business of the foreign corporation and of any changes made therein.

To make these determinations requires the application of a series of imprecise concepts, and the availability of information extremely difficult to obtain.

The determination of earnings and profits for the year or for the period since December 31, 1962, of foreign corporations presents problems which will be insurmountable in a substantial number of cases.

These determinations are dependent not only on U.S. concepts of tax accrual, tax deferments, tax elections, basis, tax exempt income, amortization and depreciation, and numerous other items completely alien to the foreign corporations and foreign accountants, but it is also affected by reorganizations, liquidations, exchanges, and distributions in kind which may or may not be tax free by American standards.

There are no provisions whatsoever under the bill for making these determinations or provisions establishing the machinery therefor.⁷

The statement presented to the committee on behalf of these attorneys by Mr. McDonald included numerous examples to show the possible undesired consequences of enactment of the administration's proposals. The statement included a section on the unworkability of the bill which suggest that the Internal Revenue Service will be confronted with the same difficulties that were perceived by these attorneys in their examination of these provisions. Mr. McDonald stated:

The bill's provisions in respect of foreign income are so complex, overlapping, and replete with unprecedented tests that it is difficult to analyze them. The members of this group submitting this report are experienced in matters of tax law; they have spent over 40 hours in group discussion and countless hours of individual study reviewing the contents of the aforementioned sections. Despite this, the practical problems of working with the proposed legislation are so immense that the group has found it difficult to understand the bill and impossible to measure its full impact. So many new concepts are included in the bill that a definite technical analysis by tax practitioners has been virtually impossible. The complexity of its provisions can only cause uneven and arbitrary enforcement and administration of the bill. Skilled tax practitioners will undoubtedly find technical loopholes. On the other hand, many U.S. entrepreneurs will by chance find themselves caught by extremely harsh provisions of the bill which by proper planning could have been avoided. Revenue agents cannot be reasonably expected to understand the provisions or to enforce them uniformly. Thus, the impact of the bill will be haphazard.⁸

In view of the fact that the enactment of section 11 will make no significant contribution to Federal revenues nor will it improve our balance-of-payments position, it is inconceivable that the Congress would enact legislation which contains so many ill-defined, complex, and conflicting provisions.

ADVERSE EFFECTS

Many witnesses who appeared before the Committee on Finance expressed concern at the serious and unintended adverse effects which the enactment of this legislation would produce.

Mr. Leslie Mills, chairman of the Committee on Federal Taxation of the American Institute of Certified Public Accountants, testified that:

Not the least of the evils which would plague business if these sections are enacted is the authority given to the Treasury Department to make unilateral determinations affecting the tax burden of the domestic corporation. In

⁷ Revenue Act of 1962, Hearings Before the Committee on Finance, U.S. Senate, 87th Cong., 2d sess. on H.R. 10650, pt. 7, pp. 3137, 3139.

⁸ Ibid., pp. 3147, 3148.

many provisions authority is given to the administration, including the Treasury Department, to make unilateral determinations, from which no appeal appears possible. As one example, a formula is provided for allocating income under certain circumstances, with a further provision that intercompany prices may be determined on an arm's-length basis. However, determination of the arm's-length character of transactions is subject to rather rigid rules which may not give effect in every case to all of the pertinent factors. Moreover, if such arm's-length determinations by the taxpayer are not satisfactory to the Treasury Department, that Department through its agents can determine the allocations which in its sole judgment are proper, without any opportunity for an impartial appraisal. This, and similar approaches to these most difficult problems leave American business operating abroad entirely at the mercy of our bureaucracy. This uncertainty alone will surely cause American business to restrict operations abroad. It certainly creates no climate for new expansion. * * *

I have endeavored to point out that the complexities in this area, and in other parts of the bill, are by themselves serious. The very existence of uncertainties hampers business. Adding these complexities to the already complicated problems of doing business abroad will have the effect of discouraging many small businesses from expanding into the international trade area. The legislative history of the bill in the foreign income area emphasizes this important problem. Business enterprises have been forced to consider a regular series of proposals in the foreign area throughout the past year, and each one has required the immediate initiation of planning to avoid the severe and haphazard penalties which would be incurred under their present organization and manner of doing business. The latest proposals are only a few weeks old, and it cannot be expected that the picture is at all clear for the many organizations, large and small, which will be vitally affected. Yet the most basic provision, with respect to income of controlled foreign corporations, would become effective less than 9 months from now, and presumably just a few months after the final form of the provisions are known if they are approved by the Congress. The far-reaching provisions concerning liquidation and sale of stock would become effective upon enactment. At the very least, therefore, businesses should have more time to turn around and reorganize their activities to avoid possible destruction of their interests. It seems particularly inappropriate to legislate such far-reaching, new, and untried concepts in our tax structure at the very time when the Treasury Department is on record as preparing to release in the near future proposals for a basic reform of the tax structure.⁹

⁹ Revenue Act of 1962, hearings before the Committee on Finance, U.S. Senate, 87th Cong., 2d sess. on H.R. 10650, pt. 2, pp. 546, 547.

Another witness, Mr. Tyrone Gillespie, assistant to the president of the Dow Chemical Co., in his testimony stated:

If the foreign income concepts are enacted into law, our company and all other companies similarly situated will be faced with the severe problem of trying to determine whether the accounting principles and methods of our foreign subsidiaries are compatible with those in the United States, and whether in those cases where we have less than 100 percent ownership, it would be possible to do so in fairness, or at all, without full concurrence of other stockholders. In any case, it would be necessary to maintain two sets of records, one to comply with foreign law and one with U.S. law, and there is a question as to where such records should be kept.

In order to comply with U.S. law, much of the information will have to be estimated because data are not available under foreign accounting systems, and certainly companies will have a built-in and continuing argument with the Treasury Department as to whether their estimates are proper or improper. We are certain that the committee is cognizant of the vast enforcement costs which will be entailed for worldwide policing most of which will gain little revenue so we will not elaborate on this point.

Another question which gives us concern is our company's position if we disclose certain data and economic information of a company in a foreign country in which we are a part owner, where the laws of the country prohibit such disclosure. Does this U.S. law force us to commit economic espionage and thereby render us liable under the laws of our host country? ¹⁰

The uncertainty alluded to by the two witnesses just cited presents a serious problem not only for the business community but for the Congress, as indecision by responsible management at this time can result in a slackening in our economy growth and a failure to provide adequate job opportunities for our growing labor force.

Furthermore, such uncertainty will not only adversely affect the earnings of business enterprises but will result in a decline in Federal tax revenues. Dr. Dan Throop Smith, professor of finance at the Harvard Graduate School of Business Administration and a former Assistant Secretary of the Treasury, posed a number of problems which may beset American business should this legislation be enacted. He informed the committee that he was undertaking a study of all the possible consequences of the pending tax legislation. He summarized his observations as follows:

Many considerations are relevant to a decision on the taxation of foreign income. I know of no single area where it is so difficult to balance the conflicting objectives of policy.

I have already written a fair amount on the subject, but in recent months have become increasingly interested and concerned with it. I have recently returned from a trip to Western Europe which I took, in connection with current

¹⁰ Revenue Act of 1962, hearings before the Committee on Finance, U.S. Senate, 87th Cong., 2d sess. on H.R. 10650, pt. 8, p. 3667.

research activities, to determine attitudes and practices regarding the taxation of foreign income in some of the industrial countries there. I shall try to state here as concisely as possible what seem to be the most significant points, pending preparation of a longer article on the subject.

Foreign operating subsidiaries are in no sense artificial or unnatural legal entities. Contrary to many foreign holding companies, foreign operating companies are used as the natural and normal means of participating in a foreign economy.

They were used long before we ever had an income tax; in some instances they are required by foreign governments. They are necessary when joint ventures are developed with local capital. It is a misconception to think that they are established primarily for tax advantages.

Furthermore, operating subsidiaries abroad are in competition with other companies located abroad. American parent companies usually establish foreign subsidiaries to maintain a position in foreign markets or to secure a position in new markets.

They do not establish foreign operating subsidiaries as an alternative to expansion at home for production of export commodities. When foreign markets become large enough and foreign conditions for production good enough, production is going to take place abroad.

There are plenty of local companies able and anxious to expand to meet domestic requirements in foreign countries, and plenty of large corporations in other major industrial countries able and anxious to set up their own foreign subsidiaries, and active in doing so.

If our country is to get its rightful competitive share in the expanding income of the world, our business firms must be free to compete where production is taking place.

This point cannot be overemphasized. Someone is going to produce abroad; it is the very essence of economic development abroad that production will take place there. It is a serious misconception to believe that if American firms cannot produce abroad, no one will do so and that foreign demands will remain unsatisfied until filled by American exports.¹¹

He further stated:

As markets grow with the rapidly expanding standards of living in the Common Market, it is important to be in on the ground floor, as it were, to have brand names known, to establish distribution channels, and to act promptly in improving products and processes.

If a company falls behind, it can catch up, if at all, only with increased outlays. If it tries belatedly to secure entry into an established market, it can probably do so, if at all, only at greatly increased cost.

¹¹ Revenue Act of 1962, hearings before the Committee on Finance, U.S. Senate, 87th Cong., 2d sess., on H.R. 10650, pt. 7, p. 3089.

These are familiar facts of business which I shall not elaborate, but they should not be overlooked if an argument is made that we need only temporarily to restrain investment, or that old investment is good but new investment is bad, because it is not immediately recouped in repatriated profits.

Business investment must be a continuing dynamic process; if it is not continued as required, the value of old investments, and the possibility of continued repatriated income from them, will wither away.

To the best of my knowledge, and I have inquired carefully, no other country in any way taxes their own companies on the basis of undistributed income of foreign subsidiaries.

Furthermore, on the basis of extensive inquiries in Europe in recent weeks, there is no indication whatsoever that other countries would follow our example. There is some concern abroad about pricing on transactions between parent companies and foreign subsidiaries—the sort of problem covered by section 482—and in some instances about foreign personal holding companies.

But I found no indication that there was any concern about the undistributed income of foreign subsidiary operating companies or any likelihood that other countries would impose taxes on their own companies similar to those proposed here.

Nor does there seem to be any political controversy or even thought to the contrary on this subject. In one place when I asked if there were arguments to the effect that foreign subsidiaries might lead to a loss of domestic employment the answer was “No; it is recognized that we must have worldwide activities to support the cost of research and development to meet intense international competition. The ability to spread costs over the business of foreign subsidiaries helps assure continued domestic employment.”

This reflects the same high degree of sophistication found in most of the European labor groups which support, instead of opposing, liberal depreciation as a basis for increased productivity, which in turn leads to higher standards of living and increased employment.

But though other countries will not follow our example in taxing their own corporations on the basis of undistributed income of their foreign operating subsidiaries, it seems very likely that they will be tempted to impose their own special taxes on the U.S.-owned subsidiaries located in their countries.

Does it not seem probable that on practical grounds if there is to be any extra tax on undistributed income of U.S.-owned subsidiaries, the countries where the subsidiaries are incorporated and where the earnings are located will want to exercise their primary right to tax them?

I was asked more than once in my recent trip, by Europeans if I did not think that the countries where the subsidiaries were located would adopt their own laws to secure for themselves the revenue to be derived by new tax burdens imposed by the United States on undistributed income of foreign subsidiaries.

And, of course, I had to admit that I supposed they would.

The actions of many of our States in imposing soak-up estate taxes to absorb the credit allowed in the Federal estate tax is a perfect precedent. The adoption of anything like section 13 will invite foreign countries to impose their own taxes and it seems likely that many of them will accept the invitation.

To the extent that foreign countries do impose their own soak-up taxes, any expected revenue to the U.S. Treasury will disappear. Increased taxes imposed by our Congress would end up in foreign treasuries, not in the U.S. Treasury.¹²

The possibility of the imposition of new retaliatory taxes by foreign governments would completely destroy the efforts that have been constantly pursued to eliminate double taxation and other hardships which restrict the flow of commerce. It is difficult to reconcile the announced goals of the administration in the Trade Expansion Act of 1962 (H.R. 11970) with the isolationist views toward foreign investment encompassed in H.R. 10650.

A further possible adverse effect which is clearly unintended by the administration is the possible disposal of a sufficient interest in a presently controlled foreign corporation to the nationals of other countries so as to relieve the American parent of the burdens imposed by section 11. This would jeopardize U.S. control over many important trading and manufacturing activities which support our exports and employment in this country.

Again a colloquy between Mr. Robert J. McDonald, a New York attorney representing a group of tax lawyers, and Senator Kerr, of Oklahoma, is significant:

Mr. McDONALD. They encourage U.S. persons to take minority rather than controlling interests in foreign businesses, with the possible consequences, among others, of loss of a favored position with respect to the sale to such businesses of domestic products.

Senator KERR. Let me interrupt you there.

Mr. McDONALD. They encourage——

Senator KERR. I say, let me interrupt you.

Mr. McDONALD. I am sorry.

Senator KERR. You have just said that, in your judgment, this bill would encourage American investors to take minority positions in foreign corporations rather than American corporations creating subsidiaries in foreign areas.

Mr. McDONALD. We believe it might have that tendency.

Senator KERR. That was one of the points that Dr. Dan Throop Smith made with reference to the investment company which asked for the conference with him and discussed the probability of their increasing foreign stocks in their portfolios of investments, although they are American investment companies, I believe.

Mr. McDONALD. Generally speaking, an American investment company, assuming it is an investment company with

¹² Ibid., pp. 3090-3091.

wide distribution of its stock, would tend not to have a controlling position, and when I say controlling I mean more than a 50-percent interest in the foreign corporation.

Senator KERR. And to the extent that it encouraged investment in minority positions in foreign corporations, it would adversely affect our balance of gold payments rather than favorably affect them.

Mr. McDONALD. It may or may not. I think that is a complicated question. I think that——

Senator KERR. If a situation arose whereby Americans took American dollars and bought stocks from foreign owners and paid for them in American dollars that went over there, that would be adverse in our balance of payments, would it not?

Mr. McDONALD. Temporarily it might.

Senator KERR. Well, the only way that those dollars could come back would be for those sellers to send them back.

Mr. McDONALD. That is correct. And if you did not have controlling positions in those companies there would be less tendency for them to find their way back.

Senator KERR. It would seem to me you were making a point which, I think, is of some significance, and I was asking you the questions only to let the record clearly reflect that as your judgment, if that is your judgment.

Mr. McDONALD. I believe it is.¹³

During the course of the interrogation of Mr. Charles W. Stewart, who appeared in opposition to the administration's foreign tax proposals on behalf of the Machinery and Allied Products Institute, Senator Morton, of Kentucky, presented a hypothetical question which is a further cause for concern in connection with the Senate's consideration of this legislation. The colloquy between Senator Morton and Mr. Stewart follows:

Senator MORTON. Now, you talked to the point of constitutionality which we have dealt with in a rather cursory manner this morning.

I happen to be one of those rare Members of this body who is a businessman and not a lawyer. Sometimes I think the United States would be better off if we were more of us and fewer lawyers here.

As I see the situation in my lay mind, it is comparable to this: Let us suppose that a trucking company in Kentucky had 10 stockholders. Five lived in Tennessee and five in Kentucky.

Let us assume that they made \$100,000 after taxes in 1 year. They decided they would pay \$25,000 in dividends, that they would retain \$75,000 in the business for the purpose of buying new trucks and expanding their operations.

The State of Tennessee has an income tax law. The State of Tennessee would say to those five Tennessee stockholders "but you must pay an income tax based on the earnings of this Kentucky corporation in which you own stock in the

¹³ Op. cit., Revenue Act of 1962, pt. 2, p. 678.

amount of four times what you paid because they earned \$100,000 and they only paid \$25,000 in dividends.”

Admitting that is an oversimplification, is that not to a lay point of view somewhat analogous to this constitutional question?

Mr. STEWART. I think you are a much better lawyer than you admit, sir.

I would say that you draw a point here that worries me beyond the scope of this bill.

It seems to me we are breaking new ground if we go to the full route of these provisions in terms of applying the same principle to our domestic tax policy. I am quite concerned about it, and your example is ecompletely on the beam in that respect.¹⁴

There would be no difficulty in continuing to review other adverse situations which could be most damaging to our economy that were presented to the Committee on Finance by witnesses experienced in every sector of the American economy.

Friendly foreign countries are already concerned with the administration's proposal, and the record of the hearings includes a press account to the effect that President Chiari of Panama has advised President Kennedy that the administration's tax proposal represents “undue interference in the internal affairs of Panama.”¹⁵

President Chiari also declared that the taxation of the earnings of Panamanian corporations on profits which have been unremitted is “almost equivalent to economic aggression.”¹⁶

The Swiss too have expressed similar concerns.

The vagueness of the administration's concepts are illustrated by a colloquy between the Secretary of the Treasury and Senator Curtis of Nebraska.

Senator CURTIS. * * * Will you define a tax haven company?

Senator DILLON. What we have done is not to define a tax haven company specifically, but to define in effect a tax haven transaction. For example, a tax haven transaction is one where a company incorporated in country A purchases from country B and resells in country C.

So in this situation there have to be three countries involved and the use of the words “tax haven company” is just a short description of companies which operate in this way. We do not have a definition of a company as a tax haven company.

Senator CURTIS. I understand it is not in the proposal, but this is presented to the country and to this committee as reference to a tax haven company, and there are people in Congress and out that are concerned about tax haven companies.

So, I would like to have a definition of the company you are speaking about when you use this term, not the name of the company but what constitutes a tax haven company.

¹⁴ Op. cit., Revenue Act of 1902, pt. 2, p. 678.

¹⁵ Revenue Act of 1962, hearings before the Committee on Finance, U.S. Senate, 87th Cong., 2d sess., H.R. 10650, pt. 1, p. 653.

¹⁶ Ibid.

Secretary DILLON. Well, I have already given a definition to the Senator. It means companies that operate in the way I have described, that are domiciled in a country, generally a very low-tax country; that do business in two other countries. We can give you a list of names of these countries if you desire.

Senator CURTIS. Now, a tax haven company is one that does business with two other companies in two other countries.

Secretary DILLON. What I have said is that in a tax haven transaction where there are two other countries involved, and one of them may be the United States.

It is also a transaction where income for a service, a commission for an item sold, a royalty for a patent, anything you wish, is received from one country by a corporation incorporated in another country.

Senator CURTIS. Now, are all such operations that you have described tax haven transactions?

Secretary DILLON. Not all such operations are necessarily tax haven transactions, and that is the specific reason why I requested in the statement I made yesterday that the Secretary of the Treasury be given authority to exempt specific transactions, specific operations that are not entered into for the purpose of tax avoidance.

I would say that three-quarters or 90 percent of the transactions that I have described are for the purpose of reducing taxes and would be tax haven transactions.

But there are some, and I can give you examples, which are not.

Senator CURTIS. Give me an example of one that is.

Secretary DILLON. One that is?

Senator CURTIS. Yes.

Secretary DILLON. A classic example of one that is, is a U.S. foreign subsidiary which has a manufacturing plant in England to make anything, condiments, if you will. It sells all its condiments that it sells on the Continent first to a U.S.-controlled Swiss sales corporation. They never go to Switzerland, but they are marketed in France, Germany, Belgium, everywhere else as the property of the Swiss sales corporation. The entire profit is lodged in Switzerland. The manufacturing company in Great Britain is paid a very small figure for the wholesale value and makes a minor profit.

That is the type of operation that clearly is a tax haven operation.

Senator CURTIS. Where does the U.S. Government come into the transaction you described?

Secretary DILLON. Where the United States comes in, in that transaction, is that these would be controlled foreign corporations the control of which is in the U.S. parent corporation.¹⁷

The complexities of transferring available funds from developed nations to investments in less developed countries will frustrate our

¹⁷ Revenue Act of 1962, hearings before the Committee on Finance, U.S. Senate, 87th Cong., 2d sess., H.R. 10650, pt. 10, pp. 4309-4310.

foreign policy objectives of encouraging private investment to assume a larger role in economic development—thus relieving the taxpayers of a portion of this burden.

The Secretary of the Treasury in his appearance before the Finance Committee on April 2 expressed the view that tax haven operations constitute a serious abuse, and he urged the committee to amend the bill as passed by the House of Representatives to completely eliminate tax deferral on the undistributed foreign income of U.S. subsidiaries operating abroad. Shortly thereafter, the Secretary addressed the Ninth Annual Monetary Conference of the American Bankers Association in Rome, Italy, on Friday, May 18. He expressed a somewhat different view as to the nature of American oversea investments in his discussion of this subject before a foreign audience. He stated:

The United States has consistently favored free capital movement the ability of individuals or companies to invest their funds where they will. There has been no change in that view. We are, however, asking our Congress to end the tax inducements to American investment in other industrialized countries, particularly the inducements which flow from the mushrooming use of so-called tax havens. The object is not to discourage capital from going abroad in search of higher gross return. That sort of investment will, in the long run, serve the investor, the United States, and the recipient country alike. We recognize that the great bulk of our foreign investment is of this type and is not tax induced. We do, however, want to make sure that our tax system does not unwittingly—and artificially—spur this outflow. We wish only to eliminate marginal foreign investment that is induced primarily by tax considerations. While there is no expectation that such action will dramatically reduce the outflow of direct investment funds from the United States, it will be of some help—and every bit counts in the effort to eliminate our payments deficit.¹⁸

The Secretary's statement shows that there is no need to risk the adverse effects that the passage of this legislation might entail, since he finds that the great bulk of our foreign investments is not tax induced and in the long run serves the investor, the United States, and the recipient country alike.

If the only concern of the Congress is to eliminate marginal foreign investment that is induced primarily by a tax consideration, then section 11 does not appear as an appropriate instrument to accomplish this end. Furthermore, the Secretary of the Treasury is on record at Rome that there is no expectation that the enactment of additional legislation will dramatically reduce the outflow of direct investment funds from the United States.

CONSTITUTIONALITY

Section 11 imposes a tax on U.S. shareholders of foreign corporations based on the earnings of such corporations even though there has been no constructive receipt of funds with which to pay the tax.

¹⁸ Remarks of the Honorable Douglas Dillon, Secretary of the Treasury, Ninth Annual Monetary Conference of the American Bankers Association, Rome, Italy, May 18, 1962, p. 10.

The establishment of tax liabilities in this manner is a reversal of existing concepts which have been established for almost 50 years. It completely disregards corporate legal entities wholly legitimate in their business purposes.

The proponents of this theory of taxation attempt to justify it under the philosophy of the foreign personal holding company provisions. A colloquy between the Secretary of the Treasury, Mr. Dillon, and Senator Curtis of Nebraska is significant:

Secretary DILLON. Under the philosophy of the foreign personal holding company provisions, the Congress has decided and the courts have upheld that where transactions are entered into for the purpose of avoiding U.S. taxes, the income can be imputed to the U.S. stockholders and that in effect is what is happening here.

Senator CURTIS. That is a personal holding company?

Secretary DILLON. That is what it is by definition.

Senator CURTIS. I thought you were describing an actual operation of manufacturing and sale of goods throughout Europe.

Secretary DILLON. There is no legal constitutional difference and we are following the exact same procedure here. We apply the same procedure to these other operations as has been applied for many years to foreign personal holding companies.

Senator CURTIS. But suppose that the parent company in the United States is a publicly held corporation and not at all in the category of a personal holding company, and it has many stockholders, is income either to the—is income to the subsidiary income to the stockholders of the parent corporation.

Secretary DILLON. We look on a parent corporation as a U.S. person under the law, and the income is imputed to the U.S. person who controls the foreign subsidiary, and that person would be the U.S. parent corporation.

Senator CURTIS. Now suppose this company in this hypothetical case you describe was set up for the purpose not of evading taxes on income earned under the American flag but was for the purpose of finding a market, developing a market that could not be developed by the parent company located in the United States.

Would that change the situation?

Secretary DILLON. I certainly recognize that there are markets that can best be developed by investment abroad. But we do not feel that it is necessary to have as an added inducement and an added factor in that development the tax inducement of partial or complete tax exemption that flows from the use of tax havens. We think that the same markets could be developed by paying a reasonable tax.

Senator CURTIS. They do pay a tax when the money is brought back, do they not?

Secretary DILLON. A tax is paid when the money is repatriated to the United States; that is correct.

Senator CURTIS. Now, speaking of operating companies that actually engaged in manufacturing, processing, selling,

all of that activity is outside the United States, isn't it true that heretofore we have adhered to a jurisdictional principle that a tax so earned outside of the United States—the U.S. tax on income earned outside the United States—is due when it is remitted to this country?

Secretary DILLON. That has been the principle in the law, except for the foreign personal holding company law.

Senator CURTIS. And this proposal would greatly change that wouldn't it?

Secretary DILLON. This proposal would very considerably modify that principle. That is the purpose of it.

Senator CURTIS. Now, you referred a moment ago to suggestions made yesterday to grant to the Treasury Department authority to by regulation—although you didn't use that word—except certain transactions or make a finding that they were not tax-haven transactions?

Now—

Secretary DILLON. That is correct.

Senator CURTIS. How is the business concern going to know what the rule of the Treasury would be 5 years from now?

Secretary DILLON. By coming in and asking.

Senator CURTIS. When? Now?

Secretary DILLON. Now.

Senator CURTIS. Would that answer be binding upon the Treasury 5 years from now?

Secretary DILLON. We would be prepared to give rulings on this sort of thing very generously ahead of time because we do not want to upset business and we don't want to have uncertainty here. We would be very glad for any business that thought it had a case to come in and talk to the Internal Revenue and we would give them a ruling in a proper situation.

Senator CURTIS. Well, I am glad you share the view that this is a decided change in the tax policy of the country.

One of the things I had in mind late yesterday afternoon when I requested that a new bill be drafted and printed as a study bill, study copy, was so that it could be examined, and to see what the proposal is made in our basic tax philosophy and practice in the light of your modified recommendations of your statement yesterday.¹⁹

It is inconceivable that the Secretary of the Treasury would suggest that exceptions to the law should be made on the basis of Treasury rulings so as not to disturb legitimate transactions.

The Foreign Personal Holding Company Act deals with passive investments that have no connection with the carrying on of an active trade or business.

The personal holding company tax was never conceived by the Congress as being applicable to the unremitted earnings of active overseas subsidiaries of U.S. business firms with widespread stockholdings.

¹⁹ "Revenue Act of 1962," hearings before the Committee on Finance, U.S. Senate, 87th Cong., 2d sess. on H.R. 10650, pt. 10, pp. 4311-4312.

The National Foreign Trade Council was organized in 1914 to promote and protect American trade and investment. Its membership is comprised of manufacturers, merchants, exporters, importers, transportation interests, bankers, insurance underwriters, and many others interested in the expansion of the Nation's foreign commerce.

Mr. Joseph B. Brady, vice president of the National Foreign Trade Council, presented an extended legal brief to the House Committee on Ways and Means on June 5, 1961. It showed that the characterization of tax deferral as a privilege is a misleading one. It developed the history underlying the present U.S. tax laws, and it showed that the proposal to tax unremitted earnings is completely contrary to our established tax policies. It presents a serious question of the constitutionality of the administration's foreign tax proposals.

Section 13 of H.R. 10650 as it was referred to the Committee on Finance was based on the concepts to which the National Foreign Trade Council took exception in June of 1961. This organization again appeared before the Committee on Finance on April 25, 1962, and Mr. Brady again presented the legal reasons for the rejection of section 13 in the House measure. This section has been amended by the Committee on Finance and is now section 11 of H.R. 10650 as amended. The amendments adopted by the committee do not alter the underlying principles with respect to the taxation of unremitted earnings nor do they remove the constitutional doubts which were raised in the original brief presented to the House Ways and Means Committee. The legal reasons to reject any proposal to tax U.S. shareholders on the undistributed profits of foreign corporations contained in the statement presented to the Committee on Finance by Mr. Brady are worthy of the considered judgment of the Senate in its further deliberation on section 11 of H.R. 10650. These salient points with respect to legal and constitutional questions of this proposal follow:

The legal reasons for rejecting the proposal to tax to the U.S. shareholder undistributed profits of foreign corporations, as provided by section 13, are discussed below.

(a) History and reasons for present law

The basic provisions of U.S. law, relating to taxation of income from foreign sources, have been in existence for nearly 50 years. All U.S. foreign investments have been made with these provisions as a background. In addition, important foreign investments have been made, under an announced policy of the U.S. Government, to encourage such investment.

Under the 1913 act, income received by foreign corporations from sources outside the United States are not taxed. U.S. shareholders were taxed only on the dividends from such corporations. These basic provisions have been retained in all subsequent reenactments of the income tax law, including the 1939 and 1954 versions. Contrary to the impressions of some persons, no provisions were introduced into U.S. tax law after World War II to encourage investment and trade in Europe by U.S. companies.

Like most features of tax law, these provisions reflect both theoretical and practical considerations. These considera-

tions generally fall either within the fiscal area, or the combined area, of public policy and trade. The recognition of the importance of foreign trade and investment, a recognition that income from foreign source is initially subject to tax in the foreign country, and the need for revenue, all form a part of the background for the enactment of our tax laws on income from foreign trade and investment.

The concept that a corporation is an entity, separate from its shareholders, has always been recognized as a fundamental in every phase of the law. The principle of the non-taxability of the shareholder on the undistributed income of a corporation has been one of the pillars on which our tax system has been constructed. In addition, considerations of international law and comity, as well as U.S. constitutional and administrative problems, are among the wide variety of factors that have affected the formulation of the basic U.S. tax provisions.

(b) Proposal is contrary to basic U.S. tax policy

It is a fundamental principle of all aspects of American and international law that a corporation is regarded as an entity separate from its shareholders. Thus the shareholder is not obligated by the contract of the corporation, and is not responsible for its wrongful acts. This principle has been incorporated in the Federal income tax law. A corporation is taxed on its income, and the shareholders are taxed only on dividends distributed to them. Any proposal to tax the U.S. shareholders on the income of the corporation would be an exception to this basic principle, which has been followed consistently by Congress, the Treasury Department, and the Supreme Court. The basic principle has been reflected in U.S. tax treaties and in the claims of tax jurisdiction which the United States has made in the absence of tax treaties.

Both in the domestic and foreign field, taxpayers are only subject to tax on income actually realized. Corporations and individuals owning shares of stock are not taxable because of accumulated earnings of the companies issuing the shares, nor are they taxable in respect of increases in the quoted market prices of those shares. Holders of corporate securities are not entitled to deduct, from their taxable income, any decreases in quoted market price or generally any operating losses of the companies which may dissipate their surplus or even impair their capital. The U.S. income tax system recognizes fully the corporate entity. A U.S. parent corporation is taxed upon the dollar dividend received from a foreign subsidiary, because that is the correct measure of its realized income.

The principle that income must be realized before it is taxable has frequently been upheld by the Supreme Court. In 1918, the Supreme Court drew a distinction between corporate accumulations and distributions, treating only the latter as taxable income. The Court stated: "It is evident that Congress intended to draw, and did draw, a distinction

between a stockholder's undivided share or interest in the gains and profits of a corporation, prior to the declaration of a dividend, and his participation in the dividends declared and paid; treating the latter in ordinary circumstances, as a part of his income for the purpose of the surtax, and not regarding the former as taxable income unless fraudulently accumulated for the purpose of evading the tax." (*Lynch v. Hornby* (247 U.S. 339 at p. 343)). The fact that income must be "realized" is clearly set forth in *Eisner v. Macomber* (252 U.S. 189, 40 Sup. Ct. 189 (1920)) and has never been reversed.

The Treasury Department has followed the concept that income must be realized in order to be taxable; e.g., Regulations 1.61-1 provides in part: Gross income includes income *realized* in any form. [*Italic added.*]

Furthermore, the treatment of a foreign corporation as an entity, distinct from its shareholders, is recognized as a fundamental principle in 21 tax treaties, affecting some 44 foreign jurisdictions, to which the United States is a party. Even in the absence of tax treaties, the United States has recognized the foreign corporation as a separate entity and has never claimed tax jurisdiction over them, because it was owned in whole or in part by U.S. shareholders.

Since the enactment of the 1913 act, the United States has claimed jurisdiction to tax on the basis of (1) citizenship and residence, and (2) source of income in the United States.

To expand this jurisdictional claim, so as to tax, directly, the income of foreign corporations, because of American ownership of shares in such corporations, would run counter to all U.S. jurisdictional claims and might well bring about conflicts with the jurisdictional claims of foreign governments. It is undesirable, if not improper, for the United States to tax foreign corporations directly on their foreign income. These same considerations should apply to taxing the foreign corporation indirectly by taxing the shareholders.

The jurisdictional claims of the United States reflect the recognition that other sovereign nations have rightful claims to the primary jurisdiction of income earned by their corporations in their home country and in all countries other than the United States. The jurisdictional concepts of the United States are formally reflected in tax treaties between the United States and foreign countries which are discussed below.

The Secretary's explanation of his proposal states that "precedent for this tax treatment may be found in the provisions of existing law dealing with U.S. shareholders of foreign personal holding companies." These provisions are not an adequate precedent for such a broad departure from established tax policy. The provisions were enacted on the assumption that foreign personal holding companies were "created with the sole purpose of avoiding or evading the imposition of the surtax on their shareholders" and the legislation was intended "to encourage the prompt dissolution of existing companies of this type," which were regarded as

"spurious" (report of the Joint Committee on Tax Evasion and Avoidance, Aug. 5, 1937, 75th Cong., 1st sess., H. Doc. 337, pp. 21 and 22). However, these provisions were never intended to, and do not, by the definition of foreign personal holding companies in the Internal Revenue Code, affect bona fide foreign business companies.

The foreign personal holding company provisions are strictly limited to the case where the foreign company is controlled by not more than five U.S. citizens or residents and derives 50 percent or more of its gross income from certain categories of income, such as dividends, interest, and capital gains (secs. 551-557, I.R.C.). The proposed recommendation by the Secretary is addressed to a situation which is quite different from that of the foreign personal holding company. With relatively few exceptions the foreign subsidiaries which will be affected are operating companies that would not be within the purview of the foreign personal holding company provisions. These foreign corporations have not been "created with the sole purpose of avoiding or evading the imposition of (a tax) on their shareholders." Rather these subsidiaries were formed to carry on U.S. trade and business in a part of the world most important from the viewpoint of national as well as business considerations. Further, it is not believed that "the prompt dissolution of existing companies of this type" is intended even by the Treasury. Therefore, it is urged that the foreign personal holding company provisions should not be regarded as precedent for the proposed legislation. An additional point which should be considered is that the foreign personal holding company provisions are primarily an extension to foreign companies of a punitive provision which previously was in effect domestically; namely, the personal holding company provisions.

The proposal to tax a shareholder on unrealized profits is, in effect, taxation by indirection of the current earnings of the foreign corporation and is designed to tax indirectly what could not be taxed directly. This policy of taxing by indirection is at least questionable from the standpoint not only of domestic tax policy but also of international comity. Probably any attempt by the United States to tax directly or indirectly foreign corporations on income not earned in the United States would be objected to by foreign countries. In the past, foreign countries have objected to the extra-territorial effect of other U.S. laws, for example, the extension of the antitrust and export control laws.

The proposals of the Secretary to impose taxes on U.S. shareholders of foreign corporations measured by the earnings of the foreign corporations as they accrue will result in a nullification of tax incentive programs designed by foreign countries to attract investment and reinvestment by foreign corporations. It would defeat the purpose of provisions under foreign tax laws, such as investment allowances, accelerated depreciation, and tax exemptions designed to promote economic development in the foreign country. It

would also ignore requirements of the foreign country that legal and statutory reserves be set aside before dividends can be paid. It would be contrary to the practice in some countries which impose through private agreement restrictions on dividend distributions.

Foreign competitors of U.S. business would still enjoy the benefit of these incentives. Where American investments are an important factor the foreign country might revise its incentives program, and attempt to bring its tax rates up as high as 52 percent in order that it may obtain taxes which otherwise would redound to the benefit of the United States.

The proposal will have an adverse effect both on the corporations and shareholders. In many instances, shareholders may not have funds available from other sources to pay the taxes. This, of course, will place pressure on the foreign corporation to remit income to pay such taxes. Where local nationals are also shareholders and have a controlling voice in the company this pressure to distribute funds which otherwise would not be distributed in order to pay U.S. tax will be resisted. From a long-range point of view, it may deter local participation in companies in which American capital is invested. Furthermore, the individual shareholder who in most instances would have no control over the foreign corporation whatsoever could receive no foreign tax credit and would be required to pay such income tax out of his capital. Many foreign incorporated subsidiaries have incurred long-term financial commitments on the reasonable assumption that neither the subsidiary nor the shareholder would be subject to U.S. tax on the undistributed income of such subsidiaries. The proposed imposition of U.S. tax on U.S. shareholders might affect drastically the ability of the subsidiary to meet the financial obligations.

The proposal to tax the U.S. shareholder of a foreign corporation on the undistributed income of such corporation is contrary to basic tax principles which have been followed since 1913. A departure from these principles would constitute a drastic change in this fundamental area of tax policy. It would constitute a deviation from the recognition of the separate entity of the corporation without which concept it would be impossible to conduct much of modern business. It would raise serious questions in the international field. Possibly one of the most important questions that should be considered would be the precedent that enactment of such proposal might constitute for taxing U.S. shareholders on the undistributed income of U.S. corporations.

(c) Constitutionality

Under the proposal, American shareholders of foreign corporations would be taxed on their share of the income of those corporations, even though it is not distributed. It has been held to be a violation of the due process clause of the 14th amendment to the Constitution for a state to measure the tax on one person's income by the income of another. *Hooper v. Tax Commission* ((1931) 284 U.S. 206). It would seem equally a violation of the due process

cess clause of the 5th amendment for the Federal Government to measure the proposed tax on the American shareholder by the income of another person, the foreign corporation.

Under the 16th amendment Congress may tax incomes, from whatever source derived, without apportionment. It should be noted, however, that the 16th amendment is applicable only to true income taxes and that a tax cannot be brought within the scope of that amendment merely by calling it an income tax.

Eisner v. Macomber ((1920) 252 U.S. 189, 206), held that income consists not in a growth or increment in value of an investment, but something of exchangeable value proceeding from the property, severed from the capital and coming into, or received by, the taxpayer, and that a stock dividend was not income within that definition because it did not accomplish an actual distribution of corporate earnings. The Court refused (p. 214) to "indulge the fiction" that the stockholders "have received and realized a share of the profits of the company which in truth they have neither received nor realized" and held that the corporation must be treated as a substantial entity separate from the stockholder. It went on to say that "enrichment through increases in value of capital investment is not income in any proper meaning of the term" and (p. 217) that to tax the shareholders upon their property interest in the stock of the corporation would be taxation of property because of ownership, and would require apportionment under article I of the Constitution. The Court expressly stated (p. 219) that "what is called the stockholder's share in the accumulated profits of the company is capital, not income." It follows from the holding in this case that the proposed tax on American shareholders of foreign corporations, measured by their shares of the undistributed income of those corporations, which they have not received as dividends, would be a direct tax on the shareholders because of ownership of shares and would not be a tax on income within the meaning of the 16th amendment. Under article I of the Constitution direct taxes must be apportioned among the States according to population. In *Pollock v. Farmer's Loan & Trust Co.* ((1895) 158 U.S. 601) it was held that taxes on personal property, or on the income of personal property, are direct taxes.²⁰

An eminent student of taxation, Dr. Dan Throop Smith, professor of finance at the Harvard Graduate School of Business Administration and a former Assistant Secretary of the Treasury, in his appearance before the Committee on Finance on April 27, in referring to section 13²¹ of the act H.R. 10650 as passed by the House said:

Section 13, I believe, is extremely bad. It seems to be based on a misconception, in fact on several misconceptions. The attempt to extend our tax jurisdiction over the undistributed income of foreign operating subsidiaries is, I submit, unsound in principle, extremely difficult in application, and

²⁰ Revenue Act of 1962, hearings before the Committee on Finance, U.S. Senate, 87th Cong., 2d sess., on H.R. 10650, pt. 6, pp. 2686-2693.

²¹ Sec. 13 was amended and is now sec. 11.

very much against the longrun national interest if the United States is to participate freely in the world's trade and income.²²

Further problems involving our treaty obligations are presented in section 11. While the language technically does not violate our tax treaties, the consequences of the enactment of the legislation would definitely be contrary to the spirit and intent of these treaties and conventions. Again, the effect of these considerations was set forth by Mr. Brady, and the pertinent portions of this statement follow:

The proposal to tax *shareholders* on the undistributed income of foreign incorporated companies which is earned outside of the United States is a principle which has no counterpart in the tax systems of the major industrialized countries of the world. An analysis by local fiscal experts of the tax systems of Australia, Belgium, Canada, Denmark, France, Germany, Italy, Japan, Netherlands, Norway, Sweden, and the United Kingdom indicates that none of them applies such a principle. In 1939 the German Government enacted a provision under which a foreign subsidiary which is dominated by a German company may be regarded as resident in Germany and taxed on all its income. Such tax would be imposed on the subsidiary and not on the shareholder. It is understood that this provision has been rarely applied in the past and that it is not anticipated that it will be enforced in the future. The United Kingdom and Japan also have in exceptional cases treated a foreign corporation as a resident for tax purposes if its mind and management are within the country, but this means that the corporation itself becomes liable for tax and not its shareholders. Under present practice the mind and management of a company will not be located in the country if the administrative office, directors' meetings and general managerial functions are conducted outside the country.

The proposal attempts to expand the jurisdiction of the United States, beyond that normally considered by any other country, so as to tax the shareholder, solely by reason of his ownership on his share of the earnings of a foreign corporation before such earnings are distributed. Inasmuch as such a policy, if adopted by United States, would add a new principle in the international tax field we do not believe that the Congress will wish to attempt to expand its taxing jurisdictions to such extremes.

In his appearance before the Committee on Ways and Means the Secretary of the Treasury stated in discussing the proposal to tax to the U.S. shareholder the undistributed income of foreign corporations:

"This method of taxing would eliminate possible conflicts with U.S. treaty obligations, which might occur if the tax were imposed directly on the income of foreign corporations."

He considers that treaty obligations would not be violated if the domestic shareholders were required to "include in gross income each year that portion of the undistributed

²² Ibid., pp. 3088-3089.

earnings and profits of the foreign corporation which they would have included in gross income had the foreign corporation distributed its entire profits for the year." Nevertheless, the tax is levied on the basis of income that belongs to the foreign corporation and not to the shareholders.

Treaties are founded on respect by one party for the laws of the other, except insofar as the treaty limits their respective jurisdiction to avoid double taxation. They respect the principle that the corporations of the other country may conduct their affairs in accordance with the laws of the other contracting party. Treaties are founded on reciprocity and if the United States invades in effect the jurisdiction of the other party to levy a tax, even if it collects the tax from its own resident shareholders, the United States could not object if the other foreign government levied a reciprocal tax based on the undistributed income of U.S. corporations. This initiation on a wholesale basis of extraterritorial taxation of the type could seriously damage international investment and business relations conducted through subsidiaries and would certainly violate the intent, spirit and basic principles of the 21 tax treaties which are in effect vis-a-vis some 44 foreign governments.

The principle that a tax can be levied generally on the basis of a foreign corporation's income or a portion thereof, but collected from the shareholder is absolutely contrary to long-established principles of international tax treaty law as well as American jurisprudence. It has been argued that, under the treaties, the United States, in determining its taxes in the case of its citizens, residents or corporations, may regardless of any other provision of the treaties, include in the basis upon which such taxes are imposed all items of income taxable under the revenue laws of the United States as if the treaties had not come into effect. This is the so-called saving clause. However, the doctrine of *Eisner v. Macomber*, that the income tax is imposed on realized income, pervaded at the time of entering into the treaties and since that time in U.S. tax law. This doctrine must be considered as reflected in the meaning of the treaty provisions. The saving clause should therefore be read to refer only to items of realized income, including dividends from a corporation of the treaty country, and not to unrealized income.

Our first tax treaty was entered into with France. The primary objective of the treaty was to prevail upon France to give up its tax on dividends distributed by U.S. corporations which were deemed to be paid out of income from French sources. Because of this tax the United States adopted the provision for a retaliatory tax against discriminatory or extraterritorial taxation now found in section 891, I.R.C. The French agreed to waive their extraterritorial dividend tax in consideration of a treaty provision authorizing the French Government to collect tax from the French company on any income shown to have been diverted from it to an American corporation. However, when this convention with France and each subsequent convention

was negotiated, no other country sought to tax shareholders resident in its territory on undistributed income of a foreign corporation because of control or ownership.

It will be observed that the United States reacted sharply to an extraterritorial imposition of tax by France. In effect the Treasury proposal would tax income of foreign corporations derived from foreign sources. The treaties specifically limit the jurisdiction of the United States over a foreign corporation to income from sources within the United States, and therefore the United States is obligated not to tax the income of a foreign corporation from sources without the United States. Would it be too much to expect that foreign countries in general, and treaty countries in particular, would react sharply by similar retaliatory taxes to U.S. taxation of the income of their corporations before it is paid out in dividends?

Congress has, through the enactment of two provisions in the code, clearly expressed its policy to be against the violation of tax treaty obligations. Section 894 requires that income of any kind, to the extent required by any treaty obligation of the United States, shall not be included in gross income and shall be exempt from tax under this subtitle. This should include the foreign income of a foreign corporation to the extent it is not distributed to U.S. shareholders.

Section 7852(d) provides that no provision of this title shall apply in any case where its application would be contrary to any treaty obligation of the United States in effect on the date of enactment of this title, and respect for international comity would require a similar provision be incorporated in any future tax legislation with international implications.

There is another provision in a number of tax conventions and executive agreements that would also be violated by the proposed amendment; namely, the provision for exemption from U.S. tax, on condition of reciprocity, of income derived in the United States from the operation of ships and aircraft which provides that such income shall not be included in the gross income of a foreign corporation and shall be exempt from taxation. Yet, if the foreign corporation which benefits from this exemption happened to be within a developed country or to be classified as a tax-haven corporation, the recommendation would tax the income that is thus not includible in the gross income of the foreign corporation.

The Supreme Court has declared: "The principles which should control the diplomatic relations of nations and the good faith of treaties as well, require that their obligations should be liberally construed so as to effect the apparent intention of the parties to secure equality and reciprocity between them" (*Jordan v. Tashiro*, 278 U.S. 123). Obviously, all our tax treaties were concluded with reference to the United States and foreign laws in effect when the treaties were negotiated, and it was not contemplated that the United States might someday tax U.S. shareholders on

the profits of foreign corporations before they are distributed. This, it is believed, violates the spirit and intent of tax treaties.²³

The many amendments adopted during the course of the committee's consideration of this measure do not alter the basic principles of levying a tax on U.S. shareholders of so-called "controlled foreign corporations" based on their unremitted earnings.

The amendments adopted by the committee have lessened the impact of the added tax burden, but they do not deal with the fundamental problem of a basic change in the concepts which have guided the Congress for almost 50 years in the enactment of all tax legislation.

Should section 11 be enacted into law, retaliatory measures may be adopted in other countries. In any event, it will most probably be difficult to negotiate new tax treaties that further the commerce and interests of our Government and its citizens.

SUMMARY AND CONCLUSIONS

These views have set forth the many reasons why the objectives the administration seeks cannot be achieved through the enactment of section 11 of H.R. 10650 as reported by the Committee on Finance. The objectives are desirable, but the means that have been recommended for their accomplishment are impractical and unworkable.

The administration has long been on record that it will recommend additional basic reforms in our tax structure for the consideration of the Congress next year to become effective January 1, 1963.

Section 11 of H.R. 10650 also provides that it shall be effective with respect to the taxable years beginning after December 31, 1962. It thus appears that if section 11 were enacted into law by the 87th Congress, the Secretary of the Treasury would have only 4 months in which to establish the rules and regulations for its implementation. Of necessity rulings would conform to the present basic tax laws. If the 88th Congress enacts a broad program of tax reform, then it will be necessary for the Secretary of the Treasury to redraft completely the rules promulgated under section 11 of the pending bill to make it conform to a new tax code which also will be effective January 1, 1963. Such a procedure will entail expense and difficulties for the Internal Revenue Service to say nothing of the confusion and cost of compliance that will confront taxpayers.

It would appear that the Internal Revenue Service should concentrate on more effective enforcement of existing law rather than apply itself to the promulgation of rules and regulations which will require revision within a matter of months.

When the Congress considers the broad issues of tax reform, it should give consideration to necessary amendments to existing law to prevent evasion and simplify the burden of reporting for both the taxpayers and the Internal Revenue Service on all phases of foreign source income.

The administration's objections will not be achieved by the enactment of section 11 of the bill as reported by the Committee on Finance at this time. The testimony that has been considered by both the House Ways and Means Committee and the Committee on Finance

²³ Ibid., pp. 2694-2698.

during the 87th Congress should supply information that will be of assistance to the administration and the Congress in developing a workable program for the collection of proper taxes on foreign investments without establishing practices which may be unconstitutional, as they impose taxes on earnings that have not been constructively received by the taxpayer. The enactment of section 11 at this time can only result in years of costly litigation. Many taxpayers will not know their true tax liabilities, and the Treasury will be unable to properly estimate the tax revenues to which it is entitled until the Supreme Court has interpreted this legislation.

The only recommendation that can be made to the Senate on the basis of a careful and deliberate consideration of the entire record is to postpone action on section 11 and reconsider this entire subject in conjunction with the administration's basic tax reform program when it is presented to the 88th Congress.

FRANK CARLSON.

WALLACE F. BENNETT.

JOHN MARSHALL BUTLER.

CARL T. CURTIS.

THRUSTON B. MORTON.

SUPPLEMENTAL AND MINORITY VIEWS OF SENATORS PAUL DOUGLAS AND ALBERT GORE

INTRODUCTION

When the administration proposed this bill a year and a half ago, it was intended to close a few of the loopholes which disgrace our tax system and cause grave injustices and irregularities in the application of our tax laws. The total amount of revenue which would have been saved to the Treasury and hence to the people was, by the terms of the President's original proposal, approximately \$2.3 billion. A brief description of these reforms and the amounts expected to be realized during the first full year of their operation will be found in the first two columns of table I.

To "sweeten" the proposals for tax reform and make them more acceptable to those who had been avoiding the just payment of taxes on certain income in the past, a tax reduction was offered consisting of a generous tax credit on most forms of net business investment in depreciable property. It was estimated that on an annual basis, this would lose \$1.7 billion in revenue.

The original plans of the administration thus provided for an overall annual increase in revenues of about \$600 million. But it is probably fair to conclude that knowing the tendency for tax reform proposals to be whittled away and indeed to evaporate as they move through Congress, the administration really would have been satisfied if the "loophole" closing and the investment credit finally offset each other so that there would have been little or no net revenue gain or loss. The basic original aim of the bill was therefore (1) to effect minor and, it was believed, less controversial changes in the field of tax reform, and (2) to balance this with an approximately equal reduction in the taxes paid by business and industry. This latter was framed in such a way that it was hoped it would stimulate new investment and the modernization of machinery and equipment.

In the long-drawn-out process of nearly a year and a half during which this bill has moved slowly through the other body and through the Finance Committee, it has been disfigured almost beyond recognition.

The proposal to repeal the 1954 dividend credit of 4 percent and exclusion of \$50 which would have reclaimed \$450 million a year for the Treasury and the people was thrown overboard early.

The main feature on the loophole closing side, namely, the withholding at the source on dividends and interest income paid by institutions, was eliminated by a lopsided vote in our committee. It is estimated that, in itself, this would lose about \$900 million in revenues from taxes which are owed but not paid. This step was taken by the committee to the accompaniment of a tornado of mail stimulated by building and loan associations, banks, and savings institutions. One

of the signers of this minority report received no less than 75,000 letters from his constituents demanding that withholding be eliminated from the bill. These letters portrayed gross misconceptions of what the withholding method really was. Thus, (1) from a third to a half of the correspondents thought that it was a new tax; of course, it was no such thing. Interest and dividends are income just as much as wages and salaries and as such are equally taxable. The fact that so many thought it would be a new tax strongly suggests that many of these people have not been paying these taxes in the past. (2) It was charged that this was a tax on capital, whereas it would only be a method to collect the tax already owed on the interest or dividend income earned. (3) The administrative difficulties as we shall see were also grossly exaggerated.

Under heavy battering from American corporations doing business abroad, the proposed levies on them based on earnings of their foreign subsidiaries were progressively softened.

On the other side of the balance sheet there was some reduction in the amounts granted for the investment credit. But the overall result is that, if the present bill is enacted, there will be a net revenue loss of at least \$550 million, and, in our judgment, nearer \$700 million a year.

What was originally a bill in which the revenue losses would at least be balanced by the revenue gains has now become a bill in which the revenue losses greatly exceed the revenue gains.

What was originally a bill in which a few of the most glaring and, on the whole, less controversial loopholes were to be closed has, in its present form, turned into a bill in which a few minor loopholes are closed but in which some new major loopholes and truckholes are opened.

What was originally a bill to stimulate new marginal net investment has now become a bill in which a tax favor is granted even for less investment than in the past.

What was originally a bill to close some of the most glaring loopholes with respect to business expense account deductions has now become a bill in which business groups will be given new deductions for lobbying on behalf of their own selfish interests.

In other words, in its present form, what was on balance a tax loop-hole closing bill has, on balance, become a tax loophole opening bill.

Unless major changes are made in this bill either on the floor of the Senate or in conference, we must vote against it.

TABLE I.—*Evolution of the Revenue Act of 1962—with pertinent revenue estimates*¹

LOOPHOLE CLOSERS

President's proposals of Apr. 20, 1960	Revenue gain	House bill	Revenue gain	Revenue decrease compared to President's proposal	Finance Committee bill	Revenue gain	Revenue decrease compared to House bill	Revenue decrease compared to President's proposal
	Millions		Millions	Millions		Millions	Millions	Millions
Sec. 4. Expense accounts Provides that the cost of business entertainment, including club dues, and the maintenance of entertainment facilities (such as yachts and hunting lodges) be disallowed in full as a tax deduction. Restrictions should also be imposed on the amount to be deducted as business gifts, on travel expenses for vacations that are combined with business travel, and on excessive personal living expenses incurred on business travel away from home.	\$250	Under the House bill expenditures for entertainment activities must be directly related to the active conduct of the taxpayer's trade or business and those for entertainment facilities such as yachts must meet an additional test of being primarily in furtherance of the trade or business. Deduction was denied for business gifts in excess of \$25, a standard of "reasonableness," was added to the provisions dealing with traveling expenses, and a good rule requiring substantiation of expenditures was adopted.	\$125	\$125	The Finance Committee added to the directly related test of the House bill a liberalizing test permitting the deduction of entertainment expenditures if they are directly "associated with" the taxpayer's trade or business. In addition, the committee's report is very weak and confusing—quite unlike the report of the House Ways and Means Committee which provided some meaningful guidelines that made the House provision workable and effective.	\$60	\$65	\$190
Sec. 6. Mutual savings banks The existing bad debt reserve formula of 12 percent of deposits, which has resulted in virtual tax exemption, would be reviewed to assure "non-discriminatory treatment." The Treasury Department Report of July 1961 suggested alternative methods of taxation to produce revenue of between \$150 to \$416 million, at 1963 levels of income, depending upon alternative selected.	\$150-416	Provided a bad debt reserve deduction of 3 percent of the increase in real estate mortgage loans or, alternatively, a deduction of 60 percent of retained earnings. Technical provisions changed definition of "domestic building and loan association," prevented capital stock savings and loan associations from distributing to stockholders pre-1952 tax-free surplus, removed certain exemptions from excise taxes, and applied realistic rules for computing bad debts resulting from mortgage foreclosures.	\$200	-----	In the case of capital stock savings and loan associations, the special deduction of 60 percent of earnings was reduced to 50 percent to produce additional revenue of about \$5 million annually. Other changes modified definition of domestic building and loan association, broadened repeal of excise tax exemptions, imposed ceilings on amount of reserves, and took into account tax-free surplus accumulated prior to 1952 to the extent necessary to place all institutions on an equal basis.	\$205	+\$5	-----

¹ See footnotes at end of table, p. 395.

TABLE I.—*Evolution of the Revenue Act of 1962—with pertinent revenue estimates* 1—Continued

LOOPHOLE CLOSERS

President's proposals of Apr. 20, 1960	Revenue gain Millions	House bill	Revenue gain Millions	Revenue decrease compared to President's proposal Millions	Finance Committee bill	Revenue gain Millions	Revenue decrease compared to House bill Millions	Revenue decrease compared to President's proposal Millions
Sec. 8. Mutual insurance companies Provided for the elimination of the special provisions of existing law which are applicable only to mutual fire and casualty insurance companies, so as to tax such companies on total income in essentially the same manner as stock fire and casualty insurance companies.	\$50	Provided a modified total income approach which permits a portion of underwriting income to be set aside tax free in a special reserve for protection against losses. Also, provided special rules for concentrated risk companies, reciprocals, factory mutuals, mutual marine companies, and certain small mutuals.	\$40	\$10	Changed the order in which losses are to be charged to the special protection against loss reserve. Other changes liberalized the provisions of the House bill relating to concentrated risk companies, reciprocals and certain small mutuals, and provided a special rule for taxing mutual flood insurance companies.	\$35	\$5	\$15
Sec. 13. Gain on depreciable property Gain on sale of depreciable property, both real and personal, should be treated as ordinary income to extent of prior depreciation.	\$200	Removed real estate from application of provision.	\$100	\$100	Same as House bill.	\$100	\$0	\$100
Sec. 17. Cooperatives Provide that all earnings of a cooperative arising from business activities are taxable to either the cooperative or its patrons. The patrons (and not the cooperative) would pay the tax on patronage distributions in money or noncash allocations meeting certain conditions. The cooperative would be taxable on earnings which are not returned to the patrons.	\$35	The Ways and Means Committee made several refinements in the bill, none of which affected the revenue estimate. The primary change requires the patron to consent to paying the tax on noncash distributions before he is taxable and the cooperative receives a deduction.	\$35	\$0	The Senate Finance Committee made 2 changes in the House bill, none of which affects the revenue estimate. One would require the cooperative to distribute at least 20 percent of its patronage dividends in cash in order to escape tax—this replaces the 20-percent withholding that would have been required under the House bill. The other change prescribes an alternative method for a patron to consent to paying tax on noncash distributions.	\$35	\$0	\$0
Sec. 19. Withholding Provide for withholding of 20 percent from interest, dividends, and patronage dividends.	\$880	The Ways and Means Committee made several important refinements in the bill, but none of them affected the revenue estimate. The most important changes were the inclusion of exemptions for nontaxable persons and the extension of the quarterly refund procedures to taxable individuals who are subject to over- holding holding.	Same	-----	The Senate Finance Committee deleted the withholding plan and substituted an expanded information reporting plan under which all dividend, interest, or patronage dividend payments of \$10 or more a year must be reported to the Government with a copy of the information given to the payee.	\$275	\$605	\$805

FOREIGN INCOME

Sec. 12. Controlled foreign corporations

Provide for the elimination of deferral of U.S. tax of foreign subsidiaries.

\$230

The House bill would eliminate deferral with respect to certain tax haven profits, earnings not reinvested in an existing business in a developed area or in an active business in a less developed area and earnings reinvested in the United States in such a way as to constitute a constructive dividend. However, tax haven profits which were invested in less developed areas would not be covered.

\$85

\$145

The Senate Finance Committee restricted its approach to the elimination of deferral for tax haven profits and those earnings invested in the United States. It improved the taxation of tax haven profits by (a) including certain service income and branch sales profits, (b) excluding the profits of certain active businesses from the definition of tax haven profits, and (c) eliminating the "pour over" of developed-area tax haven profits into less developed countries. The committee also added 2 important exceptions for (a) the earnings of certain export trade corporations and (b) the earnings of certain foreign subsidiaries or groups of foreign subsidiaries which distributed specified minimum percentages of their after-tax earnings.

\$85

\$0

\$145

Sec. 9. Gross-up

Provide for "gross-up" of dividends received by U.S. companies from their foreign subsidiaries so as to correct the inadequacy of the existing foreign tax credit formula under which the combined U.S. and foreign tax may be substantially lower than 52 percent. Under existing law, the disparity between 52 percent and the actual combined rate varies with the actual foreign taxes paid, being highest at 26 percent and gradually diminishing as the foreign tax drops below or rises above 26 percent.

\$35

\$35

\$0

With the exception of a 2-year grace period for previously accumulated earnings, the Ways and Means Committee adopted the President's recommendation.

\$25

\$10

\$10

See footnotes at end of table, p. 395.

TABLE I.—*Evolution of the Revenue Act of 1962—with pertinent revenue estimates*¹—Continued

President's proposals of Apr. 20, 1960	Revenue gain	House bill	Revenue gain	Revenue decrease compared to President's proposal	Finance Committee bill	Revenue gain	Revenue decrease compared to House bill	Revenue decrease compared to President's proposal
	<i>Millions</i>		<i>Millions</i>	<i>Millions</i>		<i>Millions</i>	<i>Millions</i>	<i>Millions</i>
FOREIGN INCOME—continued <i>Secs. 5, 7, 10, 11, 14, 15, 16, 18, 20 and 27.</i> <i>All other foreign items.</i> (For convenience, section references refer to section numbers in the Senate Finance Committee bill.) (1) Eliminate the tax-free nature of certain distributions by foreign trusts to U.S. beneficiaries (sec. 7). (2) Eliminate the exclusion of income for U.S. citizens residing in developed areas of the world and reduce it to \$20,000 annually for those residing in less developed areas (sec. 11). (3) Eliminate the tax benefits now obtained by U.S. citizens through investments in foreign investment companies (sec. 14). (4) Eliminate the present exclusion of foreign real property from the gross estate of decedents subject to U.S. tax (sec. 18). (5) Improve the information now required regarding U.S.-owned foreign corporations (sec. 20). [No recommendations similar to secs. 5, 10, 15, 16, or 27.] <i>Repeal of dividends received credit and exclusion</i> Repeal of provision excluding first \$50 of dividends and allowing a credit of 4 percent on dividends in excess of \$50.	\$50	The Ways and Means Committee generally adopted the proposals regarding foreign trusts, foreign investment companies, foreign real estate and improved information requirements. As to the earned income exclusion, the committee provided that U.S. citizens residing abroad could annually exclude \$20,000 for the first 3 years of foreign residence and \$35,000 thereafter, without distinction between developed and less developed areas. The committee added provisions increasing the taxation of distributions in kind from foreign corporations (sec. 5), gain on the sale or exchange of stock in foreign corporations (sec. 15) and a provision regarding the relationship between the bill and existing tax treaties (sec. 27).	\$30	\$20	The Senate Finance Committee, at the recommendation of the Treasury, added a provision providing for a special computation of the foreign tax credit with respect to certain interest income designed to halt certain flows of capital abroad which are induced by the existing foreign tax credit mechanism (sec. 10) and also added a provision providing for the taxation of gain from the sale of certain patents and other intangible rights to foreign subsidiaries as ordinary income where such gain would otherwise be taxable as capital gain under existing law (sec. 16).	\$30	\$0	\$20
	\$450	Not included in bill.	\$0	\$450	Not included in bill.	\$0	\$0	\$450

LOOPHOLE OPENERS

Billions \$1.7	Billions \$1.395	Millions \$305	Billions \$1.340	Millions \$55	Millions \$360
Sec. 2. Investment credit Investment in new real and personal depreciable property having a useful life of 6 years or more qualified for a credit of 15 percent to the extent the new investment exceeded current depreciation allowances. A 6-percent credit was allowable on new investment between 50 and 100 percent of current depreciation allowances, with a minimum credit of 10 percent on the first \$5,000 of new investment. The credit was not to affect the depreciable cost of the property. Residential property, property used outside the United States, and property used by public utilities (other than transportation) were ineligible. The credit deductible in any one year was limited to 30 percent of tax liability, but the excess could be carried forward for 5 years. The proposed effective date was Jan. 1, 1961.	The House approved the tax credit plan, but made the following changes: (1) Eliminated the "excess approach" in favor of a 7-percent flat across-the-board credit; (2) Excluded all buildings and certain other real property, but made personal property of hotels and motels eligible; (3) Permitted \$50,000 of used property to qualify; (4) Eliminated any limitation on the use of the credit on the taxpayer's first \$25,000 of tax liability; adopted a 25-percent limitation on the tax liability above \$25,000; (5) Approved a 3-percent credit for public utilities; (6) Dropped the useful life requirement to 4 years, but scaled down the benefits of the credit for assets with lives between 4 and 8 years; (7) Moved the effective date up to Jan. 1, 1962.	The Senate Finance Committee modified the House bill in the following manner: (1) Required that the credit be subtracted from the taxpayer's cost of the property before permitting the taxpayer to compute his depreciation allowance. (2) Disallowed a credit upon the investment of insurance proceeds, and upon the purchase of livestock. (3) Approved a 3-year carry-back of unused credits, in addition to the 5-year carryover. (4) Moved the effective date up to July 1, 1962.	The Finance Committee expanded the House provision to cover the cost of sending lobbying material to employees and stockholders.	(3)	
Sec. 3. Lobbying expenditures The President did not recommend that a deduction be allowed for lobbying expenditures and the Treasury Department is opposed to the allowance of any deductions in this area.	The House bill permits business taxpayers to deduct the following lobbying expenditures: the cost of appearing before and communicating with committees of Federal, State, or local legislative bodies, contacting individual legislators, transmitting legislative information between a taxpayer and an organization of which he is a member, and the portion of the dues paid by a member attributable to the carrying on of such activities by the organization.				

² \$670 million (based on 1959 data) \$780 million based on 1960 data; \$880 million for 1963 based on trends from previous years.

³ No estimates available.

¹ All estimates in this table are those of the Treasury except for the investment credit as passed by the House and as passed by the Senate Finance Committee, and the revenue figures for reporting of dividends and interest, where the Joint Committee on Internal Revenue Taxation's figures are used.

THE INVESTMENT CREDIT—THE OPENING OF ANOTHER LOOPHOLE

I

WHAT THE INVESTMENT CREDIT IS

1. The bill in its present form provides a tax credit of 7 percent on amounts invested in new tangible depreciable property, other than buildings, which is subject to a depreciation life of more than 8 years. There are certain limitations which can be briefly stated: (a) If the life of the property is less than 4 years, no credit will be granted; (b) if the life is from 4 to 6 years, only one-third of the credit ($2\frac{1}{3}$ percent) will be granted; (c) if the life is from 6 to 8 years, then two-thirds of the credit ($4\frac{2}{3}$ percent) will be granted. The credit for used property is limited to the first \$50,000 of investment.

2. The bill also provides a 3-percent credit for regulated private utilities such as telephone and domestic telegraph, gas and electric companies.

3. The investment credit can be offset dollar for dollar against taxes owed up to \$25,000 but above that amount may not reduce tax liability by more than 25 percent.

4. The Long amendment adopted by the Finance Committee slightly reduces the effect of these tax credits in later years by providing that the basis cost of the asset shall not exceed the value of the asset minus the investment credit. Thus, depreciation is limited to 93 percent of the original cost of the asset (97 percent for utilities).

The Department of Commerce estimates that the production of durable equipment in 1961 amounted to \$25.5 billion. A 7-percent reduction in this would amount to \$1 $\frac{3}{4}$ billion annually. This would be reduced in practice by the lower rate for the private utilities, the exceptions listed above, and the Long amendment.

It is probably safe to estimate the initial loss of revenue from this feature of the bill at somewhere between \$1.1 billion to \$1.4 billion. We personally believe it will amount to not far from \$1.3 billion.

This measure is advocated by the majority as a means of stimulating industry to improve its plant and machinery, reduce its costs, and by stimulating investment to expand employment and reduce unemployment.

Here it should be noted that the tax credit originally proposed by the administration was on net additional investment, or the amount invested in industry over and above that allowed for depreciation. There would have been strong grounds for supporting such a proposal or one which would have given the credit to increases in investment over the average for a previous 3- or 5-year period. But during its consideration by the House Ways and Means Committee, this proposal was vulgarized almost beyond recognition. Instead of being a bonus for net additional investment or for increased investment, it was transformed into a credit for all investment (aside from buildings) or what may be termed gross investment. Thus, if a company invests less than the physical depreciation of its machinery and equipment, it will still get a 7-percent credit, or a 14-percent tax deduction on this gross investment. To repeat, an actual decrease in investment as compared with the years prior to July 1, 1962, will be rewarded.

II

WOULD THE INVESTMENT CREDIT APPRECIABLY STIMULATE INVESTMENT?

In other words, by giving the rewards on average gross investment rather than on marginal net investment any possible stimulus to added investment is greatly reduced and in our judgment is very slight indeed. We are confirmed in this opinion by the results of the McGraw-Hill survey in the spring of 1962. The question asked by McGraw-Hill was as follows:

If the administration's program of tax incentives for investment were enacted, how much would this increase your capital expenditures in 1962?

In reply to this, business as a whole indicated that it would raise its 1962 plans by only about 1 percent, or about \$300 million. Nine out of every ten companies which replied stated that they would not use such a program in 1962.

Since the bonus under the proposed investment credit will amount to about \$1.1 to \$1.4 billion, this would mean that, out of every dollar which the Government will lose in taxes, less than 30 cents will find its way into increased investment in American industry. This is a very high price to pay for a little stimulus.

The National Industrial Conference Board made a special survey in late March and early April 1962 of the 1,000 largest manufacturing corporations in the United States to determine what effect the 7-percent investment credit would have upon their capital investment. While the influence of the credit on the plans of the companies varied somewhat from industry to industry, the results were that only 8 percent of those responding said they would revise their capital spending for the balance of 1962 if the credit were enacted by mid-1962. Seventeen percent of the reporting companies said they would increase their investments in 1963 if the credit were enacted by the end of the current session of Congress. But the prospective change in the dollar volume of capital spending in 1963 as a result of the credit would be as small as 1 percent.

As the report of the survey states:

Overall, * * * the increase in 1963 outlays expected on account of the investment tax credit may be small in relation to its potential. In more than half of the industries covered, moreover, the imputed difference was less than 1 percent.¹

There are already more than adequate funds available for investment on the part of corporations which they are refusing to use for this purpose. Thus the July 1962 Survey of Current Business, issued by the Department of Commerce (p. 24), shows that in 1961 American corporations had acquired \$43.1 billion of corporate funds² but invested only \$31.3 billion in equipment and inventories.³ In this one year, therefore, they piled up nearly \$12 billion in liquid assets.

¹ The Business Record, National Industrial Conference Board, August 1962, p. 19.

² Made up as follows (in billions of dollars): Retained profits, \$7.3; depreciation, \$24.8; sale of stocks, 4.5; sale of bonds, \$5.1.

³ Made up of \$29.6 billion in plant and equipment and \$1.8 billion in inventories.

There were also very large accumulations of liquid assets in preceding years, amounting to about \$5 billion in 1960 and an equal amount in 1959.⁴ If business conditions did not cause American corporations to invest these huge sums in past years, there is little prospect that the extra bonus of \$1.3 billion will be translated into investment. What is more likely to happen is that the overwhelming proportion will also pass into the cash reserves and swell them still further. There would seem to be little prospect that the investment credit will have any real stimulative effect. It will increase the power and wealth of the already powerful and wealthy.

We should also realize that a very large percentage of plant and equipment now lies idle and unutilized primarily because there is not adequate demand for the goods which could be produced at the prices charged.

The McGraw-Hill index of plant utilization is now at approximately 85 percent. Even though the 15 percent which now lies idle is partially composed of a "standby" reserve or is markedly obsolete, it is still true that the percentage of plant utilized is 5 or 6 percent short of what would be used under full employment. Can it be maintained that, if good machinery and equipment is thus allowed to lie idle because of a shortage in effective demand relative to prices, a bonus on investment would stimulate a still further increase in machinery and equipment? For would not this still further increase the already high percentage of idle equipment?

In addition, it should be realized that, while the purpose of the investment credit is to stimulate economic growth and to help business to compete more effectively in foreign markets, it would in fact be given all the way across the board without regard to the quality or social need for the investment. Thus, the credit would be available for such investments as a new ski-lift at Sun Valley or in Vermont, an escalator in a department store, new farm machinery to spread fertilizer on lands which are already overproducing, Klieg lights in a burlesque house, and martini-mixing machines in a bar. Other investments of an even more questionable nature would receive the bonus.

It is hard to see how this increases our efficiency as compared with other countries or whether this serves meaningful economic growth.

The 3-percent credit which is to go to utilities would be completely wasted and is wholly unnecessary.

The rate of return of the private utilities is regulated by both State and Federal bodies. If regulation is properly carried out, then any favorable tax consequences of the credit would be offset by reductions in the rates charged to consumers.

If not properly carried out, it would be an outright gift to the private utilities, for it would merely increase their rate of return above that set by the regulatory bodies.

In addition, the 3-percent credit for utilities has nothing to do with other stated purposes of the credit, namely, to help modernize industry or to make it more competitive in world markets.

⁴ John K. Landrum seems to come to the same general conclusion, although with somewhat smaller increases in liquid funds. See his Corporate Profits and Cash Flow supplement to testimony before Joint Economic Committee, Aug. 10, 1962, p. 1.

III

WHO HAS BEEN GETTING THE TAX CUTS?

Let us also note the way in which tax benefits and reductions have been made during these last 8 years. In 1954, accelerated depreciation, with the double declining balance and the sum of the digits methods, was authorized by Congress. This amounted to an initial loss of revenue to the Government of at least \$2 billion a year. This went to the industrial corporations and to the industrialists. At the same time the \$50 dividend exclusion and the 4 percent credit were passed in 1954 which gave \$400 million a year more to the owners of common stocks. This summer the Treasury has issued a new Bulletin F, permitting machinery and equipment to be depreciated much more rapidly. It is estimated that this will reduce business taxes by approximately \$1.5 billion a year. All of these taken together come to just short of \$4 billion a year.

Now we have this provision for the investment credit which will give the investors in machinery and equipment at least another \$1.3 billion annually. Thus, in 8 years we have decreased the annual tax burden on industry by over \$5 billion a year. This, of course, goes to the upper income groups in society who own the overwhelming proportion of the stock of American corporations.

During this period the low- and middle-income groups have received virtually nothing in the way of tax cuts. It is about time that the United States was less partial in its distribution of favors. This is true both on economic and ethical grounds.

IV

INVESTMENT CREDIT A FORM OF THE TRICKLE-DOWN THEORY

The basic way in which investment is stimulated and the economy moved forward is not by granting incentives for increased capital expenditures at a time when the existing plant and equipment is not fully used, but by increasing the demand for the products which the existing plant and equipment can produce which, in turn, will stimulate investment. In other words, the investment credit proposed is really a form of the trickle-down theory of economics which has largely been shown to be ineffective in the past. We believe instead in the theory that purchasing power should be built from the bottom up.

V

INVESTMENT CREDIT OPENS UP ANOTHER LOOPHOLE

Finally, the investment credit would open up more tax loopholes and would be quickly extended to other fields.

As nearly as possible a proper tax system should be neutral in the way it treats both income and expenditures. If we could have an absolutely just tax system it would probably make no distinctions as to the amount of tax to be paid on income or deductions for expenditures, no matter where the funds were derived or for what they were spent. It is the failure to carry out this principle which has so eroded our present tax system and which has made it so unjust.

For example, income from a wage or salary, in general, is taxed at the full rate, but income from oil, or from stock options, or from the cutting of timber, or from dividends, or from gains on the stock market, or from the sale of real property, among others, is taxed at lower rates and has special privileges not afforded to income from a wage or salary.

On the expenditure side, money spent for entertainment expenses, for business expense accounts, including yachts, club dues, and so forth, are deductible from taxable income, while the expenses of an ordinary person driving to and from work, or the payment of rent, or expenditures for the recreation or education of one's children are not deductible. These privileges for deductions and allowances go almost entirely to the strong, the powerful, and the well-to-do, and favor high income groups and unearned income as opposed to low income groups and earned income.

The main purpose of tax reform is to try to modify or to do away with some of these inequities and privileges in the tax laws.

What the investment credit does is to say that for social purposes we should give a special tax privilege for funds used to buy most kinds of depreciable property. At least as good a case can be made that society would be as wise to allow deductions for money spent for the education of children, for a future pension, or for preventive medicine rather than for capital investment.

Every legislator is pressed almost daily by some constituent or interest group to vote for a tax deduction for their particular interest. Once we start on this road it is almost impossible to stop. For this reason alone it is very unwise to give a special deduction for funds which are spent in this particular way; namely, for capital investment. It would be equally unwise to give deductions for most of these other proposals.

If the 7-percent tax credit is allowed on machinery and equipment, it will be only a short time before it will be granted on plant and buildings, and this will amount to another revenue loss of not far from \$1.5 billion. Indeed, proposals to this effect have already been made. Residential construction would not be left behind for long and this would take another \$1.5 billion away from our revenue. It would also be inevitable that the principle of H.R. 10 would find its way into enactment, and moneys devoted to purchasing voluntary retirement plans would be exempted from taxation. So would expenditures to educate children in college.

The final result would be that only income spent for current consumption would be taxed. This would be a kind of sales tax which would be highly regressive in nature and would weigh proportionately far more heavily upon those with lower or middle incomes than upon those with large resources. State and local taxation is already highly regressive. This is only made bearable by the fact that Federal taxation is progressive and hence introduces a kind of rough proportionality over the range of most incomes. To make Federal taxation also regressive or less progressive would in our opinion be grossly unjust. And yet that is precisely the end result toward which the opening of these loopholes would tend. We cannot acquiesce in these tendencies however well intentioned they may be.

THE DELETION OF WITHHOLDING ON DIVIDENDS AND INTEREST

I

GENERAL STATEMENT

By striking out of H.R. 10650 the plan for withholding tax from dividend and interest payments, this committee is, in effect, indicating that it condones the intolerable gap in the payment of taxes on dividends and interest, in many cases the result of outright and willful evasion. The Secretary of the Treasury estimates that in 1963 the gap between the dividends and interest that should be included on tax returns, and those that actually are, will exceed \$3.7 billion. This will mean a revenue loss to the Government of almost \$1.1 billion—\$440 million of taxes owed on dividends, and \$650 million of taxes owed on interest. Withholding would collect \$880 million of this \$1.1 billion. Withholding combined with the other collection and enforcement procedures available to the Internal Revenue Service would close nearly the entire gap. Without withholding, less than one-fourth of the gap can be closed. But even this cannot be accomplished until the Internal Revenue Service's new automatic data-processing system becomes fully operational in 1967.

Why must we forego hundreds of millions of dollars of additional revenue each year which is rightfully owed the Government? Why must the millions of honest taxpayers who conscientiously report their dividends and interest continue to pay more than their fair share of taxes in order to make up the \$880 million of lost revenue that could be collected through withholding.

Why must we continue to tolerate a tax system under which millions of wage earners pay their full share of taxes while many of those more fortunate individuals who have capital to invest are allowed to escape more than a billion dollars of taxes every year on their dividends and interest? Just look at the facts. As a result of the wage withholding plan, which has been in operation since 1942, only 3 percent of the taxes due on wages go unpaid. On the other hand, in 1960, more than 11 percent of the dividends that should have been reported on tax returns of individuals were not so reported. The situation is even more intolerable for interest where more than one-third (34 percent) is omitted from tax returns.⁵ Who are the people who do not pay their taxes on interest and dividends? Of the nonreported dividends, according to a sample of from 6,000 to 8,000 returns, about 70 percent were received by individuals with *more* than \$10,000 of income. Of

⁵ The dividend and interest underreporting gaps are estimated from aggregate figures of the amounts of such payments to individuals and of the amounts reported by individuals on their tax returns. This method has also been used by the New York Stock Exchange and independent tax experts whose estimates have corresponded closely with Treasury estimates.

For dividends, the estimate is based on cash distributions to stockholders by domestic corporations, as reported in the Internal Revenue Service Statistics of Income, and adjustments are made to add foreign dividends received by individuals, and to exclude dividend payments to corporations, tax-exempt organizations, and persons not required to file tax returns and to exclude distributions which are not taxable or are capital gains. The balance presumably should appear on individual tax returns if there were complete compliance in tax reporting.

The interest underreporting gap has at times been estimated starting from the Commerce Department's estimate of interest receipts by individuals, unincorporated businesses, and nonprofit institutions. The Commerce Department's concept of personal interest income includes about \$10 billion of imputed interest (largely interest assumed to be earned on bank deposits, which is not paid to individuals but is absorbed by the bank in lieu of service charges). The large adjustments involved in the Commerce Department concept cast a good deal of doubt upon such a gap estimate. In consequence, the Treasury has used a different approach, namely, estimating directly amounts of interest payments to individuals and then deducting certain relatively small amounts of interest received by sole proprietors as business income, by individuals not required to file tax returns, and by tax-exempt organizations.

the nonreported interest, only about 30 percent was received by people with less than \$5,000 of income, while approximately 30 percent was received by those with incomes of more than \$10,000. If a withholding system is appropriate for the lower income wage earners, to make sure they pay their taxes, then what possible excuse can there be for not applying it to help collect the taxes on dividends and interest from the many higher income individuals who escape those taxes today?

The answer that is given is that withholding would be too burdensome and that it would hurt too many people. In addition, we are told that the committee's substitute, an expanded information-reporting system, will give the Internal Revenue Service all it needs to collect most of the unpaid taxes. Neither of these propositions can be supported.

II

INFORMATION RETURNS NOT A SUBSTITUTE FOR WITHHOLDING

The Commissioner of Internal Revenue, the man who actually does the job of collecting our taxes, has carefully studied both the withholding plan and the expanded information-reporting program and has concluded that information reporting, even when coupled with the Service's new automatic data-processing system, cannot be an alternative to withholding. This is because an ADP information return system in itself will not collect one penny in taxes. All it can do is identify possible discrepancies which then must be followed up through the ordinary collection and enforcement procedures available to the Internal Revenue Service.

The figures⁶ tell the story themselves:

Of the \$850-million gap in the reporting of taxes on dividends and interest, withholding *alone* would recover \$650 million at a cost of approximately \$19 million. The remaining \$200 million could be recovered in large part by the ADP system, combined with a reasonable enforcement effort for an estimated additional cost of \$29 million. In other words, the entire gap could be closed through a combination of withholding and enforcement for a cost of only \$48 million.

To close the entire gap without withholding would be physically impossible and economically unfeasible. It would mean contacting 12 million people for the purpose of checking discrepancies in their dividend-and-interest reporting turned up by ADP. This is three times as many people as the Service contacts today in its total enforcement program. It would cost \$400 million to collect the \$850 million by this method, more than eight times the cost if withholding were used.

Even if we were to collect all of the \$650 million (the dollar equivalent to the results under withholding), it would cost \$200 million to collect this amount, or more than 10 times what it would cost under withholding. In addition, the Internal Revenue Service's present enforcement staff, which through its activities collects about \$3.5 billion annually, would almost have to be doubled to collect the additional \$650 million. The resulting imbalance in enforcement effort is one that cannot be reconciled with any sound concept of tax administration.

⁶ These figures are based on the 1959 revenue gap estimate of \$850 million. It is estimated that this gap will rise to \$1.1 billion in 1963.

To look at the matter realistically, and within the concept of a sensible and effective use of equipment and enforcement manpower, based on 1959 data, the information-reporting system adopted by the committee can be expected to recover only \$200 million.

These figures, which were compiled by the Commissioner and his staff after careful study of the matter, conclusively prove that the information-reporting system adopted by this committee is not a substitute for withholding.

Even apart from its complete ineffectiveness as a tool for closing the more than \$1 billion gap in the reporting of taxes on dividends and interest, the information-reporting plan adopted by the committee is at best a clumsy and burdensome substitute for the relatively simple withholding plan adopted by the House. Under withholding, a payer of dividends or interest would merely be required to deduct a flat 20 percent from its payments to persons who have not filed exemption certificates and then make one lump-sum payment to the Government each quarter. The payers will not have to make out individual withholding receipts for each recipient nor will they be required to submit any detailed records to the Government.

The burdens under the information-reporting plan will be substantial when compared to this. At the end of the year, each payer will be required to add up all the dividend or interest payments it has made to a person during the year and, if they equal or exceed \$10 in the aggregate, make out an information return showing the name and address of that person and how much was paid to him during the year. Then this information must be filed with the Government and a copy given to the recipient. This means that the payer must make a reasonable effort to obtain the current address and account number for each of its depositors or stockholders. Translated into numbers, payers of dividends and interest will be required to complete and file with the Government 100 million pieces of paper each year and then distribute an additional 100 million copies to their depositors or stockholders.

The savings and loan industry has admitted that this information reporting plan will involve heavier administrative costs for them than withholding.

III

WITHHOLDING IS AN EFFICIENT AND EFFECTIVE METHOD TO CLOSE THE GAP

The withholding plan included in H.R. 10650 as passed by the House of Representatives has been grossly misrepresented and distorted by its opponents. They have fostered widespread misunderstanding of the plan and aroused baseless fears.

Basically, the plan is very simple. The institution which pays interest, dividends, or patronage dividends would be required to deduct a flat 20 percent from these payments and remit the total amount to the Government once a quarter. The plan includes several relief provisions which would insure that individuals and other taxpayers who owe little or no tax on their dividend and interest income will not be unduly harmed by withholding. These three basic objections have been made to the plan: it would hurt many people with low incomes who depend on their dividend and interest income for living

expenses; it would result in a maze of paperwork and confusion for the taxpayer; and it would impose heavy burdens on the paying institutions. We have already pointed out that withholding would be far less burdensome to the payers than the new information reporting plan. The other two objections are equally groundless.

1. Withholding would not hurt low-income individuals

There have been repeated accusations that withholding will unfairly deprive low-income people of funds which they need to meet their living expenses. This is just not true. Those with such low incomes that they do not owe any taxes could completely avoid withholding in most every case merely by filing simple exemption certificates with the paying institutions. Children under age 18 would be exempt from withholding regardless of their tax status. There can be no hardship for these people since withholding will not even apply.

It is true that there would be some people who, although they owe some tax, would be subject to overwithholding. These people, however, can obtain quarterly refunds of the overwithheld tax merely by filing a simple refund claim. Under the ordinary procedures, the refund would be paid within 3 to 4 weeks after the claim is filed. The Internal Revenue Service has developed a system whereby an individual who claims a refund for the first quarter will automatically be mailed claims for the next two quarters to insure that he does not forget to claim his refund. What is the hardship to these people? It is merely the loss of the interest that could be earned on the overwithholding for the first quarter, since the quarterly refund for the first quarter would offset the overwithholding in the next quarter and so on indefinitely.

The efficiency of these provisions in preventing hardship can best be shown by an illustration. Under the present law, which gives people over 65 a double exemption and also a tax credit on retirement income, an elderly couple (where it is claimed hardship will be most common) can have as much as \$5,377 in income each year from social security and interest and yet be liable for no tax and, consequently, no withholding. Such a couple would be receiving the maximum social security benefit of \$2,178 and interest income of \$3,199. This amount of interest represents a savings account of about \$80,000 earning interest at 4 percent.⁷

An elderly couple receiving the maximum social security benefit and \$4,199, rather than \$3,199, of interest would fall into the overwithholding category. The withholding each quarter would be \$210—\$160 more than their tax liability. Under the quarterly refund procedure, this couple would never be out of pocket more than the \$160 of overwithholding for the first quarter. Even if the \$160 must be withdrawn from the couple's savings account, it would mean a loss of

⁷ The following is a schedule showing the tax computation for the couple in the example:

Total income.....	\$5,377
Less social security benefits.....	2,178
Income subject to tax.....	3,199
Tax before retirement income credit (computed from optional table on the basis of 4 exemptions and the standard deduction).....	92
Retirement income credit.....	92
Tax liability.....	

The example assumes that $\frac{2}{3}$ of the social security benefits are received by the husband and $\frac{1}{3}$ by the wife, which is typical where the husband has been the wage earner.

only \$6.40 for an entire year, representing the interest on \$160 if left in their savings account at 4 percent. This \$6.40 loss must be analyzed in the context of the \$105,000 savings account which this couple must have to earn \$4,199 of interest for the year.⁸ Is there hardship in this case?

When compared to wage withholding, the overwithholding involved in dividend and interest withholding is minimal. About 37 million refunds representing overwithholding on wages are made each year with little or no complaint on the part of the taxpayers. This was about 60 percent of the wage returns upon which taxes were paid. The average return for the 37 million wage refunds amounts to about \$142. Even taking into account the fact that quarterly refunds will be permitted, only about one-fifth as many refunds will need to be made under dividend and interest withholding as under wage withholding. To look at it another way, 14.3 percent of the taxes collected by wage withholding must be refunded; the comparable figure for dividend and interest withholding is only 5.5 percent and most of this will be returned *quarterly*.

It is clear that hardship to low-income individuals cannot be used as an excuse for abandoning withholding. There just is no such hardship.

2. Withholding will be a simple and efficient means for an individual to pay his taxes on dividends and interest

It has been claimed that withholding will result in a maze of confusion for the American taxpayers. For the great majority of taxpayers, the only burden caused by withholding will be two additional computations on the tax return—those involved in a simple schedule. In addition to entering the amount of his dividends and interest on the return as at present, the taxpayer will, as a result of withholding, be required to divide this amount by four and then add these two amounts together to determine the amount of his dividends and interest to be reported as income and the amount of credit he is permitted for the withheld tax. This is the extent of the “maze of confusion” for the taxpayer.

For many taxpayers, withholding will actually reduce their paperwork, by eliminating the necessity for filing quarterly estimated tax returns.

Those who raise this objection completely ignore the fact that most Americans already operate under a much more complicated withholding system on their wages, with no maze of confusion. It is to ignore reality to say that they will not be able to adapt to the much simpler system for withholding on dividends and interest.

IV

WHO WILL BE HURT BY WITHHOLDING?

Withholding will definitely hurt a sizable group of individuals—those who fail to pay the taxes due on their dividend and interest income. It is only fair to the millions of taxpayers who already do

⁸ It has been argued that the loss from overwithholding will really be much greater because of the compounding factor. Assuming a savings account where interest is credited quarterly, the loss of interest on the \$160 over a 10-year period will only amount to \$78.22 taking into account the compounding. This is an average loss of \$7.82 each year, which is still minimal when compared to the \$105,000 savings account involved.

this that these individuals be required to do the same. One of those who signed this report received 75,000 letters on withholding and a sampling of these letters showed that between one-third and one-half of them were from people who thought withholding represented a new tax on dividends and interest. Another large group thought withholding was a tax on capital.

V

SUMMARY

Withholding on dividends and interest is urgently needed—without it, this country will continue to forfeit billions of dollars in revenue that is rightfully owed by those individuals who are not assuming their fair share of the tax burden. Information returns and ADP are not a substitute for withholding.

EXPENSE ACCOUNTS

One of the best known and most resented special privileges in the tax law today is the deductible expense account. President Kennedy described this tax giveaway as “a matter of national concern.” The House of Representatives agreed. After long and careful consideration it passed a provision which, although falling short of the President’s recommendations, would go a long way toward a fairer set of rules. It would permit deductions for entertainment more closely related to the conduct of business but would cut out deductions for many of the highly personal expenditures permitted under present law when the taxpayer can make a showing of some connection between the entertainment and the taxpayer’s trade or business.

The allowance of deductions for such essentially personal entertainment has brought the integrity of the entire revenue system into disrepute. The expense account deduction has been a breeding ground for fraud and misrepresentation. It has encouraged disrespect for honest self-compliance with the tax laws among those not in a position to claim such deductions, but who have watched others satisfy their personal amusement at the taxpayers’ expense.

What has the Finance Committee done with the House bill? It has simply pulled the teeth from the proposal, leaving it merely with a dangling tongue—a tongue which is certain to confuse taxpayer and Government official alike as to what it is trying to say. Certainly the vague and almost meaningless standard adopted by the committee will do very little, if anything, to change the style of operation of those who have been living high on their expense accounts at the cost of their fellow citizens.

Let us be more specific.

I

THE PROBLEM

The basic problem is whether this country can continue to afford to permit a small group of taxpayers to take tax deductions for highly personal items such as nightclub hopping, fancy yachts and swanky country clubs while the great majority of their fellow taxpayers cannot take such deductions. From a practical point of view the concern of the Nation is not only the basic unfairness of this situation (in itself

a vital consideration) but it is also the effect that this legally created unfairness has upon those who are discriminated against. It makes them resentful of the law which permits such a situation to exist and encourages them toward laxness in discharging their full tax obligations. It is quite natural to feel: "Why should I help keep that fellow on the gravy train—paying for his fancy yacht and swanky country club?" An expansion of this type of thinking could eventually destroy our tax system, the keystone of which is its voluntary character. We rely on each taxpayer to be his own tax assessor. The essential honesty of our citizens and, most important in this context, their respect for our tax laws, has enabled this system of voluntary self-assessment to function most effectively. However, like all good things, the system must be nurtured and protected.

Expense account abuses have become a real threat to the continued effectiveness of our self-assessing system. Much taxpayer distaste has already been voiced against this unwarranted privilege. The danger signals are loud and clear. In his testimony before the House Ways and Means Committee and the Senate Finance Committee, the Secretary of the Treasury documented the situation in great detail with numerous case studies and many samples of editorial comment from all over the country. Let's examine a few of these.

A corporation engaged in manufacturing was allowed to deduct \$991,665 in 1959 for yachts, club dues, shipboard conventions, hunting and fishing trips and parties.

A taxpayer engaged in the insurance business was allowed to deduct \$97,500 for meals, lodging, transportation, entertainment, tickets, books, gifts, et cetera. The amount covered \$6,000 for an apartment and over \$30,000 for food, beverage, and other entertainment.

A manufacturer was allowed to deduct over \$34,000 spent on liquor, football tickets, parties, and a speedboat. The expenses for liquor alone totaled \$13,750.

A family-held ship repair corporation was allowed to deduct \$23,758 for a Christmas dinner and party.

An enterprising banker effectively combined sentiment with business when he deducted, as present law permitted, a substantial part of the cost of his debutante daughter's coming-out party on the ground that some of the guests had business connections with him.

In another case, the taxpayer was allowed \$115,000 for entertainment and gifts. His expenses included \$7,500 spent at a resort hotel; \$5,400 for food, liquor, and cigars for his office and farm; and \$8,700 in cash to officers of his closely held corporation for entertainment.

A beverage manufacturer claimed and was allowed \$10,903 for entertaining customers at the Kentucky Derby.

Huge sums are allowed to business taxpayers in connection with maintenance and operation of yachts and other fancy boats. One manufacturer was allowed to deduct \$253,000 for the expense of his yacht. Another was permitted to deduct \$112,000 for such expenses (as well as an additional amount of \$362,000 for a ranch-hunting lodge, nightclub, and other similar expenses). A company in the business of selling fuel was allowed \$93,000 as deductions for a yacht, a fuel products company was allowed \$23,000 and an auto dealer was allowed yacht expenses of \$22,000.

A cake and cookie bakery was allowed \$66,000 for a yacht on which to entertain supermarket and chainstore buyers and branch managers.

Despite its rather sad undercurrents, both from the viewpoint of the tax system as well as otherwise, one of the most interesting cases is that in which a mortuary business was allowed \$26,495 for yacht expenses to entertain visiting morticians, clergymen, and for meetings of employees.

These cases could be multiplied by the thousands. Similar large expenditures are constantly being made on hunting and fishing lodges, on elaborate beach resort homes, on exotic island retreats, on extended hunting trips, including plush safaris to far off Africa and India. Indeed, just about every kind of human activity in the nature of fun and frolic is being well subsidized on behalf of a privileged few by the average taxpayer who does not happen to be engaged in a trade or business so as to enable him to join in this Government-supported high life. Is it any wonder, then, that such strong taxpayer resentment has developed against the expense account privilege. Clarence Randall, former chairman of the board of one of America's largest steel companies has vividly expressed this taxpayer resentment in the following words:

Gone are the days when a salesman occasionally wined and dined his favorite customer, or perhaps gave a small theater party. Nowadays, when the deal gets big enough, the company yacht weighs anchor and moves into position, the company plane takes off for a duckblind in Arkansas, or the best hotel in Miami throws open its doors to expectant dealers for a week of continuous circus.

The distaff side is cut in, too, on both sides of the deal. How the ladies love it. With jet travel what it is, those who were getting a little tired of White Sulphur may now hope to look in on Capri or the Riviera.

The unseen partner in all this largesse, of course, the man who rides the afterdeck of the company yacht, copilots the duck hunters' plane, sits by while the caviar is spooned out and the crepes suzettes are sizzling, the man who splits the check at the nightspot and hands the big bill to the head-waiter, is none other than Uncle Sam. * * *

But who are the silent underwriters of this frenetic spending? You and I, the general taxpayers. It is we who make up to the U.S. Treasury the revenue lost through expense-account deductions.

The important point to be derived from the foregoing is that all of the expenditures described were deductible under the broad standard of present law which permits the deduction of "all the ordinary and necessary business expenses" of the taxpayer. The fact that there is a business relationship, actual or even only hoped for, between the parties does not prevent them from enjoying the fancy resort living, the cruise on the expensive yacht, or the fancy night-club.

Suppose company A sells its product to company B. If a sales executive of company A invites his close friend, an executive of company B, to join him for a cruise on his yacht, who can say that the executive of A did not intend to promote the business relationship between the two companies? The fact is that in the usual case the businessman's friends are his business customers or prospects. Under

the test of present law, so long as this business connection exists between entertainer and entertained, the parties can enjoy tax deductible vacations in Bermuda, cruises on yachts and evenings in luxury nightclubs on a tax deductible basis. This can be done on a reciprocal arrangement of "you entertain me and I'll entertain you," with the Treasury paying half the bill for each. Business does not have to be discussed nor need the entertainment follow or precede business discussion. The taxpayer need not even be present at the entertainment. Because of absence of restrictions, taxpayers are encouraged to ask "Why should not I deduct my personal pleasures and entertainment, if everyone else can?" Because of this the expense account problem has grown to its present unmanageable proportions.

II

HOUSE SOLUTION TO THE PROBLEM

The test adopted by the House of Representatives is that the expense of an entertainment activity will not be deductible unless "directly related to the active conduct of the taxpayer's trade or business." Where an expense connected with a facility such as a yacht or a hunting lodge is involved, the taxpayer must also show that the facility "was used primarily for the furtherance of the taxpayer's trade or business." On its face, this standard seems almost as broad as present law and would appear to present many of the same problems.

However, in its report the House Ways and Means Committee has explained its test in a way which provides a number of tangible, practical, and meaningful guidelines: The report states that under its test the taxpayer—

* * * will have to show more than a general expectation of deriving some income at some indefinite future time from the making of the entertainment-type expenditure; however, he will not be required to show that income actually resulted from each and every expenditure for which a deduction is claimed.

If the expenditure is for entertainment which occurs under circumstances where there is little or no possibility of conducting business affairs or carrying on negotiations or discussions relating thereto, the expenditure will generally be considered not to have been directly related to the active conduct of business. Thus, the absence of the taxpayer or his representative from the entertainment activity ordinarily indicates that the entertainment was not directly related to the conduct of the taxpayer's trade or business. Similarly, if the group of persons entertained is large or the distractions substantial, the cost of the entertainment will not be deductible, in the absence of a clear showing of a direct relationship to the active conduct of the trade or business.

This clear statement of legislative intent coupled with the statutory language provides a workable and reasonable solution to the difficult expense account problem and should go a long way toward reducing the abuses outlined above. However, critics of the House proposal attacked this crucial committee report statement on the ground that it had no support in the statute.

In view of the broad language of the statute, requiring explanatory implementation to make it useful, this contention is baseless. The true reason for the complaint is the fact that the statute as interpreted by the Ways and Means Committee report has some real teeth in it.

Even so, we are not asking that the business community adopt Spartan standards. The House bill, which we hope will be restored, recognized the general custom of business entertaining at meals in restaurants. It specifically permits the deduction of entertainment presently allowable through furnishing food and drink in restaurants and hotels in an atmosphere conducive to business discussion. No business need be discussed. It thus leaves undisturbed the most significant portion of goodwill entertainment conducted in this country. It strikes only at the high, wide, and fancy living and indulgence in personal pleasures which all taxpayers ought to pay for themselves without Government subsidy.

III

FINANCE COMMITTEE SOLUTION—FORMULA FOR CONFUSION

The only change in the pertinent House statutory language made by the Finance Committee is the addition of the words "or associated with." Thus, a taxpayer can deduct an entertainment expenditure which is only "associated" with the active conduct of his trade or business, as well as one which is directly related thereto. Since this statutory language is quite similar to that of the House bill one would reasonably expect again to find a helpful explanation as to what the committee intended to accomplish by its additional phrase "or associated with."

Unfortunately, such is not the case. Unlike the clear, concise, and workable guidelines set forth in the House report the Finance Committee report is a mass of vague, disconnected statements and examples which are destined to spawn controversies more numerous and intense than those which occur with such disturbing frequency under present law.

Although the Senate report attempts to paint a picture of virtue and righteousness, even a casual glance beneath the surface reveals that the virtuous exterior is more illusion than reality. For example, the report states:

* * * Nothing in your committee's bill is to be construed as allowing a deduction for any expense which is against public policy or which violates the public conscience. Deducting an expense incurred for such purpose under the guise of generating "business goodwill" will not be condoned and under your committee's amendment is not deductible. Thus, the cost of liquor purchased for the entertainment of customers and the promotion of goodwill (which under existing law has been held deductible) will be disallowed if the serving of liquor violates the public morals of the community as expressed in local law. Another example of expenses for immoral purposes which have been claimed on tax returns under existing law involves expenditures to provide "call girls" for the purpose of entertaining clients. Under your

committee's amendment no deduction whatsoever is to be allowed for expenditures of this nature. In no legitimate sense are they "directly related to or associated with the active conduct" of a trade or business.

The foregoing suggests that the committee's action will serve as a moral broom to disallow expenditures where liquor is illegal under local law, and where "call girls" are utilized as "business" entertainment. However, expenditures such as these, which violate clearly defined lines of public policy, are not deductible under present law. See *Smith*, 33 T.C. 861 (1960); *R. E. L. Finley*, 27 T.C. 406 (1956); *U.S. v. Winters*, 261 F. 2d 675 (1958). What then will be accomplished under the committee's language? Is it not clear that this is simply a smokescreen thrown up to suggest that abuses are being remedied whereas in actuality little, if anything, is being accomplished beyond present law?

The Finance Committee report stresses the desirability and wholesomeness of "goodwill" entertainment. It states:

Goodwill has long been recognized as a legitimate objective of business entertaining and where the purpose of the expense and its clear relation to a business is firmly established, *the expense ordinarily will continue to be deductible*. [Emphasis added.]

The report further states:

To eliminate the harshness resulting from the House report, amendment of the language of the House bill is necessary.

* * * This new language will permit deduction of expenses for entertainment, amusement, or recreation incurred for the creation or maintenance of business goodwill without regard to whether a particular exception applies. However, this new language will apply only if the taxpayer demonstrates a clear business purpose and shows a reasonable expectation of deriving some income or other benefit to his business as a result of the expenditure. If he meets this test, the expenditure will be considered to be associated with the active conduct of his trade or business; otherwise, the expense will be disallowed under your committee's amendment.

A close analysis of these statements makes it eminently clear that expenditures for goodwill have been given preferred status. In these references to "goodwill," the committee has presented our sophisticated expense account society with a blueprint for continued high living at Government expense. These statements constitute a formula which will leave the Internal Revenue Service with an impossible enforcement task, for, in effect, almost all entertainment expenditures, both for the creation and maintenance of business goodwill are declared to be henceforth deductible. In stating that the taxpayer must demonstrate a clear business purpose and show a reasonable expectation of deriving some income or other benefit to his business from the making of the entertainment expenditure, the committee report has added nothing to the requirements of present law. The taxpayer must meet precisely the same test today, but, as hundreds of cases illustrate, such vague and generalized requirements at present are so easy to meet as to be practically meaningless.

Furthermore, although the committee report makes numerous references to goodwill, it gives no indication as to what is encompassed by this term. Nowhere is goodwill defined. How does a businessman go about creating goodwill—whatever goodwill is? It seems clear that the sky is the limit. If a businessman—in his judgment—thinks a big yacht may be helpful in developing some customers, doesn't this committee report language put the official congressional stamp of approval on his deduction of these substantial costs of maintaining and operating such a "business" asset? Is not a revenue agent foreclosed from effectively examining into the matter?

In the light of all the foregoing statements respecting good will, very little is salvaged from the following comment—particularly in view of the illustration given as to what is meant by "vague goodwill."

Where good will generated by the expense is vague or where the possibility of the expenditure resulting in the production of income is remote, no deduction will be permitted. For instance, under present law a taxpayer may deduct expenses of entertaining buyers and others associated with his trade or business even though at the time he does the entertaining he already has more business than he can handle. Under you committee's amendment, however, no deduction will be allowed because, with a large backlog of unfilled orders, such entertainment ordinarily cannot be regarded as being associated with efforts to produce income.

This narrow "exception" to the basic theme of the Finance Committee report that all good-will entertainment is deductible is scant evidence of tightening up present law. Rare indeed is the case where the taxpayer has such a backlog of unfilled orders that his entertainment activities cannot be regarded as being associated with efforts to produce income. It is interesting to note that even in such an extreme case the report hedges the consequences by providing that "ordinarily" the deduction will not be allowed. Moreover, there is a good possibility that entertainment expenditures in such a unique case are not deductible under present law because they are in the nature of capital expenditures. Cf. *James Schulz* (16 T.C. 401). Here again the committee has done nothing more than set up a strawman—to give the illusion that a cutback on existing law is being effected. In reality nothing has been accomplished—except that perhaps another arena for conflict has been created.

The "harshness" of which the report speaks is that the House provision, as explained by the Ways and Means Committee's report, has some effect and will disallow some entertainment expenditures which are deductible under present law. Presumably that is the purpose of this legislation. However, one must struggle hard to tell which of the above-described cases would be denied deduction under the Finance Committee report. How much, if anything, would be disallowed to the corporation which spent and deducted almost \$1 million in 1 year for yachts, club dues, shipboard conventions, hunting and fishing trips, and parties? Does not a corporation make such expenditures to develop good will? We have already seen that good-will expenditures are clearly deductible under the Finance Committee report. How about the banker who deducted a substantial part of the cost of his

daughter's coming-out party as a business expense? Wasn't he also developing customer good will? Certainly the Government is not, under the Finance Committee report, free to disallow expenses regardless of the form of entertainment the taxpayer may adopt to develop good will. Similarly, in all the other cases set forth above, the taxpayer would appear to be able to continue to deduct all entertainment expenditures.

Under the Finance Committee report, do yachting expenses continue to be deductible? If not, then the report should clearly so state. Does the cost of maintaining hunting lodges for entertainment continue to be deductible? If not, then the committee report should so state. Is the cost of wining and dining at nightclubs deductible? If not, the committee report should clarify the situation. Do tickets at \$30 apiece for musical comedies continue to be deductible? If not, the committee report should so indicate or provide some standard or guideline by which the answers to these questions can be determined by the taxpayers and revenue agents who will be left floundering in their attempts to know what the rules are.

One further "red herring" in the Finance Committee report should be mentioned. The report states that no deduction will be allowed for entertainment expenses "which under the circumstances in which they are incurred are lavish or extravagant." Here again no standards or guidelines are furnished. What is lavish or extravagant under the circumstances? If the circumstances involve a taxpayer accustomed to entertaining in an elaborate and expensive style, can they be held to be "lavish" under the circumstances? When does a yacht become an extravagant expenditure? When it is 60 feet in length? 100 feet in length? Would these criteria vary with the income (or expected income) of the taxpayer? Would a resident of Miami Beach, Fla., be entitled to a bigger and more expensive yacht than a resident of Providence, R.I.? Would a beach home with eight rooms be a lavish facility? What about one with 30 rooms? Would a corporate president be entitled to drink champagne whereas a vice president could have only a whisky highball and a proprietor of a country grocery store only ordinary corn liquor?

Is it not abundantly clear that the so-called "test" produced by the Finance Committee, superimposed upon the unsatisfactory test of present law, will simply compound existing difficulties? The litigation and controversy which would follow adoption of such meaningless language would even make the present situation seem a happy one. The result would be a real mess. And to what avail? In this posture of things, it seems quite proper to ask—what is wrong with the proposal adopted by the House of Representatives? It is obviously far superior to the Finance Committee's product. We urge the Senate to approve the House provision or the President's original proposal and again, as it did in 1960, produce a really significant legislative measure to deal with expense account abuses.

THE DEDUCTION FOR CERTAIN LOBBYING EXPENSES OF TAXPAYERS WITH BUSINESS INCOME

Section 3 would permit the deduction of certain lobbying expenses by taxpayers with business income. This would depart from a salutary principle which has been part of the income tax law since World

War I. It would provide unwarranted tax reduction where it is least needed for reasons which are specious. It would introduce novel distinctions into the tax law, producing new requirements difficult for the Internal Revenue Service to administer. The specific language in which the deduction is cast contains ambiguities which will create continuing uncertainty as to its exact meaning, and, most important, the relationship of this provision to the whole process by which our citizens seek to influence the enactment of legislation at all levels of government was not adequately considered. Section 3 should be deleted from the bill.

Under existing law the costs of efforts to influence legislation are not deductible, a rule applicable to *all* taxpayers. Whatever the motive for a citizen's efforts to influence legislation, he now bears the whole cost of that effort himself. No part of the expense can be passed on to the Federal Government through an income tax deduction. In the constant competition for legislative favor and results at National, State, and local levels, the Federal Treasury stands neutral—and properly so.

Section 3 would change all that. It would amend section 162 of the Internal Revenue Code of 1954, the section creating the general authority for deduction of the ordinary and necessary expenses of business operation. Section 3 would add a new subsection specifically authorizing deduction of lobbying expenses in certain categories by taxpayers with business income. Only those taxpayers with business income would receive any benefit. All others would still be subject to the existing rule of no tax benefits for lobbying, a result which follows necessarily from incorporation of the amendment in section 162 and one which is specifically spelled out by the House committee report.

Some specific typical examples will bring this into sharper focus. Suppose a measure is being considered, as many have been, involving a proposed change in the standards or testing procedures for food, drugs, or cosmetics. The costs of presenting the views of drug manufacturers and distributors would be deductible. The cost of presentations on behalf of consumers or of disinterested professional or technical advisers would not be. Or suppose that a State legislature is debating a measure designed to decrease stream pollution. Manufacturers who would be adversely affected by its enactment could deduct the cost of opposition. Members of the public interested in pure water for drinking or for recreational uses would have to finance their support of the measure entirely from their own pockets. Or, at the local level, a business owner of a piece of real estate could seek advantageous amendment of the local zoning ordinance, deducting the cost of his presentation before the local city council. The owners of nearby residences would not receive this help from the Federal Treasury in preparing the exhibits and briefs necessary for effective opposition.

These are discriminations impossible to justify. Can anyone seriously contend that consideration of legislative proposals affecting business taxpayers is seriously handicapped by absence or weakness of expression of business viewpoints? Is there any evidence that business taxpayers, individually or collectively, are now deterred from expressing themselves on these subjects by the present rule of tax neutrality which permits no deduction for lobbying expenses? To

ask these questions is to answer them. Of all viewpoints on legislative proposals, those of business are consistently the most ably represented before the Congress and before State and local legislative bodies. Why then should the cost of lobbying activities of taxpayers with business income be singled out for this preferential tax reduction? No adequate reason has been given.

Any discrimination at all among citizens in the exercise of their constitutional right to petition their representatives is patently undesirable. Discrimination by preferential tax deduction is magnified as the amounts spent for these purposes increase. Modern efforts to influence legislation cover a wide range of techniques, some of which are very costly. One can send a letter to his Senator for 4 cents. However, to stimulate tens of thousands to do so requires the expenditure of large amounts running sometimes into the hundreds of thousands, even millions, of dollars. But all this is well known. It has been thoroughly documented many times.

The application of section 3 would not be confined to nominal amounts. It would permit the deduction of some very large sums. In addition to provision for deduction of the costs involved in direct contacts with legislators (personal calls and visits, appearances before committees or statements filed with them), the cost of efforts to influence legislation indirectly are also made deductible in some instances. The costs of communications to organization members and to shareholders and employees have all been blanketed in.

When section 3 is applied to today's scene, we find that it will authorize giant corporations to deduct the cost of communicating the views of management officials to hundreds of thousands, even millions, of shareholders and employees, for the purpose of influencing them with respect to current controversial legislative proposals. To use a painfully familiar example, section 3 would authorize deduction of the cost of campaigns designed to produce a flood of letters opposing withholding on dividend income.

Under existing law these sums are not properly deductible—and never have been. To permit deduction now would shift a very large proportion of these heavy costs to the Federal Treasury, a disguised subsidy for which there would be no justification.

The effects of such subsidized efforts to influence legislation indirectly would not be confined to the recipient members, shareholders, and employees. The views expressed and their source would frequently come to the attention of families and friends of the recipients, thereby broadening the scope of the influence subsidized by the Federal Treasury. Of course, the benefits of section 3 as they would apply to these broadcast efforts to influence legislation can only benefit very large organizations. Small business taxpayers, as well as nonbusiness taxpayers, would have little or no use for it and could well suffer from its use where their interests on legislative matters are opposed to those who could take advantage of it.

True, not all lobbying costs of business taxpayers would be made deductible by section 3. The bill purports to create limitations which will restrict the kind of expenses for which a deduction can be claimed. Thus, to qualify for the deduction, the legislative proposal must be of "direct interest" to the taxpayer. In addition, specific provisions deny deductions for political campaign expenses or for efforts "to influence the general public, or segments thereof." How-

ever, a close inspection raises genuine doubt as to the precise meaning and application of these restrictions. They may, in fact, prove largely illusory.

Thus, one might ask, What subjects are not of "direct interest" to a large corporation? Any measure involving a tax or a change in the regulation of business or the marketing of securities or foreign trade or the terms of employment or labor relations or the monetary system will have some impact on every substantial business enterprise. Is it intended that the cost of testimony or statements or communications to shareholders or employees on this entire range of subjects is to be deductible? Similarly, can the prohibition against deductions for political campaign purposes be really effective? Granted that the cost of a folder urging shareholders to vote for Jim Darkwater will not be deductible, what of the cost of a folder urging a position on the principal issue dividing Darkwater from his opponent Bob Cleanriver? Can issues and the candidates be separated so easily? It is doubtful. Section 3 thus could make slightly veiled political contributions deductible. The benefit would not be universal though. To return for a moment to the anti-water-pollution measure used as an example before, suppose Darkwater is against it and Cleanriver is for it. The former's supporters could deduct the cost of their literature discussing the antipollution measure (and thus their support of Darkwater); supporters of Cleanriver could not.

Obviously, congressional memories are very short. For at least a century Senators and Representatives have regularly inveighed, individually and collectively, against lobbyists and their activities. The need for substantial disclosure by lobbyists, particularly in financial respects, has long been recognized. When a person or organization becomes a lobbyist, he is required to register as such and thereafter to report quarterly his expenditures for these purposes. In spite of these safeguards, every few years some lobbyists become so bold and their overreaching so bad that a special inquiry is required. A prime example was the creation in the 84th Congress of the Senate Special Committee To Investigate Political Activities, Lobbying, and Campaign Contributions. Its report states graphically the kinds of abuses which occur and the large sums of money available to be spent on efforts to influence legislation. Sugar quota bills attract lobbyists like flies and, like flies, their activities are not widely admired. The Senate Foreign Relations Committee is currently beginning an investigation of another group of lobbyists, an inquiry which has grown in large part out of concern for their lucrative financial arrangements. Nor are problems with lobbyists confined to Washington. Their influence on State legislators and their sometimes questionable methods in State capitols is notorious.

When projected against all this experience, section 3's proposed financial bonanza for one group of lobbyists and their employers seems ironic in the extreme, if not downright cynical.

There is no challenge here to lobbying per se. It is unquestionably legitimate. A constitutionally protected right of our citizens, it often supplies useful information and reactions on pending legislation. However, it would be foolish to exalt it unduly for these reasons. At best, lobbying is a mixed blessing for it is almost always exclusively concerned with self-interest rather than the broad public interest. Fortunately, section 3 presents only a narrow problem, viz., whether

or not the lobbying done by one segment of our society—taxpayers with business income—should be entitled to support from the Federal Treasury.

A number of arguments are made in favor of this measure. Some of them have a surface plausibility, but on close analysis none of them holds water. The issue is actually a simple one. We begin with a longstanding rule that all taxpayers, business and nonbusiness, who seek to influence the work of legislative bodies, National, State, or local, pay their own expenses in full without assistance from the Federal tax system. This neutral posture of the tax law is a healthy one and should be defended and strengthened. Legislation affects all our citizens. It is entirely suitable that all who seek to influence that legislation, directly or indirectly, should be treated alike. The expenses of all should be on the same footing as far as the Treasury of the United States is concerned. The only issue here is whether or not to depart from this principle of neutrality and equality. Plainly, the case for such a change has not been and cannot be proved.

FOREIGN OPERATIONS

I

GENERAL STATEMENT

Except for withholding on dividend and interest income, which was defeated outright, no major aspect of the President's recommendations for tax reform contained in his message to the Congress on April 20, 1961, suffered so badly at the hands of the Finance Committee as did those recommendations relating to the taxation of income and profits earned abroad by U.S. persons.

President Kennedy recommended that American corporations, as well as individual U.S. taxpayers who are "shareholders of closely held" foreign corporations, be taxed each year "on their current share of the undistributed profits" of foreign corporations in which they hold stock and which are "organized in economically advanced countries." At the same time, the President recommended "elimination of the tax haven device anywhere in the world."

The Ways and Means Committee and the House of Representatives moved resolutely, if not altogether perfectly, in the direction indicated by the President.

The Finance Committee, on the other hand, in executive session, by rollcall vote, refused even to consider the President's major recommendations in this area. Instead, the committee proceeded to adopt a watered down tax haven approach to this problem, and then, amendment by amendment, moved further to weaken even that wholly inadequate approach—this, despite the fact that the Secretary of the Treasury had agreed, in testimony before the committee, that anything short of removal of the deferral privilege, whereby U.S. taxation of profits earned abroad may be indefinitely postponed, would be but "piddling" with the problem.

Though the committee has done a fairly creditable job in reviewing and acting on many provisions in the foreign area contained in the House-passed bill, it has materially weakened the grossup provision, section 9, and section 11, which deals with earned income from sources

outside the United States. These provisions badly need strengthening. By far the most important provisions, however, are contained in section 12 dealing with controlled foreign corporations. It is here the Senate must surely act if this bill is to come even close to implementing the President's recommendations.

II

TAXATION AND CAPITAL FLOWS

One of the most startling economic phenomena of the past 5 years is the large-scale movement of American capital abroad. Though some of the economic activity represented by this movement may be desirable and may serve to increase exports, much of it directly and materially weakens the base of our economy. Some of this capital is drawn abroad for legitimate economic reasons. Much of it, far too much, is stimulated to move abroad because of faulty United States tax provisions.

Several reasons exist, of course, for this unprecedented movement of capital abroad. International barriers of all sorts are being broken down. Convertibility of currency exists in large measure. Electronic communications insure effective control of economic activities anywhere in the world from one central office. The movement of persons and goods has been speeded up and cheapened to a point where distance makes very little difference. American economic style and business organization have made American know-how welcome in most countries. American free world leadership has lent prestige to all things American.

In view of these facts—facts which we may not want to alter, even if we could—it is most inappropriate to set up additional artificial stimuli to the movement of American capital abroad, particularly into activities and in amounts which are contrary to the national interest. Existing law relating to the taxation of economic activities carried out by American interests in foreign countries constitutes just such an artificial stimulus to the movement of capital abroad into areas and activities which pose dangers to the domestic economy and make more difficult a solution of the balance-of-payments problem.

As our tax laws now stand, they constitute a positive subsidy to the movement of American capital abroad. There are numerous ways in which the taxation of profits from foreign operations can be reduced to the extent that it may be more profitable to expend American capital and American know-how in building up the economy of West Germany rather than the economy of West Virginia, or south Italy rather than South Carolina.

The existence of this unhappy circumstance is given implicit verification by virtue of the fact that this bill, in 11 of its 27 sections, deals with the taxation of foreign operations of U.S. taxpayers, both individual and corporate. Unfortunately, having recognized the existence of certain problems, the bill proceeds toward correction of these problems in a most timid and half-hearted manner.

Our tax laws regarding foreign operations are hopelessly out of date. For the most part they stem from rules laid down when the income tax was developed prior to the First World War. Develop-

ments in communications, transportation, and even in international politics and political organization have made some of these laws obsolete.

In theory, the United States taxes its citizens wherever they are and from whatever source their income is derived. Although this would seem to preclude the use of the tax laws as a subsidy to draw economic activity abroad, in practice we have nullified theory to a great extent by, first, allowing American interests to operate abroad in subsidiary form without the imposition of any U.S. taxation whatsoever on the profits from those operations until those profits are remitted—often in a form which can take a capital gains rate or no rate at all—and, second, by providing for a credit for foreign income taxes paid against ultimate U.S. taxes on income earned abroad.

It is now well past the time when we should have examined our basic concepts and tax laws in the light of current political and economic realities. It is well past the time when we should have given serious consideration to the need for continuing, through domestic tax law, the subsidization of the strengthening of the economies of the countries of Western Europe, Japan, Canada, and other countries which are, at least for the moment, our political allies and friends, but which are now, and in the foreseeable future will continue to be, our fierce economic competitors.

In reexamining our tax laws relating to foreign economic activities, there are three considerations which must, in the light of today's conditions, be kept in mind. These are (1) equity, always important to any tax system but doubly so in a voluntary system such as ours, (2) domestic economic health, particularly in these times of persistently high unemployment, and (3) the balance of payments.

III

TAX EQUITY

Equity in taxation is a subject to which lipservice is paid from time to time. Everyone claims to be in favor of equity, but many define equity in strange and tortured ways. Generally speaking, if a dollar earned by a particular type of taxpayer in any economic activity, in any geographical area, pays the same tax as another dollar earned under other circumstances by similar types of taxpayers we can say that tax equity has been achieved.

Of course, from time to time preferences are given to certain types of operations, certain areas, and certain organizations, but when this is done it should be done consciously, and deliberately, in the full knowledge of what is being done, and with the accomplishment of definite objectives in mind. When a subsidy is voted—and a subsidy can be awarded a taxpayer by giving him a tax preference just as surely as it can be awarded by way of a cash payment—it should be voted to accomplish a proper national or social goal, not done accidentally, or as a private giveaway.

For example, there is no question that the average homeowner receives better tax treatment than the average renter of living quarters. But the Congress has deliberately provided this because it is considered socially desirable to foster homeownership.

In certain other instances tax advantages are given inadvertently, or because of reasons which are no longer valid. Certain of our laws dealing with the taxation of the profits and income earned abroad by American taxpayers, both corporate and individual, directly and through technically foreign subsidiaries, fall in each of these two categories.

Business decisions today are often made on the basis of tax consequences. Many decisions as to what operations should be moved abroad are made on the basis of tax consequences. Many foreign operations are set up in order to avoid taxes, in a virtual maze of interlocking and overlapping organizations, confusing to customers and operators alike. This is hardly in keeping with concepts of equity or even good business management.

The best way to achieve tax equity, particularly in this field, is to seek tax neutrality, that is, to seek to have tax laws such that economic decisions are made on the basis of economic criteria, not on tax consequences. Unfortunately, the bill reported by the Finance Committee, although it recognizes the existence of inequity, does little to deal with it effectively. Under terms of this bill, operations carried on abroad will still receive favored tax treatment as compared with the same type of operation carried on here at home.

IV

DOMESTIC ECONOMIC HEALTH

It has been clearly recognized by government at all levels—Federal, State, and local—as well as by foreign governments, that taxation and tax differentials influence economic decisions. For that reason, we have seen some of our State and local government units offer various types of tax concessions when negotiating with industries to relocate. Some foreign governments have made concessions, including allowing new concerns to operate tax free for a specified number of years. The results of this type of stimulus can be clearly seen in Puerto Rico.

When the United States arbitrarily and unilaterally gives tax concessions to domestic industry, provided that industry will move abroad, the results are certainly foreseeable—and we are seeing them now. The end result is the weakening of our economy. But for some reason, many seem to feel that loss of capital and productive facilities is good for the United States, although bad for other countries.

The tax stimulus to the movement of productive facilities abroad is a subject which has been widely discussed for some years. For example, a study made by the American Management Association in 1960, and reported in *Business Week* for December 31, 1960, showed that, "because of tax differentials, the reinvestment of foreign earnings over a 3-year period can provide 'roughly double the rate of profit accumulation for reinvestment that is possible under domestic tax schedules.'"

With 52 percent domestic corporate tax rate, and with tax-haven countries having rates running down almost to zero in some instances on sales, service, and holding company income originating in third countries, the temptation to move facilities abroad, accumulate profits for reinvestment for a period of years, and only then begin to repatriate dividends on which an inadequate U.S. tax would finally

be paid, could hardly be resisted. In fact it has not been resisted and we have seen a rapid acceleration of the buildup of American direct investment abroad during the past 5 years.

Our total private investment abroad now exceeds \$50 billion, and is increasing at the rate of about \$5 billion per year. In the field of direct investment, and particularly with reference to tax-haven devices it is noteworthy that, according to some authorities, two-thirds of our tax-haven companies have been established within the past 5 years.

The movement of productive facilities abroad has already reached serious proportions, but even more alarming is the increasing tempo of this movement. The loss of jobs, the loss of productive facilities needed for defense and other purposes, cannot be taken lightly. It is altogether too easy for a manufacturer, when he is faced with a labor problem or with extensive replacement of machinery, to pull up stakes and move a large part of his production to a foreign country.

In this country, contrary to the practice everywhere else in the world, the direct regulation of the outflow of capital and productive facilities has always been resisted. Such direct regulation may be necessary if we are to reach a real solution. But at the very least, we must not directly and positively encourage such an outflow by giving tax concessions to those who operate abroad and thereby build up the economies of foreign countries while tearing down our own. At the very least, we should remove the tax incentive which now exists to go abroad.

There will be, even with the enactment of the tightest possible tax provisions, a continuing flow of direct investment capital and productive facilities abroad in response to economic stimuli. This will not be interfered with by this, or any other similar bill. There will also be a continuation of the outflow of other forms of capital—portfolio and short-term. These latter outflows have been troublesome during the past few years and require direct and specific regulation. This bill touches only direct investment, and touches that ever so tenderly.

Criticism has been leveled at those who wish to remove the tax incentive to take American industry and productive facilities abroad. It has been alleged that this is a new type of protectionism—a new type of isolationism.

This criticism is unwarranted, and represents the most blatant type of reverse doublethink. There is no thought, insofar as this legislation is concerned, of doing anything more than removing a positive stimulus and subsidy for American plants to be moved abroad. Of course, it may well be that this is not enough. It may be that tax neutrality may not be sufficient to slow to a tolerable rate this widespread movement of capital abroad.

Those who believe in freer trade, and who support in general the President's recommendations for legislation to improve our reciprocal trade system which has served us so well for the past 28 years, certainly cannot legitimately be accused of economic isolationism merely because they wish to achieve tax neutrality, and terminate a hurtful subsidy.

The most cruel competition which an American producer can be forced to undergo is competition from American-type goods with well-known American brand names, produced abroad by American-owned

subsidiaries which have achieved rapid growth because of the ability to dodge U.S. taxes and plow back practically all earnings, with these products distributed throughout this country through a well-established chain of wholesale and retail outlets. With a further lowering of tariffs contemplated by the trade bill now before the Finance Committee, it is certainly most inequitable to continue to give these foreign, but American-owned, producers continued tax advantages when they are competing directly with U.S. production, either in American or in foreign markets.

V

BALANCE OF PAYMENTS

It has become so fashionable to discuss any problem in terms of its effect on the balance of payments that one might properly look with suspicion on some arguments which attempt to tie balance-of-payments considerations to any possible subject matter. This has been much overdone. In the case of legislation directly affecting the flow of capital funds abroad, however, balance-of-payments considerations are certainly pertinent.

The balance-of-payments problem has been with us for some years, but has been recognized as being acute by the general public—and most Government officials—for only about the past 3 years. Prior to that time, many still talked of the dollar gap and of means of increasing the flow of capital abroad.

Although the balance-of-payments problem seems likely to be brought under control within the near future—and it must be brought under control within the next 2 or 3 years if we are to be able to avoid the use of rather drastic control methods—the problem is still acute and must be attacked from all quarters. This includes, but is not limited to, a close examination of investments made abroad by U.S. taxpayers. Those sections of the bill dealing with the taxation of profits gained from activities carried on abroad by American taxpayers will affect the balance of payments specifically and directly.

There are three principal types of capital outflows which are of concern in the balance of payments picture. Only one, that is, direct investment outflows, will be affected by the provisions of this bill. The other two, portfolio investment and short-term flows, will be little affected and must probably be dealt with in ways other than tax changes. The simplest way to deal with all three, of course, is by some system of direct licensing of capital outflows. Since we have traditionally resisted this type of regulation, however, we must be doubly sure that our tax laws are not weighted in the wrong direction. This bill does not go far enough in that regard. It does not subject income and profits earned abroad to as heavy an income tax as income and profits earned in the United States. But it does move, though haltingly and timidly, in the right direction.

There can be no question as to the effect of capital outflows on the balance of payments in the short run. There can be, of course, some question as to the long-range effects of capital outflows, particularly direct investment flows.

As to the long-range effect of direct investment outflows, the effect on the balance of payments may eventually be positive. But, with an acute situation which must be corrected within 2 or 3 years, it is

not advisable to wait for a period of years, perhaps as long as 12 to 15 years according to Treasury Department analyses, for current direct foreign investment to assist in correcting the present imbalance.

Bearing in mind that direct foreign investment is accelerating, and that the net overall balance of payments deficit this year is expected to be in the neighborhood of \$1.5 billion, an alteration of investment flows in the order of a few hundred million dollars would be significant.

Reliable estimates indicate that the complete removal of the deferral privilege would, by slowing down direct investment outflows and by speeding up repatriation of earnings, decrease the balance-of-payments deficit by about \$400 million annually. This bill, of course, would not be nearly so beneficial. In its present form it would be of little assistance. A good, tight, tax haven bill would assist in the balance of payments in the order of \$200 to \$300 million.

VI

SPECIFIC PROVISIONS

The best and indeed the only sure way to achieve substantial equity, guard against the untoward weakening of American industry and assist in the solution of the balance-of-payments problem through taxation is to tax American taxpayers annually on income and profits earned anywhere in the world. This would restore neutrality as to taxation, allowing economic forces to play their proper role in economic decisions relating to investment choices at home or abroad. This would insure that the corporation which helps to build up a depressed area in the United States would be treated as fairly by the Federal Government as the corporation which builds up the economy of Western Europe. The most important section of the subject bill dealing with foreign operations has, however, been drawn up on the theory that the partial elimination of tax haven advantages is sufficient.

There is no question that the complete elimination of tax haven operations would help materially. It is through the combination of a sales subsidiary, a service subsidiary, and a holding company located in a tax haven country, Switzerland, for example, that the U.S.-owned manufacturing company in Germany—or other relatively high-tax foreign country—is able to reduce its German tax to a rate well below the stated rate of 51 percent. If tax havens are made less profitable from a tax standpoint, the manufacturing operations which support them will have to be justified on economic grounds, not on grounds of tax avoidance, whether the taxes avoided are United States or foreign.

The Finance Committee, by approving even these imperfect provisions, does recognize that certain changes in existing law should be made.

1. It is recognized that numerous abuses exist in the operation of certain types of corporations organized in certain low-tax countries. While this tax haven problem is recognized, it is not completely corrected.

2. It is recognized that many individual U.S. citizens are living abroad for the purpose, or with the result, of escaping proper U.S. taxation. But the provisions of the bill are insufficient to deal with the problem. It will still be highly profitable, under the terms of this bill,

for a U.S. citizen to live abroad and thereby avoid paying his fair share of the cost of U.S. and free world defense and essential Government services.

3. It is recognized that there are numerous abuses in setting up foreign trusts for the purpose of escaping U.S. taxation.

4. It is recognized that there have been abuses in the liquidation of foreign corporations, with the result that accumulated ordinary income is being brought into the country in a form which allows it to be taxed at the low capital gains rate, if at all.

5. It is recognized that the U.S. estate tax has been avoided by some through the device of investing in foreign real estate, even in contemplation of death.

6. It is recognized that the law as now written allows both a partial credit and a deduction for foreign income and related taxes. For some reason, presumably because it is recognized that tax reductions do act as subsidies to draw capital investment abroad, the committee allows this double benefit to be continued in less developed countries.

7. It is recognized that present law does not require sufficiently stringent reporting of foreign economic activities of American interests.

In order for the bill to be really meaningful in correcting the imperfections in existing law which have been recognized, however, certain minimum changes must be made.

1. Section 12—Controlled foreign corporations

(a) This entire section, embodying as it does the tax haven approach, ought to be deleted and have substituted therefor the complete removal of the deferral privilege. Language to accomplish this objective exists in amendment 6-19-62—A to H.R. 10650, previously offered.

(b) The tax haven approach, if sufficiently rigorous, does represent a step forward. Should the Senate decide to proceed with this approach, this section should be amended in at least the following ways:

(1) The de minimus rule should be restored to 20 percent.

(2) The exception for export trade income of "Export Trade Corporations" should be deleted.

(3) The exception for dividend and interest income from less developed countries, together with profits realized from the sale of investments in less developed countries, should be deleted.

2. Section 9—The gross-up

This provision should be made applicable to income from subsidiary corporations operating anywhere in the world, as provided by the House-passed bill. There is no equity in allowing both a deduction and a partial credit for income taxes paid to certain countries. The operation of existing law in this area is capricious and even perverse, and is not a suitable vehicle for a subsidy, should it be felt that a subsidy is needed or desirable.

3. Section 11—Income earned abroad

There is no equity in allowing individual U.S. citizens living abroad, either temporarily or on a more permanent bona fide basis, to pay less taxes than citizens and residents here at home. All benefit from services rendered by both the U.S. Government and the government

of their host countries. All should contribute toward the cost of U.S. and free world protection. It is particularly inappropriate to allow a phasing-in of taxes on fringe benefits.

CONCLUSIONS

On balance, the bill as reported by the Finance Committee is a poor one. Although there are worthwhile sections in the bill these are hardly sufficient to outweigh those sections which are, either in whole or in part, faulty.

As we have already pointed out, many of the President's major recommendations have been ignored or watered down. The committee has chosen to strike the withholding provision, which was passed by the other body. It has failed to include in the bill such obviously needed reforms as the repeal of the dividend credit and exclusion as recommended by the President. In almost every instance, expense accounts and foreign operations, for example, where the committee did approve a section or provision recommended by the President and adopted by the House, that provision has been materially weakened.

As if the emasculation of many of the President's major recommendations were not enough, the Finance Committee has added, by way of afterthought, several rather petty addenda to the bill. Sections 21 through 26 really have no place in this bill. Some of these additions are really private bills masquerading as general legislation, while others are of such minor consequence that they have far too little stature to warrant their consideration in this bill when so many more important subjects are being left to a later, more general, tax reform bill. Some of these sections, indeed, standing alone are hardly veto proof.

The Senate must now proceed to a painstaking examination of each provision contained in this bill. We would hope that there will be full and free debate on all provisions and that each individual Senator will examine all provisions and all amendments which will be offered with care and join in an earnest endeavor to put this bill in a form more closely resembling the President's recommendations.

Should the Senate or the conference committee fail to make substantial improvements, it will be our painful duty, despite the worthwhile provisions which are contained in this bill, to oppose its final passage.

PAUL H. DOUGLAS.
ALBERT GORE.



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passage.

Calendar No. 1843

87TH CONGRESS
2^D SESSION

H. R. 10650

[Report No. 1881]

IN THE SENATE OF THE UNITED STATES

APRIL 2, 1962

Read twice and referred to the Committee on Finance

AUGUST 16 (legislative day, AUGUST 15), 1962

Reported by Mr. KERR, with amendments

[Omit the part struck through or enclosed in black brackets and insert the part printed in italic]

AN ACT

To amend the Internal Revenue Code of 1954 to provide a credit for investment in certain depreciable property, to eliminate certain defects and inequities, and for other purposes.

1 *Be it enacted by the Senate and House of Representa-*
2 *tives of the United States of America in Congress assembled,*

3 SECTION 1. SHORT TITLE, ETC.

4 (a) SHORT TITLE.—This Act may be cited as the
5 “Revenue Act of 1962”.

1 (b) TABLE OF CONTENTS.—

- Sec. 1. Short title, etc.
- (a) Short title.
 - (b) Table of contents.
 - (c) Amendment of 1954 code.
- Sec. 2. Credit for investment in certain depreciable property.
- (a) Allowance of credit.
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 - (e) Effective date.
- Sec. 3. Appearances, etc., with respect to legislation.
- (a) In general.
 - (b) Effective date.
- Sec. 4. Disallowance of certain entertainment, etc., expenses.
- (a) Denial of deduction.
 - (b) Traveling expenses.
 - (c) Effective date.
- Sec. 5. Amount of distribution where certain foreign corporations distribute property in kind.
- (a) Amount distributed.
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- Sec. 6. Amendment of section 482.
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- Sec. 7. Distributions of foreign personal holding company income.
- (a) Definition of foreign personal holding company.
 - (b) Amount of undistributed income.
 - (c) Effective date.
- Sec. 8. Mutual savings banks, etc.
- (a) Reserves for losses on loans.
 - (b) Foreclosure on property securing loans.
 - (c) Definition of domestic building and loan association.
 - (d) Clerical amendments.
 - (e) Repeal of exemption from communications and transportation of persons taxes.
 - (f) Effective dates.
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- (a) Definitions.
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Sec. 9. Distributions by foreign trusts.—Continued

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- (d) Amounts treated as received in prior years.
- (e) Special rules for foreign trusts.
- (f) Information returns with respect to foreign trusts.
- (g) Failure to file information returns.
- (h) United States person defined.
- (i) Technical amendments.
- (j) Effective date.

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- (c) Statutory underwriting income or loss.
- (d) Mutual fire insurance companies operating on basis of premium deposits.
- (e) Election of certain mutual companies to be taxed on total income.
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- (c) Determination of source of dividends received from certain foreign corporations.
- (d) Repeal of section 902(d).
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- (c) Effective date.

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(a) *Treatment for purposes of part I of subchapter Q.*

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(a) *Close of taxable year of two-man partnership when one partner dies.*

(b) *Effective date, etc.*

Sec. 27. Treaties.

2 (c) AMENDMENT OF 1954 CODE.—Whenever Except
3 as otherwise expressly provided, whenever in this Act an
4 amendment or repeal is expressed in terms of an amendment
5 to, or repeal of, a section or other provision, the reference
6 shall be considered to be made to a section or other provision
7 of the Internal Revenue Code of 1954.

8 **SEC. 2. CREDIT FOR INVESTMENT IN CERTAIN DEPRE-**
9 **CIABLE PROPERTY.**

10 (a) ALLOWANCE OF CREDIT.—Part IV of subchapter
11 A of chapter 1 (relating to credits against tax) is amended
12 by redesignating section 38 as section 40 39 and by inserting
13 after section 37 the following new section:

**1 “SEC. 38. INVESTMENT IN CERTAIN DEPRECIABLE PROP-
2 ERTY.**

3 “(a) **GENERAL RULE.**—There shall be allowed, as a
4 credit against the tax imposed by this chapter, the amount
5 determined under subpart B of this part.

6 “(b) **REGULATIONS.**—The Secretary or his delegate
7 shall prescribe such regulations as may be necessary to carry
8 out the purposes of this section and subpart B.”

9 (b) **RULES FOR COMPUTING CREDIT.**—Part IV of sub-
10 chapter A of chapter 1 is amended by adding at the end
11 thereof the following new subpart:

12 **“Subpart B—Rules for Computing Credit for Investment
13 in Certain Depreciable Property**

“Sec. 46. Amount of credit.

“Sec. 47. Certain dispositions, etc., of section 38 property.

“Sec. 48. Definitions; special rules.

14 **“SEC. 46. AMOUNT OF CREDIT.**

15 “(a) **DETERMINATION OF AMOUNT.**—

16 “(1) **GENERAL RULE.**—The amount of the credit
17 allowed by section 38 for the taxable year shall be equal
18 to 7 percent of the qualified investment (as defined in
19 subsection (c)).

20 “(2) **LIMITATION BASED ON AMOUNT OF TAX.**—
21 Notwithstanding paragraph (1), the credit allowed by
22 section 38 for the taxable year shall not exceed—

1 “(A) so much of the liability for tax for the
2 taxable year as does not exceed \$25,000, plus

3 “(B) 25 percent of so much of the liability
4 for tax for the taxable year as exceeds \$25,000.

5 “(3) LIABILITY FOR TAX.—For purposes of para-
6 graph (2), the liability for tax for the taxable year shall
7 be the tax imposed by this chapter for such year,
8 reduced by the sum of the credits allowable under—

9 “(A) section 33 (relating to foreign tax
10 credit),

11 “(B) section 34 (relating to dividends re-
12 ceived by individuals),

13 “(C) section 35 (relating to partially tax-
14 exempt interest), and

15 “(D) section 37 (relating to retirement in-
16 come).

17 For purposes of this paragraph, any tax imposed for the
18 taxable year by section 531 (relating to accumulated
19 earnings tax) or by section 541 (relating to personal
20 holding company tax) shall not be considered tax
21 imposed by this chapter for such year.

22 “(4) MARRIED INDIVIDUALS.—In the case of a
23 husband or wife who files a separate return, the amount
24 specified under subparagraphs (A) and (B) of para-
25 graph (2) shall be \$12,500 in lieu of \$25,000. This

1 paragraph shall not apply if the spouse of the taxpayer
 2 has no qualified investment for, and no unused credit
 3 *carryback or* carryover to, the taxable year of such
 4 spouse which ends within or with the taxpayer's taxable
 5 year.

6 “(5) AFFILIATED GROUPS.—In the case of an
 7 affiliated group, the \$25,000 amount specified under
 8 subparagraphs (A) and (B) of paragraph (2) shall be
 9 reduced for each member of the group by apportioning
 10 \$25,000 among the members of such group in such
 11 manner as the Secretary or his delegate shall by regula-
 12 tions prescribe. For purposes of the preceding sentence,
 13 the term ‘affiliated group’ has the meaning assigned to
 14 such term by section 1504 (a), except that all corpora-
 15 tions shall be treated as includible corporations (with-
 16 out any exclusion under section 1504 (b)).

17 ~~“(b) 5-YEAR CARRYOVER OF UNUSED CREDITS.—~~

18 ~~“(1) ALLOWANCE OF CREDIT.—If the amount of~~
 19 ~~the credit determined under subsection (a) (1) for any~~
 20 ~~taxable year exceeds the limitation provided by subsec-~~
 21 ~~tion (a) (2) for such taxable year (hereinafter in this~~
 22 ~~subsection referred to as ‘unused credit year’); such~~
 23 ~~excess shall be added to the amount allowable as a credit~~
 24 ~~by section 38 for each of the 5 succeeding taxable years~~
 25 ~~to the extent not taken into account for taxable years~~

1 intervening between the unused credit year and such
2 succeeding taxable year.

3 ~~“(2)~~ LIMITATION.—The amount of the unused
4 credit which may be added under paragraph ~~(1)~~ for any
5 succeeding taxable year shall not exceed the amount by
6 which the limitation provided by subsection ~~(a)(2)~~ for
7 such taxable year exceeds the sum of—

8 ~~“(A)~~ the credit allowable under subsection
9 ~~(a)(1)~~ for such taxable year; and

10 ~~“(B)~~ the amounts which, by reason of this
11 subsection, are added to the amount allowable for
12 such taxable year and attributable to taxable years
13 preceding the unused credit year.

14 *“(b) CARRYBACK AND CARRYOVER OF UNUSED*
15 *CREDITS.—*

16 *“(1) ALLOWANCE OF CREDIT.—If the amount of*
17 *the credit determined under subsection (a)(1) for*
18 *any taxable year exceeds the limitation provided by*
19 *subsection (a)(2) for such taxable year (hereinafter*
20 *in this subsection referred to as ‘unused credit year’),*
21 *such excess shall be—*

22 *“(A) an investment credit carryback to each*
23 *of the 3 taxable years preceding the unused credit*
24 *year, and*

1 “(B) an investment credit carryover to each
2 of the 5 taxable years following the unused credit
3 year,
4 and shall be added to the amount allowable as a credit
5 by section 38 for such years, except that such excess
6 may be a carryback only to a taxable year ending after
7 June 30, 1962. The entire amount of the unused
8 credit for an unused credit year shall be carried to the
9 earliest of the 8 taxable years to which (by reason of
10 subparagraphs (A) and (B)) such credit may be
11 carried, and then to each of the other 7 taxable years
12 to the extent that, because of the limitation contained
13 in paragraph (2), such unused credit may not be added
14 for a prior taxable year to which such unused credit
15 may be carried.

16 “(2) LIMITATION.—The amount of the unused
17 credit which may be added under paragraph (1) for
18 any preceding or succeeding taxable year shall not
19 exceed the amount by which the limitation provided
20 by subsection (a)(2) for such taxable year exceeds
21 the sum of—

22 “(A) the credit allowable under subsection
23 (a)(1) for such taxable year, and

24 “(B) the amounts which, by reason of this sub-

1 section, are added to the amount allowable for such
2 taxable year and attributable to taxable years pre-
3 ceding the unused credit year.

4 “(3) *EFFECT OF NET OPERATING LOSS CARRY-*
5 *BACK.*—To the extent that the excess described in para-
6 graph (1) arises by reason of a net operating loss carry-
7 back, subparagraph (A) of paragraph (1) shall not
8 apply.

9 “(4) *TAXABLE YEAR BEGINNING BEFORE JULY*
10 *1, 1962.*—For purposes of determining the amount of an
11 investment credit carryback that may be added under
12 paragraph (1) for a taxable year beginning before July
13 1, 1962, and ending after June 30, 1962, the amount
14 of the limitation provided by subsection (a)(2) is the
15 amount which bears the same ratio to such limitation as
16 the number of days in such year after June 30, 1962,
17 bears to the total number of days in such year.

18 “(c) *QUALIFIED INVESTMENT.*—

19 “(1) *IN GENERAL.*—For purposes of this subpart,
20 the term ‘qualified investment’ means, with respect to
21 any taxable year, the aggregate of—

22 “(A) the applicable percentage of the basis of
23 each new section 38 property (as defined in section
24 48 (b)) placed in service by the taxpayer during
25 such taxable year, plus

“(B) the applicable percentage of the cost of each used section 38 property (as defined in section 48 (c) (1)) placed in service by the taxpayer during such taxable year.

“(2) APPLICABLE PERCENTAGE.—For purposes of paragraph (1), the applicable percentage for any property shall be determined under the following table:

“If the useful life is—	The applicable percentage is—
4 years or more but less than 6 years.....	33⅓
6 years or more but less than 8 years.....	66⅔
8 years or more.....	100

For purposes of this paragraph, the useful life of any property shall be determined as of the time such property is placed in service by the taxpayer.

“(3) PUBLIC UTILITY PROPERTY.—

“(A) In the case of section 38 property which is public utility property, the amount of the qualified investment shall be 3/7 of the amount determined under paragraph (1).

“(B) For purposes of subparagraph (A), the term ‘public utility property’ means property used predominantly in the trade or business of the furnishing or sale of—

“(i) electrical energy, water, or sewage disposal services,

1 “(ii) gas through a local distribution sys-
2 tem,

3 “(iii) telephone service, or

4 “(iv) telegraph service by means of do-
5 mestic telegraph operations (as defined in
6 section 222 (a) (5) of the Communications Act
7 of 1934, as amended; 47 U.S.C., sec. 222 (a)
8 (5)),

9 if the rates for such furnishing or sale, as the case
10 may be, have been established or approved by a
11 State or political subdivision thereof, by an agency
12 or instrumentality of the United States, or by a
13 public service or public utility commission or other
14 similar body of any State or political subdivision
15 thereof.

16 “(4) *CERTAIN REPLACEMENT PROPERTY.*—*For*
17 *purposes of paragraph (1), if section 38 property is*
18 *placed in service by the taxpayer to replace property*
19 *which was—*

20 “(A) *destroyed or damaged by fire, storm, ship-*
21 *wreck, or other casualty, or*

22 “(B) *stolen,*
23 *the basis of such section 38 property (in the case of*
24 *new section 38 property), or the cost of such section*
25 *38 property (in the case of used section 38 property),*

which (but for this paragraph) would be taken into account under paragraph (1) shall be reduced by an amount equal to the amount received by the taxpayer as compensation, by insurance or otherwise, for the property so destroyed, damaged, or stolen, or to the adjusted basis of such property, whichever is the lesser. No reduction in basis or cost shall be made under the preceding sentence in any case in which the reduction in qualified investment attributable to the substitution required by section 47(a)(1) with respect to the property so destroyed, damaged, or stolen (determined without regard to section 47(a)(4)) is greater than the reduction described in the preceding sentence.

“(d) LIMITATIONS WITH RESPECT TO CERTAIN PERSONS.—

“(1) IN GENERAL.—In the case of—

“(A) an organization to which section 593 applies,

“(B) a regulated investment company or a real estate investment trust subject to taxation under subchapter M (sec. 851 and following), and

“(C) a cooperative organization described in section 1381(a),

the qualified investment and the \$25,000 amount

1 specified under subparagraphs (A) and (B) of sub-
2 section (a) (2) shall equal such person's ratable share
3 of such items.

4 “(2) Ratable share.—For purposes of para-
5 graph (1), the ratable share of any person for any
6 taxable year of the items described therein shall be—

7 “(A) in the case of an organization referred
8 to in paragraph (1) (A), 50 percent thereof,

9 “(B) in the case of a regulated investment
10 company or a real estate investment trust, the ratio
11 (i) the numerator of which is its taxable income and
12 (ii) the denominator of which is its taxable income
13 computed without regard to the deduction for divi-
14 dends paid provided by section 852 (b) (2) (D) or
15 857 (b) (2) (C), as the case may be, and

16 “(C) in the case of a cooperative organization,
17 the ratio (i) the numerator of which is its taxable
18 income and (ii) the denominator of which is its
19 taxable income increased by amounts to which
20 section 1382 (b) or (c) applies and similar amounts
21 the tax treatment of which is determined without
22 regard to subchapter T (sec. 1381 and following).

23 For purposes of subparagraph (B) of the preceding
24 sentence, the term ‘taxable income’ means in the case of
25 a regulated investment company its investment company

taxable income (within the meaning of section 852 (b) (2)), and in the case of a real estate investment trust its real estate investment trust taxable income (within the meaning of section 857 (b) (2)).

“SEC. 47. CERTAIN DISPOSITIONS, ETC., OF SECTION 38 PROPERTY.

“(a) GENERAL RULE.—Under regulations prescribed by the Secretary or his delegate—

“(1) EARLY DISPOSITION, ETC.—If during any taxable year any property is disposed of, or otherwise ceases to be section 38 property with respect to the taxpayer, before the close of the useful life which was taken into account in computing the credit under section 38, then the tax under this chapter for such taxable year shall be increased by an amount equal to the aggregate decrease in the credits allowed under section 38 for all prior taxable years which would have resulted solely from substituting, in determining qualified investment, for such useful life the period beginning with the time such property was placed in service by the taxpayer and ending with the time such property ceased to be section 38 property.

“(2) PROPERTY BECOMES PUBLIC UTILITY PROPERTY.—If during any taxable year any property taken into account in determining qualified investment becomes

1 public utility property (within the meaning of section
 2 46 (c) (3) (B)), then the tax under this chapter for
 3 such taxable year shall be increased by an amount equal
 4 to the aggregate decrease in the credits allowed under
 5 section 38 for all prior taxable years which would have
 6 resulted solely from treating the property, for purposes
 7 of determining qualified investment, as public utility
 8 property (after giving due regard to the period before
 9 such change in use) . If the application of this paragraph
 10 to any property is followed by the application of para-
 11 graph (1) to such property, proper adjustment shall be
 12 made in applying paragraph (1) .

13 “(3) ~~CARRYOVERS~~ *CARRYBACKS AND CARRY-*
 14 *OVERS ADJUSTED.*—In the case of any cessation de-
 15 scribed in paragraph (1) or any change in use described
 16 in paragraph (2) , the *carrybacks and* carryovers under
 17 section 46 (b) shall be adjusted by reason of such cessa-
 18 tion (or change in use) .

19 “(4) *PROPERTY DESTROYED BY CASUALTY,*
 20 *ETC.*—No increase shall be made under paragraph (1)
 21 and no adjustment shall be made under paragraph (3)
 22 in any case in which—

23 “(A) any property is disposed of, or otherwise
 24 ceases to be section 38 property with respect to the
 25 taxpayer, on account of its destruction or damage

by fire, storm, shipwreck, or other casualty, or by reason of its theft,

“(B) section 38 property is placed in service by the taxpayer to replace the property described in subparagraph (A), and

“(C) the reduction in basis or cost of such section 38 property described in the first sentence of section 46(c)(4) is greater than the reduction in qualified investment which (but for this paragraph) would be made by reason of the substitution required by paragraph (1) with respect to the property described in subparagraph (A).

“(b) SECTION NOT TO APPLY IN CERTAIN CASES.—

Subsection (a) shall not apply to—

“(1) a transfer by reason of death, or

“(2) a transaction to which section 381 (a) applies.

For purposes of subsection (a), property shall not be treated as ceasing to be section 38 property with respect to the taxpayer by reason of a mere change in the form of conducting the trade or business so long as the property is retained in such trade or business as section 38 property and the taxpayer retains a substantial interest in such trade or business.

“(c) SPECIAL RULE.—Any increase in tax under subsection (a) shall not be treated as tax imposed by this

1 chapter for purposes of determining the amount of any credit
2 allowable under subpart A.

3 **“SEC. 48. DEFINITIONS; SPECIAL RULES.**

4 “(a) **SECTION 38 PROPERTY.—**

5 “(1) **IN GENERAL.—**Except as provided in this
6 subsection, the term ‘section 38 property’ means—

7 “(A) tangible personal property, or

8 “(B) other tangible property (not including
9 a building and its structural components) but only
10 if such property—

11 “(i) is used as an integral part of manu-
12 facturing, production, or extraction or of fur-
13 nishing transportation, communications, elec-
14 trical energy, gas, water, or sewage disposal
15 services, or

16 “(ii) constitutes a research or storage fa-
17 cility used in connection with any of the activi-
18 ties referred to in clause (i).

19 Such term includes only property with respect to which
20 depreciation (or amortization in lieu of depreciation) is
21 allowable and having a useful life (determined as of
22 the time such property is placed in service) of 4 years
23 or more.

24 “(2) **PROPERTY USED OUTSIDE THE UNITED**
25 **STATES.—**

1 “(A) IN GENERAL.—Except as provided in
2 subparagraph (B), the term ‘section 38 property’
3 does not include property which is used predomi-
4 nantly outside the United States.

5 “(B) EXCEPTIONS.—Subparagraph (A) shall
6 not apply to—

7 “(i) any aircraft which is registered by
8 the Administrator of the Federal Aviation
9 Agency and which is operated to and from the
10 United States;

11 “(ii) rolling stock, of a domestic railroad
12 corporation subject to part I of the Interstate
13 Commerce Act, which is used within and with-
14 out the United States;

15 “(iii) any vessel documented under the
16 laws of the United States which is operated in
17 the foreign or domestic commerce of the United
18 States;

19 “(iv) any motor vehicle of a United States
20 person (as defined in section 7701 (a) (30))
21 which is operated to and from the United
22 States;

23 “(v) any container of a United States
24 person which is used in the transportation of
25 property to and from the United States; and

1 “(vi) any property (other than a vessel
2 or an aircraft) of a United States person which
3 is used for the purpose of exploring for, de-
4 veloping, removing, or transporting resources
5 from the outer Continental Shelf (within the
6 meaning of section 2 of the Outer Continental
7 Shelf Lands Act, as amended and supple-
8 mented; 43 U.S.C., sec. 1331).

9 “(3) PROPERTY USED FOR LODGING.—Property
10 which is used predominantly to furnish lodging or in
11 connection with the furnishing of lodging shall not be
12 treated as section 38 property. The preceding sentence
13 shall not apply to—

14 “(A) nonlodging commercial facilities which
15 are available to persons not using the lodging facili-
16 ties on the same basis as they are available to per-
17 sons using the lodging facilities, and

18 “(B) property used by a hotel or motel in con-
19 nection with the trade or business of furnishing
20 lodging where the predominant portion of the ac-
21 commodations is used by transients.

22 “(4) PROPERTY USED BY CERTAIN TAX-EXEMPT
23 ORGANIZATIONS.—Property used by an organization
24 (other than a cooperative described in section 521)
25 which is exempt from the tax imposed by this chapter

shall be treated as section 38 property only if such property is used predominantly in an unrelated trade or business the income of which is subject to tax under section 511.

“(5) PROPERTY USED BY GOVERNMENTAL UNITS.—Property used by the United States, any State or political subdivision thereof, any international organization, or any agency or instrumentality of any of the foregoing shall not be treated as section 38 property.

“(6) LIVESTOCK.—*Livestock shall not be treated as section 38 property.*

“(b) NEW SECTION 38 PROPERTY.—For purposes of this subpart, the term ‘new section 38 property’ means section 38 property—

“(1) the construction, reconstruction, or erection of which is completed by the taxpayer after ~~December 31, 1961~~ *June 30, 1962*, or

“(2) acquired after ~~December 31, 1961~~ *June 30, 1962*, if the original use of such property commences with the taxpayer and commences after such date.

In applying section 46(c)(1)(A) in the case of property described in paragraph (1), there shall be taken into account only that portion of the basis which is properly attributable to construction, reconstruction, or erection after ~~December 31, 1961~~ *June 30, 1962*.

1 “(c) USED SECTION 38 PROPERTY.—

2 “(1) IN GENERAL.—For purposes of this subpart,
3 the term ‘used section 38 property’ means section 38
4 property acquired by purchase after ~~December 31, 1961~~
5 *June 30, 1962*, which is not new section 38 property.
6 Property shall not be treated as ‘used section 38 prop-
7 erty’ if, after its acquisition by the taxpayer, it is used
8 by a person who used such property before such acquisi-
9 tion (or by a person who bears a relationship described
10 in section 179 (d) (2) (A) or (B) to a person who used
11 such property before such acquisition).

12 “(2) DOLLAR LIMITATION.—

13 “(A) IN GENERAL.—The cost of used section
14 38 property taken into account under section 46
15 (c) (1) (B) for any taxable year shall not exceed
16 \$50,000. If such cost exceeds \$50,000, the tax-
17 payer shall select (at such time and in such manner
18 as the Secretary or his delegate shall by regulations
19 prescribe) the items to be taken into account, but
20 only to the extent of an aggregate cost of \$50,000.
21 Such a selection, once made, may be changed only
22 in the manner, and to the extent, provided by such
23 regulations.

24 “(B) MARRIED INDIVIDUALS.—In the case of
25 a husband or wife who files a separate return, the

1 limitation under subparagraph (A) shall be
2 \$25,000 in lieu of \$50,000. This subparagraph
3 shall not apply if the spouse of the taxpayer has no
4 used section 38 property which may be taken into
5 account as qualified investment for the taxable year
6 of such spouse which ends within or with the tax-
7 payer's taxable year.

8 “(C) AFFILIATED GROUPS.—In the case of an
9 affiliated group, the \$50,000 amount specified under
10 subparagraph (A) shall be reduced for each mem-
11 ber of the group by apportioning \$50,000 among
12 the members of such group in accordance with their
13 respective amounts of used section 38 property
14 which may be taken into account.

15 “(D) PARTNERSHIPS.—In the case of a part-
16 nership, the limitation contained in subparagraph
17 (A) shall apply with respect to the partnership and
18 with respect to each partner.

19 “(3) DEFINITIONS.—For purposes of this sub-
20 section—

21 “(A) PURCHASE.—The term ‘purchase’ has
22 the meaning assigned to such term by section
23 179(d)(2).

24 “(B) COST.—The cost of used section 38
25 property does not include so much of the basis of

1 such property as is determined by reference to the
2 adjusted basis of other property held at any time by
3 the person acquiring such property. If property is
4 disposed of (*other than by reason of its destruction*
5 *or damage by fire, storm, shipwreck, or other casu-*
6 *alty, or its theft*) and used section 38 property simi-
7 lar or related in service or use is acquired as a re-
8 placement therefor in a transaction to which the pre-
9 ceding sentence does not apply, the cost of the used
10 section 38 property acquired shall be its basis re-
11 duced by the adjusted basis of the property re-
12 placed. The cost of used section 38 property shall
13 not be reduced with respect to the adjusted basis of
14 any property disposed of if, by reason of section 47,
15 such disposition involved an increase of tax or
16 a reduction of the unused credit *carrybacks or carry-*
17 *overs* described in section 46 (b) .

18 “(C) AFFILIATED GROUP.—The term ‘affili-
19 ated group’ has the meaning assigned to such term
20 by section 1504 (a) , except that—

21 “(i) the phrase ‘more than 50 percent’
22 shall be substituted for the phrase ‘at least 80
23 percent’ each place it appears in section
24 1504 (a) , and

25 “(ii) all corporations shall be treated as

1 includible corporations (without any exclusion
2 under section 1504 (b)).

3 “(d) CERTAIN LEASED PROPERTY.—A person (other
4 than a person referred to in section 46 (d)) engaged in the
5 business of leasing property *who is a lessor of property* may
6 (at such time, in such manner, and subject to such conditions
7 as are provided by regulations prescribed by the Secretary or
8 his delegate) elect with respect to any new section 38
9 property to treat the lessee as having acquired such property
10 for an amount equal to—

11 “(1) if such property was constructed by the lessor
12 (or by a corporation which controls or is controlled by
13 the lessor within the meaning of section 368 (c)), the
14 fair market value of such property, or

15 “(2) if paragraph (1) does not apply, the basis
16 of such property to the lessor.

17 The election provided by the preceding sentence may be
18 made only with respect to property which would be new
19 section 38 property if acquired by the lessee. For purposes
20 of the preceding sentence and section 46 (c) , the useful life
21 of property in the hands of the lessee is the useful life of such
22 property in the hands of the lessor. If a lessor makes the
23 election provided by this subsection with respect to any
24 property, the lessee shall be treated for all purposes of this
25 subpart as having acquired such property. *If a lessor makes*

1 *the election provided by this subsection with respect to any*
 2 *property, then, under regulations prescribed by the Secre-*
 3 *tary or his delegate, subsection (g) shall not apply with*
 4 *respect to such property and the deductions otherwise allow-*
 5 *able under section 162 to the lessee for amounts paid to the*
 6 *lessor under the lease shall be adjusted in a manner consistent*
 7 *with the provisions of subsection (g).*

8 “(e) SUBCHAPTER S CORPORATIONS.—In the case of
 9 an electing small business corporation (as defined in section
 10 1371)—

11 “(1) the qualified investment for each taxable year
 12 shall be apportioned pro rata among the persons who
 13 are shareholders of such corporation on the last day of
 14 such taxable year; and

15 “(2) any person to whom any investment has been
 16 apportioned under paragraph (1) shall be treated (for
 17 purposes of this subpart) as the taxpayer with respect
 18 to such investment, and such investment shall not (by
 19 reason of such apportionment) lose its character as an
 20 investment in new section 38 property or used section
 21 38 property, as the case may be.

22 “(f) ESTATES AND TRUSTS.—In the case of an estate
 23 or trust—

24 “(1) the qualified investment for any taxable year
 25 shall be apportioned between the estate or trust and the

beneficiaries on the basis of the income of the estate or trust allocable to each,

“(2) any beneficiary to whom any investment has been apportioned under paragraph (1) shall be treated (for purposes of this subpart) as the taxpayer with respect to such investment, and such investment shall not (by reason of such apportionment) lose its character as an investment in new section 38 property or used section 38 property, as the case may be, and

“(3) the \$25,000 amount specified under subparagraphs (A) and (B) of section 46(a)(2) applicable to such estate or trust shall be reduced to an amount which bears the same ratio to \$25,000 as the amount of the qualified investment allocated to the estate or trust under paragraph (1) bears to the entire amount of the qualified investment.

“(g) *ADJUSTMENTS TO BASIS OF PROPERTY.*—

“(1) *IN GENERAL.*—*The basis of any section 38 property shall be reduced, for purposes of this subtitle other than this subpart, by an amount equal to 7 percent of the qualified investment as determined under section 46(c) with respect to such property.*

“(2) *CERTAIN DISPOSITIONS, ETC.*—*If the tax under this chapter is increased for any taxable year under paragraph (1) or (2) of section 47(a) or an*

1 *adjustment in carrybacks or carryovers is made under*
 2 *paragraph (3) of such section, the basis of the property*
 3 *described in such paragraph (1) or (2), as the case may*
 4 *be (immediately before the event on account of which*
 5 *such paragraph (1), (2), or (3) applies), shall be in-*
 6 *creased by an amount equal to the portion of such in-*
 7 *crease and the portion of such adjustment attributable to*
 8 *such property.*

9 “~~(g)~~ (h) *CROSS REFERENCE.*—

“For application of this subpart to certain acquiring corporations, see section 381(c)(23).”

10 *(c) DEDUCTION FOR UNUSED CREDIT.*—*Part VI of*
 11 *subchapter B of chapter 1 (relating to itemized deductions*
 12 *for individuals and corporations) is amended by adding at*
 13 *the end thereof the following new section:*

14 **“SEC. 181. DEDUCTION FOR CERTAIN UNUSED INVESTMENT**
 15 **CREDIT.**

16 *“If the amount of the credit determined under section*
 17 *46(a)(1) for any taxable year exceeds the limitation pro-*
 18 *vided by section 46(a)(2) for such taxable year and if the*
 19 *amount of such excess has not, after the application of section*
 20 *46(b), been allowed to the taxpayer as a credit under section*
 21 *38 for any taxable year, then an amount equal to the amount*
 22 *of such excess not so allowed as a credit shall be allowed to*
 23 *the taxpayer as a deduction for the first taxable year follow-*
 24 *ing the last taxable year in which such excess could under*

1 *section 46(b) have been allowed as a credit. If a taxpayer*
 2 *dies or ceases to exist prior to the first taxable year following*
 3 *the last taxable year in which the excess described in the pre-*
 4 *ceding sentence could under section 46(b) have been allowed*
 5 *as a credit, the amount described in the preceding sentence,*
 6 *or the proper portion thereof, shall, under regulations pre-*
 7 *scribed by the Secretary or his delegate, be allowed to the*
 8 *taxpayer as a deduction for the taxable year in which such*
 9 *death or cessation occurs."*

10 ~~(e)~~(d) CERTAIN CORPORATE ACQUISITIONS.—Sec-
 11 tion 381 (c) (relating to items taken into account in certain
 12 corporate acquisitions) is amended by adding at the end
 13 thereof the following new paragraph:

14 " (23) CREDIT UNDER SECTION 38 FOR INVEST-
 15 MENT IN CERTAIN DEPRECIABLE PROPERTY.—The ac-
 16 quiring corporation shall take into account (to the ex-
 17 tent proper to carry out the purposes of this section and
 18 section 38, and under such regulations as may be pre-
 19 scribed by the Secretary or his delegate) the items re-
 20 quired to be taken into account for purposes of section
 21 38 in respect of the distributor or transferor corpora-
 22 tion."

23 (e) STATUTES OF LIMITATIONS AND INTEREST RE-
 24 LATING TO INVESTMENT CREDIT CARRYBACKS.—

(1) *ASSESSMENT AND COLLECTION.*—Section 6501 (relating to limitations on assessment and collection) is amended by redesignating subsection (j) as subsection (k), and inserting after subsection (i) the following new subsection:

“(j) *INVESTMENT CREDIT CARRYBACKS.*—In the case of a deficiency attributable to the application to the taxpayer of an investment credit carryback, such deficiency may be assessed at any time before the expiration of the period within which a deficiency for the taxable year of the unused investment credit which results in such carryback may be assessed.”

(2) *CREDIT OR REFUND.*—Subsection (d) of section 6511 (relating to limitations on credit or refund) is amended by adding after paragraph (3) thereof the following new paragraph:

“(4) *SPECIAL PERIOD OF LIMITATION WITH RESPECT TO INVESTMENT CREDIT CARRYBACKS.*—

“(A) *PERIOD OF LIMITATION.*—If the claim for credit or refund relates to an overpayment attributable to an investment credit carryback, in lieu of the 3-year period of limitation prescribed in subsection (a), the period shall be that period which ends with the expiration of the 15th day of the

1 40th month (or 39th month, in the case of a cor-
2 poration) following the end of the taxable year of
3 the unused investment credit which results in such
4 carryback, or the period prescribed in subsection (c)
5 in respect of such taxable year, whichever expires
6 later. In the case of such a claim, the amount of
7 the credit or refund may exceed the portion of the
8 tax paid within the period provided in subsection
9 (b)(2) or (c), whichever is applicable, to the
10 extent of the amount of the overpayment attribut-
11 able to such carryback.

12 “(B) *APPLICABLE RULES.*—If the allowance
13 of a credit or refund of an overpayment of tax
14 attributable to an investment credit carryback is
15 otherwise prevented by the operation of any law
16 or rule of law other than section 7122, relating to
17 compromises, such credit or refund may be allowed
18 or made, if claim therefor is filed within the period
19 provided in subparagraph (A) of this paragraph.
20 In the case of any such claim for credit or refund,
21 the determination by any court, including the Tax
22 Court, in any proceeding in which the decision of
23 the court has become final, shall not be conclusive
24 with respect to the investment credit, and the effect

1 of such credit, to the extent that such credit is
2 affected by a carryback which was not in issue in
3 such proceeding.”

4 (3) *INTEREST ON UNDERPAYMENTS.*—Section
5 6601(e) (relating to interest on underpayment, nonpay-
6 ment, or extensions of time for payment, of tax) is
7 amended to read as follows:

8 “(e) *INCOME TAX REDUCED BY CARRYBACK.*—

9 “(1) *NET OPERATING LOSS CARRYBACK.*—If the
10 amount of any tax imposed by subtitle A is reduced by
11 reason of a carryback of a net operating loss, such reduc-
12 tion in tax shall not affect the computation of interest
13 under this section for the period ending with the last
14 day of the taxable year in which the net operating loss
15 arises.

16 “(2) *INVESTMENT CREDIT CARRYBACK.*—If the
17 credit allowed by section 38 for any taxable year is in-
18 creased by reason of an investment credit carryback, such
19 increase shall not affect the computation of interest under
20 this section for the period ending with the last day of
21 the taxable year in which the investment credit carry-
22 back arises.”

23 (4) *INTEREST ON OVERPAYMENTS.*—Section 6611
24 (f) (relating to interest on overpayments) is amended to
25 read as follows:

1 “(f) *REFUND OF INCOME TAX CAUSED BY CARRY-*
2 *BACK.*—

3 “(1) *NET OPERATING LOSS CARRYBACK.*—For
4 *purposes of subsection (a), if any overpayment of tax*
5 *imposed by subtitle A results from a carryback of a net*
6 *operating loss, such overpayment shall be deemed not*
7 *to have been made prior to the close of the taxable year*
8 *in which such net operating loss arises.*

9 “(2) *INVESTMENT CREDIT CARRYBACK.*—For pur-
10 *poses of subsection (a), if any overpayment of tax im-*
11 *posed by subtitle A results from an investment credit*
12 *carryback, such overpayment shall be deemed not to*
13 *have been made prior to the close of the taxable year*
14 *in which such investment credit carryback arises.”*

15 “(f) *TECHNICAL AMENDMENT.*—Section 1016(a) (re-
16 *lating to adjustments to basis) is amended—*

17 (1) *by striking out the period at the end of para-*
18 *graph (18) and inserting in lieu thereof a semicolon; and*

19 (2) *by adding after paragraph (18) the following*
20 *new paragraph:*

21 “(19) *to the extent provided in section 48(g) in*
22 *the case of property which is or has been section 38*
23 *property (as defined in section 48(a));”.*

24 ~~(d) *CLERICAL AMENDMENT.*—Part IV of subchapter~~

1 ~~A of chapter 1 is amended by inserting after the heading and~~
 2 ~~before the table of sections the following:~~

3 (g) *CLERICAL AMENDMENTS.*—

4 (1) *Part IV of subchapter A of chapter 1 is*
 5 *amended by inserting after the heading and before the*
 6 *table of sections the following:*

“Subpart A. Credits allowable.

“Subpart B. Rules for computing credit for investment in
 certain depreciable property.

7 “Subpart A—Credits Allowable”

8 (2) *The table of sections for part IV of subchapter*
 9 *A of chapter 1 is amended by striking out*

“Sec. 38. Overpayments of tax.”

10 *and inserting in lieu thereof*

“Sec. 38. Investment in certain depreciable property.

“Sec. 39. Overpayments of tax.”

11 (3) *The table of sections for part VI of subchapter*
 12 *B of chapter 1 is amended by adding at the end thereof*
 13 *the following:*

“Sec. 181. Deduction for certain unused investment credit.”

14 ~~(e)~~ (h) *EFFECTIVE DATE.*—The amendments made by
 15 this section shall apply with respect to taxable years ending
 16 after ~~December 31, 1961~~ *June 30, 1962.*

17 **SEC. 3. APPEARANCES, ETC., WITH RESPECT TO LEGIS-**
 18 **LATION.**

19 (a) *IN GENERAL.*—Section 162 (relating to trade or
 20 business expenses) is amended by redesignating subsection

1 (e) as subsection (f) and by inserting after subsection (d)
 2 the following new subsection:

3 “(e) APPEARANCES, ETC., WITH RESPECT TO LEGIS-
 4 LATION.—

5 “(1) IN GENERAL.—The deduction allowed by
 6 subsection (a) shall include all the ordinary and neces-
 7 sary expenses (including, but not limited to, traveling
 8 expenses described in subsection (a) (2) and the cost
 9 of preparing testimony) paid or incurred during the tax-
 10 able year in carrying on any trade or business—

11 “(A) in direct connection with appearances
 12 before, submission of statements to, or sending com-
 13 munications to, the committees, or individual mem-
 14 bers, of Congress or of any legislative body of a
 15 State, a possession of the United States, or a politi-
 16 cal subdivision of any of the foregoing with respect
 17 to legislation or proposed legislation of direct inter-
 18 est to the taxpayer, or

19 “(B) in direct connection with communication
 20 of information between the taxpayer and an organ-
 21 ization of which he is a member with respect to
 22 legislation or proposed legislation of direct interest
 23 to the taxpayer and to such organization, or

24 “(C) in direct connection with communication
 25 of information between the taxpayer and an employee

1 *or stockholder with respect to legislation or proposed*
2 *legislation of direct interest to the taxpayer,*
3 and that portion of the dues so paid or incurred with
4 respect to any organization of which the taxpayer is a
5 member which is attributable to the expenses of the
6 activities described in subparagraphs (A) and (B)
7 carried on by such organization.

8 “(2) LIMITATION.—The provisions of paragraph
9 (1) shall not be construed as allowing the deduction of
10 any amount paid or incurred (whether by way of con-
11 tribution, gift, or otherwise) —

12 “(A) for participation in, or intervention in,
13 any political campaign on behalf of any candidate
14 for public office, or

15 “(B) in connection with any attempt to in-
16 fluence the general public, or segments thereof, with
17 respect to legislative matters, elections, or referen-
18 dums.”

19 (b) EFFECTIVE DATE.—The amendments made by this
20 section shall apply to taxable years beginning after Decem-
21 ber 31, 1962.

1 SEC. 4. DISALLOWANCE OF CERTAIN ENTERTAINMENT,
2 ETC., EXPENSES.

3 (a) DENIAL OF DEDUCTION.—

4 (1) Part IX of subchapter B of chapter 1 (relating
5 to items not deductible in computing taxable income) is
6 amended by adding at the end thereof the following new
7 section:

8 “SEC. 274. DISALLOWANCE OF CERTAIN ENTERTAINMENT,
9 ETC., EXPENSES.

10 “(a) ENTERTAINMENT, AMUSEMENT, OR RECREA-
11 TION.—

12 “(1) IN GENERAL.—No deduction otherwise allow-
13 able under this chapter shall be allowed for any item—

14 “(A) ACTIVITY.—With respect to an activity
15 which is of a type generally considered to consti-
16 tute entertainment, amusement, or recreation, unless
17 the taxpayer establishes that the item was directly
18 related to *or associated with* the active conduct of
19 the taxpayer’s trade or business, or

20 “(B) FACILITY.—With respect to a facility
21 used in connection with an activity referred to in

1 subparagraph (A), unless the taxpayer establishes
2 that the facility was used primarily for the further-
3 ance of the taxpayer's trade or business and that the
4 item was directly related to *or associated with* the
5 active conduct of such trade or business,

6 and such deduction shall in no event exceed the portion
7 of such item directly related to *or associated with* the
8 active conduct of the taxpayer's trade or business.

9 “(2) SPECIAL RULES.—For purposes of applying
10 paragraph (1) —

11 “(A) Dues or fees to any social, athletic, or
12 sporting club or organization shall be treated as
13 items with respect to facilities.

14 “(B) An activity described in section 212
15 shall be treated as a trade or business.

16 “(b) GIFTS.—

17 “(1) LIMITATION.—No deduction shall be allowed
18 under section 162 or section 212 for any expense for
19 gifts made directly or indirectly to any individual to the
20 extent that such expense, when added to prior expenses
21 of the taxpayer for gifts made to such individual during
22 the same taxable year, exceeds \$25. For purposes of
23 this section, the term ‘gift’ means any item excludable
24 from gross income of the recipient under section 102
25 which is not excludable from his gross income under any

1 other provision of this ~~chapter~~ chapter, but such term
 2 does not include—

3 “(A) an item having a cost to the taxpayer not
 4 in excess of \$4.00 on which the name of the taxpayer
 5 is clearly and permanently imprinted and which is
 6 one of a number of identical items distributed gen-
 7 erally by the taxpayer,

8 “(B) a sign, display rack, or other promotional
 9 material to be used on the business premises of the
 10 recipient, or

11 “(C) an item of tangible personal property
 12 having a cost to the taxpayer not in excess of \$100
 13 which is awarded to an employee by reason of length
 14 of service or for safety achievement.

15 “(2) SPECIAL RULES.—

16 “(A) In the case of a gift by a partnership, the
 17 limitation contained in paragraph (1) shall apply
 18 to the partnership as well as to each member
 19 thereof.

20 “(B) For purposes of paragraph (1), a hus-
 21 band and wife shall be treated as one taxpayer.

22 “(c) TRAVELING.—In the case of any individual who
 23 is traveling away from home in pursuit of a trade or business
 24 or in pursuit of an activity described in section 212, no deduc-
 25 tion shall be allowed under section 162 or section 212 for

1 *that portion of the expenses of such travel otherwise allow-*
 2 *able under such section which, under regulations prescribed*
 3 *by the Secretary or his delegate, is not allocable to such trade*
 4 *or business or to such activity. This subsection shall not*
 5 *apply to the expenses of any travel away from home which*
 6 *does not exceed one week or where the portion of the time*
 7 *away from home which is not attributable to the pursuit of*
 8 *the taxpayer's trade or business or an activity described in*
 9 *section 212 is less than 25 percent of the total time away*
 10 *from home on such travel.*

11 “~~(e)~~ (d) SUBSTANTIATION REQUIRED.—No deduction
 12 shall be allowed—

13 “(1) under section 162 or 212 for any traveling
 14 expense (including meals and lodging while away from
 15 home),

16 “(2) for any item with respect to an activity which
 17 is of a type generally considered to constitute entertain-
 18 ment, amusement, or recreation, or with respect to a
 19 facility used in connection with such an activity, or

20 “(3) for any expense for gifts,
 21 unless the taxpayer substantiates by adequate records or by
 22 sufficient evidence corroborating his own statement (A) the
 23 amount of such expense or other item, (B) the time and
 24 place of the travel, entertainment, amusement, recreation, or
 25 use of the facility, or the date and description of the gift, (C)

1 the business purpose of the expense or other item, and (D)
2 the business relationship to the taxpayer of persons enter-
3 tained, using the facility, or receiving the gift. The Secre-
4 tary or his delegate may by regulations provide that some
5 or all of the requirements of the preceding sentence shall not
6 apply in the case of an expense which does not exceed an
7 amount prescribed pursuant to such regulations.

8 “~~(d)~~ (e) SPECIFIC EXCEPTIONS TO APPLICATION OF
9 SUBSECTION (a).—Subsection (a) shall not apply to—

10 “(1) BUSINESS MEALS.—Expenses for food and
11 beverages furnished to any individual under circum-
12 stances which (taking into account the surroundings in
13 which furnished, the taxpayer’s trade, business, or in-
14 come-producing activity and the relationship to such
15 trade, business, or activity of the persons to whom the
16 food and beverages are furnished) are of a type gen-
17 erally considered to be conducive to a business dis-
18 cussion.

19 “(2) FOOD AND BEVERAGES FOR EMPLOYEES.—
20 Expenses for food and beverages (and facilities used
21 in connection therewith) furnished on the business
22 premises of the taxpayer primarily for his employees.

23 “(3) EXPENSES TREATED AS COMPENSATION.—
24 Expenses for goods, services, and facilities, to the ex-
25 tent that the expenses are treated by the taxpayer, with

1 respect to the recipient of the entertainment, amusement,
2 or recreation, as compensation to an employee on the
3 taxpayer's return of tax under this chapter and as wages
4 to such employee for purposes of chapter 24 (relating
5 to withholding of income tax at source on wages).

6 “(4) REIMBURSED EXPENSES.—Expenses paid or
7 incurred by the taxpayer, in connection with the per-
8 formance by him of services for another person
9 (whether or not such other person is his employer),
10 under a reimbursement or other expense allowance
11 arrangement with such other person, but this para-
12 graph shall apply—

13 “(A) where the services are performed for
14 an employer, only if the employer has not treated
15 such expenses in the manner provided in paragraph
16 (3), or

17 “(B) where the services are performed for a
18 person other than an employer, only if the tax-
19 payer accounts (to the extent provided by sub-
20 section ~~(e)~~ (d)) to such person.

21 “(5) RECREATIONAL, ETC., EXPENSES FOR EM-
22 PLOYEES.—Expenses for recreational, social, or similar
23 activities (including facilities therefor) primarily for
24 the benefit of employees (other than employees who
25 are officers, shareholders or other owners, or highly

compensated employees). For purposes of this paragraph, an individual owning less than a 10-percent interest in the taxpayer's trade or business shall not be considered a shareholder or other owner, and for such purposes an individual shall be treated as owning any interest owned by a member of his family (within the meaning of section 267 (c) (4)).

~~“(6) EMPLOYEE AND STOCKHOLDER BUSINESS MEETINGS.—Expenses directly related to business meetings of employees or stockholders.~~

“(6) *EMPLOYEE, STOCKHOLDER, ETC., BUSINESS MEETINGS.—Expenses incurred by a taxpayer which are directly related to business meetings of his employees, stockholders, agents, or directors.*

“(7) *MEETINGS OF BUSINESS LEAGUES, ETC.—Expenses directly related and necessary to attendance at a business meeting or convention of any organization described in section 501 (c) (6) (relating to business leagues, chambers of commerce, real estate boards, and boards of trade) and exempt from taxation under section 501 (a) .*

“(8) *ITEMS AVAILABLE TO PUBLIC.—Expenses for goods, services, and facilities made available by the taxpayer to the general public.*

“(9) *ENTERTAINMENT SOLD TO CUSTOMERS.—*

1 Expenses for goods or services (including the use
 2 of facilities) which are sold by the taxpayer in a bona
 3 fide transaction for an adequate and full consideration in
 4 money or money's worth.

5 For purposes of this subsection, any item referred to in sub-
 6 section (a) shall be treated as an expense.

7 “~~(e)~~ (f) INTEREST, TAXES, CASUALTY LOSSES, ETC.—

8 This section shall not apply to any deduction allowable to
 9 the taxpayer without regard to its connection with his trade
 10 or business (or with his income-producing activity). In the
 11 case of a taxpayer which is not an individual, the preceding
 12 sentence shall be applied as if it were an individual.

13 “~~(f)~~ (g) TREATMENT OF ENTERTAINMENT, ETC., TYPE

14 FACILITY.—For purposes of this chapter, if deductions are
 15 disallowed under subsection (a) with respect to any portion
 16 of a facility, such portion shall be treated as an asset which is
 17 used for personal, living, and family purposes (and not as
 18 an asset used in the trade or business).

19 “~~(g)~~ (h) REGULATORY AUTHORITY.—The Secretary or

20 his delegate shall prescribe such regulations as he may deem
 21 necessary to carry out the purposes of this section, includ-
 22 ing regulations prescribing whether subsection (a) or sub-
 23 section (b) applies in cases where both such subsections
 24 would otherwise apply.”

1 (2) The table of sections for such part IX is
2 amended by adding at the end thereof the following:

"Sec. 274. Disallowance of certain entertainment, etc., expenses."

3 (b) TRAVELING EXPENSES.—Section 162 (a) (2) (re-
4 lating to traveling expenses) is amended by striking out
5 “(including the entire amount expended for meals and lodg-
6 ing)” and inserting in lieu thereof “(including a reasonable
7 allowance for amounts expended for meals and lodging
8 amounts expended for meals and lodging other than amounts
9 which are lavish or extravagant under the circumstances)”.

(c) EFFECTIVE DATE.—The amendments made by this section shall apply with respect to taxable years ending after ~~June 30, 1962~~ *December 31, 1962*, but only in respect of periods after such date.

14 SEC. 5. AMOUNT OF DISTRIBUTION WHERE CERTAIN
15 FOREIGN CORPORATIONS DISTRIBUTE PROP-
16 ERTY IN KIND.

17 (a) AMOUNT DISTRIBUTED.—Section 301(b)(1)
18 (relating to amount distributed to corporate distributees) is
19 amended by adding at the end thereof the following new
20 subparagraph:

21 “(C) CERTAIN CORPORATE DISTRIBUTEES OF
22 FOREIGN CORPORATION.—Notwithstanding subpara-

graph (B), if the shareholder is a corporation and the distributing corporation is a foreign corporation, the amount taken into account with respect to property (other than money) shall be the fair market value of such property; except that if any deduction is allowable under section 245 with respect to such distribution, then the amount taken into account shall be the sum (determined under regulations prescribed by the Secretary or his delegate) of—

- “(i) the proportion of the adjusted basis of such property (or, if lower, its fair market value) properly attributable to gross income from sources within the United States, and
- “(ii) the proportion of the fair market value of such property properly attributable to gross income from sources without the United States.”

(b) BASIS.—Section 301 (d) (relating to basis of property) is amended by adding at the end thereof the following new paragraph:

“(3) CERTAIN CORPORATE DISTRIBUTEES OF FOREIGN CORPORATION.—In the case of property described in subparagraph (C) of subsection (b) (1), the basis

shall be determined by substituting the amount determined under such subparagraph (C) for the amount described in paragraph (2) of this subsection."

(c) DIVIDENDS RECEIVED FROM CERTAIN FOREIGN CORPORATIONS.—

(1) Section 245 (relating to dividends received from certain foreign corporations) is amended by adding at the end thereof the following new subsection:

"(b) PROPERTY DISTRIBUTIONS.—For purposes of subsection (a), the amount of any distribution of property other than money shall be the amount determined by applying section 301(b)(1)(B)."

(2) Section 245 is amended by striking out "In the case of" and inserting in lieu thereof "(a) GENERAL RULE.—In the case of".

~~(d) CREDIT FOR FOREIGN TAXES.—Section 902(a) (relating to credit for foreign taxes) is amended by adding at the end thereof the following new sentence: "For purposes of this subsection and subsection (b), the amount of any distribution in property other than money shall be the amount determined by applying section 301(b)(1)(B)."~~

~~(e)~~ (d) EFFECTIVE DATE.—The amendments made by this section shall apply to distributions made after December 31, 1962.

1 **SEC. 6. AMENDMENT OF SECTION 482.**

2 ~~(a)~~ **IN GENERAL.**—Section 482 ~~(relating to allocation~~
 3 ~~of income and deductions among taxpayers)~~ is amended
 4 by adding at the end thereof the following new subsection:

5 ~~“(b)~~ **SALES AND PURCHASES WITHIN A RELATED**
 6 **GROUP WHICH INCLUDES A FOREIGN ORGANIZATION.**—

7 ~~“(1)~~ **IN GENERAL.**—In applying subsection ~~(a)~~
 8 to sales of tangible property within a group of organiza-
 9 tions—

10 ~~“(A)~~ owned or controlled directly or indi-
 11 rectly by the same interests, and

12 ~~“(B)~~ at least one of which is a domestic or-
 13 ganization and at least one of which is a foreign
 14 organization,

15 the Secretary or his delegate may allocate the taxable
 16 income of the group arising from such sales in the
 17 manner set forth in paragraph ~~(2)~~. This subsection
 18 shall not apply with respect to any sale of tangible
 19 property for which the taxpayer can establish an arm's
 20 length price ~~(within the meaning of paragraph (4))~~.

21 ~~“(2)~~ **METHODS OF ALLOCATION.**—

22 ~~“(A)~~ **CONSIDERATION OF CERTAIN FAC-**
 23 **TORS.**—Except as provided in subparagraph ~~(B)~~,
 24 the allocation referred to in paragraph ~~(1)~~ shall be

made by the Secretary or his delegate by taking into consideration that portion of the following factors which is attributable to the United States and that portion thereof which is not attributable to the United States—

“(i) assets of the group, to the extent used in the production, distribution, and sale of the property,

“(ii) compensation of officers and employees, to the extent attributable to the production, distribution, and sale of the property, and

“(iii) advertising, selling, and sales promotion expenses (including technical and servicing expenses), to the extent attributable to the property.

Such method of allocation may also give consideration to other factors, including the special risks (if any) of the market in which the property is sold.

“(B) ALTERNATIVE METHODS.—If the taxpayer establishes to the satisfaction of the Secretary or his delegate that an alternative method of allocation clearly reflects the income of each member of the group with respect to the property referred to in

1 paragraph (1), such alternative method shall be
 2 used (in lieu of the method provided in subpara-
 3 graph (A)).

4 “(3) SPECIAL RULES.—In applying the method
 5 of allocation referred to in paragraph (2)(A), the
 6 following rules shall be applied:

7 “(A) ADJUSTED BASIS OF ASSETS.—The
 8 values to be assigned to the assets referred to in
 9 paragraph (2)(A)(i) is their adjusted basis in the
 10 hands of the taxpayer or, if such basis is not avail-
 11 able in the case of a foreign organization, then their
 12 book values, adjusted to approximate their adjusted
 13 basis.

14 “(B) INCLUDIBLE ASSETS.—The assets re-
 15 ferred to in paragraph (2)(A)(i) include real
 16 property and tangible personal property (whether
 17 owned or leased by a member of the group), but do
 18 not include inventory and stock in trade.

19 “(4) ARM’S LENGTH PRICE DEFINED.—For pur-
 20 poses of this subsection, the term ‘arm’s length price’
 21 means—

22 “(A) the price at which tangible property sim-
 23 ilar or comparable to the property referred to in
 24 paragraph (1) generally is or can be sold in trans-

actions in the same areas involving unrelated persons and made under similar conditions of sale; and

“(B) if subparagraph (A) does not apply, the price at which tangible property similar or comparable to the property referred to in paragraph (1) is sold in the same or other areas under similar circumstances and in transactions involving unrelated persons, with adjustment for material differences in quantity, marketing conditions (including customs duties and transportation costs), and other relevant factors.

Subparagraph (B) shall apply only if the adjustment referred to therein is properly determinable.

“(5) SALES COMMISSIONS.—The Secretary or his delegate shall by regulation prescribe rules for the allocation of commissions arising from sales of tangible property within a group of organizations described in paragraph (1). Such rules shall be consistent with the principles specified in the other paragraphs of this subsection.

“(6) GROSSLY INADEQUATE ASSETS, ETC., OUTSIDE UNITED STATES.—In allocating taxable income under this subsection, no amount shall be allocated to a foreign organization whose assets, personnel, and office

1 and other facilities which are not attributable to the
2 United States are grossly inadequate for its activities
3 outside the United States.

4 “(7) INFORMATION NECESSARY FOR CONSIDERA-
5 TION OF FACTORS.—In the case of any transaction to
6 which paragraph (2)(A) applies, if—

7 “(A) the information submitted with respect
8 to the group of organizations is insufficient for the
9 proper application of the method of allocation set
10 forth in the first sentence of such paragraph, and

11 “(B) upon request of the Secretary or his
12 delegate, such group fails to furnish such additional
13 information with respect to such transaction as may
14 be reasonably supplied,

15 the Secretary or his delegate may estimate the taxable
16 income arising from such transaction and may allocate
17 such taxable income among the members of the group
18 or to any single member thereof.

19 “(8) TREATMENT OF FOREIGN TAXES.—

20 “(A) For purposes of this subsection, taxable
21 income shall be determined without regard to any
22 income, war profits, or excess profits taxes paid to

any foreign country or to any possession of the United States.

~~“(B)~~ Where the application of this subsection results in a decrease in the taxable income of any foreign organization and an increase in the taxable income of any domestic organization, then any of the taxes referred to in subparagraph (A) paid by such foreign organization and attributable to the taxable income so transferred shall be treated for purposes of this chapter—

~~“(i)~~ as paid by such domestic organization, and

~~“(ii)~~ as not paid by such foreign organization.”

~~(b)~~ CLERICAL AMENDMENT.—Section 482 is amended by striking out “In any case of two or more organizations” and inserting in lieu thereof the following:

~~“(a)~~ GENERAL RULE.—In the case of two or more organizations”.

~~(c)~~ EFFECTIVE DATE.—The amendments made by this section shall apply with respect to taxable years beginning after December 31, 1962.

1 **SEC. 7. DISTRIBUTIONS OF FOREIGN PERSONAL HOLD-**
 2 **ING COMPANY INCOME.**

3 ~~(a)~~ **DEFINITION OF FOREIGN PERSONAL HOLDING**
 4 **COMPANY.**—So much of subsection ~~(a)~~ of section 552 (re-
 5 lating to definition of foreign personal holding company) as
 6 precedes paragraph ~~(2)~~ is amended to read as follows:

7 “~~(a)~~ **GENERAL RULE.**—For purposes of this subtitle,
 8 the term ‘foreign personal holding company’ for a taxable
 9 year beginning after December 31, 1962, means any for-
 10 eign corporation if—

11 “~~(1)~~ **GROSS INCOME REQUIREMENT.**—At least 20
 12 percent of its gross income (as defined in section 555
 13 ~~(a)~~) for the taxable year is foreign personal holding
 14 company income (as defined in section 553). For
 15 purposes of this paragraph, there shall be included in
 16 the gross income the amount includible therein as a
 17 dividend by reason of the application of section 555(c)
 18 ~~(2)~~; and”.

19 ~~(b)~~ **AMOUNT OF UNDISTRIBUTED INCOME.**—Subsec-
 20 tion ~~(a)~~ of section 556 (relating to undistributed foreign
 21 personal holding company income) is amended to read as
 22 follows:

23 “~~(a)~~ **DEFINITION.**—For purposes of this part—

24 “~~(1)~~ If the foreign personal holding company in-
 25 come of a foreign personal holding company exceeds

80 percent of its gross income, the 'undistributed foreign personal holding company income' of such company is its taxable income adjusted in the manner provided in subsection (b), minus the dividends paid deduction (as defined in section 561).

“(2) If the foreign personal holding company income of a foreign personal holding company does not exceed 80 percent of its gross income, the 'undistributed foreign personal holding company income' of such company is that amount which bears the same ratio to—

“(A) its taxable income adjusted in the manner provided in subsection (b), minus the dividends paid deduction (as defined in section 561), as

“(B) its foreign personal holding company income bears to its gross income.”

(c) **EFFECTIVE DATE.**—The amendments made by this section shall apply only in respect of taxable years of foreign corporations beginning after December 31, 1962.

SEC. 86. MUTUAL SAVINGS BANKS, ETC.

(a) **RESERVES FOR LOSSES ON LOANS.**—Section 593 is amended to read as follows:

“SEC. 593. RESERVES FOR LOSSES ON LOANS.

“(a) **ORGANIZATIONS TO WHICH SECTION APPLIES.**— This section shall apply to any mutual savings bank not having capital stock represented by shares, domestic building

1 and loan association, or cooperative bank without capital
2 stock organized and operated for mutual purposes and with-
3 out profit.

4 “(b) ADDITION TO RESERVES FOR BAD DEBTS.—

5 “(1) IN GENERAL.—For purposes of section 166
6 (c), the reasonable addition for the taxable year to the
7 reserve for bad debts of any taxpayer described in sub-
8 section (a) shall be an amount equal to the sum of—

9 “(A) the amount determined under section
10 166 (c) to be a reasonable addition to the reserve
11 for losses on nonqualifying loans, plus

12 “(B) the amount determined by the taxpayer
13 to be a reasonable addition to the reserve for losses
14 on qualifying real property loans, but such amount
15 shall not exceed the amount determined under para-
16 graph (2), (3), or (4), whichever amount is the
17 largest, *but the amount determined under this sub-*
18 *paragraph, when added to the amount determined*
19 *under subparagraph (A), shall in no case be greater*
20 *than the amount by which 12 percent of the total*
21 *deposits or withdrawable accounts of depositors of*
22 *the taxpayer at the close of such year exceeds the sum*
23 *of its surplus, undivided profits, and reserves at the*
24 *beginning of such year (taking into account any*
25 *portion thereof attributable to the period before the*

first taxable year beginning after December 31, 1951).

“(2) ~~60~~ PERCENT PERCENTAGE OF TAXABLE INCOME METHOD.—The amount determined under this paragraph for the taxable year shall be the excess of—

“(A) ~~an amount equal to 60 percent of the taxable income for such year, over~~

“(A) *an amount—*

“(i) *in the case of a taxpayer other than a taxpayer described in clause (ii), equal to 60 percent of the taxable income for such year, or*

“(ii) *in the case of a domestic building and loan association having capital stock with respect to which any distribution of property (as defined in section 317(a)) is not allowable as a deduction under section 591, equal to 50 percent of the taxable income for such year, over*

“(B) the amount referred to in paragraph (1) (A) for such ~~year~~ year,

but the amount determined under this paragraph shall not exceed the amount necessary to increase the balance (as of the close of the taxable year) of the reserve for losses on qualifying real property loans to 6 percent of such loans outstanding at such time. For purposes of this

1 paragraph, taxable income shall be computed (i) by
 2 excluding from gross income any amount included
 3 therein by reason of subsection (f), and (ii) without
 4 regard to any deduction allowable for any addition to the
 5 reserve for bad debts.

6 “(3) ~~3 PERCENT~~ *PERCENTAGE* OF REAL PROPERTY
 7 LOANS METHOD.—The amount determined under this
 8 paragraph for the taxable year shall be an amount equal
 9 to the amount necessary to increase the balance (as of
 10 the close of the taxable year) of the reserve for losses on
 11 qualifying real property loans ~~to 3 percent of such loans~~
 12 ~~outstanding at such time:~~ *to an amount equal to—*

13 “(A) *3 percent of such loans outstanding at*
 14 *such time, plus*

15 “(B) *in the case of a taxpayer which is a new*
 16 *company and which does not have capital stock with*
 17 *respect to which distributions of property (as defined*
 18 *in section 317(a)) are not allowable as a deduction*
 19 *under section 591, an amount equal to—*

20 “(i) *2 percent of so much of the amount of*
 21 *such loans outstanding at such time as does not*
 22 *exceed \$4,000,000, reduced (but not below*
 23 *zero) by*

24 “(ii) *the amount, if any, of the balance (as*

1 *of the close of such taxable year) of the tax-*
2 *payer's supplemental reserve for losses on loans.*

3 *For purposes of subparagraph (B), a taxpayer is a*
4 *new company for any taxable year only if such taxable*
5 *year begins not more than 10 years after the first day*
6 *on which it (or any predecessor) was authorized to do*
7 *business as an organization described in subsection (a).*

8 “(4) EXPERIENCE METHOD.—The amount deter-
9 mined under this paragraph for the taxable year shall
10 be an amount equal to the amount determined under
11 section 166 (c) (without regard to this subsection) to
12 be a reasonable addition to the reserve for losses on
13 qualifying real property loans.

14 “(c) TREATMENT OF RESERVES FOR BAD DEBTS.—

15 “(1) ESTABLISHMENT OF RESERVES.—Each tax-
16 payer described in subsection (a) which uses the reserve
17 method of accounting for bad debts shall establish and
18 maintain a reserve for losses on qualifying real property
19 loans, a reserve for losses on nonqualifying loans, and a
20 supplemental reserve for losses on loans. For purposes
21 of this title, such reserves shall be treated as reserves
22 for bad debts, but no deduction shall be allowed for any
23 addition to the supplemental reserve for losses on loans.

24 “(2) ALLOCATION OF PRE-1963 RESERVES.—For
25 purposes of this section, the pre-1963 reserves shall, as

1 of the close of December 31, 1962, be allocated to, and
2 constitute the opening balance of—

3 “(A) the reserve for losses on nonqualifying
4 loans,

5 “(B) the reserve for losses on qualifying real
6 property loans, and

7 “(C) the supplemental reserve for losses on
8 loans.

9 “(3) METHOD OF ALLOCATION.—The allocation
10 provided by paragraph (2) shall be made—

11 “(A) first, to the reserve described in para-
12 graph (2) (A), to the extent such reserve is not
13 increased above the amount which would be a
14 reasonable addition under section 166(c) for a
15 period in which the nonqualifying loans increased
16 from zero to the amount thereof outstanding at the
17 close of December 31, 1962;

18 “(B) second, to the reserve described in para-
19 graph (2) (B), to the extent such reserve is not
20 increased above the amount which would be deter-
21 mined under paragraph ~~(3)~~ (3)(A) or (4) of
22 subsection (b) (whichever such amount is the
23 larger) for a period in which the qualifying real
24 property loans increased from zero to the amount
25 thereof outstanding at the close of December 31,
26 1962; and

1 “(C) then to the supplemental reserve for
2 losses on loans.

3 “(4) PRE-1963 RESERVES DEFINED.—For purposes
4 of this subsection, the term ‘pre-1963 reserves’ means
5 the net amount, determined as of the close of December
6 31, 1962 (after applying subsection (d) (1)), accumu-
7 lated in the reserve for bad debts pursuant to section
8 166(c) (or the corresponding provisions of prior reve-
9 nue laws) for taxable years beginning after December
10 31, 1951.

11 “(5) CERTAIN PRE-1952 SURPLUS.—If after the
12 application of paragraph (3), the opening balance of the
13 reserve described in paragraph (2)(B) is less than the
14 amount described in paragraph (3)(B), then, for pur-
15 poses of this subsection, the term ‘pre-1963 reserves’ in-
16 cludes so much of the surplus, undivided profits, and bad
17 debt reserves (determined as of December 31, 1962)
18 attributable to the period before the first taxable year
19 beginning after December 31, 1951, as does not exceed
20 the amount by which such opening balance is less than
21 the amount described in paragraph (3)(B). For pur-
22 poses of the preceding sentence, the surplus, undivided
23 profits, and bad debt reserves attributable to the period
24 before the first taxable year beginning after December 31,

1951, shall be reduced by the amount thereof which is attributable to interest which would have been excludable from gross income under section 22(b)(4) of the Internal Revenue Code of 1939 (relating to interest on governmental obligations) or the corresponding provisions of prior laws. Notwithstanding the second sentence of paragraph (1), any amount which, by reason of the application of the first sentence of this paragraph, is allocated to the reserve described in paragraph (2)(B) shall not be treated as a reserve for bad debts for any purpose other than determining the amount referred to in subsection (b)(1)(B), and for such purpose such amount shall be treated as remaining in such reserve.

“(5) (6) CHARGING OF BAD DEBTS TO RESERVES.—

Any debt becoming worthless or partially worthless in respect of a qualifying real property loan shall be charged to the reserve for losses on such loans, and any debt becoming worthless or partially worthless in respect of a nonqualifying loan shall be charged to the reserve for losses on nonqualifying loans; except that any such debt may, at the election of the taxpayer, be charged in whole or in part to the supplemental reserve for losses on loans.

“(d) TAXABLE YEARS BEGINNING IN 1962 AND ENDING IN 1963.—In the case of a taxable year beginning before

1 January 1, 1963, and ending after December 31, 1962, of
2 a taxpayer described in subsection (a) which uses the
3 reserve method of accounting for bad debts, the taxable in-
4 come shall be the sum of—

5 “(1) that portion of the taxable income allocable
6 to the part of the taxable year occurring before January
7 1, 1963, reduced by the amount of the deduction for an
8 addition to a reserve for bad debts which would be allow-
9 able under section 166(c) (without regard to the
10 amendments made by section 8 6 of the Revenue Act of
11 1962) if such part year constituted a taxable year, plus

12 “(2) that portion of the taxable income allocable
13 to the part of the taxable year occurring after December
14 31, 1962, reduced by the amount of the deduction for
15 an addition to a reserve for bad debts which would be
16 allowed under section 166(c) (taking into account the
17 amendments made by section 8 6 of the Revenue Act of
18 1962) if such part year constituted a taxable year.

19 For purposes of the preceding sentence, the taxable income
20 shall be determined without regard to any deduction under
21 section 166(c), and the portion thereof allocable to each
22 part year shall be determined on the basis of the ratio which
23 the number of days in such part year bears to the number
24 of days in the entire taxable year.

25 “(e) LOANS DEFINED.—For purposes of this section—

1 “(1) QUALIFYING REAL PROPERTY LOANS.—The
 2 term ‘qualifying real property loan’ means any loan se-
 3 cured by an interest in improved real property or secured
 4 by an interest in real property which is to be improved
 5 out of the proceeds of the loan, but such term does not
 6 include—

7 “(A) any loan evidenced by a security (as de-
 8 fined in section 165 (g) (2) (C)) ;

9 “(B) any loan, whether or not evidenced by a
 10 security (as defined in section 165 (g) (2) (C)) ,
 11 the primary obligor on which is—

12 “(i) a government or political subdivision
 13 or instrumentality thereof;

14 “(ii) a bank (as defined in section 581) ;
 15 or

16 “(iii) another member of the same affil-
 17 iated group;

18 “(C) any loan, to the extent secured by a
 19 deposit in or share of the taxpayer; or

20 “(D) any loan which, within a 60-day period
 21 beginning in one taxable year of the creditor and
 22 ending in its next taxable year, is made or acquired
 23 and then repaid or disposed of, unless the trans-

actions by which such loan was made or acquired
and then repaid or disposed of are established to be
for bona fide business purposes.

For purposes of subparagraph (B) (iii), the term
'affiliated group' has the meaning assigned to such term
by section 1504 (a) ; except that (i) the phrase 'more
than 50 percent' shall be substituted for the phrase 'at
least 80 percent' each place it appears in section 1504
(a), and (ii) all corporations shall be treated as
includible corporations (without any exclusion under
section 1504 (b)).

“(2) NONQUALIFYING LOANS.—The term 'non-
qualifying loan' means any loan which is not a quali-
fying real property loan.

“(3) LOAN.—The term 'loan' means debt, as the
term 'debt' is used in section 166.

“(f) DISTRIBUTIONS TO SHAREHOLDERS.—

“(1) IN GENERAL.—For purposes of this chapter,
any distribution of property (as defined in section 317
(a)) by a domestic building and loan association to a
shareholder with respect to its stock, if such distribution
is not allowable as a deduction under section 591, shall
be treated as made—

1 “(A) first out of its earnings and profits accu-
2 mulated in taxable years beginning after December
3 31, 1951, to the extent thereof,

4 “(B) then out of the reserve for losses on quali-
5 fying real property loans, to the extent additions
6 to such reserve exceed the additions which would
7 have been allowed under subsection (b) (4),

8 “(C) then out of the supplemental reserve for
9 losses on loans, to the extent thereof,

10 “(D) then out of such other accounts as may
11 be proper.

12 This paragraph shall apply in the case of any distribu-
13 tion in redemption of stock or in partial or complete
14 liquidation of the association, except that any such distri-
15 bution shall be treated as made first out of the amount
16 referred to in subparagraph (B), second out of the
17 amount referred to in subparagraph (C), third out of
18 the amount referred to in subparagraph (A), and then
19 out of such other accounts as may be proper.

20 “(2) AMOUNTS CHARGED TO RESERVE ACCOUNTS
21 AND INCLUDED IN GROSS INCOME.—If any distribution
22 is treated under paragraph (1) as having been made
23 out of the reserves described in subparagraphs (B) and
24 (C) of such paragraph, the amount charged against
25 such reserve shall be the amount which, when reduced

by the amount of tax imposed under this chapter and attributable to the inclusion of such amount in gross income, is equal to the amount of such distribution; and the amount so charged against such reserve shall be included in gross income of the taxpayer.

“(3) SPECIAL RULES.—

“(A) For purposes of paragraph (1) (B), additions to the reserve for losses on qualifying real property loans for the taxable year in which the distribution occurs shall be taken into account.

“(B) For purposes of computing under this section the amount of a reasonable addition to the reserve for losses on qualifying real property loans for any taxable year, any amount charged during any year to such reserve pursuant to the provisions of paragraph (2) shall not be taken into account.”

(b) FORECLOSURE ON PROPERTY SECURING LOANS.—

Part II of subchapter H of chapter 1 (relating to mutual savings banks, etc.) is amended by adding at the end thereof the following new section:

“SEC. 595. FORECLOSURE ON PROPERTY SECURING LOANS.

“(a) NONRECOGNITION OF GAIN OR LOSS AS A RESULT OF FORECLOSURE.—In the case of a creditor which is an organization described in section 593 (a), no gain or loss shall be recognized, and no debt shall be considered as be-

1 coming worthless or partially worthless, as the result of such
2 organization having bid in at foreclosure, or having otherwise
3 reduced to ownership or possession by agreement or process
4 of law, any property which was security for the payment of
5 any indebtedness.

6 “(b) CHARACTER OF PROPERTY.—For purposes of
7 sections 166 and 1221, any property acquired in a trans-
8 action with respect to which gain or loss to an organization
9 was not recognized by reason of subsection (a) shall be
10 considered as property having the same characteristics as
11 the indebtedness for which such property was security. Any
12 amount realized by such organization with respect to such
13 property shall be treated for purposes of this chapter as a
14 payment on account of such indebtedness, and any loss with
15 respect thereto shall be treated as a bad debt to which the
16 provisions of section 166 (relating to allowance of a deduc-
17 tion for bad debts) apply.

18 “(c) BASIS.—The basis of any property to which sub-
19 section (a) applies shall be the basis of the indebtedness for
20 which such property was security (determined as of the date
21 of the acquisition of such property) properly increased for
22 costs of acquisition.

23 “(d) REGULATORY AUTHORITY.—The Secretary or his
24 delegate shall prescribe such regulations as he may deem
25 necessary to carry out the purposes of this section.”

(c) DEFINITION OF DOMESTIC BUILDING AND LOAN ASSOCIATION.—Paragraph (19) of section 7701(a) (definition of domestic building and loan association) is amended to read as follows:

“(19) DOMESTIC BUILDING AND LOAN ASSOCIATION.—The term ‘domestic building and loan association’ means a domestic building and loan association, a domestic savings and loan association, and a Federal savings and loan association, which—

“(A) is an insured institution (within the meaning of section 401(a) of the National Housing Act (12 U.S.C., sec. 1724(a)), or

“(B) is subject by law to supervision and examination by State or Federal authority having supervision over such associations,

if substantially all of its business consists of accepting savings and investing the proceeds (i) in loans secured by an interest in real property which is (or, from the proceeds of the loan, will become) residential real property, and (ii) in other loans, to the extent such other loans would be authorized to be made by a Federal savings and loan association under section 5(e) of the Home Owners’ Loan Act, as amended (12 U.S.C., sec. 1464(e)).”

“(19) DOMESTIC BUILDING AND LOAN ASSOCIA-

1 *TION.—The term ‘domestic building and loan association’*
 2 *means a domestic building and loan association, a domes-*
 3 *tic savings and loan association, and a Federal savings*
 4 *and loan association—*

5 *“(A) which either (i) is an insured institution*
 6 *(within the meaning of section 401(a) of the Na-*
 7 *tional Housing Act (12 U.S.C., sec. 1724(a)), or*
 8 *(ii) is subject by law to supervision and examination*
 9 *by State or Federal authority having supervision*
 10 *over such associations;*

11 *“(B) substantially all of the business of which*
 12 *consists of acquiring the savings of the public and*
 13 *investing in loans described in subparagraph (C);*

14 *“(C) at least 90 percent of the amount of the*
 15 *total assets of which (as of the close of the taxable*
 16 *year) consists of (i) cash, (ii) obligations of the*
 17 *United States or of a State or political subdivision*
 18 *thereof, and stock or obligations of a corporation*
 19 *which is an instrumentality of the United States or*
 20 *of a State or political subdivision thereof, (iii) loans*
 21 *secured by an interest in real property and loans*
 22 *made for the improvement of real property, (iv)*
 23 *loans secured by a deposit or share of a member,*
 24 *and (v) property acquired through the liquidation*
 25 *of defaulted loans described in clause (iii);*

1 “(D) of the assets of which taken into account
2 under subparagraph (C) as assets constituting the
3 90 percent of total assets—

4 “(i) at least 80 percent of the amount of
5 such assets consists of assets described in clauses
6 (i) and (ii) of such subparagraph and of loans
7 secured by an interest in real property which is
8 (or, from the proceeds of the loan, will become)
9 residential real property or loans made for the
10 improvement of residential real property; and

11 “(ii) at least 70 percent of the amount of
12 such assets consists of assets described in clauses
13 (i) and (ii) of such subparagraph and of
14 loans secured by an interest in real property
15 which is (or, from the proceeds of the loan, will
16 become) residential real property containing 4
17 or fewer family units, or loans made for the
18 improvement of residential real property con-
19 taining 4 or fewer family units;

20 “(E) not more than 18 percent of the amount of
21 the total assets of which (as of the close of the taxable
22 year) consists of assets other than those described
23 in clause (i) of subparagraph (D), and not more
24 than 27 percent of the amount of the total assets of
25 which (as of the close of the taxable year) consists

of assets other than those described in clause (ii) of subparagraph (D), except that the 18 percent and 27 percent limitations contained in this subparagraph shall be increased by the number, if any, of percentage points (including any fraction of a percentage point) by which 10 percent exceeds the percentage of the total assets consisting of assets described in clauses (i) and (ii) of subparagraph (C); and

“(F) except for property described in subparagraph (C), none of the assets of which consists of stock of any corporation.”

(d) CLERICAL AMENDMENTS.—The table of sections for part II of subchapter H of chapter 1 is amended—

(1) by striking out the third item and inserting in lieu thereof the following:

“Sec. 593. Reserves for losses on loans.”

and

(2) by adding at the end thereof the following:

“Sec. 595. Foreclosure on property securing loans.”

~~(e) REPEAL OF EXEMPTION FROM COMMUNICATIONS AND TRANSPORTATION OF PERSONS TAXES.—Notwithstanding any other provision of law, Federal savings and loan associations shall not be exempt as such from the~~

1 taxes imposed by section 4251 (relating to excise tax on
2 communications) and section 4261 (relating to excise tax
3 on transportation of persons) of the Internal Revenue Code
4 of 1954.

5 (e) *REPEAL OF EXEMPTION FROM CERTAIN EXCISE*
6 *TAXES.*—

7 (1) *AMENDMENT TO HOME OWNERS' LOAN ACT.*—
8 Section 5(h) of the Home Owners' Loan Act, as
9 amended (12 U.S.C. sec. 1464(h)), is amended to read
10 as follows:

11 “(h) *EXEMPTION FROM DISCRIMINATORY STATE AND*
12 *LOCAL TAXATION.*—No State, county, municipal, or local
13 taxing authority shall impose any tax on such associations or
14 their franchise, capital, reserves, surplus, loans, or income
15 greater than that imposed by such authority on other similar
16 local mutual or cooperative thrift and home financing institu-
17 tions.”

18 (2) *CERTAIN DOCUMENTARY STAMP TAXES.*—Sec-
19 tion 4382(a)(2) (relating to exemptions from docu-
20 mentary stamp taxes) is amended to read as follows:

21 “(2) *DOMESTIC BUILDING AND LOAN ASSOCIA-*
22 *TIONS AND MUTUAL DITCH OR IRRIGATION COM-*
23 *PANIES.*—Shares or certificates of stock issued by domes-
24 tic building and loan associations and cooperative banks,

1 *to the extent such shares or certificates represent deposits*
 2 *or withdrawable accounts; or shares or certificates of*
 3 *stock and certificates of indebtedness issued by mutual*
 4 *ditch or irrigation companies.”*

5 *(f) DEDUCTION FOR DIVIDENDS OR INTEREST PAID*
 6 *ON DEPOSITS.—Section 591 (relating to deduction for divi-*
 7 *dends paid on deposits) is amended—*

8 *(1) by striking out “and domestic building and*
 9 *loan associations” and inserting in lieu thereof the follow-*
 10 *ing: “domestic building and loan associations, and other*
 11 *savings institutions chartered and supervised as savings*
 12 *and loan or similar associations under Federal or State*
 13 *law”; and*

14 *(2) by inserting after “dividends” the following:*
 15 *“or interest”.*

16 ~~(f)~~ *(g) EFFECTIVE DATES.—*

17 *(1) The amendment made by subsection (a) shall*
 18 *apply to taxable years ending after December 31, 1962,*
 19 *except that section 593 (f) of the Internal Revenue*
 20 *Code of 1954 shall apply to distributions after Decem-*
 21 *ber 31, 1962, in taxable years ending after such date.*

22 *(2) The amendment made by subsection (b) shall*

1 apply to transactions described in section 595 (a) of the
2 Internal Revenue Code of 1954 occurring after Decem-
3 ber 31, 1962, in taxable years ending after such date.

4 *(3) The amendment made by subsection (c) shall*
5 *apply to taxable years beginning after the date of the*
6 *enactment of this Act.*

7 ~~(3) Subsection (c) of this section shall apply—~~

8 ~~(A) in the case of the tax imposed by section~~
9 ~~4251 of the Internal Revenue Code of 1954, with~~
10 ~~respect to amounts paid pursuant to bills rendered~~
11 ~~after June 30, 1962; and~~

12 ~~(B) in the case of the tax imposed by section~~
13 ~~4261 of such Code, with respect to transportation~~
14 ~~beginning after June 30, 1962.~~

15 *(4) Subsection (e) of this section shall become effec-*
16 *tive on January 1, 1963, except that—*

17 *(A) in the case of the tax imposed by section*
18 *4251 of the Internal Revenue Code of 1954, such*
19 *subsection shall apply only with respect to amounts*
20 *paid pursuant to bills rendered after December 31,*
21 *1962; and*

22 *(B) in the case of the tax imposed by section*

1 *4261 of such Code, such subsection shall apply only*
 2 *with respect to transportation beginning after De-*
 3 *cember 31, 1962.*

4 **SEC. 97. DISTRIBUTIONS BY FOREIGN TRUSTS.**

5 (a) DEFINITIONS.—

6 (1) INCOME OF FOREIGN TRUST.—Section 643 (a)

7 (6) (relating to modifications taken into account in com-
 8 puting distributable net income) is amended to read as
 9 follows:

10 “(6) INCOME OF FOREIGN TRUST.—In the case of
 11 a foreign trust—

12 “(A) There shall be included the amounts of
 13 gross income from sources without the United States,
 14 reduced by any amounts which would be deductible
 15 in respect of disbursements allocable to such income
 16 but for the provisions of section 265 (1) (relating
 17 to disallowance of certain deductions).

18 “(B) Gross income from sources within the
 19 United States shall be determined without regard
 20 to section 894 (relating to income exempt under
 21 treaty).

22 “(C) Subsection ~~(a)(3)~~ of this section *Para-*
 23 *graph (3)* shall not apply to a foreign trust created
 24 by a United States person. In the case of such a
 25 trust, (i) there shall be included gains from the

1 sale or exchange of capital assets, reduced by losses
 2 from such sales or exchanges to the extent such
 3 losses do not exceed gains from such sales or ex-
 4 changes, and (ii) the deduction under section 1202
 5 (relating to deduction for excess of capital gains
 6 over capital losses) shall not be taken into account.”

7 (2) FOREIGN ESTATES AND TRUSTS.—Section 643
 8 (relating to definitions) is amended by adding at the
 9 end thereof the following new subsection:

10 “(d) FOREIGN TRUSTS CREATED BY UNITED STATES
 11 PERSONS.—For purposes of this part, the term ‘foreign trust
 12 created by a United States person’ means ~~a foreign trust (as~~
 13 ~~defined in section 7701(a)(31)) to which money or prop-~~
 14 ~~erty has been transferred that portion of a foreign trust (as~~
 15 ~~defined in section 7701(a)(31)) attributable to money or~~
 16 ~~property transferred~~ directly or indirectly by a United States
 17 person (as defined in section 7701(a)(30)), or under the
 18 will of a decedent who at the date of his death was a United
 19 States citizen or resident.”

20 (b) ACCUMULATION DISTRIBUTIONS OF FOREIGN
 21 TRUSTS.—

22 (1) Section 665(b) (relating to definitions
 23 applicable to subpart D) is amended by striking out

24 “(b) ACCUMULATION DISTRIBUTION.—For purposes

1 of this subpart,” and inserting in lieu thereof the fol-
2 lowing:

3 “(b) ACCUMULATION DISTRIBUTIONS OF TRUSTS
4 OTHER THAN CERTAIN FOREIGN TRUSTS.—For purposes of
5 this subpart, in the case of a trust (other than a foreign trust
6 created by a United States person),”.

7 (2) Section 665 is amended by redesignating sub-
8 sections (c) and (d) as (d) and (e), respectively,
9 and by inserting after subsection (b) the following
10 new subsection:

11 “(c) ACCUMULATION DISTRIBUTION OF CERTAIN
12 FOREIGN TRUSTS.—For purposes of this subpart, in the case
13 of a foreign trust created by a United States person, the term
14 ‘accumulation distribution’ for any taxable year of the trust
15 means the amount by which the amounts specified in para-
16 graph (2) of section 661 (a) for such taxable year exceed
17 distributable net income, reduced by the amounts specified
18 in paragraph (1) of section 661 (a). For purposes of this
19 subsection, the amount specified in paragraph (2) of section
20 661 (a) shall be determined without regard to section 666.
21 Any amount paid to a United States person which is from
22 a payor who is not a United States person and which is
23 derived directly or indirectly from a foreign trust created by
24 a United States person shall be deemed in the year of pay-
25 ment to have been directly paid by the foreign trust.”

1 (c) ALLOCATION OF ACCUMULATION DISTRIBUTIONS
 2 TO PRECEDING YEARS.—Section 666 (a) (relating to ac-
 3 cumulation distribution allocated to 5 preceding years) is
 4 amended—

5 (1) by striking out “(a) AMOUNT ALLOCATED.—
 6 In the case of a trust” and inserting in lieu thereof the
 7 following:

8 “(a) AMOUNT ALLOCATED.—In the case of a trust
 9 (other than a foreign trust created by a United States
 10 person)”; and

11 (2) by adding at the end thereof the following
 12 new sentence:

13 “In the case of a foreign trust created by a United States
 14 person, this subsection shall apply to the preceding tax-
 15 able years of the trust without regard to any provision of
 16 the preceding sentences which would (but for this sentence)
 17 limit its application to the 5 preceding taxable years.”

18 (d) AMOUNTS TREATED AS RECEIVED IN PRIOR
 19 YEARS.—Section 668 (a) (relating to amounts treated as
 20 received in prior taxable years) is amended by adding at
 21 the end thereof the following new sentence: “Except as
 22 provided in section 669, in the case of a foreign trust created
 23 by a United States person the preceding sentence shall not
 24 apply to any beneficiary who is a United States person.”

25 (e) SPECIAL RULES FOR FOREIGN TRUSTS.—Subpart

1 D of part I of subchapter J of chapter 1 (relating to treat-
2 ment of excess distributions by trusts) is amended by adding
3 at the end thereof the following new section:

4 **“SEC. 669. SPECIAL RULES APPLICABLE TO CERTAIN FOR-**
5 **EIGN TRUSTS.**

6 “(a) **LIMITATION ON TAX.—**

7 “(1) **GENERAL RULE.—**At the election of a bene-
8 ficiary who is a United States person (as defined in
9 section 7701 (a) (30)) and who satisfies the require-
10 ments of subsection (b), the tax attributable to the
11 amounts treated under section 668 (a) as having been
12 received by him from a foreign trust created by a United
13 States person on the last day of a preceding taxable
14 year of the trust shall not be greater than—

15 “(A) the tax determined under the next to the
16 last sentence of section 668 (a), or

17 “(B) the tax determined by multiplying by
18 the number of preceding taxable years of the trust,
19 on the last day of each of which an amount is
20 deemed under section 666 (a) to have been distrib-
21 uted, the average of the increase in tax attributable
22 to recomputing the beneficiary’s gross income for
23 the taxable year and each of his 2 taxable years im-
24 mediately preceding the year of the accumulation
25 distribution by adding to the income of each of such

1 years an amount determined by dividing the amount
2 required to be included in income under section
3 668 (a) by such number of preceding taxable years
4 of the trust. The recomputation for the taxable year
5 shall be made without regard to the inclusion in
6 income required by section 668 (a) of any amount
7 other than pursuant to this paragraph.

8 “(2) EXCEPTIONS.—

9 “(A) When an accumulation distribution is
10 deemed under section 666 (a) to have been distrib-
11 uted on the last day of less than 3 taxable years
12 of the trust, the taxable years of the beneficiary for
13 which a recomputation is made under subsection
14 (a) (1) (B) shall equal the number of years to
15 which section 666 (a) applies, commencing with
16 the most recent taxable year of the beneficiary.

17 “(B) If a beneficiary was not alive on the last
18 day of each preceding taxable year of the trust
19 with respect to which a distribution is deemed made
20 under section 666 (a), paragraph (1) (A) of this
21 subsection shall not apply. In applying paragraph
22 (1) (B) of this subsection, no recomputation shall
23 be made for a beneficiary for a taxable year for
24 which he was not alive; if he has no preceding tax-
25 able year, the recomputation shall be made on the

1 basis of his taxable year without regard to the in-
2 clusion in income required by section 668 (a) of
3 any amount other than pursuant to paragraph
4 (1) (B).

5 “(3) EFFECT OF PRIOR ELECTION.—In comput-
6 ing the limitation on tax under paragraph (1) of this
7 subsection for any beneficiary—

8 “(A) SUBSEQUENT ELECTION UNDER PARA-
9 GRAPH (1)(A).—If an election has been made under
10 paragraph (1) (B) of this subsection, for purposes
11 of a subsequent election under paragraph (1) (A)
12 the income of any year with respect to which an
13 amount is deemed distributed to a beneficiary under
14 section 666 (a) shall include amounts previously
15 deemed distributed to such beneficiary for such
16 year as a result of an accumulation distribution with
17 respect to which an election under paragraph (1)
18 (B) was made.

19 “(B) SUBSEQUENT ELECTION UNDER PARA-
20 GRAPH (1)(B).—If with respect to an accumulation
21 distribution an election has been made under either
22 paragraph (1) (A) or paragraph (1) (B) of this
23 subsection, or the next to the last sentence of section
24 668 (a) has applied, for purposes of a subsequent
25 election under paragraph (1) (B) the number of

preceding taxable years of the trust with respect to which an amount is deemed distributed to a beneficiary under section 666 (a) shall be determined without regard to any such year with respect to which an amount was previously deemed distributed to such beneficiary.

“(b) INFORMATION REQUIREMENT.—The election of a beneficiary to apply the limitations on tax provided in subsection (a) of this section shall not be effective unless the beneficiary at the time of making the election supplies such information with respect to the operation and accounts of the trust, for each taxable year on the last day of which an amount is deemed distributed under section 666 (a), as the Secretary or his delegate may by regulations prescribe.”

(f) INFORMATION RETURNS WITH RESPECT TO FOREIGN TRUSTS.—Subpart B of part III of subchapter A of chapter 61 (relating to information concerning transactions with other persons) is amended by adding at the end thereof the following new section:

“SEC. 6047. RETURNS AS TO CREATION OF OR TRANSFERS TO CERTAIN FOREIGN TRUSTS.

“(a) GENERAL RULE.—On or before the 90th day after—

“(1) the creation of any foreign trust by a United States person, or

1 “(2) the transfer of any money or property to a
2 foreign trust by a United States person,
3 the grantor in the case of an inter vivos trust, the fiduciary
4 of an estate in the case of a testamentary trust, or the trans-
5 feror, as the case may be, shall make a return in compliance
6 with the provisions of subsection (b).

7 “(b) FORM AND CONTENTS OF RETURNS.—The re-
8 turns required by subsection (a) shall be in such form and
9 shall set forth, in respect of the foreign trust, such informa-
10 tion as the Secretary or his delegate prescribes by regulation
11 as necessary for carrying out the provisions of the income
12 tax laws.

13 “(c) CROSS REFERENCES.—

 “(1) For provisions relating to penalties for violations
 of this section, see sections 6677 and 7203.

 “(2) For definition of the term ‘foreign trust created
 by a United States person’, see section 643(d).”

14 “(g) FAILURE TO FILE INFORMATION RETURNS.—
15 Subchapter B of chapter 68 (relating to assessable penalties)
16 is amended by adding at the end thereof the following new
17 section:

18 “SEC. 6677. FAILURE TO FILE INFORMATION RETURNS
19 WITH RESPECT TO CERTAIN FOREIGN
20 TRUSTS.

21 “(a) CIVIL PENALTY.—In addition to any criminal
22 penalty provided by law, any person required to file a return

1 under section 6047 who fails to file such return at the time
 2 provided in such section, or who files a return which does not
 3 show the information required pursuant to such section, shall
 4 pay a penalty equal to 5 percent of the amount transferred
 5 to a trust, but not more than \$1,000, unless it is shown that
 6 such failure is due to reasonable cause.

7 “(b) DEFICIENCY PROCEDURES NOT TO APPLY.—
 8 Subchapter B of chapter 63 (relating to deficiency proce-
 9 dures for income, estate, and gift taxes) shall not apply in
 10 respect of the assessment or collection of any penalty
 11 imposed by subsection (a).”

12 (h) UNITED STATES PERSON DEFINED.—Section
 13 7701 (a) is amended by adding at the end thereof the
 14 following new paragraphs:

15 “(30) UNITED STATES PERSON.—The term
 16 ‘United States person’ means—

17 “(A) a citizen or resident of the United States,

18 “(B) a domestic partnership,

19 “(C) a domestic corporation, and

20 “(D) any estate or trust (other than a foreign
 21 estate or foreign trust, within the meaning of sec-
 22 tion 7701 (a) (31)).

23 “(31) FOREIGN ESTATE OR TRUST.—The terms
 24 ‘foreign estate’ and ‘foreign trust’ mean an estate or
 25 trust, as the case may be, the income of which from

1 sources without the United States is not includible in
2 gross income under subtitle A.”

3 (i) TECHNICAL AMENDMENTS.—

4 (1) The table of sections for subpart D of sub-
5 chapter J of chapter 1 (relating to treatment of excess
6 distributions by trusts) is amended by adding at the end
7 thereof

“Sec. 669. Special rules applicable to certain foreign trusts.”

8 (2) The table of sections for subpart B of part III
9 of subchapter A of chapter 61 (relating to information
10 concerning transactions with other persons) is amended
11 by adding at the end thereof

“Sec. 6047. Returns as to creation of or transfers to certain
foreign trusts.”

12 (3) The table of sections for subchapter B of
13 chapter 68 (relating to assessable penalties) is amended
14 by adding at the end thereof

“Sec. 6677. Failure to file information returns with respect
to certain foreign trusts.”

15 (j) EFFECTIVE DATE.—The amendments made by this
16 section (other than by subsections (f), (g), and (h)) shall
17 apply with respect to distributions made ~~in taxable years of~~
18 ~~trusts beginning~~ after the date of the enactment of this Act.

1 **SEC. 40 8. MUTUAL INSURANCE COMPANIES (OTHER**
 2 **THAN LIFE, MARINE, AND CERTAIN FIRE**
 3 **OR FLOOD INSURANCE COMPANIES), ETC.**

4 (a) IMPOSITION OF TAX.—So much of part II of sub-
 5 chapter L (relating to mutual insurance companies, other
 6 than life or marine or fire insurance companies issuing per-
 7 petual policies) of chapter 1 as precedes section 822 is
 8 amended to read as follows:

9 **“PART II—MUTUAL INSURANCE COMPANIES**
 10 **(OTHER THAN LIFE AND CERTAIN**
 11 **MARINE INSURANCE COMPANIES**
 12 **AND OTHER THAN FIRE OR FLOOD**
 13 **INSURANCE COMPANIES WHICH OP-**
 14 **ERATE ON BASIS OF PERPETUAL**
 15 **POLICIES OR PREMIUM DEPOSITS)**

“Sec. 821. Tax on mutual insurance companies to which
 part II applies.

“Sec. 822. Determination of taxable investment income.

“Sec. 823. Determination of statutory underwriting income
 or loss.

“Sec. 824. Adjustments to provide protection against losses.

“Sec. 825. Unused loss deduction.

“Sec. 826. Election by reciprocal.

1 **"SEC. 821. TAX ON MUTUAL INSURANCE COMPANIES TO**
 2 **WHICH PART II APPLIES.**

3 “(a) IMPOSITION OF TAX.—A tax is hereby imposed
 4 for each taxable year beginning after December 31, 1962,
 5 on the mutual insurance company taxable income of every
 6 mutual insurance company (other than a life insurance com-
 7 pany and other than a ~~fire~~ *fire, flood*, or marine insurance
 8 company subject to the tax imposed by section 831). Such
 9 tax shall consist of—

10 ~~“(1) NORMAL TAX.—A normal tax of 25 percent~~
 11 ~~of the mutual insurance company taxable income, or~~
 12 ~~50 percent of the amount by which such taxable income~~
 13 ~~exceeds \$6,000, whichever is the lesser; plus~~

14 “(1) NORMAL TAX.—

15 “(A) TAXABLE YEARS BEGINNING BEFORE
 16 *JULY 1, 1963.—In the case of taxable years beginning*
 17 *before July 1, 1963, a normal tax of 30 percent of*
 18 *the mutual insurance company taxable income, or 60*
 19 *percent of the amount by which such taxable income*
 20 *exceeds \$6,000, whichever is the lesser;*

21 “(B) TAXABLE YEARS BEGINNING AFTER
 22 *JUNE 30, 1963.—In the case of taxable years begin-*
 23 *ning after June 30, 1963, a normal tax of 25 per-*
 24 *cent of the mutual insurance company taxable*
 25 *income, or 50 percent of the amount by which such*

1 *taxable income exceeds \$6,000, whichever is the*
 2 *lesser; plus*

3 “(2) SURTAX.—A surtax of 22 percent of the
 4 mutual insurance company taxable income (computed
 5 without regard to the deduction provided in section 242
 6 for partially tax-exempt interest) in excess of \$25,000.

7 “(b) MUTUAL INSURANCE COMPANY TAXABLE IN-
 8 COME DEFINED.—For purposes of this part, the term ‘mutual
 9 insurance company taxable income’ means, with respect to
 10 any taxable year, the amount by which—

11 “(1) the sum of—

12 “(A) the taxable investment income (as de-
 13 fined in section 822 (a) (1)),

14 “(B) the statutory underwriting income (as
 15 defined in section 823 (a) (1)), and

16 “(C) the amounts required by section 824 (d)
 17 to be subtracted from the protection against loss
 18 account, exceeds

19 “(2) the sum of—

20 “(A) the investment loss (as defined in sec-
 21 tion 822 (a) (2)),

22 “(B) the statutory underwriting loss (as de-
 23 fined in section 823 (a) (2)), and

24 “(C) the unused loss deduction provided by
 25 section 825 (a) .

1 “(c) ALTERNATIVE TAX FOR CERTAIN SMALL COM-
2 PANIES.—

3 “(1) IMPOSITION OF TAX.—In the case of taxable
4 years beginning after December 31, 1962, there is here-
5 by imposed for each taxable year on the income of each
6 mutual insurance company to which this subsection
7 applies a tax (which shall be in lieu of the tax imposed
8 by subsection (a)) computed as follows:

9 “~~(A)~~ NORMAL TAX.—A normal tax of 25
10 percent of the taxable investment income, or 50
11 percent of the amount by which such taxable in-
12 come exceeds \$3,000, whichever is the lesser; plus

13 “(A) NORMAL TAX.—

14 “(i) TAXABLE YEARS BEGINNING BEFORE
15 JULY 1, 1963.—In the case of taxable years be-
16 ginning before July 1, 1963, a normal tax of
17 30 percent of the taxable investment income, or
18 60 percent of the amount by which such taxable
19 income exceeds \$3,000, whichever is the lesser;

20 “(ii) TAXABLE YEARS BEGINNING AFTER
21 JUNE 30, 1963.—In the case of taxable years be-
22 ginning after June 30, 1963, a normal tax of
23 25 percent of the taxable investment income, or
24 50 percent of the amount by which such taxable

1 *income exceeds \$3,000, whichever is the lesser;*

2 *plus*

3 “(B) SURTAX.—A surtax of 22 percent of the
4 taxable investment income (computed without re-
5 gard to the deduction provided in section 242 for
6 partially tax-exempt interest) in excess of \$25,000.

7 “(2) GROSS AMOUNT RECEIVED, OVER ~~\$75,000~~
8 *\$150,000* BUT LESS THAN ~~\$125,000~~ *\$250,000*.—If the gross
9 amount received during the taxable year from the items
10 described in section 822 (b) (other than paragraph
11 (1) (D) thereof) and premiums (including deposits
12 and assessments) is over ~~\$75,000~~ *\$150,000* but less than
13 ~~\$125,000~~ *\$250,000*, the tax imposed by paragraph (1)
14 shall be reduced to an amount which bears the same
15 proportion to the amount of the tax determined under
16 paragraph (1) as the excess over ~~\$75,000~~ *\$150,000* of
17 such gross amount received bears to ~~\$50,000~~ *\$100,000*.

18 “(3) COMPANIES TO WHICH SUBSECTION AP-
19 PLIES.—

20 “(A) IN GENERAL.—Except as provided in
21 subparagraph (B), this subsection shall apply to
22 every mutual insurance company (other than a life
23 insurance company and other than a ~~fire~~ *fire, flood,*
24 or marine insurance company subject to the tax im-

posed by section 831) which received during the taxable year from the items described in section 822 (b) (other than paragraph (1) (D) thereof) and premiums (including deposits and assessments) a gross amount in excess of ~~\$75,000~~ \$150,000 but not in excess of ~~\$300,000~~ \$600,000.

“(B) EXCEPTIONS.—This subsection shall not apply to a mutual insurance company for the taxable year if—

“(i) there is in effect an election by such company made under subsection (d) to be taxable under subsection (a) ; or

“(ii) there is any amount in the protection against loss account at the beginning of the taxable year.

“(d) ELECTION TO INCLUDE STATUTORY UNDERWRITING INCOME OR LOSS.—

“(1) IN GENERAL.—Any mutual insurance company which is subject to the tax imposed by subsection (c) may elect, in such manner and at such time as the Secretary or his delegate may by regulations prescribe, to be subject to the tax imposed by subsection (a) .

“(2) EFFECT OF ELECTION.—If an election is made under paragraph (1), the electing company shall be subject to the tax imposed by subsection (a) (and shall

not be subject to the tax imposed by subsection (c))
 for the first taxable year for which such election is made
 and for all taxable years thereafter unless the Secretary
 or his delegate consents to a revocation of such election.

“(e) NO UNITED STATES INSURANCE BUSINESS.—

Foreign mutual insurance companies (other than a life
 insurance company and other than a fire fire, flood, or marine
 insurance company subject to the tax imposed by section
 831) not carrying on an insurance business within the
 United States shall not be subject to this part but shall be
 taxable as other foreign corporations.

“(f) SPECIAL TRANSITIONAL UNDERWRITING LOSS.—

“(1) COMPANIES TO WHICH SUBSECTION AP-
 PLIES.—*This subsection shall apply to every mutual
 insurance company which has been subject to the tax
 imposed by this section (as in effect before the enactment
 of this subsection) for the 6 taxable years immediately
 preceding January 1, 1963, and has incurred an under-
 writing loss for at least 5 of such 6 taxable years.*

“(2) REDUCTION OF MUTUAL INSURANCE COM-
 PANY TAXABLE INCOME.—*For purposes of this part,
 the mutual insurance company taxable income for the
 taxable year with respect to a company described in par-
 agraph (1) shall be the mutual insurance company tax-*

1 *able income for the taxable year (determined without*
 2 *regard to this subsection) reduced by the amount by*
 3 *which—*

4 *“(A) the sum of the underwriting losses of such*
 5 *company for the 6 taxable years prior to January*
 6 *1, 1963, reduced by the underwriting gain for such*
 7 *years, exceeds*

8 *“(B) the total amount by which the mutual in-*
 9 *surance company taxable income was reduced by*
 10 *reason of this subsection for prior taxable years.*

11 *“(3) For purposes of this subsection—*

12 *“(A) The term ‘underwriting loss’ means*
 13 *statutory underwriting loss, computed without any*
 14 *deduction under section 824(a).*

15 *“(B) The term ‘underwriting gain’ means*
 16 *statutory underwriting income, computed without*
 17 *any deduction under section 823(c) or any*
 18 *deduction under section 824(a).*

19 *“(4) YEARS TO WHICH SUBSECTION APPLIES.—*

20 *This subsection shall apply with respect to any taxable*
 21 *year beginning after December 31, 1962, and before*
 22 *January 1, 1968, for which the taxpayer is subject to the*
 23 *tax imposed by subsection (a).*

~~(f)~~ (g) CROSS REFERENCES.—

“(1) For exemption from tax of certain mutual insurance companies, see section 501(c)(15).

“(2) For alternative tax in case of capital gains, see section 1201(a).”

(b) TAXABLE INVESTMENT INCOME.—

(1) IN GENERAL.—Section 822 (relating to determination of mutual insurance company taxable income) is amended by striking out the heading and subsection (a) and inserting in lieu thereof the following:

“SEC. 822. DETERMINATION OF TAXABLE INVESTMENT INCOME.

“(a) DEFINITIONS.—For purposes of this part—

“(1) The term ‘taxable investment income’ means the gross investment income, minus the deductions provided in subsection (c).

“(2) The term ‘investment loss’ means the amount by which the deductions provided in subsection (c) exceed the gross investment income.”

(2) CONFORMING AMENDMENTS.—Subsections (c) and (e) of section 822 are each amended by striking out “mutual insurance company taxable income” each place it appears and inserting in lieu thereof “taxable investment income”.

(3) DIVIDENDS RECEIVED DEDUCTION.—Section

1 822 (c) (7) (relating to special deductions) is amended
 2 by adding at the end thereof the following new sentence:
 3 “In applying section 246 (b) (relating to limitation on
 4 aggregate amount of deductions for dividends received)
 5 for purposes of this paragraph, the reference in such
 6 section to ‘taxable income’ shall be treated as a reference
 7 to ‘taxable investment income’.”

8 (4) REDESIGNATION OF SECTION 823.—Part II of
 9 subchapter L of chapter 1 is amended by striking out
 10 “SEC. 823. OTHER DEFINITIONS.

11 “‘For purposes of this part—”,
 12 and inserting in lieu thereof (at the end of section 822)
 13 the following:

14 “(f) DEFINITIONS.—For purposes of this part—”.

15 (c) STATUTORY UNDERWRITING INCOME OR LOSS.—
 16 Part II of subchapter L of chapter 1 is amended by adding
 17 after section 822 (f) (as redesignated by subsection (b) (4)
 18 of this section) the following new sections:

19 “SEC. 823. DETERMINATION OF STATUTORY UNDERWRIT-
 20 ING INCOME OR LOSS.

21 “(a) IN GENERAL.—For purposes of this part—

22 “(1) The term ‘statutory underwriting income’
 23 means the amount by which—

24 “(A) the gross income which would be taken

1 into account in computing taxable income under
 2 section 832 if the taxpayer were subject to the tax
 3 imposed by section 831, reduced by the gross in-
 4 vestment income, exceeds

5 “(B) the sum of (i) the deductions which
 6 would be taken into account in computing taxable
 7 income if the taxpayer were subject to the tax im-
 8 posed by section 831, reduced by the deductions
 9 provided in section 822 (c), plus (ii) the deductions
 10 provided in subsection (c) and section 824 (a).

11 “(2) The term ‘statutory underwriting loss’ means
 12 the excess of the amount referred to in paragraph
 13 (1) (B) over the amount referred to in paragraph
 14 (1) (A).

15 “(b) MODIFICATIONS.—In applying subsection (a)—

16 “(1) NET OPERATING LOSS DEDUCTION.—The de-
 17 duction for net operating losses provided in section 172
 18 shall not be allowed.

19 “(2) INTERINSURERS.—In the case of a mutual in-
 20 surance company which is an interinsurer or reciprocal
 21 underwriter—

22 “(A) there shall be allowed as a deduction the
 23 increase for the taxable year in savings credited to
 24 subscriber accounts, or

1 “(B) there shall be included as an item of
2 gross income the decrease for the taxable year in
3 savings credited to subscriber accounts.

4 For purposes of the preceding sentence, the term ‘sav-
5 ings credited to subscriber accounts’ means such portion
6 of the surplus as is credited to the individual accounts
7 of subscribers before the 16th day of the third month
8 following the close of the taxable year, but only if the
9 company would be obligated to pay such amount
10 promptly to such subscriber if he terminated his con-
11 tract at the close of the company’s taxable year. For
12 purposes of determining his taxable income, the sub-
13 scriber shall treat any such savings credited to his ac-
14 count as a dividend paid or declared.

15 “(c) SPECIAL DEDUCTION FOR SMALL COMPANY
16 HAVING GROSS AMOUNT OF LESS THAN ~~\$900,000~~
17 \$1,200,000.—

18 “(1) IN GENERAL.—If the gross amount received
19 during the taxable year by a taxpayer subject to the tax
20 imposed by section 821 (a) from the items described
21 in section 822 (b) (other than paragraph (1) (D)
22 thereof) and premiums (including deposits and assess-
23 ments) does not equal or exceed ~~\$900,000~~ \$1,200,000,
24 then in determining the statutory underwriting income
25 or loss for the taxable year there shall be allowed an

additional deduction of \$6,000; except that if such gross amount exceeds ~~\$300,000~~ \$600,000, such additional deduction shall be equal to 1 percent of the amount by which ~~\$900,000~~ \$1,200,000 exceeds such gross amount.

“(2) LIMITATION.—The amount of the deduction allowed under paragraph (1) shall not exceed the statutory underwriting income for the taxable year, computed without regard to any deduction under this subsection or section 824 (a).

**“SEC. 824. ADJUSTMENTS TO PROVIDE PROTECTION
AGAINST LOSSES.**

“(a) ALLOWANCE OF DEDUCTION.—

“(1) IN GENERAL.—In determining the statutory underwriting income or loss for any taxable year there shall be allowed as a deduction the sum of—

“(A) an amount equal to 1 percent of the losses incurred during the taxable year (as determined under section 832 (b) (5)), plus

“(B) an amount equal to 25 percent of the underwriting gain for the taxable year, plus

“(C) if the concentrated windstorm, etc., premium percentage for the taxable year exceeds ~~50~~ 40 percent, an amount determined by applying so much of such percentage as exceeds ~~50~~ 40 percent to the underwriting gain for the taxable year.

1 For purposes of this paragraph, the term ‘under-
 2 writing gain’ means statutory underwriting income, com-
 3 puted without any deduction under this subsection.

4 “(2) SPECIAL RULE FOR COMPANIES HAVING CON-
 5 CENTRATED WINDSTORM, ETC., RISKS.—For purposes
 6 of paragraph (1) (C), the term ‘concentrated wind-
 7 storm, etc., premium percentage’ means, with respect to
 8 any taxable year, the percentage obtained by dividing—

9 “(A) the amount of the premiums earned
 10 on insurance contracts during the taxable year (as
 11 defined in section 832 (b) (4)), to the extent at-
 12 tributable to insuring against losses arising in any
 13 ~~one State arising, either in any one State or within~~
 14 *200 miles of any fixed point selected by the taxpayer,*
 15 from windstorm, hail, flood, earthquake, or similar
 16 hazards, by

17 “(B) the amount of the premiums earned
 18 on insurance contracts during the taxable year (as
 19 so defined).

20 “(b) PROTECTION AGAINST LOSS ACCOUNT.—Each
 21 insurance company subject to the tax imposed by section
 22 821 (a) for any taxable year shall, for purposes of this part,
 23 establish and maintain a protection against loss account.

24 “(c) ADDITIONS TO ACCOUNT.—There shall be added
 25 to the protection against loss account for each taxable year

1 an amount equal to the amount allowable as a deduction for
 2 the taxable year under subsection (a) (1).

3 “(d) SUBTRACTIONS.—

4 “(1) ANNUAL SUBTRACTIONS.—After applying
 5 subsection (c), there shall be subtracted for the taxable
 6 year from the protection against loss account—

7 ~~“(A) first, an amount equal to the excess of~~
 8 ~~the statutory underwriting loss for the taxable year~~
 9 ~~over the underwriting loss (as defined in paragraph~~
 10 ~~(6)) for the taxable year,~~

11 *“(A) first, an amount equal to the excess (if*
 12 *any) of the deduction allowed under subsection (a)*
 13 *for the taxable year over the underwriting gain*
 14 *(within the meaning of subsection (a)(1)) for the*
 15 *taxable year,*

16 “(B) then, the amount (if any) by which—

17 “(i) the sum of the investment loss for
 18 such year and the ~~underwriting loss statutory~~
 19 ~~underwriting loss (reduced by the amount re-~~
 20 ~~ferred to in subparagraph (A)) for such year,~~
 21 exceeds

22 “(ii) the sum of the statutory underwrit-
 23 ing income for such taxable year and the taxable
 24 investment income for such taxable year,

25 “(C) next (in the order in which the losses

1 occurred), amounts equal to the unused loss carry-
2 overs to such year,

3 “(D) next, any amount remaining which was
4 added to the account for the fifth preceding taxable
5 year, minus one-half of the amount remaining in the
6 account for such taxable year which was added
7 by reason of subsection (a) (1) (B), and

8 “(E) finally, the amount by which the total
9 amount in the account exceeds whichever of the
10 following is the greater:

11 “(i) 10 percent of premiums earned on in-
12 surance contracts during the taxable year (as
13 defined in section 832 (b) (4)) less dividends
14 to policyholders (as defined in section
15 832 (c) (11)), or

16 “(ii) the total amount in the account at
17 the close of the preceding taxable year.

18 “(2) RULES FOR CEILING ON PROTECTION
19 AGAINST LOSS ACCOUNT.—For purposes of paragraph
20 (1) (E), the total amount in the account shall be
21 determined—

22 “(A) after the application of this section with-
23 out regard to paragraph (1) (E), and

24 “(B) without taking into consideration
25 amounts remaining in the account which were

1 added, with respect to all taxable years, by reason
2 of subsection (a) (1) (C).

3 “(3) PRIORITIES.—The amounts required to be
4 subtracted from the protection against loss account—

5 “(A) under subparagraphs (A), (B), and
6 (C) of paragraph (1) shall be subtracted—

7 “(i) first (on a first-in, first-out, basis)
8 from amounts in the account with respect to
9 the five preceding taxable years and the taxable
10 year, and

11 “(ii) then from amounts in the account
12 with respect to earlier years,

13 “(B) under subparagraph (E) of paragraph
14 (1) shall be subtracted only from amounts in the
15 account with respect to the taxable year, and

16 “(C) under paragraphs (A), (B), (C), and
17 (E) of paragraph (1) shall, if the amount to be
18 subtracted from the total amounts in the account
19 with respect to any taxable year is less than such
20 total, be subtracted from each of the amounts (re-
21 ferred to in subsection (a) (1)) in the account with
22 respect to such year in the proportion which each
23 bears to such total.

24 “(4) TERMINATION OF TAXABILITY UNDER SEC-
25 TION 821.—If the taxpayer is not subject to tax under

1 section 821 for any taxable year, the entire amount in
 2 the account at the close of the preceding taxable year
 3 shall be subtracted from the account in such preceding
 4 taxable year.

5 “(5) ELECTION TO SUBTRACT AMOUNT FROM
 6 ACCOUNT.—

7 “(A) A taxpayer may elect for any taxable
 8 year for which it is subject to tax under section
 9 821 (a) to subtract from its protection against loss
 10 account any amount which, but for the application of
 11 this subparagraph, would be in such account as of
 12 the close of such taxable year.

13 “(B) The election provided by subparagraph
 14 (A) for any taxable year shall be made (in such
 15 manner and in such form as the Secretary or his
 16 delegate may by regulations prescribe) after the
 17 close of such taxable year and not later than the time
 18 prescribed by law for filing the return (including
 19 extensions thereof) for the taxable year following
 20 such taxable year. Such an election, once made,
 21 may not be revoked.

22 “~~(6)~~ UNDERWRITING LOSS DEFINED.—For pur-
 23 poses of paragraph ~~(1)~~, the term ‘underwriting loss’
 24 means the amount by which—

25 “~~(A)~~ the deductions which would be taken

1 into account in computing taxable income under sec-
 2 tion 832 if the taxpayer were subject to the tax im-
 3 posed by section 831, reduced by the sum of (i)
 4 the deductions provided in section 822(e), and (ii)
 5 the deduction for dividends to policyholders provided
 6 by section 832(e) (11); exceeds

7 “(B) the amount referred to in section 823
 8 (a) (1) (A).

9 **“SEC. 825. UNUSED LOSS DEDUCTION.**

10 “(a) **AMOUNT OF DEDUCTION.**—For purposes of this
 11 part, the unused loss deduction for the taxable year shall be
 12 an amount equal to the unused loss carryovers or carrybacks
 13 to the taxable year.

14 “(b) **UNUSED LOSS DEFINED.**—For purposes of this
 15 part, the term ‘unused loss’ means, with respect to any tax-
 16 able year, the amount (if any) by which—

17 “(1) the sum of the statutory underwriting loss
 18 and the investment loss, exceeds

19 “(2) the sum of—

20 “(A) the taxable investment income,

21 “(B) the statutory underwriting income, and

22 “(C) the amounts required by section 824 (d)
 23 to be subtracted from the protection against loss
 24 account.

25 “(c) **LOSS YEAR DEFINED.**—For purposes of this part

1 the term 'loss year' means, with respect to any company
2 subject to the tax imposed by section 821 (a), any tax-
3 able year in which the unused loss (as defined in subsection
4 (b)) of such taxpayer is more than zero.

5 “(d) YEARS TO WHICH CARRIED.—The unused loss
6 for any loss year shall be—

7 “(1) an unused loss carryback to each of the 3
8 taxable years preceding the loss year, and

9 “(2) an unused loss carryover to each of the 5
10 taxable years following the loss year.

11 “(e) AMOUNT OF CARRYBACKS AND CARRYOVERS.—
12 The entire amount of the unused loss for any loss year shall
13 be carried to the earliest of the taxable years to which such
14 loss may be carried. The portion of such loss which shall
15 be carried to each of the other taxable years shall be the
16 excess (if any) of the amount of such loss over the sum
17 of the offsets (as defined in subsection (f)) for each of the
18 prior taxable years to which such loss may be carried.

19 “(f) OFFSET DEFINED.—For purposes of subsection
20 (e), the term 'offset' means with respect to any taxable year
21 (hereinafter referred to as the 'offset year') —

22 “(1) in the case of an unused loss carryback from
23 the loss year to the offset year, the mutual insurance
24 company taxable income for the offset year; or

25 “(2) in the case of an unused loss carryover from

1 the loss year to the offset year, an amount equal to the
2 sum of—

3 “(A) the amount required to be subtracted
4 from the protection against loss account under sec-
5 tion 824(d)(1)(C) for the offset year, plus

6 “(B) the mutual insurance company taxable
7 income for the offset year.

8 For purposes of paragraphs (1) and (2)(B), the mutual
9 insurance taxable income for the offset year shall be deter-
10 mined without regard to any unused loss carryback or carry-
11 over from the loss year or any taxable year thereafter.

12 “(g) LIMITATIONS.—For purposes of this part, an un-
13 used loss shall not be carried—

14 “(1) to or from any taxable year beginning before
15 January 1, 1963,

16 “(2) to or from any taxable year for which the
17 insurance company is not subject to the tax imposed by
18 section 821(a), nor

19 “(3) to any taxable year if, between the loss year
20 and such taxable year, there is an intervening taxable
21 year for which the insurance company was not subject
22 to the tax imposed by section 821(a).

23 **“SEC. 826. ELECTION BY RECIPROCAL.**

24 “(a) IN GENERAL.—Except as otherwise provided in
25 this section, any mutual insurance company which is an

1 interinsurer or reciprocal underwriter (hereinafter in this
 2 section referred to as a 'reciprocal') subject to the taxes im-
 3 posed by section 821 (a) may, under regulations prescribed
 4 by the Secretary or his delegate, elect to be subject to the
 5 limitation provided in subsection (b). Such election shall
 6 be effective for the taxable year for which made and for all
 7 succeeding taxable years, and shall not be revoked except
 8 with the consent of the Secretary or his delegate.

9 “(b) LIMITATION.—The deduction for amounts paid or
 10 incurred in the taxable year to the attorney-in-fact by a
 11 reciprocal making the election provided in subsection (a)
 12 shall be limited to, but in no case increased by, the deduc-
 13 tions of the attorney-in-fact allocable, in accordance with
 14 regulations prescribed by the Secretary or his delegate, to the
 15 income received by the attorney-in-fact from the reciprocal.

16 “(c) EXCEPTION.—An election may not be made by a
 17 reciprocal under subsection (a) unless the attorney-in-fact
 18 of such reciprocal—

19 “(1) is subject to the taxes imposed by section 11
 20 (b) and (c) ;

21 “(2) consents in such manner as the Secretary or
 22 his delegate shall prescribe by regulations to make
 23 available such information as may be required during the

period in which the election provided in subsection (a) is in effect, under regulations prescribed by the Secretary or his delegate;

“(3) reports the income received from the reciprocal and the deductions allocable thereto under the same method of accounting under which the reciprocal reports deductions for amounts paid to the attorney-in-fact; and

“(4) files its return on the calendar year basis.

~~“(d) SPECIAL RULE.—For purposes of computing the deduction provided in section 824(a) and the additions to the account provided by section 824(e) with respect to any reciprocal electing to be subject to the limitation provided in subsection (b), such limitation shall not be taken into account.~~

“(d) SPECIAL RULE.—In applying section 824(d)(1)(D), any amount which was added to the protection against loss account by reason of an election under this section shall be treated as having been added by reason of section 824(a)(1)(A).

“(e) CREDIT.—Any reciprocal electing to be subject to the limitation provided in subsection (b) shall be credited with so much of the tax paid by the attorney-in-fact as is

1 attributable, under regulations prescribed by the Secre-
 2 tary or his delegate, to the income received by the attorney-
 3 in-fact from the reciprocal in such taxable year.

4 “(f) SURTAX EXEMPTION DENIED.—Any increase in
 5 taxable income of a reciprocal attributable to the limitation
 6 provided in subsection (b) shall be taxed without regard
 7 to the surtax exemption provided in section 821(a)(2).

8 “(g) ADJUSTMENT FOR REFUND.—If for any taxable
 9 year an attorney-in-fact is allowed a credit or refund for
 10 taxes paid with respect to which a reciprocal was allowed
 11 a credit credit or refund to the reciprocal resulted under
 12 subsection (e), the taxes of such reciprocal for such taxable
 13 year shall be properly adjusted under regulations prescribed
 14 by the Secretary or his delegate.

15 “(h) TAXES OF ATTORNEY-IN-FACT UNAFFECTED.—
 16 Nothing in this section shall increase or decrease the taxes
 17 imposed by this chapter on the income of the attorney-in-
 18 fact.”

19 (d) EXEMPTION FROM TAX.—Section 501(c)(15)
 20 (relating to exemption from tax of certain mutual insurance
 21 companies) is amended by striking out “\$75,000” and in
 22 lieu thereof inserting “\$150,000”.

23 ~~(d)~~ (e) MUTUAL FIRE INSURANCE COMPANIES OPER-
 24 ATING ON BASIS OF PREMIUM DEPOSITS.—

25 (1) APPLICATION OF SECTION 831(a).—Section

831 (a) (imposing a tax on certain mutual marine and fire insurance companies and on stock insurance companies which are not life insurance companies) is amended to read as follows:

“(a) IMPOSITION OF TAX.—Taxes computed as provided in section 11 shall be imposed for each taxable year or the taxable income of—

“(1) every insurance company (other than a life or mutual insurance company),

“(2) every mutual marine insurance company, and

“(3) every mutual fire or *flood* insurance company—

“(A) exclusively issuing perpetual policies, or

“(B) whose principal business is the issuance of policies for which the premium deposits are the same, regardless of the length of the term for which the policies are written, if the unabsorbed portion of such premium deposits not required for losses, expenses, or establishment of reserves is returned or credited to the policyholder on cancellation or expiration of the policy.”

(2) TREATMENT OF UNABSORBED PREMIUM DEPOSITS.—Section 832 (b) (4) (relating to definition of premiums earned) is amended by adding at the end thereof the following new sentence: “For purposes of

1 this subsection, unearned premiums of mutual fire in-
 2 surance companies described in section 831 (a) (3) (B)
 3 means (with respect to the policies described in section
 4 831 (a) (3) (B)) the amount of unabsorbed premium
 5 deposits which the company would be obligated to re-
 6 turn to its policyholders at the close of the taxable year
 7 if all of its policies were terminated at such time; and
 8 the determination of such amount shall be based on the
 9 schedule of unabsorbed premium deposit returns for each
 10 such company then in effect.”

11 (3) CONFORMING AMENDMENT.—Section 832 (b)
 12 (1) (C) is amended by striking out “section 831 (a),”
 13 and inserting in lieu thereof “section 831 (a) (3) (A),”.

14 (4) ADJUSTMENT OF PREMIUM DEPOSIT.—Section
 15 832 (c) (11) is amended to read as follows:

16 “(11) dividends and similar distributions paid or
 17 declared to policyholders in their capacity as such, ex-
 18 cept in the case of a mutual fire insurance company de-
 19 scribed in section 831 (a) (3) (A). For purposes of
 20 the preceding sentence, the term ‘dividends and similar
 21 distributions’ includes amounts returned or credited to
 22 policyholders on cancellation or expiration of policies
 23 described in section 831 (a) (3) (B). For purposes of
 24 this paragraph, the term ‘paid or declared’ shall be con-
 25 strued according to the method of accounting regularly

employed in keeping the books of the insurance company; and”.

(5) ADDITIONAL ITEM OF INCOME.—Section 832 (b) (1) is amended by striking out “and” at the end of subparagraph (B), by striking out the period at the end of subparagraph (C) and inserting in lieu thereof “, and”, and by adding at the end thereof the following new subparagraph:

“(D) in the case of a mutual fire insurance company described in section 831 (a) (3) (B), an amount equal to 2 percent of the premiums earned on insurance contracts during the taxable year with respect to policies described in section 831 (a) (3) (B) after deduction of premium deposits returned or credited during the same taxable year.”

~~(e)~~ (f) ELECTION OF CERTAIN MUTUAL COMPANIES TO BE TAXED ON TOTAL INCOME.—Section 831 is amended by redesignating subsection (c) as subsection (d), and by inserting after subsection (b) the following new subsection:

“(c) ELECTION FOR MULTIPLE LINE COMPANY TO BE TAXED ON TOTAL INCOME.—

“(1) IN GENERAL.—Any mutual insurance company engaged in writing marine, fire, and casualty insurance which for any 5-year period beginning after December 31, 1941, and ending before January 1, 1962,

was subject to the tax imposed by section 831 (or the tax imposed by corresponding provisions of prior law) may elect, in such manner and at such time as the Secretary or his delegate may by regulations prescribe, to be subject to the tax imposed by section 831, whether or not marine insurance is its predominant source of premium income.

“(2) EFFECT OF ELECTION.—If an election is made under paragraph (1), the electing company shall (in lieu of being subject to the tax imposed by section 821) be subject to the tax imposed by this section for taxable years beginning after December 31, 1961. Such election shall not be revoked except with the consent of the Secretary or his delegate.”

~~(f)~~ (g) TECHNICAL AMENDMENTS, ETC.—

(1) CREDIT FOR FOREIGN TAXES.—Section 841 (relating to credit for foreign taxes) is amended by striking out “and” at the end of paragraph (1), by renumbering paragraph (2) as paragraph (3), and by inserting after paragraph (1) the following new paragraph:

“(2) in the case of the tax imposed by section 821 (a), the mutual insurance company taxable income (as defined in section 821 (b)) ; and in the case of the

1 tax imposed by section 821 (c), the taxable investment
2 income (as defined in section 822 (a)), and”.

3 (2) ADJUSTMENTS TO BASIS FOR DEPRECIATION
4 SUSTAINED.—Section 1016 (a) (3) (relating to adjust-
5 ments to basis for depreciation, etc., sustained) is
6 amended by striking out “and” at the end of subpara-
7 graph (B), by inserting “and” at the end of sub-
8 paragraph (C), and by inserting after subparagraph
9 (C) the following new subparagraph:

10 “(D) since February 28, 1913, during which
11 such property was held by a person subject to tax
12 under part II of subchapter L (or the corresponding
13 provisions of prior income tax laws), to the extent
14 that paragraph (2) does not apply,”.

15 (3) ALTERNATIVE TAX ON CAPITAL GAINS.—
16 Section 1201 (a) (relating to alternative tax on corpo-
17 rations) is amended by striking out “821 (a) (1) or
18 (b),” and inserting in lieu thereof “821 (a) or (c),”.

19 ~~(4) CLERICAL AMENDMENT.~~—The table of parts
20 for subchapter L is amended by striking out the portion
21 referring to part II and inserting in lieu thereof the
22 following:

“Part II. Mutual insurance companies (other than life and
certain marine insurance companies and other
than fire insurance companies which operate
on basis of perpetual policies or premium de-
posits).”

1 **(4) CLERICAL AMENDMENTS.—**

2 (A) *The table of parts for subchapter L is*
 3 *amended by striking out the portion referring to part*
 4 *II and inserting in lieu thereof the following:*

“Part II. Mutual insurance companies (other than life and certain marine insurance companies and other than fire or flood insurance companies which operate on basis of perpetual policies or premium deposits).”

5 (B) *The heading to section 831 is amended to*
 6 *read as follows:*

7 **“SEC. 831. TAX ON INSURANCE COMPANIES (OTHER THAN**
 8 **LIFE OR MUTUAL), MUTUAL MARINE INSURANCE**
 9 **COMPANIES, AND CERTAIN MUTUAL FIRE OR**
 10 **FLOOD INSURANCE COMPANIES.”**

11 (C) *The table of sections for part III of sub-*
 12 *chapter L is amended by striking out the portion*
 13 *referring to section 831 and inserting in lieu*
 14 *thereof the following:*

“Sec. 831. Tax on insurance companies (other than life or mutual), mutual marine insurance companies, and certain mutual fire or flood insurance companies.”

15 ~~(g)~~(h) **EFFECTIVE DATE.**—The amendments made by
 16 this section (other than by subsection ~~(e)~~(f)) shall apply
 17 with respect to taxable years beginning after December 31,
 18 1962.

1 SEC. 49. DOMESTIC CORPORATIONS RECEIVING DIVI-
 2 DENDS FROM FOREIGN CORPORATIONS.

3 ~~(a)~~ ENTIRE AMOUNT OF FOREIGN TAX TO BE TAKEN
 4 INTO ACCOUNT.—

5 ~~(1)~~ DEFINITION OF ACCUMULATED PROFITS.—So
 6 much of paragraph ~~(1)~~ of section 902(c) (relating to
 7 applicable rules for computing credit for corporate stock-
 8 holder in foreign corporation) as precedes the semicolon
 9 is amended to read as follows:

10 “~~(1)~~ The term ‘accumulated profits’, when used in
 11 this section in reference to a foreign corporation, means
 12 the amount of its gains, profits, or income computed
 13 without reduction by the amount of the income, war
 14 profits, and excess profits taxes imposed on or with re-
 15 spect to such profits or income by any foreign country
 16 or any possession of the United States”.

17 ~~(2)~~ CONFORMING AMENDMENTS.—

18 ~~(A)~~ Section 902(a) is amended by striking
 19 out “which the amount of such dividends bears to
 20 the amount of such accumulated profits” and insert-
 21 ing in lieu thereof “which the amount of such
 22 dividends (determined without regard to section
 23 78) bears to the amount of such accumulated profits

1 in excess of such income, war profits, and excess
2 profits taxes ~~(other than those deemed paid)~~”.

3 ~~(B)~~ Section 902~~(b)~~ is amended by striking
4 out “which the amount of such dividends bears to
5 the amount of such accumulated profits” and in-
6 serting in lieu thereof “which the amount of such
7 dividends bears to the amount of such accumulated
8 profits in excess of such income, war profits, and
9 excess profits taxes”.

10 (a) *FOREIGN TAXES DEEMED PAID BY DOMESTIC*
11 *CORPORATIONS.*—Section 902 (relating to credit for
12 corporate stockholder in foreign corporations) is amended
13 to read as follows:

14 “SEC. 902. CREDIT FOR CORPORATE STOCKHOLDER IN FOREIGN
15 CORPORATION.

16 “(a) *TREATMENT OF TAXES PAID BY FOREIGN*
17 *CORPORATION.*—For purposes of this subpart, a domestic
18 corporation which owns at least 10 percent of the voting
19 stock of a foreign corporation from which it receives
20 dividends in any taxable year shall—

21 “(1) to the extent such dividends are paid by such
22 foreign corporation out of accumulated profits (as
23 defined in subsection (c)(1)(A)) of a year for which
24 such foreign corporation is not a less developed country
25 corporation, be deemed to have paid the same proportion

1 of any income, war profits, or excess profits taxes paid
2 or deemed to be paid by such foreign corporation to any
3 foreign country or to any possession of the United
4 States on or with respect to such accumulated profits,
5 which the amount of such dividends (determined with-
6 out regard to section 78) bears to the amount of such
7 accumulated profits in excess of such income, war profits,
8 and excess profits taxes (other than those deemed paid);
9 and

10 “(2) to the extent such dividends are paid by such
11 foreign corporation out of accumulated profits (as defined
12 in subsection (c)(1)(B)) of a year for which such
13 foreign corporation is a less developed country corpora-
14 tion, be deemed to have paid the same proportion of any
15 income, war profits, or excess profits taxes paid or deemed
16 to be paid by such foreign corporation to any foreign
17 country or to any possession of the United States on or
18 with respect to such accumulated profits, which the
19 amount of such dividends bears to the amount of such
20 accumulated profits.

21 “(b) FOREIGN SUBSIDIARY OF FOREIGN CORPORA-
22 TION.—If such foreign corporation owns 50 percent or more
23 of the voting stock of another foreign corporation from which
24 it receives dividends in any taxable year, it shall be deemed to
25 have paid the same proportion of any income, war profits, or

1 *excess profits taxes paid by such other foreign corporation to*
 2 *any foreign country or to any possession of the United States,*
 3 *on or with respect to the accumulated profits of the corpora-*
 4 *tion from which such dividends were paid which—*

5 “(1) for purposes of applying subsection (a)(1),
 6 *the amount of such dividends bears to the amount of the*
 7 *accumulated profits (as defined in subsection (c)(1)*
 8 *(A)) of such other foreign corporation from which such*
 9 *dividends were paid in excess of such income, war profits,*
 10 *and excess profits taxes, or*

11 “(2) for purposes of applying subsection (a)
 12 (2), *the amount of such dividends bears to the amount*
 13 *of the accumulated profits (as defined in subsection*
 14 *(c)(1)(B)) of such other foreign corporation from*
 15 *which such dividends were paid.*

16 “(c) *APPLICABLE RULES.—*

17 “(1) *ACCUMULATED PROFITS DEFINED.—For*
 18 *purposes of this section, the term ‘accumulated profits’*
 19 *means with respect to any foreign corporation—*

20 “(A) for purposes of subsections (a)(1) and
 21 (b)(1), *the amount of its gains, profits, or income*
 22 *computed without reduction by the amount of the*
 23 *income, war profits, and excess profits taxes im-*

1 *posed on or with respect to such profits or income*
2 *by any foreign country or any possession of the*
3 *United States; and*

4 *“(B) for purposes of subsections (a)(2) and*
5 *(b)(2), the amount of its gains, profits, or income*
6 *in excess of the income, war profits, and excess*
7 *profits taxes imposed on or with respect to such*
8 *profits or income.*

9 *The Secretary or his delegate shall have full power*
10 *to determine from the accumulated profits of what year*
11 *or years such dividends were paid, treating dividends*
12 *paid in the first 60 days of any year as having been*
13 *paid from the accumulated profits of the preceding year*
14 *or years (unless to his satisfaction shown otherwise),*
15 *and in other respects treating dividends as having been*
16 *paid from the most recently accumulated gains, profits,*
17 *or earnings.*

18 *“(2) ACCOUNTING PERIODS.—In the case of a*
19 *foreign corporation, the income, war profits, and excess*
20 *profits taxes of which are determined on the basis of an*
21 *accounting period of less than 1 year, the word ‘year’*
22 *as used in this subsection shall be construed to mean such*
23 *accounting period.*

1 “(d) *LESS DEVELOPED COUNTRY CORPORATION*
2 *DEFINED.*—For purposes of this section, the term ‘less de-
3 veloped country corporation’ means—

4 “(1) a foreign corporation which, for its taxable
5 year, is a less developed country corporation within the
6 meaning of section 955(c) (1) or (2), and

7 “(2) a foreign corporation which owns 10 percent
8 or more of the total combined voting power of all classes
9 of stock entitled to vote of a foreign corporation which is
10 a less developed country corporation within the meaning
11 of section 955(c) (1), and—

12 “(A) 80 percent or more of the gross income
13 of which for its taxable year meets the requirement
14 of section 955(c) (1) (A); and

15 “(B) 80 percent or more in value of the assets
16 of which on each day of such year consists of prop-
17 erty described in section 955(c) (1) (B).

18 A foreign corporation which is a less developed country
19 corporation for its first taxable year beginning after December
20 31, 1962, shall, for purposes of this section, be treated as
21 having been a less developed country corporation for each
22 of its taxable years beginning before January 1, 1963.

1 “(e) *CROSS REFERENCES.*—

 “(1) *For inclusion in gross income of an amount equal to taxes deemed paid under subsection (a)(1), see section 78.*

 “(2) *For application of subsections (a) and (b) with respect to taxes deemed paid in a prior taxable year by a United States shareholder with respect to a controlled foreign corporation, see section 960.*

 “(3) *For reduction of credit with respect to dividends paid out of accumulated profits for years for which certain information is not furnished, see section 6038.*”

2 (b) *INCLUSION IN GROSS INCOME OF AMOUNT*
 3 *EQUAL TO TAXES DEEMED PAID.*—Part II of subchapter B
 4 of chapter 1 (relating to items specifically included in gross
 5 income) is amended by adding at the end thereof the fol-
 6 lowing new section:

7 “**SEC. 78. DIVIDENDS RECEIVED FROM CERTAIN FOREIGN**
 8 **CORPORATIONS BY DOMESTIC CORPORATIONS**
 9 **CHOOSING FOREIGN TAX CREDIT.**

10 “If a domestic corporation chooses to have the benefits
 11 of subpart A of part III of subchapter N (relating to foreign
 12 tax credit) for any taxable year, an amount equal to the
 13 taxes deemed to be paid by such corporation under section
 14 ~~902~~ 902(a)(1) (relating to credit for corporate stockholder
 15 in foreign corporation) or under section ~~957(a)~~ 960(a)(1)
 16 (C) (relating to taxes paid by foreign corporation) for such
 17 taxable year shall be treated for purposes of this title (other

1 than section 245) as a dividend received by such domestic
2 corporation from the foreign corporation.”

3 (c) DETERMINATION OF SOURCE OF DIVIDENDS RE-
4 CEIVED FROM CERTAIN FOREIGN CORPORATIONS.—Section
5 861 (a) (2) (B) (relating to dividends from foreign corpo-
6 rations treated as income from sources within the United
7 States) is amended by striking out “to the extent exceeding
8 the amount of the deduction allowable under section 245 in
9 respect of such dividends” and inserting in lieu thereof “to
10 the extent exceeding the amount which is 100/85ths of the
11 amount of the deduction allowable under section 245 in
12 respect of such dividends”.

13 ~~(d) REPEAL OF SECTION 902(d).—Subsection (d)~~
14 ~~(relating to special rules for certain wholly owned foreign~~
15 ~~corporations) is hereby repealed.~~

16 ~~(e)~~ (d) TECHNICAL AMENDMENTS.—

17 (1) The table of sections for part II of subchapter
18 B of chapter 1 is amended by adding at the end thereof
19 the following:

“Sec. 78. Dividends received from *certain* foreign corpora-
tions by domestic corporations choosing foreign
tax credit.”

20 (2) Section 535 (b) (1) and the first sentence of
21 section 545 (b) (1) are each amended by striking out
22 “accrued during the taxable year,” and inserting in lieu

thereof "accrued during the taxable year or deemed to be paid by a domestic corporation under section ~~902~~ 902 (a)(1) or 960(a)(1)(C) for the taxable year,".

(3) Section 901(d) is amended by adding the following new paragraph:

"(4) For reduction of credit for failure of a United States person to furnish certain information with respect to a foreign corporation controlled by him, see section 6038."

~~(4)~~ Section 902 is amended by striking out subsection ~~(e)~~ and inserting in lieu thereof the following:

~~"(d)~~ CROSS REFERENCES.—

"(1) For inclusion in gross income of an amount equal to taxes deemed paid under this section, see section 78.

"(2) For reduction of credit with respect to dividends paid out of accumulated profits for years for which certain information is not furnished, see section 6038."

~~(f)~~ (e) EFFECTIVE DATE.—The amendments made by this section shall apply—

(1) in respect of any distribution received by a domestic corporation after December 31, 1964, and

(2) in respect of any distribution received by a domestic corporation before January 1, 1965, in a taxable year of such corporation beginning after December 31, 1962, but only to the extent that such distribution

1 is made out of the accumulated profits of a foreign
 2 corporation for a taxable year (of such foreign corpora-
 3 tion) beginning after December 31, 1962.

4 For purposes of paragraph (2), a distribution made by a
 5 foreign corporation out of its profits which are attributable
 6 to a distribution received from a foreign subsidiary to which
 7 section 902 (b) applies shall be treated as made out of the
 8 accumulated profits of a foreign corporation for a taxable
 9 year beginning before January 1, 1963, to the extent that
 10 such distribution was paid out of the accumulated profits of
 11 such foreign subsidiary for a taxable year beginning before
 12 January 1, 1963.

13 *SEC. 10. SEPARATE LIMITATION ON FOREIGN TAX CREDIT*
 14 *WITH RESPECT TO CERTAIN INTEREST INCOME.*

15 *(a) LIMITATION ON FOREIGN TAX CREDIT.—Section*
 16 *904 (relating to limitations on foreign tax credit) is amended*
 17 *by redesignating subsection (f) as subsection (g) and by*
 18 *inserting after subsection (e) the following new subsection:*

19 *“(f) APPLICATION OF SECTION IN CASE OF CERTAIN*
 20 *INTEREST INCOME.—*

21 *“(1) IN GENERAL.—The provisions of subsections*
 22 *(a), (c), (d), and (e) of this section shall be applied*
 23 *separately with respect to—*

24 *“(A) the interest income described in paragraph*
 25 *(2), and*

1 “(B) income other than the interest income de-
2 scribed in paragraph (2).

3 “(2) INTEREST INCOME TO WHICH APPLICABLE.—

4 For purposes of this subsection, the interest income de-
5 scribed in this paragraph is interest other than interest—

6 “(A) derived from any transaction which is
7 directly related to the active conduct of a trade or
8 business in a foreign country or a possession of the
9 United States,

10 “(B) derived in the conduct of a banking,
11 financing, or similar business, or

12 “(C) received from a corporation in which the
13 taxpayer owns at least 10 percent of the voting
14 stock.

15 (3) OVERALL LIMITATION NOT TO APPLY.—The
16 limitation provided by subsection (a)(2) shall not ap-
17 ply with respect to the interest income described in para-
18 graph (2). The Secretary or his delegate shall by
19 regulations prescribe the manner of application of sub-
20 section (e) with respect to cases in which the limitation
21 provided by subsection (a)(2) applies with respect
22 to income other than the interest income described in para-
23 graph (2).

24 “(4) TRANSITIONAL RULES FOR CARRYBACKS AND
25 CARRYOVERS.—

“(A) CARRYBACKS TO YEARS PRIOR TO REVENUE ACT OF 1962.—Where, under the provisions of subsection (d), taxes (i) paid or accrued to any foreign country or possession of the United States in any taxable year beginning after the date of the enactment of the Revenue Act of 1962 are deemed (ii) paid or accrued in one or more taxable years beginning on or before the date of enactment of the Revenue Act of 1962, the amount of such taxes deemed paid or accrued shall be determined without regard to the provisions of this subsection. To the extent the taxes paid or accrued to a foreign country or possession of the United States in any taxable year described in clause (i) are not, with the application of the preceding sentence, deemed paid or accrued in any taxable year described in clause (ii), such taxes shall, for purposes of applying subsection (d), be deemed paid or accrued in a taxable year beginning after the date of the enactment of the Revenue Act of 1962, with respect to interest income described in paragraph (2), and with respect to income other than interest income described in paragraph (2), in the same ratios as the amount of such taxes paid or accrued with respect to interest income described in paragraph (2), and the

1 *amount of such taxes paid or accrued with respect to*
2 *income other than interest income described in*
3 *paragraph (2), respectively, bear to the total*
4 *amount of such taxes paid or accrued to such foreign*
5 *country or possession of the United States.*

6 “(B) CARRYOVERS TO YEARS AFTER REVE-
7 *NUE ACT OF 1962.—Where, under the provisions of*
8 *subsection (d), taxes (i) paid or accrued to any for-*
9 *foreign country or possession of the United States in*
10 *any taxable year beginning on or before the date*
11 *of the enactment of the Revenue Act of 1962 are*
12 *deemed (ii) paid or accrued in one or more taxable*
13 *years beginning after the date of the enactment of*
14 *the Revenue Act of 1962, the amount of such taxes*
15 *deemed paid or accrued in any year described in*
16 *clause (ii) shall, with respect to interest income*
17 *described in paragraph (2), be an amount which*
18 *bears the same ratio to the amount of such taxes*
19 *deemed paid or accrued as the amount of the taxes*
20 *paid or accrued to such foreign country or possession*
21 *for such year with respect to interest income de-*
22 *scribed in paragraph (2) bears to the total amount*
23 *of the taxes paid or accrued to such foreign country*
24 *or possession for such year; and the amount of such*
25 *taxes deemed paid or accrued in any year described*

1 in clause (ii) with respect to income other than
 2 interest income described in paragraph (2) shall
 3 be an amount which bears the same ratio to the
 4 amount of such taxes deemed paid or accrued for
 5 such year as the amount of taxes paid or accrued
 6 to such foreign country or possession for such year
 7 with respect to income other than interest income
 8 described in paragraph (2) bears to the total
 9 amount of the taxes paid or accrued to such for-
 10 eign country or possession for such year.”

11 (b) *EFFECTIVE DATE.*—The amendments made by
 12 subsection (a) shall apply with respect to taxable years
 13 beginning after the date of the enactment of this Act, but
 14 only with respect to interest resulting from transactions con-
 15 summated after April 2, 1962.

16 **SEC. 11. EARNED INCOME FROM SOURCES WITHOUT**
 17 **THE UNITED STATES.**

18 (a) *LIMITATION ON AMOUNT AND TYPE OF INCOME*
 19 *EXCLUDED.*—Section 911 (relating to earned income from
 20 sources without the United States) is amended to read as
 21 follows:

22 **“SEC. 911. EARNED INCOME FROM SOURCES WITHOUT**
 23 **THE UNITED STATES.**

24 “(a) *GENERAL RULE.*—The following items shall not
 25 be included in gross income and shall be exempt from taxa-
 26 tion under this subtitle:

1 “(1) BONA FIDE RESIDENT OF FOREIGN COUN-
2 TRY.—In the case of an individual citizen of the United
3 States who establishes to the satisfaction of the Secre-
4 tary or his delegate that he has been a bona fide resident
5 of a foreign country or countries for an uninterrupted
6 period which includes an entire taxable year, amounts
7 received from sources without the United States (except
8 amounts paid by the United States or any agency there-
9 of) which constitute earned income attributable to serv-
10 ices performed during such uninterrupted period. The
11 amount excluded under this paragraph for any taxable
12 year shall be computed by applying the special rules
13 contained in subsection (c).

14 “(2) PRESENCE IN FOREIGN COUNTRY FOR 17
15 MONTHS.—In the case of an individual citizen of the
16 United States who during any period of 18 consecutive
17 months is present in a foreign country or countries dur-
18 ing at least 510 full days in such period, amounts re-
19 ceived from sources without the United States (except
20 amounts paid by the United States or any agency
21 thereof) which constitute earned income attributable to
22 services performed during such 18-month period. The
23 amount excluded under this paragraph for any taxable
24 year shall be computed by applying the special rules
25 contained in subsection (c).

1 An individual shall not be allowed, as a deduction from his
2 gross income, any deductions (other than those allowed by
3 section 151, relating to personal exemptions) properly allo-
4 cable to or chargeable against amounts excluded from gross
5 income under this subsection.

6 “(b) DEFINITION OF EARNED INCOME.—For purposes
7 of this section, the term ‘earned income’ means wages, sal-
8 aries, or professional fees, and other amounts received as
9 compensation for personal services actually rendered, but
10 does not include that part of the compensation derived by
11 the taxpayer for personal services rendered by him to a
12 corporation which represents a distribution of earnings or
13 profits rather than a reasonable allowance as compensation
14 for the personal services actually rendered. In the case of
15 a taxpayer engaged in a trade or business in which both
16 personal services and capital are material income-producing
17 factors, under regulations prescribed by the Secretary or his
18 delegate, a reasonable allowance as compensation for the
19 personal services rendered by the taxpayer, not in excess of
20 30 percent of his share of the net profits of such trade or
21 business, shall be considered as earned income.

22 “(c) SPECIAL RULES.—For purposes of computing the
23 amount excludable under subsection (a), the following rules
24 shall apply:

25 “(1) LIMITATIONS ON AMOUNT OF EXCLUSION.—

1 The amount excluded from the gross income of an
2 individual under subsection (a) for any taxable year
3 shall not exceed an amount which shall be computed on
4 a daily basis at an annual rate of—

5 “(A) except as provided in subparagraph (B),
6 \$20,000 in the case of an individual who qualifies
7 under subsection (a), or

8 “(B) \$35,000 in the case of an individual who
9 qualifies under subsection (a) (1), but only with
10 respect to that portion of such taxable year occurring
11 after such individual has been a bona fide resident
12 of a foreign country or countries for an uninterrupted
13 period of 3 consecutive years.

14 “(2) **ATTRIBUTION TO YEAR IN WHICH SERVICES**
15 **ARE PERFORMED.**—For purposes of applying paragraph
16 (1), amounts received shall be considered received in
17 the taxable year in which the services to which the
18 amounts are attributable are performed.

19 “(3) **TREATMENT OF COMMUNITY INCOME.**—In
20 applying paragraph (1) with respect to amounts re-
21 ceived for services performed by a husband or wife
22 which are community income under community prop-
23 erty laws applicable to such income, the aggregate
24 amount excludable under subsection (a) from the gross
25 income of such husband and wife shall equal the amount

1 which would be excludable if such amounts did not con-
2 stitute such community income.

3 “(4) REQUIREMENT AS TO TIME OF RECEIPT.—

4 No amount received after the close of the taxable year
5 following the taxable year in which the services to which
6 the amounts are attributable are performed may be ex-
7 cluded under subsection (a).

8 “(5) CERTAIN AMOUNTS NOT EXCLUDABLE.—No
9 amount—

10 “(A) received as a pension or annuity, or

11 “(B) included in gross income by reason of
12 section 402 (b) (relating to taxability of benefi-
13 ciary of non-exempt trust), section 403 (c) (relat-
14 ing to taxability of beneficiary under a non-quali-
15 fied annuity), or section 403 (d) (relating to
16 taxability of beneficiary under certain forfeitable
17 contracts purchased by exempt organizations),
18 may be excluded under subsection (a).

19 “(6) TEST OF BONA FIDE RESIDENCE.—A state-
20 ment by an individual who has earned income from
21 sources within a foreign country to the authorities of that
22 country that he is not a resident of that country, if he is
23 held not subject as a resident of that country to the
24 income tax of that country by its authorities with respect
25 to such earnings, shall be conclusive evidence with respect

1 to such earnings that he is not a bona fide resident of that
2 country for purposes of subsection (a)(1).

3 “(7) CERTAIN NONCASH REMUNERATION.—If an
4 individual who qualifies under subsection (a)(1) receives
5 compensation from sources without the United States
6 (except from the United States or any agency thereof) in
7 the form of the right to use property or facilities, the
8 limitation under paragraph (1) applicable with respect
9 to such individual—

10 “(A) for a taxable year ending in 1963, shall
11 be increased by an amount equal to the amount of
12 such compensation so received during such taxable
13 year;

14 “(B) for a taxable year ending in 1964, shall
15 be increased by an amount equal to two-thirds of
16 such compensation so received during such taxable
17 year; and

18 “(C) for a taxable year ending in 1965, shall
19 be increased by an amount equal to one-third of such
20 compensation so received during such taxable year.

21 “(d) CROSS REFERENCES.—

 “**For administrative and penal provisions relating to
the exclusion provided for in this section, see sections
6001, 6011, 6012(c), and the other provisions of subtitle F.**”

22 (b) COMPUTATION OF EMPLOYEES' CONTRIBU-
23 TIONS.—Section 72 (f) (relating to special rules for comput-

1 ing employees' contributions) is amended by adding after
2 paragraph (2) the following new sentences:

3 "Paragraph (2) shall not apply to amounts which were
4 contributed by the employer after December 31, 1962, and
5 which would not have been includible in the gross income of
6 the employee by reason of the application of section 911 if
7 such amounts had been paid directly to the employee at the
8 time of contribution. The preceding sentence shall not apply
9 to amounts which were contributed by the employer, as de-
10 termined under regulations prescribed by the Secretary or his
11 delegate, to provide pension or annuity credits, to the extent
12 such credits are attributable to services performed before
13 January 1, 1963, and are provided pursuant to pension or
14 annuity plan provisions in existence on March 12, 1962,
15 and on that date applicable to such services."

16 (c) EFFECTIVE DATE.—

17 (1) IN GENERAL.—Except as provided in para-
18 graph (2), the amendments made by this section shall
19 apply to taxable years ending after December 31, 1962.

20 (2) AMENDMENTS TO SECTION 911.—The amend-
21 ment made by subsection (a) shall apply only with
22 respect to amounts received after December 31, 1962,
23 and which are attributable either to—

24 (A) services performed after such date, or

25 (B) services performed on or before such date,

1 but only if on March 12, 1962, there existed
 2 no right (whether forfeitable or nonforfeitable) to
 3 receive such amounts.

4 **SEC. 13. CONTROLLED FOREIGN CORPORATIONS.**

5 ~~(a)~~ **IN GENERAL.**—Part III of subchapter N of chapter
 6 1 ~~(relating to income from sources without the United~~
 7 ~~States)~~ is amended by adding at the end thereof the follow-
 8 ing new subpart:

9 **“Subpart F—Controlled Foreign Corporations**

“Sec. 951. Amounts included in gross income of United
 States persons.

“Sec. 952. Subpart F income defined.

“Sec. 952. Investment of earnings in nonqualified property.

“Sec. 954. Controlled foreign corporations.

“Sec. 955. Rules for determining stock ownership.

“Sec. 956. Exclusion from gross income of previously taxed
 earnings and profits.

“Sec. 957. Special rules for foreign tax credit.

“Sec. 958. Adjustments to basis of stock in controlled for-
 eign corporations and of other property.

10 **“SEC. 951. AMOUNTS INCLUDED IN GROSS INCOME OF**
 11 **UNITED STATES PERSONS.**

12 **“(a) AMOUNTS INCLUDED.—**

13 **“(1) IN GENERAL.**—If a foreign corporation is a
 14 controlled corporation on any day of a taxable year be-
 15 ginning after December 31, 1962, every United States
 16 person ~~(as defined in section 7701(a)(30))~~ who owns
 17 ~~(within the meaning of section 955(a))~~ stock in such
 18 corporation on the last day, in such year, on which such
 19 corporation is a controlled foreign corporation shall in-

1 elude in his gross income, for his taxable year in which
 2 or with which such taxable year of the corporation
 3 ends—

4 “~~(A)~~ his pro rata share ~~(determined under~~
 5 ~~paragraph (2))~~ of the corporation’s subpart F
 6 income for such year, and

7 “~~(B)~~ his pro rata share ~~(determined under~~
 8 ~~section 953(a)(2))~~ of the corporation’s increase
 9 in earnings invested in nonqualified property for
 10 such year ~~(but only to the extent not excluded~~
 11 ~~from gross income under section 956(a)(2))~~.

12 “~~(2)~~ PRO RATA SHARE OF SUBPART F INCOME.—
 13 The pro rata share referred to in paragraph ~~(1)(A)~~
 14 in the case of any United States person is the amount—

15 “~~(A)~~ which would have been distributed with
 16 respect to the stock which such person owns ~~(with-~~
 17 ~~in the meaning of section 955(a))~~ in such cor-
 18 poration if on the last day, in its taxable year, on
 19 which the corporation is a controlled foreign cor-
 20 poration it had distributed pro rata to its share-
 21 holders an amount ~~(i)~~ which bears the same ratio
 22 to its subpart F income for the taxable year, as
 23 ~~(ii)~~ the part of such year during which the corpora-
 24 tion is a controlled foreign corporation bears to the
 25 entire year, reduced by

1 “(B) the amount of any distribution received
2 by any other United States person during such
3 year as a dividend with respect to such stock.

4 “~~(3)~~ LIMITATION ON AMOUNT OF PRO RATA
5 SHARE OF INVESTMENT IN NONQUALIFIED PROPERTY
6 INCLUDED IN GROSS INCOME.—For purposes of para-
7 graph ~~(1)~~-(B), the pro rata share of any United States
8 person in the increase of the earnings of a controlled
9 foreign corporation invested in nonqualified property
10 shall not exceed an amount ~~(A)~~ which bears the same
11 ratio to his pro rata share of such increase ~~(as deter-~~
12 mined under section 953~~(a)~~-(2)) for the taxable
13 year, as ~~(B)~~ the part of such year during which the
14 corporation is a controlled foreign corporation bears to
15 the entire year.

16 “~~(b)~~ LESS THAN 10 PERCENT OWNERSHIP.—No per-
17 son shall be required to include any amount in gross income
18 under subsection ~~(a)~~ unless he can be considered, by apply-
19 ing the rules of ownership of section 955~~(b)~~, as owning,
20 directly or indirectly, on any day during the taxable year
21 of the corporation on which it was a controlled foreign cor-
22 poration, 10 percent or more of the total combined voting
23 power of all classes of stock, or of the total value of shares
24 of all classes of stock, of such corporation.

25 “~~(c)~~ COORDINATION WITH ELECTION OF A FOREIGN

1 INVESTMENT COMPANY TO DISTRIBUTE INCOME.—A
 2 United States person who, for his taxable year, is a qualified
 3 shareholder ~~(within the meaning of section 1247(c))~~ of a
 4 foreign investment company with respect to which an elec-
 5 tion under section 1247 is in effect shall not be required to
 6 include in gross income, for such taxable year, subpart F
 7 income of such company.

8 **“SEC. 952. SUBPART F INCOME DEFINED.**

9 **“(a) IN GENERAL.—**

10 **“(1) ITEMS TAKEN INTO ACCOUNT.—**For purposes
 11 of this subpart, the term ‘subpart F income’ means, in
 12 the case of any controlled foreign corporation, the sum
 13 of—

14 **“(A)** income derived from insurance of United
 15 States risks ~~(as determined under subsection (b))~~,

16 **“(B)** income from United States patents,
 17 copyrights, and exclusive formulas and processes
 18 ~~(as determined under subsection (c))~~, and

19 **“(C)** the net foreign base company income
 20 ~~(as determined under subsection (d))~~, except that
 21 this subparagraph shall apply only in the case of a
 22 controlled foreign corporation in which 5 or fewer
 23 United States persons own, by applying the rules of
 24 ownership of section 955(b), more than 50 percent

of the total combined voting power of all classes of stock entitled to vote.

“(2) EXCLUSION OF UNITED STATES INCOME.—

Subpart F income does not include any item includible in gross income under this chapter (other than this subpart) as income derived from sources within the United States of a foreign corporation engaged in trade or business in the United States.

“(3) NOT TO EXCEED EARNINGS AND PROFITS.—

The subpart F income of any controlled foreign corporation for any taxable year shall not exceed the earnings and profits of such corporation for such year.

“(b) INCOME FROM INSURANCE OF UNITED STATES RISKS.—

“(1) GENERAL RULE.—If a controlled foreign corporation receives premiums or other consideration in respect of any reinsurance or the issuing of any insurance or annuity contract—

“(A) in connection with property in, or residents of, the United States; or

“(B) in connection with property not in, or nonresidents of, the United States as the result of any arrangement whereby another corporation re-

receives a substantially equal amount of premiums or other consideration in respect of any reinsurance or the issuing of any insurance or annuity contract in connection with property in, or residents of, the United States;

then for purposes of subsection ~~(a)(1)(A)~~, the term 'income derived from the insurance of United States risks' means that income which ~~(subject to the modifications provided by subparagraphs (A), (B), and (C) of paragraph (2))~~ would be taxed under subchapter L of this chapter if such corporation were a domestic corporation.

~~“(2) SPECIAL RULES.—For purposes of paragraph (1)—~~

~~“(A) In the application of part I of subchapter L, life insurance company taxable income is the gain from operations as defined in section 809(b).~~

~~“(B) A corporation which would, if it were a domestic corporation, be taxable under part II of subchapter L shall apply paragraph (1) as if it were taxable under part III of subchapter L.~~

~~“(C) The following provisions of subchapter L shall not apply:~~

~~“(i) Section 809(d)(4) (operations loss deduction).~~

1 ~~“(ii) Section 809(d)(5) (certain non-~~
2 ~~participating contracts).~~

3 ~~“(iii) Section 809(d)(6) (group life,~~
4 ~~accident, and health insurance).~~

5 ~~“(iv) Section 809(d)(10) (small business~~
6 ~~deduction).~~

7 ~~“(v) Section 817(b) (gain on property~~
8 ~~held on December 31, 1958, and certain sub-~~
9 ~~stituted property acquired after 1958).~~

10 ~~“(vi) Section 832(b)(5) (certain capital~~
11 ~~losses).~~

12 ~~“(D) ‘Gross amount’ to the extent provided in~~
13 ~~section 809(c) (1) and (2), less ‘increase in~~
14 ~~certain reserves’ as defined in section 809(d)(2),~~
15 ~~and ‘premiums earned’ as defined in section 832(b)~~
16 ~~(4) shall be taken into account only to the extent~~
17 ~~they are in respect of any reinsurance or the issuing~~
18 ~~of any reinsurance or the issuing of any insurance~~
19 ~~or annuity contract described in paragraph (1).~~

20 ~~“(E) All items of income (other than those~~
21 ~~taken into account under subparagraph (D)) and~~
22 ~~all items of expenses, losses, and deductions shall~~
23 ~~be properly allocated or apportioned under regula-~~
24 ~~tions prescribed by the Secretary or his delegate.~~

1 “(c) INCOME FROM UNITED STATES PATENTS, COPY-
2 RIGHTS, AND EXCLUSIVE FORMULAS AND PROCESSES.—

3 “(1) GENERAL RULE.—For purposes of subsection
4 ~~(a)~~ (1) (B), the term ‘income from United States
5 patents, copyrights, and exclusive formulas and proc-
6 esses’, means the amount of gross rentals, royalties, or
7 other income derived from the license, sublicense, sale,
8 exchange, use, or other means of exploitation of patents,
9 copyrights, and exclusive formulas and processes—

10 “(A) substantially developed, created, or pro-
11 duced in the United States, or

12 “(B) acquired from any United States person
13 which, directly or indirectly, owns or controls, or
14 is owned or controlled by, or is under common
15 ownership or control with, the controlled foreign
16 corporation,

17 less the cost and expense allowance defined in para-
18 graph (2).

19 “(2) COST AND EXPENSE ALLOWANCE.—An al-
20 lowance shall be made, in accordance with regulations
21 prescribed by the Secretary or his delegate, for ordinary
22 and necessary expenses incurred by the controlled foreign
23 corporation in the receipt or production of the income
24 described in paragraph (1), including taxes and any
25 amortization or depreciation of the cost to such corpo-

ration of such property or rights described in paragraph (1), but not including any production, manufacturing, or similar expenses incurred in the use or other means of exploitation of such property or rights.

~~“(3) DETERMINATION OF INCOME FROM USE.—~~

The income from use or other means of exploitation by the controlled foreign corporation of the property or right described in paragraph (1) shall be the amount which would be obtained as a gross rent, royalty, or other payment in an arm’s length transaction with an unrelated person for similar use or exploitation, of the property or right.

~~“(d) NET FOREIGN BASE COMPANY INCOME.—~~For

purposes of subsection (a)(1)(C), the term ‘net foreign base company income’ means—

~~“(1) the foreign base company income for the taxable year, determined under subsection (e), reduced by~~

~~“(2) the increase in investment in qualified property in less developed countries for the taxable year, determined under subsection (f).—~~

~~“(e) FOREIGN BASE COMPANY INCOME.—~~

~~“(1) IN GENERAL.—~~For purposes of subsection (d)(1), the term ‘foreign base company income’ means the foreign personal holding company income (as de-

1 fined in section 553) for the taxable year, modified and
 2 adjusted as provided in this subsection.

3 “(2) CERTAIN SALES INCOME INCLUDED.—The
 4 term ‘foreign base company income’ includes foreign
 5 base company sales income if, for the taxable year, such
 6 income is equal to at least 20 percent of the gross income
 7 of the foreign corporation (not including for this purpose
 8 other foreign base company income under this subsec-
 9 tion). For purposes of this paragraph, the term ‘foreign
 10 base company sales income’ means income (whether in
 11 the form of profits, commissions, fees, or otherwise)
 12 derived in connection with the purchase of personal
 13 property from a related person and its sale to any per-
 14 son, or the purchase of personal property from any
 15 person and its sale to a related person, where—

16 “(A) the property which is purchased is manu-
 17 factured, produced, grown, or extracted outside
 18 the country under the laws of which the controlled
 19 foreign corporation is created or organized, and

20 “(B) the property is sold for use, consumption,
 21 or disposition outside such foreign country.

22 For purposes of the preceding sentence, a person is a
 23 related person with respect to the controlled foreign
 24 corporation if he, directly or indirectly, owns or con-
 25 trols, or is owned or controlled by, or is under common

ownership or control with, the controlled foreign corporation.

~~“(3) RENTS INCLUDED WITHOUT REGARD TO 50-PERCENT LIMITATION.—All rents shall be included in foreign base company income without regard to whether or not such rents constitute more than 50 percent of gross income.~~

~~“(4) INSURANCE AND PATENT INCOME EXCLUDED.—The term ‘foreign base company income’ does not include any income derived from insurance of United States risks (as determined under subsection (b)) or income from United States patents, copyrights, and exclusive formulas and processes (as determined under subsection (c)).~~

~~“(5) INCOME OF CERTAIN BANKS AND BANK-CONTROLLED CORPORATIONS EXCLUDED.—The term ‘foreign base company income’ does not include—~~

~~“(A) the income of any corporation described in section 552(b) (relating to exception for banks and exempt corporations), or~~

~~“(B) the income of any foreign corporation if 50 percent or more of the fair market value of its outstanding stock is owned directly or indirectly by a domestic corporation which is either organized under section 25(a) of the Federal Reserve~~

Act ~~(12 U.S.C., secs. 611-631)~~, or has an agreement or understanding with the Board of Governors of the Federal Reserve System under section 25 of the Federal Reserve Act ~~(12 U.S.C., secs. 601-604)~~, if all of the stock ~~(except qualifying shares)~~ of the domestic corporation is owned by a national or State bank which is a member of the Federal Reserve System.

~~“(6) SPECIAL RULE WHERE FOREIGN BASE COMPANY INCOME IS LESS THAN 20 PERCENT OR MORE THAN 80 PERCENT OF GROSS INCOME.—For purposes of this subsection—~~

~~“(A) If the foreign base company income (determined without regard to paragraph (7)) is less than 20 percent of gross income, no part of the gross income of the taxable year shall be treated as foreign base company income.~~

~~“(B) If the foreign base company income (determined without regard to paragraph (7)) exceeds 80 percent of gross income, the entire gross income of the taxable year shall be taken into account in determining foreign base company income.~~

~~“(7) DEDUCTIONS TO BE TAKEN INTO ACCOUNT.—The foreign base company income for the tax-~~

able year shall be reduced so as to take into account deductions (including taxes) properly allocable to such income.

~~“(f) INVESTMENT IN QUALIFIED PROPERTY IN LESS DEVELOPED COUNTRIES.—~~

~~“(1) GENERAL RULE.—~~For purposes of subsection ~~(d) (2)~~, the increase in investment in qualified property in less developed countries for any taxable year is the amount by which—

~~“(A) the aggregate amount of property described in sections 953(b)(2) (C) and (D) and property (including money) which is located outside the United States and is ordinary and necessary for the active conduct of a qualified trade or business described in section 953(b)(3)(A)(ii) held at the close of the taxable year, exceeds~~

~~“(B) the aggregate amount of property described in subparagraph (A) held at the close of the preceding taxable year.~~

~~“(2) INVESTMENTS AFTER CLOSE OF YEAR.—~~

Under regulations prescribed by the Secretary or his delegate, a controlled foreign corporation may elect to make the determinations under subparagraphs (A) and (B) of paragraph (1) as of the close of the 75th day after the close of each taxable year.

1 “(3) AMOUNT ATTRIBUTABLE TO PROPERTY.—

2 The amount taken into account under paragraph (1)
3 with respect to any property shall be its adjusted basis,
4 reduced by any liability to which the property is subject.

5 “SEC. 953. INVESTMENT OF EARNINGS IN NONQUALIFIED
6 PROPERTY.

7 “(a) GENERAL RULES.—For purposes of this subpart—

8 “(1) AMOUNT OF INVESTMENT.—The amount of
9 earnings of a controlled foreign corporation invested in
10 nonqualified property at the close of any taxable year
11 is the aggregate amount of such property held at the
12 close of the taxable year, to the extent such amount
13 does not exceed the sum of (A) the earnings and profits
14 for the taxable year, and (B) the earnings and profits
15 accumulated for prior taxable years beginning after
16 December 31, 1962.

17 “(2) PRO RATA SHARE OF INCREASE FOR YEAR.—

18 In the case of any United States person, the pro rata
19 share of the increase for any taxable year in the earn-
20 ings of a controlled foreign corporation invested in a
21 nonqualified property is the amount determined by sub-
22 tracting—

23 “(A) his pro rata share of the amount deter-
24 mined under paragraph (1) for the close of the
25 preceding taxable year, reduced by amounts paid

during the taxable year to which section 956(e)(1) applies; from

~~“(B) his pro rata share of the amount determined under paragraph (1) for the close of the taxable year.~~

~~“(3) AMOUNT ATTRIBUTABLE TO PROPERTY.—~~

~~The amount taken into account under paragraph (1) or (2) with respect to any property shall be its adjusted basis, reduced by any liability to which the property is subject.~~

~~“(b) NONQUALIFIED PROPERTY DEFINED.—For purposes of this subpart—~~

~~“(1) GENERAL RULE.—The term ‘nonqualified property’ means any money or other property (tangible or intangible) acquired after December 31, 1962, which is not qualified property.~~

~~“(2) QUALIFIED PROPERTY.—The term ‘qualified property’ means—~~

~~“(A) Any money or other property which is located outside the United States and is ordinary and necessary for the active conduct of a qualified trade or business (as determined under paragraph (3)) carried on by the controlled foreign corporation.~~

~~“(B) Property which would qualify under sub-~~

1 paragraph (A) except for the fact that it is located
2 in the United States, but only if such property is—

3 “(i) obligations of the United States,
4 money, or deposits with persons carrying on
5 the banking business;

6 “(ii) property purchased in the United
7 States for export to, or for use in, foreign
8 countries; or

9 “(iii) any loan arising in connection with
10 the sale of property if the amount of such loan
11 outstanding at no time during the taxable year
12 exceeds the amount which would be ordinary
13 and necessary to carry on the trade or business
14 of both the lending corporation and the borrow-
15 ing United States person had the sale been
16 made between unrelated persons.

17 “(C) Stock owned by the controlled foreign
18 corporation in another controlled foreign corpora-
19 tion in which it owns at least 10 percent of the vot-
20 ing stock and 10 percent of the value of all classes of
21 stock and in which it together with four or fewer
22 United States persons, owns, directly or indirectly,
23 more than 50 percent of the voting stock (unless
24 under the laws of a less developed country such per-
25 centage of ownership is not permitted, in which

ease such lesser percentage as is permitted); but this subparagraph shall apply only if—

“(i) substantially all of the property of such other controlled foreign corporation is ordinary and necessary for the active conduct of a trade or business engaged in by it almost wholly within a less developed country or countries, and

“(ii) such other controlled foreign corporation is created or organized under the laws of one of such countries in which it is so engaged.

“(D) Any investment which is required because of restrictions imposed by a less developed country, and any investment which, when made, was so required and which would result in substantial losses if withdrawn.

“(3) QUALIFIED TRADE OR BUSINESS.—

“(A) A trade or business is a qualified trade or business if such trade or business (or substantially the same trade or business)—

“(i) is carried on by the controlled foreign corporation outside the United States and has been so carried on by such corporation, while controlled by substantially the same United

1 States persons since December 31, 1962, or
2 during the 5-year period ending with the close
3 of the preceding taxable year, or

4 “(ii) is carried on by the controlled foreign
5 corporation almost wholly within a less devel-
6 oped country or countries.

7 “(B) A trade or business which is a qualified
8 trade or business for a corporation in which the
9 controlled foreign corporation owns at least 80 per-
10 cent of the total combined voting power of all classes
11 of stock entitled to vote and at least 80 percent of
12 the total value of all classes of stock shall be treated
13 as a qualified trade or business for the controlled
14 foreign corporation if such percentage of stock was
15 owned continuously since December 31, 1962, or
16 during the 5-year period ending with the close of
17 the preceding taxable year.

18 “(4) SITUS OF CERTAIN PROPERTY.—Property
19 which is an obligation of, or pledges and guarantees
20 made with respect to obligations of, United States persons
21 shall be considered as property located in the United
22 States.

23 “(5) LESS DEVELOPED COUNTRY DEFINED.—The
24 term ‘less developed country’ means (in respect of any
25 foreign corporation) any foreign country (other than

an area within the Sino-Soviet bloc) or any possession of the United States, with respect to which on the first day of the taxable year, there is in effect an Executive order by the President of the United States designating such country or possession as an economically less developed country for purposes of this subpart. For purposes of the preceding sentence, an oversea territory, department, province, or possession may be treated as a separate country. No designation shall be made under this paragraph with respect to—

Australia	Liechtenstein
Austria	Luxembourg
Belgium	Monaco
Canada	Netherlands
Denmark	New Zealand
France	Norway
Germany (Federal	Union of South Africa
Republic)	San Marino
Hong Kong	Sweden
Italy	Switzerland
Japan	United Kingdom

“SEC. 954. CONTROLLED FOREIGN CORPORATIONS.

“(a) GENERAL RULE.—For purposes of this subpart, the term ‘controlled foreign corporation’ means any foreign corporation of which more than 50 percent of the total com-

1 bined voting power of all classes of stock entitled to vote is
 2 owned, directly or indirectly (within the meaning of section
 3 955(b)), by United States persons on any day during the
 4 taxable year of such foreign corporation.

5 “(b) SPECIAL RULE FOR INSURANCE.—For purposes
 6 only of taking into account income described in section
 7 952(a)(1)(A) (relating to income derived from insurance
 8 of United States risks), the term ‘controlled foreign corpora-
 9 tion’ includes not only a foreign corporation as defined by
 10 subsection (a) but also one of which more than 25 percent
 11 of the total combined voting power of all classes of stock is
 12 owned, directly or indirectly (within the meaning of sec-
 13 tion 955(b)), by United States persons on any day dur-
 14 ing the taxable year of such corporation, if the gross amount
 15 of premiums or other consideration in respect of reinsurance
 16 or the issuing of insurance or annuity contracts in connec-
 17 tion with property in, or residents of, the United States, ex-
 18 ceeds 75 percent of the gross amount of all premiums or
 19 other consideration in respect of all risks.

20 “(c) SPECIAL RULE FOR CERTAIN LESS DEVELOPED
 21 COUNTRIES.—In the case of any foreign corporation to
 22 which section 953(b)(2)(C) applies, the maximum per-
 23 centage of ownership permitted under the laws of a less
 24 developed country shall be considered, in lieu of the more

1 than 50 percent requirement in subsection (a), the per-
 2 centage required under subsection (a) in order for the cor-
 3 poration to be classified as a controlled foreign corporation.

4 **"SEC. 955. RULES FOR DETERMINING STOCK OWNERSHIP.**

5 **"(a) FOR PURPOSES OF SECTION 951(a).—**

6 **"(1) GENERAL RULE.—**For purposes of section
 7 951(a), stock owned means—

8 **"(A)** stock owned directly, and

9 **"(B)** stock owned with the application of para-
 10 graph (2).

11 **"(2) STOCK OWNERSHIP THROUGH FOREIGN EN-**
 12 **TITIES.—**For purposes of subparagraph (B) of para-
 13 graph (1), stock owned, directly or indirectly, by or
 14 for a foreign corporation, foreign partnership, or foreign
 15 trust or foreign estate (within the meaning of section
 16 7701(a)(31)) shall be considered as being owned pro-
 17 portionately by its shareholders, partners, or benefi-
 18 ciaires. Stock considered to be owned by a person by rea-
 19 son of the application of the preceding sentence shall, for
 20 purposes of applying such sentence, be treated as actually
 21 owned by such person.

22 **"(3) SPECIAL RULE FOR MUTUAL INSURANCE**
 23 **COMPANIES.—**For purposes of applying paragraph (1)

1 in the case of a foreign mutual insurance company, the
2 term 'stock' shall include any certificate entitling the
3 holder to voting power in the corporation.

4 “(b) OTHER PROVISIONS.—For purposes of sections 951
5 (b), 952(a)(1)(C), and 954, section 318(a) (relating to
6 constructive ownership of stock) shall apply to the extent
7 that the effect is to subject a United States person to the
8 requirement of section 951(a), to treat 5 or fewer United
9 States persons as owning more than 50 percent of all classes
10 of stock entitled to vote of a controlled foreign corporation,
11 or to make a foreign corporation a controlled foreign cor-
12 poration under section 954, except—

13 “(1) In applying paragraph (1)(A) of section
14 318(a), stock owned by a nonresident alien individual
15 (other than a foreign trust or foreign estate) shall not
16 be considered as owned by a citizen or by a resident
17 alien individual.

18 “(2) In applying the first sentence of subpara-
19 graphs (A) and (B), and in applying clause (i) of
20 subparagraph (C), of section 318(a)(2)—

21 “(A) if a partnership, estate, trust, or corpora-
22 tion owns, directly or indirectly, more than 50 per-
23 cent of the total combined voting power of all classes
24 of stock entitled to vote of a corporation, it shall be

1 considered as owning all the stock entitled to vote,
2 and

3 “~~(B)~~ if a partnership, estate, trust, or corpora-
4 tion owns, directly or indirectly, more than 50 per-
5 cent of the total value of shares of all classes of stock
6 of a corporation, it shall be considered as owning
7 the total value of all of the outstanding stock of such
8 corporation. The application of this subparagraph
9 shall not have the effect of increasing voting power
10 of a partner, beneficiary, or shareholder, for pur-
11 poses of subparagraph ~~(A)~~.

12 “~~(3)~~ Stock owned by a partnership, estate, trust,
13 or corporation, by reason of the application of the second
14 sentence of subparagraphs ~~(A)~~ and ~~(B)~~, and the appli-
15 cation of clause ~~(ii)~~ of subparagraph ~~(C)~~, of section
16 318(a)(2), shall not be considered as owned by such
17 partnership, estate, trust, or corporation, for the purposes
18 of applying the first sentence of subparagraphs ~~(A)~~ and
19 ~~(B)~~, and in applying clause ~~(i)~~ of subparagraph ~~(C)~~,
20 of section 318(a)(2).

21 “~~(4)~~ In applying clause ~~(i)~~ of subparagraph ~~(C)~~
22 of section 318(a)(2), the 50-percent limitation con-
23 tained in subparagraph ~~(C)~~ shall not apply.

1 **"SEC. 956. EXCLUSION FROM GROSS INCOME OF PREVI-**
 2 **OUSLY TAXED EARNINGS AND PROFITS.**

3 ~~(a)~~ **EXCLUSION FROM GROSS INCOME OF UNITED**
 4 **STATES PERSONS.**—For purposes of this chapter, the earn-
 5 ings and profits for a taxable year of a foreign corporation
 6 attributable to amounts which are, or have been, included in
 7 the gross income of a United States person under section
 8 951~~(a)~~ shall not, when—

9 ~~"(1)~~ such amounts are distributed to, or

10 ~~"(2)~~ such amounts would, but for this subsection,
 11 be included under section 951~~(a)~~~~(1)~~~~(B)~~ in the gross
 12 income of,

13 such person ~~(or any other United States person who acquires~~
 14 ~~from any person any portion of the interest of such United~~
 15 ~~States person in such foreign corporation, but only to the ex-~~
 16 ~~tent of such portion, and subject to such proof of the identity~~
 17 ~~of such interest as the Secretary or his delegate may by regu-~~
 18 ~~lations prescribe)~~ directly, or indirectly through a chain of
 19 ownership described under section 955~~(a)~~, be again included
 20 in the gross income of such United States person ~~(or of such~~
 21 ~~other United States person).~~

22 ~~"(b)~~ **EXCLUSION FROM GROSS INCOME OF CERTAIN**
 23 **FOREIGN SUBSIDIARIES.**—For purposes of section 951~~(a)~~,
 24 the earnings and profits for a taxable year of a controlled
 25 foreign corporation attributable to amounts which are, or

1 have been, included in the gross income of a United States
 2 person under section 951(a), shall not, when distributed
 3 through a chain of ownership described under section 955
 4 (a), be also included in the gross income of another con-
 5 trolled foreign corporation in such chain for purposes of the
 6 application of section 951(a) to such other controlled foreign
 7 corporation with respect to such United States person (or to
 8 any other United States person who acquires from any per-
 9 son any portion of the interest of such United States person
 10 in the controlled foreign corporation, but only to the extent of
 11 such portion, and subject to such proof of identity of such
 12 interest as the Secretary or his delegate may prescribe by
 13 regulations).

14 “(c) ALLOCATIONS OF DISTRIBUTIONS.—For purposes
 15 of subsections (a) and (b), section 316(a) shall be ap-
 16 plied by applying paragraph (2) thereof, and then para-
 17 graph (1) thereof—

18 “(1) first to earnings and profits attributable to
 19 amounts included in gross income under section 951
 20 (a)(1)(B) (or which would have been included except
 21 for section 956(a)(2)),

22 “(2) then to earnings and profits attributable to
 23 amounts included in gross income under section 951(a)
 24 (1)(A) (but reduced by amounts not included under

1 section 951(a)(1)(B) because of the exclusion in sec-
 2 tion 956(a)(2)), and

3 “(3) then to other earnings and profits.

4 “(d) DISTRIBUTIONS EXCLUDED FROM GROSS IN-
 5 COME NOT TO BE TREATED AS DIVIDENDS.—Except as
 6 provided in section 957(a)(3), any distribution excluded
 7 from gross income under subsection (a) shall be treated, for
 8 purposes of this chapter, as a distribution which is not a
 9 dividend.

10 “SEC. 957. SPECIAL RULES FOR FOREIGN TAX CREDIT.

11 “(a) TAXES PAID BY A FOREIGN CORPORATION.—

12 “(1) GENERAL RULE.—For purposes of subpart A
 13 of this part, if there is included, under section 951(a),
 14 in the gross income of a domestic corporation any
 15 amount attributable to earnings and profits—

16 “(A) of a foreign corporation at least 10 per-
 17 cent of the voting stock of which is directly owned
 18 by such domestic corporation; or

19 “(B) of a foreign corporation at least 50 per-
 20 cent of the voting stock of which is directly owned
 21 by a foreign corporation at least 10 percent of the
 22 voting stock of which is in turn directly owned by
 23 such domestic corporation;

24 then, under regulations, prescribed by the Secretary or
 25 his delegate, such domestic corporation shall be deemed

1 to have paid the same proportion of the total income;
2 war profits; and excess profits taxes paid (or deemed
3 paid; if, paragraph (4) applies) to a foreign country
4 or possession of the United States for the taxable year
5 which the amount of earnings and profits of such foreign
6 corporation so included in gross income of the domestic
7 corporation bears to the entire amount of the total earn-
8 ings and profits of such foreign corporation for such
9 taxable year.

10 “(2) TAXES PREVIOUSLY DEEMED PAID BY DO-
11 MESTIC CORPORATION.—If a domestic corporation re-
12 ceives a distribution from a foreign corporation, any
13 portion of which is excluded from gross income under
14 section 956, the income, war profits, and excess profits
15 taxes paid or deemed paid by such foreign corporation
16 to any foreign country or to any possession of the United
17 States in connection with the earnings and profits of
18 such foreign corporation from which such distribution
19 is made shall not be taken into account for purposes
20 of section 902, to the extent such taxes were deemed
21 paid by such domestic corporation under paragraph (1)
22 for any prior taxable year.

23 “(3) TAXES PAID BY FOREIGN CORPORATION AND
24 NOT PREVIOUSLY DEEMED PAID BY DOMESTIC CORPO-
25 RATION.—Any portion of a distribution from a foreign

1 corporation received by a domestic corporation which is
 2 excluded from gross income under section 956(a) shall
 3 be treated by the domestic corporation as a dividend,
 4 solely for purposes of taking into account under section
 5 902 any income, war profits, or excess profits taxes paid
 6 to any foreign country or to any possession of the United
 7 States, on or with respect to the accumulated profits of
 8 such foreign corporation from which such distribution is
 9 made, which were not deemed paid by the domestic
 10 corporation under paragraph (1) for any prior taxable
 11 year.

12 “(4) TAXES PAID BY A FOREIGN SUBSIDIARY.—If
 13 subparagraph (A) of paragraph (1) applies with re-
 14 spect to an amount included in gross income under sec-
 15 tion 951(a) for a taxable year, then such amount shall
 16 be considered a dividend for purpose of the application
 17 of section 902(b).

18 (5) INCLUSION IN GROSS INCOME.—

“For inclusion in gross income of amount equal to
 taxes deemed paid under paragraph (1), see section 78.

19 “(b) SPECIAL RULES FOR FOREIGN TAX CREDIT IN
 20 YEAR OF RECEIPT OF PREVIOUSLY TAXED EARNINGS AND
 21 PROFITS.—

22 “(1) INCREASE IN SECTION 904 LIMITATION.—In
 23 the case of any taxpayer who—

1 “~~(A)~~ either ~~(i)~~ chose to have the benefits of
2 subpart A of this part for a taxable year in which
3 he was required under section 951~~(a)~~ to include in
4 his gross income an amount in respect of a con-
5 trolled foreign corporation, or ~~(ii)~~ did not pay or
6 accrue for such taxable year any income, war profits
7 or excess profits taxes to any foreign country or to
8 any possession of the United States, and

9 “~~(B)~~ chooses to have the benefits of subpart
10 A of this part for the taxable year in which he re-
11 ceives a distribution or amount which is excluded
12 from gross income under section 956~~(a)~~ and which
13 is attributable to earnings and profits of the con-
14 trolled foreign corporation which was included in
15 his gross income for the taxable year referred to in
16 subparagraph ~~(A)~~, and

17 “~~(C)~~ for the taxable year in which such dis-
18 tribution or amount is received, pays, or is deemed
19 to have paid, or accrues income, war profits, or ex-
20 cess profits taxes to a foreign country or to any
21 possession of the United States with respect to such
22 distribution or amount,

23 the applicable limitation under section 904 for the tax-
24 able year in which such distribution or amount is re-
25 ceived shall be increased as provided in paragraph ~~(2)~~,

1 but such increase shall not exceed the amount of such
2 taxes paid, or deemed paid, or accrued with respect
3 to such distribution or amount.

4 “~~(2)~~ AMOUNT OF INCREASE.—The amount of in-
5 crease of the applicable limitation under section 904(a)-
6 for the taxable year in which the distribution or amount
7 referred to in paragraph ~~(1)(B)~~ is received shall be
8 an amount equal to—

9 “~~(A)~~ the amount by which the applicable lim-
10 itation under section 904(a) for the taxable year
11 referred to in paragraph ~~(1)(A)~~ was increased by
12 reason of the inclusion in gross income under section
13 951(a) of the amount in respect of the controlled
14 foreign corporation, reduced by

15 “~~(B)~~ the amount of any income, war profits,
16 and excess profits taxes paid, or deemed paid, or
17 accrued to any foreign country or possession of the
18 United States which were allowable as a credit
19 under section 901 for the taxable year referred to in
20 paragraph ~~(1)(A)~~ and which would not have been
21 allowable but for the inclusion in gross income of the
22 amount described in subparagraph ~~(A)~~.

23 “~~(3)~~ CASES IN WHICH TAXES NOT TO BE AL-
24 LOWED AS DEDUCTION.—In the case of any taxpayer
25 who—

1 “(A) chose to have the benefits of subpart A
2 of this part for a taxable year in which he was re-
3 quired under section 951(a) to include in his gross
4 income an amount in respect of a controlled foreign
5 corporation; and

6 “(B) does not choose to have the benefits of
7 subpart A of this part for the taxable year in which
8 he receives a distribution or amount which is ex-
9 cluded from gross income under section 956(a) and
10 which is attributable to earnings and profits of the
11 controlled foreign corporation which was included
12 in his gross income for the taxable year referred to
13 in subparagraph (A);

14 no deduction shall be allowed under section 164 for the
15 taxable year in which such distribution or amount is
16 received for any income, war profits, or excess profits
17 taxes paid or accrued to any foreign country or to any
18 possession of the United States on or with respect to
19 such distribution or amount.

20 “(4) INSUFFICIENT TAXABLE INCOME.—If an in-
21 crease in the limitation under this subsection exceeds the
22 tax imposed by this chapter for such year, the amount
23 of such excess shall be deemed an overpayment of tax
24 for such year.

1 **"SEC. 958. ADJUSTMENTS TO BASIS OF STOCK IN CON-**
2 **TROLLED FOREIGN CORPORATION AND OF**
3 **OTHER PROPERTY.**

4 **"(a) INCREASE IN BASIS.**—Under regulations pre-
5 scribed by the Secretary or his delegate, the basis of a United
6 States person's stock in a controlled foreign corporation, and
7 the basis of property of a United States person by reason of
8 which he is considered under section 955(a)(2) as owning
9 stock of a controlled foreign corporation, shall be increased
10 by the amount required to be included in his gross income
11 under section 951(a) with respect to such stock or with
12 respect to such property, as the case may be, but only to the
13 extent to which such amount was included in the gross
14 income of such person.

15 **"(b) REDUCTION IN BASIS.**—

16 **"(1) IN GENERAL.**—Under regulations prescribed
17 by the Secretary or his delegate, the adjusted basis of
18 stock or other property with respect to which a United
19 States person receives an amount which is excluded from
20 gross income under section 956(a) shall be reduced by
21 the amount so excluded.

22 **"(2) AMOUNT IN EXCESS OF BASIS.**—To the ex-
23 tent that an amount excluded from gross income under
24 section 956(a) exceeds the adjusted basis of the stock
25 or other property with respect to which it is received,

the amount shall be treated as gain from the sale or exchange of property."

~~(b)~~ TECHNICAL AND CLERICAL AMENDMENTS.—

~~(1)~~ Section 551(b) ~~(relating to foreign personal holding company income included in gross income of United States shareholders)~~ is amended by adding at the end thereof the following new sentence: "The amount included in the gross income of any United States shareholder for any taxable year under the preceding sentence shall be reduced by such shareholder's proportionate share of the undistributed personal holding company income which is included in his gross income under section 951(a)(1)(A) ~~(relating to amounts included in gross income of United States persons)~~ for such taxable year as his pro rata share of the subpart F income of the company."

~~(2)~~ Section 901 ~~(relating to foreign tax credit)~~ is amended by striking out "section 902" and inserting in lieu thereof "sections 902 and 957".

~~(3)~~ Section 902(c) is amended to read as follows:

~~"(c)~~ CROSS REFERENCES.—

"(1) For application of subsections (a) and (b) with respect to taxes deemed paid in a prior taxable year by a United States person with respect to a controlled foreign corporation, see section 957.

"(2) For reduction of credit with respect to dividends paid out of accumulated profits for years for which certain information is not furnished, see section 6038."

1 ~~(4)~~ Section 904(f) is amended to read as follows:

2 ~~“(f)~~ CROSS REFERENCES.—

~~“(1)~~ For increase of applicable limitation under subsection (a) for taxes paid with respect to amounts received which were included in the gross income of the taxpayer for a prior taxable year as a United States person with respect to a controlled foreign corporation, see section 957(b).

~~“(2)~~ For special rule relating to the application of the credit provided by section 901 in the case of affiliated groups which include Western Hemisphere trade corporations for years in which the limitation provided by subsection (a)(2) applies, see section 1503(d).”

3 ~~(5)~~ The table of subparts for part III of subchapter
4 N of chapter 1 is amended by adding at the end thereof
5 the following:

 “Subpart F. Controlled foreign corporations.”

6 ~~(6)~~ Section 1016(a) (relating to adjustments to
7 basis) is amended—

8 ~~(A)~~ by striking out the period at the end of
9 paragraph ~~(18)~~ and inserting in lieu thereof
10 a semicolon; and

11 ~~(B)~~ by adding after paragraph ~~(18)~~ the following new paragraph:

12 ~~“(19)~~ to the extent provided in section 958 in
13 the case of stock in controlled foreign corporations (or
14 foreign corporations which were controlled foreign cor-
15

perations) and of property by reason of which a person is considered as owning such stock."

(c) **EFFECTIVE DATE.**—The amendments made by this section shall apply with respect to taxable years of foreign corporations beginning after December 31, 1962, and to taxable years of United States persons within which or with which such taxable years of such foreign corporations end.

SEC. 12. CONTROLLED FOREIGN CORPORATIONS.

(a) *IN GENERAL.*—Part III of subchapter N of chapter 1 (relating to income from sources without the United States) is amended by adding at the end thereof the following new subparts:

"Subpart F—Controlled Foreign Corporations

"Sec. 951. Amounts included in gross income of United States shareholders.

"Sec. 952. Subpart F income defined.

"Sec. 953. Income from insurance of United States risks.

"Sec. 954. Foreign base company income.

"Sec. 955. Withdrawal of previously excluded subpart F income from qualified investment.

"Sec. 956. Investment of earnings in United States property.

"Sec. 957. Controlled foreign corporations; United States persons.

"Sec. 958. Rules for determining stock ownership.

"Sec. 959. Exclusion from gross income of previously taxed earnings and profits.

"Sec. 960. Special rules for foreign tax credit.

"Sec. 961. Adjustments to basis of stock in controlled foreign corporations and of other property.

"Sec. 962. Election by individuals to be subject to tax at corporate rates.

"Sec. 963. Receipt of minimum distributions by domestic corporations.

"Sec. 964. Miscellaneous provisions.

1 “SEC. 951. AMOUNTS INCLUDED IN GROSS INCOME OF UNITED
2 STATES SHAREHOLDERS.

3 “(a) AMOUNTS INCLUDED.—

4 “(1) IN GENERAL.—If a foreign corporation is a
5 controlled foreign corporation for an uninterrupted period
6 of 30 days or more during any taxable year beginning
7 after December 31, 1962, every person who is a United
8 States shareholder (as defined in subsection (b)) of
9 such corporation and who owns (within the meaning of
10 section 958(a)) stock in such corporation on the last
11 day, in such year, on which such corporation is a con-
12 trolled foreign corporation shall include in his gross in-
13 come, for his taxable year in which or with which such
14 taxable year of the corporation ends—

15 “(A) the sum of—

16 “(i) except as provided in section 963, his
17 pro rata share (determined under paragraph
18 (2)) of the corporation’s subpart F income for
19 such year, and

20 “(ii) his pro rata share (determined under
21 section 955(a)(3)) of the corporation’s pre-
22 viously excluded subpart F income withdrawn
23 from investment in less developed countries for
24 such year; and

25 “(B) his pro rata share (determined under

section 956(a)(2)) of the corporation's increase in earnings invested in United States property for such year (but only to the extent not excluded from gross income under section 959(a)(2)).

“(2) *PRO RATA SHARE OF SUBPART F INCOME.*—

The pro rata share referred to in paragraph (1)(A)(i) in the case of any United States shareholder is the amount—

“(A) which would have been distributed with respect to the stock which such shareholder owns (within the meaning of section 958(a)) in such corporation if on the last day, in its taxable year, on which the corporation is a controlled foreign corporation it had distributed pro rata to its shareholders an amount (i) which bears the same ratio to its subpart F income for the taxable year, as (ii) the part of such year during which the corporation is a controlled foreign corporation bears to the entire year, reduced by

“(B) the amount of distributions received by any other person during such year as a dividend with respect to such stock, but only to the extent of the dividend which would have been received if the distribution by the corporation had been the amount (i) which bears the same ratio to the sub-

part *F* income of such corporation for the taxable year, as (ii) the part of such year during which such shareholder did not own (within the meaning of section 958(a)) such stock bears to the entire year.

“(3) *LIMITATION ON PRO RATA SHARE OF PREVIOUSLY EXCLUDED SUBPART F INCOME WITHDRAWN FROM INVESTMENT.*—For purposes of paragraph (1)(A)(ii), the pro rata share of any United States shareholder of the previously excluded subpart *F* income of a controlled foreign corporation withdrawn from investment in less developed countries shall not exceed an amount (A) which bears the same ratio to his pro rata share of such income withdrawn (as determined under section 955(a)(3)) for the taxable year, as (B) the part of such year during which the corporation is a controlled foreign corporation bears to the entire year.

“(4) *LIMITATION ON PRO RATA SHARE OF INVESTMENT IN UNITED STATES PROPERTY.*—For purposes of paragraph (1)(B), the pro rata share of any United States shareholder in the increase of the earnings of a controlled foreign corporation invested in United States property shall not exceed an amount (A) which bears the same ratio to his pro rata share of such increase (as determined under section 956(a)(2)) for the taxable year, as (B) the part of such year during which

1 *the corporation is a controlled foreign corporation bears*
2 *to the entire year.*

3 “(b) *UNITED STATES SHAREHOLDER DEFINED.—For*
4 *purposes of this subpart, the term ‘United States share-*
5 *holder’ means, with respect to any foreign corporation, a*
6 *United States person (as defined in section 957(d))*
7 *who owns (within the meaning of section 958(a)), or is*
8 *considered as owning by applying the rules of ownership of*
9 *section 958(b), 10 percent or more of the total combined*
10 *voting power of all classes of stock entitled to vote of such*
11 *foreign corporation.*

12 “(c) *COORDINATION WITH ELECTION OF A FOREIGN*
13 *INVESTMENT COMPANY TO DISTRIBUTE INCOME.—A*
14 *United States shareholder who, for his taxable year, is a*
15 *qualified shareholder (within the meaning of section*
16 *1247(c)) of a foreign investment company with respect to*
17 *which an election under section 1247 is in effect shall not*
18 *be required to include in gross income, for such taxable*
19 *year, any amount under subsection (a) with respect to such*
20 *company.*

21 “(d) *COORDINATION WITH FOREIGN PERSONAL*
22 *HOLDING COMPANY PROVISIONS.—A United States share-*
23 *holder who, for his taxable year, is subject to tax under*
24 *section 551(b) (relating to foreign personal holding com-*
25 *pany income included in gross income of United States share-*
26 *holders) on income of a controlled foreign corporation shall*

1 *not be required to include in gross income, for such taxable*
2 *year, any amount under subsection (a) with respect to*
3 *such company.*

4 **"SEC. 952. SUBPART F INCOME DEFINED.**

5 *"(a) IN GENERAL.—For purposes of this subpart,*
6 *the term 'subpart F income' means, in the case of any*
7 *controlled foreign corporation, the sum of—*

8 *"(1) the income derived from the insurance of*
9 *United States risks (as determined under section 953),*
10 *and*

11 *"(2) the foreign base company income (as deter-*
12 *mined under section 954).*

13 *"(b) EXCLUSION OF UNITED STATES INCOME.—Sub-*
14 *part F income does not include any item includible in gross in-*
15 *come under this chapter (other than this subpart) as income*
16 *derived from sources within the United States of a foreign*
17 *corporation engaged in trade or business in the United States.*

18 *"(c) LIMITATION.—For purposes of subsection (a),*
19 *the subpart F income of any controlled foreign corporation*
20 *for any taxable year shall not exceed the earnings and profits*
21 *of such corporation for such year reduced by the amount*
22 *(if any) by which—*

23 *"(1) an amount equal to—*

24 *"(A) the sum of the deficits in earnings and*
25 *profits for prior taxable years beginning after De-*
26 *cember 31, 1962, plus*

1 “(B) the sum of the deficits in earnings and
2 profits for taxable years beginning after December
3 31, 1959, and before January 1, 1963 (reduced
4 by the sum of the earnings and profits for such
5 taxable years); exceeds

6 “(2) an amount equal to the sum of the earnings
7 and profits for prior taxable years beginning after De-
8 cember 31, 1962, allocated to other earnings and profits
9 under section 959(c)(3).

10 For purposes of the preceding sentence, any deficit in earn-
11 ings and profits for any prior taxable year shall be taken into
12 account under paragraph (1) for any taxable year only to
13 the extent it has not been taken into account under such
14 paragraph for any preceding taxable year to reduce earn-
15 ings and profits of such preceding year.

16 “(d) SPECIAL RULE IN CASE OF INDIRECT OWNER-
17 SHIP.—For purposes of subsection (c), if—

18 “(1) a United States shareholder owns (within the
19 meaning of section 958(a)) stock of a foreign corpora-
20 tion, and by reason of such ownership owns (within the
21 meaning of such section) stock of any other foreign cor-
22 poration, and

23 “(2) any of such foreign corporations has a deficit
24 in earnings and profits for the taxable year,
25 then the earnings and profits for the taxable year of each such
26 foreign corporation which is a controlled foreign corpora-

tion shall, with respect to such United States shareholder, be properly reduced to take into account any deficit described in paragraph (2) in such manner as the Secretary or his delegate shall prescribe by regulations.

“SEC. 953. INCOME FROM INSURANCE OF UNITED STATES RISKS.

“(a) *GENERAL RULE.*—For purposes of section 952 (a)(1), the term ‘income derived from the insurance of United States risks’ means that income which—

“(1) is attributable to the reinsurance or the issuing of any insurance or annuity contract—

“(A) in connection with property in, or liability arising out of activity in, or in connection with the lives or health of residents of, the United States, or

“(B) in connection with risks not included in subparagraph (A) as the result of any arrangement whereby another corporation receives a substantially equal amount of premiums or other consideration in respect to any reinsurance or the issuing of any insurance or annuity contract in connection with property in, or liability arising out of activity in, or in connection with the lives or health of residents of, the United States, and

“(2) would (subject to the modifications provided by paragraphs (1), (2), and (3) of subsection (b))

1 *be taxed under subchapter L of this chapter if such*
2 *income were the income of a domestic insurance corpo-*
3 *ration.*

4 *This section shall apply only in the case of a controlled*
5 *foreign corporation which receives, during any taxable year,*
6 *premiums or other consideration in respect of the reinsurance,*
7 *and the issuing, of insurance and annuity contracts described*
8 *in paragraph (1) in excess of 5 percent of the total*
9 *of premiums and other consideration received during such*
10 *taxable year in respect of all reinsurance and issuing of*
11 *insurance and annuity contracts.*

12 “(b) *SPECIAL RULES.*—For purposes of subsection
13 (a)—

14 “(1) *In the application of part I of subchapter L,*
15 *life insurance company taxable income is the gain from*
16 *operations as defined in section 809(b).*

17 “(2) *A corporation which would, if it were a*
18 *domestic insurance corporation, be taxable under part II*
19 *of subchapter L shall apply subsection (a) as if it were*
20 *taxable under part III of subchapter L.*

21 “(3) *The following provisions of subchapter L shall*
22 *not apply:*

23 “(A) *Section 809(d)(4) (operations loss de-*
24 *duction).*

1 “(B) Section 809(d)(5) (certain nonpar-
2 ticipating contracts).

3 “(C) Section 809(d)(6) (group life, accident,
4 and health insurance).

5 “(D) Section 809(d)(10) (small business
6 deduction).

7 “(E) Section 817(b) (gain on property
8 held on December 31, 1958, and certain substituted
9 property acquired after 1958).

10 “(F) Section 832(b)(5) (certain capital
11 losses).

12 “(4) The items referred to in—

13 “(A) section 809(c)(1) (relating to gross
14 amount of premiums and other considerations),

15 “(B) section 809(c)(2) (relating to net
16 decrease in reserves),

17 “(C) section 809(d)(2) (relating to net
18 increase in reserves), and

19 “(D) section 832(b)(4) (relating to pre-
20 miums earned on insurance contracts),

21 shall be taken into account only to the extent they are in
22 respect of any reinsurance or the issuing of any insurance
23 or annuity contract described in subsection (a)(1).

24 “(5) All items of income, expenses, losses, and
25 deductions (other than those taken into account under

paragraph (4)) shall be properly allocated or apportioned under regulations prescribed by the Secretary or his delegate.

“SEC. 954. FOREIGN BASE COMPANY INCOME.

“(a) FOREIGN BASE COMPANY INCOME.—For purposes of section 952(a)(2), the term ‘foreign base company income’ means for any taxable year the sum of—

“(1) the foreign personal holding company income for the taxable year (determined under subsection (c) and reduced as provided in subsection (b)(5)),

“(2) the foreign base company sales income for the taxable year (determined under subsection (d) and reduced as provided in subsection (b)(5)), and

“(3) the foreign base company services income for the taxable year (determined under subsection (e) and reduced as provided in subsection (b)(5)).

“(b) EXCLUSIONS AND SPECIAL RULES.—

“(1) EXCLUSION OF CERTAIN DIVIDENDS, INTEREST, AND GAINS FROM QUALIFIED INVESTMENTS IN LESS DEVELOPED COUNTRIES.—For purposes of subsection (a), foreign base company income does not include—

“(A) dividends and interest received during the taxable year from investments which at the time of receipt are qualified investments in less de-

1 *veloped countries (as defined in section 955(b)),*
2 *or*

3 *“(B) if the gains from the sale or exchange*
4 *during the taxable year of investments which at the*
5 *time of sale or exchange are qualified investments*
6 *in less developed countries exceed the losses from*
7 *the sale or exchange during the taxable year of*
8 *such qualified investments, the amount by which*
9 *such gains exceed such losses.*

10 *The preceding sentence shall apply only to the extent*
11 *that the sum of the dividends and interest described in*
12 *subparagraph (A) and the amount described in sub-*
13 *paragraph (B) does not exceed the increase for the tax-*
14 *able year in qualified investments in less developed*
15 *countries of the controlled foreign corporation (as deter-*
16 *mined under subsection (f)).*

17 *“(2) EXCLUSION OF CERTAIN SHIPPING IN-*
18 *COME.—For purposes of subsection (a), foreign base*
19 *company income does not include income derived from,*
20 *or in connection with, the use (or hiring or leasing for*
21 *use) of any aircraft or vessel in foreign commerce, or*
22 *the performance of services directly related to the use of*
23 *any such aircraft or vessel.*

24 *“(3) SPECIAL RULE WHERE FOREIGN BASE COM-*
25 *PANY IS LESS THAN 30 PERCENT OR MORE THAN 70*

1 *PERCENT OF GROSS INCOME.—For purposes of subsec-*
2 *tion (a)—*

3 “(A) *If the foreign base company income*
4 *(determined without regard to paragraphs (1) and*
5 *(5)) is less than 30 percent of gross income, no part*
6 *of the gross income of the taxable year shall be treated*
7 *as foreign base company income.*

8 “(B) *If the foreign base company income*
9 *(determined without regard to paragraphs (1) and*
10 *(5)) exceeds 70 percent of gross income, the entire*
11 *gross income of the taxable year shall, subject to the*
12 *provisions of paragraphs (1), (2), (4), and (5), be*
13 *treated as foreign base company income.*

14 “(4) *EXCEPTION FOR FOREIGN CORPORATIONS*
15 *NOT AVAILABLE TO REDUCE TAXES.—For purposes of*
16 *subsection (a), foreign base company income does not*
17 *include any item of income received by a controlled*
18 *foreign corporation if it is established to the satisfaction*
19 *of the Secretary or his delegate with respect to such item*
20 *that the creation or organization of the controlled foreign*
21 *corporation receiving such item under the laws of the*
22 *foreign country in which it is incorporated does not have*
23 *the effect of substantial reduction of income, war profits,*
24 *or excess profits taxes or similar taxes.*

25 “(5) *DEDUCTIONS TO BE TAKEN INTO AC-*

1 *COUNT.—For purposes of subsection (a), the foreign*
 2 *personal holding company income, the foreign base*
 3 *company sales income, and the foreign base company*
 4 *services income shall be reduced, under regulations*
 5 *prescribed by the Secretary or his delegate, so as to*
 6 *take into account deductions (including taxes) properly*
 7 *allocable to such income.*

8 *“(c) FOREIGN PERSONAL HOLDING COMPANY IN-*
 9 *COME.—*

10 *“(1) IN GENERAL.—For purposes of subsection*
 11 *(a)(1), the term ‘foreign personal holding company*
 12 *income’ means the foreign personal holding company*
 13 *income (as defined in section 553), modified and ad-*
 14 *justed as provided in paragraphs (2), (3), and (4).*

15 *“(2) RENTS INCLUDED WITHOUT REGARD TO 50*
 16 *PERCENT LIMITATION.—For purposes of paragraph*
 17 *(1), all rents shall be included in foreign personal hold-*
 18 *ing company income without regard to whether or not*
 19 *such rents constitute 50 percent or more of gross income.*

20 *“(3) CERTAIN INCOME DERIVED IN ACTIVE CON-*
 21 *DUCT OF TRADE OR BUSINESS.—For purposes of para-*
 22 *graph (1), foreign personal holding company income*
 23 *does not include—*

24 *“(A) rents and royalties which are derived in*
 25 *the active conduct of a trade or business and which*

are received from a person other than a related person (within the meaning of subsection (d)(3)), or

“(B) dividends, interest, and gains from the sale or exchange of stock or securities derived in the conduct of a banking, financing, or similar business, or derived from the investments made by an insurance company of its unearned premiums or reserves ordinary and necessary for the proper conduct of its insurance business, and which are received from a person other than a related person (within the meaning of subsection (d)(3)).

“(4) CERTAIN INCOME RECEIVED FROM RELATED PERSONS.—For purposes of paragraph (1), foreign personal holding company incomes does not include—

“(A) dividends and interest received from a related person which (i) is organized under the laws of the same foreign country under the laws of which the controlled foreign corporation is created or organized, and (ii) has a substantial part of its assets used in its trade or business located in such same foreign country;

“(B) interest received in the conduct of a banking, financing, or similar business from a related person engaged in the conduct of a banking,

1 *financing, or similar business if the businesses of the*
 2 *recipient and the payor are predominantly with per-*
 3 *sons other than related persons; and*

4 *“(C) rents, royalties, and similar amounts re-*
 5 *ceived from a related person for the use of, or the*
 6 *privilege of using, property within the country under*
 7 *the laws of which the controlled foreign corporation*
 8 *is created or organized.*

9 *“(d) FOREIGN BASE COMPANY SALES INCOME.—*

10 *“(1) IN GENERAL.—For purposes of subsection*
 11 *(a)(2), the term ‘foreign base company sales income’*
 12 *means income (whether in the form of profits, commis-*
 13 *sions, fees, or otherwise) derived in connection with the*
 14 *purchase of personal property from a related person and*
 15 *its sale to any person, the sale of personal property to*
 16 *any person on behalf of a related person, the purchase*
 17 *of personal property from any person and its sale to a*
 18 *related person, or the purchase of personal property*
 19 *from any person on behalf of a related person where—*

20 *“(A) the property which is purchased (or in*
 21 *the case of property sold on behalf of a related per-*
 22 *son, the property which is sold) is manufactured,*
 23 *produced, grown, or extracted outside the country*
 24 *under the laws of which the controlled foreign*
 25 *corporation is created or organized, and*

1 “(B) the property is sold for use, consump-
2 tion, or disposition outside such foreign country, or,
3 in the case of property purchased on behalf of a
4 related person, is purchased for use, consumption,
5 or disposition outside such foreign country.

6 “(2) CERTAIN BRANCH INCOME.—For purposes
7 of determining foreign base company sales income
8 in situations in which the carrying on of activities by a
9 controlled foreign corporation through a branch or simi-
10 lar establishment outside the country of incorporation of
11 the controlled foreign corporation has substantially the
12 same effect as if such branch or similar establishment
13 were a wholly owned subsidiary corporation deriving
14 such income, under regulations prescribed by the Secre-
15 tary or his delegate the income attributable to the carry-
16 ing on of such activities of such branch or similar estab-
17 lishment shall be treated as income derived by a wholly
18 owned subsidiary of the controlled foreign corporation
19 and shall constitute foreign base company sales income
20 of the controlled foreign corporation.

21 “(3) RELATED PERSON DEFINED.—For purposes
22 of this section, a person is a related person with respect
23 to a controlled foreign corporation, if—

24 “(A) such person is an individual, partner-

1 *ship, trust, or estate which controls the controlled*
 2 *foreign corporation;*

3 “(B) such person is a corporation which con-
 4 trols, or is controlled by, the controlled foreign cor-
 5 poration; or

6 “(C) such person is a corporation which is
 7 controlled by the same person or persons which con-
 8 trol the controlled foreign corporation.

9 *For purposes of the preceding sentence, control means*
 10 *the ownership, directly or indirectly, of stock possessing*
 11 *more than 50 percent of the total combined voting*
 12 *power of all classes of stock entitled to vote. For pur-*
 13 *poses of this paragraph, the rules for determining owner-*
 14 *ship of stock prescribed by section 958 shall apply.*

15 “(e) *FOREIGN BASE COMPANY SERVICES INCOME.—*
 16 *For purposes of subsection (a)(3), the term ‘foreign base*
 17 *company services income’ means income (whether in the*
 18 *form of compensation, commissions, fees, or otherwise) de-*
 19 *rived in connection with the performance of technical, man-*
 20 *agerial, engineering, architectural, scientific, skilled, indus-*
 21 *trial, commercial, or like services which—*

22 “(1) *are performed for or on behalf of any related*
 23 *person (within the meaning of subsection (d)(3)), and*

1 “(2) are performed outside the country under the
2 laws of which the controlled foreign corporation is
3 created or organized.

4 The preceding sentence shall not apply to income derived
5 in connection with the performance of services which are di-
6 rectly related to the sale or exchange by the controlled foreign
7 corporation of property manufactured, produced, grown, or
8 extracted by it and which are performed prior to the time of
9 the sale or exchange, or of services directly related to an offer
10 or effort to sell or exchange such property.

11 “(f) INCREASE IN QUALIFIED INVESTMENTS IN LESS
12 DEVELOPED COUNTRIES.—For purposes of subsection (b)
13 (1), the increase for any taxable year in qualified invest-
14 ments in less developed countries of any controlled foreign
15 corporation is the amount by which—

16 “(1) the qualified investments in less developed
17 countries (as defined in section 955(b)) of the con-
18 trolled foreign corporation at the close of the taxable
19 year, exceeds

20 “(2) the qualified investments in less developed
21 countries (as so defined) of the controlled foreign
22 corporation at the close of the preceding taxable year.

1 **"SEC. 955. WITHDRAWAL OF PREVIOUSLY EXCLUDED SUBPART**
2 **F INCOME FROM QUALIFIED INVESTMENT.**

3 **"(a) GENERAL RULES.—**

4 **"(1) AMOUNT WITHDRAWN.—***For purposes of*
5 *this subpart, the amount of previously excluded subpart*
6 *F income of any controlled foreign corporation with-*
7 *drawn from investment in less developed countries for*
8 *any taxable year is an amount equal to the decrease in*
9 *the amount of qualified investments in less developed*
10 *countries of the controlled foreign corporation for such*
11 *year, but only to the extent that the amount of such*
12 *decrease does not exceed an amount equal to—*

13 **"(A) the sum of the amounts excluded under**
14 *section 954(b)(1) from the foreign base company*
15 *income of such corporation for all prior taxable*
16 *years, reduced by*

17 **"(B) the sum of the amounts of previously**
18 *excluded subpart F income withdrawn from invest-*
19 *ment in less developed countries of such corporation*
20 *determined under this subsection for all prior tax-*
21 *able years.*

22 **"(2) DECREASE IN QUALIFIED INVESTMENTS.—**
23 *For purposes of paragraph (1), the amount of the de-*
24 *crease in qualified investments in less developed coun-*

tries of any controlled foreign corporation for any taxable year is the amount by which—

“(A) the amount of qualified investments in less developed countries of the controlled foreign corporation at the close of the preceding taxable year, exceeds

“(B) the amount of qualified investments in less developed countries of the controlled foreign corporation at the close of the taxable year,

to the extent the amount of such decrease does not exceed the sum of the earnings and profits for the taxable year and the earnings and profits accumulated for prior taxable years beginning after December 31, 1962.

For purposes of this paragraph, if qualified investments in less developed countries are disposed of by the controlled foreign corporation during the taxable year, the amount of the decrease in qualified investments in less developed countries of such controlled foreign corporation for such year shall be reduced by an amount equal to the amount (if any) by which the losses on such dispositions during such year exceed the gains on such dispositions during such year.

“(3) PRO RATA SHARE OF AMOUNT WITHDRAWN.—In the case of any United States shareholder,

1 *the pro rata share of the amount of previously excluded*
 2 *subpart F income of any controlled foreign corporation*
 3 *withdrawn from investment in less developed countries*
 4 *for any taxable year is his pro rata share of the amount*
 5 *determined under paragraph (1).*

6 “(b) *QUALIFIED INVESTMENTS IN LESS DEVELOPED*
 7 *COUNTRIES.—*

8 “(1) *IN GENERAL.—*For purposes of this subpart,
 9 *the term ‘qualified investments in less developed coun-*
 10 *tries’ means property which is—*

11 “(A) *stock of a less developed country corpo-*
 12 *ration held by the controlled foreign corporation,*
 13 *but only if the controlled foreign corporation owns*
 14 *10 percent or more of the total combined voting*
 15 *power of all classes of stock of such less developed*
 16 *country corporation;*

17 “(B) *an obligation of a less developed country*
 18 *corporation held by the controlled foreign corpora-*
 19 *tion, which, at the time of its acquisition by the con-*
 20 *trolled foreign corporation, has a maturity of 5 years*
 21 *or more, but only if the controlled foreign corpora-*
 22 *tion owns 10 percent or more of the total combined*
 23 *voting power of all classes of stock of such less*
 24 *developed country corporation; or*

25 “(C) *an obligation of a less developed country.*

1 “(2) *COUNTRY CEASES TO BE LESS DEVELOPED*
2 *COUNTRY.*—*For purposes of this subpart, property which*
3 *would be a qualified investment in less developed coun-*
4 *tries, but for the fact that a foreign country has, after*
5 *the acquisition of such property by the controlled foreign*
6 *corporation, ceased to be a less developed country, shall*
7 *be treated as a qualified investment in less developed*
8 *countries.*

9 “(3) *INVESTMENTS AFTER CLOSE OF YEAR.*—
10 *For purposes of this subpart, a controlled foreign corpo-*
11 *ration may, under regulations prescribed by the Secre-*
12 *tary or his delegate, elect to treat property described in*
13 *paragraph (1) or (2) which was acquired after the close*
14 *of the taxable year and on or before the close of the follow-*
15 *ing taxable year, or on or before such day after the*
16 *close of the following taxable year as such regulations*
17 *may prescribe, as having been acquired on the last day*
18 *of the taxable year.*

19 “(4) *AMOUNT ATTRIBUTABLE TO PROPERTY.*—
20 *The amount taken into account under this subpart with*
21 *respect to any property described in paragraph (1) or*
22 *(2) shall be its adjusted basis, reduced by any liability*
23 *to which such property is subject.*

24 “(c) *LESS DEVELOPED COUNTRY CORPORATIONS.*—

25 “(1) *IN GENERAL.*—*For purposes of this sub-*

1 *part, the term 'less developed country corporation'*
2 *means a foreign corporation which is created or organized*
3 *under the laws of a less developed country and which*
4 *during the taxable year is engaged in the active conduct*
5 *of one or more trades or businesses and—*

6 *“(A) 80 percent or more of the gross income*
7 *of which for the taxable year is derived from sources*
8 *within less developed countries; and*

9 *“(B) 80 percent or more in value of the*
10 *assets of which on each day of the taxable year*
11 *consists of—*

12 *“(i) property used in such trades or busi-*
13 *nesses and located in less developed countries,*

14 *“(ii) money, and deposits with persons*
15 *carrying on the banking business,*

16 *“(iii) stock, and obligations which, at the*
17 *time of their acquisition, have a maturity of 5*
18 *years or more, of any other less developed coun-*
19 *try corporation,*

20 *“(iv) an obligation of a less developed*
21 *country,*

22 *“(v) an investment which is required be-*

1 *cause of restrictions imposed by a less developed*
 2 *country, and*

3 “(vi) *property described in section 956*
 4 *(b)(2).*

5 *For purposes of subparagraph (A), the determination*
 6 *as to whether income is derived from sources within less*
 7 *developed countries shall be made under regulations*
 8 *prescribed by the Secretary or his delegate.*

9 “(2) *SHIPPING COMPANIES.*—*For purposes of this*
 10 *subpart, the term ‘less developed country corporation’*
 11 *also means a foreign corporation—*

12 “(A) *80 percent or more of the gross income of*
 13 *which for the taxable year consists of—*

14 “(i) *gross income derived from, or in con-*
 15 *nection with, the using (or hiring or leasing*
 16 *for use) in foreign commerce of aircraft or*
 17 *vessels registered under the laws of a less de-*
 18 *veloped country, or from, or in connection with,*
 19 *the performance of services directly related to*
 20 *use of such aircraft or vessels, or from the sale*
 21 *or exchange of such aircraft or vessels, and*

22 “(ii) *dividends and interest received from*

1 *foreign corporations which are less developed*
2 *country corporations within the meaning of this*
3 *paragraph and 10 percent or more of the total*
4 *combined voting power of all classes of stock*
5 *of which are owned by the foreign corporation,*
6 *and gain from the sale or exchange of stock or*
7 *obligations of foreign corporations which are*
8 *such less developed country corporations, and*

9 “(B) 80 percent or more of the assets of which
10 *on each day of the taxable year consists of (i) assets*
11 *used, or held for use, for or in connection with the*
12 *production of income described in subparagraph*
13 *(A), and (ii) property described in section*
14 *956(b)(2).*

15 “(3) *LESS DEVELOPED COUNTRY DEFINED.*—For
16 *purposes of this subpart, the term ‘less developed coun-*
17 *try’ means (in respect of any foreign corporation) any*
18 *foreign country (other than an area within the Sino-*
19 *Soviet bloc) or any possession of the United States with*
20 *respect to which, on the first day of the taxable year, there*
21 *is in effect an Executive order by the President of the*
22 *United States designating such country or possession as*
23 *an economically less developed country for purposes of*
24 *this subpart. For purposes of the preceding sentence,*

an overseas territory, department, province, or possession may be treated as a separate country. No designation shall be made under this paragraph with respect to—

<i>Australia</i>	<i>Liechtenstein</i>
<i>Austria</i>	<i>Luxembourg</i>
<i>Belgium</i>	<i>Monaco</i>
<i>Canada</i>	<i>Netherlands</i>
<i>Denmark</i>	<i>New Zealand</i>
<i>France</i>	<i>Norway</i>
<i>Germany (Federal</i>	<i>Union of South Africa</i>
<i>Republic)</i>	<i>San Marino</i>
<i>Hong Kong</i>	<i>Sweden</i>
<i>Italy</i>	<i>Switzerland</i>
<i>Japan</i>	<i>United Kingdom</i>

After the President has designated any foreign country or any possession of the United States as an economically less developed country for purposes of this subpart, he shall not terminate such designation (either by issuing an Executive order for that purpose or by issuing an Executive order under the first sentence of this paragraph which has the effect of terminating such designation) unless, at least 30 days prior to such termination, he has notified the Senate and the House of Representatives of his intention to terminate such designation.

1 **"SEC. 956. INVESTMENT OF EARNINGS IN UNITED STATES**
2 **PROPERTY.**

3 **"(a) GENERAL RULES.—***For purposes of this sub-*
4 *part—*

5 **"(1) AMOUNT OF INVESTMENT.—***The amount of*
6 *earnings of a controlled foreign corporation invested in*
7 *United States property at the close of any taxable year*
8 *is the aggregate amount of such property held, directly*
9 *or indirectly, by the controlled foreign corporation at the*
10 *close of the taxable year, to the extent such amount*
11 *would have constituted a dividend (determined after the*
12 *application of section 955(a)) if it had been distributed.*

13 **"(2) PRO RATA SHARE OF INCREASE FOR YEAR.—**
14 *In the case of any United States shareholder, the pro*
15 *rata share of the increase for any taxable year in the*
16 *earnings of a controlled foreign corporation invested in*
17 *United States property is the amount determined by*
18 *subtracting his pro rata share of—*

19 **"(A) the amount determined under paragraph**
20 *(1) for the close of the preceding taxable year, re-*
21 *duced by amounts paid during such preceding taxable*
22 *year to which section 959(c)(1) applies, from*

23 **"(B) the amount determined under paragraph**
24 *(1) for the close of the taxable year.*

25 *The determinations under subparagraphs (A) and (B)*

shall be made on the basis of stock owned (within the meaning of section 958(a)) by such United States shareholder on the last day during the taxable year on which the foreign corporation is a controlled foreign corporation.

“(3) *AMOUNT ATTRIBUTABLE TO PROPERTY.*—

The amount taken into account under paragraph (1) or (2) with respect to any property shall be its adjusted basis, reduced by any liability to which the property is subject.

“(b) *UNITED STATES PROPERTY DEFINED.*—

“(1) *IN GENERAL.*—For purposes of subsection (a), the term ‘United States property’ means any property acquired after December 31, 1962, which is—

“(A) tangible property located in the United States;

“(B) stock of a domestic corporation;

“(C) an obligation of a United States person;

or

“(D) any right to the use in the United States of—

“(i) a patent or copyright,

“(ii) an invention, model, or design (whether or not patented),

“(iii) a secret formula or process, or

1 “(iv) any other similar property right,
2 which is acquired or developed by the controlled
3 foreign corporation for use in the United States.

4 “(2) EXCEPTIONS.—For purposes of subsection
5 (a), the term ‘United States property’ does not in-
6 clude—

7 “(A) obligations of the United States, money,
8 or deposits with persons carrying on the banking
9 business;

10 “(B) property located in the United States
11 which is purchased in the United States for export
12 to, or use in, foreign countries;

13 “(C) any obligation of a United States per-
14 son arising in connection with the sale or processing
15 of property if the amount of such obligation out-
16 standing at no time during the taxable year exceeds
17 the amount which would be ordinary and necessary
18 to carry on the trade or business of both the other
19 party to the sale or processing transaction and the
20 United States person had the sale or processing
21 transaction been made between unrelated persons;

22 “(D) any aircraft, railroad rolling stock, ves-
23 sel, motor vehicle, or container used in the trans-
24 portation of persons or property in foreign com-

merce and used predominantly outside the United States;

“(E) an amount of assets of an insurance company equivalent to the unearned premiums or reserves ordinary and necessary for the proper conduct of its insurance business attributable to contracts which are not contracts described in section 953(a)(1); and

“(F) an amount of assets of the controlled foreign corporation equal to the earnings and profits accumulated after December 31, 1962, and excluded from subpart F income under section 952(b).

“(c) **PLEDGES AND GUARANTEES.**—For purposes of subsection (a), a controlled foreign corporation shall, under regulations prescribed by the Secretary or his delegate, be considered as holding an obligation of a United States person if such controlled foreign corporation is a pledgor or guarantor of such obligation.

“SEC. 957. CONTROLLED FOREIGN CORPORATIONS; UNITED STATES PERSONS.

“(a) **GENERAL RULE.**—For purposes of this subpart, the term ‘controlled foreign corporation’ means any foreign corporation of which more than 50 percent of the total combined voting power of all classes of stock entitled to vote

1 is owned (within the meaning of section 958(a)), or is
2 considered as owned by applying the rules of ownership of
3 section 958(b), by United States shareholders on any day
4 during the taxable year of such foreign corporation.

5 “(b) *SPECIAL RULE FOR INSURANCE.*—For purposes
6 only of taking into account income described in section 953
7 (a) (relating to income derived from insurance of United
8 States risks), the term ‘controlled foreign corporation’ in-
9 cludes not only a foreign corporation as defined by subsec-
10 tion (a) but also one of which more than 25 percent of the
11 total combined voting power of all classes of stock is owned
12 (within the meaning of section 958(a)), or is considered as
13 owned by applying the rules of ownership of section 958(b),
14 by United States shareholders on any day during the tax-
15 able year of such corporation, if the gross amount of pre-
16 miums or other consideration in respect of the reinsurance or
17 the issuing of insurance or annuity contracts described in sec-
18 tion 953(a)(1) exceeds 75 percent of the gross amount of
19 all premiums or other consideration in respect of all risks.

20 “(c) *CORPORATIONS ORGANIZED IN UNITED STATES*
21 *POSSESSIONS.*—For purposes of this subpart, the term ‘con-
22 trolled foreign corporation’ does not include any corporation
23 created or organized in the Commonwealth of Puerto Rico or
24 a possession of the United States or under the laws of the

1 *Commonwealth of Puerto Rico or a possession of the United*
2 *States if—*

3 “(1) 80 percent or more of the gross income of
4 such corporation (computed without regard to section
5 931) for the 3-year period immediately preceding the
6 close of the taxable year (or for such part of such period
7 immediately preceding the close of such taxable year as
8 may be applicable) was derived from sources within
9 the Commonwealth of Puerto Rico or a possession of
10 the United States; and

11 “(2) 50 percent or more of the gross income of
12 such corporation (computed without regard to section
13 931) for such period, or for such part thereof, was
14 derived from the active conduct within the Common-
15 wealth of Puerto Rico or a possession of the United
16 States of any trades or businesses constituting the manu-
17 facture or processing of goods, wares, merchandise, or
18 other tangible personal property; the processing of agri-
19 cultural or horticultural products or commodities (in-
20 cluding but not limited to livestock, poultry, or fur-
21 bearing animals); the catching or taking of any kind
22 of fish or the mining or extraction of natural resources,
23 or any manufacturing or processing of any products or

1 *commodities obtained from such activities; or the owner-*
2 *ship or operation of hotels.*

3 *For purposes of paragraphs (1) and (2), the deter-*
4 *mination as to whether income was derived from sources*
5 *within the Commonwealth of Puerto Rico or a possession*
6 *of the United States and was derived from the active conduct*
7 *of a described trade or business within the Commonwealth*
8 *of Puerto Rico or a possession of the United States shall*
9 *be made under regulations prescribed by the Secretary or*
10 *his delegate.*

11 “(d) UNITED STATES PERSON.—*For purposes of this*
12 *subpart, the term ‘United States person’ has the meaning*
13 *assigned to it by section 7701(a)(30) except that—*

14 “(1) *with respect to a corporation organized under*
15 *the laws of the Commonwealth of Puerto Rico, such term*
16 *does not include an individual who is a bona fide resident*
17 *of Puerto Rico, if a dividend received by such individual*
18 *during the taxable year from such corporation would,*
19 *for purposes of section 933(1), be treated as income*
20 *derived from sources within Puerto Rico,*

21 “(2) *with respect to a corporation organized under*
22 *the laws of the Virgin Islands, such term does not include*
23 *an individual who is a bona fide resident of the Virgin*
24 *Islands and whose income tax obligation under this*
25 *subtitle for the taxable year is satisfied pursuant to sec-*

tion 28(a) of the Revised Organic Act of the Virgin Islands, approved July 22, 1954 (48 U.S.C. 1642), by paying tax on income derived from all sources both within and outside the Virgin Islands into the treasury of the Virgin Islands, and

“(3) with respect to a corporation organized under the laws of any other possession of the United States, such term does not include an individual who is a bona fide resident of any such other possession and whose income derived from sources within possessions of the United States is not, by reason of section 931(a), includible in gross income under this subtitle for the taxable year.

“SEC. 958. RULES FOR DETERMINING STOCK OWNERSHIP.

“(a) DIRECT AND INDIRECT OWNERSHIP.—

“(1) GENERAL RULE.—For purposes of this subpart (other than sections 955(b)(1) (A) and (B), 955(c)(2)(A)(ii), and 960(a)(1)), stock owned means—

“(A) stock owned directly, and

“(B) stock owned with the application of paragraph (2).

“(2) STOCK OWNERSHIP THROUGH FOREIGN ENTITIES.—For purposes of subparagraph (B) of para-

1 *graph (1), stock owned, directly or indirectly, by or*
2 *for a foreign corporation, foreign partnership, or foreign*
3 *trust or foreign estate (within the meaning of section*
4 *7701(a)(31)) shall be considered as being owned pro-*
5 *portionately by its shareholders, partners, or bene-*
6 *ficiaries. Stock considered to be owned by a person by*
7 *reason of the application of the preceding sentence shall,*
8 *for purposes of applying such sentence, be treated as*
9 *actually owned by such person.*

10 “(3) *SPECIAL RULE FOR MUTUAL INSURANCE*
11 *COMPANIES.—For purposes of applying paragraph (1)*
12 *in the case of a foreign mutual insurance company, the*
13 *term ‘stock’ shall include any certificate entitling the*
14 *holder to voting power in the corporation.*

15 “(b) *CONSTRUCTIVE OWNERSHIP.—For purposes of*
16 *sections 951(b), 954(d)(3), and 957, section 318(a)*
17 *(relating to constructive ownership of stock) shall apply to*
18 *the extent that the effect is to treat any United States per-*
19 *son as a United States shareholder within the meaning of*
20 *section 951(b), to treat a person as a related person within*
21 *the meaning of section 954(d)(3), or to treat a foreign*
22 *corporation as a controlled foreign corporation under section*
23 *957, except that—*

24 “(1) *In applying paragraph (1)(A) of section*
25 *318(a), stock owned by a nonresident alien individual*

(other than a foreign trust or foreign estate) shall not be considered as owned by a citizen or by a resident alien individual.

“(2) In applying the first sentence of subparagraphs (A) and (B), and in applying clause (i) of subparagraph (C), of section 318(a)(2), if a partnership, estate, trust, or corporation owns, directly or indirectly, more than 50 percent of the total combined voting power of all classes of stock entitled to vote of a corporation, it shall be considered as owning all the stock entitled to vote.

“(3) Stock owned by a partnership, estate, trust, or corporation, by reason of the application of the second sentence of subparagraphs (A) and (B), and the application of clause (ii) of subparagraph (C), of section 318(a)(2), shall not be considered as owned by such partnership, estate, trust, or corporation, for purposes of applying the first sentence of subparagraphs (A) and (B), and in applying clause (i) of subparagraph (C), of section 318(a)(2).

“(4) In applying clause (i) of subparagraph (C) of section 318(a)(2), the phrase ‘10 percent’ shall be substituted for the phrase ‘50 percent’ used in subparagraph (C).

“(5) The second sentence of subparagraphs (A)

1 *and (B), and clause (ii) of subparagraph (C), of*
 2 *section 318(a)(2) shall not be applied so as to consider*
 3 *a United States person as owning stock which is owned*
 4 *by a person who is not a United States person.*

5 *“SEC. 959. EXCLUSION FROM GROSS INCOME OF PREVIOUSLY*
 6 *TAXED EARNINGS AND PROFITS.*

7 *“(a) EXCLUSION FROM GROSS INCOME OF UNITED*
 8 *STATES PERSONS.—For purposes of this chapter, the earn-*
 9 *ings and profits for a taxable year of a foreign corporation*
 10 *attributable to amounts which are, or have been, included in*
 11 *the gross income of a United States shareholder under sec-*
 12 *tion 951(a) shall not, when—*

13 *“(1) such amounts are distributed to, or*

14 *“(2) such amounts would, but for this subsection,*
 15 *be included under section 951(a)(1)(B) in the gross*
 16 *income of,*

17 *such shareholder (or any other United States person who*
 18 *acquires from any person any portion of the interest of such*
 19 *United States shareholder in such foreign corporation, but*
 20 *only to the extent of such portion, and subject to such proof*
 21 *of the identity of such interest as the Secretary or his delegate*
 22 *may by regulations prescribe) directly, or indirectly through*
 23 *a chain of ownership described under section 958(a), be*
 24 *again included in the gross income of such United States*
 25 *shareholder (or of such other United States person).*

1 “(b) *EXCLUSION FROM GROSS INCOME OF CERTAIN*
 2 *FOREIGN SUBSIDIARIES.*—For purposes of section 951(a),
 3 the earnings and profits for a taxable year of a controlled
 4 foreign corporation attributable to amounts which are, or
 5 have been, included in the gross income of a United States
 6 shareholder under section 951(a), shall not, when distributed
 7 through a chain of ownership described under section
 8 958(a), be also included in the gross income of another con-
 9 trolled foreign corporation in such chain for purposes of the
 10 application of section 951(a) to such other controlled foreign
 11 corporation with respect to such United States shareholder
 12 (or to any other United States shareholder who acquires
 13 from any person any portion of the interest of such United
 14 States shareholder in the controlled foreign corporation, but
 15 only to the extent of such portion, and subject to such proof
 16 of identity of such interest as the Secretary or his delegate
 17 may prescribe by regulations).

18 “(c) *ALLOCATION OF DISTRIBUTIONS.*—For pur-
 19 poses of subsections (a) and (b), section 316(a) shall be
 20 applied by applying paragraph (2) thereof, and then para-
 21 graph (1) thereof—

22 “(1) first to earnings and profits attributable to
 23 amounts included in gross income under section 951
 24 (a)(1)(B) (or which would have been included ex-
 25 cept for subsection (a)(2) of this section),

1 “(2) then to earnings and profits attributable to
2 amounts included in gross income under section 951
3 (a)(1)(A) (but reduced by amounts not included un-
4 der section 951(a)(1)(B) because of the exclusion in
5 subsection (a)(2) of this section), and

6 “(3) then to other earnings and profits.

7 “(d) *DISTRIBUTIONS EXCLUDED FROM GROSS IN-*
8 *COME NOT TO BE TREATED AS DIVIDENDS.*—Except as
9 provided in section 960(a)(3), any distribution excluded
10 from gross income under subsection (a) shall be treated, for
11 purposes of this chapter, as a distribution which is not a
12 dividend.

13 “SEC. 960. *SPECIAL RULES FOR FOREIGN TAX CREDIT.*

14 “(a) *TAXES PAID BY A FOREIGN CORPORATION.*—

15 “(1) *GENERAL RULE.*—For purposes of subpart
16 A of this part, if there is included, under section 951(a),
17 in the gross income of a domestic corporation any amount
18 attributable to earnings and profits—

19 “(A) of a foreign corporation at least 10 per-
20 cent of the voting stock of which is owned by such
21 domestic corporation, or

22 “(B) of a foreign corporation at least 50 per-
23 cent of the voting stock of which is owned by a foreign
24 corporation at least 10 percent of the voting stock of
25 which is in turn owned by such domestic corporation,

1 *then, under regulations prescribed by the Secretary or*
2 *his delegate, such domestic corporation shall be deemed*
3 *to have paid the same proportion of the total income,*
4 *war profits, and excess profits taxes paid (or deemed*
5 *paid) by such foreign corporation to a foreign country or*
6 *possession of the United States for the taxable year on*
7 *or with respect to the earnings and profits of such foreign*
8 *corporation which the amount of earnings and profits*
9 *of such foreign corporation so included in gross income*
10 *of the domestic corporation bears to—*

11 “(C) if the foreign corporation at least 10
12 percent of the voting stock of which is owned by such
13 domestic corporation referred to in subparagraph
14 (A) or (B) is not a less developed country cor-
15 poration (as defined in section 902(d)) for such
16 taxable year, the entire amount of the earnings and
17 profits of such foreign corporation for such taxable
18 year, or

19 “(D) if the foreign corporation at least 10
20 percent of the voting stock of which is owned by
21 such domestic corporation referred to in subpara-
22 graph (A) or (B) is a less developed country cor-
23 poration (as defined in section 902(d)) for such
24 taxable year, the sum of the entire amount of the
25 earnings and profits of such foreign corporation for

1 *such taxable year and the total income, war profits,*
2 *and excess profits taxes paid by such foreign corpo-*
3 *ration to foreign countries or possessions of the*
4 *United States for such taxable year.*

5 “(2) *TAXES PREVIOUSLY DEEMED PAID BY DO-*
6 *MESTIC CORPORATION.—If a domestic corporation re-*
7 *ceives a distribution from a foreign corporation, any*
8 *portion of which is excluded from gross income under*
9 *section 959, the income, war profits, and excess profits*
10 *taxes paid or deemed paid by such foreign corporation to*
11 *any foreign country or to any possession of the United*
12 *States in connection with the earnings and profits of*
13 *such foreign corporation from which such distribution is*
14 *made shall not be taken into account for purposes of*
15 *section 902, to the extent such taxes were deemed paid*
16 *by a domestic corporation under paragraph (1) for*
17 *any prior taxable year.*

18 “(3) *TAXES PAID BY FOREIGN CORPORATION AND*
19 *NOT PREVIOUSLY DEEMED PAID BY DOMESTIC CORPO-*
20 *RATION.—Any portion of a distribution from a foreign*
21 *corporation received by a domestic corporation which is*
22 *excluded from gross income under section 959(a) shall*
23 *be treated by the domestic corporation as a dividend,*
24 *solely for purposes of taking into account under section*
25 *902 any income, war profits, or excess profits taxes*

1 *paid to any foreign country or to any possession of the*
2 *United States, on or with respect to the accumulated*
3 *profits of such foreign corporation from which such*
4 *distribution is made, which were not deemed paid by*
5 *the domestic corporation under paragraph (1) for any*
6 *prior taxable year.*

7 “(b) *SPECIAL RULES FOR FOREIGN TAX CREDIT IN*
8 *YEAR OF RECEIPT OF PREVIOUSLY TAXED EARNINGS*
9 *AND PROFITS.—*

10 “(1) *INCREASE IN SECTION 904 LIMITATION.—*
11 *In the case of any taxpayer who—*

12 “(A) *either (i) chose to have the benefits of*
13 *subpart A of this part for a taxable year in which*
14 *he was required under section 951(a) to include in*
15 *his gross income an amount in respect of a controlled*
16 *foreign corporation, or (ii) did not pay or accrue*
17 *for such taxable year any income, war profits, or*
18 *excess profits taxes to any foreign country or to any*
19 *possession of the United States, and*

20 “(B) *chooses to have the benefits of subpart*
21 *A of this part for the taxable year in which he re-*
22 *ceives a distribution or amount which is excluded*
23 *from gross income under section 959(a) and which*
24 *is attributable to earnings and profits of the con-*
25 *trolled foreign corporation which was included in*

1 *his gross income for the taxable year referred to in*
 2 *subparagraph (A), and*

3 “(C) for the taxable year in which such dis-
 4 *tribution or amount is received, pays, or is deemed*
 5 *to have paid, or accrues income, war profits, or*
 6 *excess profits taxes to a foreign country or to any*
 7 *possession of the United States with respect to such*
 8 *distribution or amount,*

9 *the applicable limitation under section 904 for the tax-*
 10 *able year in which such distribution or amount is re-*
 11 *ceived shall be increased as provided in paragraph (2),*
 12 *but such increase shall not exceed the amount of such*
 13 *taxes paid, or deemed paid, or accrued with respect to*
 14 *such distribution or amount.*

15 “(2) AMOUNT OF INCREASE.—*The amount of*
 16 *increase of the applicable limitation under section 904*
 17 *(a) for the taxable year in which the distribution or*
 18 *amount referred to in paragraph (1)(B) is received*
 19 *shall be an amount equal to—*

20 “(A) *the amount by which the applicable*
 21 *limitation under section 904(a) for the taxable year*
 22 *referred to in paragraph (1)(A) was increased by*
 23 *reason of the inclusion in gross income under section*
 24 *951(a) of the amount in respect of the controlled*
 25 *foreign corporation, reduced by*

“(B) the amount of any income, war profits, and excess profits taxes paid, or deemed paid, or accrued to any foreign country or possession of the United States which were allowable as a credit under section 901 for the taxable year referred to in paragraph (1)(A) and which would not have been allowable but for the inclusion in gross income of the amount described in subparagraph (A).

“(3) CASES IN WHICH TAXES NOT TO BE ALLOWED AS DEDUCTION.—In the case of any taxpayer who—

“(A) chose to have the benefits of subpart A of this part for a taxable year in which he was required under section 951(a) to include in his gross income an amount in respect of a controlled foreign corporation, and

“(B) does not choose to have the benefits of subpart A of this part for the taxable year in which he receives a distribution or amount which is excluded from gross income under section 959(a) and which is attributable to earnings and profits of the controlled foreign corporation which was included in his gross income for the taxable year referred to in subparagraph (A),

no deduction shall be allowed under section 164 for the

1 *taxable year in which such distribution or amount is*
 2 *received for any income, war profits, or excess profits*
 3 *taxes paid or accrued to any foreign country or to any*
 4 *possession of the United States on or with respect to such*
 5 *distribution or amount.*

6 “(4) *INSUFFICIENT TAXABLE INCOME.*—If an
 7 *increase in the limitation under this subsection exceeds*
 8 *the tax imposed by this chapter for such year, the*
 9 *amount of such excess shall be deemed an overpayment*
 10 *of tax for such year.*

11 “SEC. 961. *ADJUSTMENTS TO BASIS OF STOCK IN CONTROLLED*
 12 *FOREIGN CORPORATION AND OF OTHER PROP-*
 13 *ERTY.*

14 “(a) *INCREASE IN BASIS.*—Under regulations pre-
 15 *scribed by the Secretary or his delegate, the basis of a United*
 16 *States shareholder's stock in a controlled foreign corporation,*
 17 *and the basis of property of a United States shareholder by*
 18 *reason of which he is considered under section 958(a)(2)*
 19 *as owning stock of a controlled foreign corporation, shall be*
 20 *increased by the amount required to be included in his gross*
 21 *income under section 951(a) with respect to such stock or*
 22 *with respect to such property, as the case may be, but only*
 23 *to the extent to which such amount was included in the gross*
 24 *income of such United States shareholder. In the case of a*
 25 *United States shareholder who has made an election under*

1 *section 962 for the taxable year, the increase in basis pro-*
2 *vided by this subsection shall not exceed an amount equal to*
3 *the amount of tax paid under this chapter with respect to the*
4 *amounts required to be included in his gross income under*
5 *section 951(a).*

6 “(b) *REDUCTION IN BASIS.*—

7 “(1) *IN GENERAL.*—Under regulations prescribed
8 by the Secretary or his delegate, the adjusted basis of
9 stock or other property with respect to which a United
10 States shareholder or a United States person receives an
11 amount which is excluded from gross income under sec-
12 tion 959(a) shall be reduced by the amount so excluded.
13 In the case of a United States shareholder who has made
14 an election under section 962 for any prior taxable year,
15 the reduction in basis provided by this paragraph shall
16 not exceed an amount equal to the amount received
17 which is excluded from gross income under section
18 959(a) after the application of section 962(d).

19 “(2) *AMOUNT IN EXCESS OF BASIS.*—To the ex-
20 tent that an amount excluded from gross income under
21 section 959(a) exceeds the adjusted basis of the stock
22 or other property with respect to which it is received,
23 the amount shall be treated as gain from the sale or ex-
24 change of property.

1 **“SEC. 962. ELECTION BY INDIVIDUALS TO BE SUBJECT TO TAX**
2 **AT CORPORATE RATES.**

3 **“(a) GENERAL RULE.**—Under regulations prescribed
4 *by the Secretary or his delegate, in the case of a United*
5 *States shareholder who is an individual and who elects to*
6 *have the provisions of this section apply for the taxable*
7 *year—*

8 **“(1)** *the tax imposed under this chapter on*
9 *amounts which are included in his gross income under*
10 *section 951(a) shall (in lieu of the tax determined*
11 *under section 1) be an amount equal to the tax which*
12 *would be imposed under section 11 if such amounts*
13 *were received by a domestic corporation, and*

14 **“(2)** *for purposes of applying the provisions of*
15 *section 960 (relating to foreign tax credit) such amounts*
16 *shall be treated as if they were received by a domestic*
17 *corporation.*

18 **“(b) ELECTION.**—An election to have the provisions
19 *of this section apply for any taxable year shall be made*
20 *by a United States shareholder at such time and in such*
21 *manner as the Secretary or his delegate shall prescribe by*
22 *regulations. An election made for any taxable year may*
23 *not be revoked except with the consent of the Secretary*
24 *or his delegate.*

25 **“(c) SURTAX EXEMPTION.**—For purposes of applying

1 subsection (a)(1), the surtax exemption provided by section
 2 11(c) shall not exceed, in the case of any United States share-
 3 holder, an amount which bears the same ratio to \$25,000 as
 4 the amounts included in his gross income under section 951
 5 (a) for the taxable year bears to his pro rata share of the
 6 earnings and profits for the taxable year of all controlled
 7 foreign corporations with respect to which such United States
 8 shareholder includes any amount in gross income under
 9 section 951(a).

10 “(d) *SPECIAL RULE FOR ACTUAL DISTRIBUTIONS.*—
 11 The earnings and profits of a foreign corporation attributable
 12 to amounts which were included in the gross income of a
 13 United States shareholder under section 951(a) and with
 14 respect to which an election under this section applied shall,
 15 when such earnings and profits are distributed, notwithstand-
 16 ing the provisions of section 959(a)(1), be included in gross
 17 income to the extent that such earnings and profits so dis-
 18 tributed exceed the amount of tax paid under this chapter on
 19 the amounts to which such election applied.

20 “SEC. 963. RECEIPT OF MINIMUM DISTRIBUTIONS BY DOMES-
 21 TIC CORPORATIONS.

22 “(a) *GENERAL RULE.*—In the case of a United States
 23 shareholder which is a domestic corporation and which con-
 24 sents to all the regulations prescribed by the Secretary or his
 25 delegate under this section prior to the last day prescribed

1 *by law for filing its return of the tax imposed by this chapter*
2 *for the taxable year, no amount shall be included in gross*
3 *income under section 951(a)(1)(A)(i) for the taxable*
4 *year with respect to the subpart F income of a controlled*
5 *foreign corporation, if—*

6 “(1) *in the case of a controlled foreign corpora-*
7 *tion described in subsection (c)(1), the United States*
8 *shareholder receives a minimum distribution of the earn-*
9 *ings and profits for the taxable year of such controlled*
10 *foreign corporation;*

11 “(2) *in the case of controlled foreign corporations*
12 *described in subsection (c)(2), the United States*
13 *shareholder receives a minimum distribution with re-*
14 *spect to the consolidated earnings and profits for the*
15 *taxable year of all such controlled foreign corporations;*
16 *or*

17 “(3) *in the case of controlled foreign corporations*
18 *described in subsection (c)(3), the United States*
19 *shareholder receives a minimum distribution of the con-*
20 *solidated earnings and profits for the taxable year of*
21 *all such controlled foreign corporations.*

22 “(b) *MINIMUM DISTRIBUTIONS.—For purposes of this*
23 *section, a minimum distribution with respect to the earnings*
24 *and profits for the taxable year of any controlled foreign*
25 *corporation or corporations shall, in the case of any United*

1 *States shareholder, be its pro rata share of an amount deter-*
 2 *mined in accordance with the following table:*

<i>"If the effective foreign tax rate is (percentage):</i>	<i>The required minimum dis- tribution of earnings and profits is (percentage):</i>
<i>Under 10-----</i>	<i>90</i>
<i>10 or over but less than 20-----</i>	<i>80</i>
<i>20 or over but less than 30-----</i>	<i>70</i>
<i>30 or over but less than 40-----</i>	<i>60</i>
<i>40 or over but less than 42-----</i>	<i>50</i>
<i>42 or over but less than 44-----</i>	<i>38</i>
<i>44 or over but less than 46-----</i>	<i>26</i>
<i>46 or over but not more than 47-----</i>	<i>14</i>
<i>Over 47-----</i>	<i>0</i>

3 *"(c) AMOUNTS TO WHICH SECTION APPLIES.—*

4 *"(1) FOREIGN SUBSIDIARIES.—Subsection (a) (1)*
 5 *shall apply to amounts which (but for the provisions of*
 6 *this section) would be included in the gross income of the*
 7 *United States shareholder under section 951(a) (1) (A)*
 8 *(i) by reason of its ownership, within the meaning of*
 9 *section 958(a) (1) (A), of stock of a controlled foreign*
 10 *corporation.*

11 *"(2) CHAIN OF CONTROLLED FOREIGN CORPORA-*
 12 *TIONS.—Subsection (a) (2) shall apply to amounts which*
 13 *(but for the provisions of this section) would be included*
 14 *in the gross income of the United States shareholder*
 15 *under section 951(a) (1) (A) (i)—*

16 *"(A) by reason of its ownership, within the*
 17 *meaning of section 958(a) (1) (A), of stock of a*
 18 *controlled foreign corporation, and*

1 “(B) to the extent that the United States share-
 2 holder so elects, by reason of its ownership, within
 3 the meaning of section 958(a)(2), of stock of any
 4 other controlled foreign corporation (on account of
 5 its ownership of the stock described in subparagraph
 6 (A) or of stock described in this subparagraph),
 7 but only if there is taken into account the earnings
 8 and profits of each foreign corporation, whether or
 9 not a controlled foreign corporation, by reason of
 10 which the United States shareholder owns, within the
 11 meaning of section 958(a)(2), stock of such con-
 12 trolled foreign corporation.

13 “(3) ALL CONTROLLED FOREIGN CORPORA-
 14 TIONS.—Except as provided in paragraph (4), subsec-
 15 tion (a)(3) shall apply to amounts which (but for the
 16 provisions of this section) would be included in the gross
 17 income of the United States shareholder under section
 18 951(a)(1)(A)(i)—

19 “(A) by reason of its ownership, within the
 20 meaning of section 958(a)(1)(A), of stock of all
 21 controlled foreign corporations in which it owns
 22 stock within the meaning of such section, and

23 “(B) by reason of its ownership, within the
 24 meaning of section 958(a)(2), of stock of all con-
 25 trolled foreign corporations in which it owns stock

1 *within the meaning of such section, but only if there*
2 *is taken into account the earnings and profits of*
3 *each foreign corporation, whether or not a controlled*
4 *foreign corporation, by reason of which the United*
5 *States shareholder owns, within the meaning of*
6 *section 958(a), stock of any of such controlled*
7 *foreign corporations.*

8 *“(4) EXCEPTIONS AND SPECIAL RULES.—*

9 *“(A) LESS DEVELOPED COUNTRY CORPORA-*
10 *TIONS.—If the United States shareholder so elects,*
11 *subsection (a)(3) and paragraph (3) of this sub-*
12 *section shall not apply to amounts which would be*
13 *included in the gross income of such shareholder*
14 *under section 951(a)(1)(A)(i) by reason of its*
15 *ownership, within the meaning of section 958(a),*
16 *of stock of controlled foreign corporations which are*
17 *less developed country corporations (as defined in*
18 *section 955(c)). This subparagraph shall not*
19 *apply with respect to a less developed country corpo-*
20 *ration if, by reason of the ownership of the stock of*
21 *such corporation, the United States shareholder*
22 *owns, within the meaning of section 958(a)(2),*
23 *stock of any other controlled foreign corporation*
24 *which is not a less developed country corporation.*
25 *Except as provided in the preceding sentence, an*

1 *election under this subparagraph may be made only*
2 *with respect to all controlled foreign corporations*
3 *which are less developed country corporations and*
4 *with respect to which the domestic corporation*
5 *making the election is a United States shareholder.*

6 “(B) *FOREIGN BRANCHES.*—*In applying sub-*
7 *section (a)(3) and paragraph (3) of this subsec-*
8 *tion, if a United States shareholder so elects, all*
9 *branches maintained by such shareholder in foreign*
10 *countries, the Commonwealth of Puerto Rico, or*
11 *possessions of the United States shall, under regula-*
12 *tions prescribed by the Secretary or his delegate, be*
13 *treated as wholly owned subsidiary corporations of*
14 *such shareholder organized under the laws of such*
15 *foreign countries, the Commonwealth of Puerto*
16 *Rico, or possessions of the United States, as the*
17 *case may be. Each branch so treated shall, for*
18 *purposes of this section, be considered to have distrib-*
19 *uted to the United States shareholder all of its*
20 *earnings and profits for the taxable year. This*
21 *subparagraph shall not apply to a branch main-*
22 *tained by a United States shareholder in the Com-*
23 *monwealth of Puerto Rico or a possession of the*
24 *United States unless—*

25 “(i) *such branch would be a controlled*

foreign corporation (as defined in section 957) if it were incorporated under the laws of the Commonwealth of Puerto Rico or the possession of the United States, as the case may be, and

“(ii) the gross income of the United States shareholder for the taxable year includes income derived from sources within the Commonwealth of Puerto Rico and possessions of the United States.

“(C) *BLOCKED FOREIGN INCOME*.—If a United States shareholder so elects, the provisions of subsection (a)(3) and of paragraph (3) of this subsection shall not apply with respect to any foreign corporation, if it is established to the satisfaction of the Secretary or his delegate that the earnings and profits of such foreign corporation could not have been distributed to United States shareholders who own (within the meaning of section 958(a)) stock of such foreign corporation because of currency or other restrictions or limitations imposed under the laws of any foreign country.

“(d) *EFFECTIVE FOREIGN TAX RATE*.—For purposes of this section, the term ‘effective foreign tax rate’ means—

“(1) with respect to a single controlled foreign corporation, the percentage which—

1 “(A) the income, war profits, or excess profits
2 taxes paid or accrued to foreign countries or pos-
3 sessions of the United States by the controlled for-
4 eign corporation for the taxable year on or with re-
5 spect to its earnings and profits for the taxable year,
6 is of

7 “(B) the sum of (i) the earnings and profits
8 of the controlled foreign corporation described in
9 subparagraph (A) and (ii) and the taxes described
10 in subparagraph (A); and

11 “(2) with respect to two or more foreign corpora-
12 tions, the percentage which—

13 “(A) the total income, war profits, or excess
14 profits taxes paid or accrued to foreign countries
15 or possessions of the United States by such foreign
16 corporations for the taxable year on or with respect
17 to the total earnings and profits of such foreign
18 corporations for the taxable year, is of

19 “(B) the sum of (i) the total earnings and
20 profits of such foreign corporations described in
21 subparagraph (A) and (ii) the taxes described in
22 subparagraph (A).

23 For purposes of the preceding sentence, in the case of any
24 United States shareholder, the computation of the effective
25 foreign tax rate applicable with respect to any controlled

1 *foreign corporation or corporations shall be made without*
2 *regard to distributions made by such controlled foreign corpo-*
3 *ration or corporations to such United States shareholder.*

4 “(e) *SPECIAL RULES.—*

5 “(1) *YEAR FROM WHICH DISTRIBUTIONS ARE*
6 *MADE.—For purposes of this section, the second sentence*
7 *of section 902(c)(1) shall apply in determining from the*
8 *earnings and profits of what year distributions are made*
9 *by any foreign corporation, except that the Secretary or*
10 *his delegate may by regulations provide a period in excess*
11 *of 60 days in lieu of the 60-day period prescribed in*
12 *such section.*

13 “(2) *INSUFFICIENT DISTRIBUTIONS.—If—*

14 “(A) *a United States shareholder, in making its*
15 *return of the tax imposed by this chapter for any*
16 *taxable year, applies the provisions of this section*
17 *with respect to any controlled foreign corporation,*

18 “(B) *it is subsequently determined that this*
19 *section did not apply with respect to such controlled*
20 *foreign corporation for such taxable year due to the*
21 *failure of the United States shareholder to receive a*
22 *minimum distribution with respect to such controlled*
23 *foreign corporation, and*

24 “(C) *such failure is due to reasonable cause,*
25 *then a subsequent distribution made with respect*

1 *to such controlled foreign corporation may, if made*
2 *at a time and in a manner prescribed by the Secretary*
3 *or his delegate by regulations, be treated, for purposes of*
4 *this chapter, as having been made for, and received*
5 *in, the taxable year of the United States shareholder*
6 *for which such shareholder applied the provisions of*
7 *this section.*

8 “(3) *AFFILIATED GROUPS OF CORPORATIONS.—*
9 *An affiliated group of corporations which is eligible to*
10 *make a consolidated return under section 1501 for the*
11 *taxable year, may, if it so elects, be treated as a single*
12 *United States shareholder for purposes of applying this*
13 *section for the taxable year.*

14 “(f) *REGULATIONS.—The Secretary or his delegate*
15 *shall prescribe such regulations as he may deem necessary to*
16 *carry out the provisions of this section, including regulations*
17 *for the determination of the amount of foreign tax credit*
18 *in the case of distributions with respect to the earnings and*
19 *profits of two or more foreign corporations.*

20 “SEC. 964. *MISCELLANEOUS PROVISIONS.*

21 “(a) *EARNINGS AND PROFITS.—For purposes of this*
22 *subpart, the earnings and profits of any foreign corporation,*
23 *and the deficit in earnings and profits of any foreign corpora-*
24 *tion, for any taxable year shall be determined according to*
25 *rules substantially similar to those applicable to domestic*

1 corporations, under regulations prescribed by the Secretary
2 or his delegate.

3 “(b) *BLOCKED FOREIGN INCOME.*—Under regulations
4 prescribed by the Secretary or his delegate, no part of the
5 earnings and profits of a controlled foreign corporation for
6 any taxable year shall be included in earnings and profits for
7 purposes of sections 952, 955, and 956, if it is established to
8 the satisfaction of the Secretary or his delegate that such part
9 could not have been distributed by the controlled foreign
10 corporation to United States shareholders who own (within
11 the meaning of section 958(a)) stock of such controlled
12 foreign corporation because of currency or other restrictions
13 or limitations imposed under the laws of any foreign country.

14 “(c) *RECORDS AND ACCOUNTS OF UNITED STATES*
15 *SHAREHOLDERS.*—

16 “(1) *RECORDS AND ACCOUNTS TO BE MAIN-*
17 *TAINED.*—The Secretary or his delegate may by regula-
18 tions require each person who is, or has been, a United
19 States shareholder of a controlled foreign corporation
20 to maintain such records and accounts as may be pre-
21 scribed by such regulations as necessary to carry out
22 the provisions of this subpart and subpart G.

23 “(2) *TWO OR MORE PERSONS REQUIRED TO*
24 *MAINTAIN OR FURNISH THE SAME RECORDS AND*
25 *ACCOUNTS WITH RESPECT TO THE SAME FOREIGN COR-*

1 *PORATION.—Where, but for this paragraph, two or more*
 2 *United States persons would be required to maintain or*
 3 *furnish the same records and accounts as may by regula-*
 4 *tions be required under paragraph (1) with respect to*
 5 *the same controlled foreign corporation for the same*
 6 *period, the Secretary or his delegate may by regulations*
 7 *provide that the maintenance or furnishing of such*
 8 *records and accounts by only one such person shall satisfy*
 9 *the requirements of paragraph (1) for such other*
 10 *persons.*

11 **“Subpart G—Export Trade Corporations**

“Sec. 970. Reduction of subpart F income of export trade corporations.

“Sec. 971. Definitions.

“Sec. 972. Consolidation of group of export trade corporations.

12 **“SEC. 970. REDUCTION OF SUBPART F INCOME OF EXPORT**
 13 **TRADE CORPORATIONS.**

14 **“(a) EXPORT TRADE INCOME CONSTITUTING FOR-**
 15 **EIGN BASE COMPANY INCOME.—**

16 **“(1) IN GENERAL.—***In the case of a controlled*
 17 *foreign corporation (as defined in section 957) which*
 18 *for the taxable year is an export trade corporation, the*
 19 *subpart F income (determined without regard to this*
 20 *subpart) of such corporation for such year shall be*
 21 *reduced by an amount equal to so much of the export*
 22 *trade income (as defined in section 971(b)) of such*

1 corporation for such year as constitutes foreign base
2 company income (as defined in section 954), but only
3 to the extent that such amount does not exceed whichever
4 of the following amounts is the lesser:

5 “(A) an amount equal to $1\frac{1}{2}$ times so much of
6 the export promotion expenses (as defined in section
7 971(d)) of such corporation for such year as is
8 properly allocable to the export trade income which
9 constitutes foreign base company income of such
10 corporation for such year, or

11 “(B) an amount equal to 10 percent of so much
12 of the gross receipts for such year (or, in the case
13 of gross receipts arising from commissions, fees, or
14 other compensation for its services, so much of the
15 gross amount upon the basis of which such commis-
16 sions, fees, or other compensation is computed) ac-
17 cruing to such export trade corporation from the sale,
18 installation, operation, maintenance, or use of prop-
19 erty in respect of which such corporation derives
20 export trade income as is properly allocable to the
21 export trade income which constitutes foreign base
22 company income of such corporation for such year.
23 The allocations with respect to export trade income which
24 constitutes foreign base company income under sub-

1 paragraphs (A) and (B) shall be made under regula-
 2 tions prescribed by the Secretary or his delegate.

3 “(2) OVERALL LIMITATION.—The reduction under
 4 paragraph (1) for any taxable year shall not exceed
 5 an amount which bears the same ratio to the increase
 6 in the investments in export trade assets (as defined in
 7 section 971(c)) of such corporation for such year as
 8 the export trade income which constitutes foreign base
 9 company income of such corporation for such year bears
 10 to the entire export trade income of such corporation
 11 for such year.

12 “(b) INCLUSION OF CERTAIN PREVIOUSLY EXCLUDED
 13 AMOUNTS.—Each United States shareholder of a controlled
 14 foreign corporation which for any prior taxable year was an
 15 export trade corporation shall include in his gross income
 16 under section 951(a)(1)(A)(ii), as an amount to which sec-
 17 tion 955 (relating to withdrawal of previously excluded sub-
 18 part F income from qualified investment) applies, his pro rata
 19 share of the amount of decrease in the investments in export
 20 trade assets of such corporation for such year, but only to
 21 the extent that his pro rata share of such amount does not
 22 exceed an amount equal to—

23 “(1) his pro rata share of the sum of (A) the
 24 amounts by which the subpart F income of such cor-
 25 poration was reduced for all prior taxable years under
 26 subsection (a), and (B) the amounts not included in

subpart F income (determined without regard to this subpart) for all prior taxable years by reason of the application of section 972, reduced by

“(2) the sum of the amounts which were included in his gross income under section 951(a)(1)(A)(ii) under the provisions of this subsection for all prior taxable years.

“(c) INVESTMENTS IN EXPORT TRADE ASSETS.—

“(1) AMOUNT OF INVESTMENTS.—For purposes of this section, the amount taken into account with respect to any export trade asset shall be its adjusted basis, reduced by any liability to which the asset is subject.

“(2) INCREASE IN INVESTMENTS IN EXPORT TRADE ASSETS.—For purposes of subsection (a), the amount of increase in investments in export trade assets of any controlled foreign corporation for any taxable year is the amount by which—

“(A) the amount of such investments at the close of the taxable year, exceeds

“(B) the amount of such investments at the close of the preceding taxable year.

“(3) DECREASE IN INVESTMENTS IN EXPORT TRADE ASSETS.—For purposes of subsection (b), the amount of decrease in investments in export trade assets

1 *of any controlled foreign corporation for any taxable*
 2 *year is the amount by which—*

3 *“(A) the amount of such investments at the*
 4 *close of the preceding taxable year (reduced by an*
 5 *amount equal to the amount of net loss sustained*
 6 *during the taxable year with respect to export trade*
 7 *assets), exceeds*

8 *“(B) the amount of such investments at the*
 9 *close of the taxable year.*

10 *“(4) SPECIAL RULE.—A United States shareholder*
 11 *of an export trade corporation may, under regulations*
 12 *prescribed by the Secretary or his delegate, make the*
 13 *determinations under paragraphs (2) and (3) as of the*
 14 *close of the 75th day after the close of the years referred*
 15 *to in such paragraphs in lieu of on the last day of such*
 16 *years. An election under this paragraph made with*
 17 *respect to any taxable year shall apply to such year and*
 18 *to all succeeding taxable years unless the Secretary or*
 19 *his delegate consents to the revocation of such election.*

20 *“SEC. 971. DEFINITIONS.*

21 *“(a) EXPORT TRADE CORPORATION.—For pur-*
 22 *poses of this subpart, the term ‘export trade corporation’*
 23 *means—*

24 *“(1) IN GENERAL.—A controlled foreign corpora-*

tion (as defined in section 957) which satisfies the following conditions:

“(A) 90 percent or more of the gross income of such corporation for the 3-year period immediately preceding the close of the taxable year (or such part of such period subsequent to the effective date of this subpart during which the corporation was in existence) was derived from sources without the United States, and

“(B) 75 percent or more of the gross income of such corporation for such period constituted gross income in respect of which such corporation derived export trade income.

“(2) SPECIAL RULE.—If 50 percent or more of the gross income of a controlled foreign corporation in the period specified in subsection (a)(1)(A) is gross income in respect of which such corporation derived export trade income in respect of agricultural products grown in the United States, it may qualify as an export trade corporation although it does not meet the requirements of subsection (a)(1)(B).

“(b) EXPORT TRADE INCOME.—For the purposes of this subpart, the term ‘export trade income’ means net income from—

1 “(1) the sale to an unrelated person for use, con-
2 sumption, or disposition outside the United States of
3 export property (as defined in subsection (e)), or from
4 commissions, fees, compensation, or other income from
5 the performance of commercial, industrial, financial,
6 technical, scientific, managerial, engineering, architec-
7 tural, skilled, or other services in respect of such sales
8 or in respect of the installation or maintenance of such
9 export property;

10 “(2) commissions, fees, compensation, or other
11 income from commercial, industrial, financial, technical,
12 scientific, managerial, engineering, architectural, skilled,
13 or other services performed in connection with the use
14 by an unrelated person outside the United States of
15 patents, copyrights, secret processes and formulas, good-
16 will, trademarks, trade brands, franchises, and other like
17 property acquired or developed and owned by the manu-
18 facturer, producer, grower, or extractor of export prop-
19 erty in respect of which the export trade corporation
20 earns export trade income under paragraph (1);

21 “(3) commissions, fees, rentals, or other compensa-
22 tion or income attributable to the use of export property
23 by an unrelated person or attributable to the use of

export property in the rendition of technical, scientific,
or engineering services to an unrelated person; and

“(4) interest from export trade assets described in
subsection (c)(4).

For purposes of paragraph (3), if a controlled foreign corporation receives income from an unrelated person attributable to the use of export property in the rendition of services to such unrelated person together with income attributable to the rendition of other services to such unrelated person, including personal services, the amount of such aggregate income which shall be considered to be attributable to the use of the export property shall (if such amount cannot be established by reference to transactions between unrelated persons) be that part of such aggregate income which the cost of the export property consumed in the rendition of such services (including a reasonable allowance for depreciation) bears to the total costs and expenses attributable to such aggregate income.

“(c) *EXPORT TRADE ASSETS*.—For purposes of this subpart, the term ‘export trade assets’ means—

“(1) working capital reasonably necessary for the production of export trade income,

1 “(2) inventory of export property held for use,
2 consumption, or disposition outside the United States,

3 “(3) facilities located outside the United States for
4 the storage, handling, transportation, packaging, or
5 servicing of export property, and

6 “(4) evidences of indebtedness executed by persons,
7 other than related persons, in connection with payment
8 for purchases of export property for use, consumption, or
9 disposition outside the United States, or in connection
10 with the payment for services described in subsections
11 (b) (2) and (3).

12 “(d) *EXPORT PROMOTION EXPENSES.*—For pur-
13 poses of this subpart, the term ‘export promotion expenses’
14 means the following expenses paid or incurred in the receipt
15 or production of export trade income—

16 “(1) a reasonable allowance for salaries or other
17 compensation for personal services actually rendered for
18 such purpose,

19 “(2) rentals or other payments for the use of prop-
20 erty actually used for such purpose,

21 “(3) a reasonable allowance for the exhaustion,
22 wear and tear, or obsolescence of property actually used
23 for such purpose, and

24 “(4) any other ordinary and necessary expenses of

1 *the corporation to the extent reasonably allocable to the*
 2 *receipt or production of export trade income.*

3 *No expense incurred within the United States shall be treated*
 4 *as an export promotion expense within the meaning of the*
 5 *preceding sentence, unless at least 90 percent of each cate-*
 6 *gory of expenses described in such sentence is incurred out-*
 7 *side the United States.*

8 “(e) *EXPORT PROPERTY.*—*For purposes of this sub-*
 9 *part, the term ‘export property’ means any property or any*
 10 *interest in property manufactured, produced, grown, or ex-*
 11 *tracted in the United States.*

12 “(f) *UNRELATED PERSON.*—*For purposes of this sub-*
 13 *part, the term ‘unrelated person’ means a person other than a*
 14 *related person as defined in section 954(d)(3).*

15 “*SEC. 972. CONSOLIDATION OF GROUP OF EXPORT TRADE*
 16 *CORPORATIONS.*

17 “*For purposes of this subpart and subpart F of this*
 18 *part, a United States shareholder of a controlled foreign cor-*
 19 *poration which is an export trade corporation may, under*
 20 *regulations prescribed by the Secretary or his delegate, treat*
 21 *as a single controlled foreign corporation—*

22 “(1) *such controlled foreign corporation,*

23 “(2) *all controlled foreign corporations which are*
 24 *export trade corporations and 80 percent or more of*

1 *the total combined voting power of all classes of stock*
 2 *entitled to vote of which is owned by such controlled*
 3 *foreign corporation; and*

4 *“(3) all controlled foreign corporations which are*
 5 *export trade corporations and 80 percent or more of*
 6 *the total combined voting power of all classes of stock*
 7 *entitled to vote of which is owned by controlled for-*
 8 *ign corporations described in paragraph (2).”*

9 ***(b) TECHNICAL AND CLERICAL AMENDMENTS.—***

10 ***(1) Section 901 (relating to foreign tax credit)***
 11 ***is amended by striking out “section 902” and inserting in***
 12 ***lieu thereof “sections 902 and 960”.***

13 ***(2) Section 904(g) (as redesignated by section***
 14 ***10(a) of this Act) is amended to read as follows:***

15 ***“(g) CROSS REFERENCES.—***

“(1) For increase of applicable limitation under sub-
section (a) for taxes paid with respect to amounts re-
ceived which were included in the gross income of the
taxpayer for a prior taxable year as a United States
shareholder with respect to a controlled foreign corpora-
tion, see section 960(b).

“(2) For special rule relating to the application of the
credit provided by section 901 in the case of affiliated
groups which include Western Hemisphere trade corpo-
rations for years in which the limitation provided by
subsection (a)(2) applies, see section 1503(d).”

1 (3) *The table of subparts for part III of sub-*
2 *chapter N of chapter 1 is amended by adding at the end*
3 *thereof the following:*

“Subpart F. Controlled foreign corporations.

“Subpart G. Export trade corporations.”

4 (4) *Section 1016(a) (relating to adjustments to*
5 *basis) is amended by adding after paragraph (19) (as*
6 *added by section 2(f) of this Act) the following new*
7 *paragraph:*

8 *“(20) to the extent provided in section 961 in the*
9 *case of stock in controlled foreign corporations (or for-*
10 *ign corporations which were controlled foreign cor-*
11 *porations) and of property by reason of which a person*
12 *is considered as owning such stock.”*

13 (c) *EFFECTIVE DATE.*—*The amendments made by*
14 *this section shall apply with respect to taxable years of foreign*
15 *corporations beginning after December 31, 1962, and to*
16 *taxable years of United States shareholders within which or*
17 *with which such taxable years of such foreign corporations*
18 *end.*

1 SEC. 14 13. GAIN FROM DISPOSITIONS OF CERTAIN DE-
2 PRECIABLE PROPERTY.

3 (a) IN GENERAL.—

4 (1) Part IV of subchapter P of chapter 1 (relating
5 to special rules for determining capital gains and losses)
6 is amended by adding at the end thereof the following
7 new section:

8 “SEC. 1245. GAIN FROM DISPOSITIONS OF CERTAIN DE-
9 PRECIABLE PROPERTY.

10 “(a) GENERAL RULE.—

11 “(1) ORDINARY INCOME.—Except as otherwise
12 provided in this section, if section 1245 property is dis-
13 posed of after the date of the enactment of the Revenue
14 Act of 1962 *during a taxable year beginning after*
15 *December 31, 1962*, the amount by which the lower of—

16 “(A) the recomputed basis of the property, or

17 “(B) (i) in the case of a sale, exchange, or
18 involuntary conversion, the amount realized, or

19 “(ii) in the case of any other disposition, the
20 fair market value of such property,

21 exceeds the adjusted basis of such property shall be
22 treated as gain from the sale or exchange of property
23 which is neither a capital asset nor property described in
24 section 1231. Such gain shall be recognized notwith-
25 standing any other provision of this subtitle.

“(2) RECOMPUTED BASIS.—For purposes of this section, the term ‘recomputed basis’ means, with respect to any property, its adjusted basis recomputed by adding thereto all adjustments, ~~for taxable years beginning~~ *attributable to periods* after December 31, 1961, reflected in such adjusted basis on account of deductions (whether in respect of the same or other property) allowed or allowable to the taxpayer or to any other person for depreciation, or for amortization under section 168. For purposes of the preceding sentence, if the taxpayer can establish by adequate records or other sufficient evidence that the amount allowed for depreciation, or for amortization under section 168, for any ~~taxable year~~ *period* was less than the amount allowable, the amount added for such ~~taxable year~~ *period* shall be the amount allowed.

“(3) SECTION 1245 PROPERTY.—For purposes of this section, the term ‘section 1245 property’ means any property (other than livestock) which is or has been property of a character subject to the allowance for depreciation provided in section 167 and is either—

“(A) personal property, or

“(B) other property (not including a building or its structural components) but only if such other property is tangible and has an adjusted basis in which there are reflected adjustments described in

1 paragraph (2) for a period in which such prop-
2 erty (or other property) —

3 “(i) was used as an integral part of manu-
4 facturing, production, or extraction or of fur-
5 nishing transportation, communications, electri-
6 cal energy, gas, water, or sewage disposal serv-
7 ices, or

8 “(ii) constituted research or storage facili-
9 ties used in connection with any of the activi-
10 ties referred to in clause (i).

11 “(b) EXCEPTIONS AND LIMITATIONS.—

12 “(1) GIFTS.—Subsection (a) shall not apply to a
13 disposition by gift.

14 “(2) TRANSFERS AT DEATH.—Except as provided
15 in section 691 (relating to income in respect of a de-
16 cedent), subsection (a) shall not apply to a transfer at
17 death.

18 “(3) CERTAIN TAX-FREE TRANSACTIONS.—If the
19 basis of property in the hands of a transferee is deter-
20 mined by reference to its basis in the hands of the trans-
21 feror by reason of the application of section 332, 351,
22 361, 371 (a), 374 (a), 721, or 731, then the amount of
23 gain taken into account by the transferor under subsec-
24 tion (a) (1) shall not exceed the amount of gain recog-
25 nized to the transferor on the transfer of such property

(determined without regard to this section). This paragraph shall not apply to a disposition to an organization (other than a cooperative described in section 521) which is exempt from the tax imposed by this chapter.

“(4) LIKE KIND EXCHANGES; INVOLUNTARY CONVERSIONS, ETC.—If property is disposed of and gain (determined without regard to this section) is not recognized in whole or in part under section 1031 or 1033, then the amount of gain taken into account by the transferor under subsection (a) (1) shall not exceed the sum of—

“(A) the amount of gain recognized on such disposition (determined without regard to this section), plus

“(B) the fair market value of property acquired which is not section 1245 property and which is not taken into account under subparagraph (A).

“(5) SECTION 1071 AND 1081 TRANSACTIONS.—Under regulations prescribed by the Secretary or his delegate, rules consistent with paragraphs (3) and (4) of this subsection shall apply in the case of transactions described in section 1071 (relating to gain from sale or exchange to effectuate policies of FCC) or section 1081 (relating to exchanges in obedience to SEC orders).

1 “(6) PROPERTY DISTRIBUTED BY A PARTNERSHIP
2 TO A PARTNER.—

3 “(A) IN GENERAL.—For purposes of this sec-
4 tion, the basis of section 1245 property distributed
5 by a partnership to a partner shall be deemed to
6 be determined by reference to the adjusted basis of
7 such property to the partnership.

8 “(B) ADJUSTMENTS ADDED BACK.—In the
9 case of any property described in subparagraph
10 (A), for purposes of computing the recomputed
11 basis of such property the amount of the adjustments
12 added back for periods before the distribution by
13 the partnership shall be—

14 “(i) the amount of the gain to which sub-
15 section (a) would have applied if such property
16 had been sold by the partnership immediately
17 before the distribution at its fair market value
18 at such time, reduced by

19 “(ii) the amount of such gain to which
20 section 751 (b) applied.

21 “(c) ADJUSTMENTS TO BASIS.—The Secretary or his
22 delegate shall prescribe such regulations as he may deem
23 necessary to provide for adjustments to the basis of property
24 to reflect gain recognized under subsection (a).

1 “(d) APPLICATION OF SECTION.—This section shall
2 apply notwithstanding any other provision of this subtitle.”

3 (2) The table of sections for such part IV is
4 amended by adding at the end thereof the following:

“Sec. 1245. Gain from dispositions of certain depreciable
property.”

5 (b) CHANGE IN METHOD OF DEPRECIATION.—Sub-
6 section (e) of section 167 (relating to depreciation) is
7 amended to read as follows:

8 “(e) CHANGE IN METHOD.—

9 “(1) CHANGE FROM DECLINING BALANCE
10 METHOD.—In the absence of an agreement under sub-
11 section (d) containing a provision to the contrary, a
12 taxpayer may at any time elect in accordance with regu-
13 lations prescribed by the Secretary or his delegate to
14 change from the method of depreciation described in
15 subsection (b) (2) to the method described in subsec-
16 tion (b) (1).

17 “(2) CHANGE WITH RESPECT TO SECTION 1245
18 PROPERTY.—A taxpayer may, ~~within~~ such period after
19 the date of the enactment of the Revenue Act of 1962
20 *on or before the last day prescribed by law (including*
21 *extensions thereof) for filing his return for his first tax-*
22 *able year beginning after December 31, 1962, and in*
23 *such manner as the Secretary or his delegate shall by*

1 regulations prescribe, elect to change his method of
 2 depreciation in respect of section 1245 property (as
 3 defined in section 1245 (a) (3)) from any declining
 4 balance or sum of the years-digits method to the
 5 straight line method. An election may be made under
 6 this paragraph notwithstanding any provision to the
 7 contrary in an agreement under subsection (d)."

8 (c) SALVAGE VALUE OF PERSONAL PROPERTY.—

9 (1) AMOUNT TAKEN INTO ACCOUNT.—Section
 10 167 (relating to depreciation) is amended by redesignat-
 11 ing subsections (f), (g), and (h) as (g), (h), and
 12 (i), respectively, and by inserting after subsection (e)
 13 the following new subsection:

14 "(f) SALVAGE VALUE.—

15 "(1) GENERAL RULE.—Under regulations pre-
 16 scribed by the Secretary or his delegate, a taxpayer may,
 17 for purposes of computing the allowance under sub-
 18 section (a) with respect to personal property, reduce
 19 the amount taken into account as salvage value by an
 20 amount which does not exceed 10 percent of the basis
 21 of such property (as determined under subsection (g)
 22 as of the time as of which such salvage value is required
 23 to be determined).

24 "(2) PERSONAL PROPERTY DEFINED.—For pur-

1 poses of this subsection, the term ‘personal property’
 2 means depreciable personal property (other than live-
 3 stock) with a useful life of 3 years or more acquired after
 4 the date of the enactment of the Revenue Act of 1962.”

5 (2) CONFORMING AMENDMENTS.—

6 (A) Sections 179 (d) (5) and 642 (e) are
 7 each amended by striking out “167 (g)” and in-
 8 serting in lieu thereof “167 (h)”.

9 (B) Section 179 (d) (8) is amended by strik-
 10 ing out “167 (f)” and inserting in lieu thereof
 11 “167 (g)”.

12 (d) SPECIAL RULE FOR CHARITABLE CONTRIBUTIONS
 13 OF SECTION 1245 PROPERTY.—Section 170 (relating to
 14 charitable, etc., contributions and gifts) is amended by re-
 15 designating subsections (e) and (f) as (f) and (g), re-
 16 spectively, and by inserting after subsection (d) the follow-
 17 ing new subsection:

18 “(e) SPECIAL RULE FOR CHARITABLE CONTRIBU-
 19 TIONS OF SECTION 1245 PROPERTY.—The amount of any
 20 charitable contribution taken into account under this section
 21 shall be reduced by the amount which would have been
 22 treated as gain to which section 1245 (a) applies if the prop-
 23 erty contributed had been sold at its fair market value
 24 (determined at the time of such contribution).”

1 *(e) COMPUTATION OF TAXABLE INCOME FOR PUR-*
 2 *POSES OF LIMITATION ON PERCENTAGE DEPLETION*
 3 *DEDUCTION.—Section 613(a) (relating to percentage deple-*
 4 *tion) is amended by inserting after the second sentence thereof*
 5 *the following new sentence: “For purposes of the preceding*
 6 *sentence, the allowable deductions taken into account with*
 7 *respect to expenses of mining in computing the taxable in-*
 8 *come from the property shall be decreased by an amount*
 9 *equal to so much of any gain which (1) is treated*
 10 *under section 1245 (relating to gain from disposition*
 11 *of certain depreciable property) as gain from the sale or ex-*
 12 *change of property which is neither a capital asset nor prop-*
 13 *erty described in section 1231, and (2) is properly allocable*
 14 *to the property.”*

15 ~~(e)~~ *(f) TECHNICAL AMENDMENTS.—*

16 *(1) SPECIAL RULE FOR PARTNERSHIPS.—Section*
 17 *751 (c) (relating to definition of “unrealized receiv-*
 18 *ables” for purposes of subchapter K) is amended by*
 19 *adding after paragraph (2) the following:*

20 *“For purposes of this section and sections 731, 736, and*
 21 *741, such term also includes section 1245 property (as de-*
 22 *finied in section 1245 (a) (3)), but only to the extent of the*
 23 *amount which would be treated as gain to which section*
 24 *1245 (a) would apply if (at the time of the transaction de-*

1 scribed in this section or section 731, 736, or 741, as the
2 case may be) such property had been sold by the partner-
3 ship at its fair market value.”

4 (2) CORPORATE DISTRIBUTION OF PROPERTY.—
5 Subsections (b) and (d) of section 301 (relating to
6 amount distributed) are each amended by striking out
7 “subsection (b) or (c) of section 311” and inserting in
8 lieu thereof “subsection (b) or (c) of section 311 or
9 under section 1245 (a)”.

10 (3) EFFECT ON EARNINGS AND PROFITS.—Section
11 312 (c) (3) (relating to adjustments of earnings and
12 profits) is amended by striking out “subsection (b)
13 or (c) of section 311” and inserting in lieu thereof
14 “subsection (b) or (c) of section 311 or under sec-
15 tion 1245 (a)”.

16 (4) COLLAPSIBLE CORPORATIONS.—Section 341
17 (e) (relating to collapsible corporations) is amended
18 by inserting after paragraph (11) the following new
19 paragraph:

20 “(12) NONAPPLICATION OF SECTION 1245(a).—
21 For purposes of this subsection, the determination of
22 whether gain from the sale or exchange of property
23 would under any provision of this chapter be considered
24 as gain from the sale or exchange of property which is

1 neither a capital asset nor property described in section
 2 1231 (b) shall be made without regard to the applica-
 3 tion of section 1245 (a).”

4 (5) INSTALLMENT OBLIGATIONS IN CERTAIN
 5 LIQUIDATIONS.—

6 (A) Section 453 (d) (4) (A) (relating to
 7 distribution of installment obligations in section 332
 8 liquidations) is amended by adding at the end there-
 9 of the following new sentence: “If the basis of the
 10 property of the liquidating corporation in the hands
 11 of the distributee is determined under section 334
 12 (b) (2) then the preceding sentence shall not apply
 13 to the extent that under paragraph (1) gain to the
 14 distributing corporation would be considered as gain
 15 to which section 1245 (a) applies.”

16 (B) Section 453 (d) (4) (B) (relating to dis-
 17 tribution of installment obligations in liquidations
 18 to which section 337 applies) is amended by adding
 19 at the end thereof the following new sentence: “The
 20 preceding sentence shall not apply to the extent that
 21 under paragraph (1) gain to the distributing cor-
 22 poration would be considered as gain to which sec-
 23 tion 1245 (a) applies.”

24 ~~(f)~~ EFFECTIVE DATE.—The amendments made by this
 25 section shall apply to taxable years beginning after December

1 ~~31, 1961, and ending after the date of the enactment of~~
 2 ~~this Act.~~

3 (g) *EFFECTIVE DATES.*—The amendments made by
 4 this section (other than the amendments made by subsection
 5 (c)) shall apply to taxable years beginning after December
 6 31, 1962. The amendments made by subsection (c) shall
 7 apply to taxable years beginning after December 31, 1961,
 8 and ending after the date of the enactment of this Act.

9 **SEC. ~~15~~ 14. FOREIGN INVESTMENT COMPANIES.**

10 (a) TREATMENT OF SALE OF STOCK OF FOREIGN
 11 INVESTMENT COMPANIES.—

12 (1) IN GENERAL.—Part IV of subchapter P of
 13 chapter 1 (relating to special rules for determining
 14 capital gains and losses) is amended by adding after
 15 section 1245 (as added by section ~~14~~ 13 of this Act) the
 16 following new sections:

17 **“SEC. 1246. GAIN ON FOREIGN INVESTMENT COMPANY**
 18 **STOCK.**

19 “(a) TREATMENT OF GAIN AS ORDINARY INCOME.—

20 “(1) GENERAL RULE.—In the case of a sale or
 21 exchange (or a distribution which, under section 302 or
 22 331, is treated as an exchange of stock) after December
 23 31, 1962, of stock in a foreign corporation which was a
 24 foreign investment company (as defined in subsection

1 “(b)) at any time during the period during which
 2 the taxpayer held such stock, any gain shall be treated
 3 as gain from the sale or exchange of property which
 4 is not a capital asset, to the extent of the taxpayer’s
 5 ratable share of the earnings and profits of such
 6 corporation accumulated for taxable years beginning
 7 after December 31, 1962.

8 “(2) Ratable share.—For purposes of this sec-
 9 tion, the taxpayer’s ratable share shall be determined
 10 under regulations prescribed by the Secretary or his
 11 delegate, but shall include only his ratable share of the
 12 accumulated earnings and profits of such corporation—

13 “(A) for the period during which the taxpayer
 14 held such stock, but

15 ~~“(B) excluding such earnings and profits~~
 16 ~~which were taxed to such taxpayer under section~~
 17 ~~951 or under section 551.~~

18 “(B) *excluding such earnings and profits at-*
 19 ~~tributable to any amount previously included in the~~
 20 ~~gross income of such taxpayer under section 951~~
 21 ~~(but only to the extent the inclusion of such amount~~
 22 ~~did not result in an exclusion of any other amount~~
 23 ~~from gross income under section 959).~~

24 “(3) TAXPAYER TO ESTABLISH EARNINGS AND
 25 PROFITS.—Unless the taxpayer establishes the amount

1 of the accumulated earnings and profits of the foreign
2 investment company and the ratable share thereof for
3 the period during which the taxpayer held such stock,
4 all the gain from the sale or exchange of stock in such
5 company shall be considered as gain from the sale or
6 exchange of property which is not a capital asset.

7 “(4) HOLDING PERIOD OF STOCK MUST BE MORE
8 THAN 6 MONTHS.—This section shall not apply with
9 respect to the sale or exchange of stock where the hold-
10 ing period of such stock as of the date of such sale or
11 exchange is 6 months or less.

12 “(b) DEFINITION OF FOREIGN INVESTMENT COM-
13 PANY.—For purposes of this section, the term ‘foreign in-
14 vestment company’ means any foreign corporation *which,*
15 *for any taxable year beginning after December 31, 1962,*
16 *is—*

17 “(1) registered under the Investment Company
18 Act of 1940, as amended (15 U.S.C. 80a-1 to 80b-2),
19 either as a management company or as a unit invest-
20 ment trust, or

21 “(2) engaged (or holding itself out as being
22 engaged) primarily in the business of investing, rein-
23 vesting, or trading in securities (within the meaning of
24 section 3 (a) (1) of such Act, *as limited by paragraphs*
25 *(2) through (10) (except paragraph (6)(C)) and*

1 *paragraphs (12) through (15) of section 3(c) of such*
 2 *Act)* at a time when more than 50 percent of the total
 3 combined voting power of all classes of stock entitled to
 4 vote, or of the total value of shares of all classes of stock,
 5 was held, directly or indirectly (within the meaning of
 6 section ~~955~~ 958 (a)), by United States persons (as de-
 7 fined in section 7701 (a) (30)).

8 “(c) STOCK HAVING TRANSFERRED OR SUBSTITUTED
 9 BASIS.—To the extent provided in regulations prescribed
 10 by the Secretary or his delegate, stock in a foreign corpora-
 11 tion, the basis of which (in the hands of the taxpayer selling
 12 or exchanging such stock) is determined by reference to the
 13 basis (in the hands of such taxpayer or any other person)
 14 of stock in a foreign investment company, shall be treated
 15 as stock of a foreign investment company and held by the
 16 taxpayer throughout the holding period for such stock (deter-
 17 mined under section 1223) .

18 “(d) RULES RELATING TO ENTITIES HOLDING FOR-
 19 EIGN INVESTMENT COMPANY STOCK.—To the extent pro-
 20 vided in regulations prescribed by the Secretary or his
 21 delegate—

22 “(1) trust certificates of a trust to which section
 23 677 (relating to income for benefit of grantor) applies,
 24 and

25 “(2) stock of a domestic corporation,

1 shall be treated as stock of a foreign investment company
 2 and held by the taxpayer throughout the holding period for
 3 such certificates or stock (determined under section 1223)
 4 in the same proportion that the investment in stock in a for-
 5 eign investment company by the trust or domestic corpora-
 6 tion bears to the total assets of such trust or corporation.

7 “(e) RULES RELATING TO STOCK ACQUIRED FROM A
 8 DECEDENT.—

9 “(1) BASIS.—In the case of stock of a foreign
 10 investment company acquired by bequest, devise, or
 11 inheritance (or by the decedent’s estate) from a dece-
 12 dent dying after December 31, 1962, the basis deter-
 13 mined under section 1014 shall be reduced (but not
 14 below the adjusted basis of such stock in the hands of
 15 the decedent immediately before his death) by the
 16 amount of the decedent’s ratable share of the ~~accumu-~~
 17 ~~lated earnings and profits of such company~~ *earnings and*
 18 *profits of such company accumulated after December 31,*
 19 *1962.* Any stock so acquired shall be treated as stock
 20 described in subsection (c).

21 “(2) DEDUCTION FOR ESTATE TAX.—If stock to
 22 which subsection (a) applies is acquired from a dece-
 23 dent, the taxpayer shall, under regulations prescribed
 24 by the Secretary or his delegate, be allowed (for the
 25 taxable year of the sale or exchange) a deduction from

1 gross income equal to that portion of the decedent's
2 estate tax deemed paid which is attributable to the excess
3 of (A) the value at which such stock was taken into
4 account for purposes of determining the value of the
5 decedent's gross estate, over (B) the value at which
6 it would have been so taken into account if such value
7 had been reduced by the amount described in para-
8 graph (1).

9 “(f) INFORMATION WITH RESPECT TO CERTAIN
10 FOREIGN ~~INVESTMENT~~ INVESTMENT COMPANIES.—Every
11 United States person who, on the last day of the taxable
12 year of a foreign investment company beginning after
13 December 31, 1962, owns 5 percent or more in value of the
14 stock of such company shall furnish with respect to such
15 company such information as the Secretary or his delegate
16 shall by regulations prescribe.

17 “(g) NONAPPLICATION OF SECTION 367 IN CERTAIN
18 CASES.—Section 367 shall not apply in respect of a foreign
19 investment company described in paragraph (1) of subsection
20 (b) which is a party to a reorganization in which all of its
21 properties are acquired before January 1, 1964, by a
22 domestic corporation which is a regulated investment company
23 under section 851 for its first taxable year ending after the
24 reorganization, but only if such foreign investment company

1 *made the election described in section 1247 with respect to its*
 2 *taxable years beginning after December 31, 1962.*

3 “~~(g)~~ (h) CROSS REFERENCE.—

“For special rules relating to the earnings and profits
 of foreign investment companies, see section 312(1).

4 “SEC. 1247. ELECTION BY FOREIGN INVESTMENT COM-
 5 PANIES TO DISTRIBUTE INCOME CUR-
 6 RENTLY.

7 “(a) ELECTION BY FOREIGN INVESTMENT COM-
 8 PANY.—

9 “(1) IN GENERAL.—If a foreign investment com-
 10 pany which is described in section 1246(b) (1) elects
 11 (in the manner provided in regulations prescribed by
 12 the Secretary or his delegate) on or before December
 13 31, 1962, with respect to each taxable year beginning
 14 after December 31, 1962, to—

15 “(A) distribute to its shareholders 90 percent
 16 or more of what its taxable income would be if it
 17 were a domestic corporation;

18 “(B) designate in a written notice mailed to
 19 its shareholders at any time before the expiration
 20 of 30 45 days after the close of its taxable year the
 21 pro rata amount of the excess (determined as if such
 22 corporation were a domestic corporation) of the net
 23 long-term capital ~~gains~~ gain over the net short-term

1 ~~capital losses~~ *loss of the taxable year*; and the portion
2 thereof which is being distributed; and

3 “(C) provide such information as the Secre-
4 tary or his delegate deems necessary to carry out the
5 purposes of this section,

6 then section 1246 shall not apply with respect to the
7 qualified shareholders of such company during any
8 taxable year to which such election applies.

9 “(2) SPECIAL RULES.—

10 “(A) COMPUTATION OF TAXABLE INCOME.—

11 For purposes of paragraph (1) (A), the taxable
12 income of the company shall be computed without
13 regard to—

14 “(i) the excess of ~~capital gains~~ *over losses*
15 *the net long-term capital gain over the net short-*
16 *term capital loss* referred to in paragraph (1)
17 (B),

18 “(ii) section 172 (relating to net operating
19 losses), and

20 “(iii) any deduction provided by part VIII
21 of subchapter B (other than the deduction pro-
22 vided by section 248, relating to organizational
23 expenditures).

24 “(B) DISTRIBUTIONS AFTER THE CLOSE OF
25 THE TAXABLE YEAR.—For purposes of paragraph

(1) (A), a distribution made after the close of the taxable year and on or before the 15th day of the third month of the next taxable year shall be treated as distributed during the taxable year to the extent elected by the company (in accordance with regulations prescribed by the Secretary or his delegate) on or before the 15th day of such third month.

“(C) CARRYOVER OF CAPITAL LOSSES FROM NONELECTION YEARS DENIED.—In computing the excess of ~~capital gains over losses~~ *the net long-term capital gain over the net short-term capital loss* referred to in paragraph (1) (B), section 1212 shall not apply to losses incurred in or with respect to taxable years before the first taxable year to which the election applies.

“(b) YEARS TO WHICH ELECTION APPLIES.—The election of any foreign investment company under this section shall terminate as of the close of the taxable year preceding its first taxable year in which any of the following occurs:

“(1) the company fails to comply with the provisions of subparagraph (A), (B), or (C) of subsection (a) (1), unless it is shown that such failure is due to reasonable cause and not due to willful neglect,

1 “(2) the company is a foreign personal holding
2 company, or

3 “(3) the company is not a foreign investment com-
4 pany which is described in section 1246 (b) (1).

5 “(c) QUALIFIED SHAREHOLDERS.—For purposes of
6 this section—

7 “(1) IN GENERAL.—The term ‘qualified share-
8 holder’ means any shareholder who is a United States
9 person (*as defined in section 7701(a)(30)*), other than
10 a shareholder described in paragraph (2).

11 “(2) CERTAIN UNITED STATES PERSONS EX-
12 CLUDED FROM DEFINITION.—A United States person
13 shall not be treated as a qualified shareholder for the
14 taxable year if for such taxable year (or for any prior
15 taxable year) he did not include, in computing his long-
16 term capital gains in his return for such taxable year,
17 the amount designated by such company pursuant to
18 subsection (a) (1) (B) as his share of the undistributed
19 capital gains of such company for its taxable year end-
20 ing within or with such taxable year of the taxpayer.
21 The preceding sentence shall not apply with respect
22 to any failure by the taxpayer to treat an amount as
23 provided therein if the taxpayer shows that such failure
24 was due to reasonable cause and not due to willful
25 neglect.

1 “(d) **ADJUSTMENTS.**—Under regulations prescribed
2 by the Secretary or his delegate, proper adjustment shall be
3 made—

4 ~~“(1)~~ in the earnings and profits of the electing
5 foreign investment company, and

6 ~~“(2)~~ the adjusted basis of stock of such company
7 held by qualified shareholders,
8 to reflect the inclusion in gross income by such shareholders
9 of undistributed capital gains.

10 “(d) *TREATMENT OF DISTRIBUTED AND UNDIS-*
11 *TRIBUTED CAPITAL GAINS BY A QUALIFIED SHARE-*
12 *HOLDER.*—Every qualified shareholder of a foreign invest-
13 ment company for any taxable year of such company with
14 respect to which an election pursuant to subsection (a) is
15 in effect shall include, in computing his long-term capital
16 gains—

17 “(1) for his taxable year in which received, his pro
18 rata share of the distributed portion of the excess of the
19 net long-term capital gain over the net short-term capital
20 loss for such taxable year of such company, and

21 “(2) for his taxable year in which or with which
22 the taxable year of such company ends, his pro rata share
23 of the undistributed portion of the excess of the net
24 long-term capital gain over the net short-term capital loss
25 for such taxable year of such company.

1 “(e) *ADJUSTMENTS.*—Under regulations prescribed
2 by the Secretary or his delegate, proper adjustment shall be
3 made—

4 “(1) in the earnings and profits of the electing
5 foreign investment company and a qualified shareholder’s
6 ratable share thereof, and

7 “(2) in the adjusted basis of stock of such company
8 held by such shareholder,
9 to reflect such shareholder’s inclusion in gross income of
10 undistributed capital gains.

11 “(f) *ELECTION BY FOREIGN INVESTMENT COMPANY*
12 *WITH RESPECT TO FOREIGN TAX CREDIT.*—A foreign in-
13 vestment company with respect to which an election pur-
14 suant to subsection (a) is in effect and more than 50 per-
15 cent of the value (as defined in section 851(c)(4)) of
16 whose total assets at the close of the taxable year consists
17 of stock or securities in foreign corporations may, for such
18 taxable year, elect the application of this subsection with
19 respect to income, war profits, and excess profits taxes
20 described in section 901(b)(1) which are paid by the for-
21 eign investment company during such taxable year to foreign
22 countries and possessions of the United States. If such elec-
23 tion is made—

24 “(1) the foreign investment company—

25 “(A) shall compute its taxable income, for pur-

1 *poses of subsection (a)(1)(A), without any deduc-*
2 *tions for income, war profits, or excess profits taxes*
3 *paid to foreign countries or possessions of the United*
4 *States, and*

5 *“(B) shall treat the amount of such taxes, for*
6 *purposes of subsection (a)(1)(A), as distributed*
7 *to its shareholders;*

8 *“(2) each qualified shareholder of such foreign in-*
9 *vestment company—*

10 *“(A) shall include in gross income and treat*
11 *as paid by him his proportionate share of such taxes,*
12 *and*

13 *“(B) shall treat, for purposes of applying sub-*
14 *part A of part III of subchapter N, his proportion-*
15 *ate share of such taxes as having been paid to the*
16 *country in which the foreign investment company*
17 *is incorporated, and*

18 *“(C) shall treat as gross income from sources*
19 *within the country in which the foreign investment*
20 *company is incorporated, for purposes of applying*
21 *subpart A of part III of subchapter N, the sum of*
22 *his proportionate share of such taxes and any*
23 *dividend paid to him by such foreign investment*
24 *company.*

25 *“(g) NOTICE TO SHAREHOLDERS.—The amounts to be*

1 *treated by qualified shareholders, for purposes of subsection*
2 *(f)(2), as their proportionate share of the taxes described in*
3 *subsection (f)(1)(A) paid by a foreign investment company*
4 *shall not exceed the amounts so designated by the foreign*
5 *investment company in a written notice mailed to its share-*
6 *holders not later than 45 days after the close of its taxable*
7 *year.*

8 “(h) *MANNER OF MAKING ELECTION AND NOTIFY-*
9 *ING SHAREHOLDERS.—The election provided in subsection*
10 *(f) and the notice to shareholders required by subsection (g)*
11 *shall be made in such manner as the Secretary or his delegate*
12 *may prescribe by regulations.*

13 “~~(e)~~ (i) *LOSS ON SALE OR EXCHANGE OF CERTAIN*
14 *STOCK HELD LESS THAN 6 MONTHS.—If—*

15 “(1) *under this section, any qualified shareholder*
16 *treats any amount designated under subsection (a)(1)*
17 *(B) with respect to a share of stock as long-term capital*
18 *gain, and*

19 “(2) *such share is held by the taxpayer for less*
20 *than 6 months,*

21 *then any loss on the sale or exchange of such share shall,*
22 *to the extent of the amount described in paragraph (1),*
23 *be treated as loss from the sale or exchange of a capital*
24 *asset held for more than 6 months.”*

(2) The table of sections for such part IV is amended by adding at the end thereof the following:

“Sec. 1246. Gain on foreign investment company *stock*.

“Sec. 1247. Election by foreign investment companies to distribute income currently.”

(b) CONFORMING AMENDMENTS.—

(1) EARNINGS AND PROFITS OF FOREIGN INVESTMENT COMPANIES.—Section 312 (relating to effect on earnings and profits) is amended by adding after subsection (k) the following new subsection:

“(1) EARNINGS AND PROFITS OF FOREIGN INVESTMENT COMPANIES.—

“(1) ALLOCATION WITHIN AFFILIATED GROUP.—

In the case of a sale or exchange of stock in a foreign investment company (as defined in section 1246 (b)) by a United States person (as defined in section 7701 (a) (30)), if such company is a member of an affiliated group, then the accumulated earnings and profits of all members of such affiliated group shall be allocated, under regulations prescribed by the Secretary or his delegate, in such manner as is proper to carry out the purposes of section 1246.

“(2) AFFILIATED GROUP DEFINED.—For purposes of paragraphs ~~(1)~~ and ~~(2)~~ paragraph (1) of this subsection, the term ‘affiliated group’ has the meaning assigned to such term by section 1504 (a) ; except that

1 (A) ‘more than 50 percent’ shall be substituted for
2 ‘80 percent or more’, and (B) all corporations shall be
3 treated as includible corporations (without regard to the
4 provisions of section 1504 (b)).

5 “(3) PARTIAL LIQUIDATIONS AND REDEMP-
6 TIONS.—

7 “(A) IN GENERAL.—If a foreign investment
8 company (as defined in section 1246) distributes
9 amounts in partial liquidation or in a redemption to
10 which section 302 (a) or 303 applies, the part of
11 such distribution which is properly chargeable to
12 earnings and profits shall be an amount which is
13 not in excess of the ratable share of the earnings
14 and profits of the company accumulated after
15 February 28, 1913, attributable to the stock so
16 redeemed.

17 “(B) EFFECTIVE DATE.—Subparagraph (A)
18 shall apply only with respect to distributions made
19 after December 31, 1962.”

20 “(2) SALE OR EXCHANGE OF INTEREST IN PART-
21 NERSHIP.—Section 751 (d) (2) (relating to inventory
22 items which have appreciated substantially in value) is
23 amended by striking out “and” at the end of subpara-
24 graph (B) , and by striking out subparagraph (C) and
25 inserting in lieu thereof the following new subparagraphs:

1 “(C) any other property of the partnership
2 which, if sold or exchanged by the partnership,
3 would result in a gain taxable under subsection (a)
4 of section 1246 (relating to gain on foreign invest-
5 ment company stock), and

6 “(D) any other property held by the partner-
7 ship which, if held by the selling or distributee part-
8 ner, would be considered property of the type
9 described in subparagraph (A), (B), or (C).”

10 (3) HOLDING PERIOD OF PROPERTY.—Section
11 1223 (relating to holding period of property) is amended
12 by redesignating paragraph (10) as paragraph (11)
13 and inserting after paragraph (9) the following para-
14 graph:

15 “(10) In determining the period for which the
16 taxpayer has held trust certificates of a trust to which
17 subsection (d) of section 1246 applies, or the period
18 for which the taxpayer has held stock in a corporation
19 to which subsection (d) of section 1246 applies, there
20 shall be included the period for which the trust or cor-
21 poration (as the case may be) held the stock of foreign
22 investment companies.”

23 (c) EFFECTIVE DATE.—The amendments made by

1 this section shall apply with respect to taxable years begin-
2 ning after December 31, 1962.

3 **SEC. 15. GAIN FROM CERTAIN SALES OR EXCHANGES**
4 **OF STOCK IN CERTAIN FOREIGN CORPORA-**
5 **TIONS.**

6 (a) TREATMENT OF GAIN FROM THE REDEMPTION,
7 CANCELLATION, OR SALE OF STOCK IN CERTAIN FOREIGN
8 CORPORATIONS.—Part IV of subchapter P of chapter 1
9 (relating to special rules for determining capital gains and
10 losses) is amended by adding after section 1247 (as added
11 by section 14 of this Act) the following new section:

12 **“SEC. 1248. GAIN FROM CERTAIN SALES OR EXCHANGES**
13 **OF STOCK IN CERTAIN FOREIGN CORPORA-**
14 **TIONS.**

15 ~~“(a) REDEMPTIONS AND LIQUIDATIONS.—If a foreign~~
16 ~~corporation redeems its stock in an exchange to which sec-~~
17 ~~tion 302(a) applies, or if a foreign corporation cancels its~~
18 ~~stock in a complete or partial liquidation in an exchange to~~
19 ~~which section 331 applies, then the gain of a United States~~
20 ~~person (as defined in section 7701(a)(30)) from the ex-~~
21 ~~change of such stock shall be included in the gross income~~
22 ~~of such person as a dividend, to the extent of such person’s~~
23 ~~proportionate share of the earnings and profits of the foreign~~
24 ~~corporation accumulated after February 28, 1913.~~

25 ~~“(b) SALES AND OTHER EXCHANGES.—If a United~~

1 States person ~~(as defined in section 7701(a)(30))~~ sells or
 2 exchanges stock in a foreign corporation; then the gain
 3 recognized on the sale or exchange of such stock shall be
 4 considered as gain from the sale or exchange of property
 5 which is not a capital asset, to the extent of such person's
 6 proportionate share of the earnings and profits of the foreign
 7 corporation accumulated during the period the stock sold or
 8 exchanged was held by such person.

9 ~~“(c) LIMITATIONS.—~~

10 ~~“(1) CONTROLLED FOREIGN CORPORATIONS.—~~

11 Subsections ~~(a)~~ and ~~(b)~~ shall apply only if the foreign
 12 corporation the stock of which is sold or exchanged ~~(A)~~
 13 is a controlled foreign corporation ~~(as defined in section~~
 14 ~~954)~~ at the time of the sale or exchange, or ~~(B)~~ was
 15 such a controlled foreign corporation at any time during
 16 the 5-year period ending on the date of the sale or
 17 exchange.

18 ~~“(2) 10 PERCENT OWNERSHIP.—~~Subsections ~~(a)~~
 19 and ~~(b)~~ shall apply only to a United States person who
 20 can be considered, by applying the rules of constructive
 21 ownership of section 955(b), as being the owner,
 22 directly or indirectly, of 10 percent or more of the total
 23 combined voting power of all classes of stock entitled
 24 to vote of the foreign corporation at the time of the sale

1 or exchange, or at any time during the 5-year period
2 ending on the date of the sale or exchange.

3 “(3) ELIMINATION FROM EARNING AND PROFITS
4 OF AMOUNTS INCLUDED IN GROSS INCOME UNDER
5 SECTION 951.—In determining the amount to be con-
6 sidered a dividend under subsection (a), or as gain from
7 the sale or exchange of property which is not a capital
8 asset under subsection (b), the United States person's
9 proportionate share of earnings and profits of the foreign
10 corporation shall be reduced by the amount previously
11 included in the gross income of such person under section
12 951, with respect to the stock sold or exchanged, but
13 only to the extent such amount did not result in an
14 exclusion from gross income under section 956.

15 “(4) REDEMPTIONS TO PAY DEATH TAXES.—Sub-
16 sections (a) and (b) shall not apply to distributions to
17 which section 303 (relating to distributions in redemp-
18 tion of stock to pay death taxes) applies.

19 “(5) ADDITIONAL CONSIDERATION IN CERTAIN
20 REORGANIZATIONS.—Subsection (b) shall not apply to
21 gain recognized on exchanges to which section 356 (re-
22 lating to receipt of additional consideration in certain
23 reorganizations) applies.

24 “(6) TREATMENT OF AMOUNTS WHICH ARE ORDI-
25 NARY INCOME, ETC., UNDER OTHER PROVISIONS.—Sub-

sections (a) and (b) shall not apply with respect to any amount to the extent that such amount is, under any other provision of this title, treated as—

“(A) a dividend;

“(B) gain from the sale of an asset which is not a capital asset; or

“(C) gain from the sale of an asset held for not more than 6 months.

“(d) **TAXPAYER TO ESTABLISH EARNINGS AND PROFITS.**—Unless the taxpayer establishes the amount of the earnings and profits of the foreign corporation to be taken into account under subsections (a) and (b), all gain from the sale or exchange shall be considered a dividend under subsection (a), or as gain from the sale or exchange of property which is not a capital asset under subsection (b), whichever applies.”

“**SEC. 1248. GAIN FROM CERTAIN SALES OR EXCHANGES OF STOCK IN CERTAIN FOREIGN CORPORATIONS.**

“(a) **GENERAL RULE.**—If—

“(1) a United States person sells or exchanges stock in a foreign corporation, or if a United States person receives a distribution from a foreign corporation which, under section 302 or 331, is treated as an exchange of stock, and

“(2) such person owns, within the meaning of sec-

1 *tion 958(a), or is considered as owning by applying*
 2 *the rules of ownership of section 958(b), 10 percent or*
 3 *more of the total combined voting power of all classes of*
 4 *stock entitled to vote of such foreign corporation at any*
 5 *time during the 5-year period ending on the date of the*
 6 *sale or exchange when such foreign corporation was a con-*
 7 *trolled foreign corporation (as defined in section 957),*
 8 *then the gain recognized on the sale or exchange of such*
 9 *stock shall be included in the gross income of such person as*
 10 *a dividend, to the extent of the earnings and profits of the*
 11 *foreign corporation attributable (under regulations prescribed*
 12 *by the Secretary or his delegate) to such stock which were*
 13 *accumulated in taxable years of such foreign corporation*
 14 *beginning after December 31, 1962, and during the period*
 15 *or periods the stock sold or exchanged was held by such person*
 16 *while such foreign corporation was a controlled foreign*
 17 *corporation.*

18 *“(b) LIMITATION ON TAX APPLICABLE TO INDIVID-*
 19 *UALS.—*

20 *“(1) IN GENERAL.—In the case of an individual,*
 21 *the tax attributable to an amount included in gross in-*
 22 *come as a dividend under subsection (a) shall not be*
 23 *greater than the tax described in paragraph (2) or in*
 24 *paragraph (3), whichever is lesser.*

25 *“(2) DOMESTIC CORPORATION LIMITATION.—*

1 *If the stock sold or exchanged is a capital asset (within*
2 *the meaning of section 1221) and has been held for*
3 *more than 6 months, a tax equal to the sum of--*

4 *“(A) a pro rata share of the excess of—*

5 *“(i) the taxes that would have been paid*
6 *by the foreign corporation with respect to its*
7 *income had it been taxed under this chapter as a*
8 *domestic corporation (but without allowance*
9 *for deduction of, or credit for, taxes described*
10 *in clause (ii)), for the period or periods the*
11 *stock sold or exchanged was held by the United*
12 *States person in taxable years beginning after*
13 *December 31, 1962, while the foreign cor-*
14 *poration was a controlled foreign corporation,*
15 *adjusted for distributions and amounts previ-*
16 *ously included in gross income of a United*
17 *States shareholder under section 951, over*

18 *“(ii) the income, war profits, or excess*
19 *profits taxes paid by the foreign corporation with*
20 *respect to such income; and*

21 *“(B) an amount equal to a tax that would re-*
22 *sult by including in gross income the amount de-*
23 *scribed in subsection (a), reduced by the excess of*
24 *the taxes described in paragraph (A)(i) over the*
25 *taxes described in paragraph (A)(ii), as gain from*

1 *the sale or exchange of a capital asset held for more*
2 *than 6 months.*

3 “(3) *ANNUAL DISTRIBUTION LIMITATION.—A tax*
4 *equal to the aggregate of the taxes which would have*
5 *been attributable to the amount described in subsection*
6 *(a) had it been included in the gross income of the*
7 *individual as a dividend in the year or years in which*
8 *earned by the foreign corporation, adjusted for losses and*
9 *distributions as provided by regulations prescribed by*
10 *the Secretary or his delegate.*

11 “(c) *SPECIAL RULES.—For purposes of this section, the*
12 *following amounts shall be excluded, with respect to any*
13 *United States person, from the earnings and profits of a*
14 *foreign corporation:*

15 “(1) *AMOUNTS INCLUDED IN GROSS INCOME*
16 *UNDER SECTION 951.—Earnings and profits of the for-*
17 *ign corporation attributable to any amount previously*
18 *included in the gross income of such person under section*
19 *951, with respect to the stock sold or exchanged, but only*
20 *to the extent the inclusion of such amount did not result*
21 *in an exclusion of an amount from gross income under*
22 *section 959.*

23 “(2) *GAIN REALIZED FROM THE SALE OR EX-*
24 *CHANGE OF PROPERTY IN PURSUANCE OF A PLAN OF*

1 *COMPLETE LIQUIDATION.—If a foreign corporation*
2 *adopts a plan of complete liquidation in a taxable year*
3 *of a foreign corporation beginning after December 31,*
4 *1962, and if section 337(a) would apply if such foreign*
5 *corporation were a domestic corporation, earnings and*
6 *profits of the foreign corporation attributable (under*
7 *regulations prescribed by the Secretary or his delegate)*
8 *to any net gain from the sale or exchange of property.*

9 “(3) *LESS DEVELOPED COUNTRY CORPORA-*
10 *TIONS.—Earnings and profits accumulated by a foreign*
11 *corporation while it was a less developed country*
12 *corporation (as defined in section 955(c)), if—*

13 “(A) *the foreign corporation qualified as a*
14 *less developed country corporation for all taxable*
15 *years of such corporation beginning after December*
16 *31, 1962, for which the country under the laws*
17 *of which the foreign corporation was created or*
18 *organized (or, in the case of a less developed country*
19 *corporation within the meaning of section 955(c)*
20 *(2), for which the country under the laws of which*
21 *the aircraft or vessels described therein were*
22 *registered) was designated a less developed country*
23 *under section 955(c)(3); and*

24 “(B) *the stock sold or exchanged was owned*

1 *for a continuous period of at least 10 years, ending*
2 *with the date of the sale or exchange, by the United*
3 *States person who sold or exchanged such stock.*

4 *In the case of stock sold or exchanged by a corporation, if*
5 *United States persons who are individuals, estates, or*
6 *trusts (each of whom owned within the meaning of section*
7 *958(a), or were considered as owning by applying the*
8 *rules of ownership of section 958(b), 10 percent or more*
9 *of the total combined voting power of all classes of stock*
10 *entitled to vote of such corporation) owned, or were con-*
11 *sidered as owning, at any time during the 10-year period*
12 *referred to in subparagraph (B) more than 50 percent*
13 *of the total combined voting power of all classes of stock*
14 *entitled to vote of such corporation, this paragraph shall*
15 *apply only if such United States persons owned, or were*
16 *considered as owning, at all times during the remainder*
17 *of such 10-year period more than 50 percent of the total*
18 *combined voting power of all classes of stock entitled to*
19 *vote of such corporation. For purposes of this para-*
20 *graph, stock owned by a United States person who is an*
21 *individual, estate, or trust which was acquired by reason*
22 *of the death of the predecessor in interest of such United*
23 *States person shall be considered as owned by such United*
24 *States person during the period such stock was owned by*
25 *such predecessor in interest, and during the period such*

1 stock was owned by any other predecessor in interest if
2 between such United States person and such other prede-
3 cessor in interest there was no transfer other than by
4 reason of the death of an individual.

5 “(4) UNITED STATES INCOME.—Any item includ-
6 ible in gross income of the foreign corporation under this
7 chapter as income derived from sources within the United
8 States of a foreign corporation engaged in trade or busi-
9 ness in the United States.

10 “(5) AMOUNTS INCLUDED IN GROSS INCOME UN-
11 DER SECTION 1247.—If the United States person whose
12 stock is sold or exchanged was a qualified shareholder
13 (as defined in section 1247(c)) of a foreign corporation
14 which was a foreign investment company (as described
15 in section 1246(b)(1)), the earnings and profits of the
16 foreign corporation for taxable years in which such per-
17 son was a qualified shareholder.

18 “(d) EXCEPTIONS.—This section shall not apply to—

19 “(1) distributions to which section 303 (relating to
20 distributions in redemption of stock to pay death taxes)
21 applies;

22 “(2) gain realized on exchanges to which section
23 356 (relating to receipt of additional consideration in
24 certain reorganizations) applies; or

1 “(3) any amount to the extent that such amount
2 is, under any other provision of this title, treated as—

3 “(A) a dividend,

4 “(B) gain from the sale of an asset which is
5 not a capital asset, or

6 “(C) gain from the sale of an asset held for
7 not more than 6 months.

8 “(e) *TAXPAYER TO ESTABLISH EARNINGS AND*
9 *PROFITS.*—Unless the taxpayer establishes the amount of the
10 earnings and profits of the foreign corporation to be taken
11 into account under subsection (a), all gain from the sale
12 or exchange shall be considered a dividend under subsection
13 (a), and unless the taxpayer establishes the amount of for-
14 eign taxes to be taken into account under subsection (b)
15 (2), the limitation of such subsection shall not apply.”

16 (b) *CLERICAL AMENDMENT.*—The table of sections for
17 such part IV is amended by adding at the end thereof the
18 following:

 “Sec. 1248. Gain from certain sales or exchanges of stock
 in certain foreign corporations.”

19 (c) *EFFECTIVE DATE.*—The amendments made by this
20 section shall apply with respect to sales or exchanges oc-
21 curring after the date of the enactment of this Act December
22 31, 1962.

1 **SEC. 16. SALES AND EXCHANGES OF PATENTS, ETC., TO CER-**
 2 **TAIN FOREIGN CORPORATIONS.**

3 *(a) TREATMENT OF GAIN AS ORDINARY INCOME.—*
 4 *Part IV of subchapter P of chapter 1 (relating to special*
 5 *rules for determining capital gains and losses) is amended*
 6 *by adding after section 1248 (as added by section 15 of this*
 7 *Act) the following new section:*

8 **“SEC. 1249. GAIN FROM CERTAIN SALES OR EXCHANGES OF**
 9 **PATENTS, ETC., TO FOREIGN CORPORATIONS.**

10 *“(a) GENERAL RULE.—Except as provided in subsec-*
 11 *tion (c), gain from the sale or exchange after December 31,*
 12 *1962, of a patent, an invention, model, or design (whether*
 13 *or not patented), a copyright, a secret formula or process,*
 14 *or any other similar property right to any foreign corporation*
 15 *by any United States person (as defined in section 7701(a)*
 16 *(30)) which controls such foreign corporation shall, if such*
 17 *gain would (but for the provisions of this subsection) be*
 18 *gain from the sale or exchange of a capital asset or of prop-*
 19 *erty described in section 1231, be considered as gain from*
 20 *the sale or exchange of property which is neither a capital*
 21 *asset nor property described in section 1231.*

22 *“(b) CONTROL.—For purposes of subsection (a), con-*
 23 *trol means, with respect to any foreign corporation, the*

1 ownership, directly or indirectly, of stock possessing more
 2 than 50 percent of the total combined voting power of all
 3 classes of stock entitled to vote. For purposes of this sub-
 4 section, the rules for determining ownership of stock pre-
 5 scribed by section 958 shall apply.

6 “(c) *EXCEPTION.*—This section shall not apply to gain
 7 realized from the sale or exchange for stock or contribution
 8 to capital of property described in subsection (a) where it
 9 is established to the satisfaction of the Secretary or his dele-
 10 gate that the principal purpose of the transfer is to enable
 11 the foreign corporation to use such property in its own manu-
 12 facturing operations.”

13 (b) *CLERICAL AMENDMENT.*—The table of sections for
 14 such part IV is amended by adding at the end thereof the
 15 following:

“Sec. 1249. Gain from certain sales or exchanges of patents,
 etc., to foreign corporations.”

16 (c) *EFFECTIVE DATE.*—The amendments made by this
 17 section shall apply to taxable years beginning after December
 18 31, 1962.

19 **SEC. 17. TAX TREATMENT OF COOPERATIVES AND PA-**
 20 **TRONS.**

21 (a) *IN GENERAL.*—Chapter 1 (relating to normal
 22 taxes and surtaxes) is amended by adding at the end thereof
 23 the following new subchapter:

1 **“Subchapter T—Cooperatives and Their Patrons**

“Part I. Tax treatment of cooperatives.

“Part II. Tax treatment by patrons of patronage dividends.

“Part III. Definitions; special rules.

2 **“PART I—TAX TREATMENT OF COOPERATIVES**

“Sec. 1381. Organizations to which part applies.

“Sec. 1382. Taxable income of cooperatives.

“Sec. 1383. Computation of tax where cooperative redeems
nonqualified written notices of allocation.

3 **“SEC. 1381. ORGANIZATIONS TO WHICH PART APPLIES.**

4 “(a) IN GENERAL.—This part shall apply to—

5 “(1) any organization exempt from tax under sec-
6 tion 521 (relating to exemption of farmers’ cooperatives
7 from tax), and

8 “(2) any corporation operating on a cooperative
9 basis other than an organization—

10 “(A) which is exempt from tax under this
11 chapter,

12 “(B) which is subject to the provisions of—

13 “(i) part II of subchapter H (relating
14 to mutual savings banks, etc.), or

15 “(ii) subchapter L (relating to insurance
16 companies), or

17 “(C) which is engaged in furnishing electric
18 energy, or providing telephone service, to persons
19 in rural areas.

20 “(b) TAX ON CERTAIN FARMERS’ COOPERATIVES.—

1 An organization described in subsection (a) (1) shall be
2 subject to the taxes imposed by section 11 or 1201.

3 **“SEC. 1382. TAXABLE INCOME OF COOPERATIVES.**

4 “(a) GROSS INCOME.—Except as provided in subsec-
5 tion (b), the gross income of any organization to which this
6 part applies shall be determined without any adjustment
7 (as a reduction in gross receipts, an increase in cost of goods
8 sold, or otherwise) by reason of any allocation or distribution
9 to a patron out of the net earnings of such organization.

10 “(b) PATRONAGE DIVIDENDS.—In determining the
11 taxable income of an organization to which this part applies,
12 there shall not be taken into account amounts paid during
13 the payment period for the taxable year—

14 “(1) as patronage dividends (as defined in section
15 1388 (a)), to the extent paid in money, qualified writ-
16 ten notices of allocation (as defined in section 1388
17 (c)), or other property (except nonqualified written
18 notices of allocation (as defined in section 1388 (d)))
19 with respect to patronage occurring during such taxable
20 year; or

21 “(2) in money or other property (except written
22 notices of allocation) in redemption of a nonqualified
23 written notice of allocation which was paid as a patron-
24 age dividend during the payment period for the taxable
25 year during which the patronage occurred.

1 For purposes of this title, any amount not taken into ac-
 2 count under the preceding sentence shall be treated in the
 3 same manner as an item of gross income and as a deduction
 4 therefrom.

5 “(c) DEDUCTION FOR NONPATRONAGE DISTRIBUTU-
 6 TIONS, ETC.—In determining the taxable income of an or-
 7 ganization described in section 1381 (a) (1), there shall be
 8 allowed as a deduction (in addition to other deductions al-
 9 lowable under this chapter) —

10 “(1) amounts paid during the taxable year as divi-
 11 dends on its capital stock; and

12 “(2) amounts paid during the payment period for
 13 the taxable year—

14 “(A) in money, qualified written notices of
 15 allocation, or other property (except nonqualified
 16 written notices of allocation) on a patronage basis
 17 to patrons with respect to its earnings during such
 18 taxable year which are derived from business done
 19 for the United States or any of its agencies or from
 20 sources other than patronage, or

21 “(B) in money or other property (except writ-
 22 ten notices of allocation) in redemption of a non-
 23 qualified written notice of allocation which was paid,
 24 during the payment period for the taxable year dur-

1 ing which the earnings were derived, on a patron-
2 age basis to a patron with respect to earnings de-
3 rived from business or sources described in subpara-
4 graph (A).

5 “(d) PAYMENT PERIOD FOR EACH TAXABLE YEAR.—

6 For purposes of subsections (b) and (c) (2), the payment
7 period for any taxable year is the period beginning with the
8 first day of such taxable year and ending with the fifteenth
9 day of the ninth month following the close of such year.
10 *For purposes of subsections (b)(1) and (c)(2)(A), a*
11 *qualified check issued during the payment period shall be*
12 *treated as an amount paid in money during such period if*
13 *endorsed and cashed on or before the 90th day after the*
14 *close of such period.*

15 “(e) PRODUCTS MARKETING UNDER POOLING AR-
16 RANGEMENTS.—For purposes of subsection (b), in the case
17 of a pooling arrangement for the marketing of products, the
18 patronage shall (to the extent provided in regulations pre-
19 scribed by the Secretary or his delegate) be treated as
20 patronage occurring during the taxable year in which the
21 pool closes.

22 “(f) TREATMENT OF EARNINGS RECEIVED AFTER
23 PATRONAGE OCCURRED.—If any portion of the earnings
24 from business done with or for patrons is includible in the
25 organization’s gross income for a taxable year after the

1 taxable year during which the patronage occurred, then for
 2 purposes of applying subsection (b) to such portion the
 3 patronage shall, to the extent provided in regulations pre-
 4 scribed by the Secretary or his delegate, be considered to
 5 have occurred during the taxable year of the organization
 6 during which such earnings are includible in gross income.

7 **“SEC. 1383. COMPUTATION OF TAX WHERE COOPERATIVE**
 8 **REDEEMS NONQUALIFIED WRITTEN NO-**
 9 **TICES OF ALLOCATION.**

10 “(a) **GENERAL RULE.**—If, under section 1382 (b) (2)
 11 or (c) (2) (B), a deduction is allowable to an organization
 12 for the taxable year for amounts paid in redemption of non-
 13 qualified written notices of allocation, then the tax imposed
 14 by this chapter on such organization for the taxable year
 15 shall be the lesser of the following:

16 “(1) the tax for the taxable year computed with
 17 such deduction; or

18 “(2) an amount equal to—

19 “(A) the tax for the taxable year computed
 20 without such deduction, minus

21 “(B) the decrease in tax under this chapter
 22 for any prior taxable year (or years) which would
 23 result solely from treating such nonqualified written
 24 notices of allocation as qualified written notices of
 25 allocation.

1 “(b) SPECIAL RULES.—

2 “(1) If the decrease in tax ascertained under sub-
3 section (a) (2) (B) exceeds the tax for the taxable year
4 (computed without the deduction described in subsection
5 (a)) such excess shall be considered to be a payment
6 of tax on the last day prescribed by law for the payment
7 of tax for the taxable year, and shall be refunded or
8 credited in the same manner as if it were an overpay-
9 ment for such taxable year.

10 “(2) For purposes of determining the decrease in
11 tax under subsection (a) (2) (B), the stated dollar
12 amount of any nonqualified written notice of allocation
13 which is to be treated under such subsection as a quali-
14 fied written notice of allocation shall be the amount paid
15 in redemption of such written notice of allocation which
16 is allowable as a deduction under section 1382 (b) (2)
17 or (c) (2) (B) for the taxable year.

18 “(3) If the tax imposed by this chapter for the tax-
19 able year is the amount determined under subsection
20 (a) (2), then the deduction described in subsection (a)
21 shall not be taken into account for any purpose of this
22 subtitle other than for purposes of this section.

1 **"PART II—TAX TREATMENT BY PATRONS OF**
2 **PATRONAGE DIVIDENDS**

"Sec. 1385. Amounts includible in patron's gross income.

3 **"SEC. 1385. AMOUNTS INCLUDIBLE IN PATRON'S GROSS**
4 **INCOME.**

5 " (a) GENERAL RULE.—Except as otherwise provided
6 in subsection (b), each person shall include in gross
7 income—

8 " (1) the amount of any patronage dividend which
9 is paid in money, a qualified written notice of allocation,
10 or other property (except a nonqualified written notice
11 of allocation), and which is received by him during the
12 taxable year from an organization described in section
13 1381 (a), and

14 " (2) any amount, described in section 1382 (c) (2)
15 (A) (relating to certain nonpatronage distributions by
16 tax-exempt farmers' cooperatives), which is paid in
17 money, a qualified written notice of allocation, or other
18 property (except a nonqualified written notice of alloca-
19 tion), and which is received by him during the taxable
20 year from an organization described in section 1381 (a)
21 (1).

1 “(b) EXCLUSION FROM GROSS INCOME.—Under regu-
 2 lations prescribed by the Secretary or his delegate, the
 3 amount of any patronage dividend, and any amount re-
 4 ceived on the redemption, sale, or other disposition of a non-
 5 qualified written notice of allocation which was paid as a
 6 patronage dividend, shall not be included in gross income to
 7 the extent that such amount—

8 “(1) is properly taken into account as an adjust-
 9 ment to basis of property, or

10 “(2) is attributable to personal, living, or family
 11 items.

12 “(c) TREATMENT OF CERTAIN NONQUALIFIED WRIT-
 13 TEN NOTICES OF ALLOCATION.—

14 “(1) APPLICATION OF SUBSECTION.—This sub-
 15 section shall apply to any nonqualified written notice of
 16 allocation which—

17 “(A) was paid as a patronage dividend, or

18 “(B) was paid by an organization described in
 19 section 1381 (a) (1) on a patronage basis with re-
 20 spect to earnings derived from business or sources
 21 described in section 1382 (c) (2) (A).

22 “(2) BASIS; AMOUNT OF GAIN.—In the case of
 23 any nonqualified written notice of allocation to which
 24 this subsection applies, for purposes of this chapter—

25 “(A) the basis of such written notice of alloca-

tion in the hands of the patron to whom such written notice of allocation was paid shall be zero,

“(B) the basis of such written notice of allocation which was acquired from a decedent shall be its basis in the hands of the decedent, and

“(C) gain on the redemption, sale, or other disposition of such written notice of allocation by any person shall, to the extent that the stated dollar amount of such written notice of allocation exceeds its basis, be considered as gain from the sale or exchange of property which is not a capital asset.

“PART III—DEFINITIONS; SPECIAL RULES

“Sec. 1388. Definitions; special rules.

“SEC. 1388. DEFINITIONS; SPECIAL RULES.

“(a) **PATRONAGE DIVIDEND.**—For purposes of this subchapter, the term ‘patronage dividend’ means an amount paid to a patron by an organization to which part I of this subchapter applies—

“(1) on the basis of quantity or value of business done with or for such patron,

“(2) under an obligation of such organization to pay such amount, which obligation existed before the organization received the amount so paid, and

“(3) which is determined by reference to the net

1 earnings of the organization from business done with or
2 for its patrons.

3 Such term does not include any amount paid to a patron to
4 the extent that (A) such amount is out of earnings other
5 than from business done with or for patrons, or (B)
6 such amount is out of earnings from business done with or
7 for other patrons to whom no amounts are paid, or to whom
8 smaller amounts are paid, with respect to substantially
9 identical transactions.

10 “(b) WRITTEN NOTICE OF ALLOCATION.—For pur-
11 poses of this subchapter, the term ‘written notice of alloca-
12 tion’ means any capital stock, revolving fund certificate,
13 retain certificate, certificate of indebtedness, letter of advice,
14 or other written notice, which discloses to the recipient the
15 stated dollar amount allocated to him by the organization
16 and the portion thereof, if any, which constitutes a patronage
17 dividend.

18 “(c) QUALIFIED WRITTEN NOTICE OF ALLOCATION.—

19 “(1) DEFINED.—For purposes of this subchapter,
20 the term ‘qualified written notice of allocation’ means—

21 “(A) a written notice of allocation which may
22 be redeemed in cash at its stated dollar amount at
23 any time within a period beginning on the date such
24 written notice of allocation is paid and ending not
25 earlier than 90 days from such date, but only if the

1 distributee receives written notice of the right of
 2 redemption at the time he receives such written
 3 notice of allocation; and

4 “(B) a written notice of allocation which the
 5 distributee has consented, in the manner provided
 6 in paragraph (2), to take into account at its stated
 7 dollar amount as provided in section 1385 (a).

8 *Such term does not include any written notice of alloca-*
 9 *tion which is paid as part of a patronage dividend or as*
 10 *part of a payment described in section 1382(c)(2)(A),*
 11 *unless 20 percent or more of the amount of such patron-*
 12 *age dividend, or such payment, is paid in money*
 13 *or by qualified check.*

14 “(2) MANNER OF OBTAINING CONSENT.—A dis-
 15 tributee shall consent to take a written notice of alloca-
 16 tion into account as provided in paragraph (1) (B)
 17 only by—

18 “(A) making such consent in writing, ~~or~~

19 “(B) obtaining or retaining membership in the
 20 organization after—

21 “(i) such organization has adopted (after
 22 the date of the enactment of the Revenue Act
 23 of 1962) a bylaw providing that membership
 24 in the organization constitutes such consent, and

1 “(ii) he has received a written notifica-
2 tion and copy of such ~~bylaw~~ bylaw, or

3 “(C) if neither subparagraph (A) nor (B)
4 applies, endorsing and cashing a qualified check,
5 paid as a part of the patronage dividend or pay-
6 ment of which such written notice of allocation is
7 also a part, on or before the 90th day after the close
8 of the payment period for the taxable year of the
9 organization for which such patronage dividend or
10 payment is paid.

11 “(3) PERIOD FOR WHICH CONSENT IS EFFEC-
12 TIVE.—

13 “(A) GENERAL RULE.—Except as provided in
14 subparagraph (B)—

15 “(i) a consent described in paragraph
16 (2) (A) shall be a consent with respect to all
17 patronage of the distributee with the organiza-
18 tion occurring (determined with the application
19 of section 1382 (e)) during the taxable year of
20 the organization during which such consent is
21 made and all subsequent taxable years of the
22 organization; and

23 “(ii) a consent described in paragraph
24 (2) (B) shall be a consent with respect to all
25 patronage of the distributee with the organiza-

tion occurring (determined without the application of section 1382 (e)) after he received the notification and copy described in paragraph (2) (B) (ii) .

“(B) REVOCATION, ETC.—

“(i) Any consent described in paragraph (2) (A) may be revoked (in writing) by the distributee at any time. Any such revocation shall be effective with respect to patronage occurring on or after the first day of the first taxable year of the organization beginning after the revocation is filed with such organization; except that in the case of a pooling arrangement described in section 1382 (e) , a revocation made by a distributee shall not be effective as to any pool with respect to which the distributee has been a patron before such revocation.

“(ii) Any consent described in paragraph (2) (B) shall not be effective with respect to any patronage occurring (determined without the application of section 1382 (e)) after the distributee ceases to be a member of the organization or after the bylaws of the organization cease to contain the provision described in paragraph (2) (B) (i) .

1 “(4) *QUALIFIED CHECK*.—For purposes of this
2 subchapter, the term ‘qualified check’ means only a check
3 (or other instrument which is redeemable in money)
4 which is paid as a part of a patronage dividend, or as a
5 part of a payment described in section 1382(c)(2)(A),
6 to a distributee who has not given consent as provided
7 in paragraph (2) (A) or (B) with respect to such
8 patronage dividend or payment, and on which there is
9 clearly imprinted a statement that the endorsement and
10 cashing of the check (or other instrument) constitutes the
11 consent of the payee to include in his gross income, as
12 provided in the Federal income tax laws, the stated dollar
13 amount of the written notice of allocation which is a part
14 of the patronage dividend or payment of which such
15 qualified check is also a part. Such term does not
16 include any check (or other instrument) which is paid
17 as part of a patronage dividend or payment which does
18 not include a written notice of allocation (other than
19 a written notice of allocation described in paragraph
20 (1)(A)).

21 “(d) *NONQUALIFIED WRITTEN NOTICE OF ALLOCA-*
22 *TION*.—For purposes of this subchapter, the term ‘nonquali-

23 fied written notice of allocation’ means a written notice of

24 allocation which is not described in subsection (c) or a quali-

25 fied check which is not cashed on or before the 90th day after

1 *the close of the payment period for the taxable year for which*
 2 *the distribution of which it is a part is paid.*

3 “(e) DETERMINATION OF AMOUNT PAID OR RE-
 4 CEIVED.—For purposes of this subchapter, in determining
 5 amounts paid or received—

6 “(1) property (other than a written notice of allo-
 7 cation) shall be taken into account at its fair market
 8 value, and

9 “(2) a qualified written notice of allocation shall
 10 be taken into account at its stated dollar amount.”

11 (b) TECHNICAL AMENDMENTS.—

12 (1) Section 521 (a) (relating to exemption of farm-
 13 ers’ cooperatives from tax) is amended by striking out
 14 “section 522” each place it appears therein and inserting
 15 in lieu thereof “part I of subchapter T (sec. 1381 and
 16 following)”.

17 (2) Section 522 (relating to tax on farmers’ coop-
 18 eratives) is hereby repealed.

19 ~~(3) Section 6044 (relating to returns regarding~~
 20 ~~patronage dividends)~~ is amended to read as follows:

21 **~~“SEC. 6044. RETURNS REGARDING PATRONAGE DIVI-~~**
 22 **~~DENDS.~~**

23 ~~“Any organization to which part I of subchapter T of~~
 24 ~~chapter 1 (relating to tax treatment of cooperatives) ap-~~
 25 ~~plies which pays amounts described in section 1382(b), or~~

1 ~~(in the case of an organization described in section 1381~~
 2 ~~(a)-(1))~~ amounts described in section 1382(e)(2); shall,
 3 when required by regulations of the Secretary or his delegate,
 4 make a return showing—

5 “~~(1)~~ the name and address of each patron to whom
 6 it has made such payments during the calendar year; and

7 “~~(2)~~ the amount of such payments to each patron.”

8 ~~(4)~~ (3) Section 6072 (d): (relating to time for filing
 9 income tax returns of exempt cooperative associations)
 10 is amended to read as follows:

11 “(d) RETURNS OF COOPERATIVE ASSOCIATIONS.—In
 12 the case of an income tax return of—

13 “(1) an exempt cooperative association described
 14 in section 1381 (a) (1), or

15 “(2) an organization described in section 1381
 16 (a) (2) which is under an obligation to pay patronage
 17 dividends (as defined in section 1388 (a)) in an
 18 amount equal to at least 50 percent of its net earnings
 19 from business done with or for its patrons, or which
 20 paid patronage dividends in such an amount out of the
 21 net earnings from business done with or for patrons dur-
 22 ing the most recent taxable year for which it had such
 23 net earnings,

24 a return made on the basis of a calendar year shall be filed
 25 on or before the 15th day of September following the close

1 of the calendar year, and a return made on the basis of a
2 fiscal year shall be filed on or before the 15th day of the 9th
3 month following the close of the fiscal year.”

4 ~~(5)~~ (4) The table of subchapters for chapter 1 is
5 amended by adding at the end thereof the following:

“SUBCHAPTER T. Cooperatives and their patrons.”

6 ~~(6)~~ (5) The table of sections for part III of sub-
7 chapter F of chapter 1 is amended by striking out the
8 last line thereof.

9 (c) EFFECTIVE DATES.—

10 (1) FOR THE COOPERATIVES.—Except as provided
11 in paragraph (3), the amendments made by subsections
12 (a) and (b) shall apply to taxable years of organiza-
13 tions described in section 1381 (a) of the Internal Reve-
14 nue Code of 1954 (as added by subsection (a)) begin-
15 ning after December 31, 1962.

16 (2) FOR THE PATRONS.—Except as provided in
17 paragraph (3), section 1385 of the Internal Revenue
18 Code of 1954 (as added by subsection (a)) shall
19 apply with respect to any amount received from any
20 organization described in section 1381 (a) of such Code,
21 to the extent that such amount is paid by such organiza-
22 tion in a taxable year of such organization beginning
23 after December 31, 1962.

1 (3) APPLICATION OF EXISTING LAW.—In the case
2 of any money, written notice of allocation, or other prop-
3 erty paid by any organization described in section
4 1381 (a) —

5 (A) before the first day of the first taxable
6 year of such organization beginning after December
7 31, 1962, or

8 (B) on or after such first day with respect to
9 patronage occurring before such first day,
10 the tax treatment of such money, written notice of allo-
11 cation, or other property (including the tax treatment of
12 gain or loss on the redemption, sale, or other disposition
13 of such written notice of allocation) by any person shall
14 be made under the Internal Revenue Code of 1954 with-
15 out regard to subchapter T of chapter 1 of such Code.

16 **SEC. 18. INCLUSION OF FOREIGN REAL PROPERTY IN**
17 **GROSS ESTATE.**

18 (a) AMENDMENTS TO INCLUDE FOREIGN REAL PROP-
19 erty.—

20 (1) Section 2031 (a) (relating to definition of gross
21 estate) is amended by striking out “, except real prop-
22 erty situated outside of the United States”.

23 (2) The following provisions of chapter 11 (impos-
24 ing an estate tax) are amended by striking out “(except
25 real property situated outside of the United States)”:

1 (A) section 2033 (relating to property in
2 which the decedent had an interest),

3 (B) section 2034 (relating to dower or curtesy
4 interests),

5 (C) section 2035 (a) (relating to transactions
6 in contemplation of death),

7 (D) section 2036 (a) (relating to transfers
8 with retained life estate),

9 (E) section 2037 (a) (relating to transfers
10 taking effect at death),

11 (F) section 2038 (a) (relating to revocable
12 transfers),

13 (G) section 2040 (relating to joint interests),
14 and

15 (H) section 2041 (a) (relating to powers of
16 appointment).

17 (b) EFFECTIVE DATE.—

18 (1) Except as provided in paragraph (2), the
19 amendments made by subsection (a) shall apply to the
20 estates of decedents dying after the date of the enactment
21 of this Act.

22 (2) In the case of a decedent dying after the date
23 of the enactment of this Act and before ~~July 1, 1964~~
24 *January 1, 1963*, the value of real property situated

1 outside of the United States shall not be included in the
2 gross estate (as defined in section 2031 (a)) of the
3 decedent—

4 (A) under section 2033, 2034, 2035 (a) ,
5 2036 (a) , 2037 (a) , or 2038 (a) to the extent the
6 real property, or the decedent's interest in it, was
7 acquired by the decedent before February 1, 1962 ;

8 (B) under section 2040 to the extent such
9 property or interest was acquired by the decedent
10 before February 1, 1962, or was held by the dece-
11 dent and the survivor in a joint tenancy or tenancy
12 by the entirety before February 1, 1962 ; or

13 (C) under section 2041 (a) to the extent that
14 before February 1, 1962, such property or interest
15 was subject to a general power of appointment (as
16 defined in section 2041) possessed by the decedent.

17 In the case of real property, or an interest therein, sit-
18 uated outside of the United States (including a general
19 power of appointment in respect of such property or
20 interest, and including property held by the decedent
21 and the survivor in a joint tenancy or tenancy by the
22 entirety) which was acquired by the decedent after
23 January 31, 1962, by gift within the meaning of sec-
24 tion 2511, or from a prior decedent by devise or inherit-
25 ance, or by reason of death, form of ownership, or other

conditions (including the exercise or nonexercise of a power of appointment), for purposes of this paragraph such property or interest therein shall be deemed to have been acquired by the decedent before February 1, 1962, if before that date the donor or prior decedent had acquired the property or his interest therein or had possessed a power of appointment in respect of the property or interest.

SEC. 19. WITHHOLDING OF INCOME TAX AT SOURCE ON INTEREST, DIVIDENDS, AND PATRONAGE DIVIDENDS.

~~(a)~~ IN GENERAL.—

~~(1)~~ AMENDMENT OF SUBTITLE C.—Subtitle C (relating to employment taxes and collection of income tax at source) is amended by redesignating chapter 25 as chapter 26 and by inserting after chapter 24 the following new chapter:

“CHAPTER 25—COLLECTION OF INCOME TAX AT SOURCE ON INTEREST, DIVIDENDS, AND PATRONAGE DIVIDENDS

“SUBCHAPTER A. Interest.

“SUBCHAPTER B. Dividends.

“SUBCHAPTER C. Patronage dividends.

“SUBCHAPTER D. General provisions.

“Subchapter A—Interest

“Sec. 3451. Income tax collected at source on interest.

“Sec. 3452. Interest defined.

1 **"SEC. 3451. INCOME TAX COLLECTED AT SOURCE ON**
 2 **INTEREST.**

3 **"(a) REQUIREMENT OF WITHHOLDING.**—Except as
 4 otherwise provided in this chapter, every person who pays
 5 interest shall deduct and withhold on such interest a tax
 6 equal to 20 percent of the amount thereof.

7 **"(b) PAYEE UNKNOWN.**—If the withholding agent is
 8 unable to determine the person to whom the interest is pay-
 9 able, the tax under this section shall be deducted and with-
 10 held at the time payment of the interest would be made if
 11 such person were known.

12 **"(c) CROSS REFERENCES.**—

"(1) For credit, against income tax of the recipient of the income, of amounts deducted and withheld under this section, see section 39.

"(2) For special rules as to credit or refund of such amounts, see sections 3484, 3485, 3486, 3487, and 3505.

"(3) For exemption from requirement of deducting and withholding on certain interest paid to certain persons, see section 3483.

13 **"SEC. 3452. INTEREST DEFINED.**

14 **"(a) GENERAL RULE.**—For purposes of this chapter,
 15 the term 'interest' means—

16 **"(1) interest on evidences of indebtedness (includ-**
 17 **ing bonds, debentures, notes, and certificates) issued by**
 18 **a corporation with interest coupons or in registered**
 19 **form, and, to the extent provided in regulations pre-**

scribed by the Secretary or his delegate; interest on other evidences of indebtedness issued by a corporation of a type offered by corporations to the public;

“(2) interest on deposits with persons carrying on the banking business;

“(3) amounts (whether or not designated as interest) paid by a mutual savings bank, savings and loan association, building and loan association, cooperative bank, homestead association, credit union, or similar organization, in respect of deposits, investment certificates, or withdrawable or repurchasable shares;

“(4) interest on amounts held by an insurance company under an agreement to pay interest thereon;

“(5) interest on deposits with stockbrokers;

“(6) interest on obligations of the United States;

and

“(7) in the case of a non-interest-bearing obligation of the United States—

“(A) issued on a discount basis, and

“(B) having a maturity date more than one year from the date of issue,

the amount by which the amount paid on surrender or redemption exceeds the issue price.

“(b) EXCEPTIONS.—For purposes of this chapter, the term ‘interest’ does not include—

1 “(1) interest on obligations described in section
2 103(a) (1) or (3) (relating to interest on certain
3 governmental obligations);

4 “(2) any amount paid by—

5 “(A) a foreign government or international
6 organization;

7 “(B) a foreign corporation not engaged in
8 trade or business within the United States;

9 “(C) a nonresident alien individual not en-
10 gaged in trade or business within the United States;
11 or

12 “(D) a partnership not engaged in trade or
13 business within the United States and composed in
14 whole or in part of nonresident aliens;

15 “(3) interest on deposits with persons carrying on
16 the banking business paid to a person described in para-
17 graph (2) (B), (C), or (D);

18 “(4) any amount paid by one corporation to an-
19 other corporation, if both corporations are members of
20 the same affiliated group which filed a consolidated re-
21 turn for the preceding taxable year of the affiliated
22 group;

23 “(5) interest subject to withholding under subchap-
24 ter A of chapter 3 (sec. 1441 and following, relating to
25 withholding of tax on nonresident aliens and foreign cor-

perations) by the person paying such interest, or which would be so subject to withholding by such person, but for the fact that it is not treated as income from sources within the United States;

“(6) any amount on which the withholding agent is required to deduct and withhold a tax under section 1451 (relating to tax-free covenant bonds), or would be so required but for section 1451(d) (relating to benefit of personal exemptions);

“(7) to the extent provided in regulations prescribed by the Secretary or his delegate, any amount payable with respect to deposits in school savings accounts; and

“(8) any amount described in subsection (a)(2), (3), or (7) paid to a State or a foreign government or international organization (other than any amount described in subsection (a)(3) paid in respect of a transferable certificate or share).

“(c) EXEMPTION FOR UNITED STATES.—The Secretary may authorize exemption from the tax imposed by section 3451 for any amount paid by the United States or any wholly owned agency or instrumentality thereof to the United States or any wholly owned agency or instrumentality thereof if the Secretary determines that the imposition of the tax with respect to such amount will cause a burden

1 or expense which can be avoided by granting the tax
2 exemption.

3 **“Subchapter B—Dividends**

“Sec. 3461. Income tax collected at source on dividends.

“Sec. 3462. Dividend defined.

4 **“SEC. 3461. INCOME TAX COLLECTED AT SOURCE ON** 5 **DIVIDENDS.**

6 **“(a) REQUIREMENT OF WITHHOLDING.**—Except as
7 otherwise provided in this chapter, every person who pays
8 a dividend shall deduct and withhold on such dividend a tax
9 equal to 20 percent of the amount thereof.

10 **“(b) PAYEE UNKNOWN.**—If the withholding agent is
11 unable to determine the person to whom the dividend is
12 payable, the tax under this section shall be deducted and
13 withheld at the time payment of the dividend would be
14 made if such person were known.

15 **“(c) AMOUNT OF DIVIDEND UNKNOWN.**—If the with-
16 holding agent is unable to determine the portion of a dis-
17 tribution which is a dividend, the tax under this section
18 shall be computed on the entire amount of the distribution.

19 **“(d) CROSS REFERENCES.**—

“(1) For credit, against income tax of the recipient of the income, of amounts deducted and withheld under this section, see section 39.

“(2) For special rules as to credit or refund of such amounts, see sections 3484, 3485, 3486, 3487, and 3505.

“(3) For exemption from requirement of deducting and withholding on dividends paid to certain individuals, see section 3483.

1 **"SEC. 3462. DIVIDEND DEFINED.**

2 ~~"(a) GENERAL RULE.~~—For purposes of this chapter,
3 the term 'dividend' means—

4 ~~"(1)~~ any distribution by a corporation which is a
5 dividend (as defined in section 316); and

6 ~~"(2)~~ any payment made by a stockbroker to any
7 person as a substitute for a dividend (as so defined).

8 ~~"(b) EXCEPTIONS.~~—For purposes of this chapter, the
9 term 'dividend' does not include—

10 ~~"(1)~~ any amount paid in the stock, or rights to
11 acquire the stock, of the distributing corporation if the
12 distribution is not includible in gross income of the re-
13 cipient under the provisions of section 305 (relating to
14 distributions of stock and stock rights);

15 ~~"(2)~~ any distribution to the extent that, under
16 chapter 1—

17 ~~"(A)~~ the amount thereof is treated by the re-
18 cipient as an amount received on the sale or ex-
19 change of property, or

20 ~~"(B)~~ gain or loss to the recipient is not recog-
21 nized;

22 ~~"(3)~~ any amount which is includible in gross in-
23 come as a taxable dividend by reason of the provisions
24 of section 302 (relating to redemptions of stock), 306
25 (relating to dispositions of certain stock), 356 (relating

1 to receipt of additional consideration in connection with
 2 certain reorganizations), or ~~1081(c)(2)~~ (relating to
 3 certain distributions pursuant to order of the Securities
 4 and Exchange Commission);

5 “~~(4)~~ any amount paid by one corporation to an-
 6 other corporation, if both corporations are members of
 7 the same affiliated group which filed a consolidated re-
 8 turn for the preceding taxable year of the affiliated
 9 group;

10 “~~(5)~~ an amount which—

11 “~~(A)~~ is subject to withholding under subchap-
 12 ter A of chapter 3 (sec. 1441 and following, relating
 13 to withholding of tax on nonresident aliens and for-
 14 eign corporations) by the person paying such
 15 amount, or

16 “~~(B)~~ would be subject to withholding under
 17 such subchapter A by the person paying such
 18 amount but for—

19 “~~(i)~~ the fact that it is attributable to in-
 20 come from sources outside the United States, or

21 “~~(ii)~~ the fact that the payor thereof is
 22 excepted from the application of section
 23 1441(a) by the provisions of section 1441(c);

1 “(6) any amount paid by a foreign corporation not
2 engaged in trade or business within the United States;

3 “(7) any amount described in section 1373 (relat-
4 ing to undistributed taxable income of electing small
5 business corporations); and

6 “(8) amounts paid pursuant to the terms of a
7 lease entered into before January 1, 1954, if under such
8 lease the shareholders of the lessor corporation are en-
9 titled to such amounts without deduction for any tax
10 which any law of the United States might require to be
11 deducted and withheld on the payment of dividends.

12 **“Subchapter C—Patronage Dividends**

 “Sec. 3471. Income tax collected at source on patronage
 dividends.

 “Sec. 3472. Amounts subject to withholding.

13 **“SEC. 3471. INCOME TAX COLLECTED AT SOURCE ON** 14 **PATRONAGE DIVIDENDS.**

15 “(a) REQUIREMENT OF WITHHOLDING.—Except as
16 otherwise provided in this chapter, every cooperative to
17 which part I of subchapter T of chapter 1 applies which pays
18 an amount described in section 3472 shall deduct and with-
19 hold on such amount a tax equal to 20 percent of such
20 amount.

21 “(b) PAYEE UNKNOWN.—If the withholding agent is

1 unable to determine the person to whom the amount is pay-
 2 able, the tax under this section shall be deducted and with-
 3 held at the time payment of the amount would be made if
 4 such person were known.

5 “(e) CROSS REFERENCES.—

“(1) For credit, against income tax of the recipient of the income, of amounts deducted and withheld under this section, see section 39.

“(2) For special rules as to credit or refund of such amounts, see sections 3484, 3485, 3486, 3487, and 3505.

“(3) For exemption from requirement of deducting and withholding on amounts paid to certain individuals, see section 3483.

6 “SEC. 3472. AMOUNTS SUBJECT TO WITHHOLDING.

7 “(a) GENERAL RULE.—Except as otherwise provided
 8 in this section or section 3483, the amounts subject to deduc-
 9 tion and withholding under section 3471 are—

10 “(1) the amount of any patronage dividend (as
 11 defined in section 1388(a)) which is paid in money,
 12 qualified written notices of allocation (as defined in sec-
 13 tion 1388(c)), or other property (except nonqualified
 14 written notices of allocation as defined in section
 15 1388(d)), and

16 “(2) any amount, described in section 1382(e) (2)
 17 (A) (relating to certain nonpatronage distributions),
 18 which is paid in money, qualified written notices of al-
 19 location, or other property (except nonqualified written
 20 notices of allocation) by an organization exempt from

1 tax under section 521 (relating to exemption of farm-
2 ers' cooperatives from tax).

3 “(b) EXCEPTIONS.—The provisions of section 3471
4 shall not apply to—

5 “(1) any amount paid by one corporation to an-
6 other corporation, if both corporations are members of
7 the same affiliated group which filed a consolidated re-
8 turn for the preceding taxable year of the affiliated
9 group;

10 “(2) an amount which—

11 “(A) is subject to withholding under sub-
12 chapter A of chapter 3 (sec. 1441 and following,
13 relating to withholding of tax on nonresident aliens
14 and foreign corporations) by the person paying such
15 amount, or

16 “(B) would be subject to withholding under
17 such subchapter A by the person paying such
18 amount but for the fact that it is attributable to
19 income from sources outside the United States; and

20 “(3) any amount paid by a foreign corporation
21 not engaged in trade or business within the United
22 States.

23 “(c) EXEMPTION FOR CERTAIN CONSUMER COOPERA-
24 TIVES.—A cooperative which the Secretary or his delegate
25 determines is primarily engaged in selling at retail goods

1 or services of a type that are generally for personal, living,
 2 or family use shall, upon application to the Secretary or his
 3 delegate, be granted exemption from the tax imposed by
 4 section 3471. Application for exemption under this sub-
 5 section shall be made in accordance with regulations pre-
 6 scribed by the Secretary or his delegate.

7 “(d) DETERMINATION OF AMOUNT PAID.—For pur-
 8 poses of this subchapter, in determining amounts paid—

9 “(1) property (other than a written notice of
 10 allocation) shall be taken into account at its fair market
 11 value, and

12 “(2) a qualified written notice of allocation shall
 13 be taken into account at its stated dollar amount.

14 “Subchapter D—General Provisions

“Sec. 3481. Liability for return and payment of withheld
 tax.

“Sec. 3482. Return and payment by United States.

“Sec. 3483. Exemption certificates.

“Sec. 3484. Refund of tax to individuals.

“Sec. 3485. Refund of tax to States, tax-exempt organiza-
 tions, etc.

“Sec. 3486. Refund of tax to corporation.

“Sec. 3487. Credit for tax withheld on corporation.

“Sec. 3488. Obligation sold between interest-payment dates.

“Sec. 3489. Presumption.

“Sec. 3490. Definitions.

15 “SEC. 3481. LIABILITY FOR RETURN AND PAYMENT OF 16 WITHHELD TAX.

17 “(a) GENERAL RULE.—Every person required to de-
 18 duct and withhold any tax under this chapter shall, on or be-

1 fore the last day of the first month following the close of each
 2 quarter of his taxable year; make a return of the tax required
 3 to be deducted and withheld during such quarter and pay the
 4 tax to the officer designated in section 6151. The withhold-
 5 ing agent shall be liable for the payment of the taxes required
 6 to be deducted and withheld under this chapter, and shall not
 7 otherwise be liable to any person for the amount of any
 8 such payment.

9 “(b) TAX PAID BY RECIPIENT.—If the withholding
 10 agent, in violation of the provisions of this chapter, fails to
 11 deduct and withhold any tax under this chapter, and there-
 12 after the tax against which such tax may be credited is
 13 paid, the tax so required to be deducted and withheld shall
 14 not be collected from the withholding agent; but this sub-
 15 section shall in no case relieve the withholding agent from
 16 liability for any penalties or additions to the tax otherwise
 17 applicable in respect of such failure to deduct and withhold.

18 “(c) CROSS REFERENCE.—

“For limitation on the use of Government depositories
 in the collection of taxes deducted and withheld under
 this chapter, see the last sentence of section 6302(c).

19 “SEC. 3482. RETURN AND PAYMENT BY UNITED STATES.

20 “If the withholding agent is the United States the re-
 21 turn of the tax deducted and withheld under this chapter may

1 be made by an officer or employee of the United States
2 having control of the payment of the amount subject to
3 withholding, or appropriately designated for that purpose.

4 **"SEC. 3483. EXEMPTION CERTIFICATES.**

5 **~~"(a)~~ GENERAL RULES.—**

6 **~~"(1)~~ INDIVIDUALS UNDER AGE 18.—**Any indi-
7 vidual may file with any withholding agent an exemp-
8 tion certificate on which he certifies the date of his
9 birth. If such a certificate is filed, all amounts pay-
10 able by such withholding agent to such individual, on
11 and after the effective date for such certificate and
12 before the beginning of the calendar year during which
13 the certificate indicates that he will attain age 18, shall
14 be exempt from the requirement of deducting and with-
15 holding under this chapter.

16 **~~"(2)~~ INDIVIDUALS OVER AGE 17.—**Any individual
17 may file with any withholding agent an exemption
18 certificate on which he certifies—

19 **~~"(A)~~** that he will have attained age 18 before
20 the close of the calendar year for which such certifi-
21 cate is filed, and

22 **~~"(B)~~** that he reasonably believes that he will
23 not ~~(after the application of the credits against tax~~
24 ~~provided by part IV of subchapter A of chapter 1,~~
25 ~~other than the credits under sections 31 and 39)~~ be

liable for the payment of any tax under chapter 1 for each of his taxable years any portion of which is included in the period for which such certificate will be in effect.

If such a certificate is filed, all amounts payable by such withholding agent to such individual during the period such certificate is in effect shall be exempt from the requirement of deducting and withholding under this chapter. Except as may otherwise be provided in regulations prescribed by the Secretary or his delegate, an exemption certificate filed by an individual described in this paragraph shall remain in effect only for the period beginning on the effective date of such certificate and ending at the close of the calendar year in which such period begins.

~~“(3) TAX EXEMPT ORGANIZATIONS.—~~

~~“(A) Any organization (other than a cooperative described in section 521) which is exempt from the tax imposed by chapter 1 may file with any withholding agent who pays amounts described in section 3452(a) (2), (3), or (7) an exemption certificate on which it certifies that it is such an organization. If such a certificate is filed, all amounts described in section 3452(a) (2),~~

1 ~~(3)~~, and ~~(7)~~ payable by such withholding agent
 2 to such organization on and after the effective date
 3 for such certificate shall ~~(except as provided in sub-~~
 4 paragraph ~~(B)~~) be exempt from the requirement
 5 of deducting and withholding under this chapter.

6 “(B) An exemption certificate filed by an
 7 organization under subparagraph ~~(A)~~ shall cease
 8 to be effective on the thirtieth day after the day on
 9 which the withholding agent, with whom such cer-
 10 tificate was filed, is notified by either the organiza-
 11 tion or the Secretary or his delegate that the
 12 organization is no longer exempt from the tax im-
 13 posed by chapter 1. If an organization ceases to be
 14 exempt from such tax, it shall, within the time speci-
 15 fied in regulations prescribed by the Secretary or his
 16 delegate, so notify each withholding agent with
 17 whom it has an exemption certificate in effect.

18 “(b) EXCEPTIONS AND SPECIAL RULES.—

19 “~~(1)~~ CERTAIN EXCEPTIONS.—This section shall
 20 not apply to any amount—

21 “~~(A)~~ described in section 3452(a)(1) ~~(re-~~
 22 lating to interest on evidences of indebtedness);

23 “~~(B)~~ described in section 3452(a)(3) paid
 24 in respect of a transferable certificate or share, or

1 ~~“(C) described in section 3452(a)(6) (relat-~~
 2 ~~ing to interest on obligations of the United States).~~

3 ~~“(2) Series E BONDS, ETC.—In the case of trans-~~
 4 ~~actions involving the redemption of one or more obliga-~~
 5 ~~tions described in section 3452(a)(7) (relating to cer-~~
 6 ~~tain obligations of the United States issued on a discount~~
 7 ~~basis); a separate certificate shall be filed with respect~~
 8 ~~to each such transaction.~~

9 ~~“(3) NOMINEES, CUSTODIANS, AND JOINT OWNER-~~
 10 ~~SHIPS.—Under regulations prescribed by the Secretary~~
 11 ~~or his delegate, the exemption provided by subsection~~
 12 ~~(a) may be extended, in a manner consistent with the~~
 13 ~~other provisions of this section, to—~~

14 ~~“(A) amounts (other than amounts described~~
 15 ~~in section 3462(a), relating to dividends) paid~~
 16 ~~through nominees;~~

17 ~~“(B) amounts paid to custodians; and~~

18 ~~“(C) amounts paid jointly to 2 or more~~
 19 ~~individuals.~~

20 ~~“(4) EFFECTIVE DATE OF CERTIFICATE.—Any~~
 21 ~~exemption certificate under this section shall take effect~~
 22 ~~on such day as is specified in accordance with regula-~~
 23 ~~tions prescribed by the Secretary or his delegate.~~

24 ~~“(5) FORM AND CONTENTS OF CERTIFICATE AND~~

1 NOTICE.—Any exemption certificate under this section,
 2 and any notice under subsection ~~(a)(3)(B)~~, shall be
 3 in such form and contain such information as the Secre-
 4 tary or his delegate may by regulations prescribe.

5 “~~(c)~~ CROSS REFERENCE.—

“For penalty for filing fraudulent certificate, or for
 failing to provide notice, under this section, see section
 7205.

6 “SEC. 3484. REFUND OF TAX TO INDIVIDUALS.

7 “~~(a)~~ GENERAL RULE.—Except as provided in subsec-
 8 tion ~~(c)~~, the tax deducted and withheld under this chapter
 9 with respect to amounts received by an individual during
 10 any quarter ~~(other than the fourth quarter)~~ of his taxable
 11 year ~~(together with any tax so deducted and withheld on~~
 12 ~~amounts which were received by him during any prior quar-~~
 13 ~~ter of such year and with respect to which no allowable claim~~
 14 ~~for refund has been filed under this section)~~ shall, to the
 15 extent such tax does not exceed his refund allowance as of
 16 the time the claim for refund is filed, be promptly refunded
 17 to him as an overpayment of tax. A refund of tax shall be
 18 made under this section only if the amount claimed and
 19 allowable equals or exceeds \$10.

20 “~~(b)~~ REFUND ALLOWANCE.—For purposes of this sec-
 21 tion, the refund allowance of an individual as of the time the
 22 claim for refund is filed is an amount equal to the excess, if
 23 any, of—

1 “(1) an amount equal to 22 percent of—

2 “(A) the total of the deductions which, on the
3 basis of facts existing at the time the claim for refund
4 is filed, such individual would be allowed for the tax-
5 able year under section 151 (relating to deductions
6 for personal exemptions); plus

7 “(B) in the case of an individual who, at the
8 time the claim for refund is filed, reasonably ex-
9 pects that he will be allowed a credit under section
10 37 (relating to retirement income) for the taxable
11 year, the amount which, at such time, such individ-
12 ual reasonably expects to be the amount of his re-
13 tirement income (as defined in section 37(c) and as
14 limited by section 37(d)) for the taxable year,
15 less

16 “(C) the amounts (other than amounts on
17 which tax is required to be deducted and withheld
18 under this chapter) which, at the time the claim for
19 refund is filed, such individual reasonably expects
20 to be includible in his gross income for the taxable
21 year; over

22 “(2) the amounts of tax with respect to which an
23 allowable claim for refund has been previously filed
24 under this section during taxable year.

25 For purposes of paragraph (1)(C), an individual who files

1 more than one claim for refund under this section for any
 2 taxable year may use the estimate for the preceding claim
 3 for such year unless, at the time he files the claim, he reason-
 4 ably expects the amounts referred to in paragraph (1) (C)
 5 to exceed such prior estimate by more than \$100.

6 “(c) MARRIED INDIVIDUALS.—For purposes of subsec-
 7 tions (a), (b), and (d), married individuals shall be treated
 8 as an individual if, at the time the claim for refund is filed,
 9 they reasonably expect that they will file a joint return for
 10 the taxable year in which such claim is filed.

11 “(d) TIME FOR FILING CLAIM.—Not more than one
 12 claim may be filed under this section by any individual
 13 during any quarter of his taxable year. A refund of tax
 14 deducted and withheld on amounts received during a taxable
 15 year shall be made under this section only if claim therefor
 16 is filed on or before the last day of such taxable year.

17 “(e) INDIVIDUALS NOT ELIGIBLE FOR REFUND.—No
 18 claim for refund may be filed under this section by—

19 “(1) any individual (other than an individual
 20 referred to in paragraph (2) or (3)) unless, at the
 21 time the claim for refund is filed, he reasonably expects
 22 that his gross income for the taxable year will not ex-
 23 ceed \$5,000;

24 “(2) any married individual unless, at the time the
 25 claim for refund is filed, he reasonably expects that the

1 aggregate gross income of such individual and his spouse
2 for the taxable year will not exceed \$10,000;

3 “(3) a head of a household (as defined in section
4 1(b)(2)) or a surviving spouse (as defined in section
5 2(b)) unless, at the time the claim for refund is filed,
6 he reasonably expects that his gross income for the
7 taxable year will not exceed \$10,000; or

8 “(4) any child, unless, at the time the claim for
9 refund is filed, he reasonably expects that no deduction
10 would be allowed for him under section 151(c)(1)(B)
11 for the taxable year of his parent (or parents) begin-
12 ning with or within the calendar year in which the
13 claim for refund is filed.

14 “(f) CROSS REFERENCE.—

“For credit or refund of amounts not refunded
under this section, see section 39.

15 **“SEC. 3485. REFUND OF TAX TO STATES, TAX-EXEMPT**
16 **ORGANIZATIONS, ETC.**

17 “(a) GENERAL RULE.—In the case of a person which
18 is—

19 “(1) the United States or a State,

20 “(2) an organization (other than a cooperative
21 described in section 521) which is exempt from the tax
22 imposed by chapter 1,

1 ~~“(3) a foreign government or international organi-~~
 2 ~~zation, or~~

3 ~~“(4) a foreign central bank of issue,~~
 4 if the tax deducted and withheld under this chapter with re-
 5 spect to amounts received by such person during any calendar
 6 quarter exceeds the credit, if any, claimed by and allowable
 7 to such person under section 3505 (relating to credit against
 8 employment taxes) for such quarter, the excess (together
 9 with any such excess for any prior quarter of the same
 10 calendar year with respect to which no refund has been
 11 claimed and allowed under this section) shall be promptly
 12 refunded or credited to such person as an overpayment of
 13 tax. In the case of a person to which paragraph (4) ap-
 14 plies, the amount which may be refunded or credited under
 15 this section shall not exceed the amount of tax deducted
 16 and withheld under section 3451 on interest paid on obliga-
 17 tions of the United States which are not held for, or used in
 18 connection with, the conduct of commercial banking functions
 19 or other commercial activities.

20 ~~“(b) CROSS REFERENCES.—~~

~~“(1) For period of limitation for filing claim under
 this section, see section 6511.~~

~~“(2) For presumed date of payment for purposes of
 (A) period of limitation, see section 6513(b), and (B)
 allowance of interest on overpayments, see section
 6611(d).~~

1 **"SEC. 3486. REFUND OF TAX TO CORPORATION.**

2 "~~(a)~~ **GENERAL RULE.**—If the tax deducted and with-
 3 held under this chapter with respect to amounts received by
 4 a corporation ~~(other than a corporation described in section~~
 5 ~~3485(a))~~ during any quarter ~~(other than the fourth quar-~~
 6 ~~ter)~~ of its taxable year exceeds the amount claimed by and
 7 allowable to such corporation under section 3487 as a credit
 8 against its liability for tax under this chapter for such quar-
 9 ter, the excess ~~(together with any such excess for any prior~~
 10 ~~quarter of the same year with respect to which no refund has~~
 11 ~~been claimed and allowed under this section)~~ shall be
 12 promptly refunded or credited to such corporation as an over-
 13 payment of tax. A refund of tax shall be made under this
 14 section only if claim therefor is filed after the close of the
 15 period covered by the claim and on or before the last day
 16 of the taxable year.

17 "~~(b)~~ **CROSS REFERENCE.**—

"For credit or refund of amounts not refunded
 under this section, see section 39.

18 **"SEC. 3487. CREDIT FOR TAX WITHHELD ON CORPORA-**
 19 **TION.**

20 "~~(a)~~ **GENERAL RULE.**—Any tax deducted and with-
 21 held under this chapter with respect to amounts received
 22 by a corporation ~~(other than a corporation described in sec-~~

1 tion 3485(a)) during a taxable year shall, to the extent not
 2 claimed and allowable as a credit or refund to the corporation
 3 under section 3486, be allowed, under regulations prescribed
 4 by the Secretary or his delegate, as a credit against (but
 5 not in excess of) the tax for which such corporation is liable
 6 under this chapter in respect of amounts paid by it during
 7 such year.

8 “(b) DIVIDENDS AND PATRONAGE DIVIDENDS PAID
 9 DURING TAXABLE YEAR.—For purposes of determining the
 10 credit allowable to any corporation under subsection (a), a
 11 dividend, or amount subject to withholding under section
 12 3471, paid by it may be considered as having been paid
 13 during the taxable year—

14 “(1) in the case of a personal holding company, if
 15 treated as paid during such taxable year under section
 16 563(b),

17 “(2) in the case of a regulated investment com-
 18 pany, if treated as paid during such taxable year under
 19 section 855(a),

20 “(3) in the case of a real estate investment trust, if
 21 treated as paid during such taxable year under section
 22 858(a), or

“(4) in the case of a cooperative described in section 1381(a), if paid during the payment period (as defined in section 1382(d)) for such taxable year.

“(c) SPECIAL RULE FOR CORPORATIONS WHICH ARE MEMBERS OF AN AFFILIATED GROUP.—To the extent and subject to such conditions as may be provided in regulations prescribed by the Secretary or his delegate, the tax deducted and withheld under this chapter with respect to amounts received by a corporation which is a member of an affiliated group which filed a consolidated return for the preceding taxable year of the affiliated group may, for purposes of this section, be treated as tax deducted and withheld under this chapter from any corporation which is a member of the same affiliated group.

“SEC. 3488. OBLIGATION SOLD BETWEEN INTEREST-PAYMENT DATES.

“For purposes of any credit or refund provided in section 3484, 3485, 3486, or 3487, in the case of an obligation which is sold or exchanged between interest-payment dates the amount required to be deducted and withheld on the interest at the end of the interest-payment period shall be treated in the manner provided in section 39(c).

1 **“SEC. 3489. PRESUMPTION.**

2 “For purposes of establishing that any person is entitled
3 to a credit or refund of any tax required to be deducted and
4 withheld under this chapter with respect to amounts received
5 by such person, the correct amount of such tax shall, in the
6 absence of evidence to the contrary, be presumed to have
7 been so deducted and withheld.

8 **“SEC. 3490. DEFINITIONS.**

9 “For purposes of this chapter—

10 “~~(1)~~ PERSON.—The term ‘person’ includes the
11 United States, a State, a foreign government, and an
12 international organization.

13 “~~(2)~~ STATE.—The term ‘State’ includes a State, the
14 District of Columbia, a possession of the United States,
15 any political subdivision of any of the foregoing, and any
16 wholly owned agency or instrumentality of any one or
17 more of the foregoing.

18 “~~(3)~~ FOREIGN GOVERNMENT.—The term ‘foreign
19 government’ includes a foreign government, a politi-

1 eal subdivision of a foreign government, and any wholly
 2 owned agency or instrumentality of any one or more of
 3 the foregoing.

4 “(4) NONRESIDENT ALIEN.—The term ‘nonresident
 5 alien individual’ includes an alien resident of Puerto
 6 Rico.”

7 (2) CLERICAL AMENDMENTS, ETC.—

8 (A) The heading for subtitle C is amended to
 9 read as follows:

10 **["Subtitle C—Employment Taxes and**
 11 **Collection of Income Tax at Source"]**

12 (B) The table of chapters for subtitle C is
 13 amended by striking out the last line and inserting
 14 in lieu thereof the following:

“CHAPTER 25. Collection of income tax at source on interest,
 dividends, and patronage dividends.

“CHAPTER 26. General provisions relating to employment
 taxes and collection of income taxes at
 source.”

15 (C) The table of subtitles under the heading
 16 “Internal Revenue Title” at the beginning of the

1 Internal Revenue Code of 1954 is amended by
 2 striking out the third line and inserting in lieu
 3 thereof the following:

~~"SUBTITLE C. Employment taxes and collection of income
 tax at source."~~

4 ~~(D)~~ The heading for chapter 26 (as redesign-
 5 nated by paragraph ~~(1)~~ of this subsection) is
 6 amended to read as follows:

7 **~~"CHAPTER 26—GENERAL PROVISIONS RE-~~**
 8 **~~LATING TO EMPLOYMENT TAXES AND~~**
 9 **~~COLLECTION OF INCOME TAXES AT~~**
 10 **~~SOURCE"~~**

11 ~~(b) CREDITS AGAINST INCOME TAX FOR TAX WITH-~~
 12 ~~HELD.—~~

13 ~~(1) ALLOWANCE OF CREDIT.—~~Part IV of sub-
 14 chapter A of chapter 1 (relating to credits against tax)
 15 is amended by inserting after section 38 (added by
 16 section 2 of this Act) the following new section:

17 **~~"SEC. 39. TAX WITHHELD ON INTEREST, DIVIDENDS, AND~~**
 18 **~~PATRONAGE DIVIDENDS.~~**

19 ~~"(a) GENERAL RULE.—~~Under regulations prescribed
 20 by the Secretary or his delegate, the tax deducted and with-
 21 held under chapter 25 (relating to withholding at source
 22 on interest, dividends, and patronage dividends) shall be
 23 allowed, to the recipient of the amount with respect to which

1 such tax was deducted and withheld, as a credit against the
 2 tax imposed by this subtitle for the taxable year in which
 3 such amount is received.

4 “(b) SPECIAL RULE FOR DEPENDENT CHILDREN.—

5 If—

6 “(1) the taxpayer for his taxable year is entitled
 7 to a deduction under section 151(c) (1) (B) with re-
 8 spect to a child, and

9 “(2) such child had, for the calendar year ending
 10 with or within the taxpayer's taxable year—

11 “(A) gross income of less than \$600, and

12 “(B) no wages (as defined in section 3401
 13 (a)) with respect to which withholding was re-
 14 quired under chapter 24,

15 then, under regulations prescribed by the Secretary or his
 16 delegate, the taxpayer shall be entitled to the credit pro-
 17 vided by subsection (a) with respect to amounts received
 18 by such child during such calendar year, but only if such
 19 child has not filed any claim for credit or refund of any por-
 20 tion of the tax deducted and withheld with respect to such
 21 amounts.

22 “(c) APPORTIONMENT OF CREDIT.—For purposes of
 23 subsection (a), if an obligation is sold or exchanged between
 24 interest payments dates—

1 ~~(1)~~ so much of the amount required to be deducted
 2 and withheld on the interest at the end of the interest-
 3 payment period as is properly allocable to that part of
 4 such period which ends on the date of the sale or ex-
 5 change shall be treated as an amount deducted and with-
 6 held from the transferor on the date of the sale or
 7 exchange; and

8 ~~“(2)~~ so much of such amount as is properly al-
 9 locable to that part of such period which begins on the
 10 day after the date of the sale or exchange shall be treated
 11 as an amount deducted and withheld from the transferee.

12 ~~“(d)~~ LIMITATIONS.—The credit provided by subsection
 13 ~~(a)~~ shall not be allowed—

14 ~~“(1)~~ REFUND TO INDIVIDUALS.—To any indi-
 15 vidual with respect to any amount of tax allowed him
 16 as a refund under section 3484.

17 ~~“(2)~~ CREDIT OR REFUND TO STATES, ETC.—To
 18 any person with respect to any amount of tax allowable
 19 to such person as a credit or refund under section 3485
 20 or as a credit under section 3505.

21 ~~“(3)~~ CREDIT OR REFUND TO CORPORATIONS.—To
 22 any person with respect to any amount of tax allowed
 23 such person as a credit or refund under section 3486 or
 24 as a credit under section 3487.

1 “~~(4)~~ CERTAIN DEPENDENT CHILDREN.—To any
2 person with respect to any amount of tax which has
3 been claimed and is allowable as a credit to such
4 person's parent by reason of the provisions of subsection
5 ~~(b)~~.”

6 “~~(5)~~ NOMINEES, ETC.—To any person with respect
7 to any amount of tax allowed such person as a credit
8 under section 1444~~(b)~~.”

9 ~~(2)~~ COMMON TRUST FUNDS.—Section 584~~(c)~~ (re-
10 lating to the income of participants in the fund) is
11 amended by adding at the end thereof the following
12 new paragraph:

13 “~~(3)~~ TAX WITHHELD AT SOURCE ON INTEREST,
14 DIVIDENDS, AND PATRONAGE DIVIDENDS.—In any case
15 where tax under chapter 25 is deducted and withheld
16 on any amounts received by a common trust fund, for
17 purposes of any credit or refund provided in section 39
18 or 3505, or chapter 25, such tax shall, in accordance
19 with regulations prescribed by the Secretary or his dele-
20 gate, be considered as having been deducted and with-
21 held proportionately from each participant.”

22 ~~(3)~~ ESTATES AND TRUSTS.—Section 642~~(a)~~ (re-
23 lating to special rules for credits and deductions in the

1 case of estates and trusts) is amended by adding at the
2 end thereof the following new paragraph:

3 “(4) TAX WITHHELD AT SOURCE ON INTEREST,
4 DIVIDENDS, AND PATRONAGE DIVIDENDS.—In any case
5 where tax under chapter 25 is deducted and withheld
6 on any amounts received by an estate or trust, for pur-
7 poses of any credit or refund provided in section 39
8 or 3505, or chapter 25, such tax shall, in accordance
9 with regulations prescribed by the Secretary or his dele-
10 gate, be considered as having been deducted and with-
11 held from each beneficiary in an amount which, when
12 added to the amounts paid, credited, or required to be
13 distributed to him, equals the amounts which would
14 have been paid, credited, or required to be distributed
15 to him in the absence of chapter 25. Any tax under
16 chapter 25 which is deducted and withheld on amounts
17 received by the estate or trust shall be considered as
18 withheld from such estate or trust to the extent it is
19 not considered as withheld from a beneficiary under
20 the provisions of the preceding sentence.”

~~(4)~~ TECHNICAL AMENDMENTS.—

~~(A)~~ Section 164(b)(1) ~~(relating to deduc-~~
~~tion denied in the case of certain taxes)~~ is amended
 by—

~~(i)~~ striking out the word “and” at the end
 of subparagraph ~~(B)~~;

~~(ii)~~ striking out the comma at the end of
 subparagraph ~~(C)~~ and inserting “; and”; and

~~(iii)~~ adding after subparagraph ~~(C)~~ the
 following new subparagraph:

“~~(D)~~ the tax withheld at source under chapter
 25 ~~(relating to collection of income tax at source~~
~~on interest, dividends, and patronage dividends)~~,”.

~~(B)~~ Section 874(a) ~~(relating to allowance of~~
~~deductions and credits to nonresident alien indi-~~
~~viduals)~~ is amended by striking “31 and 32” and
 inserting in lieu thereof “31, 32, and 39”.

~~(C)~~ Section 1314(e) ~~(relating to inapplica-~~
~~bility of part II of subchapter Q of chapter 1 of~~
~~subtitle A to taxes imposed by subtitle C)~~ is

1 amended by striking “employment taxes” and in-
 2 serting in lieu thereof “employment taxes and
 3 collection of income tax at source”.

4 ~~(D)~~ Section 6211(b)(1) ~~(relating to rules~~
 5 ~~applicable in determination of deficiency)~~ is
 6 amended by striking “31” and inserting in lieu
 7 thereof “31 or 39”.

8 ~~(E)~~ The table of sections for part IV of sub-
 9 chapter A of chapter 1 is amended by striking out
 “Sec. 38. Overpayments of tax.”
 10 and inserting in lieu thereof

“Sec. 38. Investment in certain depreciable property.
 “Sec. 39. Tax withheld on interest, dividends, and patronage
 dividends.
 “Sec. 40. Overpayments of tax.”

11 ~~(c)~~ INTEREST AND DIVIDENDS PAID TO NONRESIDENT
 12 ALIENS, ETC.—

13 ~~(1)~~ WITHHOLDING RATE.—

14 ~~(A)~~ Section 1441 ~~(relating to withholding of~~
 15 ~~tax on nonresident aliens)~~ is amended by adding at
 16 the end thereof the following new subsection:

17 “~~(c)~~ TREATIES.—In the case of amounts described in
 18 section 3452(a) ~~(relating to interest)~~; section 3462(a)
 19 ~~(relating to dividends)~~; and section 3472(a) ~~(relating to~~
 20 ~~patronage dividends)~~; the tax required to be deducted and
 21 withheld under subsection (a) shall not by reason of the

1 provisions of any treaty be less than 20 percent of such
2 amounts.”

3 ~~(B)~~ Section 1442 ~~(relating to withholding of~~
4 tax on foreign corporations) is amended by adding
5 at the end thereof the following new sentence: “In
6 the case of amounts described in section 3452(a)
7 ~~(relating to interest)~~, section 3462(a) ~~(relating to~~
8 dividends), and section 3472(a) ~~(relating to pa-~~
9 tronage dividends), the tax required to be deducted
10 and withheld under the preceding sentence shall
11 not by reason of the provisions of any treaty be
12 less than 20 percent of such amounts.”

13 ~~(2)~~ NOMINEES, ETC.—Subchapter A of chapter
14 3 ~~(relating to withholding of tax on nonresident aliens~~
15 and foreign corporations) is amended by adding at the
16 end thereof the following new section:

17 **“SEC. 1444. INTEREST AND DIVIDENDS PAID TO NOMI-**
18 **NEES; CREDITS TO WITHHOLDING AGENTS.**

19 ~~“(a)~~ WITHHOLDING OF TAX BY PAYOR.—Under regu-
20 lations prescribed by the Secretary or his delegate, every
21 person who pays amounts subject to withholding under
22 chapter 25 and who has been notified by a payee thereof that
23 the payee is a nominee required to deduct and withhold
24 on such amounts under section 1441 or 1442 shall, in
25 lieu of the nominee, deduct and withhold from such amounts

1 paid to the nominee the tax required to be deducted and
 2 withheld under section 1441 or 1442, in the same manner
 3 as if such amounts were paid by such person directly to the
 4 beneficial owner thereof.

5 “(b) CREDITS TO WITHHOLDING AGENTS.—In the case
 6 of any person who is required to deduct and withhold tax
 7 under section 1441 or 1442 in respect of amounts received
 8 by him during any calendar year on which tax was deducted
 9 and withheld (or, in the case of amounts described in section
 10 39(c)(1), was treated as deducted and withheld) under
 11 chapter 25, the taxes so deducted and withheld (or treated
 12 as deducted and withheld) under chapter 25 shall, under
 13 regulations prescribed by the Secretary or his delegate, be
 14 allowed as a credit against (but not in excess of) his liability
 15 for the year in respect of the taxes imposed by sections 1441
 16 and 1442.”

17 (3) CLERICAL AMENDMENT.—The table of sec-
 18 tions for subchapter A of chapter 3 is amended by add-
 19 ing at the end thereof the following:

“Sec. 1444. Interest and dividends paid to nominees; credits
 to withholding agents.”

20 (d) CREDIT FOR STATES AND TAX-EXEMPT ORGANI-
 21 ZATIONS.—

22 (1) ALLOWANCE OF CREDIT.—Chapter 26 (gen-
 23 eral provisions relating to employment taxes and income

tax withheld at source) is amended by adding at the end thereof the following new section:

“SEC. 3505. SPECIAL CREDIT IN CASE OF STATES OR TAX-EXEMPT ORGANIZATIONS.

“(a) GENERAL RULE.—In the case of a person which is a State (as defined in section 3490(2)) or which is an organization (other than a cooperative described in section 521) which is exempt from the tax imposed by chapter 1, the tax deducted and withheld under chapter 25 with respect to amounts received by it during any calendar quarter shall be allowed, under regulations prescribed by the Secretary or his delegate, as a credit against (but not in excess of) such person’s liability (after the adjustments, if any, provided for in sections 6205(a) and 6413(a)) for such quarter in respect of the taxes imposed by chapter 21 (Federal Insurance Contributions Act) and by chapter 24 (collection of income tax at source on wages). Such credit shall be allowed only if claim therefor is made, in accordance with such regulations, at the time of the filing of the return with respect to the taxes under chapter 21 and chapter 24 for such quarter.

“(b) OBLIGATIONS SOLD BETWEEN INTEREST-PAYMENT DATES.—For purposes of this section, in the case of an obligation which is sold or exchanged between interest-payment dates, the amount required to be deducted and with-

1 held on the interest at the end of the interest-payment period
2 shall be treated in the manner provided in section 39(c).

3 “(c) CROSS REFERENCE.—

“For refund under chapter 25, see section 3485.”

4 (2) TECHNICAL AMENDMENTS.—

5 (A) Section 3502 (relating to nondeductibil-
6 ity of taxes in computing taxable income) is
7 amended by adding at the end thereof the following
8 new subsection:

9 “(c) The tax deducted and withheld under chapter 25
10 shall not be allowed as a deduction in computing taxable
11 income under subtitle A either to the person deducting and
12 withholding the tax or to the recipient of the amounts sub-
13 ject to withholding.”

14 (B) The table of sections for chapter 26 is
15 amended by adding at the end thereof the following:

“Sec. 3505. Special credit in case of States or tax-exempt
organizations.”

16 (c) OTHER TECHNICAL AMENDMENTS.—

17 (1) DECLARATION OF ESTIMATED INCOME TAX
18 BY INDIVIDUALS.—Section 6015(a) (relating to dec-
19 laration of estimated income tax by individuals) is
20 amended by striking out the period at the end of para-
21 graph (2) and inserting in lieu thereof “and amounts on
22 which tax is required to be deducted and withheld under
23 chapter 25.”

~~(2)~~ **ADJUSTMENT OF TAX; UNDERPAYMENT.—**

~~(A)~~ Subsection ~~(a)(1)~~ of section 6205 (relating to special rules relating to assessment of employment taxes) is amended by striking out “or 3402 is paid with respect to any payment of wages or compensation,” and inserting in lieu thereof “3402, 3451, 3461, or 3471 is paid with respect to any payment of remuneration, interest, dividends, or other amounts,”.

~~(B)~~ Subsection ~~(b)~~ of such section is amended by striking out “or 3402 is paid or deducted with respect to any payment of wages or compensation” and inserting in lieu thereof “3402, 3451, 3461, or 3471 is paid or deducted with respect to any payment of remuneration, interest, dividends, or other amounts”.

~~(C)~~ The heading for such section is amended to read as follows:

“SEC. 6205. SPECIAL RULES APPLICABLE TO CERTAIN TAXES UNDER SUBTITLE C.”

~~(D)~~ The table of sections for subchapter A of chapter 63 is amended by striking out

“Sec. 6205. Special rules applicable to certain employment taxes.”

and inserting in lieu thereof

“Sec. 6205. Special rules applicable to certain taxes under subtitle C.”

1 ~~(3)~~ USE OF GOVERNMENT DEPOSITARIES.—Section
 2 6302(e) ~~(relating to use of Government depositaries)~~
 3 is amended by adding at the end thereof the following
 4 new sentence: “The Secretary or his delegate shall
 5 not require the deposit under this subsection of any
 6 tax deducted and withheld under chapter 25 ~~(relating~~
 7 to collection of income tax at source on interest, divi-
 8 dends, and patronage dividends) in a Government
 9 depository before the last day prescribed in section 3481
 10 for payment of the tax.”

11 ~~(4)~~ EXCESSIVE WITHHOLDING.—Section 6401
 12 ~~(b)~~ ~~(relating to excessive withholding)~~ is amended to
 13 read as follows:

14 “~~(b)~~ EXCESSIVE WITHHOLDING.—If the amounts al-
 15 lowable as credits under section 31 ~~(relating to credit for tax~~
 16 withheld at source under chapter 24) and section 39 ~~(relat-~~
 17 ing to credit for tax withheld on interest, dividends, and
 18 patronage dividends under chapter 25) exceed the taxes
 19 imposed by chapter 1 against which such credits are allow-
 20 able, the amount of such excess shall be considered an over-
 21 payment.”

22 ~~(5)~~ ADJUSTMENT OF TAX; OVERPAYMENT.—

23 ~~(A)~~ Subsection ~~(a)~~(1) of section 6413 ~~(re-~~
 24 lating to special credit and refund rules applicable

to certain employment taxes) is amended by striking out “or 3402 is paid with respect to any payment of remuneration,” and inserting in lieu thereof “3402, 3451, 3461, or 3471 is paid with respect to any payment of remuneration, interest, dividends, or other amounts.”.

(B) Subsection (b) of such section is amended—

(i) By striking from the heading of such subsection the words “OF CERTAIN EMPLOYMENT TAXES”; and

(ii) By striking out “or 3402 is paid or deducted with respect to any payment of remuneration” and inserting in lieu thereof “3402, 3451, 3461, or 3471 is paid or deducted with respect to any payment of remuneration, interest, dividends, or other amounts”.

(C) The following new subsection is added at the end of such section:

“(e) CROSS REFERENCES.—

“For special refunds or credits of tax withheld on interest, dividends, or patronage dividends under chapter 25, see sections 3484, 3485, 3486, 3487, and 3505.”

1 ~~(D)~~ The heading for such section is amended
2 to read as follows:

3 **~~“SEC. 6413. SPECIAL RULES APPLICABLE TO CERTAIN~~**
4 **~~TAXES UNDER SUBTITLE C.”~~**

5 ~~(E)~~ The table of sections for subchapter B of
6 chapter 65 is amended by striking out

 “Sec. 6413. Special rules applicable to certain employment
 taxes.”

7 and inserting in lieu thereof

 “Sec. 6413. Special rules applicable to certain taxes under
 subtitle C.”

8 ~~(6)~~ OVERPAYMENT NOT DEDUCTED AND WITH-
9 HELD.—Section 6414 (relating to income tax withheld)
10 is amended by striking “chapter 3” and inserting in lieu
11 thereof “chapter 3 or 25”.

12 ~~(7)~~ TIME TAX CONSIDERED PAID.—Section 6513
13 ~~(b)~~ (relating to time tax considered paid) is amended
14 by adding at the end thereof the following new sen-
15 tences: “For purposes of section 6511 or 6512, any
16 tax deducted and withheld under chapter 25 which is
17 allowable under section 39, 3484, 3485, or 3486
18 as a credit against tax or as a refund of an overpayment
19 (or an amount treated as an overpayment) of the tax
20 imposed by chapter 1 shall, in respect of the person en-
21 titled to such credit or refund, be deemed to have been
22 paid by him on the last day prescribed for filing the re-

turn ~~(determined without regard to any extension of~~
time for filing such return) of tax under chapter 1 for
his taxable year in which the amount subject to with-
holding under chapter 25 is received by him or, if such
person has no taxable year, on the fifteenth day of the
fifth calendar month following the close of such person's
annual accounting period within which such amount
is received by him. In the case of an amount allowable
as a credit under section 39(b) to the parent of a child,
such amount shall, if claimed by the parent, be deemed
to have been paid on the last day for filing his return
~~(determined without regard to any extension of time~~
for filing such return) for his taxable year which begins
with or within the calendar year in which amounts sub-
ject to withholding under chapter 25 were received by
the child."

~~(8)~~ FAILURE TO PAY ESTIMATED INCOME TAX.—

~~(A)~~ INDIVIDUALS.—Subsections ~~(e)~~ and ~~(f)~~
of section 6654 ~~(relating to failure by individual to~~
pay estimated income tax) are amended to read as
follows:

~~"(e)~~ APPLICATION OF SECTION IN CASE OF WITH-
HELD TAXES.—For purposes of applying this section—

~~"(1)~~ the estimated tax shall be computed without
any reduction for amounts which the individual estimates

1 as his credits under section 31 (relating to tax withheld
 2 at source on wages) and section 39 (relating to tax with-
 3 held on interest, dividends, and patronage dividends);
 4 and

5 “(2) the amount of the credits allowed under sec-
 6 tions 31 and 39 for the taxable year shall be deemed
 7 a payment of estimated tax; and an equal part of such
 8 amount shall be deemed paid on each installment date
 9 (determined under section 6153) for such taxable year;
 10 unless the taxpayer establishes the dates on which all
 11 amounts were actually withheld (or in the case of
 12 amounts described in section 39(e)(1), were treated
 13 as withheld); in which case the amounts so withheld
 14 shall be deemed payments of estimated tax on such
 15 dates.

16 “(f) TAX COMPUTED AFTER APPLICATION OF
 17 CREDITS AGAINST TAX.—For purposes of subsections (b)
 18 and (d), the term ‘tax’ means the tax imposed by chapter
 19 1 reduced by the credits against tax allowed by part IV of
 20 subchapter A of chapter 1, other than the credits against
 21 tax provided by section 31 (relating to tax withheld on
 22 wages) and section 39 (relating to tax withheld on interest,
 23 dividends, and patronage dividends).”

24 (B) CORPORATIONS.—Section 6655 (relating

to failure by corporation to pay estimated income tax) is amended—

(i) by striking out the period at the end of subsection (e)(2)(B) and inserting in lieu thereof “, other than the credit against tax provided by section 39 (relating to tax withheld on interest, dividends, and patronage dividends).”; and

(ii) by redesignating subsection (f) as subsection (g) and inserting after subsection (e) the following new subsection:

“(f) APPLICATION OF SECTION IN CASE OF TAX WITHHELD ON INTEREST, DIVIDENDS, AND PATRONAGE DIVIDENDS.—For purposes of applying this section—

“(1) the estimated tax shall be computed without any reduction for the amount which the corporation estimates as its credit under section 39 (relating to tax withheld on interest, dividends, and patronage dividends); and

“(2) the amount of the credit allowed under section 39 for the taxable year shall be deemed a payment of estimated tax, and an equal part of such amount shall be deemed paid on each installment date (determined under section 6154) for such taxable year, unless the

1 corporation establishes the dates on which all amounts
 2 were actually withheld (or in the case of amounts de-
 3 scribed in section 39(e)(1), were treated as withheld),
 4 in which case the amounts so withheld shall be deemed
 5 payments of estimated tax on such dates."

6 ~~(9)~~ PENALTY FOR FILING FRAUDULENT EXEMP-
 7 TION CERTIFICATE.—Section 7205 (relating to fraudu-
 8 lent withholding exemption certificate or failure to sup-
 9 ply information) is amended by adding the following
 10 new sentence at the end thereof: "Any person who
 11 willfully files an exemption certificate with any with-
 12 holding agent under section 3483, on which the certifica-
 13 tion is known by him to be fraudulent or to be false as
 14 to any material matter, or who is required to file a notice
 15 under subsection ~~(a)(3)(B)~~ of section 3483 and who
 16 willfully fails to provide such notice in the manner, at
 17 the time, and showing the information required under
 18 such subsection ~~(a)(3)(B)~~, or the regulations pre-
 19 scribed thereunder, shall, in lieu of any penalty otherwise
 20 provided, upon conviction thereof, be fined not more than
 21 \$500, or imprisoned not more than 1 year, or both."

22 ~~(10)~~ OFFENSES WITH RESPECT TO COLLECTED
 23 TAXES.—The last sentence of section 7215(b) (relating
 24 to offenses with respect to collected taxes) is amended to
 25 read as follows: "For purposes of paragraph (2), a lack

of funds existing immediately after the payment of wages or amounts subject to withholding under chapter 25 (whether or not created by the payment of such wages or amounts) shall not be considered to be circumstances beyond the control of a person."

(11) DEFINITION OF WITHHOLDING AGENT.—Section 7701(a)(16) (defining the term "withholding agent") is amended by striking out "or 1461" and inserting in lieu thereof "1461, 3451, 3461, or 3471".

(f) EFFECTIVE DATES.—

(1) GENERAL RULE.—Except as provided in paragraph (2), the provisions of this section shall apply in the case of interest and dividends paid on or after January 1, 1963.

(2) SPECIAL RULES.—

(A) In the case of transferable obligations described in paragraph (1) or (6) of section 3452(a) of the Internal Revenue Code of 1954, the provisions of this section shall apply only to interest paid with respect to interest payment periods commencing on or after January 1, 1963.

(B) The provisions of this section shall apply to amounts described in section 3472 of such Code paid on or after January 1, 1963, with respect to

1 patronage occurring on or after the first day of the
 2 first taxable year of the cooperative beginning on
 3 or after January 1, 1963.

4 **SEC. 19. REPORTING OF INTEREST, DIVIDEND, AND PATRON-**
 5 **AGE DIVIDEND PAYMENTS OF \$10 OR MORE DURING**
 6 **A YEAR.**

7 (a) RETURNS REGARDING PAYMENT OF DIVI-
 8 DENDS.—Section 6042 (relating to returns regarding cor-
 9 porate dividends, earnings, and profits) is amended to read
 10 as follows:

11 **“SEC. 6042. RETURNS REGARDING PAYMENTS OF DIVIDENDS**
 12 **AND CORPORATE EARNINGS AND PROFITS**

13 **“(a) REQUIREMENT OF REPORTING.—**

14 **“(1) IN GENERAL.—Every person—**

15 **“(A) who makes payments of dividends aggreg-**
 16 **ating \$10 or more to any other person during any**
 17 **calendar year, or**

18 **“(B) who receives payments of dividends as a**
 19 **nominee and who makes payments aggregating \$10**
 20 **or more during any calendar year to any other per-**
 21 **son with respect to the dividends so received,**

22 **shall make a return according to the forms or regulations**
 23 **prescribed by the Secretary or his delegate, setting forth**
 24 **the aggregate amount of such payments and the name**
 25 **and address of the person to whom paid.**

“(2) *RETURNS REQUIRED BY THE SECRETARY.*—

Every person who makes payments of dividends aggregating less than \$10 to any other person during any calendar year shall, when required by the Secretary or his delegate, make a return setting forth the aggregate amount of such payments, and the name and address of the person to whom paid.

“(b) *DIVIDEND DEFINED.*—

“(1) *GENERAL RULE.*—For purposes of this section, the term ‘dividend’ means—

“(A) any distribution by a corporation which is a dividend (as defined in section 316); and

“(B) any payment made by a stockbroker to any person as a substitute for a dividend (as so defined).

“(2) *EXCEPTIONS.*—For purposes of this section, the term ‘dividend’ does not include—

“(A) to the extent provided in regulations prescribed by the Secretary or his delegate, any distribution or payment—

“(i) by a foreign corporation, or

“(ii) to a foreign corporation, a nonresident alien, or a partnership not engaged in trade or business in the United States and

1 *composed in whole or in part of nonresident*
 2 *aliens; and*

3 “(B) any amount described in section 1373
 4 *(relating to undistributed taxable income of elect-*
 5 *ing small business corporations).*

6 “(3) *SPECIAL RULE.*—If the person making any
 7 *payment described in subsection (a)(1) (A) or (B) is*
 8 *unable to determine the portion of such payment which is*
 9 *a dividend or is paid with respect to a dividend, he shall,*
 10 *for purposes of subsection (a)(1), treat the entire*
 11 *amount of such payment as a dividend or as an amount*
 12 *paid with respect to a dividend.*

13 “(c) *STATEMENTS TO BE FURNISHED TO PERSONS*
 14 *WITH RESPECT TO WHOM INFORMATION IS FUR-*
 15 *NISHED.*—Every person making a return under subsection
 16 *(a)(1) shall furnish to each person whose name is set forth*
 17 *in such return a written statement showing—*

18 “(1) *the name and address of the person making*
 19 *such return, and*

20 “(2) *the aggregate amount of payments to the per-*
 21 *son as shown on such return.*

22 *The written statement required under the preceding sentence*
 23 *shall be furnished to the person on or before January 31 of*
 24 *the year following the calendar year for which the return*
 25 *under subsection (a)(1) was made. No statement shall be*

1 *required to be furnished to any person under this subsection*
 2 *if the aggregate amount of payments to such person as shown*
 3 *on the return made under subsection (a) (1) is less than \$10.*

4 “(d) *STATEMENTS TO BE FURNISHED BY CORPORA-*
 5 *TIONS TO SECRETARY.*—Every corporation shall, when re-
 6 *quired by the Secretary or his delegate—*

7 “(1) *furnish to the Secretary or his delegate a state-*
 8 *ment stating the name and address of each shareholder,*
 9 *and the number of shares owned by each shareholder;*

10 “(2) *furnish to the Secretary or his delegate a*
 11 *statement of such facts as will enable him to determine*
 12 *the portion of the earnings and profits of the corporation*
 13 *(including gains, profits, and income not taxed) accum-*
 14 *ulated during such periods as the Secretary or his dele-*
 15 *gate may specify, which have been distributed or ordered*
 16 *to be distributed, respectively, to its shareholders during*
 17 *such taxable years as the Secretary or his delegate may*
 18 *specify; and*

19 “(3) *furnish to the Secretary or his delegate a*
 20 *statement of its accumulated earnings and profits and*
 21 *the names and addresses of the individuals or share-*
 22 *holders who would be entitled to such accumulated earn-*
 23 *ings and profits if divided or distributed, and of the*
 24 *amounts that would be payable to each.”*

25 (b) *RETURNS REGARDING PAYMENT OF PATRONAGE*

1 *DIVIDENDS.*—Section 6044 (relating to returns regarding
2 patronage dividends) is amended to read as follows:

3 “SEC. 6044. RETURNS REGARDING PAYMENTS OF PATRONAGE
4 *DIVIDENDS.*

5 “(a) *REQUIREMENT OF REPORTING.*—

6 “(1) *IN GENERAL.*—Except as otherwise provided
7 in this section, every cooperative to which part I of sub-
8 chapter T of chapter 1 applies, which makes payments
9 of amounts described in subsection (b) aggregating \$10
10 or more to any person during any calendar year, shall
11 make a return according to the forms or regulations
12 prescribed by the Secretary or his delegate, setting forth
13 the aggregate amount of such payments and the name
14 and address of the person to whom paid.

15 “(2) *RETURNS REQUIRED BY THE SECRETARY.*—
16 Every such cooperative which makes payments of
17 amounts described in subsection (b) aggregating less
18 than \$10 to any person during any calendar year shall,
19 when required by the Secretary or his delegate, make a
20 return setting forth the aggregate amount of such pay-
21 ments and the name and address of the person to whom
22 paid.

23 “(b) *AMOUNTS SUBJECT TO REPORTING.*—

24 “(1) *GENERAL RULE.*—Except as otherwise pro-

vided in this section, the amounts subject to reporting under subsection (a) are—

“(A) the amount of any patronage dividend (as defined in section 1388 (a)) which is paid in money, qualified written notices of allocation (as defined in section 1388 (c)), or other property (except nonqualified written notices of allocation as defined in section 1388 (d)),

“(B) any amount described in section 1382(c)(2)(A) (relating to certain nonpatronage distributions) which is paid in money, qualified written notices of allocation, or other property (except nonqualified written notices of allocation) by an organization exempt from tax under section 521 (relating to exemption of farmers’ cooperatives from tax), and

“(C) any amount described in section 1382(b)(2) (relating to redemption of nonqualified written notices of allocation) and, in the case of an organization described in section 1381(a)(1), any amount described in section 1382(c)(2)(B) (relating to redemption of nonqualified written notices of allocation paid with respect to earnings derived from sources other than patronage).

1 “(2) *EXCEPTIONS.*—The provisions of subsection
2 “(a) shall not apply, to the extent provided in regulations
3 prescribed by the Secretary or his delegate, to any
4 payment—

5 “(A) by a foreign corporation, or

6 “(B) to a foreign corporation, a nonresident
7 alien, or a partnership not engaged in trade or
8 business in the United States and composed in whole
9 or in part of nonresident aliens.

10 “(c) *EXEMPTION FOR CERTAIN CONSUMER COOPER-*
11 *ATIVES.*—A cooperative which the Secretary or his delegate
12 determines is primarily engaged in selling at retail goods
13 or services of a type that are generally for personal, living,
14 or family use shall, upon application to the Secretary or his
15 delegate, be granted exemption from the reporting require-
16 ments imposed by subsection (a). Application for exemption
17 under this subsection shall be made in accordance with regu-
18 lations prescribed by the Secretary or his delegate.

19 “(d) *DETERMINATION OF AMOUNT PAID.*—For pur-
20 poses of this section, in determining the amount of any
21 payment—

22 “(1) property (other than a qualified written notice
23 of allocation) shall be taken into account at its fair
24 market value, and

“(2) a qualified written notice of allocation shall be taken into account at its stated dollar amount.

“(e) STATEMENTS TO BE FURNISHED TO PERSONS WITH RESPECT TO WHOM INFORMATION IS FURNISHED.—Every cooperative making a return under subsection (a)(1) shall furnish to each person whose name is set forth in such return a written statement showing—

“(1) the name and address of the cooperative making such return, and

“(2) the aggregate amount of payments to the person as shown on such return.

The written statement required under the preceding sentence shall be furnished to the person on or before January 31 of the year following the calendar year for which the return under subsection (a)(1) was made. No statement shall be required to be furnished to any person under this subsection if the aggregate amount of payments to such person as shown on the return made under subsection (a)(1) is less than \$10.”

(c) RETURNS REGARDING PAYMENT OF INTEREST.—Subpart B of part III of subchapter A of chapter 61 (relating to information returns) is amended by adding after section 6047 (as added by section 7(f) of this Act) the following new section:

1 **“SEC. 6048. RETURNS REGARDING PAYMENTS OF INTEREST.**

2 **“(a) REQUIREMENT OF REPORTING.—**

3 **“(1) IN GENERAL.—***Every person—*

4 *“(A) who makes payments of interest (as de-*
5 *defined in subsection (b)) aggregating \$10 or more*
6 *to any other person during any calendar year, or*

7 *“(B) who receives payments of interest as a*
8 *nominee and who makes payments aggregating \$10*
9 *or more during any calendar year to any other*
10 *person with respect to the interest so received.*

11 *shall make a return according to the forms or regula-*
12 *tions prescribed by the Secretary or his delegate, setting*
13 *forth the aggregate amount of such payments and the*
14 *name and address of the person to whom paid.*

15 **“(2) RETURNS REQUIRED BY THE SECRETARY.—**

16 *Every person who makes payments of interest (as defined*
17 *in subsection (b)) aggregating less than \$10 to any other*
18 *person during any calendar year shall, when required*
19 *by the Secretary or his delegate, make a return setting*
20 *forth the aggregate amount of such payments and the*
21 *name and address of the person to whom paid.*

22 **“(3) OTHER RETURNS REQUIRED BY SECRE-**

23 **TARY.—***Every corporation making payments, regardless*
24 *of amounts, of interest other than interest as defined in*
25 *subsection (b) shall, when required by regulations pre-*

scribed by the Secretary or his delegate, make a return according to the forms or regulations prescribed by the Secretary or his delegate, setting forth the amount paid and the name and address of the recipient of each such payment.

“(b) *INTEREST DEFINED.*—

“(1) *GENERAL RULE.*—For purposes of subsections (a) (1) and (2), the term ‘interest’ means—

“(A) interest on evidences of indebtedness (including bonds, debentures, notes, and certificates) issued by a corporation in registered form, and, to the extent provided in regulations prescribed by the Secretary or his delegate, interest on other evidences of indebtedness issued by a corporation of a type offered by corporations to the public;

“(B) interest on deposits with persons carrying on the banking business;

“(C) amounts (whether or not designated as interest) paid by a mutual savings bank, savings and loan association, building and loan association, cooperative bank, homestead association, credit union, or similar organization, in respect of deposits, investment certificates, or withdrawable or repurchasable shares;

“(D) interest on amounts held by an insurance

1 *company under an agreement to pay interest thereon;*
 2 *and*

3 *“(E) interest on deposits with stockbrokers and*
 4 *dealers in securities.*

5 *“(2) EXCEPTIONS.—For purposes of subsections*
 6 *(a) (1) and (2), the term ‘interest’ does not include—*

7 *“(A) interest on obligations described in section*
 8 *103(a) (1) or (3) (relating to interest on certain*
 9 *governmental obligations);*

10 *“(B) to the extent provided in regulations pre-*
 11 *scribed by the Secretary or his delegate, any amount*
 12 *paid by or to a foreign corporation, a nonresident*
 13 *alien, or a partnership not engaged in trade or*
 14 *business in the United States and composed in whole*
 15 *or in part of nonresident aliens; and*

16 *“(C) any amount on which the person making*
 17 *payment is required to deduct and withhold a tax*
 18 *under section 1451 (relating to tax-free covenant*
 19 *bonds), or would be so required but for section*
 20 *1451(d) (relating to benefit of personal exemp-*
 21 *tions).*

22 *“(c) STATEMENTS TO BE FURNISHED TO PERSONS*
 23 *WITH RESPECT TO WHOM INFORMATION IS FUR-*
 24 *NISHED.—Every person making a return under subsection*

1 (a)(1) shall furnish to each person whose name is set forth
 2 in such return a written statement showing—

3 “(1) the name and address of the person making
 4 such return, and

5 “(2) the aggregate amount of payments to the per-
 6 son as shown on such return.

7 The written statement required under the preceding sentence
 8 shall be furnished to the person on or before January 31
 9 of the year following the calendar year for which the return
 10 under subsection (a)(1) was made. No statement shall be
 11 required to be furnished to any person under this subsection
 12 if the aggregate amount of payments to such person as shown
 13 on the return made under subsection (a)(1) is less than \$10.”

14 (d) *PENALTIES FOR FAILURE TO FILE INFORMATION*
 15 *RETURNS.*—Section 6652 (relating to failure to file certain
 16 information returns) is amended to read as follows:

17 “SEC. 6652. *FAILURE TO FILE CERTAIN INFORMATION RE-*
 18 *TURNS.*

19 “(a) *RETURNS RELATING TO PAYMENTS OF DIVI-*
 20 *DENDS, INTEREST, AND PATRONAGE DIVIDENDS.*—In the
 21 case of each failure to file a statement of the aggregate
 22 amount of payments to another person required by section
 23 6042(a)(1) (relating to payments of dividends aggregating
 24 \$10 or more), section 6044(a)(1) (relating to payments of

1 patronage dividends aggregating \$10 or more), or section
2 6048(a)(1) (relating to payments of interest aggregating
3 \$10 or more), on the date prescribed therefor (determined
4 with regard to any extension of time for filing), unless it is
5 shown that such failure is due to reasonable cause and not to
6 willful neglect, there shall be paid (upon notice and demand
7 by the Secretary or his delegate and in the same manner as
8 tax), by the person failing to so file the statement, \$10 for
9 each such statement not so filed, but the total amount imposed
10 on the delinquent person for all such failures during any
11 calendar year shall not exceed \$25,000.

12 “(b) OTHER RETURNS.—In the case of each failure to
13 file a statement of a payment to another person required un-
14 der authority of section 6041 (relating to certain information
15 at source), section 6042(a)(2) (relating to payments of
16 dividends aggregating less than \$10), section 6044(a)(2)
17 (relating to payments of patronage dividends aggregating
18 less than \$10), section 6048(a)(2) (relating to payments
19 of interest aggregating less than \$10), section 6048(a)(3)
20 (relating to other payments of interest by corporations),
21 or section 6051(d) (relating to information returns with
22 respect to income tax withheld), on the date prescribed there-
23 for (determined with regard to any extension of time for
24 filing), unless it is shown that such failure is due to reason-
25 able cause and not to willful neglect, there shall be paid

1 *(upon notice and demand by the Secretary or his delegate*
 2 *and in the same manner as tax) by the person failing to so*
 3 *file the statement, \$1 for each such statement not so filed,*
 4 *but the total amount imposed on the delinquent person for*
 5 *all such failures during the calendar year shall not exceed*
 6 *\$1,000.*

7 “(c) *ALCOHOL AND TOBACCO TAXES.*—

“For penalties for failure to file certain information returns with respect to alcohol and tobacco taxes, see, generally, subtitle E.”

8 (e) *PENALTIES FOR FAILURE TO FURNISH STATE-*
 9 *MENTS TO PERSONS WITH RESPECT TO WHOM RETURNS*
 10 *ARE FILED.*—Subchapter B of chapter 68 (relating to
 11 *assessable penalties)* is amended by adding after section 6677
 12 *(as added by section 7(g) of this Act)* the following new
 13 *section:*

14 “**SEC. 6678. FAILURE TO FURNISH CERTAIN STATEMENTS.**

15 *“In the case of each failure to furnish a statement under*
 16 *section 6042(c), 6044(e), or section 6048(c) on the date*
 17 *prescribed therefor to a person with respect to whom a return*
 18 *has been made under section 6042(a)(1), 6044(a)(1), or*
 19 *6048(a)(1), respectively, unless it is shown that such failure*
 20 *is due to reasonable cause and not to willful neglect, there*
 21 *shall be paid (upon notice and demand by the Secretary or*
 22 *his delegate and in the same manner as tax), by the person*

1 failing to so furnish the statement, \$10 for each such state-
 2 ment not so furnished, but the total amount imposed on the
 3 delinquent person for all such failures during any calendar
 4 year shall not exceed \$25,000.”

5 (f) *TECHNICAL AMENDMENTS.*—Section 6041 (relat-
 6 ing to information at source) is amended—

7 (1) by striking out, in subsection (a) thereof,
 8 “(other than payments described in section 6042(1) or
 9 section 6045)” and inserting in lieu thereof “(other than
 10 payments to which section 6042(a)(1), 6044(a)(1),
 11 or 6048(a)(1) applies, and other than payments with
 12 respect to which a statement is required under the au-
 13 thority of section 6042(a)(2), 6044(a)(2), 6045,
 14 6048(a)(2), or 6048(a)(3))”; and

15 (2) by striking out subsection (c) thereof.

16 (g) *CLERICAL AMENDMENTS.*—

17 (1) The table of sections for subpart B of part III
 18 of subchapter A of chapter 61 is amended—

19 (A) by striking out

“Sec. 6042. Returns regarding corporate dividends, earn-
 ings, and profits.”

20 and inserting in lieu thereof

“Sec. 6042. Returns regarding payments of dividends and
 corporate earnings and profits.”;

1 (B) by striking out

"Sec. 6044. Returns regarding patronage dividends."

2 and inserting in lieu thereof

"Sec. 6044. Returns regarding payments of patronage dividends.";

3 and

4 (C) by adding at the end of such table the
5 following:

"Sec. 6048. Returns regarding payments of interest."

6 (2) The table of sections for subchapter B of chap-
7 ter 68 is amended by adding at the end thereof the fol-
8 lowing:

"Sec. 6678. Failure to furnish certain statements."

9 (h) EFFECTIVE DATES.—

10 (1) DIVIDENDS AND INTEREST.—The amendments
11 made by this section shall apply to payments of dividends
12 and interest made on or after January 1, 1963.

13 (2) PATRONAGE DIVIDENDS.—The amendments
14 made by this section shall apply to payments of amounts
15 described in section 6044(b) of the Internal Revenue
16 Code of 1954 made on or after January 1, 1963,
17 with respect to patronage occurring on or after the first
18 day of the first taxable year of the cooperative beginning
19 on or after January 1, 1963.

1 **SEC. 20. INFORMATION WITH RESPECT TO CERTAIN**
2 **FOREIGN ENTITIES.**

3 (a) INFORMATION TO BE FURNISHED BY INDIVID-
4 UALS, DOMESTIC CORPORATIONS, ETC., WITH RESPECT
5 TO CERTAIN FOREIGN CORPORATIONS.—Section 6038 is
6 amended to read as follows:

7 **“SEC. 6038. INFORMATION WITH RESPECT TO CERTAIN**
8 **FOREIGN CORPORATIONS.**

9 **“(a) REQUIREMENT.—**

10 **“(1) IN GENERAL.—**Every United States person
11 shall furnish, with respect to any foreign corporation
12 which such person controls (within the meaning of
13 subsection (d) (1)), such information as the Secretary
14 or his delegate may prescribe by regulations relating to—

15 **“(A)** the name, the principal place of busi-
16 ness, and the nature of business of such foreign
17 corporation, and the country under whose laws
18 incorporated;

19 **“(B)** the accumulated profits (as defined in
20 section 902 (c)) of such foreign corporation, in-
21 cluding the items of income (whether or not in-
22 cluded in gross income under chapter 1) , deductions
23 (whether or not allowed in computing taxable in-
24 come under chapter 1) , and any other items taken
25 into account in computing such accumulated profits;

1 “(C) a balance sheet for such foreign corpora-
2 tion listing assets, liabilities, and capital;

3 “(D) transactions between such foreign cor-
4 poration and—

5 “(i) such person,

6 “(ii) any other corporation which such
7 person controls, and

8 “(iii) any United States person owning,
9 at the time the transaction takes place, 10 per-
10 cent or more of the value of any class of stock
11 outstanding of such foreign corporation; and

12 “(E) a description of the various classes of
13 stock outstanding, and a list showing the name and
14 address of, and number of shares held by, each
15 United States person who is a shareholder of record
16 owning at any time during the annual accounting
17 period 5 percent or more in value of any class of
18 stock outstanding of such foreign corporation.

19 The Secretary or his delegate may also require the fur-
20 nishing of any other information which is similar or
21 related in nature to that specified in the preceding
22 sentence.

23 “(2) PERIOD FOR WHICH INFORMATION IS TO BE
24 FURNISHED, ETC.—The information required under para-
25 graph (1) shall be furnished for the annual accounting

1 period of the foreign corporation ending with or within
2 the United States person's taxable year. The informa-
3 tion so required shall be furnished at such time and in
4 such manner as the Secretary or his delegate shall by
5 regulations prescribe.

6 “(3) LIMITATION.—No information shall be re-
7 quired to be furnished under this subsection with respect
8 to any foreign corporation for any annual accounting
9 period unless such information was required to be fur-
10 nished under regulations in effect on the first day of such
11 annual accounting period.

12 “(b) EFFECT OF FAILURE TO FURNISH INFORMA-
13 TION.—

14 “(1) IN GENERAL.—If a United States person fails
15 to furnish, within the time prescribed under paragraph
16 (2) of subsection (a), any information with respect to
17 any foreign corporation required under paragraph (1)
18 of subsection (a), then—

19 “(A) in applying section 901 (relating to
20 taxes of foreign countries and possessions of the
21 United States) to such United States person for the
22 taxable year, the amount of taxes (other than taxes
23 reduced under subparagraph (B)) paid or deemed
24 paid (other than those deemed paid under section
25 904 (d)) to any foreign country or possession of the

United States for the taxable year shall be reduced by 10 percent, and

“(B) in applying sections 902 (relating to foreign tax credit for corporate stockholder in foreign corporation) and ~~957~~ 960 (relating to special rules for foreign tax credit) to any such United States person which is a corporation (or to any person who acquires from any other person any portion of the interest of such other person in any such foreign corporation, but only to the extent of such portion) for any taxable year, the amount of taxes paid or deemed paid by each foreign corporation with respect to which such person is required to furnish information during the annual accounting period or periods with respect to which such information is required under paragraph (2) of subsection (a) shall be reduced by 10 percent.

If such failure continues 90 days or more after notice by the Secretary or his delegate to the United States person, then the amount of the reduction under this ~~subsection~~ *paragraph* shall be 10 percent plus an additional 5 percent for each 3-month period, or fraction thereof, during which such failure to furnish information continues after the expiration of such 90-day period.

“(2) *LIMITATION.*—*The amount of the reduction*

1 *under paragraph (1) for each failure to furnish infor-*
 2 *mation with respect to a foreign corporation required*
 3 *under subsection (a)(1) shall not exceed whichever of*
 4 *the following amounts is the greater:*

5 “(A) \$10,000, or

6 “(B) *the income of the foreign corporation for*
 7 *its annual accounting period with respect to which*
 8 *the failure occurs.*

9 “~~(2)~~ (3) SPECIAL RULES.—

10 “(A) No taxes shall be reduced under this sub-
 11 section more than once for the same failure.

12 “(B) For purposes of this subsection, the time
 13 prescribed under paragraph (2) of subsection (a)
 14 to furnish information (and the beginning of the
 15 90-day period after notice by the Secretary) shall
 16 be treated as being not earlier than the last day on
 17 which (as shown to the satisfaction of the Secretary
 18 or his delegate) reasonable cause existed for failure
 19 to furnish such information.

20 “(C) In applying subsections (a) and (b) of
 21 section 902, and in applying subsection (a) of sec-
 22 tion ~~956~~ 960, the reduction provided by this subsec-
 23 tion shall not apply for purposes of determining the
 24 amount of accumulated profits in excess of in-
 25 come, war profits, and excess profits taxes.

1 “(c) TWO OR MORE PERSONS REQUIRED TO FURNISH
2 INFORMATION WITH RESPECT TO SAME FOREIGN COR-
3 PORATION.—Where, but for this subsection, two or more
4 United States persons would be required to furnish informa-
5 tion under subsection (a) with respect to the same foreign
6 corporation for the same period, the Secretary or his dele-
7 gate may by regulations provide that such information shall
8 be required only from one person. To the extent practicable,
9 the determination of which person shall furnish the informa-
10 tion shall be made on the basis of actual ownership of stock.

11 “(d) DEFINITIONS.—For purposes of this section—

12 “(1) CONTROL.—A person is in control of a cor-
13 poration if such person owns stock possessing more than
14 50 percent of the total combined voting power of all
15 classes of stock entitled to vote, or more than 50 per-
16 cent of the total value of shares of all classes of stock,
17 of a corporation. If a person is in control (within the
18 meaning of the preceding sentence) of a corporation
19 which in turn owns more than 50 percent of the total
20 combined voting power of all classes of stock entitled to
21 vote of another corporation, or owns more than 50 per-
22 cent of the total value of the shares of all classes of stock
23 of another corporation, then such person shall be
24 treated as in control of such other corporation. For
25 purposes of this paragraph, the rules prescribed by

1 section 318(a) for determining ownership of stock
 2 shall apply; ~~except that clause (i) of section 318(a)~~
 3 ~~(2)(C) shall be applied without regard to the 50 per-~~
 4 ~~cent limitation contained in such section. except that—~~

5 “(A) the second sentence of subparagraphs
 6 (A) and (B), and clause (ii) of subparagraph
 7 (C), of section 318(a)(2) shall not be applied so
 8 as to consider a United States person as owning
 9 stock which is owned by a person who is not a United
 10 States person, and

11 “(B) in applying clause (i) of subparagraph
 12 (C) of section 318(a)(2), the phrase ‘10 percent’
 13 shall be substituted for the phrase ‘50 percent’ used
 14 in subparagraph (C).

15 “(2) ANNUAL ACCOUNTING PERIOD.—The annual
 16 accounting period of a foreign corporation is the annual
 17 period on the basis of which such corporation regularly
 18 computes its income in keeping its books.

19 “(e) CROSS REFERENCES.—

“(1) For provisions relating to penalties for violations
 of this section, see section 7203.

“(2) For definition of the term ‘United States person’.
 see section 7701(a)(30).”

20 (b) INFORMATION AS TO ORGANIZATION OR REOR-
 21 GANIZATION OF FOREIGN CORPORATIONS AND AS TO AC-
 22 QUISSIONS OF THEIR STOCK.—Section 6046 (relating to

1 returns as to creation or organization, or reorganization, of
 2 foreign corporations) is amended to read as follows:

3 **"SEC. 6046. RETURNS AS TO ORGANIZATION OR REORGAN-**
 4 **IZATION OF FOREIGN CORPORATIONS AND**
 5 **AS TO ACQUISITIONS OF THEIR STOCK.**

6 **"(a) REQUIREMENT OF RETURN.**—A return comply-
 7 ing with the requirements of subsection (b) shall be made
 8 by—

9 **"(1)** each United States citizen or resident who
 10 is ~~an officer or director of a foreign corporation on Jan-~~
 11 ~~uary 1, 1963~~ *on January 1, 1963, an officer or director*
 12 *of a foreign corporation, 5 percent or more in value of*
 13 *the stock of which is owned by a United States person, or*
 14 who becomes such an officer or director at any time
 15 after such date,

16 **"(2)** each United States person who on January
 17 1, 1963, owns 5 percent or more in value of the stock
 18 of a foreign corporation, or who, at any time after such
 19 date—

20 **"(A)** acquires stock which, when added to any
 21 stock owned on January 1, 1963, has a value equal
 22 to 5 percent or more of the value of the stock of a
 23 foreign corporation, or

24 **"(B)** acquires an additional 5 percent or more
 25 in value of the stock of a foreign corporation, and

1 “(3) each person who at any time after January 1,
2 1963, becomes a United States person while owning
3 5 percent or more in value of the stock of a foreign
4 corporation.

5 “(b) FORM AND CONTENTS OF RETURNS.—The re-
6 turns required by subsection (a) shall be in such form and
7 shall set forth, in respect of the foreign corporation, such
8 information as the Secretary or his delegate prescribes by
9 forms or regulations as necessary for carrying out the pro-
10 visions of the income tax laws, *except that in the case of*
11 *persons described only in subsection (a)(1) the information*
12 *required shall be limited to the names and addresses of persons*
13 *described in subsection (a)(2).*

14 “(c) OWNERSHIP OF STOCK.—For purposes of subsec-
15 tion (a) ~~(2)~~ and ~~(3)~~, stock owned directly or indirectly by
16 a person (including, in the case of an individual, stock owned
17 by members of his family) shall be taken into account. For
18 purposes of the preceding sentence, the family of an indi-
19 vidual shall be considered as including only his brothers
20 and sisters (whether by the whole or half blood), spouse,
21 ancestors, and lineal descendants.

1 “(d) **TIME FOR FILING.**—Any return required by sub-
 2 section (a) shall be filed on or before the 90th day after
 3 the day on which, under any provision of subsection (a), the
 4 United States citizen, resident, or person becomes liable to
 5 file such return.

6 “(e) **LIMITATION.**—*No information shall be required*
 7 *to be furnished under this section with respect to any foreign*
 8 *corporation unless such information was required to be fur-*
 9 *nished under regulations which, on the date on which the*
 10 *United States citizen, resident, or person becomes liable to*
 11 *file a return required under subsection (a)—*

12 (1) *if such liability arises on or after January 1,*
 13 *1963, and before March 1, 1963, have been in effect*
 14 *since January 1, 1963 (but only if such regulations*
 15 *were prescribed before December 1, 1962), or*

16 (2) *if such liability arises on or after March 1,*
 17 *1963, have been in effect for at least 90 days.*

18 “~~(e)~~ (f) **CROSS REFERENCE.**—

“For provisions relating to penalties for violations of
 this section, see sections 6678 6679 and 7203.”

1 (c) CIVIL PENALTY FOR FAILURE TO FILE RETURN.—

2 Subchapter B of chapter 68 (relating to assessable penal-
3 ties) is amended by adding ~~at the end thereof~~ *after section*
4 *6678 (as added by section 19(e) of this Act)* the following
5 new section:

6 “SEC. ~~6678~~ 6679. FAILURE TO FILE RETURNS AS TO OR-
7 GANIZATION OR REORGANIZATION OF
8 FOREIGN CORPORATIONS AND AS TO
9 ACQUISITIONS OF THEIR STOCK.

10 “(a) CIVIL PENALTY.—In addition to any criminal
11 penalty provided by law, any person required to file a return
12 under section 6046 who fails to file such return at the time
13 provided in such section, or who files a return which does
14 not show the information required pursuant to such section,
15 shall pay a penalty of \$1,000, unless it is shown that such
16 failure is due to reasonable cause.

17 “(b) DEFICIENCY PROCEDURES NOT TO APPLY.—Sub-
18 chapter B of chapter 63 (relating to deficiency procedure
19 for income, estate, and gift taxes) shall not apply in respect
20 of the assessment or collection of any penalty imposed by
21 subsection (a).”

22 (d) TECHNICAL AMENDMENTS.—

23 (1) Section 318 (b) (relating to cross references)
24 is amended by striking out “and” at the end of paragraph
25 (5), by striking out the period at the end of paragraph

1 (6) and inserting in lieu thereof “; and”, and by add-
 2 ing at the end thereof the following:

“(7) section 6038(d)(2) (relating to information with respect to certain foreign corporations).”

3 (2) The table of sections for subpart B of part III
 4 of subchapter A of chapter 61 is amended by striking
 5 out

“Sec. 6046. Returns as to creation or organization, or re-organization, of foreign corporations.”

6 and inserting in lieu thereof

“Sec. 6046. Returns as to organization or reorganization of foreign corporations and as to acquisitions of their stock.”

7 (3) The table of sections for subchapter B of chap-
 8 ter 68 is amended by adding at the end thereof the
 9 following:

“Sec. ~~6678~~ 6679. Failure to file returns as to organization or reorganization of foreign corporations and as to acquisitions of their stock.”

10 (e) EFFECTIVE DATE.—

11 (1) The amendments made by subsection (a) shall
 12 apply with respect to annual accounting periods of
 13 foreign corporations beginning after December 31, 1962.

14 (2) The amendments made by subsection (b) shall
 15 take effect on January 1, 1963.

16 *SEC. 21. EXPENDITURES BY FARMERS FOR CLEARING LAND.*

17 (a) *ALLOWANCE OF DEDUCTION.*—Part VI of sub-
 18 chapter B of chapter 1 (relating to itemized deductions for

1 individuals and corporations) is amended by adding after
2 section 181 (as added by section 2(c) of this Act) the
3 following new section:

4 **“SEC. 182. EXPENDITURES BY FARMERS FOR CLEARING LAND.**

5 “(a) *IN GENERAL.*—A taxpayer engaged in the busi-
6 ness of farming may elect to treat expenditures which are
7 paid or incurred by him during the taxable year in the clear-
8 ing of land for the purpose of making such land suitable
9 for use in farming as expenses which are not chargeable to
10 capital account. The expenditures so treated shall be allowed
11 as a deduction.

12 “(b) *LIMITATION.*—The amount deductible under sub-
13 section (a) for any taxable year shall not exceed whichever
14 of the following amounts is the lesser:

15 “(1) \$5,000, or

16 “(2) 25 percent of the taxable income derived from
17 farming during the taxable year.

18 For purposes of paragraph (2), the term ‘taxable income
19 derived from farming’ means the gross income derived from
20 farming reduced by the deductions allowed by this chapter
21 (other than by this section) which are attributable to the
22 business of farming.

23 “(c) *DEFINITIONS.*—For purposes of subsection (a)—

24 “(1) The term ‘clearing of land’ includes (but is
25 not limited to) the eradication of trees, stumps, and brush,

1 *the treatment or moving of earth, and the diversion of*
 2 *streams and watercourses.*

3 “(2) *The term ‘land suitable for use in farming’*
 4 *means land which as a result of the activities described*
 5 *in paragraph (1) is suitable for use by the taxpayer or*
 6 *his tenant for the production of crops, fruits, or other*
 7 *agricultural products or for the sustenance of livestock.*

8 “(d) *EXCEPTIONS, ETC.—*

9 “(1) *EXCEPTIONS.—The expenditures to which*
 10 *subsection (a) applies shall not include—*

11 “(A) *the purchase, construction, installation,*
 12 *or improvement of structures, appliances, or facili-*
 13 *ties which are of a character which is subject to the*
 14 *allowance for depreciation provided in section 167,*
 15 *or*

16 “(B) *any amount paid or incurred which is*
 17 *allowable as a deduction without regard to this*
 18 *section.*

19 “(2) *CERTAIN PROPERTY USED IN THE CLEARING*
 20 *OF LAND.—*

21 “(A) *ALLOWANCE FOR DEPRECIATION.—The*
 22 *expenditures to which subsection (a) applies shall*
 23 *include a reasonable allowance for depreciation with*
 24 *respect to property of the taxpayer which is used in*
 25 *the clearing of land for the purpose of making such*

1 *land suitable for use in farming and which, if used*
 2 *in a trade or business, would be property subject*
 3 *to the allowance for depreciation provided by sec-*
 4 *tion 167.*

5 “(B) *TREATMENT AS DEPRECIATION DEDUC-*
 6 *TION.—For purposes of this chapter, any expendi-*
 7 *ture described in subparagraph (A) shall, to the*
 8 *extent allowed as a deduction under subsection (a),*
 9 *be treated as an amount allowed under section 167*
 10 *for exhaustion, wear and tear, or obsolescence of the*
 11 *property which is used in the clearing of land.*

12 “(e) *ELECTION.—The election under subsection (a) for*
 13 *any taxable year shall be made within the time prescribed*
 14 *by law (including extensions thereof) for filing the return*
 15 *for such taxable year. Such election shall be made in such*
 16 *manner as the Secretary or his delegate may by regulations*
 17 *prescribe. Such election may not be revoked except with*
 18 *the consent of the Secretary or his delegate.”*

19 (b) *CLERICAL AMENDMENT.—The table of sections*
 20 *for such part VI is amended by adding at the end thereof*
 21 *the following:*

“*Sec. 182. Expenditures by farmers for clearing land.*”

22 (c) *EFFECTIVE DATE.—The amendments made by this*
 23 *section shall apply with respect to taxable years beginning*
 24 *after December 31, 1962.*

1 SEC. 22. CHARITABLE CONTRIBUTIONS MADE FROM INCOME
2 ATTRIBUTABLE TO SEVERAL TAXABLE YEARS.

3 (a) TREATMENT FOR PURPOSES OF PART I OF SUB-
4 CHAPTER Q.—Section 1307 (relating to rules applicable to
5 part I of subchapter Q) is amended by adding at the end
6 thereof the following new subsection:

7 “(e) ELECTION WITH RESPECT TO CHARITABLE
8 CONTRIBUTIONS.—In the case of an individual who elects
9 (in such manner and at such time as the Secretary or his
10 delegate prescribes by regulations) to have the provisions of
11 this subsection apply, an amount received or accrued to which
12 this part applies shall be reduced, for purposes of computing
13 the tax liability of the taxpayer under this part with respect
14 to the amount so received or accrued, by an amount equal to
15 that portion of (1) the amount of charitable contributions
16 made by the taxpayer during the taxable year in which the
17 amount is so received or accrued which are allowable as a
18 deduction for such year under section 170 (determined with-
19 out regard to this part), as (2) the amount received or ac-
20 crued to which this part applies is of the adjusted gross income
21 for the taxable year (determined without regard to this part).
22 In any case in which the taxpayer elects to have the pro-
23 visions of this subsection apply, no portion of the amount to
24 which this part applies shall, for purposes of computing
25 the limitation on tax under this part, be taken into account

1 *for purposes of computing the limitation under section*
 2 *170(b)(1) for the taxable year in which the amount to*
 3 *which this part applies is received or accrued.”*

4 (b) *EFFECTIVE DATE.*—*The amendment made by sub-*
 5 *section (a) shall apply with respect to amounts received or*
 6 *accrued in taxable years beginning after December 31, 1961.*

7 *SEC. 23. EFFECTIVE DATE OF SECTION 1371(c) OF THE INTERNAL*
 8 *REVENUE CODE OF 1954.*

9 (a) *IN GENERAL.*—*Subject to the provisions of subsec-*
 10 *tion (b), section 1371(c) of the Internal Revenue Code of*
 11 *1954 (as added by section 2(a) of the Act entitled “An Act*
 12 *to amend the Internal Revenue Code of 1954 to provide a*
 13 *personal exemption for children placed for adoption and to*
 14 *clarify certain provisions relating to the election of small busi-*
 15 *ness corporations as to taxable status”, approved September*
 16 *23, 1959 (Public Law 86-376)), shall (notwithstanding*
 17 *the provisions of the first sentence of section 2(d) of such*
 18 *Act) also apply to taxable years beginning after December*
 19 *31, 1957, and before January 1, 1960.*

20 (b) *ELECTION AND CONSENT BY CORPORATIONS;*
 21 *CONSENTS BY SHAREHOLDERS.*—*Subsection (a) shall apply*
 22 *with respect to any corporation and its shareholders only if,*
 23 *within one year after the date of the enactment of this Act—*

24 (1) *such corporation (in such manner as the Secre-*
 25 *tary of the Treasury or his delegate prescribes by regula-*

tions) elects to have the provisions of subsection (a) apply and consents to the application of subsection (c); and

(2) each person who is a shareholder of such corporation on the date on which such corporation makes such election, and each person who was a shareholder of such corporation during any taxable year of such corporation beginning after December 31, 1957, and ending before the date of such election, consents (in such manner and at such time as the Secretary of the Treasury or his delegate prescribes by regulations) to such election and to the application of subsection (c).

(c) *TOLLING OF STATUTES OF LIMITATIONS.*—In any case in which a corporation makes an election under subsection (b)—

(1) if the assessment of any deficiency against the corporation making such election, or any shareholder of such corporation who consents to such election, for any taxable year is prevented, at any time on or before the expiration of one year after the date of such election, by the operation of any law or rule of law, assessment of such deficiency may, nevertheless, be made, to the extent such deficiency is attributable to the application of subsection (a), at any time on or before the expiration of such one-year period; and

(2) if credit or refund of any overpayment of tax

1 *by the corporation making such election, or any share-*
2 *holder of such corporation who consents to such election,*
3 *for any taxable year is prevented, at any time on or*
4 *before the expiration of one year after the date of such*
5 *election, by the operation of any law or rule of law,*
6 *credit or refund of such overpayment may, nevertheless,*
7 *be allowed or made, to the extent such overpayment is*
8 *attributable to the application of subsection (a), if claim*
9 *therefor is filed on or before the expiration of such*
10 *one-year period.*

11 **SEC. 24. CERTAIN LOSSES SUSTAINED IN CONVERTING FROM**
12 **STREET RAILWAY TO BUS OPERATIONS.**

13 *(a) IN GENERAL.—If a corporation has a net operating*
14 *loss for the taxable year ending December 31, 1953, or the*
15 *taxable year ending December 31, 1954, principally as the*
16 *result of conversion from street railways to bus operations*
17 *with respect to part or all of the company's operations, then*
18 *its unused conversion loss will be subject to the treatment*
19 *provided in subsection (c).*

20 *(b) UNUSED CONVERSION LOSS DEFINED.—The*
21 *amount of the unused conversion loss shall be the aggregate*
22 *of the net operating losses for years described in subsection*
23 *(a) reduced to the extent that they have been used as net oper-*
24 *ating loss carryovers or carrybacks to reduce taxable income*
25 *for any taxable year beginning before January 1, 1960.*

26 *(c) TREATMENT OF UNUSED CONVERSION LOSS.—If*

1 a taxpayer has an unused conversion loss, then in determin-
 2 ing the amount of the net operating loss carryover from the
 3 taxable year ending December 31, 1959, to each of the 5 tax-
 4 able years following such taxable year for purposes of sec-
 5 tion 172 of the Internal Revenue Code of 1954, such unused
 6 conversion loss shall be treated as a net operating loss for the
 7 taxable year ending December 31, 1959. This subsection
 8 shall apply only for years in which the taxpayer is engaged
 9 in the furnishing or sale of transportation (as defined in
 10 section 1503(c)(1)(A) of the Internal Revenue Code of
 11 1954).

12 (d) REGULATIONS.—The Secretary of the Treasury, or
 13 his delegate, may prescribe by regulation such rules as may
 14 be necessary to carry out the purposes of this section.

15 SEC. 25. PENSION PLAN OF LOCAL UNION NUMBERED 435, INTER-
 16 NATIONAL HOD CARRIERS' BUILDING AND COMMON
 17 LABORERS' UNION OF AMERICA.

18 The pension plan of Local Union Numbered 435 of the
 19 International Hod Carriers' Building and Common
 20 Laborers' Union of America, which was negotiated to take
 21 effect May 1, 1960, pursuant to an agreement between such
 22 union and the Building Trades Employers Association of
 23 Rochester, New York, Incorporated, and which has been
 24 held by the Internal Revenue Service to constitute a qualified
 25 trust under section 401(a) of the Internal Revenue Code
 26 of 1954, and to be exempt from taxation under section

1 *No provision of this Act shall apply in any case where*
 2 *its application would be contrary to any treaty obligation*
 3 *of the United States.*

Passed the House of Representatives March 29, 1962.

Attest:

RALPH R. ROBERTS,

Clerk.

Calendar No. 1843

87TH CONGRESS
2^D SESSION

H. R. 10650

[Report No. 1881]

AN ACT

To amend the Internal Revenue Code of 1954 to provide a credit for investment in certain depreciable property, to eliminate certain defects and inequities, and for other purposes.

APRIL 2, 1962

Read twice and referred to the Committee on Finance

AUGUST 16 (legislative day, AUGUST 15), 1962

Reported with amendments

Digest of CONGRESSIONAL PROCEEDINGS

OF INTEREST TO THE DEPARTMENT OF AGRICULTURE

OFFICE OF
BUDGET AND FINANCE

(For information only;
should not be quoted
or cited)

Issued August 24, 1962
For actions of August 23, 1962
87th-2d, No. 150

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		World Food Congress.....12

HIGHLIGHTS: Sen. Humphrey commended farm bill as passed by Senate. Senate passed bill to transfer Sec. 32 funds to Commerce for lumber research. Senate committee reported bill to authorize joint watershed surveys by USDA and Army. Senate received State proposal for holding World Food Congress. Rep. Schwengel opposed passage of public works acceleration bill.

SENATE

1. FARM PROGRAM. Sen. Humphrey reviewed and commended the provisions of the farm bill as passed by the Senate, expressed regret that it did not contain a dairy provision, and stated that "We can improve upon it and we will improve upon it, but we have made a good start in adopting an effective program for American agriculture." pp. 16374-5

2. FORESTRY. Passed as reported S. 3517, to provide for the transfer from this Department to the Commerce Department Sec. 32 funds equal to 50 percent of the gross receipts from the duties collected on lumber, flooring, mouldings, and plywood for research and experimentation on lumber production and marketing. p. 16289

The Subcommittee on Public Lands of the Interior and Insular Affairs Committee approved for full committee consideration with amendment S. 3335, to authorize the transfer of land in Mont. from the Beaverhead National Forest to the Big Hole National Battlefield. p. D761

3. WATERSHEDS. The Public Works Committee reported without amendment H. R. 3801, to authorize the Secretary of the Army and the Secretary of Agriculture to make joint surveys and investigations of watershed areas for flood prevention or the conservation, development, utilization, and disposal of water (S. Rept. 1910). p. 16284
4. WETLANDS. Passed as reported H. R. 8520, to prohibit assistance under the agricultural conservation program for wetland drainage in N. Dak., S. Dak., and Minn. on any farm where the Secretary of the Interior finds that wildlife preservation would be harmed thereby and that nondrainage will contribute to wildlife conservation. pp. 16288-9
5. RESEARCH. Passed without amendment H. R. 6984, to provide that provision may be made in cost-type research and development contracts (including grants) with universities, colleges, and other educational institutions for payment of reimbursable indirect costs on the basis of predetermined fixed-percentage rates applied to the total, or an element thereof, of the reimbursable direct costs incurred. This bill will now be sent to the President. p. 16289
6. TAXATION. As reported (see Digest 145), H. R. 10650, the proposed Revenue Act of 1962, provides that cooperatives are to receive a deduction for patronage dividends paid to the patrons in cash or by allocations if the patron has the option to redeem the allocations in cash during a 90-day period after issuance, or consents to treating this income as constructively received and reinvested in the cooperative. The patron may give his consent individually in writing, the cooperative may by its bylaws require members to give this consent, or patrons may give their consent by endorsing a check representing at least 20 percent of the total patronage dividend. At least 20 percent of the patronage dividend must be paid in cash for any allocation to be deductible to the cooperative. Any of the amounts which are deductible to the cooperative must be included in the income of the patron for tax purposes when received if the amounts arise from business activity of the patron. (These provisions do not apply to REA cooperatives). Also, the bill includes a provision permitting farmers to deduct, in computing their Federal income tax, expenditures incurred by them in clearing land to make it suitable for farming, up to \$5,000 or 25 percent of the taxable income from farming for the year, whichever is the lesser.
7. LANDS; MINERALS. The Commerce Committee reported with amendments S. 2138, to provide that a greater percentage of the income from lands administered by the Fish and Wildlife Service be returned to the counties in which such lands are situated (S. Rept. 1919). p. 16284
The Subcommittee on Public Lands of the Interior and Insular Affairs Committee approved for full committee consideration with amendments S. 3451, to provide relief for residential occupants of unpatented mining claims upon which valuable improvements have been placed, and S. 3160, to amend the act of March 8, 1922, so as to extend its provisions to the townsite laws applicable to Alaska. p. D761
8. HOLIDAYS. Passed without amendment S. J. Res. 217, to make Sept. 17 each year a legal holiday to be known as Constitution Day. p. 16292
9. DRUGS; MONOPOLIES. By a vote of 78 to 0, passed with amendments S. 1552, to amend and supplement the antitrust laws with respect to the manufacture and distribution of drugs. pp. 16302-30, 16333-60

Digest of CONGRESSIONAL PROCEEDINGS

OF INTEREST TO THE DEPARTMENT OF AGRICULTURE

OFFICE OF
BUDGET AND FINANCE

(For information only;
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Issued Aug. 27, 1962

For actions of Aug. 24 and 25, 1962
87th-2d, Nos. 151 & 152

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HIGHLIGHTS; Sen. Stennis urged additional appropriations for extension work and utilization research. Sen. Proxmire said government should pay cost of protecting milk against fallout. Senate subcommittee voted to report independent offices appropriation bill. Senate passed agricultural appropriation bill. Senate passed bill to authorize joint watershed surveys by USDA and Army. Sen. Proxmire urged caution in use of pesticides.

SENATE - August 24

1. MILK. Sen. Proxmire said the cost of protecting milk against fallout contamination should be born by the Federal Government and inserted an article on the problem. pp. 16466-7
2. APPROPRIATIONS. Sen. Stennis urged increased appropriations for the extension service and utilization research. pp. 16471-2
A subcommittee of the Appropriations Committee voted to report to the full committee H. R. 12711, the independent offices appropriation bill. p. D764
3. RECLAMATION. Concurred in the House amendments to S. 2008, to amend the act of Sept. 16, 1959, authorizing the construction, operation, and maintenance of the Spokane Valley project. This bill will now be sent to the President. p. 16470

4. TAXATION. Sens. Kuchel, Beall, and McCarthy submitted amendments intended to be proposed to H. R. 10650, the proposed Revenue Act of 1962. pp. 16378-9
Sen. Proxmire protested the investment credit provision in the tax bill and inserted an article, "The Investment Credit--The Opening of Another Loophole." pp. 16383-5
H. R. 10650, the proposed Revenue Act of 1962, was made the pending business of the Senate. pp. 16463-4
5. VETERANS. Began debate on S. 349, to provide readjustment assistance to veterans who serve in the Armed Forces between Jan. 31, 1955, and July 1, 1963. pp. 16405-13, 16427-43, 16449-60, 16461-4
6. PERSONNEL. The Commerce Committee reported with amendments S. Con. Res. 53, favoring travel by legislative and Government employees on U. S. air flag carriers (S. Rept. 1922). p. 16378
Passed without amendment S. 3319, to extend to certain employees in the Trust Territory of the Pacific Islands the benefits of the Federal Employees' Compensation Act. p. 16405
Sen. Javits inserted an article, "White House Urged To Use Compulsion in Negro Job Drive." pp. 16398-400
7. HOUSING. Sen. Williams, N. J., inserted a speech by the Assistant Administrator, Housing for Senior Citizens, Housing and Home Finance Agency, "Housing: Shelter Showcase, or Living Environment." pp. 16390-3

SENATE - August 25

8. AGRICULTURAL APPROPRIATION BILL, 1963. Passed with amendments this bill, H. R. 12648 (pp. 16488, 16492-518). Conferees were appointed (p. 16518). Agreed to the committee amendments en bloc (pp. 16492-3). Agreed to an amendment by Sen. Russell to provide that \$30 million may be transferred from CCC funds for administrative expenses for the feed grain and wheat stabilization programs, contingent upon enactment of the farm bill, H. R. 12391 (p. 16493). Agreed to an amendment by Sen. Russell to raise the statutory building limitation from \$15,000 to \$25,000 so as to authorize the construction of one building by the Soil Conservation Service at a cost of not to exceed \$25,000 (p. 16493).
9. WATERSHEDS. Passed without amendment H. R. 3801, to authorize the Secretaries of the Army and Agriculture to make joint surveys and investigations of watershed areas for flood prevention or the conservation, development, utilization, and disposal of water. This bill will now be sent to the President. p. 16488
10. PESTICIDES. Sen. Proxmire discussed the side-effects and problems that have resulted from use of pesticides in California, "urged greater caution in the use of chemical poisons, and commended the "constructive attitude" of the Departments of Agriculture and Interior regarding the use of pesticides. pp. 16578-80
11. TAXATION. Began consideration of H. R. 10650, the proposed Revenue Act of 1962. pp. 16518, 16533-78
12. WATER POLLUTION. Sen. Monroney commended the establishment of a regional laboratory at Ada, Okla., to conduct research on water pollution problems. pp. 16484-7
13. COPYRIGHTS; PUBLICATIONS. Sen. Proxmire expressed his concern over "the increasing scope of copyright protection applied to writing and other material prepared at Government expense, or on the basis of information connected with Government employment." pp. 16580-1
14. ADJOURNED until Mon., Aug. 27. p. 16583

an agreement to suspend nuclear testing.

I realize that such an agreement must be based, without question, on a system of inspection and control that works and gives us assurance, but certainly we should do everything in our power to end atmospheric nuclear tests, which are polluting the atmosphere in Minnesota, Wisconsin, and Iowa. It is going to spread through the country if nuclear tests continue. Of course, we must safeguard our security, but we must do everything within our power consistent with the security of our country to bring about a suspension of atmospheric nuclear testing.

THE NOMINATION OF JUDGE THURGOOD MARSHALL

Mr. JAVITS. Mr. President, I think today should mark the final culmination of the drama which has represented the effort to confirm the nomination of Thurgood Marshall as a judge of the Court of Appeals for the Second Circuit. Another hearing is taking place before the subcommittee. It appears now that the case is clearly made and that the story is now complete. The President has had his say. We have had our say. The subcommittee obviously is in no hurry to deal with this nomination. So it has been made very clear to me that ultimately the Senate, either by direct action or on a motion to discharge the committee, is going to have to deal with this matter.

My colleague [Mr. KEATING], who has fought so magnificently in this struggle, has today released a letter from the American Bar Association showing that all of the questions which are raised against Judge Marshall in the subcommittee hearings have no appeal in the eyes of that association, and the association found every evidence that the nominee has a keen appreciation of the canons of ethics of the American Bar Association and that he has complied with them in every respect and that it received no evidence to the contrary, and unanimously concluded that Thurgood Marshall was well qualified for the Federal judiciary.

Also, I have a telegram from Herbert Brownell, president of the bar of the city of New York, my own hometown, in answer to the argument that Judge Thurgood Marshall is not admitted in New York, and, indeed, a number of States which represent the second circuit. Mr. Brownell, former Attorney General, speaking as the president of the bar of the city of New York, and following the action of the executive committee of the bar association, stated that the executive committee adopted a resolution that the Association of the Bar of the City of New York urge the Committee on the Judiciary of the U.S. Senate to file promptly a report favorable to Judge Thurgood Marshall's confirmation and that the Senate act promptly to confirm Judge Marshall's appointment to the Court of Appeals for the Second Circuit.

The President of the United States remarked that my colleague [Mr. KEATING]

and I might have had Thurgood Marshall appointed a judge sooner.

Let me give an example of the differences in the record. As I said yesterday, I do not have to defend my record on Negroes being appointed to higher office, or on civil rights against the President or anyone else. Nevertheless, let us get the facts. Thurgood Marshall was nominated on September 24, 1961. The nomination has been languishing ever since.

Let us look at the record of the Eisenhower administration. As Al Smith used to say, "Let's look at the record."

The following Negroes were appointed to the bench in the Eisenhower administration:

Scovel Richardson, U.S. Customs Court, nominated March 4, 1957, and confirmed April 4, 1957.

The PRESIDING OFFICER (Mr. Young of Ohio in the chair). The time of the Senator has expired.

Mr. JAVITS. I ask unanimous consent that I may proceed for 2 additional minutes.

The PRESIDING OFFICER. Without objection, it is so ordered.

Mr. JAVITS. Walter A. Gordon, to the U.S. District Court, Virgin Islands, nominated January 17, 1959, and confirmed September 2, 1959.

I do not say President Eisenhower was any more sympathetic to this matter than President Kennedy. I think both men have the same desire and wish, but I only give those facts, first, in answer to the President's feeling about what happened in the previous administration, about which I think he was wrong; and, second, and far more important, to show the comparison with the record on Thurgood Marshall.

I hope the administration and the majority leader in the Senate will not wait until the final days of the session, for that would be unseemly. I think the time for action on the Marshall nomination is no later than the week of Labor Day, which is sufficiently in advance of the time when the Senate apparently will adjourn. I have no doubt that the confirmation will take place, but this has been a hard fight and is a very key question in connection with our national policy. I join with my colleague in the struggle, not only as to Judge Marshall, but to show that we practice what we preach, and that when a man who is a Negro has the eminent and distinguished qualifications to receive this kind of backing from the American Bar Association and the bar of the city of New York, he should get prompt justice at our hands. That is what we have been trying to do.

Mr. President, I have another subject to discuss, but I shall not do so at this time.

INVESTMENT TAX CREDIT INCENTIVE PROVISION PROPOSED IN COMMITTEE

Mr. PROXMIRE. Mr. President, I rise once again to protest the investment credit provision in the pending tax bill. I have already pointed out that this investment credit provision would

result in an extra billion-dollar deficit, in addition to the presently expected deficit.

Second, it is an unwanted subsidy. The great business organizations which testified before the Finance Committee represent to some extent, at least, the thinking of businessmen. The chamber of commerce opposes it. The National Association of Manufacturers opposes it. The McGraw-Hill survey has indicated that business would not use it. The National Industrial Conference Board has indicated the same result. The Wall Street Journal survey also indicates that business would not use it.

It would be a windfall, but it would be a windfall which would have very little results.

There is one other fact I should like to bring to the attention of the Senate. I have overlooked this in my previous statements on the Senate floor, and I think it is most important.

The distinguished Senator from Illinois [Mr. DOUGLAS] and the distinguished Senator from Tennessee [Mr. GORE] have filed very enlightening and informative dissenting views on the tax bill, particularly with regard to the investment credit provision. They point out that the investment credit provision has been sharply changed from the administration's original request. Originally the investment credit provision was designed to provide an incentive for additional investments; that is, if a firm invested \$1 million a year for a 3-year period it was to be entitled to get a credit to the extent it exceeded that \$1 in the fourth year. If in the fourth year the firm invested \$1,100,000, then the credit would be based on the \$100,000 additional investments. In that event it could have been a credit of 20 or 30 percent with a far lesser reduction in Federal revenues.

Mr. President, that provision could have been a substantial incentive. It would have been an incentive for several reasons. First, it would have persuaded firms to increase their investment in plant and equipment. In the second place, it would have provided an opportunity in respect to the greatest handicap toward the growth in our economic system, that if the growth of the small but highly efficient firms.

A competent, scholarly study by Professors Butters and Lintner of Harvard Business School, made several years ago, showed that under the present corporation income tax laws the very efficient and growing firms could not begin to grow as corporations grew in the past because the corporation income tax takes such a huge proportion of their income.

Mr. President, the pending investment credit provision would not provide for that kind of relief. The investment credit provision would provide that all investment—I repeat, all investment, including a reduction in investment—still would receive the investment credit. For example, if a firm invested \$1 million a year for 3 years and then reduced its investment—I repeat, cut back its investment—from \$1 million to \$900,000, the firm still would get the 7-percent

credit, which in that case would be a \$63,000 reduction in the tax liability.

So, as the Senator from Illinois [Mr. DOUGLAS] and the Senator from Tennessee [Mr. GORE] point out so well in their dissent, this provision would work as a very feeble incentive to business to increase its investment. At the same time it would constitute a billion-dollar drain on the Treasury.

I think this particular part of the dissenting views of Senators GORE and DOUGLAS is so persuasive that I ask unanimous consent that pages 396 through 400 of the report of the Committee on Finance, which embraces the dissenting views of the Senator from Illinois [Mr. DOUGLAS] and the Senator from Tennessee [Mr. GORE], be printed in the RECORD at this point.

There being no objection, the excerpt from the report was ordered to be printed in the RECORD, as follows:

THE INVESTMENT CREDIT—THE OPENING OF ANOTHER LOOPHOLE

(Dissent of Senators DOUGLAS and GORE)

WHAT THE INVESTMENT CREDIT IS

1. The bill in its present form provides a tax credit of 7 percent on amounts invested in new tangible depreciable property, other than buildings, which is subject to a depreciation life of more than 8 years. There are certain limitations which can be briefly stated: (a) If the life of the property is less than 4 years, no credit will be granted; (b) if the life is from 4 to 6 years, only one-third of the credit (2 1/3 percent) will be granted; (c) if the life is from 6 to 8 years, then two-thirds of the credit (4 2/3 percent) will be granted. The credit for used property is limited to the first \$50,000 of investment.

2. The bill also provides a 3-percent credit for regulated private utilities such as telephone and domestic telegraph, gas, and electric companies.

3. The investment credit can be offset dollar for dollar against taxes owed up to \$25,000 but above that amount may not reduce tax liability by more than 25 percent.

4. The Long amendment adopted by the Finance Committee slightly reduces the effect of these tax credits in later years by providing that the basis cost of the asset shall not exceed the value of asset minus the investment credit. Thus, depreciation is limited to 93 percent of the original cost of the asset (97 percent for utilities).

The Department of Commerce estimates that the production of durable equipment in 1961 amounted to \$25.5 billion. A 7-percent reduction in this would amount to \$1 3/4 billion annually. This would be reduced in practice by the lower rate for the private utilities, the exceptions listed above, and the Long amendment.

It is probably safe to estimate the initial loss of revenue from this feature of the bill at somewhere between \$1.1 billion to \$1.4 billion. We personally believe it will amount to not far from \$1.3 billion.

This measure is advocated by the majority as a means of stimulating industry to improve its plant and machinery, reduce its costs, and by stimulating investment to expand employment and reduce unemployment.

Here it should be noted that the tax credit originally proposed by the administration was on net additional investment, or the amount invested in industry over and above that allowed for depreciation. There would have been strong grounds for supporting such a proposal or one which would have given the credit to increases in investment over the average for a previous 3- or 5-year period. But during its consideration by the House Ways and Means

Committee, this proposal was vulgarized almost beyond recognition. Instead of being a bonus for net additional investment or for increased investment, it was transformed into a credit for all investment (aside from buildings) or what may be termed gross investment. Thus, if a company invests less than the physical depreciation of its machinery and equipment, it will still get a 7-percent credit, or a 14-percent tax deduction on this gross investment. To repeat, an actual decrease in investment as compared with the years prior to July 1, 1962, will be rewarded.

II. WOULD THE INVESTMENT CREDIT APPRECIABLY STIMULATE INVESTMENT?

In other words, by giving the rewards on average gross investment rather than on marginal net investment any possible stimulus to added investment is greatly reduced and in our judgment is very slight indeed. We are confirmed in this opinion by the results of the McGraw-Hill survey in the spring of 1962. The question asked by McGraw-Hill was as follows:

"If the administration's program of tax incentives for investment were enacted, how much would this increase your capital expenditures in 1962?"

In reply to this, business as a whole indicated that it would raise its 1962 plans by only about 1 percent, or about \$300 million. Nine out of every 10 companies which replied stated that they would not use such a program in 1962.

Since the bonus under the proposed investment credit will amount to about \$1.1 to \$1.4 billion, this would mean that, out of every dollar which the Government will lose in taxes less than 30 cents will find its way into increased investment in American industry. This is a very high price to pay for a little stimulus.

The National Industrial Conference Board made a special survey in late March and early April 1962 of the 1,000 largest manufacturing corporations in the United States to determine what effect the 7-percent investment credit would have upon their capital investment. While the influence of the credit on the plans of the companies varied somewhat from industry to industry, the results were that only 8 percent of those responding said they would revise their capital spending for the balance of 1962 if the credit were enacted by mid-1962. Seventeen percent of the reporting companies said they would increase their investments in 1963 if the credit were enacted by the end of the current session of Congress. But the prospective change in the dollar volume of capital spending in 1963 as a result of the credit would be as small as 1 percent.

As the report of the survey states:

"Overall, the increase in 1963 outlays expected on account of the investment tax credit may be small in relation to its potential. In more than half of the industries covered, moreover, the imputed difference was less than 1 percent."

There are already more than adequate funds available for investment on the part of corporations which they are refusing to use for this purpose. Thus the July 1962 Survey of Current Business, issued by the Department of Commerce (p. 24), shows that in 1961, American corporations had acquired \$43.1 billion of corporate funds¹ but invested only \$31.3 billion in equipment and inventories.² In this 1 year, therefore, they piled up nearly \$12 billion in plant and assets. There were also very large accumula-

tions of liquid assets in preceding years, amounting to about \$5 billion in 1960 and an equal amount in 1959.⁴ If business conditions did not cause American corporations to invest these huge sums in past years, there is little prospect that the extra bonus of \$1.3 billion will be translated into investment. What is more likely to happen is that the overwhelming proportion will also pass into the cash reserves and swell them still further. There would seem to be little prospect that the investment credit will have any real stimulative effect. It will increase the power and wealth of the already powerful and wealthy.

We should also realize that a very large percentage of plant and equipment now lies idle and unutilized primarily because there is not adequate demand for the goods which could be produced at the prices charged.

The McGraw-Hill index of plant utilization is now at approximately 85 percent. Even though the 15 percent which now lies idle is partially composed of a standby reserve or is markedly obsolete, it is still true that the percentage of plant utilized is 5 or 6 percent short of what would be used under full employment. Can it be maintained that, if good machinery and equipment is thus allowed to lie idle because of a shortage in effective demand relative to prices, a bonus on investment would stimulate a still further increase in machinery and equipment? For would not this still further increase the already high percentage of idle equipment?

In addition, it should be realized that, while the purpose of the investment credit is to stimulate economic growth and to help business to compete more effectively in foreign markets, it would in fact be given all the way across the board without regard to the quality or social need for the investment. Thus, the credit would be available for such investments as a new ski lift at Sun Valley or in Vermont, an escalator in a department store, new farm machinery to spread fertilizer on lands which are already overproducing, klieg lights in a burlesque house, and martini-mixing machines in a bar. Other investments of an even more questionable nature would receive the bonus.

It is hard to see how this increases our efficiency as compared with other countries or whether this serves meaningful economic growth.

The 3-percent credit which is to go to utilities would be completely wasted and is wholly unnecessary.

The rate of return of the private utilities is regulated by both State and Federal bodies. If regulation is properly carried out, then any favorable tax consequences of the credit would be offset by reductions in the rates charged to consumers.

If not properly carried out, it would be an outright gift to the private utilities, for it would merely increase their rate of return above that set by the regulatory bodies.

In addition, the 3-percent credit for utilities has nothing to do with other stated purposes of the credit, namely, to help modernize industry or to make it more competitive in world markets.

III. WHO HAS BEEN GETTING THE TAX CUTS?

Let us also note the way in which tax benefits and reductions have been made during these last 8 years. In 1954, accelerated depreciation, with the double declining balance and the sum of the digits methods, was authorized by Congress. This amounted to an initial loss of revenue to the Government of at least \$2 billion a year.

¹ The Business Record, National Industrial Conference Board, August 1962, p. 19.

² Made up as follows (in billions of dollars): Retained profits, \$7.3; depreciation, \$24.8; sale of stocks, \$4.5; sale of bonds, \$5.1.

³ Made up of \$29.6 billion in plant and equipment and \$1.8 billion in inventories.

⁴ John K. Landrum seems to come to the same general conclusion, although with somewhat smaller increases in liquid funds. See his "Corporate Profits and Cash Flow" supplement to testimony before Joint Economic Committee, Aug. 10, 1962, p. 1.

This went to the industrial corporations and to the industrialists. At the same time the \$50 dividend exclusion and the 4-percent credit were passed in 1954, which gave \$400 million a year more to the owners of common stocks. This summer the Treasury has issued a new Bulletin F, permitting machinery and equipment to be depreciated much more rapidly. It is estimated that this will reduce business taxes by approximately \$1.5 billion a year. All of these taken together comes to just short of \$4 billion a year.

Now we have this provision for the investment credit which will give the investors in machinery and equipment at least another \$1.3 billion annually. Thus, in 8 years we have decreased the annual tax burden on industry by over \$5 billion a year. This, of course, goes to the upper income groups in society who own the overwhelming proportion of the stock of American corporations.

During this period the low- and middle-income groups have received virtually nothing in the way of tax cuts. It is about time that the United States was less partial in its distribution of favors. This is true both on economic and ethical grounds.

IV. INVESTMENT CREDIT A FORM OF THE TRICKLE-DOWN THEORY

The basic way in which investment is stimulated and the economy moved forward is not by granting incentives for increased capital expenditures at a time when the existing plant and equipment is not fully used, but by increasing the demand for the products which the existing plant and equipment can produce which, in turn, will stimulate investment. In other words, the investment credit proposed is really a form of the trickle-down theory of economics which has largely been shown to be ineffective in the past. We believe instead in the theory that purchasing power should be built from the bottom up.

V. INVESTMENT CREDIT OPENS UP ANOTHER LOOPHOLE

Finally, the investment credit would open up more tax loopholes and would be quickly extended to other fields.

As nearly as possible a proper tax system should be neutral in the way it treats both income and expenditures. If we could have an absolutely just tax system it would probably make no distinctions as to the amount of tax to be paid on income or deductions from expenditures, no matter where the funds were derived or for what they were spent. It is the failure to carry out this principle which has so eroded our present tax system and which has made it so unjust.

For example, income from a wage or salary, in general, is taxed at the full rate, but income from oil, or from stock options, or from the cutting of timber, or from dividends, or from gains on the stock market, or from the sale of real property, among others, is taxed at lower rates and has special privileges not afforded to income from a wage or salary.

On the expenditure side, money spent for entertainment expenses, for business expense accounts, including yachts, club dues, and so forth, are deductible from taxable income, while the expenses of an ordinary person driving to and from work, or the payment of rent, or expenditures for the recreation or education of one's children are not deductible. These privileges for deductions and allowances go almost entirely to the strong, the powerful, and the well-to-do, and favor high income groups and unearned income as opposed to low income groups and earned income.

The main purpose of tax reform is to try to modify or to do away with some of these inequities and privileges in the tax laws.

What the investment credit does is to say that for social purposes we should give a spe-

cial tax privilege for funds used to buy most kinds of depreciable property. At least as good a case can be made that society would be as wise to allow deductions for money spent for the education of children, for a future pension, or for preventive medicine rather than for capital investment.

Every legislator is pressed almost daily by some constituent or interest group to vote for a tax deduction for their particular interest. Once we start on this road it is almost impossible to stop. For this reason alone it is very unwise to give a special deduction for funds which are spent in this particular way; namely, for capital investment. It would be equally unwise to give deductions for most of these other proposals.

If the 7-percent tax credit is allowed on machinery and equipment, it will be only a short time before it will be granted on plant and buildings, and this will amount to another revenue loss of not far from \$1.5 billion. Indeed, proposals to this effect have already been made. Residential construction would not be left behind for long and this would take another \$1.5 billion away from our revenue. It would also be inevitable that the principle of H.R. 10 would find its way into enactment, and moneys devoted to purchasing voluntary retirement plans would be exempted from taxation. So would expenditures to educate children in college.

The final result would be that only income spent for current consumption would be taxed. This would be a kind of sales tax which would be highly regressive in nature and would weigh proportionately far more heavily upon those with lower or middle incomes than upon those with large resources. State and local taxation is already highly regressive. This is only made bearable by the fact that Federal taxation is progressive and hence introduces a kind of rough proportionality over the range of most incomes. To make Federal taxation also regressive or less progressive would in our opinion be grossly unjust. And yet that is precisely the end result toward which the opening of these loopholes would tend. We cannot acquiesce in these tendencies however well intentioned they may be.

RETIREMENT OF MAJ. GEN. TERENCE P. FINNEGAN, CHIEF OF CHAPLAINS, U.S. AIR FORCE

Mr. DODD. Mr. President, a distinguished citizen of Connecticut and of the United States is about to retire from the Air Force after 25 years of outstanding service to his country.

The Chief of Chaplains of the U.S. Air Force, Maj. Gen. Terence P. Finnegan, will leave the service on August 31. His devotion to God and country is in the great tradition of our Armed Forces, a tradition which goes back to the foundation of the Republic.

Monsignor Finnegan was at Schofield Barracks in Honolulu during the infamous Japanese attack on Pearl Harbor, December 7, 1941. He worked without sleep for the next 3 days, succoring the wounded, comforting the dying, and evacuating civilians out of the danger areas.

Throughout the war, he was in the Pacific theater, almost invariably in the frontlines; he again served in the Far East during the Korean conflict. Since then, he has traveled to almost every Air Force installation, to establish with the officers and men a personal relation-

ship that has done much to make the chaplains service an integral and indispensable part of the education of our young men in the Air Force.

The Air Force moral leadership program initiated by Major General Finnegan has recently been cited by the Senate Subcommittee on Preparedness as being the best conceived, planned, and executed educational program in the armed services to date.

During his tenure of office, the very serious recruitment problems of the chaplain's service were largely overcome. Monsignor Finnegan established minimum educational standards for chaplains, and almost doubled the strength of the corps, so that the serious shortage of priests, ministers, and rabbis in the Air Force was largely alleviated.

He was substantially responsible for the magnificent design of the Air Force Academy chapel, insisting that the three major faiths should worship under one roof.

Even more important than his organizational achievements are the basic tenets which Monsignor Finnegan has impressed upon the men and officers of the U.S. Air Force. To him, the love of country, of liberty, and of justice has always been inseparable from the love of God; indeed, man's devotion to his country and to his fellow man is directly derived from the precepts of religion. To Father Finnegan, there can be no patriotism, no self-sacrifice, no freedom without the conviction that man's liberty is derived from a higher Being to whom he owes allegiance and life itself, and who is the final arbiter of man's actions.

Acutely aware of the danger which Communist atheism presents to the Western World, he told the graduating class of the Air Force Academy, in June 1960:

It shall probably be during your lifetime the coming of a decision whether our Western way of life, as we have known it, shall maintain itself and be passed on to your children's children. The world in its long history has seen great crises. The world has been in none greater than this of our day.

There still stands in the balance, and it remains yet to be decided, whether the world of tomorrow shall be the world of godless atheism or whether it shall be to live under the principles of Christ.

Perhaps Monsignor Finnegan's service to his country is best described by the citation accompanying the Distinguished Service Medal about to be awarded to him:

Chaplain, Maj. Gen. Terence P. Finnegan distinguished himself by exceptionally meritorious service to the United States in a position of great responsibility as chief of Air Force chaplains, U.S. Air Force, from August 15, 1958 to September 1, 1962.

The superb ability, exemplary leadership and selfless dedication displayed by Chaplain Finnegan significantly advanced the moral and religious program of the Air Force.

The singularly distinctive accomplishments of Chaplain Finnegan in this important assignment culminate a distinguished career in the service of his country, and his dedicated contributions reflect the highest credit upon himself and the U.S. Air Force.

THE NEUTRON BOMB

Mr. DODD. Mr. President, there has been a surprising amount of confusion, even in circles that should be informed, on the subject of the neutron bomb. This is unfortunate, because our ability to produce a pure fusion weapon and its practical application to tactical warfare have critical significance for the conduct of the test-ban negotiations in Geneva, for the future of NATO and our relations with our allies, and for our entire national security.

How widespread are the misunderstandings on the question of the neutron bomb and how deep they go was illustrated several months ago in an article written by Mr. William Laurence, Pulitzer Prize winning writer, for the Saturday Evening Post.

I first asked the Saturday Evening Post for permission to reply to Mr. Laurence's article in article form and at the same length. When the editors of the Post replied that this would not be possible, I attempted to deal with the inaccuracies contained in Mr. Laurence's article within the framework of a letter to the editor. This letter, in considerably condensed form, was printed in the Saturday Evening Post's recent issue.

Mr. President, because I consider this question to be of such very great significance, I ask unanimous consent to have printed at this point in the RECORD the uncut version of my letter to the editor of the Saturday Evening Post concerning the feasibility and potential utility of the neutron bomb.

There being no objection, the letter was ordered to be printed in the RECORD, as follows:

JULY 6, 1962.

The EDITOR, THE SATURDAY EVENING POST,
Philadelphia, Pa.

SIR: Mr. William Laurence, in his article in your issue of May 5, questioned the scientific feasibility of the neutron bomb; in effect, he said that it would have no serious military utility if it were developed; and he impugned the judgment of those who have urged a concerted effort to develop the neutron bomb. Among these was the late Thomas E. Murray, one of the most experienced and distinguished members of the Atomic Energy Commission, who, until the day he died, had full access to all material relating to nuclear weapons development.

Mr. Laurence it is clear, does not understand the concept of the neutron bomb. This is revealed by his statement that "it is easier to guard against this thermonuclear weapon, the N-bomb, than against the H- or A-bombs." The comparison is meaningless because the H-bomb and the N-bomb are weapons with totally different applications. The H-bomb is, by its nature, a strategic weapon, a weapon of mass destruction unsuitable for use in the battlefield because it would blot out the very countries we are attempting to defend. The N-bomb, in contradistinction, is conceived not as a mass destruction weapon, but as a tactical weapon which could be used with discrimination in battlefield situations and which, in addition, would provide an effective warhead for the antimissile missile. It would make an ideal defensive weapon (1) because it produces no significant fallout; (2) because it could be tailored for use in a variety of ranges, extending from several hundred yards to more than half a mile; (3) because

there would be no effective defense against it; (4) because it would be comparatively cheap to produce.

Mr. Laurence quoted a number of prominent nuclear scientists as challenging the scientific feasibility of the neutron bomb. But there are nuclear scientists of at least equal distinction who are convinced that the neutron bomb can be made, and that we should proceed with its development as a matter of highest priority. Indeed, those experts who are working on the project are of the opinion that the N-bomb can be perfected in highly sophisticated form within a reasonable short time.

One of the scientific authorities quoted by Mr. Laurence was the eminent theoretical physicist, Dr. Hans Bethe. Dr. Bethe belongs to the group of scientists who, understandably, are horrified over the potentialities of the unceasing race in nuclear technology, and who believe that somehow, this race must be stopped. Because they consider this to be of transcendent importance, these scientists, I believe without exception, all urged that we take the risk implicit in the ill-fated 3-year honor moratorium on nuclear testing. Speaking for this philosophy when the H-bomb was only a concept, Dr. Bethe once said that the H-bomb should not be made. At a later date, he said that, even if the H-bomb was built, it would not be as effective as an improved A-bomb.

There is another group of scientists who are equally horrified over the potentialities of the nuclear weapons race, but who accept the hard political fact that the Kremlin is out to cut our throats and will never tolerate the minimal measure of inspection essential to any agreement on nuclear testing or disarmament. The stand of this group is that we must run as hard and as fast as we can in the nuclear race because the Kremlin's unbroken record of aggression and dishonesty leaves us with no alternative.

It may be hard for the layman to make up his mind when two groups of equally distinguished scientists take diametrically opposed stands on a project like the N bomb. But, in general, history demonstrates that those scientists who have said "we can and we must" have far more frequently been correct than those who have said "we cannot" or "we must not," or who have minimized the importance of further technological progress in the field of nuclear weaponry.

Mr. Laurence pursued his argument against the scientific feasibility of the neutron bomb, by tying it in with Project Sherwood, which is aimed at producing industrial power through a controlled fusion process. He quoted Dr. Edward Teller as telling him that he did not expect this goal to be achieved before the end of the century. "Nor, for that matter," continued Mr. Laurence, "does anyone know whether such fusion without fission ever will be possible."

When I read this passage to Dr. Teller over the telephone, Dr. Teller replied as follows: "Because of the rigid classification imposed on the entire question of the neutron bomb, I have never offered any public opinion, either pro or con, on its feasibility or on the advisability of pursuing the project. * * * The comments I have made at various times on Project Sherwood have absolutely no bearing on the neutron bomb for the simple reason that the two projects are unrelated. As for Mr. Laurence's statement that no one actually knows whether fusion without fission will ever be possible, I would point out that in a paper published in December 1958 the Soviet physicist, L. A. Artsimovich, strongly implied that the Soviets, as early as 1952, had been able to produce a neutron-emitting thermonuclear reaction, using a high-explosive trigger."

In questioning the military utility of the neutron bomb, Mr. Laurence is pitting him-

self against the considered judgment of the Joint Chiefs of Staff, who have carefully weighed the military application of the neutron bomb and are of the opinion that it would be an extremely effective weapon, considerably more effective, in fact, than any tactical weapon developed to date.

As matters now stand, we propose, in any limited warfare situation, to limit ourselves to conventional weapons, at least in the initial stages. But suppose the Kremlin demonstrates its possession of the neutron bomb and employs it for tactical purposes in the first stage of a military encounter at Berlin or some other point. We would then be confronted with the terrible choice between surrender or escalation to the all-out thermonuclear war which we are seeking to avoid.

The development of the neutron bomb would make war less likely by increasing our defensive capabilities. And, if a limited warfare situation should erupt, the possession of this potent but discriminating and credible tactical weapon, would enable the administration to prevent or at least minimize the possibility of escalation into general thermonuclear war.

THOMAS J. DODD,
U.S. Senator.

CHAOS IN THE CONGO

Mr. DODD. Mr. President, as the Senate is aware, I have repeatedly urged that we abandon the futile policy of force in our dealings with Katanga and that we seek, instead, to find a solution for the differences between the Adoula government and the Tshombe government through the traditional devices and processes of conciliation.

There are some who attempt to justify the policy of force which has thus far produced nothing but chaos in the Congo by arguing that Mr. Tshombe cannot be trusted to keep his word, that he has repeatedly violated agreements into which he has entered. This canard has been so assiduously fostered by the United Nations and, I regret to say, by certain members of our Department of State, that it has come to enjoy a measure of acceptance even by responsible and fairminded editors.

In an editorial in the New York Herald Tribune yesterday morning we were again told—for the thousandth time—that, I quote, "the trouble is that Mr. Tshombe always agrees to proposals but that's as far as he ever goes. A few weeks pass and then one sees again that no progress whatever has been made toward a unified Congo."

I think it important to set the record straight, Mr. President, because if conciliation is to work, it is important to know in advance whether or not the parties to be conciliated have records of good faith.

The most effective answer to the Herald Tribune editorial and to the persistent canards concerning Tshombe's bad faith was, in my opinion, given by the distinguished columnist, Arthur Krock, on the editorial page of the New York Times yesterday. I believe that Mr. Krock's column should be read in juxtaposition to the Herald Tribune editorial, because such a reading will make it apparent how much misrepresentation there has been on the question of the Congo.

MONTGOMERY, ALA., August 24, 1962.
Hon. RALPH YARBOROUGH,
New Senate Office Building,
Washington, D.C.:
S. 349 one of the most important efforts
yet for veterans education and training.
Please give it your utmost support.
M. O. HULSEY,
State Supervisor, Trade and Indus-
trial Education.

Mr. President, I believe that the
argument made by the distinguished
Senator from South Carolina is utterly

without logical grounds. This bill would
be a great aid in the fight against com-
munism. These people are not demand-
ing something. The country has de-
manded something of them. It has
reached out and pulled them out of their
normal life, and, so far as most of them
are concerned, has wrecked their eco-
nomic opportunity unless they get this
retraining opportunity. I have not heard
one argument made against the bill that
is logical or sound.

Mr. President, I ask unanimous con-
sent to have printed in the RECORD a
table which appears on pages 28 and 29
of the committee report on S. 349. The
table is entitled "Probable Participation
and Total Amounts of Educational Al-
lowances by State Under Readjustment
Training Program Proposed by the Vet-
erans Readjustment Assistance Act of
1961 (S. 349)."
There being no objection, the table
was ordered to be printed in the RECORD,
as follows:

Probable participation and total amounts of educational allowances by State under readjustment training program proposed by the Veterans' Readjustment Assistance Act of 1961 (S. 349)

State	Veteran population		Experience, World War II and Korean programs		Veteran population, post-Korean induction period ³		Participation and allow- ances for post-Korean veterans (1st 5 years only)	
	World War II ¹	Korean conflict, June 30, 1960 ²	World War II veterans trained (Public Law 346)	Korean veterans trained (Public Law 550) through June 30, 1960	In civil life June 30, 1960 ⁴	Total expected through fiscal year 1973 ⁵	Veterans expected to train ⁶	Amounts of educational allowances ⁷
	(A)	(B)	(C)	(D)	(E)	(F)	(G)	(H)
Total.....	15,432,000	5,482,000	7,800,000	2,334,000	1,380,000	4,440,000	1,413,000	-----
Alabama.....	253,000	113,000	171,000	60,000	22,000	71,000	28,000	49,200,000
Alaska.....	9,000	4,000	6,000	1,500	2,000	5,000	1,500	2,100,000
Arizona.....	74,000	37,000	39,000	15,000	10,000	31,000	10,000	13,900,000
Arkansas.....	156,000	53,000	103,000	23,000	14,000	45,000	15,000	24,600,000
California.....	1,187,000	465,000	581,000	233,000	105,000	338,000	127,000	168,800,000
Colorado.....	147,000	51,000	87,000	28,000	14,000	45,000	18,000	29,200,000
Connecticut.....	224,000	79,000	88,000	29,000	20,000	66,000	18,000	20,900,000
Delaware.....	34,000	12,000	14,000	4,000	3,000	10,000	2,000	1,900,000
District of Columbia.....	107,000	28,000	99,000	31,000	7,000	22,000	18,000	29,100,000
Florida.....	289,000	144,000	171,000	66,000	30,000	98,000	33,000	45,700,000
Georgia.....	290,000	115,000	191,000	64,000	29,000	92,000	38,000	60,400,000
Hawaii.....	39,000	22,000	17,000	7,000	6,000	20,000	5,000	7,100,000
Idaho.....	57,000	21,000	32,000	8,000	6,000	20,000	6,000	9,700,000
Illinois.....	935,000	273,000	443,000	120,000	75,000	241,000	79,000	97,800,000
Indiana.....	400,000	139,000	161,000	48,000	36,000	115,000	30,000	41,500,000
Iowa.....	228,000	89,000	111,000	33,000	23,000	73,000	20,000	36,000,000
Kansas.....	188,000	67,000	88,000	23,000	14,000	47,000	12,000	16,800,000
Kentucky.....	245,000	103,000	114,000	34,000	24,000	78,000	19,000	27,600,000
Louisiana.....	238,000	86,000	155,000	45,000	25,000	79,000	31,000	55,100,000
Maine.....	82,000	36,000	39,000	8,000	11,000	35,000	6,000	8,500,000
Maryland.....	242,000	88,000	122,000	29,000	22,000	70,000	17,000	24,000,000
Massachusetts.....	522,000	168,000	248,000	74,000	39,000	127,000	42,000	50,400,000
Michigan.....	681,000	229,000	275,000	79,000	63,000	204,000	53,000	70,100,000
Minnesota.....	299,000	105,000	143,000	50,000	30,000	95,000	34,000	48,800,000
Mississippi.....	165,000	59,000	119,000	28,000	14,000	45,000	16,000	29,200,000
Missouri.....	387,000	144,000	228,000	62,000	34,000	110,000	35,000	50,700,000
Montana.....	57,000	21,000	29,000	8,000	5,000	15,000	4,000	6,100,000
Nebraska.....	122,000	50,000	60,000	23,000	14,000	44,000	15,000	24,800,000
Nevada.....	17,000	8,000	8,000	2,000	3,000	9,000	1,700	2,000,000
New Hampshire.....	57,000	24,000	23,000	6,000	5,000	15,000	3,000	4,300,000
New Jersey.....	559,000	178,000	210,000	54,000	43,000	138,000	31,000	31,400,000
New Mexico.....	71,000	24,000	37,000	12,000	7,000	22,000	9,000	12,800,000
New York.....	1,608,000	464,000	790,000	202,000	120,000	386,000	126,000	135,600,000
North Carolina.....	344,000	140,000	198,000	61,000	33,000	107,000	35,000	52,100,000
North Dakota.....	46,000	23,000	23,000	13,000	7,000	22,000	9,000	15,400,000
Ohio.....	855,000	271,000	383,000	94,000	70,000	228,000	59,000	66,600,000
Oklahoma.....	221,000	83,000	135,000	40,000	20,000	64,000	24,000	40,100,000
Oregon.....	163,000	54,000	77,000	21,000	16,000	51,000	15,000	19,700,000
Pennsylvania.....	1,179,000	373,000	588,000	142,000	96,000	310,000	88,000	112,600,000
Rhode Island.....	96,000	28,000	33,000	12,000	6,000	20,000	6,000	8,900,000
South Carolina.....	164,000	72,000	102,000	31,000	18,000	58,000	19,000	33,400,000
South Dakota.....	59,000	24,000	26,000	12,000	5,000	16,000	6,000	11,400,000
Tennessee.....	298,000	113,000	203,000	51,000	28,000	91,000	31,000	46,100,000
Texas.....	782,000	271,000	453,000	136,000	69,000	222,000	83,000	124,000,000
Utah.....	74,000	30,000	46,000	21,000	7,000	21,000	11,000	17,900,000
Vermont.....	32,000	15,000	16,000	4,000	3,000	10,000	2,000	2,700,000
Virginia.....	301,000	127,000	116,000	34,000	28,000	90,000	18,000	25,500,000
Washington.....	233,000	86,000	111,000	36,000	24,000	78,000	25,000	36,300,000
West Virginia.....	194,000	79,000	74,000	22,000	22,000	71,000	15,000	20,400,000
Wisconsin.....	313,000	121,000	132,000	42,000	32,000	103,000	27,000	40,600,000
Wyoming.....	28,000	10,000	14,000	3,500	2,000	7,000	1,800	2,800,000
Outside United States, total.....	76,000	63,000	63,000	48,000	19,000	62,000	35,000	79,400,000

¹ As of Dec. 31, 1953, which approximates peak number of World War II veterans in civil life.
² Includes approximately 962,000 veterans who also served during World War II.
³ Veterans of service period Feb. 1, 1955, through June 30, 1963.
⁴ Estimate of post-Korean veterans in civil life on June 30, 1960, based on 1 percent sample of separations from Armed Forces; does not provide for migration subsequent to separation. Data rounded to nearest thousand.
⁵ Excludes several hundred thousand career military personnel who served during the post-Korean induction period and who are expected to remain continuously in military service until after the end of fiscal year 1973.
⁶ State distribution of trainees expected in 1st 5 years is based on State distribution of post-Korean veterans and State participation rates applicable to Korean veterans.
⁷ State distribution of estimated education and training allowance is based on State distribution of trainees expected in 1st 5 years and cost factors applicable to trainees under the Korean readjustment training program.

Mr. YARBOROUGH. Mr. President,
I yield the floor at this time to the dis-
tinguished majority leader.

REVENUE ACT OF 1962
Mr. MANSFIELD. Mr. President, I
wish to compliment and commend the

distinguished Senator from Texas for
the vigorous and courageous leadership
he has shown in behalf of the postwar GI
bill of rights. He has fought hard for
the bill down through the years, and
he was successful in getting it through
the Senate in a previous Congress.
However, in view of the situation

which has developed, I should like at
this time to lay the pending bill aside
so that I may discuss it once again with
the policy committee when it next meets,
and also with the distinguished minority
leader, the Senator from Illinois, to see
if we might possibly arrive at an agree-

ment to limit debate on the bill at a future date.

I therefore move that the Senate proceed to the consideration of Calendar No. 1843, and that it be made the pending business.

Mr. JAVITS and Mr. MILLER addressed the Chair.

Mr. MANSFIELD. I yield to the Senator from New York.

Mr. JAVITS. A parliamentary inquiry.

The PRESIDING OFFICER. The Senator will state it.

Mr. JAVITS. May this be done without a vote?

Mr. MANSFIELD. It can. It can be done by unanimous consent.

The PRESIDING OFFICER. It may be done by unanimous consent.

Mr. MANSFIELD. I ask unanimous consent that the pending bill be laid aside and that the Senate proceed to the consideration of Calendar No. 1843.

The PRESIDING OFFICER. The clerk will state the bill by title for the information of the Senate.

The CHIEF CLERK. A bill (H.R. 10650) to amend the Internal Revenue Code of 1954 to provide a credit for investment in certain depreciable property, to eliminate certain defects and inequities, and for other purposes.

The PRESIDING OFFICER. Is there objection to the present consideration of the bill?

Mr. JAVITS. Has the pending bill been laid aside?

The PRESIDING OFFICER. A unanimous-consent request is pending that the Senate proceed to the consideration of the tax bill.

Mr. COOPER. Reserving the right to object, may I ask the distinguished majority leader whether he intends to bring up the veterans bill again this afternoon?

Mr. MANSFIELD. Not this afternoon. I intend to discuss it further with the policy committee and also wish to confer with the minority leader to see if it is possible to reach an arrangement under which the bill could be brought up later, under a limitation of debate.

Mr. COOPER. Not this week?

Mr. MANSFIELD. Not this week. There is nothing tricky about the request to lay the bill aside.

Mr. JAVITS. We do not mean to imply that there ever is anything tricky on the part of the majority leader. Does that include Monday as well?

Mr. MANSFIELD. It includes all of next week, as well.

Mr. COOPER. I am sure the majority leader knows that we do not mean to imply that there is anything tricky.

Mr. MANSFIELD. I am certain about that. I thought there might be a question about the request on that point. "Tricky" was the wrong word. No subterfuge is involved.

Mr. JAVITS. I voted for the bill when it was before the Senate previously. It was unfortunate that it was brought up quite suddenly, without an opportunity for study or preparation. I say that even though I was one of those who was in favor of the bill.

Mr. MANSFIELD. I have been waiting for that allegation or charge to be made.

Mr. JAVITS. I make no charge.

Mr. MANSFIELD. The fact that it came on so suddenly—and it did come on suddenly—is due to the fact that when bills are reported out of committees, they are taken up by the Policy Committee. The Policy Committee then gives the leader authority at his "discretion" to bring up a bill. What is done in effect, is that the question of scheduling is passed from the appropriate committee to the policy committee to a single individual. He looks at the calendar and wonders what he can bring up. He finds that half the bills are being objected to by Democrats and the other half by Republicans, and sometimes by both.

So he searches for something that he can bring up, first determining whether there is a Senator in the city who is either for or against it. Then the bill is called up. He is then told that the bill has been called up suddenly. Of course it has. However, what can he do under these circumstances?

There was more difficulty attached to this bill than I thought there would be when I called it up. I am glad the Senator from Texas has had an opportunity once again to show his deep interest and initiative in connection with this bill.

Mr. JAVITS. Mr. President, will the Senator yield?

Mr. MANSFIELD. I yield.

Mr. JAVITS. I wish to compliment the Senator from Montana.

Mr. MANSFIELD. The Senator always does that. I appreciate it.

Mr. JAVITS. I commend him and compliment him for his traditional fairness. The Senator has displayed again what is in his character, and I thank him for it.

Mr. PROUTY. Mr. President, I should like to point out that the substitute I intend to offer for the Cooper amendment is not ready. I am deeply concerned about the lack of progress which has been made with the higher education bill. It was my purpose to incorporate my substitute for peacetime veterans' benefits in the general higher education bill, which we all know is at present stymied in conference. I am very much in favor of this legislation and I hope it will be enacted. I believe also that the peacetime veterans should be given a preference over nonveterans where student assistance is concerned. I regret that I did not have an opportunity to offer my amendment today but I understand the circumstances, and I applaud the majority leader for deferring action in view of those circumstances.

Mr. MANSFIELD. This is one of the consequences of taking bills up suddenly. I am sure the Senator understand my problem, just as I am sure I understand why he has not had an opportunity to propose his amendment.

Mr. YARBOROUGH. Mr. President, will the distinguished majority leader yield?

Mr. MANSFIELD. I yield.

Mr. YARBOROUGH. First, I thank the majority leader for the privilege of

having made a start on the consideration of the bill. The majority leader told me he was hopeful that amendments could be disposed of rapidly and that there would be an opportunity to finish the consideration of the bill today, before other pressing measures got in the way.

I ask the majority leader if it is not probable that the Senate will return to the consideration of the bill at this session. I understand that a Senator on our side of the aisle has an amendment, in addition to the one which the distinguished Senator from Vermont [Mr. PROUTY] says he intends to offer. Will it be possible for the Senate to return to the consideration of the bill later, in the hope that there will be time in a busy schedule to complete action on the bill?

Mr. MANSFIELD. That is my hope. Mr. President has my request been agreed to?

The PRESIDING OFFICER. Is there objection to the request of the Senator from Montana that the Senate proceed to the consideration of House bill 10650?

There being no objection, the Senate proceeded to consider the bill, which had been reported from the Committee on Finance with amendments.

Mr. MANSFIELD. Mr. President, what is the pending business?

The PRESIDING OFFICER. Calendar No. 1843, H.R. 10650.

WHY PICK ON KATANGA—EDITORIAL IN THE DALLAS MORNING NEWS

MR. THURMOND. Mr. President, the Dallas Morning News of Dallas, Tex., has published in its editorial columns of August 22, 1962, some eloquent editorial comments which present a brief but powerful defense of Katanga against United Nations and United States determination to force Katanga into a coalition government with the Central Congolese Government. The arguments in this editorial are so persuasive, Mr. President and make so much practical commonsense that I fail to understand how anyone in our Government can support a policy against self determination for the people of Katanga.

The editorial is entitled "Why Pick On Katanga?" I feel that it is important enough to be read at this time to the membership of the Senate. I also respectfully remind Senators of the able and well documented address presented on the Senate floor on August 3, 1962 by the distinguished Senator from Connecticut [Mr. Dodd]. I commend to the Senate, to the House, and to every American, Senator Dodd's lengthy and scholarly address on August 3, and also the impressive editorial published in the Dallas Morning News.

The editorial reads as follows:

WHY PICK ON KATANGA?

Acting U.N. Secretary General U Thant's latest demand for a unified Congo is nothing short of an ultimatum which gives Katanga President Moïse Tshombe the alternative of accepting the United Nations terms or facing extinction. U Thant in effect has threatened

Mr. TALMADGE. Mr. President, will the Senator from Virginia yield?

The PRESIDING OFFICER (Mr. METCALF in the chair). Does the Senator from Virginia yield to the Senator from Georgia?

Mr. ROBERTSON. I yield.

Mr. TALMADGE. The distinguished Senator from Virginia has had an illustrious and honorable career in many fields of endeavor. He has served his country in uniform, in time of war. He has served his great State of Virginia, the mother State of our country, in the legislative branch, in the judicial branch, and also in the executive branch of the Government. He has served honorably and long in the Congress of the United States, both in the House of Representatives and in the Senate. But I do not believe the distinguished Senator from Virginia has ever rendered during his long career, a more outstanding service than the one has rendered today on the floor of the Senate. I have never heard a more scholarly, logical, irrefutable, eloquent legal argument in all my life. He has gone into the history and the origin of the first amendment to the Constitution of the United States. He has quoted from those who framed that amendment. He has quoted from the debates in the House of Representatives and in the Senate of the United States as to its meaning. He has traced the decisions of the U.S. Supreme Court in construing that document. He has quoted from Mr. Justice Story and from Judge Cooley, the writers of the greatest commentaries, in all the history of our country, on the meaning and the significance of that document.

He has laid threadbare the argument that government cannot participate in religion. He has clearly demonstrated that government cannot exist without religion.

Mr. President, I compliment the distinguished Senator from Virginia on the outstanding and eloquent job he has done today.

Mr. ROBERTSON. I thank the Senator. During my 30 years of service in the Congress I have discussed many issues, but none of such transcendent importance to the future of our Nation as the one I have attempted to discuss today. I only wish that, like Isaiah of old, my lips, in presenting this speech, could have been touched by a burning coal from the altar.

REVENUE ACT OF 1962

Mr. CURTIS. Mr. President, whatever feeling I may have about the provisions of H.R. 10650, I believe that section 12 of the bill, relating to controlled foreign corporations, creates a dangerous precedent and upsets many constitutional safeguards. For the first time, this bill taxes an American corporate shareholder on his share of the undistributed profits of a foreign subsidiary even though such shareholder has not received such profits and may never receive them because of the vicissitudes of business risks. If such a provision is enacted, it will upset the constitutional rule which has been in effect at least ever since the first income tax

was enacted following the adoption of the 16th amendment in 1913. This attempt to disregard the corporate entity and tax the income to the shareholder of a corporation before such income is distributed to the shareholder in the form of dividends strikes a dangerous blow at every domestic corporation doing business in the United States. The Secretary of the Treasury stated on page 322 of Vol. 1 of the House Hearings:

As far as tax law is concerned, I do not think there is anything in this proposal that we cannot do equally with domestic corporations.

In his appearance before the Senate Finance Committee the Secretary said: "We apply the same procedures as have been applied for many years to foreign personal holding companies." The Secretary is apparently confusing the situation which prevails in the case of foreign personal holding companies with the situation which exists in the case of an ordinary business corporation. When the foreign personal holding company provision was adopted pursuant to a report by the Joint Committee on Tax Evasion and Avoidance in 1937, the Committee made the following statement:

The proposal recommends a method of taxation which is a departure from any previously used with respect to corporate income. The committee feels, however, that this innovation is necessary to protect the revenue and prevent further use of one of the most glaring loopholes now existing. The proposal would affect only foreign corporations which are owned 50 percent or more by five American citizens or residents, including members of their families, and which have the same type of investment income which make a domestic corporation subject to tax as a personal holding company. Real foreign operating companies or widely held holding companies are not included.

The report continues:

There appears to be no justification for the continued existence of foreign personal holding companies * * *. It is believed as a matter of fiscal policy that the dissolution of such companies should be effected as promptly as possible * * *. (H. Doc. No. 337, p. 21).

In short, the purpose of this 1937 legislation was to impose such an onerous and punitive regime on the prescribed U.S. individual shareholders in foreign personal holding companies that they would forthwith liquidate such existing companies and would be discouraged from creating any such companies in the future.

The fact that the Treasury describes the new proposal as being similar to the 1937 measure raises the question whether it now seeks to force the liquidation of all of the foreign subsidiaries including real foreign operating companies that might fall under the proposed enactment, and prevent future recourse to foreign corporations to conduct business abroad.

In other words, by imputing tax avoidance to a foreign subsidiary's transactions in a third country although they are perfectly normal and satisfactory to the tax authorities of the countries involved, the Treasury would ask Congress to require a punishment that is modeled

on legislation intended to liquidate foreign personal holding companies. In other words, the Congress was attempting by the foreign personal holding company legislation to reach the shareholder of a foreign personal holding company only where such corporation was being utilized to avoid payment of U.S. income taxes. It was never intended to apply such a provision to operating companies that actually engage in manufacturing, processing and selling goods outside of the United States.

The Secretary's theory overlooks the elementary and fundamental principles asserted repeatedly by the Supreme Court of the United States that in the absence of fraud or evasion a corporation is an entity separate and distinct from its stockholders and that the earnings of the corporation cannot be imputed to the shareholder until distributed in the form of dividends. The courts have not disregarded the corporate entity, except to prevent fraud or evasion. Neither fraud or evasion is involved in a corporation manufacturing, processing, and selling goods abroad. The income from such activities is attributable to a foreign subsidiary operating outside of the United States and cannot be attributed to its parent corporation organized in the United States prior to distribution to its corporate shareholders.

I know there are many who do not like the corporation system under which we have been operating for many years and would like to disregard the corporate entity and tax all income to the shareholders of a corporation whether domestic or foreign. That this is a decided change in the tax policy of the country was admitted by the Secretary of the Treasury in his appearance before the Finance Committee. Perhaps the philosophy of this proposal is to remove the constitutional obstacle which prevents the taxation of income earned by a corporation directly to the shareholder before it is distributed. But we cannot overcome a constitutional prohibition by legislation. The Court will have to review this question anew. The people who advocate such a theory are in the same group as those who desire the Federal Government to remove the constitutional prohibition in the case of income from State and local obligations. If we remove these constitutional safeguards, there will be no anchors for us to cling to.

Do we want to permit these constitutional questions which have already been decided by the Supreme Court to be reviewed and reconsidered because of this bill? This is exactly what will happen if we adopt the rule of this bill in section 12. The question will involve long and costly litigation. It will take years before this question is decided by the courts. I shudder to think of the affect of such a reversal on an Oklahoma corporation, a Delaware corporation, a Nebraska corporation, or any corporation located in any State of the Union if the Federal Government should impose upon the shareholder of such a corporation a tax on the earnings of such a corporation before such earnings are distributed to its shareholders. As

well stated by the Supreme Court in *Eisner versus Macomber*, 252 U.S. 189-1920:

Certainly the interest of the stockholder is a capital interest, and his certificates of stock are but the evidence of it. They state the number of shares to which he is entitled and indicate their par value and how the stock may be transferred. They show that he or his assignors, immediate or remote, have contributed capital to the enterprise, that he is entitled to a corresponding interest proportionate to the whole, entitled to have the property and business of the company devoted during the corporate existence to attainment of the common objects, entitled to vote at stockholders' meetings, to receive dividends out of the corporation's profits if and when declared, and, in the event of liquidation, to receive a proportionate share of the net assets, if any, remaining after paying creditors. Short of liquidation, or until dividend declared, he has no right to withdraw any part of either capital or profits from the common enterprise; on the contrary, his interest pertains not to any part, divisible or indivisible, but, to the entire assets, business, and affairs of the company. Nor is it the interest of an owner in the assets themselves, since the corporation has full title, legal and equitable, to the whole. The stockholder has the right to have the assets employed in the enterprise, with the incidental rights mentioned; but, as stockholder, he has no right to withdraw, only the right to persist, subject to the risks of the enterprise, and looking only to dividends for his return.

If he desires to dissociate himself from the company he can do so only by disposing of his stock.

When we attempt to tax the stockholder on the undistributed profits of the corporation, we are not levying an income tax on the shareholder because he has received no income. We are levying a tax on him merely because of his ownership of stock. It is not an income tax, but a direct tax on the shareholder and subject to the rule of apportionment. It is in violation of the fifth amendment of the Constitution because it is attempting to collect from the shareholder a tax on income which belongs to the corporation. Such a tax bill will place an American corporation in an unfair, competitive position with its foreign competitors. The tax laws of Australia, Belgium, Canada, France, Germany, Italy, Japan, Netherlands, Norway, Sweden, and the United Kingdom do not tax the undistributed earnings of foreign subsidiaries to the parent company under any circumstances. Tough European competitors like the idea of imposing additional handicaps on American business. While these European competitors heartily approve steps to decrease the effectiveness of American business, it is notable that no single measures have been proposed by their governments with respect to their own industries. In fact, their tax policies have been in the opposite direction—to encourage expansion of their business abroad. It would appear that the Treasury is more concerned with the vigor of foreign businesses than of American businesses. It is also obvious that heavy tax burdens on American's overseas business would greatly abet the increasing economic competition of the Communists. In this bill we are asked to approve a policy which is, first, detrimental to American business; second,

beneficial to foreign business in competition with American business; and third, greatly beneficial to state-owned Communist industries which seek to bury us.

I am familiar with the escape valve prepared in the Treasury and adopted by the Finance Committee as a result of an amendment offered by the Senator from Oklahoma [Mr. KERR]. The effect of this amendment is not to apply the punitive provisions of section 12 if the combined foreign tax and the U.S. tax—to the extent the latter is paid on the distributive income—is not substantially below the U.S. corporate rate. The lower the foreign tax rate is, the greater the distribution to the shareholders must be and the greater the proportion of the total must be subject to the U.S. tax of 52 percent. Thus, whether the provisions of section 12 will apply will depend upon the effective rate of foreign tax. For example, if the effective rate of foreign tax is under 10 percent, the company will be required to distribute 90 percent of the earnings and profits to avoid the punitive provisions of section 12, and if the effective foreign rate is over 47 percent, the punitive provisions compelling distributions of earnings and profits will be dispensed with. In this connection, I would like to insert in the RECORD a table showing how the minimum distribution required varies with the effective foreign tax rates.

There being no objection, the table was ordered to be printed in the RECORD, as follows:

Required minimum distribution of earnings and profits after foreign taxes

If the effective foreign tax rate is (percentage):	Percent
Under 10.....	90
10 or over but less than 20.....	80
20 or over but less than 30.....	70
30 or over but less than 40.....	60
40 or over but less than 42.....	50
42 or over but less than 44.....	38
44 or over but less than 46.....	26
46 or over but not more than 47.....	14
Over 47.....	0

Mr. CURTIS. Mr. President, the purpose of this table is to help large companies doing business throughout the world. Despite the fact that a number of large corporations were called into the Treasury to consider this formula and although some stated that it would shield them against the punitive provisions of section 12, nevertheless they recommended strongly against the enactment of that section. Some of them pointed out that this minimum formula would provide a very strong incentive for foreign governments to raise their own tax rates on the earnings of American-controlled companies and/or on distributions to American shareholders. This would provide additional revenue to the foreign countries and protect their balance-of-payment position, both by decreasing the surplus available for dividends and by eliminating the incentive to pay dividends. The adverse effect on the United States would be obvious if the foreign effective rate was uniformly increased to 47 percent; the advantage to the United States would be eliminated. Moreover, those companies which did business in a country with a high rate of tax and also in a country with a low

rate of tax would not be benefited by the minimum distribution table if the average foreign tax rate is substantially below the U.S. rate, but would be subject to all the hardships of section 12. This section will discourage any incentive to minimize foreign taxes and because of the existence of foreign tax credit will result in less tax being paid to this country. I cannot understand why we are so anxious to increase the foreign taxes on American business operating abroad when the effect will be to reduce our taxes in this country. If a foreign country does not desire to increase its taxes, why should we try to induce it to do so?

The escape valve from section 12 still contains the fundamental error of taxing the shareholder on the corporate earnings before distribution. Furthermore, it will not apply uniformly to all foreign corporations operating abroad, but only those long-established corporations with foreign operations throughout the world. It will drastically hurt the new and developing businesses that desire to reinvest earnings overseas. In effect, it is a tax on undistributed earnings, but is collected not from the foreign corporation but from the American corporate shareholders of such corporation, although such shareholders have no right to such earnings before distribution. Our experience with undistributed tax on domestic corporations in 1936 was unfortunate and it had to be repealed in 1938. This undistributed profits tax is on the shareholder before the earnings are distributed to him. Therefore, it is even a worse approach than the 1936 provision.

If the administration had definitely set out to design a piece of legislation to discourage Americans engaging in business abroad, it could hardly find anything better than section 12.

There is another point which I wish to emphasize in the escape valve provision. Those corporations which elect to secure the benefit of the escape valve are apt to have the amount of their foreign tax credit reduced by administrative fiat instead of by act of Congress. Under the provisions of section 936(f), the Secretary is authorized to make regulations, including regulations for the determination of the amount of the foreign tax credit in the case of distributions with respect to the earnings or profits of two or more foreign corporations. The report indicates that the Treasury intends to construe the grant of authority to make regulations as authority for the right to reduce the foreign tax credit of those who elect to take advantage of the escape valve. This is not legislation by the Congress but a change in the law by administrative action. It is an assumption of legislative power by the administration, which I deplore.

One of the most vital objections to section 12 is the tremendous burden of accounting and recordkeeping it would impose on controlled foreign subsidiaries of American companies. Since the section applies to tax haven transactions, it follows that accounting and recording systems will have to be installed in every foreign-controlled corporation so that every transaction carried out by the com-

pany can be classified and recorded as being within or without the scope of section 12. When I asked Secretary Dillon in the hearings before the Senate Finance Committee to define a tax haven company, he stated:

What we have done is not to define a tax haven company specifically, but to define in effect a tax haven transaction. For example, a tax haven transaction is one where a company incorporated in country A purchases from country B and resells in country C.

So in this situation there have to be three countries involved and the use of the words "tax haven company" is just a short description of companies which operate in this way. We do not have a definition of a company as a tax haven company.

This means that in determining whether or not a transaction is a tax haven transaction, not only transaction accounting must be applied but also geographical accounting not normally followed must be applied because of the new concept as to out-of-country subsidiaries and branches. These complex and new accounting methods will apply not only to sales and service subsidiaries and branches but also to manufacturing companies involved in the chain. Failure to meet the formula by a few dollars may well mean the loss of the exemption. The determination of earnings or profits in connection with the formula will create a tremendous problem. These earnings and profits may not be determined until final settlement of the company's U.S. income tax return for which an 8- to 10-year lapse of time would not be unusual. Because the figures to be used in the computation would not be available, the financial officers of the U.S. shareholder company or companies could not determine the percentage effective rate of foreign income taxes in the year in which the dividend distribution was to be made nor indeed for a considerable number of years thereafter. The U.S. investor, therefore, would have no choice but to compel every controlled foreign subsidiary to classify and record every business transaction as within or without the scope of section 12 and to maintain these records and supporting geographical locations of income and expenses until all tax determinations have become final.

There is another point which I would like to bring up. Secretary Dillon appeared before the Senate Foreign Relations Committee in June of this year and recommended that the United States become a member of the Organization of Economic Cooperation and Development. The United States was made a member of this organization under a treaty ratified by the Senate on March 16, 1961, which was put in effect on September 30, 1961. Secretary Dillon appeared before the Senate Foreign Relations Committee and urged that the United States become a member of this organization. Both the United States and Canada are now members of the organization. A fiscal committee composed of representatives of 18 member states, including representatives of the U.S. Treasury, prepared articles to be included in a Draft Convention for the avoidance of double

taxation with respect to tax on income and capital. The Council of the OECD recommended that the member states adopt these articles in existing conventions and in negotiating future conventions. One of the basic rules laid down by the council to be adopted was in regard to the interpretation of article XX. The commentary on article XX stresses the point that the corporation is a legal entity with a separate juridical personality distinct from its shareholders and then goes on to state in regard to a shareholder:

He is not a trader and the company's profits are not his so they cannot be attributed to him. He is personally taxable only on those profits which are distributed by the company.

This is the same rule which has been applied in the United States in respect of the legal existence of bona fide corporations that have a business purpose and are not a sham; yet Mr. Dillon, after he recommended that the United States become a member of this organization which adheres to this principle, has been trying to get the Congress to abandon such a principle and tax the shareholder of a bona fide business corporation on earnings of the corporation which have not been distributed and may never be distributed because they are subject to the risk of the business. I am at a loss to understand why Mr. Dillon should come before the Congress and plead for admission of the United States to become a member of this organization and then later attempt to repudiate one of the organization's basic rules.

In closing, I wish to comment briefly on the balance-of-payment question. Testimony before our committee was unanimously of the opinion that the proposals recommended by the Treasury for taxing the undistributed earnings of foreign corporations to the American shareholder would actually adversely effect the balance-of-payment situation. At the request of the President of the United States, a committee of businessmen was appointed by the head of the Chamber of Commerce of the United States to analyze the U.S. balance-of-payments problem and offer suggestions and recommendations for dealing with it. This committee was appointed in May of this year and released its report on July 13, 1962. It is interesting to note that one of the recommendations of the report is to the effect that:

Tax proposals, such as certain of those now under consideration in H.R. 10650, which would reduce U.S. competitive capabilities in foreign markets, should not be adopted.

I ask unanimous consent to have that report printed in the RECORD at this point.

There being no objection, the report was ordered to be printed in the RECORD, as follows:

TECHNICAL MEMORANDUM ON SECTION 12

Section 12 of this bill is a very complicated provision. I do not pretend to understand all of the intricacies of this provision, nor, for that matter, do I believe that anyone else fully understands them either. I believe that a provision this complicated and difficult to understand, if enacted, will result

in confusion, uncertainty, and numerous court suits for many, many years to come.

The complexity of this provision arises from the fact that highly selective types of income are chosen for taxation and then a series of escape valves is superimposed upon this structure. The result is an exceedingly complicated statute. The result is also a statute which is highly discriminatory between different types of businesses, depending in part upon the nature of the business and in part upon its size.

Many companies, as a result of the escape valves or because their income does not come within the specified definition, will find that this provision has no effect on them. This is especially likely to be true in the case of the larger well-established businesses, whose investments have stabilized and who, therefore, can meet the conditions of the escape valve which provides for certain specified percentage distributions. On the other hand, many of our smaller enterprises with investments abroad, if this provision is enacted, will be hit with its full force, with the domestic shareholders being taxed in full on the foreign earnings.

The bill selects five different specific categories of income which, under certain conditions, are to be taxed to the U.S. shareholders, even though not distributed to them. The first of these is income derived from insurance or reinsurance of U.S. risks. This probably can be more readily justified as the type of income properly taxable to U.S. shareholders than is true of many of the other categories. However, here too, problems arise since it is necessary to break down the insurance income between that originating from U.S. risks and otherwise. Then in effect it is necessary to determine taxable income arising from this insurance business in the manner provided by our special tax statutes dealing with life insurance and casualty insurance companies.

Second, what is called foreign personal holding company income is selected for taxation to the shareholders. This is to be true, however, only if over 30 percent of the company's income arises from this and certain other sources specified in the bill. Moreover, if more than 70 percent of the income arises from these sources, then all of the income is to be taxed to the shareholders even though the remaining income may arise from manufacturing operations.

However, this foreign personal holding company income does not include dividend and interest income derived from related parties—a term which must be defined—if the corporation in which the income arises is a less developed country corporation—another term which it takes several pages to define—but only if the income is reinvested in one of these less developed country corporations. However, an intricate provision is designed to deny the exclusion of this income from that taxed to the shareholders, if in a subsequent year there is a decrease in investments in a less developed country corporation.

The third type of income selected for special taxation is "foreign base company sales income." This is a truly complicated provision. The definition of the foreign base company sales income provides that this provision is to apply only where the property involved is either purchased from a related person or sold to a related person and only if the property purchased is manufactured, produced, grown, or extracted outside of the country where the controlled foreign corporation is organized and is sold for use, consumption, or disposition outside of that country. Here problems arise not only in applying the related party concept but also in determining the ultimate destination of the goods involved. Actually if the statutory provision were to be literally applied, it would itself seem almost im-

possible to administer and also almost impossible for the taxpayer to comply with.

After all, who can fully determine the ultimate disposition of goods? Here, too, there are difficult problems in determining when the income is attributable to the sale of purchased property or when it is attributable to manufacturing or processing, since the latter is not included under this provision. To complicate the provision still further, branch operations under some conditions are to be brought under this provision and treated as if they were something they are not; namely, a separate subsidiary corporation. This will apply when the Secretary determines the branch is treated for tax purposes by the country of incorporation, or the country where it is doing business, as if it were a separate corporation.

The fourth category of income selected for special taxation to the shareholders is foreign base company services income. This is income from the performance of technical, managerial, engineering, architectural, scientific, skilled, industrial, commercial or similar services, again where they are performed for a related party and outside of the country in which the controlled foreign corporation is organized. This presents many of the same types of problems that will arise in connection with the determination of foreign base company sales income. In addition, there is the problem of determining when the income arises from the specified types of services and when it is attributable to other sources which are not selected out for this discriminatory treatment.

A fifth type of earnings which are to be taxed to the shareholders, even though not distributed, are earnings from any source which are reinvested back here in the United States. This, of course, is most peculiar, since if one were to look for investments which helped our balance-of-payments problem most it would seem as if this type of investment—which the bill selects out for punitive taxation—actually was the most beneficial in this respect. The bill first of all specifies a series of sweeping categories of reinvestments back here in the United States which will give rise to taxation to the shareholders and then as is frequently the case in these foreign income provisions, provides a series of exceptions to these rules. Thus, no tax will be imposed, for example, if the investment is in Government bonds or in a bank account but tax will be imposed if the investment is in corporate bonds or securities. Special, intricate provisions are necessary to keep the income from being taxed to the U.S. shareholder more than once; first as foreign base company sales or service income and then again as income from investments in the United States.

Superimposed on this structure are a series of relief provisions which, of course, may or may not help any given company, depending upon a variety of circumstances unique in each case. One of these I have already referred to; namely, the provision which makes section 12 generally inapplicable if a certain proportion of the income is distributed, a percentage which varies with the effective foreign tax rate. This distribution schedule appears on page 225 of your bill.

I pause here to call attention only to the fact that the so-called effective tax rate will not be easy to compute since this does not mean merely the tax rate of the foreign country but is the actual tax paid to the foreign country divided by the foreign income determined in general on the basis of the U.S. rules for taxation—modified to whatever extent the Treasury deems appropriate. In addition, this rule may be applied to each controlled foreign corporation separately, or to all of them in combination, or to each group of corporations in an ownership chain, or to the combination of those in

developed countries. Just computing the distribution percentages under all of the different combinations will be no small task.

Another major relief provision which will help some companies, but not others, is the so-called export trade corporation provision. Under this provision if you are dealing in goods produced or manufactured in this country and exported, the income derived from this under certain conditions will not be subjected to section 12. The conditions, however, in practice will be quite limiting in their application. For example, the relief under this provision is available only to the extent that the income involved does not exceed $1\frac{1}{2}$ times export promotion expenses or 10 percent of gross receipts, whichever gives the taxpayer the less liberal treatment. Also, this provision only aids those who are able to reinvest their export trade income abroad in the export trade business. Investments cannot be made, for example, in manufacturing operations even though generally under this provision manufacturing profits are not though to be bad and are not generally denied tax deferral under section 12.

My discussion of the complexities of section 12 constitutes merely the broadest sketch of this intricate provision. The tax lawyers and cost accountants will have a field day as the problems in this provision gradually unfold over the next 2 or 3 years if this provision is enacted. I suppose if this provision does nothing else, it will assure full employment for these professions for years to come. Unfortunately, however, it will also ham-string our American operations abroad and in the long run seriously damage our balance-of-payments since it is the return from these investments, and from American exports abroad, which must offset the imbalance brought about primarily by our foreign aid and foreign military expenditures.

Mr. CURTIS. Mr. President, I also ask to have printed at this point in the RECORD a brief by Adrian A. Kragen, professor of law, Berkeley, Calif., on the constitutionality of taxing the undistributed profits of a corporation to its American shareholders.

There being no objection, the brief was ordered to be printed in the RECORD, as follows:

STATEMENT OF ADRIAN A. KRAGEN

The President's tax program relative to the income of foreign corporations which originally was directed at the twofold purpose of strengthening the balance of payments position of the United States and eliminating the use of tax havens (hearings before the Committee on Ways and Means, House of Representatives, 87th Congress, 1st sess., p. 34)¹ has in the Revenue Act of 1962 been narrowed in H.R. 10650 to what purports to be an elimination of the use of tax havens (CCH staff explanation, p. 58). I therefore consider it unnecessary to comment in this discussion on the validity of the arguments in the Treasury memorandum of June 19, 1961 (hearings, p. 313, commencing at page 318) that the proposed legislation is constitutionally defensible under article I, section 8, clause 3, of the Constitution on the ground that a major purpose of the legislation is to adjust the balance of international payments.

The proposals relative to the foreign corporation which are now before this committee raise certain basic but individually independent questions which I would like to comment on in this opinion. These questions are:

A. Can undistributed corporate profits which are not actually received by a taxpayer-shareholder be considered as income to such taxpayer for U.S. income tax purposes on:

(1) The theory that accretion without more is income?

(2) The theory of constructive receipt?

B. Is ownership by U.S. shareholders of more than 50 percent of the shares of a foreign corporation legal justification for the treatment of the prorata share of undistributed corporate income as constructively received by each of the U.S. shareholders holding 10 percent or more of the shares?

A(1). Accretion: The answer to the question A(1) is fundamental to the entire consideration of the validity of the legislation. In the event that an accretion to wealth in and of itself can be considered as income for U.S. income tax purposes, we would only need to consider whether the proposal to measure an income tax by such accretion accorded the taxpayer due process of law. In essence this is the much considered and discussed question of whether "realization" is necessary in order to have "income" within the meaning of that word in the 16th amendment of the U.S. Constitution. The Treasury memorandum discusses this matter at some length and comes to the conclusion that there is a strong possibility that the Supreme Court would, if faced with the direct issue, override the "realization doctrine" as expressed in *Eisner v. Macomber* (1920) 252 U.S. 189. My examination of the decisions has led me to doubt the validity of this conclusion.

The focal point for any discussion of the doctrine of realization is the classic *Eisner v. Macomber* case. In that case, the court defined income as (p. 207):

"The gain derived from capital, from labor, or from both combined," provided it be understood to include profit gained through a sale or conversion of capital assets.

"Here we have the essential matter: not a gain accruing to capital, not a growth or increment of value in the investment; but a gain, a profit, something of exchangeable value proceeding from the property, severed from the capital however invested or employed, and coming in, being 'derived,' that is, received or drawn by the recipient (the taxpayer) for his separate use, benefit and disposal;—that is income derived from property. Nothing else answers the description."

In *Eisner v. Macomber* there was, in my opinion, a clear and unequivocal statement that income of a corporation could not be taxed to the shareholder without a receipt of that income by the shareholder, i.e., that realization in some measure is essential to the definition of income for Federal income tax purposes.

The Treasury over a long period has attacked that concept and has consistently urged the overruling of *Eisner v. Macomber*. Despite such urging the Supreme Court of the United States has never seen fit to overrule the fundamental doctrine enunciated in the case. In fact, even where the Court has distinguished *Eisner v. Macomber*, it has actually impliedly recognized the continuing validity of the definition insofar as realization is concerned. Thus, in *Commissioner v. Glenshaw Glass Co.* (1955) 384 U.S. 426, the Court in distinguishing *Eisner v. Macomber* stated (pp. 430-431):

"The Court was there endeavoring to determine whether the distribution of a corporate stock dividend constituted a realized gain to the shareholder, or changed 'only the form, not the essence,' of his capital investment. Id., at 210. It was held that the taxpayer had 'received nothing out of the company's assets for his separate use and benefit.'"

"Here we have instances of undeniable accretions to wealth, clearly realized, and over

¹ Hereinafter referred to as "hearings."

which the taxpayers have complete dominion."

In *Helvering v. Griffiths* (1943) 318 U.S. 371, the Court specifically declined to rule on the question and the Treasury Department finds comfort in this negative determination. However, the pronouncement quoted above from *Glenshaw Glass* appears to me clearly to set forth the present vitality of the realization rule of *Eisner v. Macomber*.

Helvering v. Bruun (1940), 309 U.S. 461, is used by the Treasury Department and some legal scholars as a harbinger of the demise of the realization requirement for income inclusion. It is my opinion that the Bruun case does not derogate from the basic doctrine enunciated in *Eisner v. Macomber*. In Bruun there was an actual realization in the receipt by the taxpayer of something of actual value. Prior to the cancellation of the lease, all that the lessor had was a fee in land. The building on that land, having a useful life less than the life of the lease, was for the purposes of the lessor nonexistent.

When the lease was canceled, it resulted in the receipt by the lessor of a building with a then value in excess of \$50,000. This was a clear realization of something new which constituted income under the *Eisner v. Macomber* definition. It was property separate and apart from the land itself whether or not it was practical at the moment to sever it physically. Nowhere in the Bruun opinion is there any indication that the realization test is abandoned or even weakened (see Roehner & Roehner, "Realization: Administrative Convenience or Constitutional Requirement?" 8 Tax L. Rev. (1953) 173).

The Treasury in its memorandum while conceding that the "question of the need for the realization of the income has not yet been squarely met by the Court" (p. 315, House hearings) relies on *Helvering v. Horst* (1940) 311 U.S. 112 as another indicia of the loss of vitality of *Eisner v. Macomber*. In my opinion the Horst case strengthens rather than weakens the requirement of realization. The Court throughout its opinion emphasizes the necessity for realization and for something more than mere enhancement in value of a capital asset held by the taxpayer. It simply recognizes that the actual exercise of the power to dispose of a right to income is in itself a realization even though the tangible receipt of the income is by another. It nowhere indicates that mere accretion in value is realization or that the power to dispose of a right to income is the equivalent of the exercise of that power.

My examination of the decisions of the Supreme Court of the United States has resulted in my opinion that *Eisner v. Macomber* is still the controlling authority on the issue of the necessity for realization for the purpose of the determination of income under our income tax laws. Therefore, I must conclude that an attempt to tax a shareholder in general on the undistributed profits of the corporation on the theory of accretion is of very dubious constitutionality under article 1, section 2, clause 3, and article 1, section 9, clause 4.²

A(2) Constructive receipt: The Treasury Department attempts to support the proposed legislation upon the ground that it will tax income which can be considered as constructively received by the shareholder.

Since 1871³ Congress with certain excep-

tions⁴ has levied a tax upon the income of corporations at the corporate level and has treated the shareholders as separate and distinct from the corporate entity. Since 1921, the only legislation imposing a compulsory tax on the shareholders of a corporation based on a pro rata share of corporate income, whether distributed or not, is the Foreign Personal Holding Company Act.

The Treasury Department relies on these provisions as a precedent for the present proposal. In my opinion there is no authority specifically supporting the constitutionality of the foreign personal holding company provisions. Even if there were such authority, I do not believe it could be considered as controlling in regard to the present statutory proposal.

I have found four cases which consider the foreign personal holding company provisions. In two of these, *Alvord v. C.I.R.* (4 Cir. 1960) 277 F. 2d 713 and *Marsman v. C.I.R.* (4 Cir. 1953) 205 F. 2d 335, no constitutional issue appears to have been raised or discussed. In one, *Rodney v. Hoey* (S.D.N.Y. 1944) 53 F. Supp. 604, the plaintiff apparently argued that it was unconstitutional to tax constructive receipt of income without discussing the question of realization and the court rejected the contention merely by citing *Eder v. Commissioner of Internal Revenue* (2 Cir. 1943) 138 F. 2d 27. The *Eder* case discusses the constitutionality in a single sentence. Actually the only allegation of unconstitutionality raised by the plaintiff was on the ground that the inability to distribute in dollars due to blockage rules precluded taxability. The constitutionality of the foreign personal holding company provisions was not presented to the court. This decision cannot be considered to be a definitive upholding of the statute even by the circuit court. The *Eder* case was not taken to the Supreme Court probably because on remand the Tax Court valued the blocked pesos at about one-half of the amount determined by the Commissioner.

All of the cases involving the foreign personal holding company sections discuss the purpose of the legislation, that is, the closing of a loophole that allowed the widespread evasion of income taxes by the device of the "incorporated pocketbook." The section did not purport to and was not intended to cover bona fide operating companies engaged in the sale of goods.

The presence of the tax evasion factor in the enactment of the foreign personal holding company provisions is clear from the legislative history. It is also clear that this tax evasion factor was the major argument of the Treasury Department against the contention of constitutional invalidity: For example, Arthur H. Kent, then General Counsel of the Treasury, testified before the Joint Committee on Tax Evasion and Avoidance as follows:

(1870), 79 U.S. 1, sustained this legislation without passing upon its constitutionality. In *Eisner v. Macomber*, supra, the Supreme Court stated (pp. 218-219) that the Hubbard case had been quereuled.

⁴ The Revenue Acts of 1913, 1916, 1917, and 1918, levied a tax on shareholders measured by their pro rata share of undistributed corporate profits in the case of "personal service corporations" and when corporate income had been accumulated in order to avoid taxes.

In 1921, Congress, doubting the constitutionality of this procedure, levied the tax on the corporation (see Ways and Means Committee Rept. No. 350, 67th Cong., 1st sess., p. 13; Senate Finance Rept. No. 275, 67th Cong., 1st sess., pp. 16-17).

"Mr. REED. Have you considered the constitutional question involved?"

"Mr. KENT. We have given a good deal of thought to that, Mr. Reed, and we believe that if the courts appreciate, as they well do if the facts are properly presented to them, that this does not represent any attempt to avoid in any general way the principles laid down in past decisions, but is simply a bona fide effort by the Congress of the United States to prevent its citizens, residents of this country, from resorting to foreign laws to beat our taxes, that it will be sustained.

"Mr. REED. In view of previous decisions of the courts in relation to the tax on incomes and the tax on capital?"

"Mr. KENT. If those decisions were applied according to their letter, the plan might fail. But the courts have always shown a quite different attitude where you are dealing with a tax evasion situation and this situation can hardly be described in any other way." (Testimony of Arthur H. Kent, General Counsel of the Treasury before Joint Committee on Tax Evasion and Avoidance, 75th Cong., hearings Aug. 9 and 10, 1937, p. 76.)

Although the protection of the revenues against tax evasion has not been determined by the Supreme Court to be an adequate justification for the taxing of corporate income to the shareholders, the present proposal does not purport to rely for important provisions on the presence of widespread or flagrant tax evasion. The committee report on H.R. 10650 states that certain types of income, namely, foreign corporate income from the insurance of American risks and income from patents, copyrights, etc., developed in the United States have tax avoidance aspects but the committee report equally indicates that income of foreign corporations from other sources does not fall within that category. However, it determines that such income should be taxed to American shareholders unless used in certain ways, one of which is "in accord with the policy enunciated by the President," i.e., invested in business in less developed countries. Even if we assume that widespread tax evasion would justify the action proposed, this premise is not available in relation to shareholders of bona fide operating corporations whose income is from activities falling outside those classified in the tax evasion category by the Ways and Means Committee.

The doctrine that the corporate entity is an entity distinct and apart from that of its shareholders is one of long standing in Anglo-American law and in our revenue system.⁵ The Supreme Court in *Eisner v. Macomber* placed this doctrine on a constitutional footing when it stated that the income of a corporation was not income to a shareholder within the meaning of that term in the 16th amendment. The Court stated (p. 219):

"The amendment (16th amendment) applies to income only, and what is called the stockholder's share in the accumulated profits of the company is capital, not income. As we have pointed out, a stockholder has no individual share in accumulated profits, nor in any particular part of the assets of the corporation, prior to dividend declared."

The Supreme Court has indicated that this constitutional prohibition does not exist when the corporate entity is not a real entity, when the corporate entity is in effect a

⁵ See, e.g., *Klein v. Board of Supervisors* (1930) 282 U.S. 19, 24; *Burnet v. Commonwealth Imp. Co.* (1932) 287 U.S. 415; *New Colonial Ice Co. v. Helvering* (1934) 292 U.S. 435, 442; *Nat'l Carbide Corp. v. Comm'r*, (1949) 336 U.S. 422.

⁶ See also, e.g., *Lynch v. Hornby* (1918) 247 U.S. 339, 344.

² *Pollock v. Farmer's Loan & Trust Co.* (1895) 158 U.S. 601.

³ The Civil War Revenue Acts taxed the shareholder on corporate profits whether distributed or not. *Collector v. Hubbard*

mere form without substance. Thus, in *Moline Properties v. Comm'r.* (1943) 319 U.S. 436, the Supreme Court stated (pp. 438-439):

"The doctrine of corporate entity fills a useful purpose in business life. Whether the purpose be to gain an advantage under the law of the State of incorporation or to avoid or to comply with the demands of creditors or to serve the creator's personal or undisclosed convenience, so long as that purpose is the equivalent of business activity or is followed by the carrying on of business by the corporation, the corporation remains a separate taxable entity.

"In general, in matters relating to the revenue, the corporate form may be disregarded where it is a sham or unreal. In such situations the form is a bald and mischievous fiction."

In 1939, a distinguished committee established by the National Tax Association to study the taxation of domestic corporations concluded that application of the partnership method of taxation to a corporation whereby the shareholders would be required to include in their income the undistributed corporate profits would probably require an amendment to the Constitution (1939 proceedings of the National Tax Association, pp. 534, 548).⁸

The Treasury memorandum takes the position that when the U.S. shareholders of a foreign corporation have such power over the corporate income that they can either distribute it to themselves in the form of dividends or use it for their benefit, the corporate entity may be disregarded for tax purposes without regard to whether that entity is bona fide or is "sham and unreal." The Treasury believes that this is a theory of constructive receipt and that *Eisner v. Macomber* would be no bar to its utilization.

I would submit that this position is by no means clearly correct and that there is a serious constitutional question under the 16th amendment in a situation where the shareholders in a bona fide operating corporation have the actual power over the income unless and until the Supreme Court overturns *Eisner v. Macomber*.

If, however, we assume that in such a situation *Eisner v. Macomber* does not constitute a bar, we still must find, as the Treasury memorandum recognizes, an actual command of income in order to avoid the constitutional doctrine of due process of law to the effect that A cannot be taxed on the income of B.⁹

B. Ten-percent shareholder; 51-percent majority:

The Treasury relied in its presentation on the proposition that the income of a "controlled corporation" could be considered for Federal income tax purposes as constructively received by its shareholders. The provisions of section 13 of H.R. 10650 implement this contention. It proposes to tax any United States shareholder who holds 10 percent or more of the voting stock or of the total value of the shares of a foreign corporation over 50 percent of whose voting stock is owned by United States persons. (In regard to "foreign base company income" as defined in section 952(d), the requirement is that five

or fewer U.S. persons own more than 50 percent of the voting power.)¹⁰

The Treasury memorandum, written in support of the original proposal that a 10 percent share interest would be sufficient "control" to support a legislative determination that income was constructively received by the shareholder, relied on a group of cases under the Securities and Exchange Act and the Public Utility Holding Company Act. These authorities are not pertinent to the present situation. We are dealing in the area of taxation with a constitutional definition of income enunciated by the Supreme Court and with the apparently established right of the taxpayer under the due process clause of the Constitution to be free from compulsory taxation on that which is not and cannot be obtained or enjoyed by him. Whether the shareholder has sufficient "control" to be an "insider" for the purposes of the Securities and Exchange Act or has sufficient "control" to be considered as falling within the reach of the Public Utility Holding Company Act¹¹ is not relevant in the instant situation where established specific constitutional questions must be resolved.

In the cases decided since *Collector v. Hubbard*, *supra*, which have determined that the corporate entity should be disregarded and corporate income attributed for tax purposes to the shareholders, there was no doubt that actual command of the corporate income existed in the shareholders.¹²

¹⁰ The original Treasury proposal attributed the income of foreign corporations to American shareholders with respect to corporations in existence prior to the passage of the bill only if there were 10 or fewer shareholders who owned more than 50 percent of the corporate shares. With respect to corporations established after the bill, any American shareholder who owned 10 percent of the shares, whether or not the majority of the shares were held by American shareholders, was taxable on his pro rata share of the undistributed profits. The second Treasury draft eliminated the distinction between corporations in existence on the date of the bill's enactment and those to be set up thereafter and attributed the income of foreign corporations to American shareholders only when five or fewer American shareholders owned 50 percent or more of the total corporate shares.

¹¹ The presumption in that act is prima facie only. See *Electric Bond & Share Co. v. S.E.C.* (2 Cir. 1937) 92 F. 2d 580, 590, affirmed (1938) 303 U.S. 419.

¹² See e.g., *Hay v. Commissioner of Internal Revenue* (4 Cir. 1944) 145 F. 2d 1001, certiorari denied (1945) 324 U.S. 863 (sole stockholder); *Commissioner of Internal Revenue v. Smith* (2 Cir. 1943) 136 F. 2d 556 (sole stockholder); *Paul Plunkett & Co.* (1940) 42 B.T.A. 464 (sole stockholder); *G. M. Jackson* (1939) 39 B.T.A. 937; *Kaspars Cohn Co. Ltd.* (1937) 35 B.T.A. 646 (sole stockholder); cf. *Advance Machinery Exch. v. Commissioner of Int. Rev.* (2 Cir. 1952) 196 F. 2d 1006 (corporation had actual control over the income of two other corporations and a partnership); *Shaw Construction Company* (1961) 35 T.C. 1102 (corporation had actual control over the income of other multiple corporate entities); *Munson S.S. Line v. Commissioner of Int. Rev.* (2 Cir. 1935) 77 F. 2d 849 (sole stockholder); *Southern Pacific Co. v. Lowe* (1918) 247 U.S. 330 (sole stockholder); *Gulf Oil Corp. v. Lewellyn* (1918) 248 U.S. 71 (sole stockholder except for qualifying shares); *Asiatic Petroleum Co. v. Commissioner of Int. Rev.* (2 Cir. 1935) 79 F. 2d 234, certiorari denied (1935) 296 U.S. 645 (corporation had actual control over income realized by sister subsidiary); Rev. Rule 54-596, C.B. 1954-2, 51.

This actual command of the income is the essence of the Treasury's own regulation on constructive receipt of income (Reg. 1-452.2(a)). However, the provisions of section 13 of H.R. 10650 would allow the taxation of income to shareholders who had no command of the income and no possibility of acquiring actual control of it. Under the provisions of section 13, a shareholder who owned 10 percent of the voting power¹³ of a foreign corporation and who had no relationship with the other shareholders, no representation on its board of directors and no actual power to determine its policies would be considered to have constructively received income of the corporation which as a matter of actual fact he might never receive or have command over. Further, this attribution might occur even though the corporation could not have distributed the income to its shareholders by reason of the law of the country of its organization. The fact that the shareholder happened to be an American and that 51 percent of the total corporate shares were held by Americans is hardly a sufficient basis upon which to conclude that he had actual control over the corporate income. It cannot be logically reasoned that the remaining American shareholders were subject to his domination and control as if they were members of his family for it is manifest that shareholders who possess only a common nationality do not have the same common economic interests as do members of a natural family group.

With respect to the 10-percent American shareholder, there is in my view no difference between a situation where 41 percent of a 51-percent American majority is in the hands of unrelated Americans and one where all the shares other than his 10 percent are in the hands of foreign shareholders. The requirement of a 51-percent majority by American shareholders appears to have been inserted in the bill in order to arrive at a more satisfactory definition of an actual control situation. Upon close analysis it will be seen that this provision adds nothing.

The attribution of the income of a bona fide operating corporation as provided in section 13 of H.R. 10650 would appear to attribute the income of A to B in violation of constitutional principles discussed hereinabove.

Should the present bill be changed and limited to foreign corporations with a small group of American shareholders, there is further question in my opinion as to the constitutionality under the fifth amendment to the U.S. Constitution of the application of this special treatment to the shareholders of one class of bona fide corporations. Congress admittedly has a broad discretion when it engages in classification under the taxation power. We are dealing here, however, in the main with bona fide foreign corporations that are being singled out for special treatment solely because they cannot be jurisdictionally taxed by the United States. These words of the Supreme Court with reference to the power of classification are appropriate:

"There are, however, limits to the power of Congress to create a fictitious status under the guise of a supposed necessity." (*Helvering v. City Bank Co.* (1935), 296 U.S. 85, 92.)

This memorandum indicates at least in my opinion that there are serious doubts as to the validity under the Constitution of the basic provisions of section 13 of H.R. 10650. The testimony before the House Ways and Means Committee and, I assume, before this committee indicates considerable

¹³ A shareholder who had no voting power but owned shares valued at 10 percent of the total share value would have income attributed to him under sec. 13.

⁷ See generally, Cleary, "The Corporate Entity in Tax Cases," 1 Tax L. Rev. (1945) 3; Case, "Disregard of the Corporate Entity and Federal Taxation, The Modern Approach," 30 Va. L. Rev. (1944) 398.

⁸ See also, Ballantine, "Corporate Personality in Income Taxation," 34 Harv. L. Rev. (1920) 573, 586; cf., *Long Poultry Farms v. Commissioner of Internal Rev.* (4 Cir. 1957) 249 F. 2d 726, 731.

⁹ See *Hooper v. Tax Commission* (1931) 284 U.S. 206; *Heiner v. Donnan* (1932) 285 U.S. 312, 326-327.

difference of opinion as to the efficacy of this legislation to meet the problem, if one exists. In other sections of the bill, H.R. 10650 has taken steps to tighten up the tax treatment given to income from foreign sources and to preclude the use of devices to attribute improperly income to foreign sources. The bill also provides for the Treasury request for more extensive reporting requirements with respect to certain foreign corporations. These new weapons in the hands of the Treasury may enable it to meet adequately the problem to which its request is directed without plunging into the doubtful and exceedingly controversial area of the attribution to shareholders of the income of bona fide operating corporations organized under the laws of foreign countries.

Mr. CURTIS. Mr. President, I also wish to have printed at this point in the RECORD a memorandum on the complications which would develop if section 12 is enacted.

There being no objection, the memorandum was ordered to be printed in the RECORD, as follows:

JULY 13, 1962.

THE PRESIDENT,
The White House,
Washington, D.C.

DEAR MR. PRESIDENT: In our conversation of May 17, I promised to appoint a committee that would analyze the U.S. balance-of-payments problem and offer suggestions and recommendations on behalf of the Chamber of Commerce of the United States for dealing with it. The committee that I appointed was, as you will see from the attached roster of its members, drawn from the business community and is composed of men who by reason of their training and responsibilities inherent in their individual positions may, I think, be regarded as having special competence in this field. The committee's report, which I attach hereto, is submitted with the concurrence of all its members and with the unanimous approval of the board of directors of the national chamber.

I think it fair to observe that this report, while in no sense neglectful of specifics, addresses itself more fully than do most such reports to what may perhaps be described as the larger economics of the situation in which we find ourselves. It is concerned with the implications of the reemergence, after many years, of an international competitive order, and with the necessity of fitting our economy to the requirements of that order. It is especially concerned that this be done without sacrifice of any of the commercial principles for which we have stood as sponsor for a generation. I may add that while the report in no way minimizes the gravity of the situation, it is a hopeful and even confident report.

I am authorized by the committee to offer you its further services if, in your judgment, those services can in any way be useful to you.

Sincerely,

H. LADD PLUMLEY.

THE U.S. BALANCE-OF-PAYMENTS SITUATION

We can and we must meet the problem posed by the deficit in our international balance of payments. The problem is a serious one for two reasons:

First, there is in the current balance of payments situation a threat to existing monetary arrangements, here and in the world generally. Gold losses of the magnitude experienced in recent years cannot long be sustained even though the reserves of our monetary system are large. Persistence of such losses and any prolonged accumulation at recent rates of foreign short-term claims against the dollar pose a threat to continued

acceptance of the dollar as a reserve currency and thus endanger the entire free world structure of international liquidity, payments and trade. A crisis of confidence in the dollar would deal a serious blow to the position of the United States as leader of the free world and would dangerously restrict its flexibility of movement.

There is a second aspect of the problem which is of equal concern. This is a danger that, in concern over its gravity, steps may be taken and measures adopted the abiding effect of which will be to compromise or abridge the essential principles of the kind of international economic community we have sought to foster and have invested billions of dollars to achieve.

The balance of payments situation in which we find ourselves is thus serious, and urgently so, but it does not follow that it is immediately critical or that it is unmanageable.

That the situation is not immediately critical is chiefly due to two circumstances. The first is that this country's international liquidity position—defined as its gold stock and holdings of convertible currencies plus the world's willingness to accept and hold dollar assets—is not critically impaired. The second is that a number of steps have been taken, typically in concert with other nations, to supplement the resources and facilities that would, in the event of emerging crisis, be available to this country's monetary authorities.

We here refer to the operations of the Treasury and the Federal Reserve in the international money market, and to increased multilateral cooperation through the Basle Group, the gold pool, and IMF. These measures are to be commended. They add to our strength and assurance as we deal with the fundamental problem of improving the long-range competitive position of the United States in the world economy, and they have in them a basis for strengthening the international financial structure.

We have said further that the balance-of-payments situation is not unmanageable.

That situation is not the result of a sudden reversal in the balance of our international accounts; it comes instead from a substantial increase of an imbalance that had prevailed for the greater part of a decade. This substantial increase of imbalance was, furthermore, contemporaneous with the reemergence after a long lapse of years of something approximating an international competitive system. Productive capacities, particularly those of Europe, had been restored and had become competitive with our own. No longer were we in the position of being the world's one certain source of supply for most manufactured goods. Equally important was the reconstruction of the world's monetary system on a basis of external convertibility, which had the effect of exposing the dollar to international pressures not experienced for over a generation.

In short, the problem that confronts us is not that of repairing a disrupted American economy but of adjusting it to a world competitive order—the kind of order that we have worked ever since World War II to achieve.

There appear to the committee to be reasons for believing that the required process of adjustment can be realized and that, in particular, it can and must be realized without resort to unwise expedients, such as, for example, control of capital movement or foreign exchange.

The process of international adjustment to an emergent world competitive system will in some part take place in other countries, as indeed it is already beginning to do. The rapid rate of growth in Western Europe and Japan is leading to relatively rapid increases in wages and, to a measurable extent, in prices as well. These changes will undoubtedly have the effect of helping in

some measure to restore equilibrium to the international payments situation.

It appears reasonable to expect countries experiencing sustained surpluses on balance of payments to embrace policies appropriate to their creditor position. Nevertheless, the task of the United States is inescapable, and can neither be avoided nor deferred. It is mandatory that the U.S. economy maintain and improve its competitive position, and that we comply fully with our responsibilities as the world's banker and custodian of the key international currency.

The Nation's task, as it is defined by these observations, appears to require two directions for action. The first is to settle upon what is to be the U.S. economy's role, within the world economy and the second is to insure that the U.S. economy is adequately competitive to fulfill that role.

THE ROLE OF THE UNITED STATES IN THE WORLD ECONOMY

A primary consideration here is the magnitude of outlay for military expenditures abroad and economic aid to developing countries for which our economy must make provision in the form of an excess of exports over imports of goods and services. These items are sometimes said to be the seat of our present serious problem, and it is inescapable that the greater their amount the more rigorously competitive must our economy become.

Military expenditures and economic aid are here considered apart from private capital flows for two reasons. In the first place, their size, and indeed the fact that they exist at all, is not primarily determined by economic forces, as are international capital movements. In the second place, these are outlays that, bearing as they do on the general interests of an Atlantic community now substantially restored to economic health, can be more equitably shared than would have been possible 10 or even 5 years ago. It is the view of the committee that the encouragingly productive efforts of recent years to secure the sharing of these outlays must be pursued with unremitting vigor.

The role of the U.S. economy within the world economy so far as private capital is concerned is a different matter.

It is the conviction of this committee that the United States must be preserved as a free and unrestricted market for capital funds, whichever may be the direction—in or out—of the flow of such funds. For one thing, it is seriously to be doubted that the integrity of the dollar as a reserve currency can be maintained unless the market for capital be free. But beyond this is the evident fact that private investments abroad are today a substantial source of international income to an economy seriously in need of it. The unimpeded flow of such productive investment funds is thus essential to the United States if we are to take advantage of the opportunities which will prevail in an expanding international economy. If foreign investment is discouraged, an important and rising long-term source of revenue from abroad will be seriously impaired to the detriment of the country's future balance-of-payments position.

If freedom of capital movement is thus to be preserved, as we believe is required, then it follows that we must, as the occasion demands, adopt and adhere to monetary and fiscal policies consistent with our role in the world economy. If interest rates in the United States are too low in relation to the rates at which funds can be effectively placed or borrowed abroad, either our rates must rise or foreign rates must decline. At this time, it seems obvious that interest rates in the United States must be allowed to rise. Flexible interest rates are an essential part of the balance-of-payments adjustment mechanism. While it is of utmost impor-

tance that interest rate flexibility be accepted in the other major countries also, the United States cannot avoid this same discipline if we are to retain the dollar as a key unit of international exchange.

Finally, this committee believes that there is no justification for a change in the dollar price of gold, and that such a change, if effected, would make no useful contribution to the solution of our balance-of-payments problem.

MAINTAINING THE COMPETITIVENESS OF THE U.S. ECONOMY

It is imperative that every present action be shaped to the pattern of the kind of economy that can be a continuing viable part of the competitive world economy that is now emergent. Restriction, for example, of investment abroad for the sake of relief from today's pressures would be as short-sighted as restriction of commodity imports. The sustained strength of the U.S. payments position on commercial account provides substantial basis for faith that our economy has the resourcefulness to maintain its place in a competitive world order, provided only that we are prepared to abide by the rules of such an order.

The first requisite of such an order is that the private sector of the American economy be made able to produce a current balance of goods and services that, after provisions for its investment abroad, is adequate to cover our outlays for military expenditure and foreign aid. The second requisite is that this end be realized within the context of a commercial policy exemplified so far as commodity trade is concerned by the tariff proposals in title II of the Trade Expansion Act of 1962 (H.R. 11970).

To be made competitive in the degree required by the obligations of military assistance and foreign aid, two types of action are required.

The first is that we must hold the line so far as costs are concerned. This is a minimum requirement, because, while we are presently competitive in the sense that our economy continues to provide an export balance on current account, we are not competitive enough to provide the balance required of us. Holding the line on costs requires forthright rejection of inflationary monetary and fiscal policies.

This is not only a minimum requirement, it is imperative. The situation in which, as far as the balance of payments is concerned, we find ourselves is so serious that we cannot afford to lose ground. Indeed, it is the conviction of this Committee that, with due allowance for essential defense requirements, the balance-of-payments situation is so pressing that until the required improvement has been registered in the U.S. position within the world competitive order, any other objectives of national fiscal and credit policy must be subordinated to this one. The Committee does not believe that this objective is inconsistent with, but rather that it is prerequisite to, sustained full employment and economic growth. In fact, a U.S. economy that is a continuing viable part of the competitive world economy has its own contribution to make to the attainment of these domestic objectives as well.

The second requirement is that policy must be directed to increasing the effectiveness of the American economy both in supplying commodities in the world market and in the provision of income from services, including tourist expenditures in the United States and, conspicuously, the growth of earnings from investments abroad.

Taxation of foreign source income should be compatible with the vital objective of obtaining a maximum penetration of the world market. It should preserve flexibility for American business, operations overseas in covering multiple markets, and should permit reinvestment of earnings and expan-

sion of effort in all free world markets. Tax proposals, such as certain of those now under consideration in H.R. 10650, which would reduce U.S. competitive capabilities in foreign markets should not be adopted.

Other policies affecting our competitive ability to supply goods in the world market include tax revisions appropriate to the stimulation of investment both at home and abroad. It is the opinion of the committee that each such revision should be made the occasion for careful and discriminating review of Government expenditure, in order to minimize the net impact on the Government's budgetary position. Continued deficit financing can produce neither confidence nor sound progress. It is essential, too, to encourage U.S. firms to compete more actively abroad. In this latter respect, we particularly endorse the trade promotion program of the Department of Commerce, the export credit insurance program of the Export-Import Bank, and the continuing efforts of the responsible agencies to abate and remove all remaining restraints upon the movement of U.S. products into foreign markets.

Our future balance-of-payments position will be determined primarily by just one thing: the ability of American business to compete successfully and adequately in all markets of the free world.

In summary, this committee recommends the following policy guidelines for dealing with the balance-of-payments situation:

1. Continued efforts to develop multilateral cooperation for strengthening the international financial structure.
2. Reassessment of U.S. unilateral governmental transfers and military expenditures abroad, to eliminate unnecessary drains wherever possible.
3. Increased efforts to persuade our major allies to shoulder a greater share of the common burden of free world defense and aid to the developing areas.
4. Rejection of any move in the direction of limitation of the United States as a capital market.
5. Adoption of an interest rate policy sufficiently flexible to bring U.S. rates into line with those of our major trading partners whenever necessary.
6. Maintenance of the present dollar price of gold.
7. Forthright rejection of inflationary monetary and fiscal policies.
8. Increasing efforts along the lines set forth in title II of the Trade Expansion Act to reduce tariffs and other barriers to world trade.
9. Reduction and revision of U.S. tax schedules appropriate to the stimulation of investment both at home and abroad.
10. Continued encouragement of U.S. firms to compete more actively abroad.

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Mr. CURTIS. Mr. President, I am not in favor of permitting foreign corporations being organized to avoid the Federal tax on income attributable to activities in this country. If they are sham corporations or corporations organized to avoid the American tax, this can be prevented without violating the Constitution. Section 482 of the existing law gives the Treasury authority to allocate income and deductions among related taxpayers where he determines that such allocation is necessary in order to prevent evasion of taxes. The Internal Revenue Service today is checking very carefully on the transfer pricing of exports, particularly where foreign subsidiaries are involved. In addition, if we should find that a corporation is being organized abroad for the purpose of unreasonably accumulating its income to avoid the Federal income tax, we can apply the same rule that we now apply in the case of a domestic corporation which is unreasonably accumulating its surplus to avoid the payment of its income tax. This can adequately be done under the bill and I hope an amendment will be offered to accomplish that purpose.

TIGHT-MONEY POLICY PREVENTED FED HELP THIS YEAR

Mr. PROXMIRE. Mr. President, this morning's New York Times reports the statement of a Director of the Federal Reserve Board, George W. Mitchell. Mr. Mitchell, who, incidentally, was the most recent appointee, and I understand the only Kennedy appointee, to the Federal Reserve Board, says:

The balance-of-payments problem has prevented the Federal Reserve System from pursuing an easier money policy that might have helped the Nation's economy grow faster this year.

This is a very significant statement, because it contradicts a statement made before the Joint Economic Committee by the Secretary of the Treasury and the Chairman of the Board of Governors of the Federal Reserve Board. I very strongly agree with Mr. Mitchell. I think he is a refreshing breath on the Federal Reserve Board. However, I do feel very strongly, also, that it is a great mistake for us to tailor our monetary policy to the notion that we have an unfavorable balance of payments, when the authori-

ties who have studied this agree overwhelmingly that the interest differential plays a very minor—in fact, an insignificant—part in determining the flow of capital funds.

This opinion has been given by outstanding authorities on the question, including the Federal Reserve's Economist Robert Comar, Assistant Treasury Secretary Robert Roosa, and Dr. Philip Bell, of Haverford University, who included well-thought-out and well-documented evidence before the committee.

Again and again we have asked our top money managers when they excused high interest rates on the alibi that our balance of payments require them to document their position, by proving high interest is necessary to prevent adverse capital flows they have not been able to do so. Even the studies made by the Federal Treasury and the Federal Reserve Board have supported the position we take that higher interest rates as a method of preventing capital outflow or to lure money into this country is not an effective method of accomplishing either purpose.

I ask unanimous consent that the article from the New York Times of today, under the headline, "Payments Deficit Seen Credit Bar" be printed in the RECORD at this point.

There being no objection, the article was ordered to be printed in the RECORD, as follows:

PAYMENTS DEFICIT SEEN CREDIT BAR—MAY HAVE PUT UNWARRANTED CHECKS ON ECONOMY, SAYS DIRECTOR OF RESERVE

WASHINGTON, August 24.—The balance-of-payments problem has prevented the Federal Reserve System from pursuing an easier money policy that might have helped the Nation's economy grow faster this year, according to George W. Mitchell of the Federal Reserve Board.

Mr. Mitchell, formerly director of research for the Federal Reserve Bank of Chicago, is the only appointee of President Kennedy on the seven-man board. He stated his views in a speech yesterday at Madison, Wis.

Mr. Mitchell did not say that the system should have been maintaining looser reins on credit, or even that such a program would have prevented this year's slowdown in the economic uptrend.

POSSIBLE RESTRICTIVE EFFECTS

He did say, however, contrary to recent statements by other authorities in this field, that the international payments problem may have had unwanted restrictive effects on the domestic economy.

The problem is this: to cope with the balance-of-payments deficit—more money flowing out than in—the Federal Reserve and the Treasury have sought to keep short-term interest rates high enough to discourage an outflow of funds seeking better returns abroad. To cope with the domestic problem, the money-policy managers want to avoid interest rates that would discourage borrowing and expansion at home.

CHAIRMAN TESTIFIES

William McChesney Martin, Jr., Chairman of the Federal Reserve Board, testified to the Joint Economic Committee of Congress last week that this problem "has not yet constituted as clear cut a dilemma as some observers suggest." Up to now, he said, the Federal Reserve has not had to choose between the domestic and international problems in deciding what policy to adopt.

Douglas Dillon, the Secretary of the Treasury, testified the following day that "there is no lack of credit availability from domestic expansion."

A basic Martin-Dillon point was that while short-term interest rates had indeed been pushed upward recently for the specific purpose of discouraging outflow, long-term rates had remained relatively steady and some, notably mortgage rates, had actually been declining.

Walter W. Heller, Chairman of President Kennedy's Council of Economic Advisers, had testified to the same committee a week earlier that the late-spring uptrend in rates on long-term Government securities was "a very serious source of concern to us."

He underscored his concern by saying that "interest rates must not be tightened one basis point (one one-hundredth of 1 percent) more, and credit must not be tightened \$1 more, than required by the balance of payments."

SITUATION DELICATE

The Dillon, Martin, and Heller statements, and now the Mitchell speech, do not mean that there is conflict among the policymakers. Rather, they reflect the delicacy of making policy in the present situation.

According to the Martin and Dillon testimony, the present outlook is for interest rates to continue more or less as they are, barring a strong upsurge in demand for loans.

Mr. Mitchell's actual words were: "The slower expansion thus far in 1962 suggests that a more aggressive money policy involving greater availability might have led to a fuller utilization of resources." The Reserve System, however, has had to balance that possibility against the risk that lower interest rates might have worsened the balance-of-payments problem, he said.

He said that the System's actions to support short-term rates may have kept long-term rates from declining more, mainly because the higher short-term rates made short-term investment "too attractive in this period of uncertainty."

REVENUE ACT OF 1962

The Senate resumed the consideration of the bill (H.R. 10650) to amend the Internal Revenue Code of 1954 to provide a credit for investment in certain depreciable property, to eliminate certain defects and inequities, and for other purposes.

WHY INVESTMENT CREDIT SHOULD BE KNOCKED OUT OF TAX BILL

Mr. PROXMIRE. Mr. President, what is the pending business?

The PRESIDING OFFICER. The business pending before the Senate is H.R. 10650, the tax bill.

Mr. PROXMIRE. I asked that question because I intend to make a somewhat protracted speech on the tax bill. I wish to emphasize that, while this will be a long speech, I deliberately chose a late hour on Saturday afternoon because I wanted it understood that I have no intention of delaying consideration or a vote on the tax bill. Also, my remarks, while they will take some time, will be as relevant and as pertinent as I can make them. I not only will make them relevant to the tax bill, but to one section. There are other sections on which I feel strongly, but I am going to discuss only one, that on investment credit.

The investment credit provision was proposed by the administration, I am sure with great sincerity, for the purpose of encouraging an increase in investment in plant and equipment. However, in the process of consideration for 10 months last year by the Ways and Means Committee of the House, and for many months this year by the Finance Committee of the Senate, that original proposal has been changed enormously.

It is my belief that investment credit, which I very strongly oppose, will result in a tax loss for this Government of more than \$1 billion. That \$1 billion loss of revenue will be at a time when we have a large deficit. We had a big deficit last year. We are going to have a deficit this year, and everybody knows it, regardless of business conditions, and even without a tax cut which the President has said will be recommended next year. A tax cut will increase that deficit further.

In addition to the deficit anticipated for this last year, we have an additional \$1½ billion tax cut which the Treasury has already given to business by adjustment in depreciation schedules.

This is not only a tax reduction and, in my judgment, and in the judgment of most of the witnesses who appeared before the Finance Committee and testified on this subject—and I have very carefully gone through all the testimony on investment credit—it is a subsidy, and is defined and described as a subsidy, but the amazing thing is that it is an unwanted subsidy. Business does not want it. Spokesmen for business, from outstanding business firms or business associations, chambers of commerce, oppose it emphatically and clearly, and the National Association of Manufacturers opposes it, and did so with great emphasis and detail in those hearings.

I am going to quote a number of business leaders who oppose it for definite reasons, and not merely because the Kennedy administration offered it. On the contrary, they oppose it because they think it is unfair, will not work, is a subsidy, and will increase our deficit.

I say it will not work, not merely on the basis of simple opposition to it, but on the basis of a very careful business survey. McGraw-Hill, which is recognized as one of the most competent and careful business surveying organizations in the country, made a survey of business recently, very widespread and extensive, and found that the \$1,300 million reduction in revenues would result next year in a \$300 million increase in plant and equipment, if the hundreds of people who were interviewed reflect business opinion. On the basis of the McGraw-Hill surveys, which have been extraordinarily accurate in the past, there is every reason to believe that this is a pretty close and accurate estimate.

Think of it, a tax loss to our Treasury of \$1,300 million. But how much of a stimulus to the economy? Over \$300 million. It is pathetically inadequate. There are reasons for that, which I shall point out.

The National Industrial Conference has made a study of the impact of in-

vestment credit, and it arrived at almost the same figure. It found the increase in plant and equipment would be about 1 percent—in fact, a little less than 1 percent. Since the investment in plant and equipment is expected to be about \$38 billion, that increase would also be about \$300 million.

The Wall Street Journal made a survey of some 68 firms, and it found that of these leading firms—firms that would certainly have to be an important factor if we are going to have a substantial increase in plant and equipment—only 1 out of the 68 leading firms in our country said it would increase or modify or change its investment policy because of the investment tax credit—one firm.

Mr. President, the argument which is used in great detail and with very great emphasis by the Secretary of the Treasury and by others who favor this measure is that it is necessary because it would improve our balance of trade and would put us in a stronger position to compete with other countries. The argument is made that other countries have similar credits or have more rapidly accelerated depreciation and that business firms operating in other countries have an advantage over American business firms.

Mr. President, this is not true on any basis at all. It cannot be shown, as I shall show, that the firms of other countries have a competitive advantage because of depreciation policy. It cannot be shown, as a matter of fact—and this is the telling point, in my judgment—that we suffer at the present time or are likely to suffer in the near future an adverse balance of trade.

It is true that we have an adverse balance of payments, but we have a favorable balance of trade. When I say "favorable," I mean emphatically favorable. We have a favorable balance of trade now which is running about \$5 billion a year. We sell \$5 billion a year more abroad than we buy from abroad. That means that other countries have an adverse balance of trade. The foreign nations might be anxious to modify their labor policies, their tax policies, or other policies, to see if they can correct their adverse balances of trade, but we have a very favorable balance of trade.

Some people say we have that favorable balance of trade because of our foreign aid program, which ties in a lot of offshore procurement; that is, other countries have to buy, with the proceeds of foreign aid, goods from this country. It is true that this is a factor. It is also true that we export a great deal of food which is paid for on a soft currency basis, which we never really receive.

Nevertheless, leaving that out of account, our commercial surplus, or our commercial favorable balance of trade, is \$2.6 billion a year.

This means that Americans are selling commercially more abroad than Americans are buying from abroad; leaving out all foreign aid, leaving out all military purchases, and leaving out all the influence of the Government in the economic picture. Concentrating

only on the commercial area, we have a favorable balance of trade with other countries of \$2.6 billion a year, which is a very substantial proportion of the total amount of exports and the total amount of imports. It is heavy indeed.

It is unlikely that we can maintain that favorable balance of trade. Once again I insist that other countries cannot, for long, continue to have an unfavorable balance of trade.

Therefore, I argue that the contention on the part of the Secretary of the Treasury—and this is the point at which he puts overwhelming weight in his argument—that we must provide a tax "gimmick" of this kind, a tax subsidy of this kind to business, which business does not want, to increase the competitive efficiency of its operations compared to other nations simply does not hold up.

On the basis of the clear comparison of our capacity to sell abroad in competition with the capacity of foreign firms to sell in this country, we are competing extraordinarily well right now.

Mr. President, as this incentive provision was originally designed, it made a certain amount of sense.

As it was originally designed, this proposal would have provided a 15-percent credit, but only for additional investment. It would have provided for a 6-percent credit for 50 percent of regular investment. That would have provided a real incentive for firms to increase their investment and to invest more. Of course, that kind of incentive would have been far less expensive.

I give Senators a quick example. If a firm ordinarily invested \$1 million a year in plant and equipment—I am speaking of a large firm—under the provision, as it has emerged from the Committee on Finance, if the firm did not increase its investment at all it would still receive a credit of \$70,000.

If the firm should reduce its investment from \$1 million a year to \$900,000, it still would receive a big credit. Then it would receive a credit of \$63,000. If the firm should increase its investment from \$1 to \$1.1 million, over the base period—in other words, by \$100,000—it would receive a credit of an extra \$7,000.

It is no wonder that businessmen, when queried by the National Industrial Conference Board and by McGraw-Hill, have said they would not change their investment policies. Of course they would not. They would get the credit whether they increased their investments or not. There would be no real incentive to change. There would be no substantial reason for businessmen to increase their investments.

Mr. President, as I intend to point out in some detail, because I think this must be documented, one of the weakest and worst aspects of the bill is that it would apply to every single utility in the country. When we speak of utilities, it is well known that the utilities have all the funds they need, that they can get all the funds they need, to buy all the equipment they need. Their income, of course, is regulated, almost by definition.

Any time a utility feels it is desirable to build additional plant or to buy addi-

tional equipment, such as an additional generator, it is the easiest thing in the world, in this country—everywhere, and I am speaking of every utility—to get the money, either by use of the depreciation reserve route, or by use of earnings, or by selling obligations to the public. The testimony is clear that utilities have no difficulty at all in getting additional funds, and that their customers would be required to pay for the cost of that additional equipment by every public service regulatory agency in the country. There is no question about it.

As a matter of fact, I think, with all the obloquy which was heaped on the A.T. & T. in the past couple of weeks, it should be pointed out that the A.T. & T. has shown real business statesmanship in this regard. A.T. & T. is a company which invests an enormous amount of money and buys a tremendous amount of plant and equipment. The representatives of A.T. & T. appeared before the Finance Committee and said, in effect, "We do not want this credit." They pointed out that even with a 3-percent investment credit they would get \$75 million a year. That \$75 million a year would be net. That is what they would receive after taxes, if this provision is passed. They said, in effect, "This is so inequitable, so useless. It is not going to persuade us to buy another nickel's worth of equipment. It is a stupid provision. From the standpoint of good public policy, good economic policy, and good tax policy we oppose it."

Not only would the investment credit permit A.T. & T. to get \$75 million a year—which, incidentally, would be 7½ percent of all the credit allowed to all the corporations, all the businesses, and all the individuals in the entire country, which would be a lot of it, and which is not wanted—but, in addition, it would provide that any number of firms, businesses, and individuals who have nothing whatsoever to do with the growth of or the foreign trade aspects of our country would receive juicy handouts.

For example, bar equipment would be included. If a firm should buy a new martini mixer, or if it should buy swizzle-sticks or anything for a bar, it would get a 7-percent credit. Businesses would be encouraged to buy these things. They would get a subsidy for making this kind of investment, which is supposed to provide for the growth of our country.

As was pointed out in the hearings, glass tabletops at the "21 Club" would be included. The Secretary of the Treasury had to agree, in the testimony.

No matter what kind of equipment is bought, whether it be a lighting machine in a burlesque house, a slot machine, or equipment bought by A.T. & T. which they say would have no effect whatsoever on their purchases, they would still receive a 7-percent credit. There would still be a reduction in the revenues needed by our Government at a time when taxes are much too high and the deficit is high and growing.

Probably the strongest argument against the investment credit is the fact that it is not needed. What we need is increased demand.

The fact is that today throughout our country firms are not running close to capacity. The McGraw-Hill survey, which I shall cite in a few moments, shows that firms are now running at something like 85 percent of capacity. Very few firms are close to 90 percent of capacity.

Some industries, like the steel industry, are operating well below the 85 percent of capacity. So long as firms are operating below capacity, there is no reason why they should buy more equipment.

It is true that there may be some modernization, regardless of capacity operation. Why do firms modernize? Why do they buy new equipment? Tax laws may have some influence on that decision. But the overwhelming reason is that firms can economize on their costs, and can reduce their costs, principally labor costs.

As wages rise, and as a firm becomes labor conscious, it is very likely to buy automated machinery which will replace expensive manpower in order to reduce costs. I submit that the evidence is clear that this is an overwhelming reason why firms modernize and why they buy equipment if they are not expanding. If they wish to expand, of course, they may buy additional equipment so that they can produce more. But if they are not going to expand, the big reason for buying new equipment is to reduce costs.

Mr. President, to sum up, I oppose the investment credit provision because it would not work. It would be unfair to other taxpayers who could not take advantage of it, because it is hypercyclical. I have not stressed that point. What the investment credit would do runs counter to everything else that the President has asked for.

It would tend to expand investment in periods of prosperity, expansion and inflation, when profits are high, and firms have something to write it off against, and it would tend to discourage investment in periods of recession and unemployment when profits were going down and firms had very little to write off their increased investment against.

INVESTMENT CREDIT IS INEQUITABLE

The proposed investment credit would not meet the test of tax equity on any score. It would give business firms benefits which would be more than 100 percent of costs. It would permit a firm to write off equipment which it buys at a rate of more than 100 percent.

For a corporation in the 52-percent bracket, the investment credit is equivalent to a depreciation of 107 percent of the cost of the newly acquired asset. Other taxpayers, except those who receive percentage depletion allowance, are limited to deductions of 100 percent of cost.

Granting such an exceptional privilege raises a serious question of tax equity.

It is true that the only other example of this kind of tax privilege, this kind of loophole, and this kind of gross equity is the notorious loophole of the oil depletion allowance.

LOOPHOLE WILL SPREAD

Second, it is almost impossible to remove such a provision from the law once it is in.

That is the difficulty with the provision about which I have been speaking. It will be extremely difficult to get it out of the law should it get in.

It would not only be difficult to get the provision out of the law but also, I predict, that type of provision would spread. It would spread rapidly. Soon it would include buildings. After all, what sense does it make if we give a firm an incentive to buy new equipment, if it must put such equipment in an old, rickety plant that is falling apart?

Therefore I am concerned, as I am sure other Senators must be, about the potentially dangerous precedent set by the investment credit. It is not unlikely that other groups will request similar tax treatment. Retailers may request more than 100 percent deductions for the costs of carrying inventory. Construction firms may request more than 100 percent deductions for buildings they own. Teachers could request deductions for more than 100 percent of the costs of advanced courses. Individuals who borrow money to invest in homes may request more than 100 percent deductions of their interest costs incurred in the purchase of homes.

I mentioned the fact that the proposal is an unfortunate provision because of its hypercyclical aspect. Let me now show why I think it would be hypercyclical. It would aggravate the business cycle by encouraging investment during a period of inflation and discouraging it relatively in a recession, when businesses have less income against which to write off new investment.

Therefore, in periods of recession, these firms will not be able to carry back this credit to a prosperous period. As a matter of fact, the typical growing small firm is likely to go several years, especially a manufacturing firm, before it makes enough money to count. Most investors recognize that, and do not expect a firm to make much money in that period. At the same time, they have to be prepared to go several years before they can expect to make any money. So there will be no credit against which many of these firms can write it off.

If the proposed credit stimulates investment—which I doubt—the stimulus will be greater in those periods when investment is likely to be high in any case. Thus, investment will be stimulated exactly in those periods when there is little or no need for an investment stimulus. Contrariwise, the investment credit will have its least stimulative effect when investment prospects are dim. Hence, the credit will tend to accentuate present fluctuations in investment. If there is any single goal sought by administration economic policy, it is to increase growth by stabilizing the economy and ironing out fluctuations. This proposal will have exactly the opposite

effect. It will be inflationary in boom times. It will increase unemployment in recession periods.

The investment credit is also undesirable from a cyclical standpoint because it serves to reduce Government revenues exactly at those times when Government revenues should be raised to curb private demands for goods and services, namely, in inflationary periods. If the Federal budget were otherwise in balance during a prosperous period, the effect of the investment credit would be to create budget deficits in the prosperous periods. Certainly this is fiscal irresponsibility in its purest form. Moreover, it is bad economics. Almost all economists, regardless of their political persuasion, feel that the Government should run surpluses during periods of high employment. The investment credit will serve to reduce those surpluses, or throw the budget into a deficit position, exactly in those periods when surpluses would be most appropriate.

One basic criticism of the investment credit is that the goals which are sought by this device are inappropriate. Specifically, the credit is designed to stimulate artificially the rate of physical investment in the United States. Why do we need an artificial stimulus to obtain more investment than the free market deems appropriate? A fundamental tenet of our economic system is that, wherever possible and to the greatest possible extent, we will permit free market forces to determine the amounts and types of goods to be produced. The investment credit attempts to interfere with the free market decisions of consumers and producers.

It is argued that the investment credit is needed to stimulate physical investment to compete with foreign countries. Such competition takes many forms. If standard of living is the area of competition, then we have managed well to date without the investment credit.

If "competition with foreign countries" refers to our balance-of-payments position, then it seems ridiculous to support the investment credit for all industries in the United States simply to aid the relatively few firms that actually compete overseas.

I shall go into detail on this point in a few minutes.

Moreover, there has been remarkably little evidence provided indicating that lack of investment is holding back U.S. firms in foreign competition. First, it is not clear that U.S. firms are suffering significantly in their competition with foreign industry.

As I pointed out, we have a highly favorable balance of trade.

Second, it is not clear that, if such suffering is occurring, it is due to lack of investment. It could just as easily be due to lack of initiative, weakness of new designs, excessive labor costs, insufficient mobility, or many other reasons which would not be affected by the investment credit. Surely, the burden of proof is on those who support the investment credit to indicate that the problems of

foreign competition—which were so heavily stressed by Secretary Dillon—in fact exist and would be significantly reduced by adoption of the investment credit.

Mr. President, there has been some criticism of the investment credit for a year and a half, ever since it was introduced early in 1961. These questions have not been answered. The proponents of the investment credit simply come up to Congress and insist that it is going to work, and insist that it will make us more competitive, and insist that it will make business more efficient. However, they never prove their case. They assert it. They assert it, Mr. President. The big question is how something of this kind, which is opposed by all the business organizations, opposed by AFL-CIO, opposed by the Farmers Union, and opposed by the Farm Bureau Federation. How can it pass the Ways and Means Committee?

Any time, certainly any time when it is possible to initiate a tax cut for certain groups and get the President behind it, and the executive branch, including the Secretary of the Treasury, no matter what it is for, no matter how unjust and unfair or unnecessary it may be, or how adverse it may be to our revenues, it is sure to get the support of some people who have an immediate and personal financial interest. There were a few people like that who testified for it. These people are very likely to let their representatives know how they feel about it.

Nobody really seems to care about the loss of a billion dollars, because we become so inured to enormous deficits and enormous spending so that it does not seem like very much. The result is no one fights against it very hard, at least no big group. We do not get the Farm Bureau to come in to do the kind of job that they were able to do on the farm bill in the House of Representatives. We do not get the AFL-CIO to do the kind of job that they would do on a specific piece of labor legislation. Neither will the chamber of commerce do what they would ordinarily do for one of its members when legislation more directly and more adversely to their interests is involved.

So that while people know it is wrong and say so, because they know it is bad social policy and it is bad economic policy and it has a harmful effect on the country, one still cannot get the hard-tough, concerned organization action from groups with political power against such a worthless giveaway.

What grounds do we have for doubting the efficacy of the investment credit?

First, the credit will be given to business firms even if they do not change their investment decisions by one iota. Obviously, business firms are always engaged in making investments. On all of these investments, they will obtain the proposed credit. But the only justification for the credit is that new investment, over and above what would normally be made by a business firm, will be encouraged as a result of the credit. Nonetheless, business firms receive the

cake-credit—and can eat it—without taking any new and additional actions to earn it.

Second, businessmen themselves are not responding favorably to the proposed credit.

It is rare in the area of tax policy to have advance laboratory tests of the potential effectiveness of policy proposals. Such laboratory tests, when available, should certainly be examined closely. In this case we have the example of the accelerated depreciation methods which were introduced in the 1954 Internal Revenue Code. One of the primary purposes of these accelerated methods was to encourage greater business investment in plant and equipment.

Yet, look what happened. Before the enactment of these new methods, the growth in capital stock per worker was roughly 3.5 percent per year. After the adoption of the accelerated depreciation methods, capital stock per worker grew by only 1.9 percent per year from 1954 to 1960. In other words, instead of acceleration of business investment as a result of the new depreciation methods, there was a very substantial drop-off, so that the rate of increase was only about one-half what it had been in the earlier period. The effect of this on output per worker was significant.

Let me digress here to say that, of course, I do not say that because we had more rapid depreciation and greater incentive for business to buy plant and equipment, that was the reason why there was a dropoff in business investment and plant and equipment.

But I say that the depreciation acceleration was swamped, as the investment credit is going to be swamped, by such dominant economic influences as demand, and the percentage of capacity that is being utilized, as the cost of production, including labor costs and the other costs; and these big economic influences are going to swamp investment credit, too.

The effect of these dominant economic influences on output per worker was significant. Output per worker in the period from 1947 to 1954 increased by 3.3 percent per year. After the accelerated depreciation methods were enacted, the rate through 1960 was only 2.1 percent per year.

So we tried this tax gimmickry before. It did not work. We found that our efficiency rate with respect to plant and equipment sharply declined.

How can we explain this lack of effectiveness of a tax stimulus to investment so analogous to the investment credit? It seems to me there are several available explanations in addition to the ones I have given. One, while the tax benefits were being given, there was still no corresponding increase in aggregate demand for the goods and services which additional investment could produce. Therefore, while there were cost savings through tax reductions, there was no particular stimulus to obtain more investment to produce more goods and services. The tax stimulus, as I am sure will be the case with the investment credit, was simply reflected in increased

profits, rather than increased production.

Two, the period since 1954 has been generally one of excess capacity due to inadequacy of consumer demand. Given this excess capacity, there are relatively few marginal investment decisions which will be encouraged by an investment tax stimulus such as accelerated depreciation or the proposed credit.

CREDIT COULD BE INFLATIONARY

I wish to emphasize this, because it is an extremely important point. The investment tax credit may work when industrial operations are close to capacity. The incentive may work, but it does not work, and the experience between 1954 and 1961 shows that it does not work, when industry is operating well below capacity operations, as it is now. This ties in beautifully with the argument I made that this is a hypercyclical, supercyclical, likely to be inflationary incentive, because what happens in the good and prosperous years, when capacity is crowded and industry is operating close to capacity? Then there will be an incentive to invest, and then, believe me, that is exactly the time when there is every incentive for business to increase its prices. It has always been done before. Now it will be done a fortiori; it will be done with great emphasis, because there is an additional stimulus working in the economy, but only working fully at a time when we do not need it, only at a time when there is pressure on limited facilities.

Third, there is ample indication that prices of products are sometimes administered prices. When this is the case, prices are less subject to market forces. We know this is not simply an occasional situation. We know it is true in the steel industry, and throughout much industry. We know it is true to a considerable extent in the tobacco industry, the insurance industry, and, to a lesser extent, the automobile industry and in the oil industry.

Such prices tend to stay up under circumstances in which they could be reduced. Returns from increased investment for a business firm come only if the firm reduces its prices to sell the increased quantities that can be produced with the additional investment.

Rather than expanding plant and equipment to produce more goods and then lowering prices in order to sell the additional goods, some firms have been content to maintain prices and sell lesser quantities that require lesser amounts of plant and equipment.

A classic example is steel, which now has a break-even point of 40 percent of capacity, and makes a very good profit at 70 percent of capacity, and is in a position where this kind of incentive would be of almost no value, or almost minimal value. In fact, steel officials admitted this to McGraw-Hill interrogators.

Almost every economist who testified at the hearing agreed that this would have very little stimulating effect on steel. Yet it is interesting that the one industry which the Secretary of the

Treasury said is really watering at the mouth for this privilege is the steel industry. The steel industry wants it, but it will not have any favorable economic effect upon the country through what the steel industry will do with it, because there is no argument, there is no question that steel will use it for anything except to increase its after-tax income to capacity.

The tax stimuli to investment, therefore, reflect themselves merely in higher after-tax profits at constant price levels, rather than in greater production at lower price levels.

A principal argument for the investment credit is that business firms need additional cash for additional requirements. The facts refute this justification. There is no evidence that the major firms, which do the great amount of investing in the United States, need additional cash flows to finance further investment.

On this point I shall really give it to the Senate in spades tonight, because I have it documented completely. There is no question about it. I shall do that in a few minutes.

We can take General Motors, for example. General Motors set aside depreciation reserves of \$1,637 million during the years 1957 to 1960, while it invested only \$1,589 million in plant and equipment combined. During those same years, it retained profits after payments of dividends in the amount of \$1,017 million, out of which it added \$965 million to its cash and security holdings—rather than in physical investment—so that the total of its financial holdings at the end of 1960 was \$1,637 million—ironically, the same amount as its depreciation reserves.

In this instance, General Motors in a sense did not use any depreciation reserves for plant and equipment at all. General Motors kept that in Treasury bills and notes. I suppose they invested also, to some extent, in the obligations of other firms.

Surely General Motors has not been in need of an artificial tax advantage to support further physical investment.

The GM case is typical of many large firms and reflects the situation in industry generally. Table 1, drawn from the recent report of the President's Council of Economic Advisers, indicates that, in the period from 1959 to 1961, funds available from internal sources alone exceeded total plant and equipment outlays for industry generally. This is completely aside from the additional funds that would be available through new debt financing or new equity issues.

I may say that is completely aside from the \$1,500 million tax cut for this purpose which the Treasury has already given business.

Mr. President, I ask unanimous consent to have printed at this point in the RECORD a table showing the relationship of plant and equipment outlays to internal funds.

There being no objection, the table was ordered to be printed in the RECORD, as follows:

TABLE 1.—Relationship of plant and equipment outlays to internal funds

[Billions of dollars]			
Period	Plant and equipment outlays	Funds available from internal sources ¹	Col. (2) as percent of col. (1)
	(1)	(2)	(3)
1950-54.....	\$107.2	\$97.1	90.6
1955-58.....	113.2	108.4	95.8
1959-61.....	88.9	93.0	104.6

¹ Retained profits and depletion allowances, and depreciation and amortization allowances.

Source: Table B-65, report of the Council of Economic Advisers, January 1962, p. 283.

Mr. PROXMIRE. Mr. President, it has been alleged that the low level of investment in recent years has been due to a squeeze on corporate profits. Two sets of facts indicate that this reasoning is fallacious. The first set of facts involves the history of the last few years. This history indicates quite clearly that corporate profits are quite sensitive to the rate at which capacity is being utilized. Corporate profits have been low only when capacity is not being fully utilized. Since the rate of utilization was higher in the early period of this decade, it follows that the ratio of profits to GNP would be higher in the earlier period. This in turn, suggests that the lack of investment has been due to an inadequacy of final demand, rather than a lack of corporate profits. Lack of investment is a symptom, not a cause.

The second set of facts concerns the relationship between corporate profits and that part of the national income which originates in corporations. If the corporate share of economic activity falls, corporate profits decline as a percentage of GNP, even when corporate profits are a stable percentage of the income flow through corporations.

If a comparison is made simply between corporate profits and GNP, this percentage has gone down. However, if corporate profits plus capital consumption allowances are related to national income originating in corporations—which is the more relevant comparison—it is clear that the ratio in recent years has been higher than at the beginning of the decade—even though unemployment rose from 3.7 percent to 6.1 percent during the same period.

In the course of the hearings before the Joint Economic Committee, many witnesses appeared and gave testimony relating to the point about which I am now speaking.

LANGUM PROOF OF ADEQUATE CASH FLOW
WITHOUT INVESTMENT CREDIT

Mr. President, one man who appeared was John K. Langum, president of Business Economics, Inc., of Chicago, Ill. He made a very careful analysis of cash flow and what happened as to the availability of funds to business firms in this country for investment in plant and equipment. He provided a real eye opener, because I think I can show that never before in history has business had so much money available to be put into plant and equipment as it has today;

never before have we had a situation in which business has been so able to invest in that way. So the argument that a tax credit is needed, to permit business to invest in plant and equipment, is fallacious.

I quote now from the statement submitted to us by Mr. Langum:

The historical record in terms of the overall data as reported greatly exaggerate the real decline in corporate profitability which has occurred. More than that, undue concern about the profits situation has in itself caused weakening of business confidence and hurt the cause of adequate recovery. Furthermore, erroneous interpretations of the situation regarding corporate profitability directs attention away from the more basic matters making for the good health of the economy and with that the well-being of corporate profitability as well.

As I see it, there have been three fundamental factors causing the decline from the high levels of profit margins and rate of return as reported which prevailed in the early postwar years. These are: First, the unusual circumstances of the early postwar years which led to record levels of profits never reached before or after.

Mr. President, there is talk about a profits squeeze. But, Mr. President, the difficulty is that those who make such statements are comparing the situation existing at this time with the situation at a time when profits were at an all-time high, for peculiar reasons. Incidentally, profits have gone even higher recently.

I read further from the statement by Mr. Langum:

Second, the tremendous step-up in depreciation charges during the last decade which has lowered reported earnings but has increased cash flow. Third, the inadequate growth in the economy generally from 1957 on and particularly the sideways movement of real output in the private durable sector.

Unusual circumstances of high demand and short supply made the early postwar years the most profitable period corporate enterprise has ever experienced. Beyond this, costs, including the cost of plant consumed, were seriously understated and reported profits were greatly overstated. In particular, the tremendous burst of demand in the early postwar years brought about a rapid increase in prices which gave rise to major inventory profits included in reported corporate profits. The effect on profits of inventory valuation from changing prices has been specifically recognized and measured by the Department of Commerce. Some aspects of this are shown in the table on page 3 entitled "Inventory Valuation Adjustment in Relation to Corporate Profits before Taxes."

Incidentally, Mr. President, a little later I shall ask unanimous consent to have printed in the RECORD a series of tables submitted by Mr. Langum.

I read further from his statement:

The degree to which inventory valuation raised reported profits is indicated for selected early postwar years—1947, 1948, 1950—in contrast to certain recent years. When prices are rising, as they were sharply in the early postwar years, higher profits emerge from inventory valuations at lower levels of costs.

I think this fact should be called to the attention of critics who say profits have not been so good. The amazing

thing is that this year profits are going up to an alltime high, despite the fact that prices are level and despite the fact that wholesale prices have been extraordinarily stable for 5 years. A big reason for increased profits has been the change in inventory valuations. But now we have a situation in which prices are not rising at all; and under these circumstances the profit showing is a real one in terms of inventory, not simply one which results from changes in the price level.

I read further from the statement by Mr. Langum:

As a matter of fact, much of the decline in corporate profitability as indicated by reported data is simply a return to more usual circumstances from extremely abnormal situations prevailing after World War II.

This is also indicated in the tables.

Then Mr. Langum says:

Basic emphasis must be given to rising depreciation charges. Data on this matter are shown on page 1. The dollar amount of depreciation and amortization charges, as measured in the Department of Commerce series on sources and uses of corporate funds, is shown in the second column. Depreciation charges have risen from \$7.8 billion in 1950 to \$19.1 billion in 1957 and to \$24.8 billion in 1961.

CASH EARNINGS SKYROCKET

Mr. President, I wish to emphasize this point, because it has been overlooked. Again and again we hear it argued that profits are about the same now as they were in 1950. But I wish to point out, first of all, that profits were very high in 1950, as I have said, partly because prices had been rising and because inventory valuations were up. Second, I wish to point out that there has been a mammoth increase in depreciation charges since 1950; and so far as the ability of business to invest in plant and equipment is concerned, it is measured, not only by earnings, but also by depreciation reserves. And depreciation reserves have risen from \$7.8 billion in 1950 to \$24.8 billion in 1961—or an increase of \$17 billion, or an increase of well over 200 percent in 10 years—a terrific increase, which far exceeded increases in income, profits, wages, and gross national product. The increase is perfectly enormous. Of course, it is this depreciation reserve which enables business to be in a very strong position now to invest in plant and equipment, and not to need the proposed investment credit.

Mr. President, the charts Mr. Langum prepared for the Joint Economic Committee on August 10 are most persuasive on this score. As a matter of fact, if we go back a little further, they are even more persuasive. He points out that corporate profits after taxes have risen from \$13.4 billion in 1946 to \$23.3 billion in 1961—an increase of approximately 70 percent. But depreciation for the period from 1946 to 1961 increased from \$4.2 to \$24.8 billion—a six-fold increase, or 500 percent. If we add those two, we find that cash earnings—which constitute the real index of what business has available for investment in plant and equipment—increased from \$17.6 billion in 1946 to \$48.1 billion in

1961—certainly an alltime high. So business is in a very strong position to invest in plant and equipment, based on cash earnings, without any reliance whatsoever on the equity market or on the capital market in any form.

I ask unanimous consent that table

Corporate profits in relation to depreciation accruals and capital outlays, 1946-61

[In billions of dollars]

	Corporate profits after taxes	Depreciation and amortization allowances	Cash earnings	Plant and equipment outlays	Net cash earnings	Corporate dividends
1946.....	13.4	4.2	17.6	12.5	5.1	5.8
1947.....	18.2	5.2	23.4	17.0	6.4	6.5
1948.....	20.5	6.2	26.7	18.8	7.9	7.2
1949.....	16.0	7.1	23.1	16.3	6.8	7.5
1950.....	22.8	7.8	30.6	16.9	13.7	9.2
1951.....	19.7	9.0	28.7	21.6	7.1	9.0
1952.....	17.2	10.4	27.6	22.4	5.2	9.0
1953.....	18.1	11.8	29.9	23.9	6.0	9.2
1954.....	16.8	13.5	30.3	22.4	7.9	9.8
1955.....	23.0	15.7	38.7	24.2	14.5	11.2
1956.....	23.5	17.3	40.8	29.9	10.9	12.1
1957.....	22.3	19.1	41.4	32.7	8.7	12.6
1958.....	18.8	20.3	39.1	26.4	12.7	12.4
1959.....	24.5	21.6	46.1	27.7	18.4	13.7
1960.....	23.0	23.1	46.1	30.8	15.3	14.4
1961.....	23.3	24.8	48.1	29.6	18.5	15.0

Mr. PROXMIRE. Mr. President, in addition, on the basis of data furnished by the First National City Bank of New York, Mr. Langum shows the rate of return on net worth for leading manufacturing corporations. It is interesting to note that for the period 1925 through 1929, the average was 11 percent. Then, after the war, for the period 1947-51 the average was 16.2 percent. The trouble is that people are inclined to say that that 16 percent is normal, and wish to compare the figure for other periods with that one. However, it should be noted that during the next 5 years the average decreased to 13.2 percent, and during the next 5 years—from 1957 to 1961—it decreased to 11 percent. So now it is exactly at the same rate it was in the golden 1920's, which generally are regarded as years of great prosperity. But the point is that today business has far, far greater depreciation reserves—and not only in terms of gross national product or the needs of business; on any basis which one might consider, they are far greater than ever before.

I ask unanimous consent that the table to which I have referred be printed at this point in the RECORD.

There being no objection, the table was ordered to be printed in the RECORD, as follows:

Rate of return on net worth, leading manufacturing corporations

FIRST NATIONAL CITY BANK DATA

	Percent
1925.....	10.7
1926.....	10.8
1927.....	9.0
1928.....	11.6
1929.....	12.8
5-year average.....	11.0
1947.....	17.0
1948.....	18.9
1949.....	13.8
1950.....	17.1
1951.....	14.4
5-year average.....	16.2

1, entitled "Corporate Profits in Relation to Depreciation Accruals and Capital Outlays, 1946-61," be printed at this point in the RECORD.

There being no objection, the table was ordered to be printed in the RECORD, as follows:

Rate of return on net worth, leading manufacturing corporations—Continued

FIRST NATIONAL CITY BANK DATA

	Percent
1952.....	12.3
1953.....	12.5
1954.....	12.4
1955.....	15.0
1956.....	13.7
5-year average.....	13.2
1957.....	12.1
1958.....	9.8
1959.....	11.6
1960.....	10.5
1961.....	10.1
5-year average.....	11.0

BUSINESS FALLING FAR BEHIND CASH EARNINGS IN MACHINERY-EQUIPMENT INVESTMENT

Mr. PROXMIRE. The next table is a table entitled "Capital Outlays and Corporate Dividends in Relation to Cash Earnings, 1946-61."

This table shows that if we consider the relationship of plant and equipment outlays to cash earnings, we find that since 1952 the ratio has dropped from 81 percent to 61 percent. It has dropped fairly steadily and uniformly. It means business is investing a smaller and smaller part of cash earnings available in plant and equipment.

So, far from needing this additional investment credit, which would give them the capacity to invest in plant and equipment, they need it far less than they did 10 years ago.

I repeat, at that time they were investing 81 percent of their cash earnings in plant and equipment. Now it has dropped down to 61 percent. This last figure of 61 percent does not include the huge increase in depreciation reserves made by the depreciation change that gave the firms an additional \$1½ billion.

I ask unanimous consent that this table, entitled "Capital Outlays and Corporate Dividends in Relation to Cash Earnings, 1946-61," be printed in the RECORD at this point.

There being no objection, the table was ordered to be printed in the RECORD, as follows:

Percent of capital outlays and corporate dividends in relation to cash earnings 1946-61

	Plant and equipment outlays/cash earnings	Corporate dividends/corporate profits after taxes	Corporate dividends/cash earnings
1952	81.16	52.33	32.61
1953	79.93	50.83	30.77
1954	73.93	58.33	32.34
1955	62.53	48.70	28.94
1956	73.28	51.49	29.66
1957	78.99	56.50	30.43
1958	67.52	65.96	31.71
1959	60.09	55.92	29.72
1960	66.81	62.61	31.24
1961	61.54	64.38	31.18

CASH EARNINGS SUPERABUNDANT FOR BIG FIRMS

Mr. PROXMIRE. Mr. Langum's next to the last table shows cash flow in relation to sales for all manufacturing corporations, by size. The table shows that the smaller the firm, the smaller the cash flow is in relationship to sales. The bigger the firm, the bigger the cash flow. There is a tremendous difference.

With the small firms which have assets of less than \$1 million, only 3.3 percent of their sales is available for cash earnings for reinvestment. For the next sized firms the percentage is 3.8 available. The percentage rises quite sharply to 8.1 percent for the big firms with assets of \$250 million to \$1 billion. For the really big firms, with assets of \$1 billion and over, the ratio is 14 percent. In other words, there the cash flow is 14 percent of their sales.

These are the firms that are going to get the principal, the prime, the overwhelming benefit out of the investment credit.

INVESTMENT CREDIT GIVES BIG FIRMS ADVANTAGE

The very biggest firm on the face of the earth, American Telephone & Telegraph Co., is going to get about 7 percent of this whole credit. It is going to get \$75 million. It does not want it. It says it is bad public policy. Bless them for saying it, but they are going to get it. They say they do not want it.

The bigger the firm, the more investment credit it will get, whether it is growing or not. As a matter of fact, the small, growing firm is very likely not to make money for several years. It is competing with firms that invest great sums in plant and equipment. The big firm will get 7 percent for all the plant and equipment they invest in. It might buy a machine for \$10,000. It is going to cost it only \$9,300, because it can take the credit against its income. A small firm, not making money, but which is growing, as is true of most firms for the first several years, will have to pay \$10,000. This tax credit is going to be discriminatory against such firms until they make substantial amounts of money. Until then, the big firms are going to get the advantage. As I said, the bigger the firm, the bigger the advantage.

I ask unanimous consent that the table to which I have referred be printed in the RECORD at this point.

There being no objection, the table was ordered to be printed in the RECORD, as follows:

Cash flow in relation to sales, all manufacturing corporations, by size, 1961

	Percent of sales		
	Net profit after taxes	Depreciation and depletion ¹	Total
All asset sizes	4.3	3.3	7.6
Under \$1,000,000	1.2	2.1	3.3
\$1,000,000 to \$5,000,000	1.8	1.9	3.8
\$5,000,000 to \$10,000,000	2.8	2.2	5.0
\$10,000,000 to \$25,000,000	3.1	2.4	5.5
\$25,000,000 to \$50,000,000	3.8	2.8	6.6
\$50,000,000 to \$100,000,000	4.0	2.9	6.8
\$100,000,000 to \$250,000,000	4.1	3.2	7.2
\$250,000,000 to \$1,000,000,000	4.8	3.3	8.1
\$1,000,000,000 and over	8.4	5.7	14.0

¹ Including accelerated amortization of emergency facilities.

Mr. PROXMIRE. Mr. President, I ask unanimous consent to have printed at this point in the RECORD a table entitled "Annual Rate of Profit After Taxes on Stockholders' Equity at End of Period, All Manufacturing Corporations, by Size, 1961."

There being no objection, the table was ordered to be printed in the RECORD, as follows:

Annual rate of profit after taxes on stockholders' equity at end of period—All manufacturing corporations, by size, 1961

	Percent
All asset sizes	8.7
Under \$1 million	5.6
\$1 million to \$5 million	6.0
\$5 million to \$10 million	6.8
\$10 million to \$25 million	7.0
\$25 million to \$50 million	7.6
\$50 million to \$100 million	8.3
\$100 million to \$250 million	8.4
\$250 million to \$1,000 million	9.3
\$1,000 million and over	10.8

Mr. PROXMIRE. This table shows that the big firms, with assets of \$1 billion and over, had twice the average rate of return in 1961 as the small firm with assets of \$1 million and less.

NEW DEPRECIATION GUIDELINES FURTHER INCREASE CASH EARNINGS

As I said, all of this refers to the situation before the depreciation guideline rules were adopted. This year, the Secretary of the Treasury—as a matter of fact only a few weeks ago—revolutionized business costing, and, for that matter, corporation income tax procedures. He did it by his new and, I think, on the whole, laudatory and appropriate change in depreciation schedules. In doing it, he undermined the argument that business needs additional funds for investment in equipment and machinery, because, as I have pointed out, all the evidence shows that they already have ample funds. The new depreciation guidelines and rules, publication 456 will make far more money available, because this provides such a substantial

increase that I am going to read from the very concise and very well expressed introduction, which is quite short. The introduction points out:

The procedure becomes effective immediately and may be used in the preparation of any tax return due after the date of publication.

The date of publication was July.

The new guideline lives and new administrative procedures are applicable to all depreciable property, including existing assets as well as new acquisitions.

New guideline lives for machinery and equipment are set forth which, on the whole, average 30 to 40 percent shorter than those previously suggested for use by taxpayers. The new guidelines will automatically permit more rapid depreciation deductions than those presently taken on 70 to 80 percent of the machinery and equipment used by American business. They will not disturb the depreciation taken on the remaining 20 to 30 percent of business assets on which depreciation is now as fast as, or faster than, that provided in the new guidelines.

So what they do is speed up depreciation wherever people want to speed it up. Wherever they are satisfied with the rate of depreciation, they can go along at any rate they wish.

I continue to read:

A central objective of the new procedure is to facilitate the adoption of depreciable lives even shorter than those set forth in the guidelines, or shorter than those currently in use, provided only that certain standards are met and that subsequent replacement practices are reasonably consistent with the tax lives claimed.

As I am going to point out, it means they can virtually depreciate their equipment at any rate, provided they use it up, but there is no longer any limitation on depreciation, provided they comply with the reasonable provisions set forth here, and they are very reasonable, believe me.

I want to repeat, because I think it is worth emphasizing this point of the use of lives shorter than the guidelines provided.

The guideline lives will not be treated as minimums. Shorter lives which have already been established or which may in the future be justified as reflecting the taxpayer's existing or intended replacement practices will be permitted.

Thus the new procedure will not disturb the continued use of below-guideline lives which a taxpayer has already demonstrated to be realistic.

Moreover, the procedure sets forth standards under which taxpayers, including those previously using lives below the guidelines, may establish still shorter tax lives concurrent with the adoption of more progressive replacement and modernization practices.

It provides that the reserve ratio test is not exclusive; that it is an overall measure; that penalty rates will not be imposed.

Finally, it says:

Where a depreciable life used by a taxpayer cannot be justified under any of the standards provided in this procedure, including the reserve ratio test and use of all pertinent facts and circumstances, the life will be lengthened in accordance with definite rules. However, the life will in no

case be lengthened beyond the shortest life which can be justified by all the facts and circumstances. The adjusted life will be designed to reflect the taxpayer's current replacement practice for that class.

Mr. President, it seems to me that the Treasury is being as reasonable as it can possibly be and still provide any kind of justification with respect to the other taxpayers. Any businessman who wants to depreciate at any rate he wishes to depreciate can do so, provided, of course, he is actually using up the equipment. There is no limit whatsoever.

As I say, this is good. This is desirable. This is necessary. I think this is going to be good for the economy.

But, Mr. President, I think this is enough. This is a terrific reform. It is a real advantage. It goes quite far. To go further than this, and especially to go further than this with a tax credit of the kind suggested, is, plainly, unjust to the ordinary taxpayer who cannot take advantage of it.

DILLON ADMITS CASH EARNINGS ADEQUATE FOR INVESTMENT

To clinch this point on which I have been laboring so long, which I have been trying to emphasize so heavily—that business does not need additional cash earnings to buy equipment—I should like to quote from the testimony of Secretary Dillon, who is certainly the chief proponent of the proposal. Secretary Dillon appeared before the Joint Economic Committee several days ago. I asked him about this specific question. This is what Secretary Dillon said:

First, on the question of cash flow.

There is, I think, generally speaking, or there has been, adequate flow, although it has not been adequate for certain specific industries, and I mentioned the steel industry as one possibility. But for industry as a whole, I do not think cash flow is the problem.

Mr. President, I think that these words by Mr. Dillon sew the case up pretty well.

The fact that the chief proponent, the man who is fighting so hard for this provision, the real author of the proposal admits that cash flow is not a significant factor, although it may be with respect to a few isolated industries, it seems to me, buttons up the case completely.

MCGRAW-HILL SURVEY SHOWS RECORD AND RISING INVESTMENT IN PLANT AND EQUIPMENT

Mr. President, I referred earlier to the McGraw-Hill studies. McGraw-Hill is an agency to which I think the business of the Nation owes a real debt of gratitude, because they have made authoritative, competent, careful studies of business, and their surveys have been recognized as being objective, accurate, honest and fair.

The most recent survey by McGraw-Hill bears right on the point of investment credit. I shall give the highlights.

1. American business now plans to spend \$38 billion for new plants and equipment this year. If these plans are carried out, capital spending will top the previous record set in 1957, by \$1 billion. Preliminary plans for 1963-65 indicate a high level of investment in new facilities in the years ahead.

In other words, the No. 1 agency surveying business investment in plant

and equipment says that investment is going to be good this year, and that all the evidence is it is going to be good in 1963, in 1964, and in 1965, whether we provide an investment credit or not. None of this is posited on having an investment credit. We do not need it. McGraw-Hill, on the basis of a very careful, thorough, comprehensive survey of hundreds of business leaders, comes to this conclusion.

The argument has been made that perhaps we cannot expand our facilities in a period in which industry is operating well below capacity, but certainly we can modernize it at a more rapid rate, and that is where we ought to concentrate investment, rather than in the expansion of facilities.

What does McGraw-Hill say about this?

2. Manufacturers continue to stress modernization. They will devote 70 percent of this year's investment to modernization, and an almost equal percentage during 1963-65.

3. Manufacturers were operating at an average rate of 83 percent of capacity at yearend 1961, seven points below their preferred rate. They plan to increase their capacity 4 percent this year and 10 percent between 1963 and 1965. This is at about the same rate as during the past 4 years.

In other words, Mr. President, business is operating, according to McGraw-Hill, at 7 points below its optimum, and at 17 points below its maximum. There is no indication at all that business needs to increase its capacity, or that it would increase its capacity, yet this investment credit provision is designed to give to business the ability to do that, although the authoritative business agency which is studying the problem says, on the basis of these facts—at least, I would certainly so conclude—that it is not needed.

4. Manufacturers expect unit sales volume to rise 7 percent this year, and another 18 percent by 1965. For the long run, every industry expects sales to rise faster than expansion of capacity. If these sales expectations were realized, pressure for additional capacity would develop.

If that pressure develops, it is perfectly clear that it would be the real incentive for increasing plant and equipment, exactly as it has always been in the past, and exactly as it was the incentive which provided increased plant and equipment between 1947 and 1954, before there was any accelerated depreciation and before there was any tax credit incentive. At that time we had a far greater rate of expansion in plant and equipment.

5. American manufacturers, having concentrated on modernizing facilities between 1958 and 1961, have updated a large portion of their plant and equipment. Only 24 percent of plant and equipment now operating was installed prior to 1945, compared with 48 percent in August 1958.

The argument has been used over and over again by Secretary Dillon and by others, "The trouble is that American equipment is old. We cannot compete with equipment overseas, because that equipment is newer."

What does McGraw-Hill say, on the basis of the facts—not on the basis of

the theory of the Secretary of the Treasury or of some economist in the Treasury Department who has dreamed up some new "gimmick," but on the basis of what the facts show?

Only 24 percent of plant and equipment now operating was installed prior to 1945, compared with 48 percent in August 1958.

In other words, there is now a far newer industrial plant in America than there was 4 years ago.

As I said, modernization is going to be the object of 70 percent of the investment this year and in the coming years. Also, as I said, there is a perfectly enormous amount of cash earnings available for this investment.

6. Companies expect their cash flow—depreciation plus retained earnings—to rise 14 percent this year. Because of this sharp rise in internal funds, they expect their demands for external funds for all purposes will increase only 1 percent over last year.

In other words, this was done, as I understand it, before the new, generous depreciation guidelines were announced or before it could be certain they would be announced. At that time, before the guidelines were announced, there was virtually no dependence on external financing. The business firms could do it all internally, without any resort to America's unparalleled, unrivaled capital markets. Why in the world do we need an investment credit provision?

7. Industry continues to seek new products, new processes, and improvements in present products. R. & D. performed by industry will amount to nearly \$12 billion this year and \$13.3 billion by 1965.

Of course, there is the real factor which is going to stimulate investment in plant and equipment in America.

Let me go into a little bit of detail on this, because I think this argument is so important. It goes right to the point of the argument for an investment credit and the contention that it is needed this year.

Business as a whole is going to invest \$38 billion in new plant and equipment in 1962, which is more than in any previous year in history. This is \$3.5 billion, or more than 11 percent, more than was spent last year.

It is well over the top of the previous record for spending in 1957, by a billion dollars.

The manufacturers plan to spend \$15.4 billion, a 13-percent increase over 1961, but a half billion dollars short of the 1957 record.

What will be the overall effect of spending a billion dollars more?

Incidentally, most business firms have significantly raised their sights since last fall. The McGraw-Hill survey, which was taken last October, indicated a 4-percent increase in capital investment this year. The U.S. Department of Commerce, Securities and Exchange Commission survey, taken in January and early February, showed an expected 8-percent increase in overall capital spending.

The current survey also indicates that industrial firms have updated a large proportion of their plant and equipment.

Still, American manufacturers plan to continue their modernization drive. Taken

as a whole, this survey highlights industry's emphasis on modernization, on replacement of obsolete facilities, and on its continuing search for new products, new processes, and cost-cutting facilities. These are the most important findings of this, the 15th annual survey of business' plans for new plants and equipment.

I ask unanimous consent that a table from the U.S. Department of Commerce,

Securities and Exchange Commission, showing plans for capital spending by all manufacturing, mining, railroads, other transportation and communications, electric and gas utilities, commercial, and all business, be printed at this point in the RECORD.

There being no objection, the table was ordered to be printed in the RECORD, as follows:

Plans for capital spending

(Dollars in billions)

Industry	Actual, 1961	Planned, 1962	Percent change, 1961-62	Preliminary plans		
				1963	1964	1965
All manufacturing.....	\$13.67	\$15.41	13	\$14.89	\$15.15	\$15.03
Mining.....	.98	1.09	11	1.00	.99	.98
Railroads.....	.67	.85	27	.75	.77	.76
Other transportation and communications.....	5.07	5.60	8	5.07	5.05	4.94
Electric and gas utilities.....	5.52	5.74	4	5.68	6.11	6.19
Commercial.....	8.46	9.39	11	8.83	8.12	7.71
All business.....	34.37	37.98	11	36.22	36.19	35.61

Source: U.S. Department of Commerce, Securities and Exchange Commission.

Mr. PROXMIRE. Mr. President, the report continued:

Equally important as the record amount planned for this year is the high level of planning for 1963-65. Business firms already have plans for an average expenditure of almost \$36 billion per year—an amount exceeding the average spending in any 3 consecutive years in our history. Manufacturers in particular indicate a high level of investment in the years ahead. In each of the years between 1963 and 1965, they indicate investment plans more than \$1 billion higher than their 1961 investment.

WHY DO WE NEED INVESTMENT GIMMICKS NOW?

It is remarkable at this time, when the business leaders of our country, the ones who make the decisions, the ones who know, if anyone knows, according to McGraw-Hill, that they expect to increase their investment so that it will be the biggest increase we have ever had in our history, and it will be continued for the next 3 years, we have a proposal for the Treasury to provide a windfall, a giveaway, and a proposal that business says will do no good. They will take it, but it will do no good.

I wish to emphasize what McGraw-Hill has said:

The McGraw-Hill survey is not a forecast, but a report of what companies now plan to spend. Past experience indicates that a

wide variation of capital spending is possible under changing economic conditions. Plans beyond 1 year are subject to review and revision as the time approaches. In past surveys preliminary plans for future years have generally been considerably lower than plans for the current year. That is because some companies do not plan fully beyond the current year. Nor do they fully anticipate their future demands. Thus preliminary plans for the years ahead have generally been revised upward. Thus, if there is an upward revision, 1963, 1964, and 1965 will be years of high, and perhaps record, capital expenditure by business.

PLANS IN MANUFACTURING

The recovery in business sales and profits evidently has had a favorable influence on capital expenditure decisions in recent budget reviews. Almost every industry has increased its investment plans since last fall. At that time, manufacturers as a whole planned a 7-percent increase. They now indicate plans for a 13 percent increase. Only the chemical industry plans a lower level of investment than it did last fall, because of a slight cutback in petrochemical investment. Electrical machinery makers plan to reduce investment 5 percent this year, but this is a lesser reduction than the 9-percent cut indicated last fall. Apparel and textile manufacturers, who recently were permitted faster writeoffs of their equipment, have taken advantage of this provision by raising their planned investment since last fall.

All other manufacturing industries indi-

cate increases of 10 percent or more, ranging from a 30 percent increase in the rubber industry to 10 percent for paper and pulp producers.

Once again, whenever we enter into a discussion or an argument about the fact that they are using the investment credit not only for manufacturing but for all purposes, including transportation, entertainment, and creation, they say—

Yes, but the main field of competition is in manufacturing. That is where we must be competitive. We must compete with European countries. That is where we must get growth and modernization.

But what do the facts show? When we go to the business leaders who make the plans, we find that they plan to expand at a record rate. They plan to expand more rapidly than ever before.

The proposed legislation is not needed. I submit it is a tax cut at a time when we are facing a big deficit. I can think of all kinds of things we could spend the money for, including education and many other things. I can also think of many people who would like to share in a \$1 billion tax cut. That could mean a great deal of money in the pockets of Mr. and Mrs. Average Taxpayer.

But in the circumstances, we are asked to give it to businesses when they say they do not need it. Not only do they say they do not need it, but their objective testimony and the most competent survey indicate that they will not use it and will expand at a very healthy rate without it. The investment credit makes no sense.

The statement shows that railroads, commercial businesses, trade, finance, electric utilities, and so forth, plan to continue to increase their investment at a very substantial rate, with very few exceptions.

As I said, in rubber there would be an increase of 30 percent; transportation equipment, aircraft, ships, and so forth, 28 percent; autos, trucks, and parts, 20 percent; nonferrous metals, 25 percent; steel, 15 percent, and so on.

I ask unanimous consent that a table showing the plans for increased investment for 1962, and also the preliminary plans for 1963, 1964, and 1965 be printed at this point in the RECORD.

There being no objection, the table was ordered to be printed in the RECORD, as follows:

Capital spending plans of manufacturing companies

(In billions of dollars)

Industry	Actual, 1961	Planned, 1962	Percent change, 1961-62	Preliminary plans		
				1963	1964	1965
Iron and steel.....	1.13	1.30	15	1.27	1.05	0.88
Nonferrous metals.....	.26	.32	25	.37	.40	.41
Machinery.....	1.10	1.32	20	1.29	1.38	1.41
Electrical machinery.....	.69	.66	-5	.65	.67	.64
Autos, trucks, and parts.....	.75	.90	20	.86	.98	.94
Transportation equipment (aircraft, ships, railroad equipment).....	.38	.49	28	.50	.44	.42
Fabricated metals and instruments.....	.90	1.07	19	1.03	1.06	1.07
Chemicals.....	0.68	0.75	10	0.68	0.67	0.68
Paper and pulp.....	.22	.29	30	.30	.32	.32
Rubber.....	.51	.69	16	.56	.55	.58
Stone, clay, and glass.....	1.88	1.86	-1	1.92	2.00	2.12
Petroleum and coal products.....	2.76	3.09	12	3.09	3.34	3.34
Food and beverages.....	.98	1.11	13	.98	1.00	.99
Textiles.....	.50	.56	12	.48	.49	.49
Miscellaneous manufacturing.....	1.19	1.33	12	1.19	1.13	1.15
All manufacturing ²	13.67	15.41	13	14.89	15.15	15.03

¹ U.S. Department of Commerce, Securities and Exchange Commission.

² Petrochemicals, included under chemicals and petroleum and coal products, is counted only once in the total.

HUGE AMERICAN PLANT EXPANSION IN PAST 10 YEARS

Mr. PROXMIRE. In addition, McGraw-Hill has published an excellent table showing the increase in investment in plant and equipment as an index of industrial capacity. It shows how manufacturers are expanding and have been expanding since 1950. It shows that for all manufacturing in this country we have expanded our plant and equipment by 89 percent. In other words, taking

December 1950 as 100, it has gone up to 189. Transportation equipment has gone up to 288. Machinery has gone up to 203 percent; nonferrous metals 207; chemicals 230. It is a perfectly phenomenal increase.

As I point out, the increase in the coming 3 years will break all records. Yet the argument made by the Treasury is that the tax cut we need is not for the hard-pressed average taxpayer who could use

the money very readily, but for business firms which say they do not want it and cannot use it. The evidence shows overwhelmingly that they do not need it.

I ask unanimous consent that the table showing how manufacturers are expanding capacity be printed at this point in the RECORD.

There being no objection, the table was ordered to be printed in the RECORD, as follows:

How manufacturers are expanding capacity¹

[Index of Industrial Capacity (December 1950= 100)]

Industry	1960	1961	Planned		Percent increase			Industry	1960	1961	Planned		Percent increase		
			1962	1965	1960-61	1961-62	1962-65				1962	1965	1960-61	1961-62	1962-65
Iron and steel.....	145	146	150	159	1	3	6	Chemicals.....	207	219	230	253	6	5	10
Nonferrous metals.....	195	203	207	215	4	2	4	Paper and pulp.....	172	181	186	205	5	3	10
Machinery.....	191	195	203	227	2	4	12	Rubber.....	165	172	182	204	4	6	13
Electrical machinery.....	225	234	241	265	4	3	10	Stone, clay and glass.....	166	171	176	185	3	3	5
Autos, trucks, and parts.....	174	177	181	199	2	2	10	Petroleum and coal products.....	147	147	148	149	0	1	1
Transportation equipment (aircraft, ships, railroad equipment).....	267	272	288	311	2	6	8	Food and beverages.....	147	151	159	173	3	5	9
Fabricated metals and instruments.....	171	178	190	217	4	7	14	Textiles.....	122	126	132	148	3	5	12
								Miscellaneous manufacturing.....	157	165	173	194	5	5	12
								All manufacturing.....	177	182	189	208	3	4	10

NOTE.—All data as of end of year.

¹ Weighted by 1957 value added weights used by Federal Reserve Board in its calculation of the industrial production index.

PLANT MODERNIZATION WILL GET HEAVY EMPHASIS

Mr. PROXMIRE. In addition, there is a table showing more modernization and less expansion. That is on the point which, as I will show, Secretary Dillon hit so hard in his testimony. The table shows that in 1961 the actual expansion for all manufacturing—the actual increase, I should say, in replacement through modernization—was 68 percent, whereas expansions was only 32 percent.

For example, with respect to steel, replacement and modernization was 84 percent and expansion only 16 percent. In 1962 those companies plan to have even more rapid modernization and a greater emphasis on modernization. It will be 70 percent instead of 68 percent, with only 30 percent for expansion.

The table shows that during the years 1963 to 1965 the expectation is the overwhelming emphasis that will continue

to be placed on modernization and provisions for greater efficiency. That is the pattern. That is what will be done. Those are the plans. That is the full expectation.

I ask unanimous consent that the table on more modernization and less expansion be printed at this point in the RECORD.

There being no objection, the table was ordered to be printed in the RECORD, as follows:

Industry	1961 actual		1962 planned		1963-65 planned	
	Percent of capital spending for—					
	Expan- sion	Replace- ment and modern- ization	Expan- sion	Replace- ment and modern- ization	Expan- sion	Replace- ment and modern- ization
Iron and steel.....	16	84	18	82	31	69
Nonferrous metals.....	33	67	35	65	43	57
Machinery.....	30	70	24	76	30	70
Electrical machinery.....	48	52	42	58	35	65
Autos, trucks and parts.....	10	90	7	93	16	84
Transportation equipment (aircraft, ships, railroad equipment).....	38	62	35	65	37	63
Fabricated metals and in- struments.....	51	49	57	43	48	52
Chemicals.....	57	43	53	47	53	47

Industry	1961 actual		1962 planned		1963-65 planned	
	Percent of capital spending for—					
	Expan- sion	Replace- ment and modern- ization	Expan- sion	Replace- ment and modern- ization	Expan- sion	Replace- ment and modern- ization
Paper and pulp.....	29	71	31	69	29	71
Rubber.....	57	43	39	61	43	57
Stone, clay, and glass.....	47	53	44	56	49	51
Petroleum and coal prod- ucts.....	9	91	5	95	10	90
Food and beverages.....	35	65	30	70	39	61
Textiles.....	32	68	38	62	36	64
Miscellaneous manufactur- ing.....	39	61	47	53	39	61
All manufacturing.....	32	68	30	70	32	68

Mr. PROXMIRE. Mr. President, I ask unanimous consent that a very excellent explanation—I wish I had more time, I would go into it in more detail—of those two tables, one entitled "Capacity and Operating Rates" and the other entitled "Expansion Versus Modernization," be printed at this point in the RECORD.

There being no objection, the explanation was ordered to be printed in the RECORD, as follows:

CAPACITY AND OPERATING RATES

Continuing a trend which began in 1958, manufacturers are emphasizing modernization rather than expansion of capacity. They plan to add 4 percent to capacity this year and another 10 percent between the end of 1962 and 1965. One reason for the slow rate of capacity expansion is that, although some industries were operating at or close to their preferred rates at year-end 1961, a majority were not. But the operating rates have moved up since last fall. Manufacturers on the average were operating

83 percent of their capacity at the end of 1961, compared with 81 percent last September. For many companies, 83 percent is still considerably below the preferred rate. Only the petroleum industry was operating at its preferred rate, and this was due in part to seasonal factors. Hence, manufacturers as a whole plan to add modestly to capacity over the next 4 years.

However, a comparison of individual industries shows some striking differences. The steel industry's operating rate has shown greatest improvement since last fall—

from 74 percent to 83 percent of capacity, indicating considerable improvement in the general economy.

Not all industries, however, were benefiting from the economic recovery underway at year end. The stone, clay, and glass industry, for example, was operating at a lower level in December than in September. But, for the most part, this industry is geared to the construction industry, which declined at year end for many reasons, including unseasonably bad weather. The fabricated metals and instruments industry was also operating at a lower level of capacity in December than in September.

However, all industries except transportation equipment were operating well above the December 1960 levels, when the economy was still deep in a recession.

Without exception, every industry now indicates a lower preferred operating rate than it did 2 years ago. Manufacturing as a whole now indicates it prefers to operate at 90 percent of capacity, compared with the 94 percent rate of 2 years ago. One possible explanation for the lower rate is that, having devoted approximately two-thirds of their investment to modernization over the past 4 years, companies can now operate at a lower level of capacity at lower cost and greater efficiency. Companies may have come to accept a lower operating rate as typical of a highly competitive economy.

EXPANSION VERSUS MODERNIZATION

Perhaps one of the most striking findings of this survey is that once again manufacturing firms plan to devote 70 percent of their investment to replacement and modernization. That is roughly the same proportion they have devoted to such purposes every year since 1958. Of the \$53 billion spent by manufacturing firms between 1958 and 1961, more than \$34 billion has been invested in replacement and modernization. Manufacturers plan to continue this program through 1965. They now have plans to devote 68 percent of their 1963-65 expenditures to this purpose.

Of course, not all industries indicate such a high proportion for modernization. For example, in 1962 both the fabricated metals and instruments companies and the chemical companies plan to devote more than half of their investment to expansion. The chemical firms' expansion will persist through 1965. At the other extreme is the petroleum industry, which indicates that 95 percent of this year's investment will be for modernization, and 90 percent between 1963-65.

What has been the impact of all this modernization on our total stock of plant and equipment? It has served to reduce substantially the amount of antiquated facilities being maintained by U.S. industry.

In August 1958, the Department of Economics conducted a special survey to determine the modernization needs of U.S. industry. In that survey, manufacturers re-

vealed that 48 percent of all plant and equipment in operation had been installed prior to World War II. Another 19 percent had been installed between the end of World War II and the beginning of the Korean conflict, so that only 33 percent of all manufacturers' producing facilities could reasonably be considered modern.

Mr. PROXMIRE. I ask unanimous consent to have the table entitled "Planned Spending by Regions" printed in the RECORD at this point.

There being no objection, the table was ordered to be printed in the RECORD, as follows:

Planned capital spending by regions, percent of expenditures

Industry	New England ¹		Middle Atlantic ²		South Atlantic ³		North Central ⁴		South ⁵		West ⁶	
	1962	1963	1962	1963	1962	1963	1962	1963	1962	1963	1962	1963
Iron and steel.....	1	1	39	38	8	(7)	34	40	18	20	(7)	1
Nonferrous metals.....	8	5	13	7	16	19	23	40	21	19	19	10
Machinery.....	10	9	24	25	5	3	43	52	9	4	9	7
Electrical machinery.....	11	8	36	35	9	11	41	40	3	2	11	4
Autos, trucks, and parts.....	(7)	3	9	6	2	2	75	80	3	2	11	7
Transportation equipment (aircraft, ships, railroad equipment).....	14	17	5	5	9	7	14	12	1	1	57	58
Fabricated metals and instruments.....	16	14	15	16	5	4	39	38	12	13	13	15
Chemicals.....	3	2	19	16	23	19	23	27	25	24	7	12
Paper and pulp.....	17	12	7	6	22	27	19	19	13	18	22	18
Rubber.....	1	2	4	5	20	7	34	41	20	36	21	9
Stone, clay, and glass.....	1	1	19	16	9	13	41	41	22	20	8	9
Petroleum refining.....	(7)	(7)	31	33	(7)	(7)	23	24	38	43	(7)	16
Food and beverages.....	1	2	10	8	13	6	33	37	24	31	19	3
Textiles.....	7	9	17	19	57	53	4	4	12	12	3	3
Miscellaneous manufacturing.....	6	5	34	25	8	10	19	24	21	19	12	14
All manufacturing.....	5	5	23	22	10	9	31	34	20	21	11	9

¹ New England: Maine, Vermont, New Hampshire, Connecticut, Rhode Island, and Massachusetts.

² Middle Atlantic: New York, New Jersey, and Pennsylvania.

³ South Atlantic: Delaware, Maryland, Virginia, West Virginia, North Carolina, Georgia, Florida, Washington, D.C., and South Carolina.

⁴ North Central: Ohio, Michigan, Indiana, Illinois, Wisconsin, Minnesota, Iowa, Missouri, North Dakota, South Dakota, Nebraska, and Kansas.

⁵ South: Texas, Oklahoma, Arkansas, Louisiana, Kentucky, Tennessee, Mississippi, and Alabama.

⁶ West: Washington, Oregon, California, Montana, Idaho, Wyoming, Nevada, Colorado, Utah, Arizona, and New Mexico.

⁷ Less than 0.5 percent.

WHY EXPAND CAPACITY WITH SO MUCH IDLE?

Mr. PROXMIRE. Mr. President, the great difficulty in adopting an investment credit at this time is the fact that we are operating well below either the preferred rate or the maximum rate of capacity utilization.

McGraw-Hill has made a very careful survey, probably the best and most authoritative and scholarly survey anyone has made. It says, for example, that steel in 1961 was operating at 83 percent of capacity. Now it is far below that. The nonferrous metals industry was operating at 79 percent of capacity. Transportation equipment was operating at 71 percent of capacity, and so on. When our industries are operating far short of capacity, we could give a 50-percent investment credit, and we could even abolish the corporation income tax, and there would be no incentive whatever for a firm to invest more in plant for the

purpose of increasing its capacity. Why in the world should a plant increase its capacity when it is operating as far below as some of these firms are, and that being true of every industry with one exception, the paper and pulp industry? I will cite the argument made by the paper and pulp industry against the investment credit. This is the one industry that could use it. The factual evidence, however, is very clear that in the case of these industries which are operating well below capacity, they will not invest in additional equipment for the purpose of increasing capacity. They are doing it at a record rate for modernization.

I ask unanimous consent to have printed in the RECORD at this point a table headed "Capacity—Rates of Operation."

There being no objection, the table was ordered to be printed in the RECORD, as follows:

Capacity—Rates of operation

[Percent]

Industry	Actual operating rate								Preferred rate 1961	Industry	Actual operating rate								Preferred rate 1961
	1954	1955	1956	1957	1958	1959	1960	1961			1954	1955	1956	1957	1958	1959	1960	1961	
Iron and steel.....	81	98	98	68	73	96	50	83	91	Chemicals.....	79	90	83	81	80	82	75	79	91
Nonferrous metals.....	87	95	92	74	77	77	72	79	90	Paper and pulp.....	97	100	96	88	87	91	88	90	95
Machinery.....	72	87	85	76	70	76	70	75	87	Rubber.....	93	91	88	80	78	84	76	93	81
Electrical machinery.....	92	98	87	76	80	79	74	79	91	Stone, clay, and glass.....	87	94	90	74	79	78	70	71	81
Autos, trucks, and parts.....	95	96	(1)	76	78	88	80	86	91	Petroleum and coal products.....	90	96	96	90	87	86	81	90	90
Transportation equipment (aircraft, ships, railroad equipment).....	69	74	80	74	70	75	71	71	87	Food and beverages.....	82	88	80	80	82	83	81	82	86
Fabricated metals and instruments.....	81	94	83	80	80	84	76	76	83	Textiles.....	88	93	90	80	87	92	82	91	94
										Miscellaneous manufacturing.....	(1)	(1)	85	80	84	89	83	89	93
										All manufacturing.....	84	92	86	78	80	85	77	83	90

¹ Not available.

NOTE.—All rates as of end of year.

BUSINESS EXPECTS MORE CASH EARNINGS THIS YEAR—EVEN WITHOUT GOVERNMENT HELP

There is one other section in the McGraw-Hill report that I should like to deal with. It shows that business firms as a whole appear to be in a stronger financial position this year than last. The report goes on to say that they expect their cash flow—retained earnings plus depreciation allowances—to be 14 percent, compared with the 9-percent increase they expected last year. The report continues:

Businessmen as a whole expect that their demands for external financing will increase only 1 percent, while manufacturing firms expect no increase in their demands for external funds. Thus it would appear that business as a whole may rely almost entirely on its own resources to finance its spending programs this year.

Companies were asked how much they expect their demand for external financing for whatever purpose to increase or decrease between 1961 and 1962. Companies go into the financial markets for funds for many other purposes besides financing capital equipment, but, taken as a whole, their response to this question would indicate they do not anticipate exerting much pressure on the financial markets.

Mr. President, that is a masterpiece of understatement.

Since we have excellent capital markets—the best in the world—why do we need to have investment credit to provide another \$1.3 billion? It is apparent to me that it is wholly unnecessary.

To summarize my conclusion on the McGraw-Hill survey, I should like to say that this finding, that only 1 percent would be the increase in investment in equipment as a result of the investment credit—that is, that it would add \$300 million to the outlays as now planned—strongly suggests that the investment credit would be ineffectual in stimulating investment. This is especially true since the Treasury has placed great hope in the short-run stimulation in the immediate future.

This is the particular point I stressed. The Secretary of the Treasury, when I cited this McGraw-Hill finding, in the hearings before the Joint Economic Committee, said, "This is the first year. This is the first reaction." He said that after businessmen get used to the investment credit they will not increase by only 1 percent, but by a great deal more, and that it will act as an important stimulant in the future.

FIRST YEAR REACTION TO INVESTMENT CREDIT CRUCIAL

I should say exactly the opposite. All experience with such stimulations suggests that my conclusion is right and the Secretary's conclusion is wrong. The real impact is in the first year. If it is not felt in that first year, it is never felt. That was true certainly in the case of the depreciation in the 1954 Revenue Act. That came in 1955. Since then it has declined. The stimulus works up and then there is a decline, not an increase.

Another interesting aspect of the McGraw-Hill survey deals with selected industries and the percentage increase in investment which these industries thought they would make as a result of the credit.

The iron and steel industry is pressing hard for the investment credit. But the percent increase that they said the investment credit would increase their investment would be zero. In the non-ferrous metals it would be 1 percent. In electrical machinery, it would be 1 percent. In autos, trucks, and parts, it would be zero.

For transportation and equipment, it would be zero; for fabricated metals and instruments, zero; chemicals, zero; petroleum and coal products, zero; miscellaneous manufacturing, 1 percent; mining, 1 percent; railroads, 1 percent; other transportation and communications, zero.

These people say there will be no increase in investment in plant and equipment the first year because of the investment credit. None at all, Mr. President. If they do not have it in the first year, they will never have it.

CREDIT DESIGNED TO ACCOMMODATE NO INCREASE IN INVESTMENT

One of the principal reasons why the investment credit was modified from its original form providing for 15-percent credit for additional investment—not for all, but additional increment and increase over the last year—and that was knocked out and, instead, 7 percent was provided on all investment—was done primarily at the request of the railroads, because they said they could not take advantage of the provision for additional increases in investment, because they are not making any increases in investment.

They are not increasing investment, and they will not, and they confess they will not. Yet we will have a reduction in our Federal revenues by tens of millions of dollars for the benefit of the railroads, and they will do nothing, except to increase their income and increase their dividends, I suppose, but they will do nothing to stimulate the economy, resulting in an increased deficit for the Treasury and more taxes to be paid by the ordinary taxpayer.

The finding made by McGraw-Hill that U.S. business plans to spend more for new producing facilities this year than in any previous year, planning to spend a record amount in 1963–65, certainly does not suggest, as Secretary Dillon has stated, that investment will be a "soft spot" in the economy. This rapid rate of investment is almost completely independent of the proposed tax credit, and it has nothing to do with the proposed tax credit.

M'GRAW-HILL SAYS NO INVESTMENT "SOFT SPOT"

In testifying on the McGraw-Hill survey, Douglas Greenwald, manager of the department of economics, McGraw-Hill Publishing Co., appeared before the Joint Economic Committee and said:

My assignment is to discuss the current and short-run health of the economy with particular reference to the key area of the economy—private investment in new plants and equipment. My contribution, for the most part, will be based on recent important factual information from McGraw-Hill's surveys of business' anticipations. And results of these surveys indicate that capital investment intentions by business constitute an element of strength in the business outlook.

I emphasize: The McGraw-Hill expert said:

Surveys indicate that capital investment intentions by business constitute an element of strength in the business outlook—

Not as Secretary Dillon said, a "soft spot." There is strength in the business outlook, according to McGraw-Hill, which is recognized as an authoritative surveyor of the economy.

Mr. Greenwald continued:

In my department of the McGraw-Hill Publishing Co. we have made surveys of plans for business' spending on new facilities for 15 years. We also maintain a monthly index of new orders for non-electrical machinery which reflects the new incoming business of producers of capital equipment, and a quarterly forecast index of machinery orders, which reflects the producers' expectations for four quarters ahead. The indexes cover a relatively small number of large manufacturers of machinery.

We generally survey business on its plans for domestic investment twice a year—in the spring and in the fall. The spring survey is very comprehensive and is geared to longer-range plans; the fall survey covers fewer questions and is geared to short-range plans.

In October 1961 we carried out our fall survey of business' plans for 1962 and 1963. Our comprehensive survey of business' plans for 1962 to 1965 was made during March and early April of this year. At the end of June we carried out a special checkup of plans.

The McGraw-Hill checkup of spending plans showed that business, in general, is planning to invest approximately the same amount in new plants and equipment in 1962 that it reported to us in our comprehensive survey taken earlier this year, and a considerably higher amount than it anticipated last fall.

This survey was made as up to date as possible. It was made as of only a few weeks ago and was brought up to date for June.

Mr. Greenwald continued:

Our fall 1961 survey indicated that business had plans to invest \$35.84 billion in 1962, an increase of about 4 percent over 1961. Over the past several years our fall surveys of business' plans have always provided the correct direction of change in investment as well as fairly reliable indications of the degree of change.

The McGraw-Hill comprehensive survey of business' plans for new plants and equipment taken early this spring indicated that business firms had raised their investment sights significantly from the fall. Planned investment for 1962 was \$37.98 billion, up 10.5 percent over 1961.

So the later survey, in April, showed a very substantial increase, and the record spending that is now taking place for plant and equipment has reached an estimated \$38 billion for 1962, the highest in the history of the country.

Mr. Greenwald continued:

During the years that we have been making these spring surveys, they have proved remarkably accurate in indicating the trend of overall investment for the year ahead, except in 1950, when all plans were altered by the Korean war. During the last decade, the average error between the McGraw-Hill survey's planned percentage change and the Department of Commerce's percentage change for actual data is only 3.5 percent.

We do not conclude from this experience, however, that we have a sure-fire forecasting device. We claim nothing for the results of our surveys except that they report present plans. We heavily emphasize the proposi-

tion that our surveys are not promises of what is actually going to happen.

Our special checkup in late June showed that business planned to spend \$37.96 billion on new plants and equipment this year, up 10.4 percent over 1961.

That was according to the recheck taken in June, before the stock market prices began to recover. I continue:

This checkup was based on plans of a substantial cross-section of business, accounting for 35 percent of total capital investment. For the most part the results reflect the plans of large companies. This recheck provided no indication of what small companies were doing about their investment. To begin with, investment plans of small companies were not up as much for 1962 as those of larger companies.

The downward movement of the stock market in May and June may have had some impact on their investment plans. However, small companies account for a relatively small percentage of total capital investment.

Our checkup pointed up the fact that business in general had not cut back or canceled plans for investment in new facilities in 1962 as a result of the sharp drop in stock prices in May and June or the so-called loss of business confidence.

Manufacturing industries overall planned to invest \$15.3 billion this year, down about \$110 million from plans reported to us in the spring. Steel, machinery, electrical machinery, stone, clay and glass and miscellaneous manufacturing industries plan to invest less in 1962 than they did earlier. However, transportation equipment—aircraft, railroads and shipbuilding—fabricated metal products and instruments, chemicals, rubber and food industries plan to increase their capital expenditures this year more than planned originally.

Among manufacturing industries, railroads and utilities planned slightly higher capital investment for 1962 than they did earlier, while the mining industry cut its plans.

About 80 percent of the companies that answered in our recheck indicated they had made no change in their 1962 plans for new plants and equipment. The remaining 20 percent indicated some changes in their planning. But this group was split right down the middle, with half increasing plans and half cutting them.

Among the companies indicating investment cutbacks, only a very few cited economic conditions as the reason. In most cases where investment plans were lower than they were earlier, the reasons given had absolutely nothing to do with a lack of business confidence or the drop in the stock market. Instead, technological delays and construction delays were the reasons given.

We should point out that in past years of high and rising business activity a large number of companies increased investment plans during the year. This has not been the case so far in 1962.

This recheck of McGraw-Hill survey was taken before stock market prices began to recover, before margin requirements were reduced from 70 percent to 50 percent and before Revenue Procedure 62-21, with its more realistic depreciation guidelines regarding lives of machinery and equipment, became effective. It is conceivable that these three factors, along with the 7-percent tax credit for new machinery and equipment purchases, which Congress may soon make a part of the Nation's law, could result in higher capital expenditures at the end of this year than are now anticipated by companies and by business economists in general.

However, it is my opinion that their impact on capital spending may be slow in coming. We have some factual evidence on this point.

MCGRAW-HILL ESTIMATES CAUTIOUS

I think it is interesting to note that McGraw-Hill suggests that a 7 percent tax credit would not be effective and would result, at best, in only a 1 percent increase in credit. Other factors, such as improved stock prices, and general restoration of confidence in the economy should improve the plans of businessmen from what they were in June, which would seem to have been about as gloomy a month as we have had in a long time. This should emphasize that all the figures I have given show that a good outlook for business investment in plant and equipment are conservative and are based on a survey made at the time when businessmen, if ever, were probably cautious, prudent, and even pessimistic about the future.

Therefore, a survey taken in August, on the basis of the facts which I have listed here, on the basis of general improvement in conditions, would suggest that the estimates would probably be increased, and there would be an even greater increase in business investment in plant and equipment.

Mr. Greenwald continued:

In our spring survey, we asked the question, "If the administration's program of tax incentives for investment were enacted, how much would this increase your capital expenditures in 1962?"

That was a crucial question. I shall repeat it, because it is so important to the argument I am making:

If the administration's program of tax incentives for investment were enacted, how much would this increase your capital expenditures in 1962?

Business as a whole indicated that it would raise its 1962 plans by only 1 percent, or about \$300 million. Nine out of every 10 companies replying indicated that they would not use such a program at all in 1962.

The fact that American business is going ahead with its investment plans for 1962 was not a surprise to us. It confirmed our belief that business' plans for new plants and equipment, once made for the year ahead, are generally carried out. In the past, wars, recessions and booms have led to significant changes in investment plans. But in my view we are not likely to be in any of these three situations this year.

Also, it makes good sense for businessmen to go right ahead with their modernization programs in 1962. Business firms reported to us in our recent checkup that this year's capital investment programs are stressing modernization, with the hope that these cost-cutting projects will result in better profit margins.

"MODERNIZATION" A TWO-EDGED SWORD

Incidentally, modernization means, of course, generally, stress on automation; stress on automation means that this kind of investment, while highly beneficial in terms of improving plant efficiency and while it will improve, unquestionably the standard of living of the American people, will probably have an adverse effect on employment. It is much more likely to increase unemployment, certainly in the short run, than to reduce unemployment. From this standpoint, it seems to me, once again, that investment credit, to the extent it has any effect at all—and I would certainly question that it has any effect—would seem to contribute to the one particular economic problem that faces

America, the problem of unemployment, the problem of men out of work, the problem of heads of families not having jobs so that they can support the families. This would result in personal tragedy and also have a very serious effect on communities, localities, and States undertaking to provide additional relief, and so forth. I continue reading:

In our earlier survey this year, manufacturers reported that they planned to devote 70 percent of their 1962 investment dollar to modernization. The reason for their concern is obvious. About 40 percent of U.S. plant and equipment dates back to before 1951, and nearly 25 percent goes back to World War II or even before that. These significant statistics were also revealed by our spring survey.

Only a very small percentage of investment is going for new capacity this year. Most of this is going for capacity for new products which are an important part of the payoff of industry's tremendous expenditures on research and development during the last decade. Little investment is going for additional capacity for existing products.

As I pointed out, they prefer to operate at 90 percent of capacity, but they are well below it. This is another reason, of course, why the proposed investment credit is likely to be ineffectual.

I have one other reference to make to testimony, given by Mr. Greenwald, before I finish discussing the McGraw-Hill survey. He stated:

Corporations now have a high enough rate of cash flow to finance a considerably higher level of investment than is now planned for 1962.

Mr. President, this is a point which I think we have clearly established, if we have established nothing else this afternoon.

I read further from the testimony of Mr. Greenwald:

Our comprehensive survey taken early this year showed that businessmen anticipated increasing their volume of cash flow, composed of retained earnings and depreciation, at a faster rate than their investment in new plants and equipment. At that time they expected to increase cash flow by 14 percent and investment by only 10.5 percent.

Once again, Mr. President, does that make any sense, when we know that business is increasing its cash earnings—that is, its depreciation reserves plus its earnings after taxes—more rapidly than it is increasing its investment in plant and equipment? Under these circumstances, why in the world, should we provide a \$1 billion tax cut, in order to give business additional cash earnings, when business is not using what it now has, and is not beginning to tap our capital markets.

Mr. Greenwald then said:

It is my belief that the McGraw-Hill data on plant and equipment expenditures indicate that this key segment of the economy will continue to expand this year. If plans hold up for the year as a whole, then the quarterly rate of capital expenditures may be expected to reach \$39 billion in the fourth quarter, compared with a rate of about \$37 billion in the second quarter.

EUROPEAN SITUATION NOT APPLICABLE

There is one more reference which has to do with McGraw-Hill, although it is on a slightly different point. It is con-

stantly argued that we have to compete with European firms. We can answer that argument on several levels. But when Mr. Greenwald was asked about it and when he was asked whether their gross national product is expanding more rapidly and whether their plant is more efficient, he had this to say:

If you have a high rate of growth in terms of investment relative to GNP, you grow faster. I think this is fine in many areas of the world, but I don't think this applies to us any more. I think we have a great record of growth in the past and we are the richest nation in the world.

Mr. Katona, an eminent professor of economics at the University of Michigan, had this to say on the same subject:

I have just come from a study of the Common Market countries, it is very true that in the first 10 years after World War II, which is roughly 1947 to 1957 because of the previous desolation, they have spent very much more on business investment than we. The trend is downward. The new impetus in the Common Market countries comes from consumers, enormous increase in instalment credit and automobiles, consumer housing, and consumer equipment. On the whole, the Common Market countries are Americanizing rapidly and that will show up in lesser business investments, more resembling our rates, and more consumer tangible investment expenditures as well. So if you look at the trend which foreshadows the future rather than the past facts will, I believe, diminish.

I have been reading from McGraw-Hill and from the kind of distilled statistics which come from its surveys and its studies in the past.

At this point I should like to refer to the statements made by a group of very competent business executives—a group of experts in the paper industry—Henry P. Baldwin, vice president, Consolidated Water Power & Paper Co.; Alexander Calder Jr., president, Union Bag-Camp Paper Corp.; William H. Chisholm, president, Oxford Paper Co.; J. E. Cowles, treasurer, St. Regis Paper Co.; William A. Hanway, secretary, International Paper Co.; William R. Haselton, vice president, general manager, Tacoma area, St. Regis Paper Co.; Harold Holden, president, Gilman Paper Co.; J. B. Lockhart Jr., vice president and controller, Riegel Paper Corp.; Guy E. McCorison, board chairman, Thilmay Pulp & Paper Co.; and A. G. Paine, president, New York & Pennsylvania Co., Inc.

They were asked:

Question. What is your opinion of the Kennedy administration incentive proposal to let business subtract from its taxes 7 or 8 percent of what it spends on new installations or more up-to-date equipment?

Here is the reply:

Consensus. Almost to a man, each member of the panel opposed this proposal, and most of them were vehement in their reaction.

Mr. President, why do they do that? Why in the world do those businessmen oppose a tax credit which would put money in the pockets of their firms and would enable them to have higher dividends and would put them in a better cash position and would increase their income after taxes?

Here is one of the answers:

I don't feel the Government has a right to levy selective taxes or show favoritism to people who work along the lines they [the Government leaders] want. While the right to tax implies the right to destroy, it should never imply the right to dictate what should be done, as this does.

The next one said:

Wonderful, isn't it. After we have gone through a multimillion-dollar expansion and there already is overcapacity. Someone who will jump through the hoop gets it, but we don't benefit after all we have spent. This is favoritism.

The next one said:

A shoddy solution. A sort of a one-shot patch. Sort of a forgiveness, but not really changing the unfair depreciation rate. Probably OK to get textiles out of a hole.

The next one answered:

This is not a proper amendment to the tax law. Incentive is not a proper part of the tax law. Only valuable to some small companies. We are told we have reached our expansion capacity. So what? A new company gets more out of this. The 7 or 8 percent would not be meaningful. The controllers' association is against investment credit incentives.

The next one answered:

An arbitrary credit designed to compensate for something wrong with the overall tax structure—the unrealistic depreciation policy. The 7 or 8 percent could easily be changed and therefore, even if it were a good solution, it would not necessarily be a permanent one. What's needed is a fair and realistic policy for years to come.

The next one answered:

Another gimmick. Won't solve the basic problem. Qualifications accompanying this gimmick are unrealistic—a common result of most gimmicks. Will not stimulate greater investment in the heavy goods industries, where unemployment is greatest. I fear it will delay further action on the basic problem.

Another one answered:

Harmful in the long run to the general economy. Basically, tax policy should follow sound business policy. Any reduction in taxes should be made through the basic tax rate. We take this position even though our company might benefit during the first year under the proposed law.

The next one answered:

The allowance of accelerated depreciation in 1954 was to an extent more logical than the proposed credit, in that it tended to compensate for unduly long lives imposed on some corporate taxpayers by Bulletin F of the Internal Revenue Service. Here again we believe a better approach is to follow sound business policies throughout the tax law and to reduce tax rates commensurately. We see no sound reason for writing off an extra amount of an asset in the first year of its useful.

The final one answered:

I say, also, it is a gimmick. Nearly every industry already has too much production. Why ask them to increase capacity when they can't sell it?

Mr. President, these are hardheaded, tough-minded businessmen—businessmen who make the decisions on plant and equipment. This is their reaction; and it is typical of the position taken by the Chamber of Commerce of the

United States, by the Junior Chamber of Commerce, by the National Association of Manufacturers, and by a number of industry groups. They are uniformly agreed that this will not work and that they do not like it.

So why on earth should we insist on forcing on them a tax cut which they do not want, when there are so many in America who would like to have a tax cut if they could get it, and when there are many who would like to have investments in their particular area—for instance, in the public utilities—increased.

Mr. President, it is argued that, somehow, we must put ourselves on a basis of competitive equality with European business and also on a basis of taxation equality with European business.

Together with the distinguished junior Senator from Tennessee [Mr. Gore], I completely and thoroughly disassociate myself from that view. I think it is a really "phony" argument. It is the argument which those of us who served in State legislatures used to hear, and it is the same argument which I used to hear when I was Democratic nominee for Governor of Wisconsin. At that time it was argued that Wisconsin had to have what Illinois had. Wisconsin had an income tax, but no sales tax, whereas Illinois had a sales tax but no income tax. So it was argued that Wisconsin should do away with its income tax, and should institute a sales tax.

Wisconsin did not lose industry overall, although Wisconsin had an income tax, progressive taxation, one of the most progressive tax systems in the country, and Michigan which had no income tax and a sales tax did lose industry by the bushel basket. It did not work in the States. If it were to work anywhere, it would work there, where interstate industry competition and trade is so much more dominant than it is between nations. But we are getting the same old argument with relation to our tax structure at home and tax structure abroad.

The Secretary of the Treasury, when he was asked what countries had investment credit, said only Belgium, Holland, and the United Kingdom. There is no question that we can compete with the United Kingdom effectively. Incidentally, that is the only country whose gross national product has been growing at a slower rate than ours, and it has a big investment credit. As far as Belgium and Holland are concerned, it is ridiculous and fantastic to compare the productivity of the United States of America with a country the size of Belgium or Holland. If one were to compare it with that of Germany or France, there would be some basis of comparison, but not very much more.

In view of the fact that our entire foreign trade amounts to less than 5 percent of our gross national product, to base our tax system—and that is what the argument has been on this question—on what our competition is going to be with Belgium, Holland, England, France, and Germany is ridiculous.

An article on page 52 of the August 25, 1962, issue of Business Week, which is

the most recent issue, shows that the tax burden in the United States, as a percentage of gross national product, is in the middle of a list of nations. It is interesting to note that while in this country it is higher than in Spain, Switzerland, Portugal, Japan, Greece, Australia, Ireland, Belgium, Canada, and Denmark, it is lower than it is in Great Britain, the Netherlands, Italy, Sweden, Luxembourg, Norway, Finland, Austria, France, and West Germany.

The highest burden is in the country that is growing the fastest, West Germany, the country that is always held up as a model of progressive free enterprise capitalism. There the percentage of National, State, and local taxes in 1959 to gross national products was 34 percent. In this country it was 26.7 percent, far, far less.

I wish to quote from page 52 of that article in *Business Week*:

If you're rich, you might be able to hold onto more of your wealth under European income tax treatment than under the U.S. system. But if you're making under \$50,000 or so and trying to become a capitalist, you doubtless have a better chance of doing it in the United States than in most European countries. Economically, this situation may make Europe more favorable to development of venture capital, but it also may be the reason the United States gets a much greater flow of funds from middle-income earners into the capital markets.

In other words, our system makes the man who has a good income, but not a great income, not in excess of \$50,000, far better off than he is in Europe.

I continue to read from the article:

Apart from the income tax, European governments also tend to favor the man with money by a heavy reliance on indirect taxes such as those on retail sales. This shifts much of the tax burden onto middle- and low-income groups who spend relatively more of their income. In some countries, particularly France and Italy, it offsets the relatively lighter taxation of personal and corporate income.

For the economy as a whole, the sizable indirect taxes sometimes are rejiggered to encourage or discourage consumer spending. But a high level of indirect taxes weakens the automatic stabilization effect of government budgets, by which a business upswing brings in more revenue—tending to balance the economic cycle. A weaker stabilizer may be good in a recovery, since America's high tax rates tend to choke off a recovery too early. But in a downturn, a weak stabilizer is not desirable.

In other words, we not only have a lesser tax burden on the overwhelming majority of our citizens, but we also have a far sounder tax system from an economic standpoint, a tax system which is much more stable. It tends to prevent expansion from proceeding quite as rapidly, and, at the same time, it tends to prevent inflation. As *Business Week* points out, our tax system prevents a downturn from accelerating, and prevents a recession from getting very bad.

This article also discusses something to which I have already adverted:

Ancient rule forgotten. Some 2,000 years ago a Hindu law book known as the Code of

Manu laid down an oft-repeated rule of thumb on tax burdens: "A king who in times of distress taxes even the fourth part of the crops is free from guilt if he protects his subjects to the best of his ability."

That is the notion that if more than one-quarter of income is taken in taxes something may be amiss.

I continue to read:

This is indicated by the chart on this page, which shows the share of GNP taken by total tax collections—Federal, State, and local, including social security charges—in 21 nations. Starting with the U.S. at 26 percent and running up to West Germany's 34 percent, nearly all the Western industrialized nations exceed the old rule-of-thumb limit.

But, so far as the Western industrialized nations are concerned, our taxes are less burdensome than most, not more.

I continue to read from the article:

But the way the load is spread is perhaps more important than its size. The pattern of tax collections (national, State, local, and social security) in the table on page 54 indicates some of the variations in structure. Admittedly, this is not a true picture of tax incidence, which would take into account the unknown degree to which various business taxes are shifted to consumers. But collections at least show who foots the bill in the first instance, and perhaps where the intentions of government lie.

Rather surprisingly, U.S. corporations shoulder a smaller share of this Nation's total burden than do—

Let me repeat that:

Rather surprisingly, U.S. corporations shoulder a smaller share of the Nation's total burden than do those in Germany, France, Belgium, and Holland. Britain is the only major European nation in which corporations carry a lighter load than U.S. companies. Most of the countries that place a substantially lighter burden on business are small, like Switzerland, and, ironically, include such Socialist lands as Denmark and Sweden.

I ask unanimous consent that the table showing the tax burden, share of gross

national product taken by National, State, and local taxes, in 1959, the data coming from the United Nations, Yearbook of National Accounts Statistics; United Nations Statistical Yearbook; U.S. Treasury, be printed at this point in the RECORD.

There being no objection, the table was ordered to be printed in the RECORD, as follows:

The tax burden: Share of GNP taken by National, State, and local taxes, 1959

	Percent
West Germany-----	34.0
France-----	33.3
Austria-----	33.1
Finland-----	32.1
Norway-----	31.8
Luxembourg (1958)-----	30.0
Sweden-----	29.7
Italy-----	29.2
Netherlands-----	29.1
Britain-----	28.9
United States-----	26.7
Denmark (estimated)-----	24.5
Canada-----	24.3
Belgium-----	23.1
Ireland-----	22.2
Australia-----	22.0
Greece-----	20.1
Japan-----	19.0
Portugal-----	18.2
Switzerland-----	14.4
Spain (1957)-----	13.4

Data: United Nations, Yearbook of National Accounts Statistics; United Nations Statistical Yearbook; U.S. Treasury.

Mr. PROXMIRE. Mr. President, I also ask unanimous consent to have printed in the RECORD a table showing how the tax burden is spread, country by country, including Sweden, Denmark, the Netherlands, Austria, Britain, West Germany, Belgium, France, Portugal, Spain, Ireland, and the United States.

There being no objection, the table was ordered to be printed in the RECORD, as follows:

How the tax burden is spread—Country by country¹

	Percentage of total tax collections at all levels of government by source, 1958						
	Direct taxes on income, wealth, payroll						Indirect taxes (ex- cise, sales, etc.) on in- dividuals and cor- porations
	Individuals			Corporations			
	Income, wealth taxes	Social security charges	Total	Income, wealth taxes	Social security charges	Total	
Sweden.....	46	7	53	11	3	14	33
Denmark.....	43	5	48	6	-----	6	46
Netherlands.....	31	7	38	10	19	29	33
Austria.....	30	7	37	7	15	22	41
Britain.....	26	7	33	15	6	21	46
West Germany.....	18	15	33	10	14	24	43
Belgium.....	21	9	30	9	19	28	42
France.....	11	6	17	7	23	30	53
Portugal.....	10	8	16	21	15	36	48
Spain.....	10	5	15	17	14	31	54
Ireland.....	12	2	14	9	3	12	74
European average.....	23	7	30	7	11	23	47
United States.....	35	0	41	16	8	24	35

¹ For all countries, 1958 is most recent year of breakdown on social security charges.

NOTE.—Similar breakdown on Italy is not available, but ratio averages 48.5 percent from indirect; 16 percent direct taxes on corporations and individuals; 29 percent in social security charges on business; 6.5 percent in social security charges on individuals.

Data: National Institute Economic Review, Britain.

Mr. PROXMIER. Mr. President, I also ask unanimous consent that the text of the article "How Taxes Compare," from the August 25 issue of *Business Week*, be printed at this point in the RECORD.

There being no objection, the article was ordered to be printed in the RECORD, as follows:

HOW TAXES COMPARE

If you're rich, you might be able to hold onto more of your wealth under European income-tax treatment than under the U.S. system. But if you're making under \$50,000 or so and trying to become a capitalist, you doubtless have a better chance of doing it in the United States than in most European countries. Economically, this situation may make Europe more favorable to development of venture capital, but it also may be the reason the United States gets a much greater flow of funds from middle-income earners into the capital markets.

Apart from the income tax, European governments also tend to favor the man with money by a heavy reliance on indirect taxes, such as those on retail sales. This shifts much of the tax burden onto middle- and low-income groups who spend relatively more of their income. In some countries, particularly France and Italy, it offsets the relatively lighter taxation of personal and corporate income.

For the economy as a whole, the sizable indirect taxes sometimes are rejiggered to encourage or discourage consumer spending. But a high level of indirect taxes weakens the automatic stabilization effect of government budgets, by which a business upswing brings in more revenue—tending to balance the economic cycle. A weaker stabilizer may be good in a recovery, since America's high tax rates tend to choke off a recovery too early. But in a downturn, a weak stabilizer is not desirable.

ANCIENT RULE FORGOTTEN

Some 2,000 years ago, a Hindu lawbook known as the Code of Manu laid down an oft-repeated rule of thumb on tax burdens: "A king who in times of distress taxes even the fourth part of the crops is free from guilt if he protects his subjects to the best of his ability."

By this standard, few mature nations today are free from guilt. This is indicated by the chart on this page, which shows the share of GNP taken by total tax collections—Federal, State, and local, including social security charges—in 21 nations. Starting with the United States at 26 percent and running up to West Germany's 34 percent, nearly all the Western industrialized nations exceed the old rule-of-thumb limit.

DIVIDING THE LOAD

But the way the load spread is perhaps more important than its size. The pattern of tax collections (National, State, local, and social security) in the table on page 54 indicates some of the variations in structure. Admittedly, this is not a true picture of tax incidence, which would take into account the unknown degree to which various business taxes are shifted to consumers. But collections at least show who foots the bill in the first instance, and perhaps where the intentions of governments lie.

Rather surprisingly, U.S. corporations shoulder a smaller share of this Nation's total burden than do those in Germany, France, Belgium, and Holland. Britain is the only major European nation in which corporations carry a lighter load than U.S. companies. Most of the countries that place a substantially lighter burden on business are small, like Switzerland, and ironically, include such Socialist lands as Denmark and Sweden (*Business Week*, July 14, 1962, p. 72).

STEEL STUDY

One industry where this question has been studied is steel. Total taxes as a percent of sales in 1960 for steel companies in several countries were compiled recently by the International Metalworkers at Geneva. For U.S. steel producers, taxes were 7.7 percent of sales; in France, 11.5 percent; in West Germany, 7 percent; in Belgium, 7.3 percent; in Britain, 5.5 percent; and in Sweden, 4.4 percent.

In light of the considerably more favorable treatment of corporate profits taxation—as compared with the United States—it is surprising to find a similar, or heavier, tax burden in Germany, Belgium, and France. This is only one industry, of course, but three farflung U.S. companies in other industries, too, report there's "some doubt" that the total burden on their several European subsidiaries is much different from the burden on their U.S. companies.

But even if the load, company for company, is about the same, the form taken by these other taxes can have different effects.

OFFSETTING FACTOR

Payroll taxes, for one, may largely offset lower income taxes on business in many countries. In France, Germany, Belgium, Holland, and Italy, most of the direct revenue collections from corporations come from social security contributions and other payroll taxes.

French employers pay social security and other compulsory charges, such as housing allowances, averaging 44.5 percent of their payrolls—and sometimes it runs to 50 percent. Italian employers pay an average 47.8 percent of their wage bill in social security. German employers are better off, but still face payroll charges of about 16 percent. In the United States, the average is only 4.5 percent.

Even if wages are lower in Europe than in the United States, these enormous payroll charges are a considerable incentive to modernize plants to minimize labor costs. Britain, whose industry bears a social security burden closer to that of U.S. industry, has been keenly aware of this incentive on the Continent. In fact, Britain enacted a payroll tax last year, partly to discourage adding workers in boom times—which strains an already short labor supply. But trade union opposition to the tax was so strong that it has never been applied—and there's talk of repealing it.

TURNOVER TAX

Indirect taxes, too, offset the lighter profits tax in some countries. This is particularly true of the French production tax—a tax on the value added by a manufacturer. Basically, the "TVA," as it's called, is a turnover tax that is noncumulative—in contrast to a general sales tax whose total effect is multiplied as it is added on at each stage from raw material to retail customer. In effect, the French manufacturer subtracts the value of all his purchases of materials from the value of his own sales and applies the tax to the difference.

For the company that cannot pass it on, it's a sizable tax bite. The current rate is close to 20 percent, but because it is included in a company's sales figures, it is in effect a tax of close to 25 percent. But economists contend that in most cases the TVA is shifted to the buyer in the form of higher prices. Moreover, it is deductible for income-tax purposes, and it's even included in the value of depreciable assets. Thus, its real burden on profits is unknown.

For the French Government, the TVA yields as much, and sometimes more, than both personal and corporate income taxes combined. Partly because of this, and also because of its noncumulative effect, it's being considered for eventual adoption by all

Common Market countries in lieu of other types of indirect taxes.

EVASION PREVENTIVE

The heavy reliance on indirect taxes in France, as well as in Italy and other Latin countries, has developed not so much from the economic merits of this type of tax as from its collectability. Tax evasion is notorious in these nations—and to some extent it must distort the picture of the real burden on business. Corporations are known to keep separate books for the tax collector, and the tax bill is often negotiated. Unincorporated businesses often show no books at all, and taxes are sometimes assessed on the basis of floor space, number of machines, and other indirect signs of financial status.

In personal taxation, too, evasion of income taxes has forced a heavy reliance on indirect taxes. Because of inaccurate reporting by taxpayers, income taxes in France and Italy are often assessed according to the outward signs of wealth. The French taxpayer, for instance, must declare the number of rooms in his house, the number of horsepower in his car, and whether he has a maid, a pet, or a piano. If his income seems out of line with these indexes, it can bring the assessor down on his head.

CONSUMER TAXES

In Britain, the burden of indirect taxation falls on the consumer through the purchase tax, which can go as high as 50 percent on autos and other durables. The Government has the authority to move the rates up or down by 10 percent to aid in leveling off the business cycle. Rates vary widely by commodities, but they average out at about 20 percent across-the-board. A move is under way now to cut top rates and raise the lower rates gradually to bring the purchase tax to a single rate of about 20 percent. This, however, might lessen the influence of changes in the tax on consumer spending.

Business circles in Britain, mainly sparked by the powerful Federation of British Industries, are eying the use of indirect taxation on the Continent, particularly the French system. A recent FBI report suggested that the Government consider shifting some of the burden of business taxation from a direct to an indirect basis.

The export incentive aspect of indirect taxation particularly has perked the ears of Britons. The French for instance, exempt export sales from the sizable TVA. The Germans have a turnover tax, payable on all domestic sales, including intercompany sales, of 4 percent. Because its effect is compounded, the German manufacturer gets a rebate of 6 percent on his export sales, and this may be more than he has actually paid in turnover taxes.

LOCAL LEVIES

Thus, the total tax burden on European industry on the national level counts many taxes whose effect are different from direct income taxation. But other taxes have the same effect. In Sweden, companies pay a deductible local income tax of 14 percent in addition to the 40 percent corporate rate imposed by the National Government. This, in effect, raises the corporate rate to 48 percent. Germany also has a deductible municipal profits tax that goes as high as 15 percent.

In another way, leading European countries favor capital by greatly reducing double taxation on corporate dividends and profits. A stockholder gets a tax credit of 24 percent for dividends in France and 38.75 percent in Britain. In the United States the deduction is only 4 percent.

Germany taxes a corporation on its distributed profits at the rate of 15 percent, compared to the rate of 51 percent on undistributed profits—similar to a system tried in the United States in the late 1930's. Al-

though this is a definite incentive to distribution it doesn't lower the corporate tax burden as much as the difference in rates would suggest. Because local profits taxes and capital assets taxes limit the amount available for distribution, a company ends up with a total direct tax bill of 65 percent even if it distributes 40 percent of those profits that are available for dividends.

UNITED STATES WINNING TRADE COMPETITION

Mr. PROXMIRE. Mr. President, we hear over and over again that we are doing a less than adequate job in competing with other countries in trade.

For this reason, it is said, we suffer an unfortunate balance-of-payments situation. This is not true. I have said this before, and now I am going to document it with figures from the record.

I have before me a U.S. Department of Commerce survey of current business. The table shows that business in the first half of 1962, seasonally adjusted and raised to the annual rate, was the best ever in the history of this Nation. Commercial exports were \$18.1 billion.

If American business is not able to compete, if American plants are inefficient and cannot do an adequate job, how can anyone explain the fact that the United States is doing so well? More is being sold abroad than ever before, and this is exclusive of Government aid financed exports. It does not include military equipment. It does not include foreign aid. It does not include Public Law 480 shipments. It refers only to commercial exports.

Imports also have risen during this period of time, but exports have risen more rapidly. In other words, not only are our exports increasing at a healthy and rapid rate, but also they are increasing more rapidly than imports are increasing. So, on the basis of the only objective facts available, we are doing a better job than ever before.

There is a highly favorable balance of trade. There is no question about it. The favorable balance of trade can be divorced from and separated from the additional advantage we get from our foreign aid program, in addition to our favorable balance of trade.

It is true that we have an unfavorable balance of payments. That is the result of two things.

First, this results because we have a large military outlay, an economic grant, loan and foreign aid program, and troops stationed abroad. The cost of that program to our balance of payments amounted to \$5.2 billion in the first half of 1962, at an annual rate and seasonally adjusted.

In addition, we suffer from an outflow of capital. Businessmen are investing abroad. That is a very good thing. I wish businessmen could invest so much that we could sharply reduce foreign aid. This is a kind of private foreign aid. When private capital is sent abroad it performs the same function as is performed when we provide a Government loan. The difference is that the private loan has the discipline of the profit motive, and there is a very great likelihood

that it will be repaid in hard currency, and also there is a great advantage in the fact that it costs the taxpayers nothing. Also, it is a very healthy thing for the economies abroad.

This kind of aid is rapidly replacing foreign aid, such as we have provided in years past to Europe. It cannot do the job, of course, for the underdeveloped countries.

Nevertheless, this is the reason—whether it be private aid or public aid—for our adverse balance of payments. The adverse balance of payments itself has been diminishing.

Any argument that we face an internal situation in this country which results in our factories being so inefficient that in order to get their costs down we must give them a subsidy, a special "gimmick," a special tax reduction so that they can buy new equipment, is not corroborated by the facts.

I ask unanimous consent that the table from the Survey of Current Business entitled "U.S. Balance of Payments, 1958-62" be printed in the RECORD at this point.

There being no objection, the table was ordered to be printed in the RECORD, as follows:

U.S. balance of payments, 1958-62

[In billions of dollars]

	1958-60 average	1961		1962, 1st half ¹
		Full year	2d half ¹	
Commercial exports.....		17.7	17.8	18.1
Government aid- financed exports ²	17.4	2.2	2.4	2.6
Imports.....	-14.3	-14.5	-15.5	-15.9
Surplus on trade.....	3.1	5.4	4.7	4.8
Services rendered.....	7.0	7.7	7.8	8.2
Services received ³	-5.9	-6.3	-6.5	-6.5
Surplus on services.....	1.1	1.4	1.3	1.7
Surplus on trade and services.....	4.2	6.8	6.0	-6.5
Military outlays ⁴	-2.9	-2.5	-2.4	-2.0
Economic grants.....	-1.6	-1.9		
Loans ⁵	-0.8	-0.9	-4.0	-3.2
Total Govern- ment outlays.....	-5.3	-5.3	-6.4	-5.2
Private long-term cap- ital:				
Inflow.....	.3	.6	.1	.3
Outflow.....	-2.4	-2.5	-2.8	-2.5
Net.....	-2.1	-1.9	-2.7	-2.2
Total Government outlays and pri- vate long-term capital.....	-7.4	-7.2	-9.1	-7.4
Basic deficit.....	3.2	.4	3.0	.9
Private short-term capital:				
Recorded outflow.....	-0.6	-1.5	-1.2	-0.8
Errors and omissions.....	.1	-0.6	-0.4	.5
Net.....	-0.5	-2.1	-1.6	-0.3
Overall deficit.....	3.7	2.5	4.6	1.2

¹ Seasonally adjusted, raised to annual rate.

² Excluding shipments under military aid programs.

³ Including private remittances and Government pensions.

⁴ Net of sales of military equipment.

⁵ Net of repayments.

NOTE.—Details may not add to totals because of rounding.

Source: U.S. Department of Commerce, Survey of Current Business. Figures for the 1st half of 1962 are educated guesses based on preliminary and incomplete data.

NEED MORE CONSUMER PURCHASING POWER

Mr. PROXMIRE. Mr. President, Dr. Otto Eckstein, a witness before the Joint Economic Committee recently pointed to our real need. He said:

We have already had a liberalization of depreciation allowances which will save business about \$2 billion a year.

That was the recent revision of schedule F by the Secretary of the Treasury. Continuing—

The investment credit which may be enacted in this session would add at least another billion-plus to business tax relief.

Thus, these two measures alone would reduce corporation income tax payments by \$3 to \$4 billion, thereby increasing the supply of investible funds. If further substantial relief is given in business taxation, while at the same time lack of growth of consumer purchasing power keeps the demand for final products relatively low, there is little chance that the additional savings being made available will in fact be invested.

That is a masterpiece of understatement, when one recognizes the fact that even before we made the depreciation schedules available, let alone the investment credit, business was not coming close to using its cash earnings. As has been pointed out, there has rarely been a situation, as far back as we can go, in which the ratio of plant and equipment investment to cash earnings has been as low as it is now.

Dr. Eckstein proceeded to say:

Thus, a tax cut which only adds to savings may very well do more harm than good in dealing with the central economic problem of our day, which is the shortfall of demand below potential supply.

That sentence from Dr. Eckstein is mighty significant.

A tax cut which only adds to savings may very well do more harm than good in dealing with the central economic problem of our day, which is the shortfall of demand below potential supply.

Where will the tax cut for business go, when businessmen say they do not want it and will not use it, other than into savings? That is where it will go.

A.T. & T. is to get a \$75 million tax cut, which it does not want. A.T. & T. representatives testified before the Finance Committee against this proposal. That money will go into savings, because they will not use it. They will not increase their investment by \$1 because of it.

Dr. Eckstein says that this may very well do more harm than good.

On the other side, increased international competition and the need for high long-term growth to meet our obligations requires us to take some additional steps toward raising the fraction of GNP which is invested.

The statistics which we have placed in the RECORD take care of the latter part of Dr. Eckstein's argument, I think.

NO REAL PRECEDENT FOR INVESTMENT CREDIT

The testimony by Secretary Dillon, who was the principal witness in favor of the bill, is really the cornerstone on which this provision is based. Secretary Dillon said:

This method of investment stimulation is presently in use in the United Kingdom, Belgium, and the Netherlands and is in the

process of being enacted by the Australian Parliament. It is a tried and proven approach.

Again, I point out that there could not be a more unfortunate example. The only countries in the world, apparently, which have the investment credit are the United Kingdom, Belgium, and the Netherlands.

The United Kingdom has a slower rate of growth than ours, the slowest of any industrialized country in the world. The United Kingdom has not increased its growth. It has not improved its ability to trade. It has not increased efficiency. It is the only industrialized country of the world with a record of growth worse than ours.

What are the other countries? Belgium and Holland have this provision. To compare the economy of the United States of America with the economies of Belgium and Holland is like comparing a Cadillac with a "kiddy-car" or with a tricycle. There is no comparison. Belgium and Holland are fine countries, but they are little countries. They are very small countries.

They depend on foreign trade overwhelmingly. They have moved now into a brand new economic situation by joining the Common Market. The comparison there is obviously void.

Mr. Dillon said that the Australian Parliament is in the process of adopting it but it has not been adopted. So that could hardly be an effective test.

I suppose in Australia they are saying that the U.S. Congress is in the process of adopting investment credit. We may be. But certainly our experience cannot be used as an example of how it is likely to work.

Mr. Dillon went on to say that the investment credit will stimulate investment in industrial capacity.

If my very extensive and elaborate belaboring of the McGraw-Hill study today did nothing else, it established the fact that we are already performing a tremendous task of modernization of our plant and equipment, the biggest job we have ever done. Last year the figure was 68 percent; this year 70 percent. In the coming years at least 68 or 70 percent of all our investment will be for modernization.

The evidence is that in some industries it even will be higher. That is a remarkable performance. It is particularly remarkable in view of the further fact that the McGraw-Hill survey shows that we are investing a record amount—never as much overall.

As far as increasing the expansion of our industrial capacity is concerned, Mr. Dillon would have to agree that that would not do it. The only way we can increase the expansion of equipment is by increasing demand. Nobody is going to buy more equipment if he does not have a use or a market for it.

Whenever we have gotten advocates of investment credit to testify, they have conceded that the main thrust will not be on expansion but on modernization. But as the McGraw-Hill survey shows modernization is preceeding apace.

Mr. Dillon said that in the second place, it would strengthen our whole economy.

It cannot strengthen our whole economy. As Dr. Eckstein so well said, a tax cut that adds to savings will do more harm than good.

Mr. Dillon said that it would contribute to economic growth.

Obviously, if it is not going to be invested or will not result in additional expansion or modernization—and the testimony is overwhelming that it will not—it will not contribute to economic growth.

Mr. Dillon said that it would substantially increase the competitiveness of American products in markets at home and abroad. I think we have already answered that by pointing out the fact that we are already competing with the greatest effectiveness overseas. We have done so to such an extent that I think the problem is how we should increase the capacity of countries overseas so that they can rectify their balance of trade, and so that it will not be necessary for us to carry such a big share of the burden of our foreign aid program.

COLD EVIDENCE OF MARKETPLACE: AMERICA MORE EFFICIENT

Mr. Dillon went on to say:

Our balance-of-payments positions, as well as our standard of living in the long run, can be improved or even maintained only if we can increase our efficiency and productivity at a rate at least equal to that of other leading industrialized nations.

That seems to be pretty much the cornerstone of Mr. Dillon's argument. We must be able to increase our productivity as rapidly as do countries abroad. Every survey and study shows that countries abroad have increased their productivity for a very obvious reason. They rebuilt their economies from scratch. They were in a position in which they had no buildings, factories, or equipment. The people had too few clothes. They had nothing. They have come a long way. Of course, in that process a country grows when it starts from scratch. The war-ravaged economies have been rebuilt. They are not completed yet. What is now happening in Europe is that they are going through an Americanization process. The Americanization process is to do what they can, as rapidly as possible, to get the same kind of standard of living there as we have here. That means further growth in their countries.

Whereas in our country 9 out of 10 homes have television, only about 2 out of 10 homes in Europe have television.

In our country 99 families out of 100 have refrigerators; less than half the homes in Europe have refrigerators. They have an enormous market and a great need for goods. That means they will grow, especially in view of the fact that they have high skills. They pay increasing wages. They suffer inflation of a much more serious kind than we do.

Under those circumstances it is not accurate or responsible to compare our rate of growth with that of countries abroad. It does not make sense, because we would compare entirely different things.

Unless we wish to make comparisons on the basis of which country is best able to trade in the world, I submit on the basis of statistics which I put in the RECORD showing our overwhelming balance of trade—even if we left out of

account foreign aid and military troops abroad—there is real evidence of a strong balance of trade.

There is real evidence that we are competing very effectively and that we are more efficient than they. While there may be some plants which are newer than ours, because they started later, nevertheless, overall, we have a more productive and efficient economy than exists in Europe. I think we can keep it that way by relying on our market economy and by doing what a number of economists have stressed over and over again, which is to get a fuller utilization of our present plant.

The way to increase efficiency is to operate at the optimum rate. The reason we are less efficient is that plants abroad are operating at their maximum capacity. When a plant operates at 100 percent of capacity, its overhead is spread over a much larger volume of production. When we operate our plants at 85 percent of capacity or, as in the steel industry, at 50 or 60 percent of capacity at times, we must spread the overhead over a more limited volume, so the overhead is twice as great per unit at 50 percent of capacity as it is at 100 percent of capacity.

The way that we can reduce our unit cost is to get our rate of capacity of operations up. We do not get the rate of capacity of operations up by building a capacity that we do not need. That would drive us in the opposite direction.

Mr. Dillon went on to say:

These nations have now largely achieved the conditions needed to attract massive investment in productive facilities—including external currency convertibility, price stability, and political stability—and they are providing effective tax incentives designed to accelerate investment and growth. We cannot, therefore, afford to stand by and do nothing, or put off affirmative action to a later day. We need to increase our investment in machinery and equipment now—delay can only place greater strains on our international payments position and put off the achievement of the rate of growth we must achieve if we are to meet our domestic and international commitments and provide jobs for our ever-increasing labor force.

That is really Alice in Wonderland. One would think from hearing Mr. Dillon testify that we had an unfavorable balance of trade instead of the extremely favorable balance of trade that I have already established.

Mr. Dillon went on to say:

Machinery and equipment expenditures—the type of business capital expenditure which is basic to the creation of new products and which also makes the most direct contribution to cost-cutting, productivity, and efficiency—constitute a smaller percentage of the gross national product in the United States than in any major industrial nation of the world.

Of course, Mr. President. We are a service economy. We are a mature economy. We are not still building our factories. We are not equipping our factories from scratch. We are an economy, as Dr. Katona pointed out, in which we are consumer oriented. We are producing for the consumer. That is the reason.

Of course, it is also true that we have a much greater absolute investment in a

per capita sense and on any other basis than any of these other countries. We have greater absolute investment in plant and equipment than they. Theirs are poor economies.

The point I should like to make is that this investment credit does not encourage investment in equipment alone. This provides credit for any depreciable asset including martini mixers, glass table tops, escalators, and almost anything one can think of.

Mr. Dillon goes on to say:

Recent studies indicate a close correlation between the ratio of investment in productive equipment to GNP and the rate of economic growth. In view of the relatively small proportion of GNP that has been allocated to investment in machinery and equipment in the United States, it is not surprising to find that the average annual rate of growth (in constant prices) experienced in the United States in the decade of the fifties was only 3 percent, compared with more than 7 percent for West Germany, and with a range of 4 to 6 percent for most other industrial countries of Western Europe.

Mr. President, the answer is that we have far greater investment than exists abroad. We have a much greater economy, much more expansive demand for all goods, and a much greater production of all goods than they. We have had an increase in our gross national product of \$50 billion over a period of 18 months. This is an increase of 10 percent. If the British, German, French, and Italian economies grew by \$50 billion, it would be an increase of perhaps 50 percent or 60 percent or 70 percent. We are growing much more rapidly than they are. Our rate is less because our base is far greater. Only one of the countries mentioned by Mr. Dillon has an investment credit, and that is the United Kingdom, and that country grew less rapidly than we did.

Mr. Dillon goes on to say:

We cannot hope to achieve the increased rate of capital formation necessary to more rapid economic growth and full employment unless we bring our tax treatment of capital investment into line with the standards which our European competitors have used so successfully, over the past decade.

This country is far more efficient, far more productive, than the European countries. They have grown because they have grown from a smaller base. Economists who come before our Joint Economic Committee from Italy, England, and Switzerland say they come to a country which is the most greatly admired, which has an industrial efficiency that far surpasses theirs. They admit it.

For us to have to key our tax policies to the policies of Europe, in view of our great record, is almost insulting, as well as being extraordinarily regressive, because the fact is that in Europe the tax burden is overwhelmingly on the little man, and the man with big income, especially the man with an income of more than \$50,000, is far less heavily taxed, and has many more loopholes available to him. I do not see that there is any basis, based on the record, for us to change our economy and model it after European economies in view of the over-

all record of the United States of America as compared with the economies abroad.

WHY SHOULD AMERICA MATCH INEQUITABLE FOREIGN TAX PROVISIONS?

Mr. Dillon goes on to say:

The revised depreciation guidelines, to be announced in late spring of this year, will constitute the first really major change in the administration of depreciation since the early 1930's. The establishment of a modern depreciation system which takes account of the current faster tempo of obsolescence will help to stimulate investment in this country. But I must emphasize the shortening of depreciable lives to a fully realistic basis will not bring American industry abreast of its foreign competitors. For all the other major industrialized nations of the free world provide for either the use of unrealistically short lives for depreciation purposes, a practice which distorts income and cost statements, or for special initial allowances or investment allowances which supplement regular depreciation charges, or for a combination of two or more of these incentives.

This is very discouraging reading, to have the Secretary of the Treasury say that because Europeans have very unsound and inferior and inequitable situation at the present time, we ought to do the same thing.

What he did in changing our depreciation schedules was good and praiseworthy, in providing that our depreciation shall be as realistic as it can be, with just as short a life as business can establish for every item of equipment. To say that we should do more than this, does not make sense. It is morally wrong to permit a company or a person to depreciate more than 100 percent. That this is wrong is exactly the position taken by Senator BYRD and Senator WILLIAMS of Delaware, in the hearings of the Senate Finance Committee. These men have been conservatives and have fought hard throughout the years for conservative principles. They understand business and are supported by American business. They know that this kind of provision is wrong, because they are men who believe in morality and recognize that it does not make any sense to permit people to depreciate more than 100 percent, to get back more than they put in. This is a clear subsidy.

Secretary Dillon also said:

It is essential to our competitive position in markets, both here, at home, and abroad, that American industry be put on the same basis as foreign industry. Unless this is done, increased imports and decreased exports will unnecessarily add to the burden of our balance-of-payment deficit.

The whole case is built around the notion that because other countries provide an unjust break for their business people, we must do exactly the same thing. As I said earlier, exactly the same argument is made in every State of the Union before every State legislature. It is the old Gresham's law that prods legislatures to a regressive tax system, because that is the way business likes it.

In this case, apparently, someone in the Treasury thinks we should push business in that direction, even though business does not like it, but that does

not make sense. This cannot be justified on the basis of our balance of trade, because it is favorable, and not unfavorable.

FACTS FLATLY CONTRADICT DILLON ON NEED FOR CASH

Mr. Dillon says:

An increase of this magnitude will provide a major stimulus to business firms to replace older, less efficient machinery and equipment, and, in the process, incorporate the most recent technological developments into productive facilities. Investment decisions are influenced as well by the availability of funds. Since the credit will increase the flow of cash available for investment, it will stimulate investment through this effect as well as through its effect on profitability. The increased cash flow will be particularly important for new and smaller firms, which do not have ready access to the capital markets and whose growth is often restrained by a lack of capital funds.

We have already documented that right up to the hilt. We have shown that there is no dearth of capital funds, that cash earnings are more than sufficient, and that there is a surplus of cash funds.

We have rarely, if ever, in our history had a situation in which there was such a small amount of investment in equipment and plant in relationship to cash earnings available. The responses to the McGraw-Hill survey show there will be resort to capital markets to the extent of only 1 percent of the need for investment in plant and equipment.

Mr. Dillon goes on to say:

Another interesting comparison may be made, one that should intrigue those who favor a low-interest rate as a primary investment stimulus. An 8-percent investment credit reduces the gross financing costs of a 10-year asset as much as would a reduction of the interest rate from 5 to 3½ percent, for a 15-year asset from 5 to 3¼ percent. But the credit does not entail the balance of payments and other difficulties that would accompany a concerted effort to bring long-term interest rates down by such a large extent.

As I stated earlier, when I discussed this subject about 3 o'clock this afternoon, all the scholarly studies show that interest differentials have little effect on the balance of payments.

But to get back to his point, while it is true that this might have a greater effect so far as business being able to borrow is concerned, the overwhelming experience is that interest rates have almost no effect on business investment in plant and equipment.

The classic experience was from 1955 to 1957. In that period, the Federal Reserve Board followed a policy of very tight interest rates. The discount rate was increased and open market operations to drive interest rates up. Tight money conditions existed for about 3 years. Conditions were so tight that the homebuilding industry took a very serious beating, and the number of housing starts dropped precipitously below a million starts a year.

The important point was that that was a period of high and rising interest rates. Yet it was the best period, from the standpoint of investment in plant and equipment, that this country has

ever had. So the analogy that the Secretary of the Treasury makes does not bear out the idea that either interest rates or a tax credit will be decisive factors in determining whether businessmen will make investments in plant and equipment. Such investments will be made based largely on cost and whether the businessman has a market sufficient to persuade him that he can make such an investment and make a profit.

I continue reading:

**M'GRAW HILL REFUSES DILLON ON
MODERNIZATION**

The American economy now is much in need of modernization of its capital equipment which, in the technological environment of the 1960's, requires an increase in the ratio of capital to output. One of the important means of achieving a higher rate of economic growth lies precisely in increasing this ratio, and a direct approach to investment incentives is needed to accomplish this.

Unfortunately, Mr. Dillon does not prove this. The McGraw-Hill survey states exactly the opposite. McGraw-Hill shows that we have a record investment in equipment. Never was it so big. It will be bigger next year, and bigger the year after. Most of it is going into modernization. But this fact the Secretary of the Treasury chooses to ignore.

**DILLON RIGHT IN OPPOSING 3-PERCENT UTILITY
CREDIT STILL IN BILL**

Mr. Dillon continues:

H.R. 10650 provides a partial credit of 3 percent with respect to otherwise qualified outlays by regulated public utilities such as electric power, gas, and telephone companies. The full credit is allowed transportation companies which do not enjoy the monopoly privileges of the other utilities and whose rates are not regulated in a manner designed to permit a specific rate of return for each company. The full credit is also allowed to gas pipelines.

Of course, this is ridiculous. Providing a 3-percent credit for utilities is an absolute waste of money. The Secretary of the Treasury knows it, and he testified to that effect. He is against this proposal. He testified against it, and he submitted excellent documentation, which I shall place in the RECORD shortly, which establishes why providing an incentive for utilities does not stand up.

Finally Mr. Dillon says:

Far from adding to the forces responsible for alternative recessions and recoveries, it will be of major assistance in strengthening our present recovery and enabling us to attain a higher rate of growth and sustained full employment.

There is no corroboration of this. It is merely an assertion; but it does not stand up against the very careful analysis, which I made earlier, showing that the effect would be supercyclical. It cannot be anything else. It is sure to have that effect. Certainly in a period of expanding business conditions, when profits are good, firms will be more likely to use investment credit, because they can then reduce their tax liability.

In these times of large inventory, when the Government is anxious to do all it can do to reduce the pressure on limited resources, there will be every temptation and every reason for a firm to buy

equipment so as to be able to reduce its tax liability.

Furthermore, this is exactly the period of time when the Government will want to maintain a surplus, so that it can also in this way discourage inflation and keep inflation within bounds. But both these purposes would be subverted by investment credit. Investment credit as an offset would persuade businessmen to invest in equipment at a time when Government ought to reap a surplus. Exactly the reverse situation would happen in a recession and drive us deeper into a recession, because businessmen would postpone the purchase of equipment until they were sure they would have income against which to write it off, and will postpone it to a period when profits are down.

If we should again have a recession when many corporations operate at a net loss, the investment credit would be a serious deterrent for anybody to invest in plant and equipment. Purchases would be postponed, doubly aggravating the recession or depression.

Secretary Dillon was most thoughtful in analyzing his reasons for the exclusion of public utilities from the investment credit. He pointed out that public utilities are a regulated monopoly industry and are subject to ratemaking procedures.

Of course, that would mean that consumers, in effect, would be subsidized at the expense of the general taxpayers.

I think that is clear from the arguments I have already made.

Mr. President, I ask unanimous consent to have printed at this point in the RECORD the detailed arguments for the exclusion of public utilities from the investment credit and supporting data, to be found on pages 126 through 143 of the hearings.

There being no objection, the excerpt from the hearings was ordered to be printed in the RECORD, as follows:

**DETAILED ARGUMENT FOR THE EXCLUSION OF
PUBLIC UTILITIES FROM THE INVESTMENT
CREDIT AND SUPPORTING DATA**

**1. Utilities' investment needs are determined
by public demand**

The public utilities are regulated monopoly industries which are legally obligated to serve public needs and which construct their facilities on a demand basis to meet public requirements. Studies of investment in both the telephone and electric power industries conclude that the relationship between present demand and capacity is the primary determinant of investment. Investment in utilities does not occur spontaneously to create new demand but is determined by demand.¹

**2. Utilities are regulated monopolies afforded
the opportunity to earn just and reasonable
rates of return after tax**

In return for their authorization to operate as regulated service corporations, they

are assured consumer rate charges which will cover their costs of operation, including Federal income taxes, plus a just and reasonable rate of return on investment. This rate of return is set so as to attract the capital needed to serve the public convenience and necessity.² For the vast majority of utilities the rate of return presently available, when adjusted for the lack of risk on that investment, equals or exceeds the rate of return in other industries. Furthermore, the rate of return is gaged to enable the utility to obtain adequate capital at whatever cost is required.

(See appendix A to exhibit I-C.)

Because the corporate income tax is treated as a cost of operation, the utilities and their investors do not bear the burden of the tax. They are therefore not subject to the disincentive effects which the tax may have on investment decisions of other industries not sheltered by regulated monopoly conditions. In addition, the risk of investment in the utility field is less than in industry generally. The utilities have no difficulty raising capital needed for expansion.

**3. Utilities will not raise investment
significantly in response to the credit**

With a captive monopoly market, guaranteed rates of return, ready access to capital funds, and need for new investment determined largely by long-range trends in consumer demand, public utilities are not likely to respond in the same manner as other industrial corporations operating in competitive markets to tax incentives such as the investment credit.

Unlike manufacturers who can stimulate new markets by developing new products, the gas and electric utilities offer a commodity that has changed imperceptibly over the past half century. They cannot stimulate new types of demand that the manufacturing firm can tap with new products. Rather the utilities' new investment satisfies growing consumer needs that they are legally required to meet and that they can readily project for the years ahead.

**4. Experience with amortization program in
regulated industries was unsatisfactory**

The unsatisfactory results of attempts to stimulate public utility investment are exemplified by the recent experience with accelerated amortization in the electric utility field. This experience was critically reviewed by the Congress when it restricted the further issuance of amortization certificates in 1957. Chairman BYRD of the Senate Finance Committee, in commenting on the matter in 1957, stated that he regarded such rapid tax writeoffs for utilities as without any justification whatever because utilities are guaranteed profits.³

The report of the Senate Judiciary Committee made by its Subcommittee on Antitrust and Monopoly concerning the experience of regulated industries under rapid amortization stated:

"Grave consequences have followed the enormous grants of tax amortization to operating utilities in the electric power field. Consumers have fared badly, for the Federal Power Commission rules that lower rates were not the purpose of the tax amortization statute, and the courts have sustained the FPC. As a result of the hearings, the Fed-

² Typically the firm's rates are individually regulated in such a way as to provide the full amount of revenue required to service its long-term debt and preferred stock, as well as a return on common stock which is "fair," as judged by price earning ratios and similar measures of the cost of equity capital.

³ U.S. Senate, Committee on Finance, "Rapid Amortization of Emergency Facilities," hearings before the Committee on Finance, 85th Cong., 1st sess., on S. 1795, May 7 and 9, 1957, p. 9.

¹ See Avram Kisslegoff and Franco Modigliani: "Private Investment in the Electric Power Industry and the Acceleration Principle," Review of Economics and Statistics 39 (1957), pp. 363-379 and Paul G. Clark, "The Telephone Industry: A Study in Private Investment," in Wassily Leontieff, Studies in the Structure of the American Economy (New York: Oxford University Press 1953), pp. 243-94.

eral Power Commission surveyed operating utilities and it was established that to an unsuspected extent, tax-free dividends were being paid. Public power witnesses complained of predatory practices by utilities enjoying the lower net taxable income coming from high-depreciation charges, and the subcommittee obtained a listing of all acquisitions made by utilities subsequent to obtaining amortization."⁴

(See app. B to exhibit I-C.)

5. *Investment credit would tend to be passed on to consumers and in the process would gravely complicate rate regulation*

The extension of the investment credit to the utilities would tend to bring heavy pressure on the various regulatory commissions to pass the benefit on to consumers in the form of lower rates. Assuming such a pass-through, there would be little, if any, incentive effect to utility investment. While some of the pass-through would serve to reduce costs slightly for industrial users, much of the benefits would affect residential consumption.

There is, however, serious doubt as to how the investment credit might be treated by the various regulatory agencies. While existing law would appear generally to call for the flow-through approach, it is possible that the credit might lead to pressures for some type of tax-normalization approach which would permit the utilities to retain the credit in addition to their fair rate of return on investment. In any event, the credit would gravely complicate the regulatory process and become a continuing source of controversy and litigation.

In view of the conflicting pressures on the regulatory agencies, the treatment of the credit would probably not be uniform in all jurisdictions. Moreover, before the issues were resolved there would be a period of uncertainty and confusion which would not be favorable for investment or the orderly operation of the utilities. Granting the credit to utilities would introduce discriminatory treatment of different firms, as regulatory agencies responded with different procedures for passing the credit through to consumers.

Special difficulties would be involved in applying the flow-through principle to the credit because, unlike general tax reduction, the credit would vary from year to year with the capital expenditures of the utility corporation. This variance in the tax reduction from year to year would make it extremely difficult for the regulatory authority to determine the proper rate adjustments. Substantial tax credits would be likely to go neither to lower rates nor to additional investment, but into dividends to shareholders. The resulting erratic distribution of the credit in the regulated area and the numerous disputes it would engender would not serve the best interests of either the utilities industry or the Nation in the long run.

(See app. C to exhibit I-C.)

6. *Insignificant effect of the credit on consumer demand*

Some utilities have contended that if the credit were passed on so as to lower the cost of service to consumers, this would increase demand and therefore provide a basis for additional investments in production facilities.

Estimates of the possible effect of passing on the entire amount of the benefit of a 3 percent credit in the form of lower utility rates suggest an average reduction of cost

to electricity consumers of less than 1 percent.⁵ For the average residential customer whose electric bill was about \$7.25 a month in 1959, the resulting reduction would amount to about 7 cents a month. Similarly, for industrial and commercial customers whose average electric bill in 1959 was \$880 a year or about \$73 a month, the adjustment would be about \$69 a month. These reductions are so small as to be an insignificant stimulus to the consumer in changing his use of electricity, even if the demand were reasonably elastic. While reliable estimates are not available on the elasticity or responsiveness of demand for electric power to price changes, there is reason to believe that it has a relatively low degree of elasticity.⁶

7. *High levels of excess capacity now exist in the electric utility industry*

The high levels of excess capacity which now exist in the case of the electric utilities suggest that the investment credit would not be effective and is not needed in this area.

The data on the growth of excess reserves of kilowatts stated as a percentage of December peak loads indicate that in the post-war period reserve capacity over the peak load reached a level of 19.3 percent in 1954, declined to 17.3 percent in 1956, but rose steadily since then to a high of 28.6 percent for 1960.⁷

(See app. D to exhibit I-C.)

The 1956 report of the Joint Committee on Internal Revenue Taxation on the 5-year amortization program indicated that the Office of Defense Mobilization operated on the assumption that an excess capacity reserve in the neighborhood of 24 percent would be required for full mobilization in 1955, which is well above the actual reserves maintained during the Korean war. When reserve capacity reached 20 percent, the goal was closed, presumably because this level was deemed adequate.⁸

⁵ The 1-percent figure is based on an estimate of \$88.5 million credit which the electric power utilities would have received on their 1959 eligible investment in relation to \$9.5 billion of operating revenues.

⁶ Franklin Fisher and Carl Kaysen estimate that household demand for electricity is inelastic; sales would not respond to price declines sufficiently to maintain their revenues from households. Industrial demand tends to be somewhat more elastic, but on the average, one must conclude that overall elasticity of demand in industry is probably close to unity, indicating only slight increases in gross revenues from industry with decreasing prices.

(See app. E to exhibit I-C.)

Demand for gas is also inelastic. A. M. Strout estimates that elasticity of demand for all heating fuels is about three-tenths, indicating that a 1-percent decrease in price would stimulate three-tenths of a percent increase in quantity sold or a loss in revenues of approximately seven-tenths of 1 percent. (See A. M. Strout, "Weather and the Demand for Space Heat" Review of Economics and Statistics, 43 (May 1961) pp. 185-192.) Though greater substitution among fuels can be anticipated in the long-run and the long-run elasticity will be higher, competition between fuels is effectively limited by the high costs of conversion and one can expect little response from the consumer to a reduction in prices.

⁷ Data from June 1961, issue of FPC "Electric Power Statistics."

⁸ U.S. Congress, Joint Committee on Internal Revenue Taxation, "A Report on 5-Year Amortization of Emergency Defense Facilities Under Sec. 168 of the Internal Revenue Code of 1954," Dec. 1956, p. 25.

8. *The investment credit is especially inappropriate for gas pipelines*

The natural gas pipeline industry has expanded at a very rapid rate without the investment credit. As of the end of 1960, the index of plant investment was around 350, as compared to 100 at the end of 1950.

So far as is known, no desirable expansion or modernization has been prevented by lack of readily available funds.

Expansion of interstate natural gas pipelines can be effectuated only with a certificate of convenience and necessity issued by the FPC. The Commission requires an affirmative showing of the adequacy of reserves before any such certificate will be granted. Certification procedures are designed to assure orderly growth in the industry, and will limit the extent to which the investment credit can stimulate growth.

9. *The investment credit as a stimulus to investment*

The investment credit is required to provide the maximum stimulus to investment that will raise our rate of growth, increase productivity, and assist sectors of the economy where economic conditions have caused business to fall behind in its modernization of equipment. The utility industries are not in special need of such a stimulus.

The investment credit specifically excludes buildings and residential construction, as investment in those areas contributes little to modernization of the Nation's industrial productivity. Excluding utilities is but another way in which the impact of the credit would remain focused on investment that will best strengthen our industrial efficiency.

10. *The credit is not discriminatory to public utilities*

Exempting utilities from the credit is not discriminatory to the public utility industry. The legally intended incidence of the income tax paid by the public utilities is on their consumers. Consistent with this principle, the benefits would be passed on to consumers and the utilities would have no net gain from receiving the credit.

11. *Purpose of strengthening international competitive position of American industry is primarily applicable to businesses other than public utilities*

The credit is intended to aid manufacturing and other industries in strengthening their ability to compete with foreign producers for markets here and abroad. This goal is largely inapplicable to utilities which are only indirectly concerned with problems of foreign competition. The need for the credit is clearly greatest in the case of manufacturing and other businesses which need to keep abreast of foreign competition that already receives special investment tax incentives.

12. *Industries would not construct their own utility facilities to obtain advantage of the credit*

The proportion of the total electric power generated by industrial firms has declined steadily since the late 1930's.

(See appendix F to exhibit I-C.)

This suggests that the utility industry has been able to make increasing use of economies of scale in large generating plants. Increasing size of generating installations makes it uneconomic for most manufacturers to generate their own power. As the initial investment has an expected life of about 30 years, and most industrial plants would have a highly variable need for power over that period, it is highly unlikely that a shift to self-generating power by industrial corporations would be stimulated by the

⁴ U.S. Senate, Committee on the Judiciary, Subcommittee on Antitrust and Monopoly, "Rapid Amortization in Regulated Industries," 85th Cong., 2d sess., S. Rept. No. 1380, Mar. 12, 1958, p. 67.

credit.* In fact the current trend would appear to be in the opposite direction. Many companies now lease production machinery, vehicles, and special equipment, as well as buildings, in order to minimize the capital investment required and permit flexible changes in the product lines, method of production, and location.

13. Impact of the credit on small utilities

It has been contended that the investment credit would be a boon to small utilities that do not have ready access to the capital market and have a low rate of return. With the exception of a few firms that account for a very small part of the market, there does not appear to be any support for the contention that rates of return are lower in small utilities. In electric utilities, for example, many of the smaller companies with assets of \$5 to \$50 million enjoy a rate of return of 3.1 to 4.5 percent, a return substantially in excess of the 2.8-percent return enjoyed by the industry's largest firms.¹⁰

About four-fifths of the investment in utilities is concentrated in firms with over a quarter of a billion dollars in total assets that have ready access to the capital market and a rate of return that appears comparable to manufacturing when it is discounted for the lack of risk in utilities and the greater ratio of debt to equity financing. This implies that only a minuscule portion of the credit granted to utilities would go to smaller firms.

(See App. G to exhibit 1-C.)

14. Revenue consideration

The extension of the credit at 3 percent to the public utilities would involve a revenue cost of \$225 million at anticipated 1962 investment levels. This cost is considerably more than the cost of raising the proposed credit in other areas by a whole percentage point, a rise which can be expected to stimulate considerable quantities of new investment in manufacturing and elsewhere.

The investment credit would not only have a substantial initial cost in the utility industry, it would also be more expensive in the long run. Due to the fact that the credit is expected to stimulate less investment in the utility sector than in other industries, less growth in GNP and eventual recoupment of initial revenue losses can be expected from credits extended to the utility than can be expected from credits granted elsewhere.

15. If the credit is not passed on to consumers, windfall benefits accrue to stockholders

Utilities have had ready access to funds for financing new investments during past years. They are much less likely than other industries to have a backlog of investment projects which could not be financed if funds were not made available through the investment credit. For this reason the utilities are more likely than any other group to pay out the case benefits of the investment credit in the form of dividends. As a consequence much of the reduction in tax liabilities made possible by a credit to utilities will become an immediate benefit to the stockholder, rather than a stimulus to additional investment.

* Profitability calculations indicate that the value of the credit is less on 30-year assets than on assets with a shorter life. Hence there is less incentive to the industrial producer here than in an investment in production machinery and equipment with a life of 15 years.

¹⁰ These rates are based on net income after taxes as reported on tax returns. Book incomes will be somewhat higher, and will indicate a greater ratio to return.

16. Competitive position of the utilities in relation to other energy suppliers who will receive the full amount of the credit

Even though the utilities do not receive the credit, there is little reason to believe that their sales will suffer as a result of competition from oil, coal, and other energy sources. Use of these other energy sources on existing equipment would require conversion of equipment that could only be undertaken at great expense.

Thus only new investment would be strongly affected by the price differential. In the case of electric utilities a large part of demand resulting from new investment is entirely independent of other fuels as there are not satisfactory substitutes for electric illumination, small electric motors, and electric power for chemical purifying and refining uses which account for a high proportion of the sales of electricity. In the case of natural gas, it is questionable whether the price differential arising from granting the credit to nonutility industries would give oil and coal a sufficient competitive edge to capture a greater share of new installations for heating, where the automatic delivery, cleanliness, and low maintenance costs of gas are important factors in the choice of heating fuels.

17. Conclusion

The available evidence indicates that the credit would not achieve its intended incentive to investment in the case of the regulated monopoly industries. The application of the credit would be inappropriate in the case of corporations enjoying sheltered markets and just and reasonable rates of return which, in effect, insulate them from the corporate income tax. Exclusion of utilities from the credit will not impair their right to realistic depreciation revision which may be found appropriate in the light of Treasury depreciation studies. Extension of the credit to utilities, on the other hand, would cost disproportionate amounts of revenue. As recognized by important sectors of the utility industry itself, the credit might be prejudicial to the best interests of the utilities in the long run.

[App. A to exhibit I-C]

STATE COURT OPINIONS FAVORING PASS THROUGH OF TAX INCENTIVE BENEFITS

In holding that utilities should be required to pass on to their ratepayers the benefits of liberalized depreciation under section 167 of the Internal Revenue Code, the Pennsylvania Superior Court said (*City of Pittsburgh v. Pennsylvania P.U.C.*, 182 Pa. Superior Ct. 551, 125 A. 2d 372, 382-383):

"Counsel asserts that, since utilities are an important segment of the national economy, they must likewise benefit. The weakness in this assertion is in failing to recognize the distinct nature of a utility as a regulated quasi-monopoly. As such it may obtain funds for modernization and expansion at the current reasonable cost, and it is allowed to pass this cost on to its customers in an annual depreciation allowance and its annual allowable net return as well. In fixing the rate of return the commission takes cognizance of the cost of capital to the utility. It appears therefore that this general desire of Congress to provide working capital and funds for modernization and expansion is, and has been for many years, adequately met for public utilities through rate proceedings."

Similarly, the Supreme Court of Illinois, said (*City of Alton v. Commerce Commission*, 19 Ill. 2d 76, 165 N.E. 2d 513, 520-521):

"Under the policy of this State, utilities are allowed a rate of return calculated to attract the capital required for necessary expansion."

* * * Since in this respect utilities differ from other corporations, the purpose of section 167 would not be thwarted nor would

discrimination be introduced into the Federal tax law by requiring utilities to pass the savings of accelerated depreciation on to their customers. * * * Utilities are at least partial monopolies, and no competition exists to induce them to pass savings on to the public."

[App. B to exhibit I-C]

HISTORICAL PRECEDENT OF ACCELERATED AMORTIZATION

The FPC, in line with perhaps the majority of other regulatory bodies passing on the issue, permitted utilities to normalize income taxes paid with the benefit of accelerated amortization under section 168 of the Internal Revenue Code. (The FPC and many State commissions have adopted the same procedure with respect to liberalized depreciation under section 167.) Utilities thereby accumulated very substantial reserves. Yet the fact is, as set forth at some length in a report of the Subcommittee on Antitrust and Monopoly of the Senate Judiciary Committee, that accelerated amortization had no real tendency to encourage construction of emergency facilities.

For example, the subcommittee said: "Under the policies then (i.e., April 1955) in force, no clear relation to defense needs was required for approval of certificates for electric power generation as they were granted on the basis of total demand, including civilian as well as military needs. The lack of incentive was indicated by the fact that in the few instances where proposed facilities were held ineligible—because of location in target areas—the utility companies constructed them despite the rejection."

The subcommittee further said: "Of the applications considered by the Department of the Interior and the Office of Defense Mobilization, approval was given to facilities scheduled to bring in 13,013,450 kilowatts. Applications which were denied because of their target area location totaled 5,298,000. All of the projects so denied still are scheduled for completion in 1958, despite the withholding of the tax-amortization inducement."

[App. C to exhibit I-C]

"FLOW THROUGH" OF THE CREDIT TO CONSUMERS AND ASSOCIATED COMPLICATIONS

The rate-regulating agency would have to monitor each utility's investment in every year to assure that the company did not earn an excessive return through the investment credit. The following table indicates the varying effect of the credit among companies during the period 1958-60.

Estimated effect of 3-percent tax credit, customer benefit versus stockholder benefit, selected utilities, 1958-60 data

Company	Results whether customer or stockholder gets benefits	
	Customer benefit per year ¹	Stockholder benefit extra return on equity ²
		Percent
Consolidated Edison Co. of New York:		
1958.....	\$0.83	1.04
1959.....	1.11	1.33
1960.....	1.99	2.17
Northern States Power Co. (Minnesota):		
1958.....	.61	.66
1959.....	1.18	1.13
1960.....	1.35	1.32
The Detroit Edison Co.:		
1958.....	1.37	1.00
1959.....	1.14	.84
1960.....	.45	.33

Footnotes at end of table.

Estimated effect of 3-percent tax credit, customer benefit versus stockholder benefit, selected utilities, 1958-60 data—Continued

Company	Results whether customer or stockholder gets benefits	
	Customer benefit per year ¹	Stockholder benefit extra return on equity ²
Pacific Gas & Electric Co.:		Percent
1958.....	\$1.36	1.20
1959.....	.85	.78
1960.....	.81	.76
Appalachian Power Co.:		
1958.....	2.88	2.78
1959.....	.57	.55
1960.....	.57	.54

¹ Average reduction in residential electric bills consequent to rate reductions on residential sales made possible by the investment credit.

² Average percentage point increase in rate of return to equity made possible by passing the investment credit through to stockholders.

[App. D to exhibit I-C]

System capacity and peakloads, 1940-60, U.S. totals for major systems

[Kilowatts]

End of year	Dependable (adverse water year)	December peakloads	Indicated reserves (excess of dependable over December peakload as percent of peak)
1940.....	34,403,434	27,948,071	23.1
1941.....	37,353,709	31,531,206	18.3
1942.....	39,665,335	32,942,464	20.4
1943.....	42,416,767	37,060,061	14.5
1944.....	43,760,322	37,853,847	15.6
1945.....	45,373,031	37,368,925	19.8
1946.....	45,701,894	43,173,803	5.9
1947.....	48,146,326	47,554,537	1.2
1948.....	52,689,808	51,611,873	2.1
1949.....	59,285,449	54,238,069	9.3
1950.....	65,574,230	61,719,096	6.2
1951.....	72,687,954	67,869,836	7.1
1952.....	80,035,407	73,055,403	9.6
1953.....	89,802,220	78,592,567	14.3
1954.....	102,055,254	85,580,848	19.3
1955.....	114,512,107	98,291,077	16.5
1956.....	120,453,230	102,723,432	17.3
1957.....	128,325,252	107,388,343	19.5
1958.....	141,827,422	113,679,341	24.8
1959.....	154,537,818	121,561,168	27.1
1960.....	165,536,249	128,713,483	28.6

Source: June 1961 issue of FPC Electric Power Statistics.

[App. E to exhibit I-C]

ELASTICITY OF ELECTRIC DEMAND

HOUSEHOLD DEMAND

Long run household demand is influenced primarily by the acquisition of electric appliances. A recent statistical study concludes: ¹

¹ Fisher, Franklin M. and Kaysen, Carl, A Study in Econometrics: The Demand For Electricity In the United States, Amsterdam: North-Holland Publishing Co. (1962) 5-7.

"In summary, these long-run results indicate that the growth of the stock of appliances is insensitive to the price of electricity within the range of experienced prices. Whether much larger differences in the prices of appliances than those previously observed would make a difference in the rate of growth of the appliance stock is not clear from these data, nor are these regressions a really adequate explanation of appliance ownership as such. They do suffice to indicate the effect of electricity price, however, which is all that is at issue here."

INDUSTRIAL DEMAND

Long run industrial demand is shaped by changing technology as well as the price of electricity. The same study concludes:

"The results are generally significant and correlations are quite high. The upper limit to price elasticity is somewhat greater than unity in six out of the 10 industries (highest 2.6, for the chemicals industry), unity or less in two more and zero in the remaining two (fabricated metal products and transportation equipment). Similar results are obtained for the mineral industries. Altogether, there is reason to expect a fairly high degree of sensitivity to electricity price in industrial demand given the technology of 1956. The paucity of the data makes it fairly difficult to be certain, however, and the effects of technological change are certainly more important than in the price effect just discussed."

[App. F to exhibit I-C]

Generating capacity, privately owned electric utilities and industrial establishments, 1939-60

[Thousand kilowatts]

Year	Combined Capacity	Privately owned utilities capacity	Industrial establishments	
			Capacity	Percent of combined capacity
1939.....	44,483	33,908	10,575	24
1940.....	45,433	34,398	11,035	24
1941.....	47,681	36,041	11,590	24
1942.....	49,626	37,442	12,184	25
1943.....	51,717	39,128	12,589	24
1944.....	52,610	39,733	12,877	24
1945.....	53,064	40,307	12,757	24
1946.....	53,104	40,355	12,749	24
1947.....	54,816	41,987	12,829	23
1948.....	58,436	45,381	13,055	22
1949.....	63,954	50,484	13,470	21
1950.....	69,106	55,175	13,931	20
1951.....	74,544	60,192	14,352	19
1952.....	79,435	64,349	15,086	19
1953.....	87,053	71,201	15,852	18
1954.....	95,413	79,127	16,286	17
1955.....	103,311	86,887	16,424	16
1956.....	107,790	91,145	16,645	15
1957.....	114,474	97,376	17,098	15
1958.....	126,256	108,202	18,054	14
1959.....	136,510	118,999	17,511	13
1960.....	145,793	128,000	17,793	12

Source: FPC.

[App. G to exhibit I-C]

THE INVESTMENT CREDIT AND SMALL UTILITY COMPANIES

It has been argued that the credit will provide aid to small utility companies that have difficulty financing new investment projects by issues of stock and bonds in the capital market. Clearly such companies are an infinitesimal portion of the industry. If future investment is roughly proportional to the present investment in utility companies corporations with assets in excess of a quarter of a billion dollars will receive four-fifths of the \$225 million benefits that would be granted by a 3-percent credit.

The attached tables present the investment in utility companies, their rate of return, and the percent of total investment held by companies, by size of total assets. For purposes of comparison a similar table has been prepared for all manufacturing corporations. The tables indicate:

1. Investment in heavily concentrated in utility companies with more than a quarter of a billion dollars of assets. (See table 1.) Firms of that size have ready access to the capital market and can attract equity or debt capital on favorable terms.

2. The rate of return as reported by utilities of different sizes does not appear to vary systematically, while the rate of return in manufacturing increases with the size of the firm. (See tables 2 and 3.) Thus while there may be some justification in special aid to small manufacturing corporations to help them raise their return, no such aid to the utilities would appear necessary or desirable.

The rate of return as reported by the telephone industry appears higher than that reported by the gas and electric utilities, but this is partially the result of the fact that 30 percent of the investment in gas and electric utilities is being depreciated under accelerated methods while only 1 percent of the investment in telephone and telegraph is being depreciated under these methods. Taking account of the reduced risk of investment in utilities and the typically high ratio of debt to equity capital, utilities' rates of return are roughly comparable to rates of return in manufacturing. Ratios of bonds with maturity of 1 or more years to total capital account are about 16 percent for manufacturing, 35 percent for communications and 52 percent for gas and electric companies. If equity financing requires a yield approximately 1½ to 2 times that required for bonds, the difference in capital structure would account for most of the observed difference in rate of return.

¹ Variation in rate of return does occur as utilities are individually regulated in a way to reflect difference in the structure of their capital and the cost of capital which may vary according to market valuations of the firm's management, potential for growth, and so forth.

TABLE 1.—Percent of investment in electric, gas, and telephone utilities, by size of firm, 1958-59

Site of firm	Telephone communications	Gas production and distribution ¹	Electric companies and systems	Site of firm	Telephone communications	Gas production and distribution ¹	Electric companies and systems
Under \$100,000.....	0.2	(2)	(2)	\$25,000,000, less than \$50,000,000.....	.8	4.4	1.4
\$100,000, less than \$500,000.....	.8	0.3	(2)	\$50,000,000, less than \$100,000,000.....	1.9	5.6	2.5
\$500,000, less than \$1,000,000.....	.7	.1	(2)	\$100,000,000, less than \$250,000,000.....	.5	16.7	18.3
\$1,000,000, less than \$2,500,000.....	.7	.5	0.2	\$250,000,000 and over.....	92.0	67.5	76.1
\$2,500,000, less than \$5,000,000.....	.4	.6	.4	Total percent.....	100.0	100.0	100.0
\$5,000,000, less than \$10,000,000.....	.8	1.2	.2	Total amount (in billions of dollars).....	\$24.0	\$14.5	\$40.8
\$10,000,000, less than \$25,000,000.....	1.2	3.1	.9				

¹ Excluding natural gas production.

² Less than 0.05 percent.

Source: "Statistics of Income Data Sourcebook."

EXHIBIT I-C

TABLE 2.—Rate of return and investment in public utilities as measured by the ratio of net profits after taxes to total assets less accumulated depreciation and amortization, by size of corporation (tax year 1958-59)

Total assets of corporation	Telephone communication		Gas production and distribution ¹		Electric companies and systems		Total assets of corporation	Telephone communication		Gas production and distribution ¹		Electric companies and systems	
	Investment	Rate of return	Investment	Rate of return	Investment	Rate of return		Investment	Rate of return	Investment	Rate of return	Investment	Rate of return
	Millions	Percent	Millions	Percent	Millions	Percent		Millions	Percent	Millions	Percent	Millions	Percent
Under \$100,000.....	\$42.3	5.3	\$5.2	0.9	\$3.3	3.0	\$50,000,000, less than \$100,000,000.....	\$457.2	3.6	\$816.2	3.0	\$1,002.7	3.3
\$100,000, less than \$500,000.....	190.9	2.9	37.8	1.7	16.7	13.9	\$100,000,000, less than \$250,000,000.....	120.4	8.8	2,424.7	1.7	7,467.7	2.8
\$500,000, less than \$1,000,000.....	158.2	2.9	15.9	.2	19.9	4.2	\$250,000,000 and over.....	22,092.9	5.7	9,798.7	2.1	31,019.3	2.8
\$1,000,000, less than \$2,500,000.....	180.0	2.1	65.6	4.0	68.2	6.9	Total.....	24,002.6	5.5	14,506.7	2.3	40,786.6	2.8
\$2,500,000, less than \$5,000,000.....	99.4	4.9	86.7	5.3	165.0	1.0							
\$5,000,000, less than \$10,000,000.....	203.3	4.1	171.2	3.7	88.4	4.5							
\$10,000,000, less than \$25,000,000.....	255.3	3.6	451.3	3.9	382.3	3.1							
\$25,000,000, less than \$50,000,000.....	202.7	4.0	633.4	3.7	553.1	3.8							

¹ Excluding natural gas production.

Source: "Statistics of Income Data Sourcebook."

NOTE.—The rate of return estimates are based on net income for tax purposes related to net total assets. These rates will be much smaller than book net income related to equity.

TABLE 3.—Investment and rate of return in manufacturing as measured by the ratio of net profits after taxes to total assets less accumulated depreciation and amortization (tax year, 1958-59)

Total assets of corporation	Investment (millions)	Rate of return (percent)	Percent of total investment	Total assets of corporation	Investment (millions)	Rate of return (percent)	Percent of total investment
Under \$25,000.....	\$310	(1)	0.1	\$5,000,000, under \$10,000,000.....	\$11,177	6.0	4.8
\$25,000, under \$50,000.....	697	(1)	.3	\$10,000,000, under \$25,000,000.....	17,695	5.6	7.5
\$50,000, under \$100,000.....	1,771	(1)	.8	\$25,000,000, under \$50,000,000.....	13,523	5.5	5.7
\$100,000, under \$250,000.....	5,112	1.3	2.2	\$50,000,000, under \$100,000,000.....	18,532	6.1	7.9
\$250,000, under \$500,000.....	6,131	3.8	2.6	\$100,000,000, under \$250,000,000.....	25,586	6.2	10.8
\$500,000, under \$1,000,000.....	7,942	3.7	3.4	\$250,000,000 and over.....	104,808	5.5	44.4
\$1,000,000, under \$2,500,000.....	12,315	4.6	5.2	Total.....	235,836	5.5	100.0
\$2,500,000, under \$5,000,000.....	10,237	5.3	4.3				

¹ Losses reported in 1958-59.

Source: "Statistics of Income Data Sourcebook."

NOTE.—The rate of return estimates are based on net income for tax purposes related to net total assets. These rates will be much smaller than book net income related to equity.

Mr. PROXMIRE. Mr. President, I should like to skip a little bit ahead in the hearings, to the testimony of Donald C. Cook. He is president of the American Electric Power Co. He made the most effective presentation in favor of providing this incentive for utilities, and I think this is the appropriate place to refer to it, because I have discussed what I think is a very adequate and effective refutation of the argument made by Mr. Dillon.

Mr. Cook said:

Section 2—

The section setting forth the proposed investment credit—

is intended to encourage additional capital investment by providing for a tax credit in proportion to the amount of the taxpayer's investment in certain new facilities.

I believe that this concept—which I understand was proposed and supported by the administration—is, in the case of public utilities at least, well calculated to achieve the stated purposes.

Section 2, in the form in which it passed the House, provides that, in the case of property with a life of at least 8 years, the credit for most taxpayers is 7 percent; in the case of electric utilities, however, the credit is only 3 percent.

I think it clear—and I intend to show—that, in the case of electric utilities, the tax credit will do more to increase construction and, therefore, to bring about the desired growth in the economy, than in the case of nonutilities.

Then he said—and these are the arguments against it:
To support both the original exclusion of utilities and the proposed discriminatory

treatment, it has been asserted (1) that the availability of the tax credit would not in fact induce greater investment by utilities, because in any event, they would have to build all the facilities necessary to enable them to meet the demand for their service; (2) that if, on the one hand, the tax reduction were retained by a utility the credit would not achieve its intended incentive to investment, and that if, on the other hand, it were passed on to consumers the credit would still not provide any incentive; (3) that the demand for electricity and, therefore, the facilities necessary to supply it are fixed and would not be increased by the tax credit; and (4) that electric utilities are not subject to competition.

Each of these assertions is invalid, and I propose to show it. In addition, at the conclusion of my testimony—to provide concrete evidence that the tax credit would, in fact, represent an important incentive to increased construction expenditures by electric utilities—I will present to the committee a list of projects, together with their estimated costs, never before included in any budgeted construction by any company in the American electric power system, which we are prepared to go forward with immediately if the tax incentive provisions of the legislation are applicable to electric utility companies.

His argument was that the investment credit is so attractive that in the event it is granted, his company stands ready to invest immediately in \$21 million worth of projects which otherwise it would skip.

This is a highly intriguing method of testifying, because it is very concrete and specific, and it says to Congress that the practical consequence of passing the investment credit will be that thousands

of people will be put to work by that company, alone at once in specific States. That argument is very appealing; but I think it is as fallacious as can be.

In the interrogation of Mr. Cook, I think the pro and the con arguments in connection with this issue were rather well developed.

After stating:

If the credit available to electric utilities were 7 percent, rather than 3 percent, the American Electric Power System would forthwith embark upon additions to its scheduled construction projects in a total amount of \$21,020,000.

In reply to a question by the chairman of the committee, the Senator from Virginia [Mr. BYRD], Mr. Cook said:

The CHAIRMAN. This is for 1 year?

Mr. Cook. This is for 1 year only and it is predicated on the basis that for every dollar of tax credit relief which we would receive in the year 1962 we would expend at least \$2 for construction which we never had theretofore budgeted.

COOK'S \$21 MILLION PROJECTS RIGHT OUT OF THIN AIR

Mr. President, the witness really pulled that out of the air. He said, "We are making the basic assumption that if we get this credit, we will invest twice as much as the credit thus would make available." He did not explain why, but he said they would invest it. Apparently, his reasoning was that it would make the profitability that much greater. But he did not explain. His statement was really based on a formula that for every dollar obtained by means of the proposed credit, they would spend

\$2. He referred to the investment they probably would make in the next few years, anyway; and he said, in referring to the total: "We will make this in 1962, if you give us this tax credit"—which would be about a \$10 million tax benefit to them.

Mr. Cook replied to a question by the chairman of the committee questioned whether the tax credit would result in any increase in electrical service. The chairman asked whether Mr. Cook would send to the committee a memorandum to support his position that Secretary Dillon was incorrect and that the proposed tax credit would increase use of electric energy. Mr. Cook replied:

Mr. Cook. Yes, I will, and indeed some of my testimony this morning, Senator, indicated where it was incorrect. I think it was particularly incorrect—and the part that bothered me the most—in the position taken that reductions in rates would not increase the use of electric energy, when there is within the executive branch of the Government, to my certain knowledge, clear information that the facts are to the contrary.

That statement was made when that gentleman testified before the Finance Committee on April 9, 1962. But when the hearings were published—only a few days ago—the memorandum he had promised to send had not been received. But Mr. Cook has not documented his statement that the proposed tax credit would result in increased use of electrical energy. He said he would document that statement; but since April, there has been nothing but silence from him; he has not provided the documentation which he promised to provide.

At the hearing there was very enlightening colloquy between the Senator from Delaware [Mr. WILLIAMS] and Mr. Cook on this issue:

Senator WILLIAMS. Mr. Cook, on page 18 of your statement you list approximately \$21 million which would be spent in additional improvements over a seven-State area, as I understand it, if the 7-percent credit is approved in the bill.

Mr. Cook. Yes, Senator.

Senator WILLIAMS. Do I understand that it is your feeling that these expenditures would not be made if the 7-percent credit is not approved?

Mr. Cook. I so state categorically they will not be made.

Senator WILLIAMS. Now, if the 7-percent credit is approved would they be made this year or over the next 2 or 3 years?

Mr. Cook. These projects are not complicated projects, Senator. The details are set forth in the appendix to my statement—

Senator WILLIAMS. I have examined them.

Mr. Cook. And because they are not complicated projects it should be possible for the modest engineering required and the modest amount of design work required to go forward promptly.

Senator KERR. Well, your statement a while ago was to the fact of effect that would be a 1-year result?

Mr. Cook. That is correct, sir.

Senator KERR. That was your statement to the chairman.

Senator WILLIAMS. That is my question, "Would they be approved in addition this year?"

Mr. Cook. The answer is "Yes."

Senator WILLIAMS. Would they be spent this year or would they be approved?

Mr. Cook. They would be approved, they would be engineered and designed and con-

struction would be started this year but I cannot represent categorically to the committee that they will all be completed in 1962.

Senator WILLIAMS. That was my understanding that they would be planned and started but perhaps completed over this year, next year, and maybe over in 1964.

Did you have anything further to add on that?

Mr. Cook. The chances are that they would not be completed this year, and therefore, the expenditures would extend over 1962 and 1963 with a significant amount being spent in 1963.

Senator WILLIAMS. Yes.

Now, what are your projected expenditures for 1962 without this improvement?

Mr. Cook. Without this credit?

Senator WILLIAMS. Without the credit.

Mr. Cook. That is set forth on the second page of the appendix at \$152 million.

Senator WILLIAMS. What are your projected expenditures for 1963?

Mr. Cook. \$118 million.

Senator WILLIAMS. And I think you said in 1964, well you have \$64 million, it would no doubt be \$100 million anyway?

Mr. Cook. I would guess in the neighborhood of \$90 to \$100 million.

Senator WILLIAMS. That is the 3-year period, that is \$370 million of your expenditures that you are planning to make without any investment credit?

Mr. Cook. Yes, sir.

Senator WILLIAMS. If your investment credit is approved you will spend an additional \$21 million?

Mr. Cook. Yes, sir; in the period indicated.

Senator WILLIAMS. How much would this investment credit be worth on the \$370 million expenditures at 7 percent?

Mr. Cook. If it were applicable to \$370 million at 7 percent it would aggregate for that 3-year period approximately \$26 million.

Senator WILLIAMS. That you would receive as a tax credit?

Mr. Cook. That is correct.

Senator WILLIAMS. Now, as I understand it, what you are telling the committee is that it is the plans of your company to spend \$370 million over the next 3 years without any investment credit?

Mr. Cook. That is correct, sir.

Senator WILLIAMS. But if we approve an investment credit which will give you a \$26 million tax reduction you will spend \$21 million of it in additional capital—

Mr. Cook. No, that would be \$21 million that would be spent immediately, Senator, but if the tax credit remains as a permanent part of the tax structure we would have added to that by quite similar amounts in future years.

Senator WILLIAMS. But you are speaking now, as I understand it, you can only outline \$21 million which would not be spent if you don't get it. Am I to understand that the financial condition of your company is such that you cannot afford to spend this \$21 million if you don't get the \$26 million tax credit?

Mr. Cook. No, Senator, I have not testified to that. As a matter of fact, I testified to the contrary and I would like to state it categorically here.

Senator WILLIAMS. I didn't think you wanted to leave that impression but that was the impression I was getting.

Mr. Cook. No.

My testimony is specifically that it really is almost a matter of indifference as to whether we retain in the company the amount of cash that would be generated by a reduction in the tax rate.

The point is that we could pass these amounts on to our customers but by virtue of the basic economics of our industry. The fact that our revenue requirements are greatly influenced by the extent of the fixed

charges applicable to plant investment and the fact that Federal income taxes represent a major part of those fixed charges and the further fact that as a result of the elimination of those fixed charges represented by the Federal income tax component, makes economically feasible many, many marginal projects.

And this is true regardless of whether we would retain the tax reduction or pass it on to our customers in whole or in part.

This is the essence of Mr. Cook's testimony. I submit an argument cannot be made that a utility will increase its investments because of what I think is a ridiculous, wasteful, and totally unjustified credit of 3 percent to utilities. He never said how it would work. He merely makes the assertion, and he brings it in very cleverly. This reference to \$21 million of named projects is persuasive argument, but it fades away on analysis.

I read further:

Senator WILLIAMS. Are these projects which you have outlined in the \$21 million category essential to your company in order to provide adequate service in the communities which you serve?

Mr. Cook. They are not in the essential category, Senator, but they are desirable projects which otherwise would not come along until 1965 or thereafter.

Senator WILLIAMS. They would be, but they would be furnished at a later year anyway, is that correct?

Mr. Cook. It is likely as to most of them that sometime, whether it is 1965 or 1966 or 1967 or whenever, at some time most of these projects would be carried forward.

There is your answer, Mr. President. By far the most effective witness for investment credit, which is going to cost hundreds of millions of dollars, admits that not one of these projects involving \$21 million is a new project that otherwise would not be engaged in. It would be a matter of speeding up by a year or two. It would involve borrowing investment from the future to make it in the present.

There are times when we would want to do that, but to make it the permanent policy of our country at a time of relative prosperity, at a time when McGraw-Hill indicates a favorable outlook for investment, when they expect investment to expand, is most unwise.

I think the colloquy between the Senator from Delaware [Mr. WILLIAMS] and Mr. Cook exposes it very well.

I would like to read a little further, because I think this is the kind of consideration which can be answered specifically and almost arithmetically, because it can be handled on such a factual basis.

Let me read this colloquy:

Senator WILLIAMS. Would you suggest that this tax credit be taken into consideration in the overall depreciation, with a 100-percent limitation on the amount which can be depreciated?

Mr. Cook. I would regard that, Senator, as nothing but a depreciation reform proposal in a disguised form.

The great merit of the tax credit proposal is that it has no relationship to the aggregate investment in plant and equipment except insofar as that aggregate investment is a measuring stick.

Senator WILLIAMS. As I understand it, the reason you are endorsing the investment credit formula is that you think that indus-

try is entitled to be able to depreciate 116 percent of the cost of any equipment.

Mr. COOK. No, sir; I do not.

Senator WILLIAMS. Do you think it should be limited to 100 percent?

Mr. COOK. It is widely urged in some quarters that we have what is known as economic depreciation which would result in depreciation allowances in excess of 100 percent. I personally do not believe in them. I believe that depreciation should be confined to the amount of capital invested in the assets and should be limited to 100 percent.

Senator WILLIAMS. Well that was the point I was raising. If you agree that the amount of depreciation which is allowed on any equipment should be restricted to 100 percent, do you recommend that if this investment credit is left in this bill and broadened to 7 percent, as you recommend, that we put an overall limitation of 100-percent recovery for any industry?

Mr. COOK. I think the two are unrelated, Senator, and I think to the extent that that limitation is placed on it, by the same token, it will limit the effectiveness of the tax credit device as a means of expanding plants and equipment in the United States.

Senator WILLIAMS. I am having difficulty in reconciling your statement. As I understand it, a moment ago you said you thought that the depreciation schedule should be limited to 100 percent.

Mr. COOK. I do.

Senator WILLIAMS. Do I understand except as it would apply to this case you can get 116 percent now. Either we—

Mr. COOK. I am sorry.

Senator WILLIAMS. I do not quite understand your reasoning.

Mr. COOK. I will be glad to try to explain it. Senator WILLIAMS. Under this formula—

Mr. COOK. The tax credit, Senator, and there is no disguising it, and there is no reason why anyone should not be candid about it, the tax credit proposal is a tax reduction.

Senator WILLIAMS. It is a subsidy.

Mr. COOK. The only significance of the plant account in connection with it is that it is used as the measuring stick, if you will, to determine the amount of the tax credit.

Senator WILLIAMS. Would you characterize it as a subsidy?

I think that colloquy emphasizes that, although witnesses who favor the investment credit may duck and dodge, they cannot avoid the irresistible logic of the fact that this is a subsidy, that any time more than a 100-percent depreciation is provided—and this is in excess of 100 percent depreciation—it is a subsidy.

Under the circumstances, even those who favor the investment credit have great difficulty justifying it, because over and over again in the colloquy Mr. Cook, on principle, had to oppose depreciation which exceeded 100 percent, although that is exactly what investment credit is. If it does not do that, it does not do anything, as Mr. Cook pointed out.

There is another colloquy I should like to read:

Senator WILLIAMS. What were your capital expenditures in 1960 and 1959?

Mr. COOK. In 1960—one moment, sir—I do not have the exact figure here, Senator. My recollection was that it was about \$100 million in 1960.

Senator KERR. In 1961?

Mr. COOK. It would be approximately the same amount—in 1961 our expenditures were approximately \$97 million.

Senator WILLIAMS. Approximately \$100 million, yes. You have a 50-percent expansion in this year's expenditures which were budgeted before you were advised of the possibility of the incentive credit.

Mr. COOK. Yes, Senator; that is correct.

There we have it, Mr. President. This firm has already increased its investment 50 percent, and it did it before there was any notion of investment credit. Now it is said that there would be an additional 6- or 8-percent increase if they could get the 3-percent credit.

I submit that, on the basis of this testimony, and on the basis of very astute interrogation by the Senator from Delaware [Mr. WILLIAMS], the only conclusion one can reach is that there would be no real incentive and there could be no real incentive for utilities in getting the 3-percent cut which would be allowed under the proposed law, and that it is unjustified.

A.T. & T. DOES NOT WANT \$75 MILLION

I come back to the testimony by Mr. Dillon. In the course of the interrogation of Mr. Dillon by the Senator from Virginia [Mr. BYRD], the chairman of the committee, the Senator said:

Consider A.T. & T. They are not lacking funds or progress, they are one of the leading companies in the world. Is it true that A.T. & T. will get 104 million?

That was on the assumption by the chairman that there was to be a 4-percent credit for utilities. It is to be 3 percent, so A.T. & T. would get \$75 million.

Secretary Dillon then said:

I agree with everything you have to say about the A.T. & T. because we are recommending that the investment credit not apply to the A.T. & T., and they don't want it to apply because they are a regulated public utility and they agree with us it shouldn't apply to regulated public utilities.

Thus the chairman of the Committee on Finance, the Secretary of the Treasury speaking for the President of the United States, and A.T. & T. itself have all agreed they should not get a credit, yet they are going to get it. It is written into the bill. They are going to get a \$75 million a year credit out of the Federal Treasury which they do not want.

A little further on the chairman, in questioning Secretary Dillon, said:

Do you agree with Mr. Stam that the loss from the investment proposal will be \$1.4 billion the first year, and \$2.4 billion in the 10th year?

Secretary DILLON. I think our figures for 10 years probably would not be far different from Mr. Stam's, but we do not think there would be any loss, because we think, as a result of this bill, there will be a great deal more business, a great deal more people employed, a great deal more activity, which will all bring in additional taxes which you would not get otherwise, and that, therefore, this would pretty well offset itself.

This is always the argument made in respect to every tax cut. It is always said, "It is not going to cost anything." Of course that is impossible. We cannot cut taxes and expect to get back more than the amount by which we reduce taxes. It cannot be done.

In the instant case, it is doubtful that there would be any stimulation. The business experts say that in the first year, the year with most impact, the stimulation in investment in plant and equipment would be only \$300 million. We will not get back much money if the

increase in the investment in plant and equipment is only about one-fourth of the tax cut.

I submit that the estimates by Mr. Dillon are wrong. It is clear there would be a loss. We might as well face it. The loss would double by the end of 10 years.

DOUGLAS EXPOSES GROWTH FALLACY

A little further along in the testimony the Senator from Illinois [Mr. DOUGLAS], questioning Mr. Dillon, said this:

If a supermarket buys 100 pushwagons in order to increase the speed with which the suburban housewife may move through the supermarket, will this receive an 8-percent—

It was then to be 8 percent—

investment credit in order that the American supermarket may excel those in Holland, Belgium, and West Germany?

Secretary DILLON. It will make our commercial distribution, I would hope, more effective. It will release individual labor for more effective work in industry.

Senator DOUGLAS. And, similarly, will the credit be given for the installation of more shelves in which deodorants and other facial and body aids may be purchased? Will this increase the productive efficiency of the American public and aid in the competition for foreign markets with the chemical industry of Germany?

Secretary DILLON. I am not sure that a shelf is a piece of equipment.

That was one of the things which was recommended; that the bill provide that a shelf be defined as a piece of equipment.

Senator DOUGLAS. Well, then, would an atomizer to kill flies in the supermarket, which is a certain piece of tangible property, receive an 8-percent investment credit in order that the glories of the American trading system may show its superiority to those of continental Europe?

Secretary DILLON. I think that may be so.

Senator DOUGLAS. Would this apply to tangible personal property in the field of commercialized recreation?

Secretary DILLON. Commercialized recreation, yes.

Senator DOUGLAS. Would a ski lift in Sun Valley receive the 8-percent investment credit?

Secretary DILLON. I could not answer that. I do not know whether that is equipment or whether that is real property.

Senator DOUGLAS. It would be used as an integral part of what is defined as the production of utilities?

Secretary DILLON. An automatic pin setting machine—

Senator DOUGLAS. Let us put it this way:

Would you say that the purchase of skis and snowshoes by Sun Valley, which is certainly tangible personal property, would receive an investment credit?

Secretary DILLON. They are not machinery and equipment. They are not—

Senator DOUGLAS. It is tangible personal property?

Secretary DILLON. I think you will see the bill applies to depreciable equipment and I do not think personal skis are depreciable equipment, Senator.

Senator DOUGLAS. Then what about the ski lift?

Secretary DILLON. I do not know whether that would be or not.

Senator DOUGLAS. Well, put it this way: Would the installation of a popcorn machine in the Yankees' ball park, which would last over 8 years, be subject to the 8-percent credit?

Secretary DILLON. If that is machinery or equipment—

Senator DOUGLAS. It is certainly machinery, yes.

Secretary DILLON. Then it would be, I would assume.

Senator DOUGLAS. And the purpose of this, I assume, is so that American industry may have:

- (a) A faster rate of growth; and,
- (b) That it may compete more effectively with the European Market.

Secretary DILLON. Senator, I agree with you that these may be considered anomalies, but that is not the purpose.

The reason for their inclusion is that we did not feel that it was possible or practicable to start a whole new era in the tax law by trying to divide out just where was industrial equipment and where was commercial equipment, and what should be helped and what should not be helped, because we would have had to write hundreds of pages of tax laws.

Senator DOUGLAS. You have taken in a pretty broad territory.

Secretary DILLON. I think that is correct, I agree with that.

Senator DOUGLAS. And even assuming it is a good idea, is not the question whether you should restrict it somewhat?

I do not wish to humiliate you, but I would like to go on with some further illustrations, if I may.

Secretary DILLON. It might well be restricted, if the committee decided that it can do it.

Senator DOUGLAS. Would an escalator in a movie house be regarded as a piece of machinery and equipment?

Secretary DILLON. To that I would have to again give the same answer:

I am not sure whether that is attached or whether it is equipment. If it is a structural part of the building it would not be eligible for the credit.

Senator DOUGLAS. A movie house in the same way?

Secretary DILLON. Same way, wherever it was.

Senator DOUGLAS. The justification for this would be to increase the growth rate in the United States and also to enable the American movie houses to compete more effectively with foreign movie houses so that Americans would stay in the United States and would watch movies?

Secretary DILLON. It certainly would help the escalator business.

Senator DOUGLAS. Or possibly the foreigners would come here in order to avoid walking upstairs?

Secretary DILLON. It would employ people making escalators. But, on reflection, I am quite sure that an escalator would not qualify for the credit.

Senator DOUGLAS. Now, may I ask this: Would this include the installation of automatic cocktail mixers in taverns?

Secretary DILLON. I think it includes all restaurant and bar equipment.

This includes any kind of cocktail mixer. Any kind of bar equipment would get the 7-percent credit under the terms of the bill.

I continue the quotation:

Senator DOUGLAS. And this is done to increase the growth rate and also enable American industry to compete more effectively with foreign industry?

Would the installation—let the record show the Secretary did not reply.

Senator GORE. Mr. Chairman, in all fairness, I think the record should show that he did smile.

Senator DOUGLAS. Would the installation of glass-top table in the 21 Club in New York be regarded as equipment upon which an 8-percent investment credit would be given?

Secretary DILLON. Any equipment having a useful life of more than 4 years would get at least one-third of the credit.

Senator DOUGLAS. Yes.

I take it the answer is "Yes."

And this also will increase the growth rate, I assume, and will enable American industry to compete more effectively.

Will the provision of floodlights in a burlesque house of dubious reputation get an 8-percent investment credit?

Secretary DILLON. I hope we do not have any more such dubious reputation houses.

Senator DOUGLAS. But I mean, assuming that they exist, would they get an investment credit?

Secretary DILLON. Again, that is a piece of equipment, if the law, as presently written, is passed.

Senator DOUGLAS. Are you not interpreting economic growth rather broadly?

Secretary DILLON. If this committee can find a way in which to change this, it would be all right, but I would like to point out here, just to make it clear, that all the other alternative suggestions for providing incentives to growth have just the same problem. They all apply to all sorts of equipment. There is no difference in that regard between the suggestion that we have made and the alternative suggestions for triple declining balance depreciation and more rapid depreciation of one type or another.

Senator DOUGLAS. Mr. Secretary, in 1954, your predecessor, Secretary Humphrey, appeared before this committee and asked that a 4-percent dividend credit be allowed in order to stimulate, as he said, the percentage of corporate financing which would be conducted through the purchase of equity shares.

Senator DOUGLAS. Now, I take it from your statement that you have found that 4 percent which was granted has had no effect in stimulating the percentage of corporate financing carried on by the purchase of equities?

Secretary DILLON. No, it has not.

Senator DOUGLAS. Yet, you think that an 8-percent investment credit will stimulate the total investment?

Secretary DILLON. Very much so because it is a totally different type of credit.

Senator DOUGLAS. If Mr. Humphrey was wrong on 4 percent, may you not be wrong on 8 percent?

Secretary DILLON. I do not think in this case that we are likely to be wrong this same type of law has been in effect in many other countries, and it has clearly stimulated investment there. So I assume the same thing would happen here.

UNITED KINGDOM, HOLLAND, BELGIUM TO TALK INADEQUATE EXAMPLES

Though the tax credit may have been in effect in Holland and Belgium, there is not sufficient evidence either that it has worked in Holland or Belgium, or that if it has worked in a country that small, it would work in our country. It has been in effect in England; and I submit the evidence shows that it has not stimulated impressing growth in England. England is far more comparable to this country than Belgium or Holland is. They have a lower rate of growth than we have in this country. That is the sum total of all experience with investment credit. So the statement by Secretary Dillon that it has been in effect in other countries and has stimulated the investment there does not stand up. There is no record to corroborate it.

INCENTIVE ELIMINATED BY WAYS AND MEANS

Senator DOUGLAS said:

Now, as I remember it, in the draft which you submitted last year to the House Ways and Means Committee, you provided that the investment credit would only be granted

on the net investment, the investment over and above depreciation. Is that true?

Secretary DILLON. That was the original proposal. Well, now, it was not only on that. It would be a 15-percent credit on that, and then it was a 6-percent credit on the amount that was between 50 percent of depreciation and 100 percent of depreciation.

Senator DOUGLAS. But now this credit is allowed for gross investment so that a mere replacement of wornout machinery assumes the 8-percent credit as well as an addition.

Secretary Dillon pointed out that that is what the Ways and Means Committee decided to do.

Senator DOUGLAS. The bill in this present form provides for this investment credit for the investment that would be made anyway in the absence of credit; isn't that true?

Secretary DILLON. That is true. And in the same fashion as any sort of further acceleration of depreciation—

Senator DOUGLAS. It is, therefore, a bonus on investment which would occur anyway.

Secretary DILLON. To the same extent that any such change in depreciation would be, yes.

Senator DOUGLAS. Well, if we want to stimulate investment, wouldn't it be better to have the credit on the marginal decisions, on the investment which would not be made in the absence of such credit or the investments in excess of the previous rate of investment either for the industry or for the—

Secretary DILLON. Possibly the previous rate of investment if we can find the proper formula. What you suggest might have been very great effect, Senator, and might be more reasonable.

The formula we suggested did not work in many cases because, for instance, the railroads have very large depreciation. Unfortunately, they do not have very large earnings now. Therefore, any percentage formula over and above depreciation was of no help to them.

The reason I read that part is because I want to stress what Secretary Dillon said. He is honest. It is not his fault. It is the fault of the House Ways and Means Committee. What the House decided to do was to decide that instead of providing a fairly substantial credit on the additional investment, it would provide a credit on the whole gross investment. Why did it do so? It did so because it was said that the railroads and other industries could not get much advantage out of a credit which was only on the additional investment.

TO INCLUDE DECLINING INDUSTRY KILLED CREDIT

I submit that is exactly the trouble. Surely they would not get the advantage. Why? Because they are not going to increase their investment. The whole purpose of the investment credit, if it has any purpose at all, is to increase investment. But the program has been changed and modified so as to permit the railroads to come in, even though they are declining in their investment in plant and equipment. They were permitted to come in because, it was said, they would otherwise be discriminated against.

Mr. President, there is an excellent object lesson in what happens when a country tries to insert a tax gimmick of that kind in the tax laws. It continues to spread, without any relationship to its fundamental purpose of increasing growth. What has happened is that the

growth-increasing effect is all but gone. Business reaction is clear that it will only increase by a tiny, insignificant amount. But the loss to the Treasury will be fantastically increased.

The old, original proposal of the Kennedy administration would have lost far less to the Treasury than the present proposal.

I ask unanimous consent that the remainder of the colloquy between the Senator from Illinois [Mr. DOUGLAS] and Mr. Dillon in the marked pages that I have before me, that is, the remainder of page 438 and the first one-third of page 439, be printed at this point in the RECORD.

There being no objection, the testimony was ordered to be printed in the RECORD, as follows:

So we had to find some other formula. It turned out that there were a good many industries of that nature, and many accountants testified that there would be all sorts of accounting problems as to what was and what was not proper depreciation, and, therefore, the Ways and Means Committee did decide this was the simpler method.

I must say we were convinced that tax simplification, that the advantages of ease of administration, were very large in this simple approach compared to the other.

Senator DOUGLAS. My offhand judgment is that you are going to be paying bonus to firms which do not need the bonuses in order to simulate investments for items which are of very dubious value in our economic growth and in our competition with foreign countries, as far as that is concerned.

But I have a further objection as of this moment to this plan, and that is whenever we make deductions from taxes based on ways in which income is spent, we open up the door to tremendous abuses.

Congress has now before it or the Senate has before it, H.R. 10 which would provide partial tax exemption for voluntary contributions to the self-employed for pensions.

The Senator from Tennessee and I have opposed that measure, and I assume we will oppose it in the future. But it may well pass.

If this passes, the same principle will inevitably be extended to civil service, to those on social security, to those on railway retirement, to a whole range of benefits.

Every one of us gets a big volume of correspondence asking that similar deductions be made for the cost of educating children up to and through the college level.

If you make a deduction, and this is a deduction from taxes not from taxable income, but from taxes, there will be claims that you should make similar deductions for the purchase of homes in order to encourage homeownership.

I think in your very laudable desire to close loopholes you are now opening up one of the possibilities for the biggest loopholes of all.

GORE SPOTS THREE TAX CREDIT FALLACIES

Mr. PROXMIRE. Mr. President, certainly one of the ablest Members of this body is the distinguished Senator from Tennessee [Mr. GORE]. The Senator from Tennessee has a remarkable grasp of fiscal, financial, and tax policy. He made what I thought was a brilliant analysis of investment credit during the hearings.

The investment credit is based upon three fallacious principles. They are wrong. The first fallacy, the first error, is that U.S. tax policy should and must conform to the tax policies of other industrialized nations.

Said the Senator from Tennessee [Mr. GORE]:

The United States, I have conceived, is a leader in the free world economy. You say, let me read from your statement, that—"It is essential to our competitive position and markets, both here and abroad, that American industry be put on the same basis as foreign industry."

Now, if we do that, we let the plutocrat industrialists, who seem to dominate in West Germany, and the Tory government in England, fix the tax policy of the United States.

If we compete with them in their present preferential tax treatment, then suppose they up us again, must we again meet their standards?

Secretary DILLON. I think that is a very real and difficult problem. I would not say that the European governments are generally all conservative governments, because the government that gives probably the greatest benefits to industry for depreciation is the Socialist government of Sweden. So it is a general thing in European tax policy that they do give substantially greater benefits for writeoffs of depreciation than we do.

Now we are in a world that is a competitive world, and the thing I just cannot see is how we are going to compete unless we allow our industry to compete on an even basis with these foreign competitors.

I do not like, any more than you, having to pass laws or enact provisions because they are the type of provisions that have been enacted somewhere else.

I would like to think that we could operate all by ourselves.

But I just do not feel we are in a vacuum, and I think we are facing a very real competitive situation, and this particularly applies to the question of the choice between investment in this country and investment overseas. It certainly is true that an American company that is able to make that choice gets better treatment if it invests its money overseas than if it invests it here today on this basis.

Senator GORE. You have moved to correct the preferential treatment of income earned abroad by our citizens.

Secretary DILLON. Only part of it; except for the investment credit, which is a very important part, and the treatment of depreciation, we cannot correct that by foreign tax measures. We can only correct that by equalizing opportunities for business here at home with those abroad, because there is no other way of doing it.

Senator GORE. That further illustrates the policy of the treadmill if the U.S. Government undertakes to match tax concessions for business. The Government of West Germany, although I do not ask you to agree with this, pursues a policy under which the mass of the people are underpaid; people underconsume; the profits and the privileges of the few maximized. Yet this investment credit is advocated on the basis that we must match West Germany, and other European countries.

Before I go further, I wish to say that that is exactly the point I made before. I wish to emphasize and underline it. We are leading the world. We are not losing out. Our plant is not less efficient. It is more efficient. Our industry does a better job. The hard, tough, objective, stubborn answer that will not go away, that cannot be refuted, is that we have a very favorable balance of trade on commercial exports, where we compete abroad.

We sell more abroad than other countries sell abroad. We have a favorable balance of trade. They have an unfavorable balance of trade. It is an

essential fact. This establishes the fact that we are more efficient, in spite of our higher standard of living, and higher wages. Notwithstanding all that, we still can outsell every country in the world. To say that somehow or other because other countries have been growing from virtually nothing we should therefore drastically modify our tax system to provide a privilege that business does not want and says will not work, does not add up. It does not make sense.

Senator GORE goes on to say:

That leads to the second of what I regard as fallacious premises. You propose to give unjustified benefits to just about all types of business and industry in the United States, the overwhelming proportion of which is not engaged in foreign commerce, and does not make any significant contribution to foreign commerce, on the grounds that such benefits are necessary for U.S. industry to compete internationally.

Now, I will not cite examples. Both Senator WILLIAMS and Senator DOUGLAS cited them. I could cite hundreds of them, as I am sure you could, such as elevators in a downtown parking garage.

Yet all these people, the bowling alleys—I said I would not cite more of them—are given this unjustified tax benefit on the basis that the small percentage of our industry and business engaged in international commerce needs tax breaks to compete, because the industrialists of Germany and Sweden and England have such breaks and benefits.

I said I would not ask you a lot of questions.

Secretary DILLON. Shall I comment on that?

Senator GORE. Yes, yes, indeed.

Secretary DILLON. I would say that one of the basic reasons for this proposal, and the reason I gave first, and which I will advert to frequently, is the balance-of-payments reason. That, of course, applies both to competition abroad in the export field and to competition here in the United States against imports.

It is important, but it is not the only reason. There is another reason which we feel is equally important, which is the reason which is spelled out at some length in the report of the President's Council of Economic Advisers.

It should be noted again that the balance of payment has been improving all the time. The fact is we can hardly make a greater contribution to the balance of payment by changing our balance of trade, because the overwhelming proof shows that obviously the way we can improve our balance of payment—even foreigners who come here admit it—is by reducing the foreign aid and our military commitment, and in trying to persuade our allies to play a greater role in the defense of the free world. This is the way in which we can reduce our balance-of-payment problem.

Furthermore, one other reason our balance of payment is adverse is due to American investment abroad. That means that as the years pass there will be a greater return on capital from abroad to this country. That means that basically our creditor position is being built up and reinforced and strengthened, and it is certain that we are going to get greater returns from abroad, and not less.

Then Secretary Dillon goes on to say:

We do feel that an increase in investment and the rate of investment is necessary for the economic growth of this country and to solve the problems of growth and unemployment here in this country.

We do feel that this can be brought about—will be brought about—by the investment credit, and in that aspect these other types of investments take on a somewhat different characteristic: Different industries, no matter how unimportant they may be for exports, are vitally important because they give employment and are part of our overall economy here at home. And we do feel that this is an important part of our economic growth.

Investment is the one kind of spending which has been stimulated over and over again since 1954. The whole 1954 Revenue Act was designed to encourage investment. The action taken earlier this year by the Secretary of the Treasury, in reducing the depreciation rate, was designed to increase consumer demand. It was a tax cut designed for business, so that it could increase investment. That is where we have concentrated our attention. This where we do not need it. The facts are clear that we do not need it, because we already have excess capacity. As the McGraw-Hill survey showed we have, we will this year have the biggest investment in plant and equipment we have ever had. It will be bigger next year, and bigger every year thereafter. Most of it is from modernizing at a very rapid rate.

Senator GORE then says:

Well, that leads to the third premise which I regard as fallacious, and that is that you urge more productive capacity when idle capacity, surplus production, and widespread unemployment constitute our most gnawing domestic problem.

That is exactly the point I made.

Secretary Dillon said:

The only thing I have to say on that last is that we do believe that increased expenditure for capital goods will create employment by itself, and that this is just a question of economic theory. I must say that I am not an economist, I do not pretend to be. But certainly the President's Council of Economic Advisers are very capable.

Top economists before our Joint Economic Committee have advised exactly the opposite course. They have stated that where we need help is in the consumer area, not in the investment area.

TOP BUSINESS ORGANIZATIONS DIRECTLY OPPOSE INVESTMENT CREDIT

The testimony before the Committee on Finance, which was also very telling, and which I feel must be called to the attention of the Senate, included an excellent statement by Mr. Walter A. Slowinski, of the Chamber of Commerce of the United States. His statement is less than one page in length. It is worth emphasizing and commenting on:

At yesterday's hearings the Secretary of the Treasury indicated the Chamber of Commerce of the United States had not taken a position on the investment incentive credit at its last tax policy committee meeting. This is in error. The chamber has consistently opposed the investment incentive credit in each of its several forms which have been considered by the chamber's committee on taxation as well as its board of directors.

In each case the vote has been adverse to this type of investment subsidy.

The chamber again recommends against the adoption of this novel and untried preferential tax credit subsidy for business. It is unnecessarily complex and it will be difficult to administer such new concepts in our code as "section 38 property," "qualified investments," "carryover adjustments," and "unused credit years."

The opposition by the chamber to the tax credit is not influenced in any manner by the other proposals contained in H.R. 10650. If all other sections were stripped from this bill, the position of the chamber in opposition to the tax credit as a subsidy would remain.

The investment incentive credit has no place in an income tax law. Its rate (now at 7 percent) and its tenure (somewhat uncertain) continue to be uncertain in the light of the last-minute downward changes which occurred during the last few days of March in the Ways and Means Committee.

The credit gives preferential tax treatment to certain taxpayers in favored groups.

It may actually be a windfall to a business which had already fortuitously planned to purchase new facilities later in 1962. On the other hand it will work against small businesses or lose companies which have no current funds for expansion or no taxable income to be offset by the credit.

More importantly, the adoption of the credit at a revenue loss of at least \$1.175 billion may prejudice and delay meaningful depreciation reform promised by the Secretary of the Treasury this spring.

Many countries provide such initial allowances to measure reasonably the cost of first-year obsolescence. This type of initial allowance has already been adopted in our Internal Revenue Code on a small scale in the 20-percent first-year depreciation allowance for small business in section 179 of the code, but it is limited to \$10,000.

There is no question that the chamber of commerce, which is a body representing a tremendous number of businessmen throughout the country, emphatically opposes the investment credit. While I have often disagreed with the chamber of commerce, and expect to do so in the future, I believe it should be given very sober and thoughtful and respectful attention on this kind of testimony which deals with a tax cut for business. When it appears against this tax reduction on the ground that it is not businesslike and does not work, and is not favorable for business, I think we must recognize that it is entitled to respectful attention and should be given real weight.

Also testifying before the Committee on Finance was a representative of the National Association of Manufacturers, Mr. Harold H. Scaff, who is chairman of the Tax Committee of the National Association of Manufacturers. Mr. Scaff's statement on investment credit was even shorter.

Mr. Scaff said:

The proposed credit is a means for providing varying degrees of relief for some taxpayers but not for others. It is not in form or substance a part of, or in substitution for, or in addition to, or a companion of, depreciation reform. It would simply provide reduction in effective tax rates for taxpayers who use their income, or other funds, as the Government thinks is best for the economy at a particular time.

There has been a tendency to promote and discuss the investment tax credit apart from the price which it would exact in terms of other changes in the tax law. Even without the exaction of such a price, we would op-

pose the credit for the reasons set forth in the appendix attached hereto. Very simply, we believe that tax reduction should be afforded by direct means. We would take this position even if, in our opinion, all of the other provisions of H.R. 10650 constituted sound tax policy.

Consistently, we would not favor legislation of the character of H.R. 10650, even if the tax reduction feature were of the kind to which we subscribe. Despite any seeming temporary advantage, we do not believe that the reshuffling approach offers significant promise for the reduction of the tax burden on capital accumulation and use. Instead, as I have indicated, we look upon it as providing a green light for more Federal spending, which would tend to perpetuate or even increase the restraint of taxation on capital formation and economic progress. This is why we say that H.R. 10650 would provide a red light against adequate growth in the private economy. We believe that the whole approach reflected in H.R. 10650 should be abandoned and that instead the Government should turn to an alternative program of releasing the tax blocks to economic growth, combined with reduction and control of the spending level.

I ask unanimous consent that a more detailed explanation of Mr. Scaff's position on behalf of the National Association of Manufacturers, appearing on pages 536 and 537 of the hearings, be printed at this point in the RECORD.

There being no objection, the excerpt was ordered to be printed in the RECORD, as follows:

APPENDIX—INVESTMENT TAX CREDIT

1. Nature of credit: In the administration's advocacy of an investment tax credit, there has been a persistent tendency to view it as being a part of, or in substitution for, or addition to, or as a companion of, depreciation reform.

Actually, such a credit, in form or in substance, has no connection with depreciation reform. Instead, it is in form and in substance simply a means for lowering effective tax rates to the extent of qualification. The result would be to increase the effective graduation of the corporate tax, and also the personal tax as applied to the income of unincorporated businesses.

2. Subsidy: In economic substance, the investment tax credit would be a subsidy. This fact was first stated by an administration spokesman in March 1961. As a subsidy, it is essentially an expenditure program. Its effect would be no different from establishing a Federal agency for the purpose of paying subsidies to businesses at the rate of \$8 (\$7 in H.R. 10650) for each \$100 of expenditure for specified types of property.

3. Carrot or stick: As between businesses which do or do not, or could or could not, take advantage of such a credit, or which do so in varying degree, the credit is as much a tax penalty as it is a tax favor. The objective could be as well achieved by reducing business tax rates and then applying penalty superrates for failure to reinvest in given property categories in varying proportion to profits.

This is only to say that tax manipulation of the economy is a two-edged sword. Favoring and penalizing by taxation are actually one and the same thing. The abortive undistributed profits tax of 1936 placed the emphasis on penalizing, but, as against those penalized, the result would have been to favor those who conformed to the Government-desired pattern of economic action.

Whether the carrot or the stick is used, the end result of this kind of device is the same. Those who do what the Government wants done at a particular time are favored, and those who for whatever reason do not are penalized.

4. Economic effect: Despite its subsidy nature, there is no reason to believe that an investment tax credit would make any greater contribution to sustained, long-range economic growth than would result from release to business through orthodox means of a comparable amount of tax dollars, for the following reasons:

(a) If the administration had stayed with its original implication of a short-term, "stimulative" device, there may have been some tendency for business to move forward its plans for expenditure in affected categories in order to get sure advantages of the credit. When the administration shifted to an all-out context of permanency, it eliminated the reason for moving expenditures forward. The fact that the word "stimulation," with its short-term or temporary, artificial meaning, is still used in advocating the credit, does not impart character to the credit that does not otherwise exist. Reference to "stimulation" of long-term economic growth is an incongruity.

(b) Regardless of the short-term or long-term nature of the credit, however, or the semantics used in promoting it, it could have no more effect than the tax dollars involved except as (i) business diverted funds from other uses to expenditure for affected categories of property, or (ii) makes more use of bank credit than otherwise would be the case.

In a short-range context, it might be that a credit would excite business to make somewhat greater use of bank credit than otherwise would be the case. However, such an excitement could not be given effect for long, unless the Nation were to accept a continually inflationary expansion of bank credit, or credit were to be diverted from other uses. When the economy achieves full recovery, we inevitably will be faced with a new period of financial tightness. Under such conditions, there is no reason to believe that an investment credit would affect the natural allocation of funds based on rate of interest.

It seems to be believed in some quarters that more liberal use of bank credit is a substitute for the savings of individuals and business. Quite the opposite is true. The greater the total of savings, the greater the use that can be made of bank credit without inflationary consequences. The smaller the total of savings, the less the bank credit which may be used without inflationary consequences.

(c) Businesses which receive the advantage of a credit would be just as free to use the dollars so gained in disbursements to owners, or for kinds of expenditure not qualifying for the credit, as they would be to so use tax reduction dollars made available through other means. There is no reason to believe that the use of business funds after enactment of the credit would to any significant extent overrule normal business judgment as to the best use of such funds.

5. Foreign experience: England is often cited as one of the nations which employs an investment tax credit. Such nations as Germany, France, and Italy, with their faster moving and more stable economies, do not employ such a device. The credit in England covers plant as well as productive equipment. The credit has not solved their problems of an uneconomic tax structure, and it is hardly to be expected that it would solve ours.

6. The basic tax problem: Except for the excessive and uneconomic use of tax rates and methods, there would be no reason to advocate an investment tax credit. In view of the need in the national interest to remove the tax blocks to greater economic growth, it is unfortunate that nearly a year has now been taken in discussion of a device that runs around the problem instead of meeting it. The public welfare will suffer further if consideration of this device continues to becloud tax discussions.

7. Principles of Credit: Through less complicated and manipulative than the original credit proposed, the flat credit is no different in basic principle. As would be expected, some of the testimony against the credit in the 1961 hearings was primarily directed at the complications of the then-pending proposal. But a great part if not the bulk of the testimony reflected opposition or dissatisfaction with the credit principle itself.

Mr. PROXMIRE. Once again, I emphasize that when the National Association of Manufacturers takes a position on legislation of this kind, on legislation that is alleged to relate to the ability of our firms to be able to compete with firms overseas in manufacturing, and when the National Association of Manufacturers takes a position emphatically and clearly against the investment tax credit, and when they document it, as I think anyone who reads the RECORD can see they document it, we should pay very respectful attention to it.

AFL-CIO EMPHATICALLY OPPOSES INVESTMENT CREDIT

One of the outstanding economists in the country is Stanley Ruttenberg, of the AFL-CIO. Not only is he a fine economist; he is an esteemed gentleman, who appeared before the Committee on Finance, representing the considered opinion of the leadership of the 13 million men and women who make up the AFL-CIO. In the course of his appearance before the Committee on Finance, he said:

We cannot and we do not support the investment credit. It is justified by its supporters on the ground that, one, it will improve our world competitive position. We deal in my statement with this problem. Suffice it to say that I can't see how our world competitive position can be improved as a result of this bill. In the year 1961 our export surplus was already \$5½ billion as compared with an export surplus over imports in 1959 of only \$1 billion.

As a matter of fact, more than \$5 billion of the \$5½ billion surplus is due exclusively to a surplus in manufacturing export items over manufactured import items. If we were not competitive, it seems to me we would not be able to maintain this kind of an export surplus.

I think that statement says it very well. It is the same argument I have tried to make today.

Mr. Ruttenberg continues:

The second point which is advanced as an argument in support of investment credit is that it would increase the cash flow to corporations and thereby supplement funds that corporations need to promote financial investment.

We do not think that any of the facts justify the view that there is a shortage of investment funds on the part of American corporations today.

In the post-World War II period from 1946 through 1961 American corporations, excluding financial institutions, invested \$374 billion in new plant and equipment. And over this period of time an amount equal to 96 percent of that total investment was supplied by two sources, depletion allowances and retained earnings after distribution of dividends. And in the year 1961 these sources of corporation funds exceeded plant and equipment expenditures by 6 percent.

Once again, this is the argument I have pointed out. I think that what

Mr. Ruttenberg said when he appeared several months ago before the Committee on Finance is much truer now that we have revised the allowance for greater cash earnings available to American business. Mr. Ruttenberg documents this argument thus:

Third, it is argued that it will stimulate private capital investment that wouldn't occur otherwise.

It is argued that our equipment is older and, therefore, ipso facto, not as modern or as efficient as that of other countries. We challenge those who say that our equipment is not as efficient and modern as that found in other countries around the world and we challenge the statistics which try to show that the average age of our equipment is, therefore, much older and, therefore, consequently, they say less efficient in other countries around the world.

I think the challenge of Mr. Ruttenberg, of the AFL-CIO, very well taken on the basis of facts and statistics I have poured into the RECORD this afternoon from McGraw-Hill and other sources. I think it is clear that the documentation is all on our side. It has to be on our side. The assertion is made that our equipment is growing older. The fact is that it is so efficient that we are able to outproduce, outcompete, and outtrade other countries of the world. What more do they want?

Mr. Ruttenberg continued:

There is another argument which is being made currently. As a matter of fact, the Secretary of the Treasury made the argument in his presentation here the other day. He said that if you compare depreciation rates in the United States with rates of other countries around the world, you find that the representative tax life of equipment in the United States has averaged 19 years as compared with an average of anywhere from 5 years in Sweden to 10 years in most of the other European countries to 16 years in Japan, and 27 years in Great Britain.

Therefore, the argument is made if we want to compete with these companies overseas it is essential for us, in our approach to tax laws through investment credit or depreciation changes, to change our law so that Americans too can write off equipment faster.

I have a table and a memorandum which deals with this subject. I wish I had time to go into it but suffice it to say that the general conclusion is that if you look at these average lives of depreciable assets in countries abroad and in the United States and then compare these rates with the rise in industrial production, there is no correlation whatsoever.

Some of the countries of Europe who write off 90 or 95 percent of their equipment in the first 5 years have had lower increases in industrial production and gross national product than some of the other countries that write off equipment, not in the first 5 years at 90 percent but write it off at 60 or 65 percent.

The point made by Mr. Ruttenberg is absolutely true. The country which has the biggest, juiciest investment credit is Great Britain; and Great Britain also has the slowest rate of growth, the slowest rate of investment in plant and equipment.

I ask unanimous consent to have printed at this point in the RECORD the documentation by Mr. Ruttenberg that appears at pages 599 and 600 of the hearings.

There being no objection, the statement and table were ordered to be printed in the RECORD, as follows:

The attached table points up one serious fallacy in using international comparisons to prove that the United States needs to adopt the investment credit and faster depreciation incentives: There is no correlation between faster tax writeoffs or liberal incentive allowances and changes in economic growth rates or industrial production improvements.

All but the last two columns in the table have been used by Secretary of the Treasury Dillon (see table 1, p. 9, of his testimony on April 2 before the Senate Finance Committee) to demonstrate that U.S. depreciation and other allowances are not so rapid or so liberal as those in other industrial countries. The last two columns, however, point up some of the inconsistencies of using this type of data to prove that America must try to emulate foreign tax systems in order to accomplish faster growth or needed rises in industrial production.

For example, Sweden is the country with the fastest tax writeoffs and possibly "life span" for equipment, according to the table. Equipment may be written off 100 percent in 5 years in Sweden. The "representative tax life" of Swedish equipment, according to the Secretary's table, is 5 years. But the rise of Swedish gross national product between 1953 and 1960 was among the lower of the countries shown on the table, 30 percent in the period; its industrial production increased 35 percent.

But Japan, a country whose tax writeoff

is considerably less than Sweden's—only 68.2 percent in the first 5 years, for equipment with a representative tax life among the longest, 16 years—had the most rapid growth both in gross national product and in industrial production—77 percent and 168 percent, respectively, between the years 1953 and 1960.

Again, Belgium, with 92.5 percent writeoff in the first 5 years, has equipment with the short lifespan of only 8 years. But even the United Kingdom, with a representative equipment life of 27 years and only a 64 percent writeoff in the first 5, shows a faster growth rate than Belgium, both in terms of gross national product and in terms of industrial production.

Or, if there is a correlation, why should France, whose equipment is written off 76.3 percent in the first 5 years have a slower growth rate than West Germany, whose equipment is written off 67.2 percent in that period? Yet the table clearly shows France well behind West Germany, in both growth and industrial production rises between 1953–60.

The table does show that U.S. depreciation allowances and typical lifespans of equipment as well as growth and industrial production rises have been less rapid than other countries. It also shows, however, that changing the U.S. tax provisions would not mean that the U.S. industrial production or gross national product increases would improve.

It is not only wrong to consider these items in a vacuum, as this table does. It is also wrong to draw from the table's data policy conclusions which the data itself does not support.

posals. Its authors are to be commended, at least, for their recognition that fiscal policies can and must be shaped to achieve more than the traditional objective of raising adequate revenue and doing it fairly. Just as fast tax writeoffs served successfully to spur defense-related construction, special tax concessions are wisely granted to encourage small business and temporary tax cuts to counter future business downturns are now properly being supported by the President—practical new fiscal tools must be conceived and used to achieve priority national goals as the need arises. Although we view the investment credit to be an undesirable tax device, we recognize the values of the search for new and imaginative fiscal policies to help solve pressing problems.

It is being argued by the administration that this costly credit is vitally needed to stimulate capital investment and, particularly, to increase our ability to compete overseas. It is our view that this super-billion-dollar permanent subsidy—which will absorb all the revenue from loophole closings—will do little to help achieve these desirable ends. In fact, in the long run it could well do more harm than good. Essentially, the enactment of this scheme would simply substitute a new tax loophole for the discarded older ones.

If we could believe, with its proponents, that this investment credit crash program could truly spur and sustain economic growth and resolve the balance of payments problem quickly, the AFL-CIO would support it. Unfortunately, these problems will not be ended or even mitigated by this tax windfall, no matter how well intended.

In determining what should and should not be done to come to grips realistically with our economic growth and balance-of-payments problems, a number of widespread fallacies need to be exposed. Toward this end, the following questions must be raised as this committee weighs the merits of the investment credit proposal and they should be reasonably answered.

(1) Is it indeed true that American industry is substantially obsolete and therefore is being outcompeted in the markets of the world?

(2) Is it true that American business needs the tax credit to help finance new investments because otherwise funds would not be available?

(3) To what extent would the tax actually stimulate new capital outlays in enterprises vital to our national goals? To what extent would the tax credit simply subsidize investment that would occur without it?

(4) With much of our productive capacity still idle because of lagging domestic demand, how long could the spur of the tax credit sustain investment growth? Should not a top priority now be given to tax policies that will encourage the higher demand that is the essential underpinning for sustained investment growth?

(5) What fruitful measure should now be pursued to deal with the balance-of-payments deficit?

Are we outcompeted in world markets?

Investment credit enthusiasts have overcapitalized on the alarmist view that a crisis of obsolescence has overtaken the American economy—a view that is not supported by the facts.

In 1962, private business firms are reported to be spending a record \$37.2 billion on new plant and equipment, a rate about 8 percent higher than in 1961. Since World War II, as a matter of fact, capital investment in the United States, excluding agriculture, has exceeded \$425 billion—an unparalleled record anywhere.

The view that we are being outproduced and outcompeted is largely due to a misunderstanding of the balance-of-international-

Comparison of depreciation deductions, initial and incentive allowances¹ for industrial equipment in leading industrial countries with similar deductions and allowances in the United States

	Representative tax lives (years)	Depreciation deductions, initial and investment allowances (percentage of cost of asset)			Rise in gross national product, 1953–60 (percent)	Rise in industrial production, 1953–60 (percent)
		1st year	1st 2 years	1st 5 years		
Belgium.....	8	22.5	45.0	92.5	21	27
Canada.....	10	30.0	44.0	71.4	22	30
France.....	10	25.0	43.0	76.3	36	68
West Germany.....	10	20.0	36.0	67.2	61	80
Italy.....	10	25.0	50.0	100.0	49	82
Japan.....	16	43.4	51.0	68.2	77	168
Netherlands.....	10	26.2	49.6	85.6	42	57
Sweden.....	5	30.0	51.0	100.0	30	35
United Kingdom.....	27	39.0	46.3	64.0	22	30
United States.....	19	10.5	19.9	42.7	19	19

¹ The deductions and allowances for each of the foreign countries have been computed on the basis that the investment qualifies fully for any special allowances or deductions permitted. The deductions in the United States have been determined under the double declining balance depreciation method, without regard to the limited 1st-year allowances for small business.

Source: Statement by Douglas Dillon before Senate Finance Committee, Apr. 2, 1962, table 1, p. 9; and Organization for European Economic Cooperation, "General Statistics," July 1961, No. 4.

Mr. PROXMIRE. Mr. Ruttenberg goes on to emphasize, I think very eloquently, the utter waste in the investment credit, when he says:

If you really believe, however, you need to help our foreign competitive trade situation, rather than having an investment credit which goes across the board—it helps barber-shops, it helps agriculture, it helps bowling alleys, it helps equipment in shopping centers, thank goodness it doesn't apply to plant but only to equipment as it is written in the bill, that is a help; it applies also to utilities which obviously don't need the help—why don't we direct the investment credit to just those industries involved in international trade, export industries and others that have serious import disadvantages. In this way we could apply the use of this mechanism selectively for a limited period of time, as long as we have a balance-of-payments crisis.

Senator GORE. Could I make one addition? I feel myself in sympathy with much of what you have suggested if you would add to it that the credit only apply to that degree of plant improvement which is over and above the normal experience of the industry.

Of course, Mr. Ruttenberg wholeheartedly agreed with the statement of Senator GORE.

Mr. President, I ask unanimous consent to have printed at this point in the RECORD a more detailed explanation of the investment credit, as submitted by Mr. Ruttenberg, on pages 632 to 637.

There being no objection, the excerpt from the hearings was ordered to be printed in the RECORD, as follows:

THE INVESTMENT CREDIT

At the outset, we wish to make one laudatory comment about this ill-conceived pro-

payments problem. While it is true that the balance of payments has been negative, the balance of trade has been decidedly positive. In 1961, our nonmilitary exports (\$20.1 billion) actually exceeded imports (\$14.7 billion) by about \$5½ billion. Actually, almost all the balance in our favor comes from finished manufactured products.

"In 1961, they amounted to over \$10 billion while our imports of manufactured products were only \$5 billion," Secretary of Labor Goldberg proudly announced in public testimony 3 weeks ago. Indeed, "our biggest dollar earners are our exports of manufactured products," he added. Surely, this record doesn't indicate that American industry is too obsolete to compete.

While it may be true that some of our enterprises lag technologically for special reasons, and that total new investment would be even higher if domestic demand was growing fast enough to support it, we hardly can be convinced that technological rigor mortis has overtaken the Nation. Too many American workers have been automated out of their jobs or have justifiable reason to fear that they soon will be, for us to have any illusion that our productive system is standing still.

Is a public subsidy needed to finance private investment?

There is just no evidence that American business needs an across-the-board tax credit subsidy to help pay for its new investment. Larger capital outlays are not being deterred because of any overall lack of available private investable funds.

On the contrary, savings available for capital formation are substantial. Actually many businesses now finance new plant and equipment solely with their own internally generated funds—money accumulated from retained profits and depreciation set-asides. From 1946 through 1961, American corporations—excluding financial institutions—invested \$374 billion in new plant and equipment. However, their internally generated funds available for new investment over the 15-year period actually totaled 96 percent of that sum. In 1961, this internal cash flow actually exceeded last year's total outlay for new plant and equipment by 6 percent.

In recent years the cash available for investment from depreciation set-asides alone has grown spectacularly. This is due both to the tremendous aggregate rise in postwar investment and the liberalization of depreciation allowances in 1954 and 1958. While in 1953 corporate depreciation allowances totaled less than \$12 billion, equal to only 49 percent of capital outlays that year, in 1961 these set-asides reached a staggering total of more than \$24 billion, a sum equal to 80 percent of all corporate new plant and equipment expenditure last year. And, with the further liberalization of schedule F now being put into effect by the Treasury, depreciation set-asides will grow even faster.

According to the Council of Economic Advisers, about two-thirds of our manufacturing exports are accounted for by the metal, machinery, and transport industries. Yet, it is precisely the major companies in these industries that are most generously endowed with internally generated funds available for capital improvements. In fact, in recent years they have seldom been forced to sell stock or borrow to meet their new investment needs.

It should also be recalled that the substantial effort to encourage business investment through tax aids has not been confined to liberalized depreciation allowances alone. In 1954, the Congress for the first time also sanctioned the writeoff of research and development outlays as a current cost of doing business. Although this tax law change has also resulted in a substantial Federal revenue loss, it, too, serves as a substantial stimulant to technological progress. In 1960,

the U.S. outlay for research and equipment by our industries reached a record \$10.5 billion compared with less than \$2 billion for all the Common Market nations combined.

It is our view that the Congress has already been more than generous in its effort to spur new investment via tax law. In the fact of the ample resources available to business for new plant and equipment, a further across-the-board public subsidy clearly cannot be justified on the basis of overall need.

Can the tax credit assure investment that serves essential national needs and that wouldn't occur without it?

America's productive plant is neither obsolete, outcompeted nor do businessmen lack access to funds for its expansion. We are told nonetheless, that the investment tax credit is vitally needed. Moreover, the administration is seeking this generous across-the-board business subsidy not just for a year or two; it is being urged "as a continuing part of our tax structure." According to some estimates the original credit proposal would have cost the Treasury more than \$26 billion over the next 10 years.

Will this mountainous giveaway advance the national interest in any relation to its tremendous cost?

Actually, it isn't likely that much additional investment will result from this public outlay that wouldn't occur without it.

While the President's original tax credit proposal was at least aimed at rewarding increased investment from year to year, the House enacted bill now proposes to give this handout to a business even when its new investment is not rising—in fact, even when it is going down. What is more, the committee has lengthened the list of investment credit free riders thereby adding hundreds of millions of dollars to the Treasury's annual revenue loss. Furthermore, as the new equipment (paid for by the public through the subsidy device) wears out, the committee would allow full depreciation set-asides against it. Thus, the benefit from each of these freeloading investment credit handouts would go on and on in perpetuity.

While the tax credit will scarcely assure much added investment that wouldn't occur without it, its payout in tax savings to business will delight the beneficiaries. For example, had it been on the books from 1957 through 1960, Ford and General Motors together would have enjoyed nearly \$100 million more in profits after tax.

According to a recent Wall Street Journal survey of business intentions, if the tax credit becomes law, spokesmen for 67 companies out of 68 said it would have no significant effect on their investment plans. As one business leader put it: "This program won't alter our construction program one bit; it's nothing more than a windfall."

According to J. A. Livingston, the popular business columnist, the whole tax investment credit idea is "just another loophole."

Despite its multibillion-dollar cost, most of the tax credit subsidy would also be of dubious value in achieving vital national objectives. It would reward investors in a host of undertakings—from bowling alleys to barber shops—that have little bearing on our ability to raise exports or on other priority national goals. Even new investment in agriculture will be rewarded despite the fact that this industry now receives a vast public subsidy precisely because it is already producing too much. In a similarly generous spirit utilities are included too, although they enjoy a guaranteed rate of profit and already are legally obligated to provide the new investment required to meet expansion needs.

Actually, the major beneficiaries of the billions of dollars about to be squandered under the investment tax credit scheme will be the 500 largest and richest industrial giants of America. These are the enter-

prises that, according to Fortune magazine, now account for more than half of all manufacturing and mining production and profits. They account for the lion's share of investment in new plant and equipment as well.

Thus, it is evident that the tax credit would neither guarantee a significant net addition to private investment nor would it selectively stimulate these forms of capital outlay that most serve the Nation's needs. Furthermore, over the years it would impose a burden of billions upon the public for subsidies totally unrelated to the financial need of the business beneficiaries.

Can the tax credit assure sustainable investment growth?

Let us now briefly consider the proposed investment credit against the broader backdrop of the Nation's growth needs.

Enactment of the credit might temporarily nudge business investment higher, but it certainly will not encourage balanced and sustainable economic growth. On the contrary, it would more likely distort the recovery and hasten the next recession just as the overgenerous tax benefits for investors after 1954 temporarily stimulated investment from 1955 to 1957 while consumption lagged. Inevitably, the recession of 1957-58 and a substantial accumulation of unused plant and equipment ensued. Today the tax credit stimulus could be expected to be less because of excess production capacity already in existence. The artificially continued investment stimulus would be short lived.

The major prerequisite for increased and sustained business investment is high-level use of existing plant and equipment and the expectation that sales will continue to rise. When demand and sales are high and give promise of being sustained, American businessmen generally need little prodding to expand their productive facilities. And even when demand is sluggish, they seem ready enough to improve the efficiency of their capital stock in order to reduce unit production costs.

Today, with substantial American productive capacity still idle, demand must catch up to insure a sustainable investment rise. Since domestic sales are the major support of most of our companies that also export overseas, rising demands in our home market coupled with a more strenuous effort to sell abroad are now needed to set the stage for a durable investment boom.

Even the most generous investment credit handout cannot stimulate private investment for long in the absence of adequately rising demand.

The findings of the Wall Street Journal's survey support this conclusion completely. It found many concerns are now worried "by excess capacity, which makes spending large sums of money for new machinery seem to them a dubious proposition regardless of tax laws." As one business executive put it, "the problem now is trying to find markets for our present production, not getting money to make more."

With much of our already existing productive capacity still idle for lack of orders, further tax benefits for business should be given the lowest priority. For this reason, and the additional fact that the productivity of new capital investment constantly is rising and multiplying the potential output of goods and services which must be sold, highest priority today should be given to tax policies which broadly stimulate consumer demand.

The kind of spur business needs most is the durable stimulus of rising family spendable income, which lower income taxes for the middle and lower brackets could now help provide. Instead of squandering the revenue from loophole closing on an unwarranted tax credit scheme, it would be far wiser to use it to cut personal taxes and raise consumer demand.

Last spring, when spokesmen for American business were testifying before the Ways and Means Committee, they appeared to be cool to the investment tax credit plan. We assume that this was not to any desire to reject this lush multibillion-dollar bonanza out of hand, but rather because they preferred to bargain with the Federal Government for a further increase in depreciation allowances, which they cherish even more.

Depreciation set-asides are entered on the books as a cost of doing business; when depreciation allowances are liberalized, after-tax profits are held down. The investment credit, on the other hand, would have the effect of raising profits after tax. In this form, windfalls are more visible and can be embarrassing. What is more, because faster depreciation writeoffs raise bookkeeping production costs, they invite price markups. A tax credit, however, prevents price distortion.

Although depreciation benefits already have been liberalized twice, in 1954 and 1958, the Treasury recently announced that it is increasing them still further through an overall downward revision of its "useful life" Bulletin F schedule of depreciable business assets. It is estimated that this administrative adjustment alone will increase depreciation set-asides by about \$2½ billion annually. In our view, the actual useful life of a business asset is the proper depreciation rate yardstick—no more and no less. If inequities exist under the old Bulletin F schedule, because of an accelerating rate of capital replacement, the AFL-CIO supports their removal.

Having won their faster depreciation write-off victory over at the Treasury, however, the business community apparently decided to seek a second victory by substituting a still faster depreciation writeoff scheme in lieu of the administration's tax credit proposal. Until hours before the House vote this was the Republican plan, and it was finally abandoned only for reasons of political expediency.

However, whether the additional \$1.2 billion business tax benefit had been gained via the investment credit or the still faster depreciation writeoff route, in our view makes little difference. Either way, the deck is loaded against the average taxpaying family and the national interest.

How should we resolve the balance-of-payments problem?

If the investment credit is not the way to meet the balance-of-payments deficit, then how do we effectively cope with this continuing national problem?

According to a report of Secretary of the Treasury Dillon a week ago, the basic dollar deficit of the United States as a consequence of all our transactions with foreigners except the international ebb and flow of short-term capital, was \$600 million in 1961. This was a very substantial reduction from the basic deficit of \$1.9 billion in 1960 and \$4.3 billion in 1959. The growth of our trade surplus from \$1 billion in 1959 to \$4.7 billion in 1960 and \$5.5 billion in 1961 largely accounts for this reduction.

As long as governments continue to settle their international transactions by a transfer of the world's limited supply of gold, countries with adverse balances and too little gold are faced with trouble. For this reason, the United States, with its postwar hoard of gold, has taken drastic and generous steps to help other nations that have, or had, too little. Now that postwar reconstruction and prosperity have been achieved by many nations, some now find themselves in possession of a growing accumulation of gold and dollars. On the other hand, in recent years America's international accounts have gotten out of balance and our gold loss has been substantial. Steps to rectify this situation are clearly necessary.

There are many things that can be done.

In the first place, the administration's effort to insure greater opportunities for the sale of U.S. products in world trade through tariff reduction, must be supported.

Second, it is imperative that other prospering nations that enjoyed our generosity during the postwar years now shoulder a larger share of the rising cost of economic and military aid and of maintaining international institutions.

What is more, we must now institute a system of offshore procurement in reverse. Just as a few years ago we wisely build up the dollar earnings of other nations by buying military and other supplies from them, other countries now must be encouraged to buy from us, particularly those who are directly receiving or indirectly benefiting from our aid.

In addition, special inducements to export American capital due to the unwarranted and outdated preferential tax treatment we still accord income earned abroad, must now be ended as requested by the President. The bill before you goes only part of the way in closing these loopholes. Completing the job, as we will point out later, will reduce the balance-of-payments deficit and recoup \$250 million in needed revenue for the Treasury.

If further drastic steps are needed—and other countries have not hesitated to use them when confronted by a payments crisis—the movement of private capital abroad should be restricted and directed in accordance with priority national needs. Moreover, the travel outlays of Americans abroad could be further limited, temporarily. Under any circumstance, a far more vigorous effort to encourage foreign tourists to visit and spend in the United States must now be undertaken.

A combination of some or all of these measures will end the balance-of-payments problem. Although the administration is already pushing some of them a greater effort is needed.

Finally, we should also strive to raise our export surplus still further, although there must be a realistic limit to our expectations. The economic resurgence of other countries and the reduction of tariff barriers amongst them are inevitably creating sharper competition for America. It is well to recall that the era in which our industries alone remained unscathed by the devastation of war has receded far into history. What is more, many nations must, indeed, "export or die"; in our zeal to sell abroad we must not undermine the economies of our friends.

However, instead of rushing to enact the blunderbuss investment credit scheme in the name of spurring exports—which would only distort economic growth at home and impose an unjustifiable and costly burden on the taxpayer—we should be shaping wiser and less expensive policies to spur sales overseas.

American businessmen themselves should work harder to sell to potential customers abroad and to compete more effectively at home against imports as well. As a dramatic example of this need, it is important to recall the costly failure of the automobile industry to anticipate the growing domestic and foreign preference for compact cars. As a consequence, our loss of sales and of dollar exchange in both areas was tremendous. Although foreign trade has been vitally important to a few American industries, exports still account for less than 5 percent of the sale of America's total national product. For this reason, export potentialities have not been a major preoccupation of the business community or even of the Federal Government, until recently. The balance-of-payments problem clearly requires a change of view.

What is more, money now being sought for the wasteful investment tax credit should

be selectively used and be limited to the creation of a variety of aids that specifically encourage a favorable U.S. balance of trade.

While international agreements should properly prohibit aids that lead to the dumping of goods overseas, much can be done—and now is being done by other governments—to legitimately stimulate exports.

In the first place, if an investment tax credit has validity it should be restricted to enterprises engaged in production for export or in strenuous competition with imports.

Secondly, the granting of one or another form of direct tax concession related specifically to levels of export sales, might well be explored by this committee. However, such tax benefits, including investment credits, should be allowed only temporarily, for as long as our balance-of-payments deficit continues.

Furthermore, low-cost credit for loans for oversea customers and low-cost insurance to cover the commercial and political risks associated with foreign sales, must be made more widely available. Toward this end, the activities of the Export-Import Bank must be increased.

In our view, this committee would perform a great service by thoroughly studying the feasibility of these and all other export stimulating alternatives. We are advised that as long as these devices do not result in lower selling prices abroad than in our own domestic market, they are not barred by any international pact.

We are convinced that wise selection from among many constructive available means of attacking the balance-of-payments problem—short of resorting to the costly and unwarranted across-the-board investment credit—will bring results.

CLOSING TAX LOOPHOLES

Tax withholding on dividend and interest income

One of the important features of the bill before you is that it will withhold dividend and interest income tax purposes, in accordance with the President's request.

This proposal imposes no new tax; it simply would enforce payment of what has long been due.

Gross discrimination now exists between wage and salary income and dividend and interest income because withholding applies to one and not the other.

The withholding system leaves no room for the forgetful, the neglectful, or those who would deliberately try to avoid payment of taxes. Uncle Sam receives his due share of wage income almost at the same time that the wages are paid to the worker.

As a result of withholding, 97 percent of all wage and salary income is reported on Federal income tax returns. Because no withholding system applies to dividends, to interest, or to any other type of income, a far larger proportion of this income is not reported in income tax returns. Treasury data shows that for 1959, 9 percent of all dividends and 35 percent of all interest remained unreported. It is estimated that the total of unreported income in these two categories amount to \$3.8 billion.

As long as the withholding system applies only to wages and salaries, a gross injustice exists which forces wage and salary income to pay a greater share of the tax burden than other types of income. Clearly the answer is to equalize this treatment by instituting a withholding system on other types of income.

What have been the objections to this proposal? Some of those who regularly pay dividends and interest to holders of their securities have insisted that a withholding system would be too great an administrative burden for them to bear. However, it would be far less than the burden they now assume in withholding income taxes from wages and

salaries. Moreover, in the past few years, many firms have introduced mechanical operations into their dividend and interest payment procedures so that whatever additional bookkeeping is involved can be swiftly handled.

Another objection has been a concern that many low-income recipients not subject to tax would find their dividend and interest payments reduced by the amount of the withholding, and be forced to undergo personal hardship while awaiting refunds from the Treasury.

This is a problem of but minor proportion.

In the first place, Treasury figures reveal that only 11 percent of unreported dividends, and 29 percent of unreported interest is received by taxpayers with incomes below \$5,000. The great bulk of it belongs to those with higher incomes.

What is more, for those with low incomes the bill before you provides for an equitable arrangement whereby individuals who expect no tax liability can avoid withholding, as can all individuals under 18. Besides, married couples with less than \$10,000 income and individuals with less than \$5,000 can receive quarterly refunds if they expect to have less tax liability for the year than the amount withheld.

BYRD EMPHASIZES INJUSTICE TO STRUGGLING SMALL BUSINESS

Mr. PROXMIRE. Mr. President, I wish to refer to another point, which was developed at the hearings when I appeared before the Finance Committee and testified against the proposed investment credit. A very excellent point was made by the chairman of the committee, the Senator from Virginia [Mr. BYRD]. He said—and I think this should not be missed, and I wish to discuss it now:

The CHAIRMAN. Just one more comment, Senator.

The more you consider this plan the less effective it will be, I think. Now, you take a struggling young industry. They frequently have to lose money for some years in competition with some well-established business. Then the well-established business will take 8 percent credit on its taxes, the struggling young business that hasn't got firmly established and wasn't up to that time enabled to make a profit would get nothing.

I think the chairman of the committee was absolutely correct, and I think this can often happen. I know the small firm with which I was once associated had a similar experience. Any struggling, young firm can expect to lose money for quite a time. When, a little later, it wishes to buy a piece of equipment costing \$1,000, in competition with a big competitor, the small firm has to pay \$1,000 for it, for it has no past operations to constitute a basis against which to take a tax credit. So the struggling young firm would not find the proposed tax credit of any use to it. Meanwhile, its big competitor could, under this proposal, purchase the same piece of equipment, but would not have to pay \$1,000 for it; it would have to pay in effect only \$930, net, because it would have the benefit of a \$70 credit under this proposal. So under such circumstances the new, struggling firm would be at a real competitive disadvantage.

The statistics show that over 300,000 American corporations lost money last year, and that large numbers of individual proprietorships—all of which are

small—made little money, and that even those which made money would have received only a limited amount of credit from this source.

A moment after that statement by the chairman of the committee, I said:

Senator PROXMIRE. It favors the stable company which is earning a substantial amount, and reinvesting amounts over the years, and now growing. It disadvantages the growing company and especially the growing small company.

BASIS FOR A.T. & T. OPPOSITION TO \$75 MILLION GIFT

Mr. President, one of the most impressive appearances before the committee was made by Alexander L. Stott, vice president and comptroller of the American Telephone & Telegraph Co., because that company stands to gain \$75 million after taxes, every year, as soon as this proposal goes into effect. Why does this firm oppose it? Mr. Stott testified:

The Bell System construction program for 1962 is approximately \$2.8 billion and it will probably remain in this general area in the immediate future.

This construction is designed to meet the needs of the public for telephone service. We have an obligation to construct adequate facilities to meet this need. Clearly, it would not be economically desirable to build excess plant merely to obtain a tax credit. The Bell System companies have been able, under sound regulation, to obtain the additional amount of new capital from investors required to carry on construction of new facilities. Therefore, we can see no justification for using tax moneys to help finance our expansion. As the proposed incentive now stands, our business would obtain substantial benefits whether its construction were increased or not. For example, under a 3-percent rate our credit would be in the range of \$75 million for 1962; at a 4-percent rate it would be about \$100 million; and at an 8-percent rate it would be about \$200 million. If we received this credit we would be taking money from the taxpayers for expansion which we believe should properly be obtained from investors.

He went on to document that in spades.

I ask unanimous consent to have the excellent statement submitted by Mr. Stott, on pages 897 and 898, printed at this point in the RECORD, because I think it is very rare to have a situation in which a firm at any time turns down \$75 million a year.

There being no objection, the excerpt from the hearing was ordered to be printed in the RECORD, as follows:

STATEMENT OF ALEXANDER L. STOTT, VICE PRESIDENT AND COMPTROLLER OF AMERICAN TELEPHONE & TELEGRAPH CO., ON H.R. 10660

This statement is made on behalf of the Bell System companies to give our views on the proposal in the pending legislation for an incentive tax credit and other matters. Because the Bell System is a heavy user of capital equipment, it has always had a keen interest in construction and depreciation matters. In recent years the construction program of the Bell System companies has been running in the neighborhood of \$2.5 billion a year.

There can be no disagreement with the objective of stimulating modernization and expansion of the Nation's productive facilities. If our Nation is to create the jobs needed for its expanding work force and improve our competitive position in world markets, our productive facilities must be rapidly modernized.

Since the purpose of the incentive tax credit is to promote construction and growth, the question is whether it would have that result. As far as the Bell System companies are concerned it will not. Apparently this is also true of many other companies. On February 8, 1962, the Wall Street Journal published the results of a survey it had made of the plans of 68 large corporations. All except 1 stated that their construction programs would not be significantly affected if the proposal should be enacted, and 29 stated that the credit would not change their capital spending plans at all.

The Bell System's construction program for 1962 is approximately \$2.8 billion and will probably remain in this general area in the immediate future. This construction is designed to meet the needs of the public for telephone service and we have an obligation to construct adequate facilities to meet this need. Clearly it would not be economically desirable to build excess plant merely to obtain a tax credit. We have been able, under sound regulation, to obtain from investors the additional amount of new capital required to carry on our construction of new facilities. Therefore, we can see no justification for using tax moneys to help finance our expansion. As the proposed incentive credit now stands, our business would obtain substantial benefits whether its construction were increased or not. For example, under a 3-percent rate we estimate that our credit would be in the range of \$75 million for 1962. At a 4-percent rate it would be about \$100 million, and at an 8-percent rate it would be about \$200 million. If we received this credit we would be taking money from the Government which we should obtain from investors and not the taxpayers.

The investment credit is not a step toward needed tax reform. Rather, it is a subsidy to spur new construction by reducing the cost of acquiring new equipment. We do not think that business needs a subsidy to expand—it needs basic tax reform. In any case we are convinced that it would not be sound tax policy to offer a subsidy until faults in the present tax structure have been remedied. The credit may prove to be a windfall to many rapidly growing companies which would expand in any event. But it would be of little help to those companies whose plant and equipment is in the most need of modernization. Since one taxpayer's subsidy is another taxpayer's penalty, the credit would introduce an undesirable area of discrimination as among taxpayers. Furthermore, if the private enterprise system as we have known it is to remain strong and healthy, we believe it would be a mistake to take a step which may tend to cause business to look more and more to the Government to solve its problems.

It has been stated that the incentive credit is only part of the proposed program for spurring economic growth and that the other component would be a downward revision of depreciable lives set forth as guidelines in Bulletin F. On January 18, 1962, the Secretary of the Treasury said, "I consider our program of depreciation reform (Bulletin F)—including the investment credit—a central part of our economic policy." If the proposed incentive credit becomes law, there is a distinct possibility that it will be regarded as providing tax depreciation reform, and true reform will be long deferred.

Revision of Bulletin F may be useful in some areas. It should be kept in mind, however that Bulletin F is only an administrative guide, specifying average service lives for property by industry groups. Actual depreciation allowed for tax purposes is seldom derived solely by reference to these guidelines. This situation would not be changed simply by having the Treasury Department issue a new bulletin listing shorter

lives. Such action would certainly be of no value to us and we suspect the same would be true for many other businesses. In our case, depreciation rates are established on the basis of our own detailed engineering studies. As a matter of actual practice, the depreciation which we claim for tax purposes is based on rates prescribed for our companies by regulatory authorities for accounting purposes.

In my opinion it is important to understand why the Nation has fallen behind in modernization and expansion of productive facilities. High tax rates, and inflation in the postwar years are clearly at the root of our trouble. Depreciation allowances for tax purposes have failed to recover the purchasing power of the investment in plant being used up in providing goods and services, taxable income has been overstated, and capital has been taxed under the label of income. To main the purchasing power of its investment in plant and equipment, business must replace the capital eroded through taxation, either by undertaking outside financing or by retaining more earnings in the business. Many businesses have not been in a position to replenish their capital by these methods and so have not been able to keep their plant and equipment up to date. Furthermore even where businesses have been able to obtain the capital needed to offset this erosion, they have put a burden on the savings of the country and have reduced the amount of capital that otherwise would have been available for expansion of the economy.

We believe that the first and most important step to stimulate modernization and expansion should be basic tax reform to permit depreciation allowances adequate to preserve the purchasing power of the investment in the productive facilities of the Nation. Such depreciation allowances could be calculated by adjusting the depreciation determined on the basis of the number of dollars originally invested in plant by the changes in the price level between the year of investment and the current year. The purpose of price-level adjustment of depreciation is to allow for changes in the general purchasing power of the dollar and not for changes in the price of particular assets.

We realize that many methods have been advocated for improving tax depreciation allowances and on the basis of studies we have made, we are convinced that price-level depreciation would be the fairest method for all concerned; that is, the public, business, investors, and the Treasury. But, whatever depreciation methods are adopted, effective control of tax depreciation can be achieved through a requirement in the tax law that the taxpayer may not use for tax purposes any depreciation method that is more liberal than the method used in his books of account. Since generally accepted accounting principles require realistic depreciation methods for financial reporting and accounting purposes, this requirement would protect the Government's tax revenues by preventing the use of fast depreciation methods for tax purposes where such methods cannot be justified for financial reporting purposes.

By recognizing changes in purchasing power in the computation of depreciation allowances for tax purposes and requiring that no more liberal tax depreciation methods may be used than are used for accounting purposes, substantial amounts of new funds would become available for modernization and expansion to businesses with an appreciable investment in productive facilities. All businesses would obtain relief on an equitable basis, and businesses with the greatest need for modernization would share in the relief. Furthermore, whereas the expected cost of the proposed incentive credit is currently estimated at about \$14 billion, without including any changes in depreciation tax treatment, the cost of recognizing

realistic depreciation deductions based on purchasing power, with appropriate safeguards, would be about \$2 billion. We are convinced, too, that inadequate depreciation allowances for tax purposes have been holding back growth and that realistic tax depreciation allowances which reflect the change in the purchasing power of the dollar are a necessary condition for a dynamically growing economy.

I should like to comment briefly on two other subjects which were mentioned during the appearance of the Secretary of the Treasury before your committee earlier this week. These are, first, the suggestion to change the restricted stock option provisions presently contained in section 421 of the Internal Revenue Code and, second, a proposal to eliminate the \$50 dividend exclusion and 4-percent dividend credit presently available to individuals. Any major changes in these provisions would seriously impair our ability to continue to obtain the amounts of new capital needed in our business.

Mr. PROXMIRE. Mr. President, I wish to refer briefly to the testimony of another witness, one who favored the proposed investment credit, Mr. Arthur J. Packard, president of the American Hotel Association, which represents, as he said, an industry which has 29,000 hotels and 41,000 motels. He favors the proposed tax credit. He said:

Let me deal first with the provisions in the bill relating to the proposed 7-percent investment tax credit.

We can see why this proposal becomes politically potent, because in these circumstances the 29,000 hotels and the 41,000 motel proprietors have a solid financial reason for influencing Members of Congress, to enact the law. It is to be assumed that that is what they would do. But certainly the argument in favor of providing such a tax credit—as that argument was made by Mr. Packard—is very, very weak. He said:

We believe this approach is sound and particularly applicable to the hotel industry. Although hotels have engaged in substantial modernization programs since World War II, there is still a vast area in which hotels could modernize even farther to meet increased competition within the industry.

Of course that makes no sense at all. If they are going to modernize, in order to meet competition within the industry, and if the whole industry gets the credit, the whole industry will be able to modernize, and then all of them will be in exactly the same competitive position that they were in before.

I think the Senator from Tennessee [Mr. GORE] and the Senator from Illinois [Mr. DOUGLAS] brought out the point that the main thrust of the proponents of this measure would be to make our businesses more competitive with businesses abroad. But to make American hotels more modernized than hotels in Italy would have no really helpful effect on our economy, even if the investment credit worked and the evidence is overwhelming that it wouldn't work.

The real point in connection with Mr. Packard's statement was brought out in the following testimony:

The CHAIRMAN. You say the occupancy rates have dropped every year from 93 percent in 1946 to 62 percent in 1961.

Does that include all the motels and hotels both or what does it include?

Mr. PACKARD. That is right.

In other words, it includes both.

Obviously, if their vacancies are increasing—if they now have only 61 percent occupancy, instead of 93 percent—the last thing in the world they need is an incentive to build more motels and more hotels. I suppose some of the money would be used to make their existing facilities more attractive; but under these circumstances to build additional units would be just as stupid as the Small Business Administration policy of making loans for the construction of more hotels or motels over the country. In the present overbuilt situation, that is sure to cause even more forced selling.

RETAILERS WANT CREDIT ON PARKING LOTS

Mr. President, there is also in the RECORD a statement by Allen P. Lucht, treasurer of the Federated Department Stores. He pleaded for a little more generous definition of depreciable property. He pointed out all the benefits the retailers expect to get out of this proposal if it is enacted into law. I think a reading of his testimony, as it appears in the hearings, provides about as good an argument against the proposal as I have seen—even though he favored the proposed investment credit.

For example, he said:

The Ways and Means Committee report mentions specifically that the parking lot of a factory is not used as an integral part of manufacturing. It is for the benefit of the employees of the factory. However, the retailer's parking lot is an entirely different category. Present day consumer habits have made the customer parking lot a vital necessity. The retailer who does not have one soon falls behind in our highly competitive system.

Therefore, he said, he wanted to see a 7-percent credit made available for parking lots. No doubt he could get one under this proposal. I suppose it could be argued that a parking lot is depreciable property—that in time it will depreciate; and I suppose it does. But this does not contribute to our growth, and that would be the wasteful consequence the proposed tax credit would have on our economy.

BRISTOL-MYERS OPPOSES CREDIT

The next to the last witness whom I want to quote tonight is Walter H. Kamp, financial vice president of Bristol-Myers Co. Mr. Kamp, representing the drug industry, appeared before the committee and testified as follows:

1. INEFFECTIVENESS

As I understand it, the basic purpose of this credit is to stimulate industrial expansion and modernization and thereby promote economic growth and fuller employment. Certainly, all of us are in full accord with these objectives. However, good intentions notwithstanding, the investment credit proposal will be almost completely ineffective in achieving these objectives. If it were not for the fact that any reduction in taxes releases additional funds for expansion or other corporate purposes, it could be stated with assurance that this proposal would be wholly ineffective in stimulating industrial expansion and modernization.

However, I do not believe that the investment credit is a good method of reducing Federal income taxes since the proposed investment credit will be of the least help to those it is primarily designed to help; i.e.,

industries lagging in the modernization of plant and equipment.

You will note that I have purposely omitted from this category expansion in the productive capacity of our industrial enterprises. As one who has seen his own company's sales grow from \$6 million in 1929 (the year in which I joined Bristol-Myers Co.) to over \$164 million in 1961, I can state without hesitation that if the economic factors are right—i.e., growing consumer demand for a company's product, a reasonable price to the consumer, and an adequate return on the investment required—industry will provide its own expansion of industrial facilities and productive capacity without any need for an investment credit provision. Certainly, this has been the experience of our company throughout the entire period of my 33 years' association with it.

To return then to those industries lagging in the modernization of plant and equipment, this is due generally to either a lack of cash or unfavorable economic factors.

If the problem is lack of cash, the investment credit provision will be of no help whatsoever, because in order to obtain a tax credit of \$100,000 a company would first have to pay out \$1,400,000 for the purchase of new equipment. Obviously, if the company were short of cash to begin with, it certainly wouldn't have \$1,300,000 net to lay out for new equipment. On the other hand, accelerated depreciation could apply to equipment already purchased and would thus involve no additional cash outlay, but the savings in taxes accomplished thereby would be immediately available for either additional new equipment or the replacement of obsolete equipment.

If, however, the lag in modernization of plant and equipment is due to unfavorable economic factors, no 7-percent discount in the purchase price is going to answer or substitute for the solution of the basic underlying problems.

To summarize, then, the investment credit provision will help those people who do not need help and will be completely ineffective in helping those people who need help.

I suppose if I were a defeatist, I might say that the chances of ever obtaining any reduction in corporation taxation are infinitesimal, and therefore we ought to grab any opportunity for tax reduction that is offered us. Fortunately, our company was never built upon defeatism, and therefore my colleagues and I feel that we must oppose this investment tax provision even though—short range—it might be of immediate benefit to us. I hope you will bear with me if some of the points I make in succeeding paragraphs have already been covered by others in these hearings.

2. REVENUE LOSS

At a time when we are already faced with a substantial deficit for the current fiscal year, and the probability of an even greater deficit for the 1963 fiscal year, it would appear most unwise to increase these deficits by a costly giveaway program of highly doubtful effectiveness which business in general does not want and which, in my opinion, would be unsound at any time.

3. DISCRIMINATORY EFFECTS

As I tried to point out in section 1, the application of this provision would be highly discriminatory in its effect upon varying industries, and taxpayers who cannot qualify for the favored treatment—i.e., those who most need it—will, in effect, have to bear the load for the benefits granted to the favored few.

4. GOVERNMENT INTERFERENCE AND CONTROL

The enactment of a provision of this nature would create an extremely dangerous precedent leading to the encouragement or discouragement of any particular segment of private enterprise, depending upon the whim

or mood of the moment. Today it is an investment credit for new machinery and equipment. Tomorrow it could be an investment credit for industrial development in Africa, Latin America, Oshkosh, or Timbuktu. The scope of such favored and discriminatory treatment is limited only by the imagination of those proposing it.

In conclusion, may I say that the investment credit concept is moving far afield from the basic purpose of tax legislation; i.e., to raise the necessary governmental revenue with the least possible disruption of normal business practices.

May I thank you for granting me this opportunity of appearing before you on behalf of my company.

KEYSERLING CALLS TAX CREDIT WRONG ON EVERY SCORE

One of the most articulate economists in the country, and certainly one of the most imaginative, is Leon Keyserling. Mr. Keyserling cannot be said to be one who parrots the line of the National Association of Manufacturers or chambers of commerce. He was the Chairman of the Council of Economic Advisers under President Truman. He was chief economist for some time, as I recall, for outstanding labor organizations. He has been a teacher and a Government economist of high repute. This is what he said about the tax credit:

It seems to me a provision which business does not seek, labor does not want, the condition of the Federal budget does not justify, the state of the national economy does not call for, the full consequences of which the public does not appreciate, and which even those economists who favor it have not been able to support with careful or specific empirical analysis. The proposal cannot stand the test of logic; it should not survive the lessons of experience.

Then he goes on to recall a very interesting and to me a very persuasive analogy. He says:

The Chairman of the Federal Reserve Board and the Secretary of the Treasury, before this committee in early 1957, shortly before the Chairman proposed his extensive investigation of the financial conditions of the United States, said that we needed more plant, we needed more investment, we needed more savings; the level of consumption was too high. We were faced with a great inflationary threat. They used this in justification of the tight money policy. They used this in justification of the amortization schedules and benefits taken out of the Treasury, with which business was then being pried.

Before this committee on the record in early 1957, I said that we were in oversupply on everything; we were moving straight toward an economic recession. We had a deficiency of demand relative to our plant capacity.

The members of this committee asked the proponents of the tax amortization to run around and tell where the shortages were, and this is all on the record, they were able to find only one type of lead type.

Lo and behold, the recession came, and it was the most serious recession since World War II.

Lo and behold, Mr. Martin, Chairman of the Federal Reserve Board, came back to the same committee in 1958 and he said, in substance, that, looking backward, we had an investment boom which was too fervid relative to the demand, and that is why we had a recession.

In other words, this was a complete acceptance of what I had advanced before the committee 1 year earlier.

The argument that Mr. Keyserling made is that what happened in 1957 resulted from having provided incentives for plant and equipment which resulted in a boom in plant and equipment in 1955 and a serious recession following, because demand was falling off. That is exactly what investment credit will do. Keyserling documents it in spades. He goes on to say this:

I said at the beginning of my testimony, and I did this deliberately and advisedly, that we should have had \$90 billion more of business investment over the last 9 years, and then we would have been more competitive. We would have had more technology, we would have had more productivity. I think we should have a much higher level of business investment, over the next few years, than we are going to get.

But we are not going to get it by repeating the same errors which prevented us from getting it over the last 9 years, because business investment feeds on utilization, and merely to fan once again a fervid investment boom which gets the existing idle plant capacity, how is this in the long run going to provide a healthy climate for business investment? That is the first point.

The second point is that there has been a tremendous exaggeration of this whole international problem, as a scare device for pumping the Congress and the country into approving something that the Treasury has worked out.

Let me illustrate which I mean. I am for the trade program, although I am not prepared to debate it here. I think it will improve our foreign trade position. I think it will improve our balance of payments. I think it is a good step on international political grounds.

But for us to think, for us to think for a second, that even if the trade program were passed immediately, and even if it had optimum results, it would yield more, than a \$2 or \$3 billion annual gain in the performance of the American economy—I do not think there is a single economist who studies this subject in the whole United States who will be found to say that it will add more than \$2 or \$3 billion a year to our net performance position. I do not think it will add that much.

He refutes argument that plants overseas are more efficient than the plants in this country. He says:

Of course, steel plants in India are newer than in the United States. India did not dream of a real steel industry until just a few years ago.

Of course, steel plants in Germany and in Japan are newer. They were bombed out a few years ago. On the average they are newer.

If we were bombed out and recovered, ours would be still newer. Of course, some of the plants are newer in Italy, France, and some of the other European countries, because they have lagged so far behind us, because they have really started their industrial development so very much later than we have.

He points out that when one goes over there and travels around, he has to travel a long time and look at much equipment and many plants before he finds one that compares with a typical American factory, in efficiency or capacity of equipment.

I read from his statement:

It is argued that, if we have a higher level of business investment, we will have a higher ratio of investment to the size of our economy, and if we have a higher ratio of invest-

ment relative to the size of the economy, we will grow faster.

Well, point 1, as I have already said, you won't have a higher investment, relative to the size of your economy. You will have a smaller investment, because you will merely repeat what happened during the last 9 years, which turned investment down more than anything else because it is the most volatile sector.

Let us examine the argument itself. It is just like saying, because red blood corpuscles make a man strong, that if he has nothing but red blood corpuscles, he will be as strong as Hercules.

If he has nothing but red blood corpuscles, he will die.

The problem is, What is the ratio of the red blood corpuscles to the white blood corpuscles, to the whole man, which will keep him strong?

CONSUMER DEMAND NOT INVESTMENT INCENTIVE NEEDED

This is the point. We have been pouring on incentives for investment, when we do not need incentives for investment. This is the one area of our economy which is moving ahead, which has been built up, which has had every incentive over the past 8 years, including a big incentive this year already.

How do the proponents of a tax proposal justify the right ratio?

First of all, they look overseas. Everybody likes to look overseas now, and they say, "Why, in Japan the ratio of investment to the total economy was 40 percent."

Sure. But that is not sustainable. It is not going to be 40 percent when Japan is rebuilt. If we were bombed out and rebuilt our ratio would be 40 percent, too.

He goes on to point out that that seems to be true elsewhere.

There was a brief colloquy between the Senator from Delaware [Mr. WILLIAMS] and Mr. Keyserling which I think beautifully summarizes the situation on balance of payments and balance of trade. The Senator said:

First, as I understand your argument, you do not think that the adoption of this investment credit would in any way improve our balance-of-payments situation; is that correct?

Mr. KEYSERLING. I think it would worsen our balance-of-payments position in the sense that being an undesirable American economic policy it would worsen our economic performance, so this, in turn, would worsen our balance-of-payments position.

Senator WILLIAMS. I understand that it is your opinion that the adoption of this investment credit plan would, in effect, be starting an unwarranted subsidy for American industry.

Mr. KEYSERLING. Well, this ties in with your first question.

Then there was a colloquy with the Senator from Tennessee [Mr. GORE] on the impact of international trade. The argument was made that the investment credit of \$1.4 billion would have a massive effect on our foreign trade situation and that somehow our favorable balance of trade, which is now, as I previously pointed out, about \$5 billion a year including foreign aid and \$2.6 billion excluding foreign aid, would be improved a great deal. The Senator from Tennessee [Mr. GORE] pointed out how impossible this was in terms of simple arithmetic.

The Senator asked Mr. Keyserling:

Ten percent of this credit, \$1.4 billion, would be \$140 million.

Mr. KEYSERLING. Yes, sir.

This is apropos of the position the Senator from Tennessee [Mr. GORE] had taken that only 5 percent of our economy is involved in foreign trade but, being more generous, he would allow 10 percent. The Senator said:

I ask you, by what logic can we assume that a tax credit of \$140 million is going to improve the balance of payments by \$2, \$3, or \$4 billion?

Mr. KEYSERLING. We cannot; we cannot.

Senator GORE. I just do not see it; I agree with you.

Mr. KEYSERLING. Furthermore, Senator, it is worse than that because the method that you have used is in itself an exaggeration because you cannot say that if you have a tax credit of \$1.4 billion, and since 5 percent of the economy is engaged in trade, there is going to be a 5-percent ratio. This is not the way it works.

What the proponents of the tax credit are saying is that this tax credit, by more efficiency, will result in reduced prices, and that these reduced prices will enable us to sell more goods overseas.

When you bring that additional step in, you get down to a lot less than 5 percent, because you have to say, first, here is a certain credit to industry. This is going to change their investment pattern so much.

Now according to the judgment of Business Week, they are going to invest 1 percent more than they otherwise would, or about \$300 million more in 1962. Now by your method, we apply 5 or even 10 percent to investment in production for foreign trade.

The effect would be, we have learned, that the firms engaged in foreign trade would probably increase their investment in plant and equipment \$15 million, that is 5 percent of \$300 million.

Since foreign trade involves some \$20 billion a year, \$15 million is only a drop in the bucket and would have only an insignificant effect.

DOUGLAS-GORE DISSENT A MASTERPIECE

Mr. President, I wish to summarize. I think one of the finest analyses I have seen since I have been in the Senate in any committee report was the job done by the Senator from Illinois [Mr. DOUGLAS] and the Senator from Tennessee [Mr. GORE] in their supplemental and minority views on the tax bill.

In the course of the dissent the Senator from Illinois [Mr. DOUGLAS] and the Senator from Tennessee [Mr. GORE] point out that the loss of revenue would be between \$1.1 and \$1.4 billion, which would be a very substantial loss. They emphasize the fact that the present provision is not an effective incentive, although it started out that way when the administration originally recommended it. It is no longer an efficient incentive, because it would provide a credit for all investment, even if a firm reduced the amount of investment it made. The result would be that the increased investment would offer a very small, very modest, very weak, very slight incentive for growth.

The Senators point out that all the surveys also agree that this would provide very little increased investment in plant and equipment. These surveys have been conducted by the most au-

thoritative and highly respected business groups. Then the Senators summarize, in a statement which I think ought to be brought to the attention of the Senate, for the emphasis is on what has happened to tax benefits in the past 8 years.

In 1954, accelerated depreciation, with the double declining balance and the sum of the digits methods, was authorized by Congress. This amounted to an initial loss of revenue to the Government of at least \$2 billion a year. This went to the industrial corporations and to the industrialists. At the same time the \$50 dividend exclusion and the 4 percent credit were passed in 1954 which gave \$400 million a year more to the owners of common stocks. This summer the Treasury has issued a new Bulletin F, permitting machinery and equipment to be depreciated much more rapidly. It is estimated that this will reduce business taxes by approximately \$1.5 billion a year. All of these taken together come to just short of \$4 billion a year.

Now we have this provision for the investment credit which will give the investors in machinery and equipment at least another \$1.3 billion annually. Thus, in 8 years we have decreased the annual tax burden on industry by over \$5 billion a year. This, of course, goes to the upper income groups in society who own the overwhelming proportion of the stock of American corporations.

During this period the low- and middle-income groups have received virtually nothing in the way of tax cuts. It is about time that the United States was less partial in its distribution of favors. This is true both on economic and ethical grounds.

The Senator from Illinois [Mr. DOUGLAS] and the Senator from Tennessee [Mr. GORE] also said:

The investment credit proposed is really a form of the trickle-down theory of economics which has largely been shown to be ineffective in the past. We believe instead in the theory that purchasing power should be built from the bottom up.

I think the Senators are correct. If we add to this loophole the kinds of amendments offered by distinguished Senators to the tax bill there could be a real drain on the Treasury this year.

Mr. President, in conclusion I wish to say that the reason that I have detained the Senate so long—I have spoken now nearly 4½ hours—is not that I am sadistic, but because I felt very strongly that this statement had to be made. It had to be made in a speech.

I suppose I could have sat down and typed up my remarks, and brought them over and put them into the RECORD. Somehow those actions have a way of being totally ignored. I think, somehow, this may achieve some degree of attention and understanding on the part of other Members of the Senate.

There is no more important tax bill which is to come before the Senate in the next several years. Certainly no more important tax bill has come before the Senate since I have been a Member of the Senate. As the Secretary of the Treasury rightly said, the "guts"—the heart and soul—of this bill is the investment credit.

I am speaking at length now because I know that if I did so on Monday, Tuesday, Wednesday, Thursday, or at any

time before we take action on the bill, I would be accused, and properly so, of delaying the Senate by engaging in a filibuster and tying it up. I am sure my address has imposed a very real discomfort and inconvenience on very tolerant people tonight. I am sure that if I did it at any other time, it would have imposed a far greater degree of inconvenience on more people.

SUMMARY

In conclusion, I am opposed to the investment credit because it is a tax cut.

I have been consistently opposed to a tax cut this year. I am opposed to a tax cut which the beneficiaries do not want and a tax cut which the largest business in the world has testified it does not want and would not have. They have said it would not work, and would be bad economic and social policy. That kind of tax cut, it seems to me, is ridiculous.

Not only is the subsidy not wanted, but the McGraw-Hill survey, the National Industrial Conference Board, the Wall Street Journal, and everyone who has studied the question agrees that it would not provide a stimulation of investment. It would not work.

Furthermore, at least 80 percent of the volume of the argument of Secretary Dillon is based upon how important it is to make us competitive with industry abroad, when the facts are overwhelming that we are leading industries abroad. The United States of America has a favorable balance of trade of over \$5 billion, and \$2.6 billion of that is entirely in the commercial private sector of our economy. That means if countries abroad have an unfavorable balance of trade, we have a favorable balance of trade to that extent. We are beating them. We are still the supreme nation of the world. That does not mean we cannot improve our economy. It does not mean we cannot hope that they can also improve their economies. Of course, we do. No argument can be made on the ground of economic competition because we are trading effectively.

The proposal is also bad because, whereas it started as an incentive on the marginal investment, on additional extra investment, now it is an incentive on the gross investment—all of it. So firms will get it even if they reduce their investment.

I point out also that it would cover the entire sweep of industry. It would cover bars, burlesque houses, parking lots, and supermarkets. It has no relationship whatever to industrial policy. It would cover every kind of equipment that is legal. It would cover slot machines and driving ranges.

Mr. President, the last thing that we need economically now is increased capacity at a time when our business plant is chugging along far below capacity. Why in the world should we cut taxes for the purposes of increasing that capacity further?

When we have done that in the past, as Leon Keyserling pointed out so well, what was the result? The result was a serious recession.

It seems to me that the proposal is one that cannot be justified.

I also point out that those who are opposed to the investment credit are as responsible, able, thoughtful, and disinterested a group of Senators as I think one could find. Of all the conservative Senators, none has won greater respect on the part of business and on the part of his colleagues than has the chairman of the Committee on Finance, the Senator from Virginia [Mr. BYRD] on the Democratic side.

On the Republican side the ranking Republican member of the Committee on Finance has been recognized as a man of absolute integrity. Some might disagree with him on public policy, but no one disagrees with his integrity and ability. I refer to the Senator from Delaware [Mr. WILLIAMS]. He is also strenuously opposed to the tax credit. So the Senator from Delaware [Mr. WILLIAMS] and the Senator from Virginia [Mr. BYRD] are opposed. Also the only professional economist in the Senate, the brilliant Senator from Illinois [Mr. DOUGLAS] is opposed. He has devoted his life to the study of economics. He taught economics at the University of Chicago. He won his doctorate at the age of 25, writing his thesis on the subject of wages, which is still a definitive work on that subject. He is emphatically opposed to the proposed investment credit provision. I think Senators will find very few people who have the great competence in the field of taxation than the Senator from Tennessee [Mr. GORE], or whose integrity and ability is more widely recognized. He is also emphatically opposed to the investment credit.

On the basis of the groups opposed to the measure, whether it be labor, business, or outstanding figures in American life, those distinguished Senators who have thought the issue through most carefully are opposed to the investment credit.

As I take my seat I wish to emphasize that the proposal is wrong because it is bad public policy. It is bad economic policy. It is a giveaway at a time when our Government cannot afford to increase its deficit further.

Mr. President, with sincere apologies for detaining the Senate so long, I yield the floor.

PESTICIDES A MIXED BLESSING FOR CALIFORNIA FARMERS

Mr. PROXMIRE. Mr. President, Mr. Lawrence E. Davies has written two detailed, informative articles about side-effects and problems that have resulted from use of pesticides in California. These articles, which appeared in the New York Times of August 24 and 25, provide an interesting supplement to the series of three articles by distinguished nature writer Rachel Carson that ran in the New Yorker magazine recently, and which will be published in book form in October.

By means of anecdote and description, Mr. Davies tells how West-coast beekeepers have established informal "warning systems" to alert one another about proposed chemical poison spray activities. With sufficient warning, bees can be removed from the areas before

the spraying takes place. This prevents the chemical from being ingested by bees and thus appearing as a residue in the honey they produce.

In other instances DDT residues wind up in milk after cows are fed on truck garden waste and byproducts—such as tomato vines and skins, lettuce trimmings, and sugarbeet tops—because the truck crops were sprayed during the growing season. Cows fed on untreated pasturage near sprayed areas have also produced milk containing DDT residues—since the chemical can drift considerable distances through the air to reach what Mr. Davies terms "guiltless fields."

Each of these examples, and the many others described in these articles, illustrates the need for caution and intelligence in the use of chemical poisons. Certainly it would not make sense to prohibit their use. Without modern chemical assistance, our agriculture could not produce the magnificent abundance of fruits, vegetables, field crops, livestock, and livestock products which has made possible a massive rise in diet standards. No one wants to see a return to the mosquito-infested bogs that were the state-of-nature before invention of DDT. But the very fact that proper use of chemicals can do so much good puts a heavy responsibility on the users to make certain that they do not have unpleasant side effects. And I would observe that an effort to talk the problem out of existence is doomed to failure. Widespread public concern has already been aroused and will probably increase when Miss Carlson's book is published.

I welcome the constructive attitude of the U.S. Departments of Agriculture and Interior—the two Federal Departments most concerned—toward this situation. In letters to me, these Departments described the measures used to guide and regulate the use of pesticides and the steps being taken to explore the matter further. From Mr. Davies' articles it appears that the State of California agriculture and public health authorities are also vigilant in their concern about possible ill effects resulting from pesticide use. Other State authorities, including those in my own State of Wisconsin, are doing an excellent job of coping with the problem.

But a problem it is, and it should be recognized as such. Moderate, workable, effective solutions can be found. Irrational public panic certainly is not called for—but neither is the blinkered approach of those who state no problem exists.

Mr. President, I ask unanimous consent that the two articles I have referred to be printed at this point in the RECORD.

There being no objection, the articles were ordered to be printed in the RECORD, as follows:

[From the New York Times, Aug. 24, 1962]
SPRAY WARNINGS AID BEE RAISERS—NOTIFICATION SERVICE EASES CALIFORNIA PESTICIDE FIGHT

(By Lawrence E. Davies)

It was time for another spraying of pesticide on a field of long-staple cotton outside Bakersfield.

Digest of CONGRESSIONAL PROCEEDINGS

OF INTEREST TO THE DEPARTMENT OF AGRICULTURE

OFFICE OF
BUDGET AND FINANCE

(For information only;
should not be quoted
or cited)

Issued August 28, 1962
For actions of August 27, 1962
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HIGHLIGHTS: Rep. Avery objected to request to appoint conferees on farm bill. House passed bill to extend International Wheat Agreement. House subcommittees voted to report bills for cooperation with States in administration of Federal laws, to increase FHA loan limitation, and for lease and transfer of tobacco acreage allotments. House passed bill for housing for elderly in rural areas. Sen. Morse commended study of Federal rangelands. Sen. Humphrey expressed concern over effects of radioactive fallout on milk. Sen. Wiley urged issuance of handbook on farm laws. Senate committee voted to report measure for designation of National School Lunch Week. Senate committee reported independent offices appropriation bill. Sen. Fulbright introduced and discussed bill for holding World Food Congress.

SENATE

1. **FORESTRY.** Sen. Morse commended the joint USDA-Interior study of Federal rangelands. p. 16669
2. **SCHOOL LUNCH.** The Judiciary Committee voted to report (but did not actually report) S. J. Res. 211, providing for the designation of a week each year as National School Lunch Week. p. D772
3. **FARM PROGRAM.** Sen. Wiley renewed his request for this Department to prepare a "simplified handbook on farm laws and programs," and inserted a letter from USDA on the problems involved in preparation of such a handbook. pp. 16667-8

4. MILK. Sen. Humphrey urged a ban on the testing of nuclear weapons, stated that last week dairy farmers in Minn. removed their cows from pasture because of the mounting accumulation of radioactive iodine 131 in local milk supplies, and inserted an article, "Minnesota Acts on Iodine in Milk." pp. 16741-7
5. INDEPENDENT OFFICES APPROPRIATION BILL, 1963. The Appropriations Committee reported with amendments this bill, H. R. 12711 (S. Rept. 1923). p. 16655
6. BUILDINGS. The Foreign Relations Committee reported with amendment H. R. 11880, to authorize additional appropriations for the acquisition of sites and buildings in foreign countries for use by U. S. personnel (S. Rept. 1925). p. 16655
7. TAXATION. Continued debate on H. R. 10650, the proposed Revenue Act of 1962. pp. 16672-5, 16676-735, 16748-9
Sens. Gore, Sparkman, and Cannon submitted amendments intended to be proposed to this bill. p. 16657
8. TRANSPORTATION. Sen. Kefauver stated that current proposals for railroad mergers is "one of the broadest and boldest attempts at economic concentration in the history of our Nation." pp. 16735-40
9. EDUCATION; PERSONNEL. Sen. Proxmire expressed concern over the decrease in college graduates in the field of engineering and inserted an article, "Government, Profession Seek Reasons for Drop in Student Enrollments." pp. 16658-60
10. WEATHER. Both Houses received from the President the National Science Foundation report on weather modification for fiscal year 1961 (H. Doc. 534). pp. 16654, 16637
11. FEDERAL REGISTER. Both Houses received from GSA a proposed bill "to amend further section 11 of the Federal Register Act, as amended"; to S. Government Operations and H. Judiciary Committees. pp. 16652, 16655
12. ECONOMY. Sen. Proxmire compared the growth of our economy with those of certain European countries and inserted an article, "Myrdal Calls United States Stagnant Economy." p. 16658
13. ELECTRIFICATION. Sen. Metcalf termed "grossly misleading and erroneous" a leaflet of the Mont. Power Co. "purporting to show that the proposed Knowles multipurpose project on the Flathead River is economically unsound," and inserted figures to support his position. pp. 16661-4

HOUSE

14. FARM PROGRAM. Rep. Avery objected to a unanimous consent request by Rep. Cooley to send H. R. 12391, the proposed Food and Agriculture Act of 1962, to conference. p. 16615
15. WHEAT. Passed under suspension of the rules S. 3574, to extend the International Wheat Agreement Act of 1949 so as to extend the authority granted under the act to cover any new or revised wheat agreement. This bill will now be sent to the President. pp. 16632-5
16. INTERGOVERNMENTAL RELATIONS. The Subcommittee on Departmental Oversight of the Agriculture Committee voted to report to the full committee with amendments H. R. 12802, to provide further for cooperation with States in administration and enforcement of certain Federal laws. p. D773

has been using the words "victory" and "win" but pursues the same policies.

Senator THURMOND's campaign drew the wrath of liberals and ultraliberals throughout the land. At first, even many relatively conservative men and newspapers were skeptical of his charges.

Facts, figures, old speeches, and other odds and ends produced by Senator THURMOND and sympathetic colleagues convinced many of the once skeptical people that real substance lay behind the accusations. Actions by the administration itself also validated many of THURMOND's claims.

That the Senator's charges have now forced the administration spokesmen to use words like "victory" represents one triumph. Now Americans must back him in his efforts to force a change in policies—from appeasing attitudes to firmness and positive action—if the Nation is to survive as a great world power.

[From the Columbia Record, Aug. 24, 1962]

BERLINER VICTIM OF NO-WIN POLICY

An 18-year-old East Berliner sought the freedom of the West last weekend and lost his life. He was shot off the infamous wall and lay groaning for nearly an hour only 200 yards from Checkpoint Charlie, the main U.S. command post.

Subsequently, infuriated West Berliners booed Americans, fought their own police, and stoned Soviet cars. Their anger was understandable. With justification, they asked why the American soldiers didn't help the dying young man.

The answer was given by an Associated Press dispatch from Berlin the day after the killing:

American authorities feared a new incident that might have had dangerous cold war repercussions.

Fear. Fear of escalation of a simple incident along a wall. Only a man's life.

Across the ocean, simultaneously, Senator STROM THURMOND, of South Carolina, was repeating his charge that the State Department—despite the use of the word "victory" and "win"—still was pursuing a "no-win policy."

What better illustration of Senator THURMOND's allegations could be found than the demonstration of fear as a young man, seeking freedom, lay dying—with no American to come to his aid?

"Though the words 'victory' and 'win' have now been used by Secretary Rusk," said Senator THURMOND, "there appears to be no change in the substance of the policies which underlies the name of the policies, whether they be called win or no-win. I commend the Secretary for facing up to his error in censoring these valiant words which had always been the watchword of America in previous times of national peril. I will be the first to congratulate the Secretary when he reverses his field on coalition governments and accommodations with and concessions to and Communists. He has prepared an appealing frosting for his cake. Now he needs to bake a new cake to go with the frosting."

But neither the President nor the State Department appears prepared to bake the new cake.

Quite recently, Stewart Alsop's delineation of Mr. Kennedy's goals in foreign relations left no doubt that there the President still clings to the hope that he can persuade international communism to "live and let live." Mr. Kennedy's insistent dedication to retaining "choices" in individual international entanglements foretells a continuance of accommodations.

Secretary Rusk, following the President's lead, has said that "when we are able to find common interests which the free world and the Communist bloc share we must be prepared to talk and negotiate about ways of acting together to fulfill these interests—even if they are narrow. By this slow process

we may move toward a dampening of such crises as Berlin, a continuation of our exchange programs with the U.S.S.R., and new ventures of common advantage, as in Antarctica, public health and outer space."

Wistful hope of this sort is not nearly so dangerous, however, as the dreadful fear of thermonuclear war which pervades administrative thought.

Exemplary is Under Secretary of State George W. Ball's frank admission that the struggle between the free world and international communism conditions much of what the State Department does. "The knowledge that this struggle, now characterized by the cold war, may flame into hot wars in remote corners of the globe and that those hot wars may escalate into thermonuclear holocausts is a kind of brooding omnipresence over all of our affairs."

Herein is the key to what Senator THURMOND has called the no-win policy. Although we now seem to be not afraid to speak of victory or winning, we are willing to concede or retreat to avoid escalating.

The Soviets are, thus, left completely free to escalate any situation anywhere in the world. The United States, thus, will always be on the defensive—fearful of a thermonuclear war.

Under Secretary Ball declared that the State Department sought to avoid creation of trying situations. "We attempt to anticipate and, where possible, prevent the development of situations which can result in a direct confrontation of the great powers—a confrontation that can readily lead to the escalation of force and a major war."

Hence, we agree with the Soviet Union on a troika arrangement for Laos, which dooms the southeast Asian nation to Communist-domination. Its fate awaits only the word of Khrushchev.

Hence, we also pressure our Dutch allies to surrender West New Guinea to Indonesia while the Dutch were being invaded.

Hence, we are willing to submit Moise Tshombe and his independence-seeking people of Katanga to the will of a disturbed Central Government of the Congo.

Hence, we allow a German teenager to bleed to death within the sight of American troops, who could have gone to his rescue. He was a victim of our no-win policy.

Previously, the President had summoned Gen. Lucius Clay home because his instantaneous reaction policy to Russian pressures in Berlin might, in the judgment of the State Department, have escalated individual situations.

Only the Russians can escalate.

How right Senator THURMOND was in his first criticism. How right he is today.

[From C. F. Childs & Co. Publication, Aug. 20, 1962]

WHAT'S NEW?

In what was described as a major policy speech last week, Secretary of State Dean Rusk struck back at those who have charged the State Department particularly and the administration in general with pursuing a no-win policy in our struggle against worldwide communism. Actually, we do indeed intend to win, he declared firmly, and surely this ought to reassure and comfort all of us.

"And as my colleagues and I go about our business we have at our backs a formidable array of military strength under the command of a resolute President. This strength together with that of our many allies is capable of defending the vital interests of the free world."

Three things are in question here. We do have the formidable military strength (or at least we hope so); what is lacking is the will to use it. A second question is how many allies we have still, and the third is what is meant by "vital" interests. We seem completely capable of redefining "vital" on short

notice. For instance, in our persistent efforts to persuade the Russians to a nuclear test-ban treaty, we once considered 180 monitoring stations vital; now we think 80 will be enough. The Russians still think any is too many. In Berlin we once insisted on the untrammelled right to freedom of movement throughout the city; now we have no real objection to the existence of a dividing wall, provided that at intervals we can send a jeep through it for a brief and perilous display of the flag. There are grave suspicions that the Berlin crisis is heating up for another explosion this autumn.

In Laos we congratulate ourselves—and exchange congratulations and felicitations with Nikita Khrushchev—on establishment of a neutralist-coalition government despite the dismal record of preceding achievements of this sort. Mr. Khrushchev seemed especially pleased, in fact, which should be a sufficient warning to our side. Recent news reports say our military are pulling out of the country, in accordance with the agreement, but the Reds have not yet moved.

Another example of the manner of our winning is that of the settlement imposed in West New Guinea. For months this has been described as a "dispute" over the territory which for 134 years had been administered competently and well by the Dutch, and to which Sukarno of Indonesia had laid claim without any excuse whatever except that of a desire for aggrandizement. The dispute was settled, under pressure by the State Department of the United States. The Dutch have agreed to move out and let Sukarno have what his threats of aggression have won for him. The part of the State Department in it cannot be questioned. Many months ago, when the dispute arose—that is, when Sukarno first declared he wanted and would have West New Guinea—our Government warned the Dutch Government not to attempt to reinforce its defenses there through channels subject to our control.

This was a naked surrender to force and the threatened use of force, by a signatory to the U.N. Charter. Yet it was hailed as a famous victory, with toasts and congratulations all around for U Thant and the other negotiators.

The Premier of the Netherlands hardly can be blamed for a certain bitterness of feeling. The reason for his country's capitulation, he said, was that Holland "could not count on the support of its allies, and for that reason we had to sign."

Even the New York Times' ordinarily mild-mannered Arthur Krock was moved to write with some warmth.

"To those who feel that the threat of an aggressor to go to war is sufficient cause for the United States to abandon this historic policy (i.e., refusal to abet or to recognize successful aggression), and even assist him to gain his objective, this justification by the Government of its courses in the Dutch-Indonesian dispute will be sufficient. But the longer this reasoning controls the foreign policy of the United States, the weaker will be its influence in preserving the peace of the world which is the proclaimed goal of all its international activities. And the oftener the United States brings pressure on its friends and allies to surrender to such aggression as Sukarno's, the feebleness will be the alliances with free world nations that are the foundations of U.S. security."

After a few more such famous victories for U.S. foreign policy as that in Indonesia, Mr. Rusk as well as his fellow citizens may be brought to wonder just how many allies we really can count on in a pinch.

ROBERT VAN CLEAVE.

[From the Evening Star, Aug. 15, 1962]

VICTORY AND MR. RUSK

In his Minneapolis address to the Veterans of Foreign Wars, Secretary of State Dean Rusk has effectively addressed himself to all those rather numerous critics—such as Sen-

ators GOLDWATER and THURMOND—who have been accusing the Kennedy administration (and not without some justification) of being numbed by a “no win” psychology in dealing with the Kremlin in the cold war. The accusation, according to the Secretary is completely unjustified. As he has put it:

“We have a simple but transcendent goal. It is, in President Kennedy’s words, ‘a peaceful world community of free and independent states, free to choose their own future and their own system, so long as it does not threaten the freedom of others.’”

“This goal of ours . . . and the Communist goal are incompatible. This global struggle will continue until freedom prevails. It goes without saying that our purpose is to win.

“One hears now and then that we have a ‘no win’ purpose or politics. That is simply not so. Of course we intend to win. And we are going to win. Our objectives is a victory for all mankind.”

At this point, one might legitimately josh and twit Mr. Rusk. After all, in the recent past (extending over many months), censors in the State Department have not permitted admirals, generals, and other high officers of our armed services to speak as bluntly, or as well, as he himself has just spoken. The word “victory,” for example, the very word stressed by the Secretary in his impressive Minneapolis address, has been excised repeatedly by his underlings from numerous speeches of some of our topmost military leaders.

Why? Well, according to an explanation submitted by the State Department last May to a Senate investigating committee, “‘victory’ has a militaristic and aggressive ring” and it is therefore unsuitable because it “implies an ‘all-or-nothing’ approach leaving no room for accommodation.” So Mr. Rusk’s use of the word (he should be wryly amused) ought to be sending tremors of excitement, if not dismay, into every nook and cranny of the department’s division (if it really exists) of “associate secretaries in charge of watering down the speeches of higher-ups.”

Considerations of this sort, however, should not be allowed to obscure the meaning of Mr. Rusk’s excellent Minneapolis address. For the address makes clear (and the Kremlin would do well to comprehend it) that the United States is not going to surrender its vital interests in Berlin or anywhere else. Nikita Khrushchev and his co-conspirators are making a monumental and potentially ghastly mistake if they think otherwise.

[From the Evening Star, Aug. 15, 1962]

WE TAKE A COLD WAR WIN POLICY

(By William S. White)

The United States, after a year and a half of the Kennedy administration, has now specifically and unapologetically proclaimed a win policy in the cold war.

This, Secretary of State Dean Rusk, a combat veteran of infantry, has done in a speech before the Veterans of Foreign Wars in Minneapolis. In the domestic sense and also in its relationship to our future negotiations with the Soviet Union, it is the most important he ever delivered.

For 18 months there has been an almost constant overture of criticism from Republicans and others that this country was committing itself to something short of victory to a no-win line.

For these same 18 months the State Department, itself, has been swept by undertones of debate between those who cried for caution and those who wanted a plain, hard declaration saying that we meant to do more than merely to coexist and survive. The hard liners have at last won the long dialog.

In this passage in Mr. Rusk’s speech in Minneapolis there lies the heart of their victory:

“We have a simple but transcendent goal. It is, in President Kennedy’s words, ‘a peaceful world community of free and independent states, free to choose their own future and their own system, so long as it does not threaten the freedom of others.’”

“This goal of ours—and of most of the nations of the world—and the Communist goal are incompatible. This global struggle will continue until freedom prevails. It goes without saying that our purpose is to win.

“One hears now and then that we have a no-win purpose or policies. That is simply not so. Of course we intend to win. And we are going to win. Our objective is a victory for all mankind.”

FIRST BY TOP CIVILIAN OFFICIAL

Never before had any top figure of the administration, outside the military, been willing to say simply and clearly that to win was our purpose and our resolve.

Those insisting on describing our aims in terms softer than the term “win” had long had their way on roughly these arguments: That to speak boldly of “winning” would be to imply that we meant to go to nuclear war, to alarm our allies and to present ourselves in a falsely truculent position. So elevated an official as Under Secretary of State George Ball put substantially these arguments before Congress itself.

CONFUSED BY SOPHISTICATION

These men were not truly “soft on communism.” They were, however, somewhat confused by their own sophistication. Too, they were tempted to an excessive stubbornness by the mere fact that some—but by no means all—of those who were denouncing “no-win” were rightwingers, such as Senator BARRY GOLDWATER, of Arizona, and STROM THURMOND, of South Carolina. To some New Frontier types, of course, no rightwinger can possibly be right about anything at all.

All the same, let fairness be heard now that the argument is over and rightly and reasonably won. It is fair to say that the defenders of the short-of-victory slogan were really anxious to win the cold war. But it is equally fair to say that their critics—not excluding Senators GOLDWATER and THURMOND—served a very good purpose here.

There was always plenty of reason not to permit military men themselves to cry up “win” as a policy. For, coming from them, such a statement could be read with some approach to rational interpretation as a recommendation for war.

But for the highest diplomatic figure of this country to proclaim “win” is entirely legitimate—and also overdue. It serves to notify the increasingly belligerent Russians—or any unduly timid ally—that we really do mean business. And it serves to enlarge what is already the happily high degree of bipartisan unity in this country on the one really vital thing—the cold war.

REVENUE ACT OF 1962

Mr. MANSFIELD obtained the floor.

Mr. PROXMIRE. Madam President, will the Senator from Montana yield to me? I should like to ask him a question.

The PRESIDING OFFICER (Mrs. NEUBERGER in the chair). Does the Senator from Montana yield?

Mr. MANSFIELD. Yes.

Mr. PROXMIRE. Madam President, in this morning’s Wall Street Journal is an article on page 3 relating to the tax bill. I should like to read a portion of it to the Senator from Montana, the

majority leader, and ask him if it is true.

The article states:

Senate Democratic leaders plan to employ harsh parliamentary tactics against liberal efforts to restore some of President Kennedy’s recommendations to the Senate Finance Committee’s version of the tax-revision bill.

The article further says:

In an attempt to complete Senate action on the measure before the Labor Day weekend, the Democratic leadership—acting with the tacit acquiescence of the administration—will try to table, or kill, most, if not all of the Kennedy proposals being offered by liberal Democratic Senators as amendments to the bill. Because a tabling motion is not debatable, this tactic tends to accelerate action by the slow-moving Senate. Debate on the measure began Saturday afternoon and will continue today.

The question by the Senator from Wisconsin is: Has there been any plan, or has there been any agreement, that the leadership would move to cut off debate on the amendments?

This Senator feels very strongly, as he indicated by his discussion of the bill on Saturday last, that this is a tremendously important bill which goes right to the heart of our whole economic system.

I think it is a bill which will require very protracted and detailed debate. I think it would be most unfortunate if the Senate, which is known as the greatest deliberative body in the world, should decide to cut off debate, and particularly debate on amendments designed to restore the proposals of the administration originally made with respect to the tax bill.

Mr. MANSFIELD. No; no agreement has been made. I do not know anything about the story to which the Senator refers, which he states is carried in the Wall Street Journal.

However, so far as the leadership is concerned, it would not foreclose the use of tabling motions on occasion. It is within the rules of the Senate to use them. It has not been decided what procedure we shall follow.

I wish to state, so long as the Senator has raised the question, that he has written me a letter to the effect that he would object to any unanimous-consent request seeking to limit debate on this bill. If that is the case, and if there will be no limitation, then of course the leadership will feel free at any time to move to table motions or amendments.

Mr. PROXMIRE. Madam President, will the Senator yield for a minute?

Mr. MANSFIELD. If I may continue, I have not had any conversations with anybody in the administration about this. I do not intend to. What will be done on this side will be done on my own responsibility.

Mr. PROXMIRE. I say to the Senator that there is absolutely no intention on the part of this Senator, or on the part of any Senator of whom I know, to prevent a final vote on the bill. We all want a vote on the bill, one way or the other, up or down. This is the reason why this Senator chose Saturday afternoon to make his long speech. In that way I did not delay the bill one minute.

On the other hand, I do feel, in all fairness, there should be as much time as possible for a thorough and complete debate on each of these very, very important amendments. If the consideration of the bill does take a week, or even more than a week, it seems to me it would be a week very well spent.

Mr. MANSFIELD. I assure the Senator that if tabling motions are offered they will be offered only after there is a reasonable amount of debate on the amendments being offered.

Mr. PROXMIER. I hope that we can get together on a reasonable period, so that there will be an opportunity for thorough discussion, particularly in view of the fact that there is absolutely no intent to return the bill to the committee or to delay the bill for weeks or to set off the vote until 1963. The intention is only to make sure that there is ample time for all views to be discussed. Members on the other side of the aisle feel fully as strongly as Members on this side of the aisle in respect to the bill.

Mr. GORE. Madam President, will the Senator from Montana yield?

Mr. MANSFIELD. I yield.

Mr. GORE. I should like respectfully to suggest to the able and distinguished majority leader that if the time arrives when no other Senator seeks recognition to speak on an amendment, a motion to table would be unnecessary because then the Senate could at that time vote on the merits of the amendment. It would seem to me that a vote directly upon acceptance or rejection of the amendment would be far preferable to a tabling motion.

I recognize that there are circumstances under which the majority leader would feel justified in resorting to a motion to lay on the table. I am also confident that he recognizes it is the most severe legislative restriction within the rule book. I would hope that he would lean over backward to permit votes on amendments up or down on the merits rather than on motions to table.

I offer that only as a friendly suggestion, and as a Member of the Senate who loves this arm of the Government and likes to see it proceed to consider measures on the basis of substance and merit.

Mr. MANSFIELD. I thank the Senator.

Mr. WILLIAMS of Delaware. Madam President, will the Senator yield?

Mr. MANSFIELD. I yield.

Mr. WILLIAMS of Delaware. I wish to join others in suggesting that there be no effort to railroad the bill through by tabling amendments without giving those offering such amendments an opportunity to get a vote on the merits of their amendments. I know of no disposition on the part of any Senator to delay consideration of the bill, if the leadership wants it scheduled. However, as the leadership knows, several amendments will be offered. Personally, I think the administration is making a great mistake to schedule the bill at the present time because we have in our committee the bill to extend the Reciprocal Trade Act. I think that that is one of the most important bills now awaiting the

consideration of the Senate. I regret to see it being bypassed.

Mr. MANSFIELD. Madam President, the administration is not scheduling the tax proposal at the present time. It is being scheduled by the majority leader because it has been cleared by both the Finance Committee and the Policy Committee. It should take its turn on the calendar. There is nothing much else we could turn to. But I wish to make very clear that it is not being done at the suggestion or the desire of the administration. It is a move which has been made solely as the responsibility of the Democratic leader.

Mr. WILLIAMS of Delaware. I appreciate the fact that the majority leader is taking the responsibility for it. But I am still not unmindful of the fact that some time ago representatives of the administration, I understand, contacted the chairman of the committee. He can speak for himself; but I do know that I was contacted with the strong suggestion that the trade bill be given top priority. There was a request and assurance that there would be no consideration of the tax bill until after the trade bill was reported.

Mr. MANSFIELD. That is news to me. I was not contacted in that way. I know of no such happening. I do not doubt the Senator's word. I am sure that what he has stated did happen, but so far as I am concerned, no one approached me about it.

Mr. WILLIAMS of Delaware. I was given that assurance, and the first indication I had that the bills would be scheduled otherwise was a newspaper report that as a result of a meeting at the White House the tax bill would be scheduled earlier, thus giving it priority over the trade bill.

This action may well jeopardize the enactment of the trade bill at this session.

The White House report was the basis of my statement that the administration was a party to the rescheduling of these bills.

I have supported the reciprocal trade program in the past, and I have every reason to think that I would support it again this year. However, it is an important measure and one which will require several days of work in executive session in our committee. I would have liked to have seen us get the trade bill before the Senate—at least on the calendar—before Labor Day in order that it could have been given prompt consideration. However, as the majority leader knows, with the tax bill before the Senate, those of us who are on the Finance Committee will now be required to be on the floor of the Senate, which means that there can be no further serious consideration in the Finance Committee of the trade bill until after the tax bill is disposed of. We cannot be in both places. For that reason only I make this statement.

Mr. MANSFIELD. I am not aware of any statement issued by the White House as to when the tax bill would be taken up. I can state, however, that there was a meeting of the Democratic policy committee on last Tuesday. That was the

first time the committee had an opportunity to consider the tax bill on the calendar. It was reported by the policy committee, I believe, unanimously. After the policy committee meeting was concluded, I informed the press that it was my intention to take up the tax bill after certain other bills were out of the way. I did so because there was not much else on the calendar to which we could refer.

As far as meetings are concerned, I offer to the distinguished chairman of the Finance Committee, the senior Senator from Virginia [Mr. BYRD], the use of the leadership office, room P-34, right outside the Senate Chamber, for any meetings he desires to hold on any subject, including the trade bill, during the course of the consideration of the tax bill.

Mr. WILLIAMS of Delaware. I appreciate that. The majority leader has always been most cooperative, and I wish to cooperate. But one cannot be in the office of the majority leader, room P. 34, working on the trade bill and at the same time be on the floor of the Senate, following the debate on the tax bill.

Mr. MANSFIELD. That is true, but if there is an opportunity, the committee could go in there and use the room.

Mr. WILLIAMS of Delaware. I suggest that during the period the tax bill is under consideration there can be no further consideration of the trade bill. I am sure that the administration recognizes that. The members of the Finance Committee cannot be present on the floor of the Senate and keep informed as to what is going on here and at the same time doing their duty as members of any committee meeting in executive session.

Mr. MANSFIELD. That is a matter which the committee itself must consider.

Mr. KERR. Madam President, will the Senator yield?

Mr. MANSFIELD. I yield.

Mr. KERR. I should like to ask the Senator from Delaware if he knows by what authority he can say there would be no further consideration in the Finance Committee of the trade bill so long as the tax bill is pending on the floor of the Senate?

Mr. WILLIAMS of Delaware. Madam President, will the Senator from Montana yield?

Mr. MANSFIELD. I yield.

Mr. WILLIAMS of Delaware. I am speaking only from a practical standpoint. The Finance Committee does have permission to continue its meetings. I agreed to that permission in the Senate at the time it was requested, and I recognize that if the Finance Committee, with its 17 members, insisted on meeting, they could get a quorum, even though some of us were following the tax bill on the floor of the Senate; but I do not think they will take advantage of any of us in that manner. I only say that I, as one member of the committee, would regret very much to have a procedure adopted by which meetings of the Finance Committee would be held simultaneously with consideration of the tax bill in the Senate, thereby depriving some members of the committee of an

opportunity to do their work on that bill. I hope there will not be such steam-roller tactics threatened or recommended by the administration at this time. This is not a national convention.

Mr. KERR. Madam President, will the Senator yield?

Mr. MANSFIELD. I yield.

Mr. KERR. The Senator from Oklahoma is one who believes that the Finance Committee has the capacity to continue to give consideration to the trade bill while the tax bill is under consideration on the floor of the Senate. The Senator from Oklahoma would not agree to the conclusion that the Finance Committee did not have greater capacity than that. The Finance Committee began consideration of the tax bill on April 2. It has been the subject of as many hearings as any bill that I can recall ever being considered by the committee. I hope there is room on the desk of each Senator for all the volumes of hearings the committee produced on that subject. The committee considered the bill for weeks. I do not know of many provisions in the bill that have the unanimous approval of all members of the committee. Every provision in the bill was thoroughly discussed, debated, negotiated, and explored before conclusions were reached. The committee reported the bill. The Senator from Oklahoma is aware that many members of the committee are going to give the Senate an opportunity to sit in on the deliberations on various features of the bill which may be both educational and at times inspirational.

No one is more certain than the Senator from Oklahoma that the Senate can, if it so chooses, proceed with the orderly consideration of the tax bill, and that the Finance Committee, with its tremendously able leadership and the magnificent mental qualification of the ranking Republican member and the devotion of all of its members on both sides of the aisle, can proceed with its deliberations, especially in view of the courteous offer of the majority leader that the committee may use an office immediately off the floor for its deliberations while we go through whatever may occur on the floor, and each Senator will reserve the right, and probably use it, to describe his views in connection with the deliberations and actions by the Senate on the tax bill.

Mr. CURTIS. Madam President, will the Senator yield?

Mr. MANSFIELD. I yield.

Mr. CURTIS. Whatever is decided by the leadership, I certainly will willingly comply with. I wish to point out one of the problems of having the Senate Committee on Finance meet at the same time the tax bill is being considered on the floor. The Senator from Oklahoma can only be in one or the other of two places. That will mean that one of the places, either in the committee room or in the Senate Chamber, will be deprived of the services of the Senator from Oklahoma. With his unusual charm he can persuade in the most eloquent manner. He has a keen mind and he can reach back in history for important incidents and recite them. He knows the Internal Revenue

Code thoroughly. He has had wide business experience. I merely wish to say that should we decide to operate in two places at the same time, that meeting which is deprived of the presence of the distinguished Senator from Oklahoma probably will be able to get along without him, but not nearly as well as if he were present.

Mr. KERR. Madam President, I did not know that CURTIS was of such highly concentrated Irish origin. The only thing this reminds me of, along with the green color of the volumes of the hearings, is that what he has said is the greatest blarney to which I have ever been subjected.

Were the Senator from Oklahoma able to encompass in the limited mental dimensions that he has the great knowledge and background and experience the Senator from Nebraska ascribes to him, along with that of his own limited understanding, he might approach the stature described so entertainingly and charmingly by the Senator from Nebraska.

Mr. WILLIAMS of Delaware. Madam President, will the Senator from Montana yield?

Mr. MANSFIELD. I yield.

Mr. WILLIAMS of Delaware. I enjoyed the compliments being exchanged by the Senator from Nebraska and the Senator from Oklahoma, but being practical let us recognize what is happening. As the majority leader knows, we are having difficulty getting a quorum in the committee even now. The record will show that I have tried to cooperate in getting a quorum for committee meetings. On Friday last the Finance Committee sat for a full hour between 10 and 11 waiting for a quorum to develop, but we had to adjourn at 11 o'clock because a quorum could not be obtained. The chairman was present and I was present but we would not get a quorum, and the meeting had to adjourn.

The Finance Committee meeting scheduled for today had to adjourn again because a quorum could not be obtained. That meeting had been scheduled for 10 o'clock this morning. It was canceled. Why? The members of the Finance Committee had to be on the floor of the Senate. That is the kind of problem that will confront us.

There are many sections of this proposed tax bill which are highly controversial, as the Senator from Oklahoma has said. Many sections of the bill will require the full attendance of members of the committee on the floor of the Senate to discuss them. They should be on the floor of the Senate when various amendments are being proposed. I do not see how we can possibly be in both places at the same time. I am pointing all this out from a very practical standpoint. I have no intention of trying to obstruct the consideration of either bill, but it may well happen that we will not get much done on the trade bill in committee until after the tax bill has been disposed of on the floor of the Senate.

That is the practical situation which has developed in our committee.

We have a system of operation in the Committee on Finance—and no one has

suggested that we change it—that if some of the members of the committee are not present we take tentative action only on proposals. These actions can later be reconsidered by any member who was not present. That means that anyone of the members may reopen a question that had been tentatively decided by perhaps nine members of the committee. The result will be that under these circumstances, with the tax bill being considered on the floor and the committee trying to meet on the trade bill, actually nothing will be accomplished on the trade bill.

The administration is well aware of that fact, and unless they are now scuttling the trade bill I cannot understand why they agreed to set it aside.

I keep hearing a persistent rumor—I cannot conceive of its being true—that the administration is jockeying the trade bill into the position where they can settle for a 1-year extension of the Reciprocal Trade Act and then blame that decision on the Congress. I hope there is no substance to that rumor.

Mr. MANSFIELD. It is not true. The Senator has been mentioning that rumor several times. He mentioned it several times during the past week. He mentioned it on the radio, I understand, in an interview with the Senator from New York [Mr. KEATING] yesterday. There is absolutely nothing to it. The most foolish thing we could do would be to extend the Reciprocal Trade Act, since we would be legislating on nothing, because there is nothing to extend.

As far as we are concerned, we intend to take up the trade bill once it is reported from committee, and we intend to stay with it until it is disposed of one way or another. It will not be set aside. The Senator knows that that is the way things will be done.

Mr. WILLIAMS of Delaware. Madam President, I am glad to have that assurance. I assure the Senator from Montana that I did not start that rumor. It appeared in the newspaper several times last week. It has been a persistent rumor, and the action being taken here today lends credibility it. We are now proceeding in a manner which may well jockey us into that kind of position.

Mr. MANSFIELD. No. The tax bill is on the calendar. I address an inquiry to the Senator from Virginia, the distinguished chairman of the Finance Committee. Is it not true that it is the intention of the committee to consider fully the trade bill and to report it to the Senate and to have it disposed of on the floor of the Senate?

Mr. BYRD of Virginia. Yes; the Senator is correct. I wish to make a statement on that point.

As chairman of the Committee on Finance I will expedite in every possible way the completion of the committee's work on the trade bill. We have already had the hearings on the bill. Now it is a question of voting in committee on provisions in the bill.

The chairman of the Finance Committee has always insisted, and will continue to insist, that a quorum be present. If a member of the committee has a

proxy and leaves it, that would be counted for purposes of a quorum, of course. Without a quorum being present, we should not vote on these vital matters, because the trade bill, in my judgment, is one of the most important bills that has been presented to the Senate during my service in the Senate.

While we will expedite the consideration of the trade bill in every way possible, we must bear in mind that the time has come to vote on the bill in committee, not to hold hearings. The hearings have been held. It would be rather against my desires, as the chairman of the committee, to be absent from the floor of the Senate while the tax bill is under consideration.

The chairman called a meeting of the Finance Committee for 10 o'clock this morning. He did not know at the time he set the meeting that the Senate would convene at 10 o'clock. That meeting of the committee had to be called off, as a result of the Senate's meeting at 10.

I wish to say to my friend, my beloved leader—and I say with all sincerity that he is one of the finest leaders, and most able and considerate, that I have ever served with in the Senate—that I will do everything possible in handling the two bills, but I cannot do the impossible. A person cannot be in two places at the same time, as must be obvious to everyone. We will do all we can, and the chairman of the committee will use his office off the floor to do everything he can.

The hearings on the tax bill cover about 12 volumes of testimony, containing 4,934 pages. The hearings lasted, off and on, for nearly 4 months. We heard 200 witnesses. As passed by the House, this has been one of the most controversial tax bills ever to come to the Committee on Finance.

It has been the policy of the committee during all my time—and I served on it under Senator Harrison, under Senator Millikin, and under Senator George—to have full and complete hearings on vital matters referred to the committee. This policy was carried out in this case to the extent that we have nearly 5,000 pages of testimony on the bill. The committee held some hearings in the afternoon, as well as in the morning. I believe we have covered the ground. I have brought in individual views, to which I will refer.

I wish to say that I favor the bill as the committee reported it with the exception of the part that I deal with in my individual views. This is the first time during my service on the committee that I have ever submitted individual views taking exception to provisions in a committee bill. With the exception of the so-called investment credit section, I think there are many good features in the bill. In my opinion, it is a far better bill than the one which came from the House.

AMERICANS OF JAPANESE DESCENT DESERVE BETTER TREATMENT FROM INTERNAL REVENUE

Mr. CARROLL. Madam President, I pleased today to add my support to the amendment to the Revenue Act of 1962

as proposed by the distinguished Senator from California [Mr. KUCHEL].

This amendment will, I hope, receive the approval of the Senate when it takes up the tax bill this week. The interests of fair play and humanity demand that action be taken now, by the Congress, to prevent the perpetration of yet another grievous injustice to American citizens of Japanese descent.

We all know of the great hardship and personal losses suffered by the Japanese-Americans as a result of their forced evacuation from the west coast at the beginning of World War II.

It is a source of lasting embarrassment to our Nation that these brave and loyal citizens should have received such treatment at the hands of the American Government; 110,000 were evacuated from the west coast, 23,000 of these went on to fight for their country, and many died for their country. The record in battle of the courageous and respected Japanese-Americans in World War II should be a source of pride to all Americans, especially when we recall that while these men were fighting, their families were forced to live in restricted prison-like compounds.

In 1948, our Nation, in the Japanese-American Evacuation Claims Act, provided for compensation payments to be made to these citizens for the property losses which they sustained during their internment.

This compensation can only be token; for there is no way of compensating for the humiliation and unhappiness which the forced evacuation caused.

Now I am informed that the Internal Revenue Service has ruled that payments under this act—payments for loss of property because of Government action—shall be treated as income for the purposes of taxation.

This is obviously unfair.

This is the Government adding insult to injury. This is the Government taking back, in the form of taxes, money which the Congress has determined is due in simple justice to our Japanese-American citizens.

For this reason, I am pleased to join the Senator from California in urging adoption of this amendment.

This provides that these payments shall not be considered as taxable income by the Internal Revenue Service.

I hope the Senate will promptly approve this.

A most thoughtful editorial, endorsing this proposal, was recently printed in the Denver Post. It sums up well the merits of the amendment. I ask unanimous consent to have it printed in the RECORD at this point.

There being no objection, the editorial was ordered to be printed in the RECORD, as follows:

HOW TO FAIL AT JUSTICE WITHOUT TRYING

One of the dark chapters of American democracy, which almost everyone would like to forget, refuses to stay closed. The regrettable mass evacuation of Japanese Americans from the west coast 20 years ago is back in the news again because of the understandable but misguided zeal of the Internal Revenue Service.

To understand what this is all about, it is necessary to review history briefly. Early in 1942, more than 2 months after the

Japanese attack on Pearl Harbor, the Nation began to hear demands that resident Japanese-Americans be interned because they posed a danger to national security.

Immediately after Pearl Harbor the Federal Bureau of Investigation rounded up all persons it considered dangerous. The FBI felt the situation was well in hand, but this did not deter the zealots. Politicians took up the cry. Nearly 6 months after Pearl Harbor the Army ordered everyone of Japanese descent removed from the western portions of Washington, Oregon and California as a military necessity.

Approximately 110,000 men, women, and children were evacuated into inland camps, one of which was in Colorado, another in Wyoming. Two-thirds of the evacuees were American citizens. They were charged with nothing other than the "crime" of being born of Japanese lineage. They were never given a hearing.

It is to the everlasting credit of the evacuees that they cooperated with the program as their contribution to the war effort. Many enlisted in the Armed Forces and served with distinction, even while their families were still detained. Under the Government's relocation program others took farm jobs in the Rocky Mountain West, or moved to the Midwest and East and worked in war industries.

The economic loss suffered by the Japanese-Americans as a result of the evacuation was estimated by Federal Reserve bank officials at \$400 million.

Ten years ago, Congress voted to compensate the evacuees for their losses. Patrick Hillings, Congressman from California, at the time, said the awards were voted "because it seemed the only honorable thing to do for these people who had already suffered so much."

Approximately \$36 million was paid out under the program—less than 10 inflated, postwar cents for each prewar dollar.

Congress, unfortunately, neglected to specify that these awards were to be considered Federal bounty and not taxable. Recently the Internal Revenue Service, hewing to the letter of the law, instituted proceedings to tax these awards as income.

This week Senator THOMAS H. KUCHEL, of California, the Republican whip, introduced legislation to exempt compensation for evacuation losses from Federal income taxes.

The claims program, KUCHEL pointed out, was the effort of "an embarrassed Nation to right the grievous wrong done to tens of thousands of our fellow citizens of Japanese extraction."

KUCHEL's measure clarifies the original intent of Congress. It deserves approval forthwith. It is regrettable that the issue of taxing the Federal awards has come up at all.

Mr. MANSFIELD. Madam President, is there further morning business? I make the inquiry because the chairman of the committee is waiting to make his opening statement on the tax bill.

The PRESIDING OFFICER. Is there further morning business? If not, morning business is closed.

ORDER FOR ADJOURNMENT UNTIL 10 A.M. TOMORROW

Mr. YOUNG of North Dakota. Madam President, I should like to inquire of the distinguished majority leader how long we may expect the Senate to remain in session this evening.

Mr. MANSFIELD. I would estimate the Senate would be in session until 9 or 10 o'clock tonight. We will assemble early every day from now on in an attempt to expedite the business of the Senate.

Madam President, I ask unanimous consent that when the Senate concludes its deliberations this evening it stand in adjournment to meet at 10 o'clock tomorrow morning.

The PRESIDING OFFICER. Without objection it is so ordered.

REVENUE ACT OF 1962

Mr. MANSFIELD. Madam President, I ask unanimous consent that the unfinished business be laid before the Senate and made the pending business.

Without objection, the Senate resumed the consideration of the bill (H.R. 10650) to amend the Internal Revenue Code of 1954 to provide a credit for investment in certain depreciable property, to eliminate certain defects and inequities, and for other purposes.

PRIVILEGE OF THE FLOOR

Mr. BYRD of Virginia. Madam President, I ask unanimous consent that Miss Grace Gunn and Mr. James Symons, of the staff of the Joint Committee on Internal Revenue Taxation, be granted the privilege of the floor during the consideration of the tax bill.

The PRESIDING OFFICER. Is there objection? The Chair hears none, and it is so ordered.

Mr. MANSFIELD. Madam President, I suggest the absence of a quorum.

The PRESIDING OFFICER. The clerk will call the roll.

The legislative clerk called the roll, and the following Senators answered to their names:

[No. 220 Leg.]

Alken	Hart	Morse
Allott	Hartke	Moss
Beall	Hayden	Mundt
Bottom	Hickenlooper	Muskie
Burdick	Hickey	Neuberger
Bush	Hill	Pastore
Byrd, Va.	Holland	Pell
Byrd, W. Va.	Humphrey	Prouty
Cannon	Jackson	Proxmire
Carroll	Johnston	Randolph
Case	Jordan, N.C.	Robertson
Chavez	Keating	Russell
Church	Kefauver	Saltonstall
Clark	Kerr	Scott
Cooper	Kuchel	Smathers
Curtis	Lausche	Smith, Maine
Dirksen	Long, Mo.	Sparkman
Dodd	Long, Hawaii	Talmadge
Douglas	Magnuson	Thurmond
Eastland	Mansfield	Wiley
Ellender	McCarthy	Williams, Del.
Ervin	McClellan	Yarborough
Fong	McGee	Young, N. Dak.
Fulbright	McNamara	Young, Ohio
Gore	Metcalf	
Gruening	Monroney	

Mr. HUMPHREY. I announce that the Senator from Alaska [Mr. BARTLETT], the Senator from Nevada [Mr. BIBLE], the Senator from California [Mr. ENGLE], the Senator from Louisiana [Mr. LONG], the Senator from Massachusetts [Mr. SMITH], the Senator from Mississippi [Mr. STENNIS], and the Senator from New Jersey [Mr. WILLIAMS] are absent on official business.

I further announce that the Senator from New Mexico [Mr. ANDERSON], and the Senator from Missouri [Mr. SYMINGTON] are necessarily absent.

Mr. KUCHEL. I announce that the Senator from Utah [Mr. BENNETT], the Senator from Delaware [Mr. BOGGS], the Senator from Maryland [Mr. BUTLER], the Senator from Indiana [Mr. CAPE-

HART], the Senators from Kansas [Mr. CARLSON and Mr. PEARSON], the Senators from New Hampshire [Mr. COTTON and Mr. MURPHY], the Senator from Arizona [Mr. GOLDWATER], the Senator from New York [Mr. JAVITS], the Senator from Idaho [Mr. JORDAN], the Senator from Iowa [Mr. MILLER], the Senator from Kentucky [Mr. MORTON], and the Senator from Texas [Mr. TOWER] are necessarily absent.

The Senator from Nebraska [Mr. HRUSKA] is absent on official business.

The PRESIDING OFFICER. A quorum is present.

Mr. BYRD of Virginia. Madam President, the bill H.R. 10650 is the most comprehensive measure to come before the Congress since the 1954 provision of the Internal Revenue Code. Senators will observe on their desks the volumes of testimony taken by the committee. I believe there are 12 volumes of the record, containing nearly 5,000 pages of testimony given by more than 200 witnesses, indicating opposition to many sections of the bill and also the importance of it.

The bill contains a number of provisions which would close loopholes. I wish that more were closed. Those provisions I favor.

But, unfortunately, the bill also contains a provision which would open up one of the largest loopholes that has ever been written into law, to my knowledge. I refer to investment credit. I am opposed to the investment credit because it is discriminatory and because its value and need as a stimulant to so-called economic growth are both questionable and doubtful, and because it would substantially increase the budget deficit.

If we should allow the proposed investment credit on the purchase of machinery and equipment, it would naturally follow that we must later allow it for buildings, because it is not sensible to think that businessmen would put new machinery into antiquated buildings.

Again, it would undoubtedly be very much more favorable to big business than to small business because big business more often is operating at a profit. There would be no benefit in the proposed tax credit unless one did make a profit. The credit might be carried forward under the bill, or something like that, but one must have a profit and establish a tax in order to deduct from it the proposed tax credit.

Since the bill passed the House, the administration has issued regulations under which depreciation deductions are substantially increased. That I favor. That will be stimulant to investment in machinery and new plants. The regulation, which I believe was issued on July 11, is estimated to lose \$1,500 million of tax revenue. The investment credit would reduce the revenue by \$1,200 million, making a total of \$2,700 million for the same general plan of benefits, all of which, as it now appears to me, would probably be added to the public debt.

For the first time in my 30 years of membership on the Senate Finance Committee I have found it necessary to

present a minority statement on a bill reported by the committee. The committee adopted the investment credit provisions by a vote of 10 to 7. In the minority views I was joined by the Senator from Tennessee [Mr. GORE], the Senator from Delaware [Mr. WILLIAMS], and the Senator from Nebraska [Mr. CURTIS]. By reason of that I have submitted individual views I felt it was appropriate for me to request the very able ranking Democratic member of the Senate Finance Committee, the Senator from Oklahoma [Mr. KERR], to report the bill to the Senate, which he has done.

Madam President, I commend the distinguished Senator from Wisconsin [Mr. PROXMIRE], who is a cosponsor of an amendment that would eliminate the so-called investment credit provisions from the pending bill.

I commend the Senator from Wisconsin for the presentation which he made on Saturday in behalf of the amendment and against the investment credit provisions. His analysis of the situation was accurate. It was exhaustive and able, and his arguments were forceful. His position is correct. I am pleased to be associated with him in that effort. The Senate and the public is indebted to him for stating the opposition to the investment credit provisions so clearly and so fully.

The Senator from Wisconsin [Mr. PROXMIRE] appeared before the Senate Committee on Finance in opposition to the investment credit and made an extremely able argument.

Madam President, I wish to read my minority views which, as I said, I signed with great reluctance, breaking a policy of mine for 30 years.

The minority views are as follows:

We oppose section 2 of the 1962 revenue bill (H.R. 10650) which would give a 7-percent tax credit to segments of business for investment in new machinery and equipment.

Our opposition to this section of the bill is based on firm convictions after full consideration of views expressed by competent witnesses in exhaustive hearings, and those expressed in voluminous correspondence from the general public.

We have given closest possible study to statements in behalf of the administration's recommendations made before the Senate Finance Committee which, in some respects, are at variance with provisions now in the section.

Before adopting the "investment credit" (sec. 2) provisions as reported, the Senate must consider the fact that the Internal Revenue Service on July 11, 1962, substantially revised its regulations to accelerate regular depreciation.

Which, as I have said, would cost the Treasury \$1,500 million.

Our position—

That is, the signers of the minority views—

is in accord with views of a vast number of citizens, including those representing industry, business, labor, and agriculture throughout the Nation, who have testified and counseled for rejection of the provisions of section 2.

Hearings on the pending bill were held over a period of 4 months, and a substantial portion of the testimony taken was directed

to section 2. Generally, our conclusions may be summarized, but the detail must be considered, too.

In summary, we oppose "investment credit" as it would be provided by section 2 for numerous reasons including the facts that—

(1) It would be a subsidy in the nature of a windfall to be given to businesses which comply with a Government policy.

As I have stated, the big business, which most often makes a profit, would get more benefits than the smaller business.

I continue to state the minority views:

(2) It would be discriminatory in its application among various businesses, even among those similar in kind.

(3) Its value and its need as a stimulant to so-called economic growth are both questionable and doubtful.

(4) Its continuing cost would be heavy and it would increase the Federal deficit in the current fiscal year.

I will repeat what I said in the beginning. If we provide an investment credit for the installation of machinery, it naturally follows that we shall have to provide an investment credit for buildings, because if buildings were antiquated, it is not likely that a business man with judgment would install new machinery in an old building.

I continue to read from the report:

WOULD INCREASE DEFICIT

There was a Federal deficit of \$6.3 billion in fiscal year 1962 which ended June 30. There will be another deficit in the current fiscal year which started July 1. The "investment credit" provisions in H.R. 10650 would increase the 1963 deficit by \$630 million (net).

The staff of the Joint Committee on Internal Revenue Taxation, using officially budgeted expenditures, estimates that—

(1) The Federal deficit in the current fiscal year 1963 will be more than \$3.9 billion, excluding the effect of this bill.

In my judgment, this estimate is too low, because the shock that has occurred in the stock market will unquestionably reduce income in this fiscal year, and thereby reduce the receipts from taxes on income.

Second, the Federal deficit would be increased by a total of more than \$1 billion if H.R. 10650 as passed by the House of Representatives were enacted.

Third, the Federal deficit estimate would have to be increased by a total of \$630 million net if the bill as reported by the Senate Finance Committee were enacted, with the investment credit provision.

If H.R. 10650, in either the House or the Senate committee version, were enacted, a substantial portion of the estimated increase in the Federal deficit would be directly attributable to the effect of the investment credit provision alone. The joint committee staff estimates that under the House-passed version of the investment credit provision, revenue in fiscal year 1963 would be reduced by \$1.3 billion; and under the Senate committee version of the investment credit provision, revenue in fiscal year 1963 would be reduced by \$650 million gross.

If the investment credit provisions of section 2 remain in the bill and the

measure is enacted, they will become permanent in the law. For this reason it is appropriate for the Senate to examine the long-range budgetary effects.

When this is done, the enormity of the revenue loss becomes even more clear, and the budgetary effect becomes even more significant. Extending application of the investment credit provisions over an 11-year period, from 1962 to 1972, the Joint Committee staff finds that business tax liabilities would be reduced during that period by \$21 billion under the House-passed version; and business tax liabilities would be reduced in that period by \$15.6 billion under the Senate committee version.

I may say that the Senate committee amended the tax credit provision so that the revenue loss would be less than under the House bill.

Revenue loss resulting from application of the new depreciation guidelines made effective by the Treasury Department on July 11, 1962, would be in addition to the revenue loss resulting from the investment credit provisions in the bill if they were enacted.

The Treasury has estimated that in the first year of operation the recent revisions in Internal Revenue Service rules on depreciation will result in a reduction in business tax liabilities of \$1.5 billion. Estimates for subsequent years have not been made.

Let us see what is wrong in principle with the investment credit provision.

The investment credit proposed in section 2 of the pending bill is wrong in principle. It would be discriminatory in its application. It would do harm to our tax structure. It is a new gimmick, and will add nothing. It would not achieve so-called growth in investment. It is not needed under existing conditions.

Under terms of the bill, those complying with the investment credit provisions would be entitled to a tax credit which could be offset directly against income tax liability. Coupled with depreciation, investment credit would return to the investor more than he paid for the asset.

I mean by that that under the depreciation laws a person is permitted to deduct only the cost of the article, whatever it may be—machinery or anything else. Under the bill, as amended by the Committee on Finance, there would be an additional reduction because it is a credit, and not a deduction. Income tax is generally estimated at 52 percent. So that instead of being a deduction, the person who would acquire this machinery, and so forth, would get a tax credit of more than the actual cost.

Mr. GORE. Madam President, will the Senator yield?

Mr. BYRD of Virginia. I yield.

Mr. GORE. Did not the senior Senator from Virginia, like the junior Senator from Tennessee, though feeling that the recent revision of the depreciation schedule may have been overly generous, lend his support to this new approach to depreciation?

Mr. BYRD of Virginia. Yes, I did. I thought that was the proper way to

approach it. That would hold the figure down to 100 percent, as the Senator knows, but under this provision the investment credit would in effect provide depreciation in excess of 100 percent.

Mr. GORE. As the Senator knows, the depreciation schedule now in effect is so generous that a businessman can write off a new automobile entirely in 3 years.

Mr. BYRD of Virginia. The Senator is correct.

Mr. GORE. Like the Senator from Virginia, I thought that the regulations on depreciation needed attention, and have needed it for some time. I felt that if the new regulations are not sufficiently generous, the Treasury Department has authority from the committee and Congress to be more generous than the regulations that have been issued. Is that correct?

Mr. BYRD of Virginia. The Senator from Tennessee is correct.

Mr. GORE. Is it not reasonable to assume that the Treasury Department, in revising the depreciation schedule, was as generous as it felt justified in issuing the new regulations?

Mr. BYRD of Virginia. I agree with the Senator from Tennessee.

Mr. GORE. I would like to ask the Senator, if that be true, what justification is there now for piling on top of that perhaps another \$1½ billion of so-called investment credit?

Mr. BYRD of Virginia. There is no justification for it. For that reason I joined the Senator from Tennessee in signing individual views. One of the things the Senate should understand as to this particular class of people is that they would get the investment credit to provide depreciation of more than 100 percent, not 100 percent, in accordance with the regular schedule. Is that correct?

Mr. GORE. That is correct. I should like to ask the Senator if it is not true that under the bill before the Senate and under the majority report interstate gas pipelines receive a 7-percent investment credit.

Mr. BYRD of Virginia. That is correct. Slot machines would receive it, too. Anything that is bought in the way of equipment would receive it. One could use slot machines for gambling and get the credit.

Mr. GORE. I am not sure that all Members of the Senate realize to what extent effective legal meaning is given to the provisions of a tax law that is proposed by the majority report, which accompanies such a bill. I am sure the Senator will attest to the legal application of a Senate committee report with reference to its intention.

Mr. BYRD of Virginia. It does have great legal effect in the courts.

Mr. GORE. Madam President, will the Senator yield further?

Mr. BYRD of Virginia. I yield.

Mr. GORE. I should like to read from page 155 of the report:

Specific examples of qualifying property which normally would be used as an integral part of one of the specific activities are blast furnaces, oil and gas pipelines, and railroad tracks and signals. Fences will

qualify as section 38 property where used as an integral part of a specified activity as, for example, where used in connection with the raising of livestock.

Now I turn to page 14 of the report:

Public utility property is taken into account as qualified investment at three-sevenths of the amount otherwise allowable.

The Senator had previously stated that utilities which are under regulation receive not 7 percent, but 3 percent.

Mr. BYRD of Virginia. That is correct.

Mr. GORE. But as I read paragraph 4 on page 14, it will be seen that apparently the report makes an exception for gas pipelines.

Mr. BYRD of Virginia. From what page was the Senator reading?

Mr. GORE. From page 14.

Mr. BYRD of Virginia. I have been a Member of the Senate for a long time, but I have never seen on Senators' desks so many documents pertaining to one bill.

Mr. GORE. I should like to read the fourth paragraph, on page 14:

Public utility property is taken into account as qualified investment at three-sevenths of the amount otherwise allowable. Thus, in the case of 4- or 5-year public utility property, one-seventh of the investment is taken into account; in the case of 6- or 7-year property, two-sevenths of the investment is taken into account; in the case of property with a life of 8 years or more, three-sevenths is taken into account. This means that in the case of public utility property with an expected useful life of 8 years or more, in effect a 3-percent credit is allowed. Public utility property for this purpose means property used predominantly in an electrical energy, water or sewage disposal business, a local gas distribution business, a telephone business, or a domestic telegraph business, but only if the rates involved in all of these cases are subject to regulation by a governmental agency or commission.

I am advised by technicians that gas pipelines will receive 7 percent. Does the Senator confirm that understanding?

Mr. BYRD of Virginia. I think the Senator from Tennessee is correct. That means, actually, more than 100 percent of its cost because under existing law and Internal Revenue Service regulations the cost of plant, machinery, and equipment generally may be depreciated 100 percent over a specified period.

Under existing law and Internal Revenue Service regulations the cost of plant, machinery, and equipment generally may be depreciated 100 percent over specified periods; and depreciation has been accelerated under the new rules now in force.

The regulation issued by the Internal Revenue Service on July 11 made the largest increase in the depreciation allowance at one time that I have known in my service in the Senate.

Under the current administration proposal and House bill provisions "investment credit" for new machinery and equipment would be in addition to 100-percent depreciation. Under the Senate committee version of the bill the "investment credit" would be in addition to 93-percent depreciation.

The administration proposed an 8-percent investment credit (with public utilities excluded) on new machinery and equipment in addition to 100 percent depreciation. The effect of this would be to give investors generally 116 percent of what they paid for the asset.

The House bill generally would give a 7-percent investment credit for new machinery and equipment, with a 3-percent credit for public utilities, in addition to 100-percent depreciation. This would allow investors up to 114 percent of what they paid for the asset.

The Senate committee bill generally would give a 7-percent investment credit for new machinery and equipment, with 3 percent for public utilities, in addition to 93 and 97 percent depreciation, respectively. This would allow investors up to 107 percent of what they paid for the asset.

Evidence given in hearings on this bill clearly shows that investment credit is both wrong in principle and unnecessary. Numerous witnesses, including those representing four major segments of the economy, opposed the principle involved.

In view of the testimony in the published record on this proposal, it is difficult to understand the persistence of the investment credit advocates. Leaders of industry, business, labor, and agriculture all have appeared before the Senate Finance Committee to oppose it.

Stanley H. Rittenberg, research director, AFL-CIO, urged the committee to "delete this provision from the bill," because those he represented thought:

It is a multibillion dollar windfall that will not really contribute anything to our national goals and will not relieve our balance-of-payment problems as it is claimed.

Walter Slowinski, appearing in behalf of the U.S. Chamber of Commerce, with respect to the investment credit provisions, said:

The chamber again recommends against the adoption of this novel and untried preferential tax credit subsidy for business. It is also unnecessarily complex, and it will be difficult to administer.

Harold H. Scaff, chairman, tax committee, National Association of Manufacturers, said:

Investment credit would simply provide reduction in effective tax rates for taxpayers who use their income and other funds as the Government thinks is best for the economy at a particular time.

There has been a tendency to promote and discuss the investment tax credit apart from the price which it would exact in terms of other changes in the tax law. Even without the exaction of such a price, we would oppose the credit for the reasons set forth in the appendix attached hereto. Very simply, we believe that tax reductions should be afforded by direct means. We would take this position even if, in our opinion, all of the other provisions of H.R. 10650 constituted sound tax policy.

Charles B. Shuman, president, American Farm Bureau Federation, took the position that—

These provisions are both unsound and likely to have a number of undesirable effects. It would be far better to liberalize the treatment of depreciation and work toward a general reduction in income tax rates.

The proposed investment credit is a selective form of tax relief—in reality a subsidy. * * * The result would be to give some taxpayers a competitive advantage at the expense of others.

Although the Farmers Union did not send a representative to testify directly before the Finance Committee, a communication signed by James G. Patton, president, National Farmers Union, published in the CONGRESSIONAL RECORD of March 29, 1962 (p. 4984), said:

Urge your influence to delete provision giving huge private corporations operating at less than full capacity over \$1½ billion and private electrical power monopoly over \$100 million in tax subsidies which would result in the flight of capital overseas and further aggravate the dollar crisis.

The investment credit proposal would be discriminatory in obvious respects. It would discriminate against companies which were recently modernized, against poorer companies, and against companies needing new buildings with or without new machinery and equipment.

The very fact that the investment credit would give special tax reductions only to companies able and willing to invest in new machinery and equipment means that those who, for any reason, were unable to make such investments would be subjected to discrimination. Struggling small companies unable to provide investment funds which would enable them to qualify under this proposal would not be eligible to receive the credit; but their very prosperous competitors would reap a windfall from the Federal Government, through this special tax treatment.

None of the proposals in the Senate committee's version of the bill or in the House version of the bill would give investment credit for new buildings or structural components. But it is difficult to imagine that such companies would install expensive, modern machinery and equipment in old, outmoded buildings. Madam President, I predict that if the proposed tax credit is given for new equipment and machinery, it will necessarily follow that we shall have to include new buildings, because no businessman with commonsense would install a considerable amount of new machinery in an antiquated building. So if, as would necessarily follow, we would also have to include an allowance for the new buildings, the total cost would be enormous.

Plans for new facilities contemplated by advocates of the credit are formulated far in advance. Many of those who would benefit from the proposal would have developed their improvements without the incentive of investment credit. These businessmen do not decide all of a sudden to spend \$100 or \$500 million or any other considerable amount on such developments. Instead, their plans are made long in advance. In such cases, the credit would be of questionable value as a stimulant to economic growth.

On the other hand, the proposal offers neither incentive nor immediate means of expansion for companies which are hard pressed for capital. If the admin-

istration and the Congress desire to give aid to the corporations, it would be far better to do so by means of a reduction in the corporate tax in an amount which would develop a loss equivalent to that which would be experienced from the proposed investment credit, because an across-the-board reduction in the corporation tax would apply to all corporations, in accordance with their profits.

A recent McGraw-Hill survey developed the consensus that this investment credit proposal would increase 1962 investments by only about \$300 million, or 1 percent. This raises the question of the effectiveness of section 2 as a stimulant for increased investment. Of course, the loss would come in later years, inasmuch as this proposal would be a permanent part of the tax system.

Witnesses before the Finance Committee also raised the question as to the effectiveness of investment credit in this respect. For example, Augustus W. Kelley, representing the Proprietary Association, said:

The theory of the tax incentive in our opinion is based on the false premise that business investments are motivated substantially by tax considerations. In our industry, and we believe it is typical of others, the decision whether or not to invest in new machinery and equipment is based primarily on pure business consideration. Simply stated, we are not going to spend \$1 just because the Government gives us 7 cents.

In other words, a company which installed new machinery and expanded its plant would have to be certain that it would find a market for what it produced.

Otis H. Ellis, speaking for the National Jobbers Council, said:

This tax credit will not be enough to induce a single jobber to buy one item more than what he would otherwise have purchased.

The McGraw-Hill survey, previously referred to, indicates that without the investment credit business investments in plant and equipment this year may be expected to reach some \$38 billion. This would be \$1 billion more than the previous record set in 1957.

If \$38 billion is spent in new plant and equipment this year, it will exceed such investments of last year by \$3.5 billion or 11 percent; and the same survey finds reason to expect continuing high level of investment for the period of 1963-65—provided businessmen have confidence in the future of business and provided they think they can sell what they produce.

Madam President, at this point let me state that what the businessmen of the country need is confidence—confidence that the dollar will not be devalued, confidence that those in Washington will not take sides against business, but that will adopt in regard to business substantially the same policy they have adopted in regard to labor, and confidence that the budget will be balanced.

Madam President, I have talked so often about the importance of balancing the budget that I know Senators are tired of hearing me refer to it. But it is true that in this connection we could do nothing better than balance the budget.

It has been balanced only 5 times in more than 30 years. When I came to the Senate, in 1933, the national debt was less than \$20 billion; today the national debt exceeds \$300 billion; and there is no prospect that the budget will be balanced in the near future. In view of our past and present spending programs and our constantly increasing national debt—which now has reached staggering proportions—it is obvious that if this trend is continued, the time will come when we shall have gone too far. We cannot continue to be the policemen of the free world and the banker of the free world and the Santa Claus of the free world indefinitely. Other nations have tried that in a smaller way, and all of them have met with disaster.

Those of us who have signed these minority views believe that the sound way to achieve a reduction in taxes is first to eliminate unnecessary Federal expenditures, as a means of putting the Nation on a sound financial basis.

Madam President, it is bad enough to have such very large deficits; but when we consider the operations of the Government and when we see the unbelievable amounts of waste and extravagance which exist in practically every activity on the part of the Government, we realize that they make the situation even worse, because we are creating deficits by means of expenditures which do not bring in much return.

Madam President, consider the Federal payrolls. When I first came to the Senate—and I hope I may be pardoned for referring to the situation which existed some years ago, but I think it is pertinent to refer to it here—there were 500,000 Federal employees. Today, there are more than 2½ million. Mr. Hodges, the Secretary of Commerce, said in effect before a House committee that substantial savings could be made in his Department if he could get rid of the deadwood. But, on the contrary, instead of reducing the personnel in the Department of Commerce, for the month of June, 1,600 new employees were added; and in the month of June there was an increase by 35,000 in the employment in the entire Federal Government—the largest increase in any month in 10 years except for the temporary employment of 1960 Census takers.

Madam President, we do not believe that tax reductions should be discriminatory by favoring some taxpayers over others in the manner inherent in the "investment credit" proposal or otherwise.

We believe that revisions in the Federal revenue structure should not create new discriminatory and artificial distinctions among taxpayers such as this proposal would establish in the law.

We believe our attention should be directed toward reducing rather than increasing such inequities.

Madam President, these minority views are signed by myself, as chairman of the committee, and by the distinguished Senator from Tennessee [Mr. GORE], the distinguished Senator from Delaware [Mr. WILLIAMS], and the distinguished Senator from Nebraska [Mr. CURTIS].

Mr. PROXMIRE. Madam President, will the Senator from Virginia yield?

Mr. BYRD of Virginia. I yield.

Mr. PROXMIRE. I wish to say that I am very proud to have been present today to hear the distinguished chairman of the Finance Committee make his very significant and historic speech. I believe this is the first time in some 30 years that the distinguished Senator from Virginia has filed minority views.

Mr. BYRD of Virginia. That is correct.

Mr. PROXMIRE. He feels so deeply about this issue, and he believes the present tax proposal is so unconscionable and so unprincipled and so adverse to the Nation's interests, because it would "bust" the budget so drastically, that he decided it was necessary to file minority views; is that correct?

Mr. BYRD of Virginia. That is correct.

Mr. PROXMIRE. Let me say that I was tremendously impressed by what the Senator from Virginia said, and also by what the Senator from Tennessee [Mr. GORE] said in connection with the point he brought up.

The Senator from Virginia very generously referred to the speech I made on Saturday, when I spoke for 4½ hours on this subject.

A few minutes ago the Senator from Tennessee referred to the situation in regard to the pipelines. In that situation, other utilities are allowed a 3-percent deduction, but the gas pipelines are allowed a 7-percent deduction; is that correct?

Mr. BYRD of Virginia. That is true.

Mr. PROXMIRE. The oil industry already is being treated in such a favorable tax way that it is the privileged sweetheart of the Government. For example, the oil industry is receiving a 27½-percent depletion allowance, and also is receiving one for expensing credit for drilling costs, and also is receiving other substantial advantages.

Mr. BYRD of Virginia. Yes.

Mr. PROXMIRE. The minority views of the Senator from Virginia are simply irrefutable. I cannot think of a single substantial argument in favor of the proposed investment credit.

I would add only one thing. The argument has been advanced for adoption of investment credit that it is necessary to make us more competitive with economies overseas. Which countries have investment credit? The United Kingdom, Belgium, and the Netherlands. The United Kingdom is the only industrialized country that has grown less rapidly than we have in the past 10 years, except for Belgium and Sweden; and the Netherlands has grown less rapidly than any other industrialized country in Europe except for the United Kingdom, Belgium, and Sweden. So it seems, on the basis of the facts, that is not a significant argument for the need for investment credit. Is that correct?

Mr. BYRD of Virginia. The Senator is absolutely correct. The Finance Committee went fully into that question with respect to competition and conditions in other countries. The Senator has correctly stated the situation.

Mr. PROXMIRE. I thank the Senator.

Mr. GORE. Madam President, will the Senator yield?

Mr. BYRD of Virginia. I yield to the Senator from Tennessee.

Mr. GORE. I wish to compliment in the highest of terms the distinguished senior Senator from Virginia, chairman of the Finance Committee. I have some knowledge and opinion about the degree of reluctance with which the chairman of the committee filed these minority views. I know it has been only through the promptings of his conscientious convictions that he has done so; but in doing so, in my view, he has performed a signal service. I am honored and pleased to be associated with him in an attempt to strike from the bill this provision, which seems to me to stand bare of justification.

Mr. BYRD of Virginia. I thank the Senator.

Mr. WILLIAMS of Delaware. Madam President, will the Senator yield?

Mr. BYRD of Virginia. I yield to the Senator from Delaware.

Mr. WILLIAMS of Delaware. I wish to join my colleagues in complimenting the chairman of the committee upon his analysis of the pending bill. I was proud to join the Senator from Virginia in his minority views and in the effort to strike from the bill the section which would allow the 7-percent investment credit. This is the proposal which allows a taxpayer in effect to depreciate a piece of machinery for 114 percent of its cost.

The Senator from Wisconsin pointed out that one of the administration's arguments in behalf of this 7-percent investment credit was that it would enable American industry to compete with the European Common Market. That is an excuse—not a reason. The Senator knows that as the bill came from the House it included a provision for a 7-percent investment credit for racehorses and bulls. Now, how would that increase the productivity of American industry or better enable it to compete with the European Common Market?

That provision was stricken in the Finance Committee, but the bill as it came from the Senate committee still allows this special investment credit under which taxpayers could recover 107 percent of their investment for slot machines, pinsetters, equipment at the racetrack, and many other types of equipment. What have these items got to do with increasing the productive capacity of this country?

I agree fully with what the chairman of the committee has said, that there are many ways this \$1.2 billion tax reduction could have been arrived at by making the benefits more equitable available to all taxpayers. For instance, the corporate tax could have been reduced so that all taxpayers would benefit. Under this bill the benefits would go only for certain types of machinery. As the chairman knows, the benefits do not go to new buildings. What good is new machinery if there is no building to put it in?

If the depreciation schedules are going to be changed they should be changed within the framework of existing law at a time when we have the money to finance such a tax reduction without borrowing the money. Any liberalization of our depreciation allowances should be made within the framework of existing law so all taxpayers can compute it without the necessity of hiring a Harvard economist to interpret the provisions of the bill.

Mr. CURTIS. Madam President, will the Senator yield?

Mr. KERR. Madam President, a point of order. The Senator from Delaware rose to ask the Senator from Virginia a question. The Senator from Virginia agreed to answer it. The Senator from Oklahoma would like to hear the Senator's answer.

Mr. BYRD of Virginia. Madam President, I agree with the Senator from Delaware.

Mr. KERR. On what?

Mr. BYRD of Virginia. On the question.

Mr. KERR. On the question. All right.

Mr. BYRD of Virginia. I yield to the Senator from Nebraska.

Mr. CURTIS. Madam President, I commend the chairman for the excellent work he has done, not only now, but throughout the years. The minority views drafted by the chairman, in which others of us have joined, point out that if this provision remains in the bill there will be a total net loss in revenue of \$630 million.

Is it not true that the same provision in the House bill would result in a loss of revenue much greater?

Mr. BYRD of Virginia. That is true.

Mr. CURTIS. In excess of \$1 billion—to be exact, \$1.2 billion. If we had acceded to the original suggestion of the Treasury it would be substantially more than that.

I wish to point out that it is very important that the provision be stricken from the bill. I urge that the amendment of the distinguished chairman of the committee to do so, be carried out, because if it remains in the bill, when we are through with the conference, in the give-and-take that arise as a matter of necessity in conference, we are going to have, not a \$630 million net deficit, but very likely one of several hundred millions more.

Is that not correct?

Mr. BYRD of Virginia. The Senator is correct.

Madam President, I yield to the distinguished Senator from Oklahoma [Mr. KERR], who I have requested to take charge of the bill on the floor of the Senate because of the fact that I have signed the minority views.

The PRESIDING OFFICER. The Senator from Oklahoma.

Mr. KERR. Madam President, first, I ask unanimous consent that all committee amendments be adopted and that the bill as thus amended be considered as original text for the purpose of further amendment to the bill.

Mr. GORE. Madam President, I object.

The PRESIDING OFFICER. Objection is heard.

Mr. KERR. Madam President, I thank the distinguished Senator from Tennessee for showing his hand. There are many amendments in this bill, and his tactic demonstrates that he is interested purely and solely in delay, because this would change the parliamentary procedure whereby the bill would be considered. The Senator from Oklahoma does not object to that. He believes his physical endurance is equal to that of the Senator from Tennessee, although he does not know that his mental capacity is anywhere in the same orbit as the Senator from Tennessee feels his is. The Senator from Oklahoma will be glad to stand on the floor of the Senate and handle the bill in accordance with the necessary procedure, if the Senator from Tennessee still objects. The Senator from Oklahoma hopes, however, the Senator from Tennessee may reconsider and withdraw the objection.

Mr. GORE. Madam President, will the Senator yield?

Mr. KERR. I yield.

Mr. GORE. I have no dilatory motives in mind in objecting to the request. I understand that such an obnoxious amendment as H.R. 10 may be offered—

Mr. KERR. I did not ask that to be considered. I ask that the committee amendments be adopted and that the bill as thus amended be considered as original text for the purpose of further amendment to the bill. That is the ordinary procedure on every other bill that the committee brings to the floor, and is usually followed so that there may be orderly procedure. I am sure that three-fourths of the committee amendments will be acceptable to the Senator from Tennessee. Yet, under the procedure we shall have to follow if his objection is continued, we shall have to take up each committee amendment separately, as I understand the parliamentary procedure, and consider it.

Mr. GORE. Madam President, will the Senator yield?

Mr. KERR. I yield.

Mr. GORE. Nearly all of the amendments adopted by the Senate Finance Committee made the bill worse instead of better. The Senator has no right to indulge in the presumption that I would agree to most of the amendments; as a matter of fact, I am opposed to most of the amendments adopted by the Senate Finance Committee. Therefore, I shall insist upon my objection, in order to preserve my parliamentary rights to vote on those amendments.

Mr. KERR. Very well. If the Senator insists, he insists.

Mr. CURTIS. Madam President, will the distinguished Senator yield at that point?

Mr. KERR. I yield.

Mr. CURTIS. What bill is before the Senate? Is it the House bill?

Mr. KERR. The committee bill, H.R. 10650 as amended by the Senate committee, is before the Senate.

Mr. CURTIS. If I correctly understood the unanimous-consent request

made by the distinguished senior Senator from Oklahoma, to which an objection was made, my query is, Do we start out with the House bill before us?

Mr. KERR. As I understand the parliamentary procedure, in view of the objection by the Senator from Tennessee—and I will ask the Parliamentarian to advise the Presiding Officer to correct me if I am in error—under the parliamentary procedure the committee bill is before the Senate. The committee amendments will have precedence. The first procedure would be to go through the bill and to vote on the amendments as they appear in the bill.

The PRESIDING OFFICER. The Senator is correct. The House bill is before the Senate, and the committee amendments will be considered one at a time.

Mr. KERR. And the amendments will have precedence. Until they are acted upon, as some might seek to amend them when they are before the Senate, our procedure will be to go through the bill and to act on all the amendments put into the bill by the committee before other amendments, other than an amendment to a committee amendment, would be in order.

The PRESIDING OFFICER. The Senator is correct.

Mr. GORE. Madam President, will the Senator yield for a parliamentary inquiry?

Mr. CURTIS. Then if a committee amendment should fail, we would revert back to the House position on that particular amendment?

Mr. KERR. Insofar as the matter before the Senate is concerned, the Senator is correct.

Mr. WILLIAMS of Delaware. Madam President, will the Senator yield?

Mr. KERR. I yield.

Mr. WILLIAMS of Delaware. I have no objection to the unanimous-consent request which the Senator from Oklahoma has made. This is the customary procedure. As I understand it, in the absence of such an agreement the motion which the Senator from Virginia and some others of us will make to strike from the bill those sections dealing with investment credit would not be in order until after the Senate had gone through the tedious process of acting on each individual amendment in the bill.

Mr. KERR. I think that is correct. Therefore, I repeat what I said, that the action by the Senator from Tennessee can be generated from one purpose only, and that is a dilatory purpose.

Mr. GORE. Madam President, will the Senator yield?

Mr. KERR. For a question.

Mr. GORE. By what right does the senior Senator from Oklahoma attribute to the junior Senator from Tennessee a motive of which he, the senior Senator from Oklahoma, has no knowledge?

Mr. KERR. The Senator from Oklahoma makes the statement, first, on the basis of the right of freedom of expression on the Senate floor; and, second, on the basis of the evidence before the Senator from Oklahoma and the expression of an honest opinion.

There is no possible way for the Senator from Tennessee to prevent the consideration by the Senate of the committee amendments; and he knows, being the experienced parliamentarian he is and one of the most able authorities in the Senate on the rules of the Senate, that the committee amendments will have priority; and he knows that his objection and the failure of the Senate to agree to the request by the Senator from Oklahoma—a procedure which has been followed, so far as I know, in respect to 99 out of 100 bills brought before the Senate by committee—means that the Senate now will have to go through this bill of 392 pages and consider separately each amendment put in the bill by the committee. Then, following that, we shall have the usual procedure of Senators seeking to offer further amendments to the bill.

Madam President, if that is not dilatory, if that is not calculated to cause and to secure delay, then the Senator from Oklahoma is unable to read the evidence plainly before him which results from the action of the Senator from Tennessee.

Mr. GORE. Madam President, will the Senator yield?

Mr. KERR. For a question.

Mr. GORE. I take it the Senator feels that he is entitled to express his personal opinion, which he has now done?

Mr. KERR. Madam President, I do not yield for that, unless it is a question.

Mr. GORE. That is a question. I take it that the Senator feels justified in expressing his personal opinion as to the motives of the junior Senator from Tennessee. Is that correct?

Mr. KERR. That is correct.

Mr. GORE. Does that not in fact constitute a change from the Senator's previous statement, in which he made a flat-footed statement, and did not qualify it as being a matter of his opinion?

Mr. KERR. Well, the Senator may find a distinction there, but it is one without a difference.

Mr. GORE. Madam President, will the Senator yield for a question?

Mr. KERR. Yes.

Mr. GORE. Is not the matter before the Senate—

Mr. KERR. H.R. 10650.

Mr. GORE. Is there not a constitutional requirement that revenue measures shall originate in the House of Representatives?

Mr. KERR. The Senator is familiar with that provision of the Constitution, the same as is the Senator from Oklahoma.

Mr. GORE. If the Senator will permit me to preface my next question with an expression of gratitude for his generous references to my limited knowledge of the rules of the Senate, I will thank the Senator. Then I wish to say to him that I am well aware of the parliamentary rights of every Member of the Senate.

Amendments have been proposed to the bill by a majority of the Senate Finance Committee which would wreck the bill of a Democratic President. I expect to oppose the adoption of some of those amendments, and I want the right to

do so without having them summarily acted upon here by a unanimous-consent operation.

Mr. KERR. I say to the Senator from Tennessee—and he knows it as well as I—that the action requested by the Senator from Oklahoma, if agreed to, would not impair a single right or privilege that the Senator from Tennessee has in that regard. He would still have the right under the unanimous-consent agreement to offer any amendment to the bill which he now has the right to offer. The Senator knows that.

Mr. BUSH. Madam President, will the Senator yield for a question?

Mr. KERR. I yield.

Mr. BUSH. If we follow the pattern suggested by the Senator from Oklahoma, we would start consideration of the bill as though it had no amendments, would we not?

Mr. KERR. The bill will be considered an original text, and it would be subject to and open for amendment by any Senator.

Mr. BUSH. And even the committee amendments would be open to amendments, as though they were not amendments but were a part of the original bill, would they not?

Mr. KERR. The Senator is entirely correct.

Mr. BUSH. That is what the Senator from Oklahoma wants?

Mr. KERR. That is what I asked unanimous consent to obtain.

Mr. BUSH. I would think that would be the orderly way to proceed. I do not know how we can get at the bill unless we do it that way.

Mr. KERR. We will get at it. We will be in that posture many legislature hours, and perhaps days later than now. As I say, my physical endurance, I hope and the Lord be willing, is equal to that of the Senator from Tennessee. Therefore, I promise him faithfully that we will arrive at that point.

Madam President, I shall address myself briefly to some of the statements which have been made on the floor before I move into the presentation of my statement on the bill.

First, I wish to say that no man in the Senate has higher esteem or greater respect for the chairman of the committee than does the Senator from Oklahoma. I have never served with a man in the Senate who had higher ideals, greater patriotism, more rugged devotion to our way of life, our Constitution, and our country, than the great Senator from Virginia [Mr. BYRD]. One of the joys of the Senator from Oklahoma in his service in the Senate has been serving with the Senator from Virginia.

It is interesting to know that while the distinguished Senator from Tennessee [Mr. GORE] has joined in the separate views with reference to the investment credit provisions in the bill, the record of the deliberations, discussions, debate, and votes on the bill will disclose that the chairman of the committee and the Senator from Oklahoma were together 15 times as often as the Senator from Tennessee joined the great chairman in support of decisions on the

bill. I will leave it to the record of what is done on the bill as to who thinks most of the judgment and the ability of the Senator from Virginia [Mr. BYRD] with reference to the bill—the Senator from Oklahoma or the Senator from Tennessee.

The statement was made that the bill would increase the deficit. That question is debatable. I remind Senators that as the bill came to the Finance Committee and as it would have come to the floor of the Senate had the Senator from Oklahoma prevailed in his position on the bill, it would have created a net credit of revenue and no deficit. The action of the committee in deleting from the bill the withholding tax is the justification for statements by anyone who addresses himself to the bill on the basis that it would create a deficit. That is the only reason why a deficit would be created if one were created.

However, in that regard, I should say that in opposition to the withholding provision, our distinguished chairman offered an amendment that would change the present law and regulations with reference to the reporting of interest and dividends paid by payors to payees in our country. I remind my great friend from Virginia that in offering that amendment he told the committee that in his judgment, together with existing law with reference to the handling of income tax returns in the more efficient manner that has been set up for their handling, his amendment with reference to the requirement of those returns would be as productive of additional revenue as would the withholding tax.

After the withholding provision had been taken from the bill by action of the committee, the Senator from Oklahoma joined the chairman in sponsorship of the reporting amendment. In the opinion of the Senator from Oklahoma, this aided in adding to its effectiveness whereby, in the judgment of the Senator from Oklahoma, it well may be that the result of the proposed legislation, including the reporting amendment, will be to produce as much revenue, or nearly so, as the withholding tax would have produced. In that event the bill would produce a net gain and not a deficit.

The distinguished chairman, with much vigorous and enthusiastic support from other Senators, complained of the investment credit provisions in the bill on the basis that it applied to new equipment in old buildings, but would not apply to the building. I think perhaps most of the teeth were pulled from that criticism by the next statement of our distinguished and beloved chairman when he said that if it did apply to both buildings and the equipment contained in them or to be placed in them, he would be even more critical of the bill than he is without the investment credit being applicable to the buildings.

He made the statement that the investment credit provisions are more favorable to big business than to small business. I cannot agree with my great friend in that regard. It will be my purpose to state, to document, and to prove in the course of the debate that the in-

vestment credit provisions in the bill would be more beneficial and more favorable to small business than to big business, relatively and proportionately and that the provisions of the bill are especially favorable to agriculture.

It has been urged that increased and more accelerated depreciation be provided as an incentive to greater development in lieu of the investment credit. Yet the fact remains that acceleration of depreciation could not be more favorable to small business than to big business. It could not be more favorable to agriculture than to industry generally because depreciation provisions are a deduction from income, not a credit against tax. A deduction from income will help the small farmer subject to a 20-percent tax rate or the small corporation subject to a 30-percent rate less than the larger corporation subject to a 52-percent rate of tax.

But the investment credit provision in the bill, since it is a credit directly against tax, will give the small farmer or small corporation the same dollar reduction in tax as the larger corporation, assuming the same investment is made by each.

My good friend the Senator from Tennessee [Mr. GORE] had a good deal to say about the specific examples referred to at page 155 of the Senate committee report. The specific examples of qualifying property which would normally be used as an integral part of one of the specified activities include blast furnaces, oil and gas pipelines, railroad tracks, and signals. Had he gone on, he would have read that fences would qualify as section 38 property where used as an integral part of a specified activity, as, for example, where used in connection with the raising of livestock.

He made some especially critical remarks about that, by reason of the fact that the oil and gas industry would be the beneficiary. I must make two statements about that point. The language in the bill as it has come from the Finance Committee to the Senate is identical with the language in the bill as it came from the House to the Finance Committee. The Senator from Tennessee was present during the deliberations of the Finance Committee, I presume, as regularly as any other member of the committee. Not once did he raise his voice in opposition to that provision in the bill. He offered many amendments to the bill, but not to that section.

With reference to that section, I say to the Senator from Tennessee that the benefits would go to the consumers, not the gas pipelines. If the Senator from Tennessee were aware of the facts in the case, the rules and regulations of the Federal Power Commission, and the applicable law, he would have known that. The interstate gas pipeline carriers are a regulated utility, and, under the operations of the Federal Power Commission, any saving effected by them reduces their rate base.

It results directly in benefit to the consumer, not to the regulated utility which is an interstate gas carrier. The same is true with reference, in a measure, to

oil pipelines. They are common carriers. Any benefits they receive in the long practice is passed on to the consumers.

Mr. GORE. Madam President, will the Senator yield?

Mr. KERR. I will yield in a moment. My friend from Virginia referred to page 347 of the report, to the findings of the joint committee staff, reading:

Business tax liabilities would be reduced during that period—

The years 1962-72—

by \$21 billion under the House-passed version; and business tax liabilities would be reduced during that period by \$15.6 billion under the Senate committee version.

Then my good friend from Virginia says that such a tax reduction would be ineffective. How could such a tax reduction, as an incentive to the expansion of business industrial facilities be insignificant?

All who oppose the bill have hailed the action of the Treasury and the Internal Revenue Service in increasing the depreciation for a tax chargeoff of depreciable items, talking about how beneficial the savings to the taxpayers of more than a billion dollars a year would be and how it would stimulate and augment the expansion and modernization of our industrial workshop, its efficiency, its productivity, and its effectiveness.

It presents a strange paradox to the Senator from Oklahoma that the reduction of taxable income by \$1,250 million a year would be a great stimulant to industry in improving efficiency, by its machinery and its industrial workshop, but that a tax credit of \$1,250 million a year would be ineffective as a stimulant. The cold facts are that the benefits to the taxpayer of a tax credit of \$1,250 million is worth at least twice as much to the taxpayer as an increase in the amount that the depreciation chargeoff in the same amount could possibly be.

I now yield to the Senator from Tennessee for a question, if he has one.

Mr. GORE. I have two questions.

Mr. KERR. I will yield to him for one question at a time. It will be discretionary entirely with respect to each one whether I will yield.

Mr. GORE. In view of the statement of the distinguished and able senior Senator from Oklahoma, with respect to the regulation of gas and oil pipelines as utilities, how does he justify an investment credit of 7 percent to gas and oil pipelines and only 3 percent to an electric utility?

Mr. KERR. Well, I will say to my good friend from Tennessee that if the Senator from Oklahoma had had his way, the investment credit for all utilities would have been set at 7 percent. However the Senator from Tennessee, while he was opposed to any investment credit, never at one time offered an amendment, in the considerations or deliberations by the Finance Committee, that the tax credit as between utilities and nonutilities be equalized, or that the tax credit in the bill of 7 percent for interstate gas pipeline carriers, which are regulated utilities, be changed to the 3 percent tax credit of electrical utilities,

or that the one available to electric utilities be made equal to that of interstate gas pipeline carrier utilities. The Senator from Oklahoma would have made the 7 percent applicable to all of them. The Senator from Tennessee would have made it applicable to none of them. Therefore, the Senator from Oklahoma says that he is very glad to have been able to bring to the Senate as much of the administration's proposal with reference to the investment credit as he did. In order that the record may be crystal clear, on this point, however, the Senator from Oklahoma makes the statement that the administration did not ask for the application of the investment credit to regulated utilities.

Mr. GORE. Madam President, will the Senator yield?

Mr. KERR. For a question.

Mr. GORE. Being aware, as the Senator from Oklahoma is aware, that the junior Senator from Tennessee offered several amendments, as has already been attested to by the senior Senator from Oklahoma, but without having had too much luck with his amendments in the Committee on Finance, would not the junior Senator from Tennessee be clearly within his rights as a Senator to appeal to the Senate as a whole for the correction of errors and mistakes not only in the bill but in the majority report, which gives legislative intent with respect to the bill?

Mr. KERR. The Senator from Tennessee is clearly within his rights. The Senator from Oklahoma respects him as much as he respects any other Member. Like the Senator from Oklahoma, he is within his rights to do that. Although the Senator from Tennessee felt one provision of the House bill was abhorrent to him, he did not get around to offering an amendment. The Senator from Oklahoma does not know whether that was because he was weary of well-doing, or whether he decided to wait until he had a larger forum in which to give expression to his great thoughts and language, by bringing them up on the floor of the Senate.

Mr. GORE. In either event, my friend from Oklahoma will, I am sure, be happy to afford the Senator from Tennessee that opportunity.

Mr. KERR. Oh, the Senator from Oklahoma will have a lot of fun with the Senator from Tennessee.

I have great affection for the Senator from Tennessee. He and I have a great deal in common, including bull—that is, Angus bulls and Angus cattle. The Senator from Tennessee has been very close to the Senator from Oklahoma in many ways, both on and off the Senate floor. He loves him and respects him, and once in a while agrees with him. When I do agree with him, I find it a source of great pleasure. I remind my good friend from Virginia, the chairman of the committee, that he and I will be together on the bill at least 15 times for each time the Senator from Tennessee will be.

Madam President, the pending bill, H.R. 10650, represents a major revision and reform of our Federal tax system. It has been under consideration by Con-

gress since April 20, 1961, when the President sent up his tax message. It was under consideration by the other body for almost 1 year.

Your committee began hearings on this bill on April 2, 1962, and has been working on it almost constantly since that time. As indicated in the committee report, we heard testimony on the bill for 29 days. The testimony fills 12 volumes—nearly 5,000 printed pages. In addition, the Committee on Finance has considered this bill in executive session over a period of many weeks.

This has not been an easy bill. The further we discuss it, the more apparent that will become. It contains important legislation in many areas. The bill as passed by the House covered 21 separate areas, and the bill with the committee's amendments covers 27. Several of the members of the committee filed individual, additional dissenting, supplemental, or minority views on one or more provisions. Probably none of us would have phrased all of the provisions of the bill exactly as they have been phrased. First, the other body and then your committee has had to work out compromises on many of the provisions. But, Madam President, it is a tribute to our legislative system and to the Senate and the Finance Committee that differences have been resolved, decisions have been reached and this constructive bill is now before us for consideration and action.

This process is inevitable on any major tax bill. The bill of necessity must be a compromise of conflicting views. It must take account of the views of the administration; the views of the other body; and the views of the Finance Committee and the Senate. Under the leadership of our great chairman and in large part due to his continuing and patient effort, the committee has done a fine job. The very fact that some members of the committee believe the bill goes too far while others believe that it does not go far enough is an indication that the bill in fact goes down the middle of the road. Thus, we have retained the investment credit which is so necessary to our economic growth. At the same time the Long amendment—which I shall explain somewhat later—provides that to the extent taxpayers receive an investment credit with respect to property, they must reduce their depreciation basis by the amount of the credit.

That is a complete answer to the claim that the bill gives a taxpayer more than 100 cents back for every dollar of investment he makes. In the first place, a taxpayer depreciates 100 percent of the value of his investment. His investment in the property is 93 percent. He depreciates 100 percent of this amount. Depreciation is not given on any part of the tax credit. It is a reduction of income subject to tax. A taxpayer can get his credit on 7 cents of a dollar. On this he gets no depreciation. This is treated as if it were an investment made by someone else. His depreciable base will be reduced by the amount of the tax credit. As a result he can depreciate only 93 percent of the cost of a property. In this the taxpayer and the Government are treated as jointly pur-

chasing the property. This is the result of an amendment adopted by the committee. It provides that whatever the amount of the tax credit a taxpayer gets with reference to the investment in an item, the depreciation base is reduced by this amount. Thus if he gets a 7-percent tax credit, his depreciation base is reduced from \$1 to 93 cents, and the depreciation, then, which he charges off from taxable income is 93 cents on the dollar, not to 100 cents on the dollar.

In the area of taxation of foreign income, the bill is a compromise of conflicting views. The President asked us to end tax deferral for foreign subsidiaries and there are those on our committee who believe we should have done this. That was not the conclusion, however, of either the House or your committee. We recognized the principle that income earned in foreign countries by Americans through foreign subsidiaries should be treated in the same manner as income earned by the nationals of those countries—so long as the earnings remain abroad. However, many abuse situations have been called to the attention of your committee where, through the use of tax haven devices, taxes are being avoided through the diversion of income to companies incorporated outside of the countries where normal operations are being carried on. These tax haven abuse situations are corrected by your committee's bill even though tax deferral for foreign operations in general is continued. Numerous other tax loopholes which exist in the foreign area are also plugged by this bill.

In other areas as well, the committee's bill works out compromises where there are different points of view. In the taxation of mutual savings banks, and savings and loan associations, your committee's bill, while not going as far as the Administration asked, nevertheless, raises \$180 to \$205 million of additional revenue. In the tax treatment of mutual fire and casualty insurance companies you committee and the House have found a compromise that recognizes the real differences among the various kinds of companies in the industry.

In dealing with the problem of underreporting of dividends and interest, the committee also has found at least a partial answer which is a more moderate approach than withholding. We recognize that between four and five billion dollars of dividend and interest income presently is escaping taxation. However, instead of providing a withholding system which involves burdens for both the payors and the many people who owe little or no taxes, the committee has followed the course of requiring full information reporting to both the Government and the recipients on all dividend and interest payments of \$10 or more. While I personally counseled the committee to follow the course of withholding, I realize that the more moderate provision in the bill will go far to correct the underreporting of dividends and interest.

I shall refer to this again, and often, Madam President, because to the extent

it does what its principal author indicated his judgment was that it would do, it not only would eliminate any deficit by reason of the bill, it will provide a surplus by reason of the bill.

In dealing with entertainment expenditures, also, the committee has adopted a balanced approach which neither prevents the deduction of legitimate entertainment expenses nor permits the continuation of the abuse situations which have been called to your committee's attention.

I believe that the bill makes a substantial improvement in our tax structure and will lay to rest many of the tax problems which have been plaguing us for many years. At the same time this bill will, through the investment credit, provide a necessary stimulant to our economic growth.

The revenue impact of the bill is difficult to determine. Because of the nature of many of its provisions, adequate statistical information is not available. This probably accounts for the fact that the revenue estimates furnished the committee vary more than is usually the case. The estimates of the staff of the Joint Committee are that the bill on a full year's basis will result in a revenue loss of \$555 million.

The estimate made by the Joint Committee is that on a 1-year basis the bill will result in a revenue loss of \$555 million. The comparable estimate of the Treasury Department is that the bill will result in a loss of \$210 million. However, neither of these estimates takes into account the stimulative effect of the bill on investments and the level of economic activity, nor does either of them take into account the extent to which the reporting substitute will recover taxes not now being paid on unreported interest and dividends.

The Joint Committee staff has made no estimate on this basis but the Treasury Department has estimated that the stimulative effect will reduce the revenue loss under the bill to \$15 million—a negligible loss for a bill of the magnitude of H.R. 10650. If the estimates of the revenue that will be collected because of the Byrd dividend and interest reporting amendment are valid and prove to be justified, the bill will actually result in increased revenue to the Treasury. In other words, under these provisions the additional revenue collected under the provisions of this bill will exceed the amount of the revenue lost to the Treasury under the provisions of the bill.

Mr. President, at this point I ask unanimous consent to have printed in the RECORD three tables showing the revenue estimates prepared by the staff of the Joint Committee and the Treasury Department for your committee. In addition to the full-year revenue effect, these tables also show the revenue effect anticipated in the fiscal year 1963. The revenue loss in this case is greater than will be the eventual impact of the bill because the loophole closing provisions do not become effective immediately.

The PRESIDING OFFICER (Mr. METCALF in the chair). Is there objection? There being no objection, the tables were ordered to be printed in the RECORD, as follows:

TABLE 1.—Estimated full-year revenue effect on H.R. 10650¹ as passed by the House and as amended by the Senate Committee on Finance

[Millions of dollars]		
	As passed by the House	As amended by the Committee on Finance
Investment tax credit.....	-1,395	-1,340
Withholding on dividends and interest.....	+350	-----
Reporting of dividend and interest payments.....	-----	+275
Mutual banks and savings and loan associations.....	² +170	² +180
Entertainment, etc., expenses.....	+125	+85
Capital gains on depreciable property.....	+110	+105
Mutual fire and casualty companies.....	³ +25	³ +25
Cooperatives.....	+30	+30
Foreign items:		
Controlled foreign corporations.....	+50	+50
Gross-up of dividends.....	+25	+15
All other foreign items.....	+25	+25
Other (secs. 21-26 of Senate Finance Committee bill).....	-----	-5
Total.....	-285	-555

¹ At levels of income and investment estimated for the calendar year 1962, without taking into account effect of provisions on the economy; estimates are rounded to nearest \$5,000,000.

² The level of income for these thrift institutions in 1962 has been revised upward since the preparation of the revenue estimates for the House bill.

³ Revenue gain which would result if this provision were in effect for 1962 and had been in effect for the 5 preceding years, so that amounts added to the protection against loss account in the first year and not offset by losses would be brought into taxable income in 1962.

Source: Staff of the Joint Committee on Internal Revenue Taxation.

TABLE 2.—Estimated revenue effect of H.R. 10650 for the fiscal year 1963 as passed by the House and as amended by the Senate Committee on Finance

[Millions of dollars]		
	As passed by the House ¹	As amended by the Committee on Finance ¹
Investment tax credit.....	-1,340	-650
Withholding on dividends and interest.....	+170	-----
Reporting of dividend and interest payments.....	-----	0
Mutual banks and savings and loan associations.....	+10	+10
Entertainment, etc., expenses.....	+60	(+2)
Capital gains on depreciable property.....	0	0
Mutual fire and casualty companies.....	0	0
Cooperatives.....	0	0
Foreign items:		
Controlled foreign corporations.....	0	0
Gross-up of dividends.....	0	0
All other foreign items.....	+10	+10
Other (secs. 21-28 of Senate Finance Committee bill).....	-----	(?)
Total.....	-1,090	-630

¹ Estimates are rounded to nearest \$5,000,000.
² Less than \$2,500,000.

Source: Staff of the Joint Committee on Internal Revenue Taxation.

TABLE 3.—Estimated revenue effect of H.R. 10650 as amended by the Senate Finance Committee

	As passed by House of Representatives				As amended by Senate Finance Committee			
	Full year		Fiscal year 1963		Full year		Fiscal year 1963	
	Gross	Net	Gross	Net	Gross	Net	Gross	Net
Investment tax credit ¹	-1,105	-555	-1,040	-525	-1,020	-580	-520	-235
Capital gains on depreciable property.....	+100	+50	-----	-----	+100	+50	-----	-----
Withholding on dividends and interest.....	+780	+520	+245	+235	+240	+155	-----	-----
Expense accounts.....	+125	+80	+65	+40	+60	+40	+30	+20
Mutual savings banks and savings and loan associations.....	+200	+135	-----	-----	+205	+140	-----	-----
Mutual fire and casualty companies.....	+40	+25	-----	-----	+35	+20	-----	-----
Cooperatives.....	+35	+25	-----	-----	+35	+25	-----	-----
Foreign items:								
Controlled foreign corporations.....	+85	+85	-----	-----	+85	+85	-----	-----
Gross-up of dividends.....	+35	+35	-----	-----	+25	+25	-----	-----
All other foreign items.....	+30	+30	+5	+5	+30	+30	+5	+5
Miscellaneous provisions.....	-----	-----	-----	-----	-5	-5	-0	-0
Total.....	+325	+430	-725	-245	-210	-15	-485	-210

¹ At levels of income and investment estimated for 1962; modified from published estimates because of current results of the Commerce-SEC survey of planned capital expenditures. In estimating the net revenue cost of the investment credit, its favorable effects on the level of investment were computed from statistical relationships in the past years between investment and gradual changes in the cost of capital goods (profitability) and cash flow. This procedure thus does not take into account the especially favorable impact on businessmen's decisions to invest on the sudden major improvements in these factors resulting from the enactment of the credit. Taking this into account should produce more favorable effects than those shown in the table.

² Estimated gain from increased compliance because of reporting requirements.

INVESTMENT CREDIT

Mr. KERR. Mr. President, the bill provides an investment credit against taxes of 7 percent of "qualified investment." In the case of property with an expected life of 4 to 8 years, the investment taken into account for purposes of the credit is one-third of the cost in the case of assets with a life of 4 to 6 years, two-thirds of the cost for assets with a life of 6 to 8 years, and 100 percent of the cost for assets with a useful life of 8 years or more. In the case of most pub-

lic utilities, a 3 percent investment credit is allowed instead of the 7 percent credit generally available. The lower credit in this case is provided because of the belief that a portion of the investment credit in the case of these public utilities would, if the full credit were allowed, be reflected in price reductions rather than the additional investment sought by the bill and because investment by public utilities is frequently governed by their legal obligation to serve the public.

The types of property which are in-

cluded in qualified investment and which therefore are eligible for the investment credit include most depreciable tangible personal property, such as machinery and equipment—whether owned by an industrial, agricultural, mining, or any other business and whether owned by individuals or corporations. Certain real property—such as blast furnaces—apart from buildings or structural components, is also eligible for the credit.

Generally, property eligible for the credit must be new property acquired or constructed since June 30, 1962. However, in the interest of aiding small business, the bill also makes the investment credit available with respect to purchases, after that date, of up to \$50,000 per year in used property.

The credit can offset dollar-for-dollar tax liabilities up to \$25,000. In addition, the credit may offset 25 percent of tax liabilities above \$25,000. The amount of any credit which cannot be used in this manner is available as a carryback to the 3 prior years—but not before a credit is available—and then as a carry forward to the 5 succeeding years.

The bill also provides a "recapture" rule if property is disposed of within less than its estimated useful life, but only where this is less than 8 years. This recapture rule prevents taxpayers from obtaining a windfall by overestimating the useful lives of their assets.

Your committee has also added two amendments to the investment credit. One of these provides that the depreciation base is to be reduced by the amount of the credit. Thus, if a taxpayer purchases a \$100 asset and is eligible for a \$7 credit, he may then depreciate \$93 rather than \$100. This modification recognizes the fact that the taxpayer received a tax reduction of \$7 on account of the investment, and therefore should be permitted to depreciate only his actual net cost.

Your committee has also added an amendment, sponsored by the Senator from Virginia [Mr. Byrd] to provide that where property is lost by fire, theft, or other casualty, and where insurance proceeds are used to purchase other similar property, the investment credit is not to be available for such a repurchase. This denies an investment credit in cases in which the taxpayer is not himself really contributing new funds for investment purposes.

The investment credit section of this bill is the most important tax proposal to be considered by this body since the adoption of the Revenue Code of 1954. The changes it will make in our tax laws are both fundamental and far reaching.

Our tax treatment of investment has remained unchanged since 1954. In that time the role of leader of the free world has imposed on the United States a heavy burden for defense and development. One result of that burden is a deficit in our balance of payments. The most effective way to reduce and eventually eliminate that deficit—and the gold drain that it causes—is to expand our exports.

But a second development since 1954 makes expanding our trade surplus a greater task than it might at first ap-

pear. In that time—and, Mr. President, later I shall document this point in more detail—the other industrial nations, with few exceptions, have enjoyed a period of growth, development, and modernization of productive capacity unequaled in recent history. If our producers are to compete effectively against these nations—not only in world markets but even in our own markets here at home—they must marshal all their resources. We believe that the trade bill will assure that the products of American enterprise can enter these markets and compete on fair terms. But this is not enough; once there, these products must be able to compete effectively.

Our economic experience at home since 1954 is equally significant. In those years the United States watched the rapid and virtually uninterrupted postwar expansion of prosperity abroad, and suffered two recessions at home. During that time capital investment in Western Europe was growing at an annual rate of 5 percent, in West Germany at better than 7 percent, and in Japan at better than 10 percent. Our own rate was close to 3 percent, and for part of that period even dropped considerably below that. Even during recovery periods the U.S. economy seemed unable to achieve the momentum required for sustained prosperity, and unemployment has remained high. This stubborn persistence of unemployment marked each of the two recoveries in this period, and each time the problem has been more serious. Our economy has shown a tendency to pause and to slacken in pace far below full employment, far below our real potential. There is general agreement that more rapid growth is needed, and the only question is how to achieve it.

Expanded exports and faster growth are goals we can and will achieve, but they require more than faith in our system, more than faith in our ability to compete. They require a significantly higher rate of private investment in this country in more efficient productive equipment.

If the United States is going to compete effectively, greater productivity is needed and lower unit costs are required, in order to keep prices down and quality up.

This means more modern machinery, which can only be provided through greater investment.

Higher investment is also important in stepping up our long-term rate of economic growth. Almost without exception, other industrial nations with a higher proportion of output devoted to domestic investment have achieved higher growth rates. The correlation is a striking one—as investment rises, growth accelerates. The two nations which have expanded most rapidly in recent years—Germany and Japan—have devoted a proportion of output to investment almost double our own, and have grown almost twice as fast. There is nothing mystical about this. Greater investment means higher productivity, more effective utilization of industrial potential, new products, better technology, and greater efficiency all along the line—efficiency that pays off in domestic

as well as foreign markets, efficiency that pays off in jobs as well as output.

Greater investment will also pay off immediately in some significant short-term effects. The purchase of new equipment stimulates capital goods and allied industries, and will also have an effect on maintaining, rejuvenating, or expanding marginal operations which require high investment to remain competitive. Clearly, the recent lag in economic expansion we have seen was in good part the result of a lower level of capital investment than had been expected.

Last month the Treasury completed a sweeping reform of rules and procedures regarding tax treatment of depreciable equipment. This reform will result in tax savings to American producers of an estimated \$1.5 billion in the first year. It is a strong, long overdue stimulus to greater investment. It is, however, not enough. The Treasury went as far as it legally could under existing authority. What it did was to bring tax depreciation policy up to date with the modern pace of technological change and obsolescence.

It remains for the Congress to provide the further change in tax policy which will put our manufacturers on an even footing with their foreign competition with respect to the tax treatment of new investment. That is what the investment credit is designed to do.

The investment credit will stimulate investment in several ways. First, it will reduce the net cost of purchasing new equipment. This lower cost has the effect of increasing the rate of return after taxes from such equipment. It will also increase the cash flow, making available more funds to finance expansion and modernization. This will be particularly effective in stimulating greater investment by smaller firms, with limited borrowing capacity. Finally, by reducing the period of risk—the time it takes to recover the cost of new equipment—it will act as a further stimulus. Increased cash flow, reduction in risk, and higher profitability will all work toward lower existing barriers to higher investment levels, and help raise investment levels to the point where they can compare favorably not only to our previous levels—in proportion to total output—but also to current levels in other developed nations.

At first there was considerable opposition to the credit. Some businessmen opposed it because they did not initially understand its provisions and because they feared it was intended as a substitute for depreciation reform. Now the credit, and its benefits to business and the country as a whole, are more widely understood.

There was the principal source of objection, Mr. President. As Members of the Senate know, since the announcement by the Treasury of its new depreciation formula, there has been a great surge of support from across the length and breadth of this Nation, from the industrial community, for the enactment of the investment credit provision, and it has been more widely understood to be for the benefit of the country as a whole.

Despite the continuing preference of some businessmen for accelerated depreciation, the fact is that the credit provides the best investment stimulus available, and accelerated depreciation provides significantly less stimulation per dollar of tax loss to the Government.

Considerable misunderstanding of the investment credit remains, however, and this misunderstanding is responsible for some of the opposition to it.

Some opponents maintain that the Treasury depreciation reform makes the investment credit unnecessary. That simply is not correct. In first-year cost recovery which reflects the period of risk—the depreciation revision does not bring our manufacturers even halfway toward closing the gap with their European competitors. First-year cost recovery is now only 13 percent in American industry, and depreciation revision brings it only up to 17 percent, while our nine major industrial competitors average 29 percent. The investment credit, however, would not only close that gap, but even give American industry a slight edge over the average of the other nine nations. The investment credit concept is widely accepted abroad, is already in use by the United Kingdom, Belgium, and the Netherlands, and other nations use comparable measures.

Other opponents claim that the revenue loss from the credit would be better spent in a reduction of tax rates, either for individual or corporate taxpayers, or both. The credit will reduce business taxes by more than a billion dollars the first year, but the stimulative effect of a direct tax cut of that amount would be minor compared to the cumulative stimulus of the credit.

Some feel that, as long as businessmen prefer accelerated depreciation, why not give them what they want? This argument overlooks the fact that even the mildest sort of accelerated depreciation—increasing declining balance depreciation from the present 200 to 250 percent—would cost nearly as much as the credit initially, and considerably more as time went on.

Most important, this alternative would produce only a fraction of the stimulative effect—in my judgment, less than 40 percent of the effect from the 7-percent credit in the proposal before the Senate.

Some opponents of the credit claim that it is merely a subsidy for business, that it will provide a windfall gain for investment which would have been made anyway. But this is a misunderstanding of the credit.

It is not a subsidy; it is a tax reduction.

The Senator from Oklahoma has been here nearly 14 years. This is the first time he has ever seen or heard the accusation made that a tax reduction constitutes a subsidy. The provisions of this legislation, Mr. President, constitute a tax reduction, and by no stretch of the imagination can a tax reduction be made synonymous with a subsidy. Such is not the case, and the repeated statement of it does not make it so.

The tax credit gives no money to anyone. It merely permits one to retain a part of his own earnings which he is

not now permitted to retain. Any tax reduction is selective to some extent; yet I have not heard a rate cut referred to as a subsidy. Men argue, "Give us an overall corporate tax reduction instead of investment credit."

If an investment credit, available to both corporations and individuals is a subsidy, then a tax reduction to all taxpayers is a subsidy. In this case how would it be possible to fashion any tax reduction for corporations only that would not be a subsidy, and a discriminatory subsidy at that?

The tax investment credit provision before the Senate would be available to all taxpayers; farmers, individuals, partnerships, as well as corporations. It would be equally effective as applied to each and every one of them.

How can men of broad knowledge and understanding say, "Such a tax reduction, available to all taxpayers, is a subsidy. Let us abhor it. Let us repudiate it. Let us spurn it and give a tax reduction to one group only, to corporate taxpayers?"

It is true that the benefit of the investment credit will be limited to those who make investments. But even an income tax rate cut benefits those who have income and not those with no income. Moreover, any form of accelerated depreciation selects for benefit those who acquire new assets in much the same manner as the investment credit. There is no way to provide for the overriding national need for additional investment without giving those who make the needed investments some incentive and even some advantage over those who do nothing in this respect.

A survey of 6,000 executives by the Research Institute of America—a private firm—showed 65 percent in favor of the investment credit. Many associations and leading executives in the textile, machinery, coal and steel industries, railroads, and chemicals and others have publicly endorsed the investment credit provision of the bill.

FOREIGN PROVISIONS

Twelve out of the twenty-seven sections of this bill deal with foreign income or estate matters. This is a part of our tax law which is in many ways out of touch with present economic and political realities and in which many flagrant abuses and loopholes exist.

Opportunities for tax abuse in the foreign income area have received much publicity in the last few years. The proper objective of the foreign income tax provisions also is a much debated and much disputed point. The administration has requested that we end deferral of U.S. tax for U.S.-controlled foreign corporations. This bill does not adopt this principle nor achieve this objective. Instead, the foreign income provisions of the bill are aimed at a much more limited objective, which should be acceptable to all—an ending of tax haven abuses or an ending of attempts to avoid U.S. or foreign taxes by the use of artificial corporate devices or selection of countries for incorporation for tax, rather than business, purposes. The House bill had the same objective of ending tax haven abuses, but testimony

before the committee showed that in practice it would have imposed U.S. tax on the undistributed earnings of operating businesses. For that reason the committee has carefully screened out of the House provisions those features which would have interfered with legitimate foreign operations of American controlled corporations. I believe Senators will find most thoughtful businessmen who have foreign operations and who have studied the revised bill will agree that the committee's action achieves this objective.

The chief foreign income provision is section 12 which is aimed at the abuse of tax haven foreign subsidiaries. Section 12 reaches abuse situations such as are involved in U.S.-owned insurance companies which operate overseas solely for the purpose of tax avoidance—a purpose which is demonstrated by the fact that such companies insure or reinsure against risks on the lives and health of U.S. individuals and loss on property located in this country. Usually these companies are incorporated in the Bahamas or some other country having either no, or a very low, income tax.

Another common example of what we cover is the tax haven holding company—many times a mere "paper" company—which exists mainly for the purpose of receiving income which it has done nothing to earn and which prevents that income from coming home to the United States where it will help our balance of payments, produce tax revenues, and be available for investment in the United States. These are covered by taxing all investment-type income where this and other tax haven income represents 30 percent or more of the foreign corporation's income. Even then, however, dividend and interest income from a related corporation in a less developed country is not taxed to the U.S. shareholders when this income is reinvested in a less-developed country.

Another example of income taxed to U.S. shareholders under the bill is income of a tax haven trading company, such as the Swiss corporation which often serves as merely an address for sales made in every country in Europe except Switzerland. The ability to syphon off profits from Common Market operations into Switzerland or some other low-tax-rate country in many cases makes it more advantageous to manufacture in European countries, such as Germany and France, than to export from the United States to those countries.

The bill reaches this tax haven trading income by taxing to U.S. shareholders' income of a controlled foreign corporation deriving income from sales outside of the country in which it is incorporated if the products involved were either purchased from or sold to a related corporation. Income from services performed for related persons outside of the country in which the controlled foreign company is incorporated also is taxed in a similar fashion.

So far I have described to Senators how the committee's bill reaches tax haven income. However, let me make it very clear that this legislation does

not affect legitimate operations overseas. So, if an American corporation organizes a foreign subsidiary in France, for example, to manufacture goods in that country and to sell those goods directly in any country in the world, the income produced by the manufacture and sale of goods by the corporation in France is not to be taxed under this bill. Thus, we have been careful not to cover foreign subsidiaries engaged in actual mining or manufacturing, no matter where they sell their products, because these subsidiary corporations are in an entirely different class from the tax haven companies looking for a tax shelter.

There are those who do not understand these foreign provisions and believe they will hurt our legitimate operations abroad. I want to show Senators why this is not true.

As I previously indicated, we have provided a rule to the effect that unless a company has more than 30 percent tax haven income it will not be affected.

We have also developed a provision to the effect that an oversea organization which makes a minimum distribution to its U.S. parent will not be covered by the new section 12. Only those foreign operations which pay low foreign taxes and make substantial distributions to the United States—the true tax haven type of situation—will be unable to utilize this minimum distribution alternative and will still come under the new tax haven legislation. This minimum distribution alternative insures that we only reach the abuses in the foreign income area.

Further, we have developed a provision which frees from section 12 certain foreign companies that export U.S. products abroad. These companies by so doing make a contribution to our domestic economy and balance of payments and we have given them a stimulus in this bill to continue to do this. What would otherwise be the tax haven income of these companies is not taxed if it is reasonable relative to the sales made—that is, does not exceed $1\frac{1}{2}$ times export promotion expenses or 10 percent of gross receipts—and if this income is invested in the export trade business.

Mr. GORE. Mr. President, will the Senator yield?

Mr. KERR. I yield for a question.

Mr. GORE. In the light of the Senator's successful business experience, does he not think that 10 percent of gross is a remarkably large amount on which to give tax deduction or deferral?

Mr. KERR. It is "whichever is lesser," I say to the Senator, and not "whichever is greater." The 10 percent would not come into effect unless it were less than $1\frac{1}{2}$ times export promotion expenses.

The Senator from Oklahoma thinks that is not only a very effective protective feature but that taken together with others, would provide a very effective stimulant to a continuation of the effort of American productive companies to export products to foreign countries through foreign subsidiaries, which would promote jobs at home, bring back dollars to our country, improve our balance of payment, and encourage in every way the competitive position of our own

industrial workshop in the markets of the world.

Mr. GORE. Mr. President, will the Senator yield for a question?

Mr. KERR. I yield.

Mr. GORE. Would not $1\frac{1}{2}$ times export promotion expenses, assuming that the export promotion expenses are based upon the cost of the product that is being exported, amount to a 50-percent profit?

Mr. KERR. Not at all.

Mr. GORE. One and one-half times is 150 percent, is it not?

Mr. KERR. Times export promotion expenses. These are certain specified expenses listed in the bill. They do not include the cost of the product. In addition, the exemption does not apply unless the money thus made is invested in a further effort by the foreign corporation to promote the sales of American-produced products and commodities abroad.

Mr. GORE. Mr. President, will the Senator yield further?

Mr. KERR. I yield.

Mr. GORE. Does that not also include credits extended?

Mr. KERR. Only promotion expenses in connection with credits, not the credits themselves.

Mr. GORE. How does the Senator justify that?

Mr. KERR. The Senator happens to be somewhat familiar with the way business is promoted and carried on. The fact that there is more than \$50 billion of consumer credit in our country, in the form of installment payments by American consumers, is evidence of the fact that American productive facilities think that the promotion of credit in connection with the sale of its products stimulates its business. The Senator from Oklahoma thinks that the promotion expenses in connection with extending credit to foreign consumers would be small.

Mr. GORE. Mr. President, will the Senator yield?

Mr. KERR. For a question.

Mr. GORE. Would that not apply to the products of a factory situated abroad, employing exclusively foreign workers, but owned by a subsidiary of an American corporation, adding to the capital wealth exclusively of the foreign country?

Mr. KERR. The Senator's question illustrates a statement which the Senator from Oklahoma made awhile ago. If men knew more about the bill, they would oppose it less. This export trade corporation provision of the bill applies only to the sale of goods produced in this country and sold through a foreign subsidiary. It was put in the bill to promote the export of American products produced by American industry, made by American workers, and would bring back to these shores American dollars, which would benefit our balance of payments, and increase the stability, value, and reliability of the dollar.

It would provide a stimulus for the production in America of goods to move into the channels of trade in world commerce. It is calculated to stimulate industrial growth, expansion, and increase the available jobs at home. A company

that sets up a foreign subsidiary for the purpose of the sale of those American-produced products which does increase our industrial output, our taxable income, and jobs at home, an incentive is provided in the bill whereby such companies may sell and be encouraged to distribute more widely their products in the markets of the world, which are constantly expanding. If we are going to be able to compete with industrialists in other nations who have far greater tax concessions than the ones we now have and the ones proposed in the bill, we must improve the economic environment in which our industrial workshop lives, expands, and has its profitable existence. It is the purpose of the bill, and of that provision of the bill specifically, to provide that stimulant, that encouragement, and that improvement.

Also taxed to U.S. shareholders is income earned abroad which is brought back, other than in the form of a dividend, and invested in the United States. There are, of course, appropriate exceptions for assets located here which nevertheless are used in the foreign business.

Section 12 should end the tax haven abuse and, therefore, is an important loophole-closing section. On the other hand, section 12, as amended by the committee, does not interfere with those foreign operations—particularly the export of U.S. products—which are clearly in our national interest.

There is nothing in the bill that interferes with investment abroad which is made for sound economic reasons. As I mentioned before, the President asked us to impose U.S. tax on the profits of all foreign subsidiaries of U.S. companies. Neither we nor the other body felt that this was necessary in order to achieve the President's major purposes. I am convinced that under this bill we do accomplish those major purposes but without interfering in any way with the normal nontax haven foreign subsidiary abroad—such as ones engaged in manufacturing.

What purposes have we achieved? In the first place, we have eliminated special tax advantages that exist under the use of tax haven subsidiaries. It will no longer be possible to flout our tax laws by simply setting up an address company, say in Panama, to sell goods in Europe which did not originate in Panama, which never in fact were in Panama, and which had nothing to do with Panama. The elimination of such gross abuses is something that we owe to the millions of taxpayers who must pay their normal tax burdens and who cannot, or will not, take advantage of this kind of loophole.

In addition to eliminating these special tax advantages, this bill is beneficial in that it will stop the drain on our investment which is artificially induced by the low tax rates it is possible to obtain through the use of tax haven subsidiaries. On the other hand, as I have already indicated, this bill does not interfere with sound business investments abroad which do not make use of tax haven subsidiaries.

In addition to clearing up the tax haven abuse, this bill also would clear up a multitude of other loopholes in the foreign area. Section 9 of the bill contains the so-called gross-up amendment. This correction in the method of taxing dividends received by American companies from their subsidiaries is long overdue. Existing law results in double counting and has the effect of reducing in an erratic manner the proper U.S. tax that should be imposed on dividends that are repatriated. The problem arises because a credit is allowed for most of the foreign income taxes paid on a given amount of income, yet these same foreign income taxes are not included in the dividend income subject to U.S. tax. Your committee has, however, retained present law with respect to dividends from operations in less developed countries. Because of our interest in encouraging investment in these areas—which is reflected in various sections of the bill, including section 12—we have not applied gross-up in these cases.

Closely related to "gross up" is section 15, which will provide that when stock in a foreign subsidiary is sold or exchanged ordinary income tax will be payable to the extent of the earnings and profits which have been until that point untaxed by the United States. The tax "gimmick" of using a foreign subsidiary to conduct business operations, paying no dividends, and then collapsing it so that all of the profits come home with only the payment of a capital gains tax must be corrected. However, your committee has modified this provision so that individuals will not be taxed on past accumulations or more heavily than if their stock were held by domestic corporations.

Section 5 of the bill insures that a full tax will be paid when distributions are made in kind by foreign subsidiaries.

American individuals living abroad have also been given unwarranted advantages under our existing tax laws. Publicity in this respect has been directed toward movie stars and other entertainers who in many cases have avoided the payment of any U.S. tax. They are not the only ones, however, who have taken advantage of the present provisions. The committee's bill corrects this situation by limiting the exclusion for income earned abroad by American residents of foreign countries to \$20,000 for the first 3 years of residence abroad and \$35,000 thereafter. No longer will people like movie stars who have benefited from being Americans be able to avoid paying their U.S. tax liabilities. Nevertheless, certain fringe benefits these persons have enjoyed will only gradually be included in their tax base over a 4-year period.

That is, under the pending bill on these fringe benefits we have sought to correct the situation that exists with respect to a tax loophole by phasing it out. Thus the employees of American business institutions and industry abroad, who may have been induced to go there by reason of the tax provisions of our country heretofore, will not feel immediately the full impact of the bill. This provision will go into effect over a 4-year period.

Also, section 18 requires that foreign real estate now be included in the gross estate of Americans. Tens of millions of dollars have been invested in real estate in places like Bermuda and the Bahamas because upon the owner's death this real property would not be included in the tax base upon which his inheritance tax is computed.

Other provisions will stop the artificial tax advantages now accruing to foreign investment companies—largely Canadian companies—owned by Americans, and foreign trusts set up by Americans to avoid U.S. tax.

Another provision will remove the artificial incentive provided by the foreign tax credit to transfer short-term funds abroad. Still another provision will require the payment of a full U.S. tax where patents are transferred abroad. Finally, we have strengthened the information provisions so we will be in a better position to be sure that all tax liabilities due are being paid with respect to foreign income.

DIVIDENDS AND INTEREST

One of the measures in the House bill designed to decrease tax evasion was a provision for withholding on dividends, interest, and patronage dividends.

The seriousness of this evasion is indicated by the fact that the Treasury Department estimates that somewhere between \$4 and \$5 billion of dividend and interest income currently is not reported on tax returns. As a result, the Treasury estimates that close to a billion dollars of revenue is lost each year.

The House bill would have met this problem by providing 20 percent withholding for most interest, dividend and patronage dividend payments.

Your committee has studied at length the system provided by the House bill for withholding, and also has considered numerous possible modifications of the House withholding provision. The committee was convinced from this study that the provision in the House bill, no matter how modified, was either too complicated or involved substantial hardship for significant groups of taxpayers or both.

That was the conclusion of a majority of the committee. It was not unanimous.

While recognizing the shortcomings of a withholding system, the Finance Committee strongly endorsed the principle that measures must be taken to insure that everyone pays the income taxes for which he is liable. It is recognized that the underreporting of dividends and interest is a serious problem and that a means of correction must be found. For this reason this bill provides an improved reporting system for interest, dividends, and patronage dividends.

This bill requires dividend, interest and patronage dividend payments of \$10 or more per person per year to be reported to the Internal Revenue Service on annual information returns. By regulation, reporting of amounts of over \$10 a year is already required in the case of dividend payments but generally the returns are made on a quarterly basis. Interest payments, however, are reported only where they amount to \$600 or more

per person. In addition to the reports to the Internal Revenue Service under the Byrd amendment the bill provides that dividend and interest payers must send an annual statement to the persons receiving these dividends and interest payments indicating the total amount of dividend or interest payments they paid such persons during the year. Failure to report these payments to the Government or to send the required statements to the taxpayer will involve a civil penalty of \$10 for each statement or return the payer fails to file but the maximum penalty per payer will be \$25,000.

That is, the payee will get an information return sent to him by the Internal Revenue Service, to remind him of the fact that the Internal Revenue Service now has specific information as to the amount of money the payee receives.

The committee believes that this expanded reporting system complements the legislation passed last year which requires each person to supply the dividend or interest payer with his social security or tax account number. The combination of these measures will enable the Internal Revenue Service through its planned expansion of automatic data processing ultimately to check all dividend and interest payments of more than \$10 per year per person. The reporting system, when the information returns are matched with tax returns, should also show any tax due above the first bracket, and in this respect, it will be more effective than a withholding system alone.

The Senator from Oklahoma will have a great deal of pleasure in listening, over the course of the next few years, to the complaints of those who objected to the withholding provision and were successful in substituting therefor the reporting amendment. Those who complained about the withholding amendment on the basis of what it would cost the payors may find that it will cost them more to do this reporting than it would have cost them to do the withholding.

However, such is the course of the history of legislation. I have seen other examples where men have been caught in the bear trap they fashioned for others. That will be the situation with respect to the payers who contributed to the defeat of the withholding provision in the bill.

The committee believes that because of the hardships and complications involved in a withholding system for dividends and interest, the expanded use of a reporting system should first be given a fair test. If after this reporting system has been given a fair trial, should an appreciable dividend and interest gap still remain, a withholding system at that time can be reconsidered by Congress.

IMPROVEMENTS IN TAX STRUCTURE

In addition to the investment credit, foreign income and dividends and interest reporting, your committee's bill also contains a series of provisions designed to close loopholes and improve the equity of our tax structure. Although

some of these provisions are relatively technical in nature, they are exceedingly important to an improved tax structure. Their enactment will accomplish a substantial improvement in our tax law. Most of these provisions are concerned with problems which have been plaguing us since 1950 and 1951. Some of them have been troubling us for even longer periods of time.

In large part these provisions concern the tax treatment of specialized types of institutions such as cooperatives, mutual savings banks, and savings and loan associations, and mutual fire and casualty insurance companies. For one reason or another these institutions have not in the past been carrying their fair share of the tax burden. This bill removes at least substantial portions of these inequalities.

In addition, your committee's bill deals with the abuse situations which have arisen in connection with entertainment expenditures and with the gain on the disposition of depreciable property. The bill also places expenditures for appearances with respect to legislation on an even footing with similar expenditures with respect to appearances before executive agencies or the courts.

COOPERATIVES

In 1951 Congress passed legislation which generally was thought to insure that earnings of cooperatives would be currently taxable either to the cooperative or to the patrons. However, the courts in the Long Poultry Farm and B. A. Carpenter cases have held that noncash allocations of patronage dividends generally are not currently taxable to the patron although they are currently deductible to the cooperative.

The bill carries out the intent of the 1951 legislation. The House bill, which your committee has modified only slightly, provides that cooperatives need not take into their income, patronage dividends paid in money or so-called qualified allocations. A deduction for non-qualified allocations is provided the cooperative when these allocations are redeemed in cash.

For the patron, the bill provides that patronage dividends paid in cash or qualified allocations are to be included in his income in the year the allocation is made. In the case of nonqualified allocations the inclusion in his income is to occur when the paper is redeemed. Of course, this is true only of amounts which arise from business activity. As under present law, amounts attributable to purchases of personal living expense items are treated as bargain purchases and are not taxable to the patron.

Qualified allocations are those patronage dividends paid in scrip, stock, or as allocations on the books of the cooperative where the patron had the opportunity to receive the amount in cash for a 90-day period or where he has given his consent to treating the allocation as an amount paid to him which he reinvested in the cooperative. Under the bill, consent may be given by the patron in writing or by being a member of a cooperative in which the bylaws require all members of the cooperative to take

the allocations into account. In addition, your committee has amended the House bill to provide that consent may be made by the cashing and endorsement of a patronage dividend check. In this case the cashing and endorsement of the check itself represents the consent on the part of the patron.

Since the House bill applied the provision on withholding to patronage dividends, as well as dividends and interest, the House bill in effect required that at least 20 percent of all patronage dividends be paid in what was the equivalent of cash. The patron could use this 20 percent directly, either by taking it as a credit against tax liability or by obtaining a refund from the Government. The committee bill contains no provision for withholding. However, it was thought desirable that the principle in the House bill be maintained, namely, that the cooperative pay out to the patron in cash at least enough to cover his tax liability on the patronage dividend at the 20 percent first bracket rate. For that reason the committee bill requires that at least 20 percent of all patronage dividends be paid to the patron in cash if the cooperative is to exclude any amount from its tax base for qualified allocations.

MUTUAL THRIFT INSTITUTIONS

In 1951 Congress also provided that mutual savings banks, savings and loan associations and similar organizations were to be subject to the regular corporate income tax but that these institutions were to be allowed a special deduction for additions to bad debt reserves. The 1951 legislation provided that these special deductions could equal the entire taxable income of the institution for the year, or equal an amount which would bring the institution's total reserves and surpluses up to 12 percent of its deposits. The effect of this legislation was that these organizations have paid almost no tax since 1951. During the entire decade 1952-62 all mutual savings banks and savings and loan associations paid total Federal income taxes of less than \$70 million, while retaining \$5½ billion in additions to reserves, surpluses, and undivided profits.

Mr. LAUSCHE. Mr. President, will the Senator yield?

Mr. KERR. I yield.

Mr. LAUSCHE. Would the Senator mind repeating those figures, stating the period covered, the amount of taxes paid, and the amount the institutions were allowed to retain?

Mr. KERR. During the entire decade 1952-62, all mutual savings banks and savings and loan associations paid total Federal income taxes of less than \$70 million, while retaining \$5½ billion in addition to reserves, surpluses, and undivided profits.

Mr. LAUSCHE. That would be about \$7 million a year paid by all mutual thrift institutions?

Mr. KERR. All savings banks and all savings and loan associations.

Mr. LAUSCHE. That is a very small amount, is it not?

Mr. KERR. Very small.

Mr. LAUSCHE. It is practically nothing.

Mr. KERR. Almost.

Mr. LAUSCHE. I thank the Senator from Oklahoma.

Mr. KERR. I appreciate the Senator's question.

The House bill amends the existing law applicable to these thrift institutions by providing that they may add to reserves for bad debt each year whichever of the following is the greatest:

First, 60 percent of taxable income for the year; second, an amount sufficient to bring the balance of their reserve for losses on qualifying real property loans to 3 percent of these loans plus a reasonable addition for reserves for losses on other loans; or third, any greater reserve that the institution can show is reasonable in view of its loss experience.

The committee has retained this basic provision but has placed additional restrictions on these reserve deductions. It is provided, for example, that even though the taxpayer uses the first alternative; namely, 60 percent of taxable income, in determining its deduction, nevertheless the reserve on qualified real property loans may not be built up to a level in excess of 6 percent of these loans. Also, it has added a proviso to make sure that no institution may obtain a greater deduction than under present law. In the case of stock savings and loan associations, your committee has also provided that the deduction is to be 50 percent instead of 60 percent of taxable income.

The committee bill also provides a new definition of domestic building and loan associations which in general provides that 63 percent of their assets must be invested in loans for one-to-four-family residential units, 72 percent must be in residential real property, and 90 percent must be in real property loans. Certain exceptions to these rules are provided for cash and Government obligations. Other restrictions also are provided.

CASUALTY INSURANCE COMPANIES

Stock fire and casualty insurance companies have long been taxed at ordinary corporate income tax rates on both investment income and underwriting income. Mutual fire and casualty insurance companies, on the other hand, have not been taxed on their underwriting income. The bill provides that these mutual insurance companies are to pay tax not only on investment income but on their underwriting income as well. However, recognizing that these companies have no paid-in capital as a cushion against losses, the bill permits mutual companies to build up a special tax-free reserve to be used to offset these losses. The amount which can be set aside in this manner generally is equal to 1 percent of their incurred losses, plus 25 percent of their underwriting gains. However, most of this is to be a reserve only for a limited period of time. Thus, all of the remaining additions to reserves for any year which were attributable to 1 percent of incurred losses and one-half of the portion attributable to 25 percent of underwriting income, after 5 years, if still remaining, will be withdrawn from the account and included in taxable income.

Basically your committee has accepted the House version of this provision. However, it has eliminated a discrimination against dividend-paying mutual insurance companies by providing that losses attributable to their dividends may be offset first against investment income, rather than being used to offset amounts in the special protection against loss account. This will accord them in substance the same treatment available under the House bill for a company which deviates from standard insurance rates rather than paying dividends to policyholders.

The committee has also eased the tax treatment for small insurance companies by raising the total exemption of existing law from \$75,000 to \$150,000 of total receipts. Also, it has raised from \$300,000 to \$600,000 of total receipts the level at which underwriting gain will initially become taxable. Other modifications are made for mutual insurance companies specializing in windstorm, hail, or flood insurance and for reciprocal underwriters and interinsurers.

SALES OF DEPRECIABLE PROPERTY

Under present law a taxpayer may write off the cost or other basis of depreciable property over the period of the useful life of the assets in his hands. These depreciation deductions are allowed as a deduction against ordinary income. If these depreciation deductions reduce the basis for the asset faster than the decline of its actual value, then there will be a gain on the asset if it is sold. Under present law this gain is taxed as capital gain, even though the depreciation deductions had reduced ordinary income. As a result, the taxpayer who has taken depreciation at a rate faster than the actual decline in value of the property has in reality converted ordinary income into capital gain.

H.R. 10650 meets this problem by treating as ordinary income any gain on the sale or other disposition of depreciable property, but only to the extent of the depreciation deductions taken since 1961. This ordinary income treatment applies to depreciable personal property and to certain other depreciable tangible property, but does not include buildings or structural components.

Your committee has made very little change in this provision. This provision is not only of importance as a means of plugging a serious loophole in present law, but also is of major significance in connection with the recent depreciation liberalization announced by the Treasury Department. Under the new guideline schedules, taxpayers generally will be permitted to depreciate assets faster than has previously been the case. As a result, additional ordinary income could be converted into a capital gain on the sale of these assets, if it were not for this provision.

ENTERTAINMENT EXPENSES

Among the more-publicized and troublesome problems with which this bill is concerned is that of the deduction for entertainment expenses. Your committee believes that its version of this provision provides a balanced approach which eliminates abuse situations, with-

out interfering with legitimate entertainment expense deductions. Your committee's bill provides that if entertainment expenses are to be deductible, they must be directly related to, or associated with, the active conduct of a trade or business. In the case of facilities such as yachts and hunting lodges and club dues, a further restriction provides, in effect, that the facilities must be used more than 50 percent for the furtherance of the taxpayer's trade or business. This provision, unlike the House bill, would permit the deduction of expenses to generate business good will where it is shown that these expenses are directly related or associated with a trade or business. The committee report gives an extensive listing of the types of expenses which your committee intends should not be deductible under this provision.

Your committee's amendments also restrict the deduction of travel expenses on combined business and vacation trips. If the travel is for a period longer than 1 week, or more than 25 percent of the total time away from home is spent for personal purposes, only the portion of the travel expenses allocable to the business will be deductible. Of course, in order for any portion of the travel expenses to be deductible in the first place, as under present law, the trip would have to be primarily for business purposes.

LEGISLATIVE APPEARANCES

Although not explicitly provided for in the statute, court decisions in the *Cammarano* and *Straus* cases have interpreted long-existing Treasury regulations as denying a deduction for expenses incurred in making appearances, submitting material, or communicating with respect to legislative matters.

The House version of the bill would modify these court interpretations of existing law, in order to permit deductions for expenses relating to appearance before, presentation of statements to, or communications sent to a legislative body, committee, or individual legislator at any level of government if the expenses are otherwise ordinary and necessary business expenses. In addition, a similar deduction is provided for the portion of dues paid to an organization which are used for similar legislative expenses, to the extent they are related to the businesses of the members. Your committee also has added an amendment providing that expenses of communicating information with respect to legislation between the taxpayer and its employees or stockholders also are to be deductible, where the matter is of direct business concern to the taxpayer. This provision does not permit the deduction of expenses incurred in attempts to influence the general public, or large groups of the public, through advertising or other campaigns, nor does it permit the deduction of expenses associated with political campaigns.

Your committee sees no reason why legitimate expenses incurred for appearances before legislative bodies or legislators should not be deductible while similar appearance before executive officials with respect to administrative matters, or before courts with respect to judicial

matters, are deductible. Your committee believes that the legislative branch of the Government in this respect should be placed on the same footing as the other two coordinate branches of Government.

It is also believed that it is desirable that taxpayers having information bearing on the impact of present or proposed legislation which affect their trades or businesses not be discouraged in making this information available to the responsible legislators. This information is essential to a proper evaluation on the part of the legislators of the impact on businesses of present or proposed legislation.

The deduction for legislative expenses is limited to cases in which expenses are related to the trade or business of the taxpayer, since only these expenses are pertinent to the determination of true taxable income of a business. In this respect, it might be noted that this is the same distinction presently made in the case of appearances before executive or judicial bodies.

Mr. LAUSCHE. Mr. President, will the Senator from Oklahoma yield for a question?

The PRESIDING OFFICER (Mr. Hickey in the chair). Does the Senator from Oklahoma yield to the Senator from Ohio?

Mr. KERR. I yield.

Mr. LAUSCHE. Has the committee dealt at all with the problem—which has been under discussion for several years—of allowing business enterprises to deduct, as business expenses, funds spent in payment of newspaper advertisements dealing with national issues and policies pending in the Congress? This is a deduction for which business enterprises have argued to a considerable extent.

Mr. KERR. The committee went into that question at length, and during extensive periods of time. I believe that every approach which could be devised by men of ingenuity and resourcefulness was made in presenting that matter to the committee. Each approach made was discussed at great length, and was turned down by the committee as regularly as it was offered.

Mr. LAUSCHE. What the Senator from Oklahoma has just now described is as far as the committee went in allowing such a deduction for funds spent in acquainting legislatures and their members with current political and economic problems.

Mr. KERR. And also by a taxpaying corporation in explaining those matters to its own stockholders and its own employees.

Mr. LAUSCHE. I thank the Senator from Oklahoma very much.

Mr. KERR. But the general run of expenditures to influence legislation by advertisements in news media or other means of communication was discussed at great length, and the committee decided that it could not justify the allowance of deductions for the cost of such expenditures.

Mr. PROXMIRE. Mr. President, will the Senator yield?

The PRESIDING OFFICER (Mr. BURDICK in the chair). Does the Senator

from Oklahoma yield to the Senator from Wisconsin?

Mr. KERR. I yield for a question.

Mr. PROXMIRE. Did I correctly understand the Senator to say that agriculture would benefit from the investment credit provisions of the bill to the same extent that industry would benefit, or to a greater extent?

Mr. KERR. That was the statement made by the Senator from Oklahoma.

Mr. PROXMIRE. Will the Senator from Oklahoma explain to the Senator from Wisconsin how agriculture could benefit very greatly, in view of the fact that 85 percent of the farmers of our country have a net income of less than \$3,000, and two-thirds have a net income of less than \$1,000, a year, and therefore the overwhelming number of them pay no Federal income tax?

Mr. KERR. The Senator is aware of the fact that the net income of our farmers from farm sources equaled \$12 billion in 1961 and although many of the farmers of Oklahoma do not make enough to be required to pay Federal income taxes, there are certain farmers in Oklahoma, who, like some farmers in the State of Wisconsin, are in the happy situation of making enough money to pay income taxes. Certainly, neither individuals nor businesses would benefit by a tax credit if they owed no tax, but this bill has in it a provision with reference to investment credit that a credit earned at any time after June 30, 1962, is subject to a 3-year carryback and a 5-year carry forward.

I know it is the hope of the Senator from Wisconsin and of the Senator from Oklahoma that the environment in which our farmers live, breathe, and have their being and their economic existence will be improved to the point where they will be making an income sufficient to be subject to Federal taxation; and when that happy environment materializes, as I fully believe it will, they will have the benefits of this bill to look forward to.

Mr. PROXMIRE. Is it not true that 85 percent of the farmers, who pay no income taxes, but pay heavy property taxes and other taxes, would receive no benefits under the bill unless at some time in the future their income should increase sufficiently to require them to pay an income tax?

Mr. KERR. The Senator from Oklahoma is not aware of the percentage of our farmers who do not pay income taxes; and in answering the Senator neither affirms nor denies the figure of 85 percent, but repeats the answer to the Senator from Wisconsin, that neither a corporation nor an individual would receive an immediate benefit from this bill unless he had a taxable income.

Mr. PROXMIRE. I refer the Senator to the U.S. Treasury Department, Internal Revenue Service statistics of income, which I hold in my hand. I ask the Senator from Oklahoma if the argument that we need the investment credit to put us on an even footing with foreign competition, and that there is evidence that the United States is not competing

abroad—

Mr. KERR. I did not say that. I said our producers are at a disadvantage tax-wise as compared with our foreign competitors.

Mr. PROXMIRE. Would the Senator from Oklahoma question the argument that the three countries that have investment credit, namely, the United Kingdom, Belgium, and the Netherlands, have demonstrated a record of slower industrial growth, and therefore the investment credit is not an effective device for promoting growth, in view of the fact that two of the three industrialized countries have had a poorer growth record than the United States, to wit, Belgium and the United Kingdom, and that the country which has the poorest of any except those and Sweden in Europe is the Netherlands?

Mr. KERR. The Senator from Wisconsin refers to the general situation and asks the Senator from Oklahoma whether or not a certain cause produced it. One thing that has resulted in the slowing down in growth of the United Kingdom—that is, Great Britain—and the Netherlands has been the loss of their colonies, and I believe that is true also of Belgium.

Many things could have produced the slowdown which the Senator has referred to, other than the corporate tax rate.

The Senator from Oklahoma has some association with and relation to and knowledge of American industry. The Senator from Oklahoma knows that any tax reduction would have an impact upon American taxpayers and American industry. The Senator from Oklahoma knows that as of today, a manufacturer in the United States has the least beneficial tax treatment by his Government of any manufacturer in any of the countries in the Common Market, or of Western Europe or Japan.

The Senator from Oklahoma is of the opinion that in our trade program, as provided for in the bill that will be before us—and I am sure that it will be passed in some form—if American industry is to compete both at home against imports from competitors with more advantageous tax treatment and more advantageous labor costs, and compete against those same competitors in the world market, the environment of American manufacturing and industrial entities must be improved. We are not going to reduce the wages of our workers. The wages of our workers are going to be increased. The only way we can hold our own in this new world that this Nation has helped to create, and in which this Nation is coming of age, is to arm American industry with the economic and industrial weapons comparable to those in the hands of our competitors in other industrial nations; and the investment credit provided in the bill is such a weapon.

It is not the complete answer. The increase in the depreciation formula is another. But each of these two weapons will be effective once in the hands of American industrial units, as they seek not only to exist in this new era of inter-

national competition—not only to survive, but to improve their relative and competitive positions.

Mr. AIKEN. Mr. President, will the Senator yield?

Mr. KERR. I yield to the Senator from Vermont.

Mr. AIKEN. I may add to what the Senator from Oklahoma has said that it is not tax incentives alone which make it difficult for us to compete with Western Europe, but tax incentives with the rapid writeoff granted by Common Market governments are an incentive for plants located there to have at all times up-to-date machinery, which enables them to produce at less cost. I believe one of the countries referred to permits the writeoff of new equipment in 3 years, and others do it in 5 years. One of the purposes of such a law is to enable the plants to have the most modern and up-to-date machinery.

If they have that, of course, they have an advantage in equipment alone over American industry.

Many of our own industries which have established plants in Western Europe have done so not merely because of a tax incentive. There is also a difference in labor cost, which I believe is something like one-third. There is also a difference in shipping costs to various markets of the world, which costs are only about half as much as the costs to ship from American ports.

There are many advantages which can be obtained in Western Europe that do not obtain here. The principal one, I think, is the fact that the plant always can have the most modern, up-to-date machinery.

Mr. KERR. The Senator from Vermont is so eminently correct that it is impossible for the Senator from Oklahoma to understand how any objective thinker could fail to recognize the validity and effectiveness of the statement and argument made by the Senator from Vermont.

One of the things which has been going on which adversely affects our economy is the export of dollars, of American capital, for the construction of productive facilities in countries of Western Europe—for the export, thereby, of jobs from American workshops to the countries of Western Europe; for the export of income generated, which would result not only in local jobs but also in local taxes in the industrial centers of our country.

I remind Senators—and especially the Senator from Wisconsin—not only has there been the migration of industry from certain parts of our country to other parts, in search of a more encouraging tax environment and of a more encouraging labor cost environment, but also that the greatest migration of industry has been from these shores to other countries in search of a more favorable economic environment, a more favorable tax environment, and a more favorable labor cost environment.

What is the result? Income which would otherwise be taxable in our States and by our Federal Government is taxable in foreign countries. Community

Mr. KERR. I did not say that.

building activities, which we need in our own States, go to foreign countries.

We need them in the State of Oklahoma, Mr. President, and in the State of Vermont. Perhaps the State of Wisconsin does not need any further industrialization. Perhaps the State of Wisconsin would prefer an environment which would continue to spur and to stimulate American industry to go to other shores for its expansion. But the Senator from Oklahoma wants to encourage the domestic environment, in the hope that Oklahoma may secure a child's part of that increase in industrial output.

I shall not be a party to a deliberate effort to further stimulate the migration of American industry to foreign countries to find an environment of favorable tax treatment and to find an environment of a continuing lower labor cost. It shall be my purpose to help any effort by anyone to bring about an environment whereby American industry will be encouraged and stimulated to grow and to expand on these shores, not only that we may compete more effectively in the domestic markets but also that we may be able more effectively to compete in the markets of the world.

Mr. PROXMIRE and Mr. CURTIS addressed the Chair.

Mr. KERR. Let me yield one more time to my great friend from Wisconsin, and then I will yield to the Senator from Nebraska.

Mr. PROXMIRE. If the Senator will yield, I have a series of questions I should like to ask. Of course, the Senator has the floor, and I shall take whatever time the Senator permits.

I should like to ask the Senator how he explains the fact that we do not have an unfavorable balance of trade but have a highly favorable balance of trade. The favorable balance of trade in the first half of 1962, seasonally adjusted to annual basis, is \$4.8 billion.

Even if we should leave out of consideration foreign aid and military spending, the commercial favorable balance of trade is \$2.2 billion, which means that other nations have an unfavorable balance of trade vis-a-vis us to that extent. In other words, we are winning. We are competing far more effectively abroad than other nations. The statistics prove it.

Mr. KERR. I say to the Senator from Wisconsin that his figures are erroneous and his conclusions inaccurate.

Mr. PROXMIRE. I call the Senator's attention to the statistics from the Department of Commerce.

Mr. KERR. Let me answer the Senator's question.

Mr. PROXMIRE. The Senator challenged my figures. I am giving the source. Does the Senator want the facts, or not?

Mr. KERR. If I did I would not go to the Senator from Wisconsin for them.

Mr. PROXMIRE. I ask the Senator to go to the U.S. Department of Commerce for them. That is my source.

Mr. KERR. The Senator from Oklahoma will take his pitcher to whatever well he chooses.

Mr. PROXMIRE. I am sure he will. Mr. KERR. Yes.

The balance of trade, overall, that is when one gives effect to items such as foreign aid, military expenditures, and investments of American financial institutions abroad is a deficit.

Mr. PROXMIRE. The Senator is completely wrong.

Mr. KERR. Not a credit position.

Mr. PROXMIRE. The facts contradict the Senator completely.

Mr. KERR. I say to the Senator, "I will finish my speech, and then you finish yours."

We know that we have been losing gold at the rate of up to \$3½ billion a year. The only reason for that is that there have been more dollars going out than have been coming back in. So the net position has been a deficit.

In 1960 I believe the deficit was \$3.3 billion. In 1961, it was \$1.8 billion plus some million. It is hoped that this year it will not exceed \$1.5 billion.

It is true, Mr. President, that, on the strict limitation of commercial exports versus commercial imports, we have seen a favorable balance, but not enough of one to overcome the overall deficit.

The Senator from Oklahoma would like to see an environment which would enable us to achieve an overall favorable position. The adverse or contrary could be fatal.

Since 1952 our gold reserves have been reduced from \$23½ billion to a little above \$16 billion. In 1952 the total foreign claims which could be validated against the \$23½ billion gold reserves were less than \$7 billion. Today, with reference to the little more than \$16 billion, there are in excess of \$19 billion of valid foreign claims, which could be implemented against our gold reserves.

That is in spite of the fact that our law requires a 25-percent gold reserve against our currency outstanding and our Federal Reserve deposits, which requires some \$12 billion gold reserves. So above our requirements under our law, for gold backing of our own currency and our own Federal Reserve deposits, there is a net residue or surplus of some \$4 billion, against which there are more than \$19 billion of foreign claims which could be validly exercised.

In 1952 we had in excess of \$16 billion over and above the foreign claims, which left us enough for our requirements back of our currency, our Federal Reserve deposit, and a very substantial additional amount. So how can men say that our position with reference to our balance of payments has resulted in a surplus or now results in a surplus? Heaven knows that if it is possible for us to improve our export position with reference to our import position, it is incumbent upon us and highly necessary that we do so. Who can take comfort from the knowledge that there may be a \$1½ billion or a \$2 billion or a \$2½ billion favorable balance in one of the items that make up the difference between the dollars that we export and the dollars that we import, when there are 2, 3, 4, or 5 other avenues of export against our dollars with reference to which there is no counterbalance and no countercredit?

It is a situation of opening one eye just a little and looking out to a small fragment of the panorama of the economic facts of life which this Nation, as the leader of the free world, must look at in its entirety and must approach from a comprehensive point of view, taking into account all the features that go to make up the net position of our country from the standpoint of the import and export of dollars, and the resulting effect upon our balance of payments.

Mr. CURTIS. Mr. President, will the Senator yield?

Mr. KERR. I yield.

Mr. CURTIS. I thank the distinguished Senator. The distinguished Senator has referred to the establishment by American companies of factories, sales companies, and other operating companies abroad. I believe that a careful perusal of the voluminous testimony before the committee will show that it was the contention of all witnesses from industry that the establishment of plants abroad increased exports from the United States to the foreign countries. As a general rule, those plants were established to reach a market in a foreign country that we could not reach here. Sometimes a trade barrier would make it necessary for a plant to be overseas. Sometimes the local country would insist that the subsidiary be domiciled there, and that certain local citizens have a part in it. But as a result of the establishment of foreign subsidiaries, there flow from our country machines, repairs, replacements, raw materials, designs, patents, and other items that contribute to the export of goods from the United States abroad. That operation improves our dollar balance and our gold balance.

There is another section in the bill to which the distinguished Senator from Oklahoma has not yet addressed himself, which would result in placing an American foreign subsidiary operating in a foreign country on a different tax basis than the companies of other foreign countries having subsidiaries there. The overall effect of the bill would be not to enhance our trade and improve our dollar and gold balance, but the result would be the contrary.

I hope that before the bill goes to conference section 12 thereof will be stricken, notwithstanding the fact that the section was improved by the amendments of the Senator from Oklahoma.

Mr. KERR. Mr. President, I appreciate the remarks of the Senator from Nebraska. I agree in part. I disagree with him in part, I disagree with his conclusion. I cannot agree that the effort of the Congress should be to step up the export of American industrial capacity and American jobs. I agree that much of it has been going on. There has been an irresistible magnet in many of the countries of Western Europe that has drawn our investment dollar to the extent of more than \$2.5 billion a year in the building of productive facilities in Western Europe. A certain part of it will continue no matter how much we improve the environment of industry at home. But that fact should not discourage men from improving the environment here as much as possible.

Mr. CURTIS. With that I agree.

Mr. KERR. That fact should not prevent us from taking any appropriate measure that we can which would slow down the migration either of investment dollars in industry, in jobs, or in American industries, and step up production at home. The situation that the Senator has described, rather than being an argument against the proposed investment credit, is the basis of the argument of the Senator from Oklahoma for the investment credit.

Mr. AIKEN. Mr. President, will the Senator yield?

Mr. KERR. I yield.

Mr. AIKEN. I should like to point out another method which the United States has used to persuade industries to leave our country and locate in other parts of the world. That is through the system of insuring such industries against loss due to expropriation, or the inconvertibility of currency. We started that program with a \$500 million authorization. Two years ago we discovered that 80 percent of that \$500 million of insurance had been taken out by firms establishing plants or branches in Western Europe, and only 20 percent of it in the rest of the world. Congress amended the law to stop encouraging businesses to leave the United States and go to Western Europe. But the fact remains that we have continued to increase the authorization for insurance until I believe it is now \$1½ billion. In other words, we have not only failed to give incentives for industries to remain in our country, but also we have actually paid them to move out by giving them advantages which they could not secure in the United States.

Mr. KERR. The Senator is correct.

Mr. President, I remind Senators that a number of years ago there was a so-called dollar gap. Exports from our country were so much greater than the imports into our country that we accumulated a very high percentage of the total amount of gold in the free world. Our Government started deliberately to do certain things. First, it began to try to close the so-called dollar gap.

Second, to promote industrial developments in Western Europe, to help it lift itself from the position to which it had been thrust by the war. That effort was successful. However, we continue to apply the cure long after the patient has completely recovered and is even stronger and more vigorous than the doctor.

There are those now who, it seems, want us to continue to administer the cure although the patient no longer needs it, although the incentive that we have provided for the expansion of foreign industry should be provided for greater expansion at home, although the dollar gap long since has been closed; and instead of foreign countries having a dollar deficit, we have had a dollar deficit, a dollar deficit that runs into tens of billions of dollars, which has resulted in the exhaustion of our free gold reserves uncommitted and unaffected by foreign claims. The time has long since been here when our efforts should be to provide a greater stimulant for more

efficient productive capacities in our own industrial workshop, in order that we might close the opposite situation and what existed when we had a dollar gap, and which is now upon us in the form of a dollar deficit.

I congratulate the President of the United States upon the vigorous measures he has inaugurated to close this gap. I congratulate former President Eisenhower and his Secretary of the Treasury, Bob Anderson, in the efforts they made—I thought, too late, and all admit now it was too late—in the last 15 months of the Eisenhower administration, to move in an effort to close the deficit that had been created as a result of the impetus of our efforts that had been made to close the dollar gap.

When President Kennedy came into office the situation was so serious that more vigorous efforts were required. Be it said to his credit that he has inaugurated vast efforts. He inaugurated them in the manner of expenditures of our armed services abroad, and has inaugurated them in the matter of moving much farther than the previous administration had in requiring that loans made by our banking institutions to American business for investment in foreign countries be spent to a large degree in this country.

He did it by moving more vigorously in the direction of using our dollar economic aid in a manner that resulted in a higher and higher percentage of it being spent in the United States.

However, with all of these measures and others, even in 1962 we will have a deficit in our balance of payments of in excess of a billion dollars. I believe that at the year's end a balance may well be achieved. But the mere achieving of a balance, when the situation is one of such a serious lack of the adequacy of gold reserves to meet our requirements with reference to our currency and our Federal Reserve deposits to meet the legitimate demands of foreign central banks who have dollar claims against us, is not enough. We must move more vigorously. The ways our administration has devised to do that, in addition to the measures to bring about a balance, is the improvement of the efficiency and productivity of our industrial workshop.

They have done it through the revision and more favorable provisions of the depreciation formula applicable. They are seeking to do it by encouraging and obtaining enactment of the pending legislation which will give greater incentive for industry to expand on these shores—in Ohio, Florida, Illinois, Tennessee, Wisconsin, Oklahoma, Nebraska, Oregon, and North Dakota, and every other State of the Union—rather than having a situation continue in which every element of the environment is such as to be a magnet drawing more and more industrial expansion of American industry with American dollars into the more favorable environment of countries of Western Europe and other industrial workshops around the world.

Mr. LAUSCHE. Mr. President, will the Senator yield?

Mr. KERR. I yield.

Mr. LAUSCHE. My question goes to another subject. It deals with section 18, the inclusion of foreign real property in the base for real estate tax purposes. The Senator from Oklahoma has been on his feet for some time. In order to give him a little rest, I will read from a letter which has been written by an Ohio citizen to the Secretary of the Treasury, dealing with this subject.

Mr. KERR. Not real estate taxes; it is the estate taxes.

Mr. LAUSCHE. That is correct, yes. This Ohio citizen suggests a correction. He contends that the correction which he suggests is completely consistent with the philosophy of the provisions of section 12 of the Senate bill, which exempts income invested in less developed countries until a profit is returned to the United States. He further contends that his suggestion is supported by section 15 of the Senate bill, which retains capital gains treatment on the sale of stock of parent corporations operating in less developed countries. Then he goes on to say that with his holdings in the Virgin Islands, the treatment is different. He says:

All profits from Virgin Islands real estate sold by U.S. citizens already is fully subject to immediate U.S. taxes. Capital, however, which has been coaxed slowly from U.S. citizens into Virgin Islands real estate, in reliance on the integrity of the organic act, based on the 44-year-old Danish treaty, cannot be liquidated rapidly to provide funds for estate taxes. The market is small. Such real estate investment effectively is frozen over a period of years. To abruptly subject this frozen real estate investment to the excess Federal or estate taxes would impose the highest estate tax rate, and this would be payable out of the residual liquid portion of the estate.

I merely put the question for the purpose of information. The House has made the effective date of this provision later than the date the Senate bill sets.

Mr. KERR. I recall that the effective date in the House bill was July 1, 1964, and that the effective date in the Senate bill is January 1, 1963.

Mr. LAUSCHE. That is correct. May I ask what the answer is to this constituent's argument, who says he invested his money in Virgin Islands real estate under the assumption that the treaty between Denmark and the United States with respect to the Virgin Islands protected him against the sudden requirement to pay an estate tax, instead of waiting to sell the property at a time when it could be sold at what would reflect its true value?

Mr. KERR. I know of no treaty obligation between the United States Government and Denmark on this matter. In the opinion of the Senator from Oklahoma, if there is an area in which an investment in real estate, which real estate is not now subject to estate taxes under our law in the case of the death of the owner, should be made subject to it, it is investments in the Virgin Islands. The Virgin Islands belong to the United States. I can see no more justification for a citizen from Oklahoma being permitted to invest \$1 million or \$2 million in the Virgin Islands, which is

a possession of the United States and a part of the United States, and having that investment not subject to an estate tax upon his death, than there is to permit him to invest his money in real estate in any other of the 49 States, and upon his death the real estate not be subject to estate taxes.

Mr. LAUSCHE. I agree to that proposition.

Mr. KERR. If the Senator from Ohio were to visit the Virgin Islands, he would find that real estate is very expensive there; that the value of rental business property along the main street of the capital of the Virgin Islands is higher than it is on Fifth Avenue in New York. One reason is that the Virgin Islands have been a tax haven.

Another reason has been that Americans have gone there—and have been induced to go there—to bid up the values of the real property, because when they do, and when they die, the property, although owned by American citizens in an area under the American flag, is not subject to estate taxes.

There might be a basis for arguing that January 1, 1963, is a date so soon, in view of the delay with reference to the bill, that it should be moved forward. I can well recognize the validity of an argument by an American landowner, although a tax will not be imposed until he dies, life being so uncertain for any of us, that the effective date, in view of the delay in the consideration of the bill, might be moved forward.

Mr. LAUSCHE. That is, moved—

Mr. KERR. Moved beyond January 1, 1963, the date provided in the House bill. I could well understand such a person's position if that were his argument. But I cannot understand why the ownership of land in the Virgin Islands should put an American citizen in a more favorable position with respect to the inheritance tax upon his death than he would be in if he had invested the same amount of money in real estate in the Bahamas or in Panama.

Mr. LAUSCHE. I agree, except that it is argued that the treaty which the Virgin Islands had with Denmark has some impact.

If the Senator knows, was there any discussion, recorded in the transcript of hearings, relating to the Danish treaty?

Mr. KERR. The last language in the bill—the very last sentence in the bill, on page 392—as it passed the House and was reported by the Committee on Finance, provides:

No provision of this Act shall apply in any case where its application would be contrary to any treaty obligation of the United States.

Mr. LAUSCHE. As I understand from a statement by the committee staff representative, the transcript of the hearings discloses no discussion of a treaty allegedly guaranteeing certain rights to American investors in the Virgin Islands.

Mr. KERR. The treaty between the Virgin Islands and Denmark before the United States obtained the Virgin Islands?

Mr. LAUSCHE. Yes.

Mr. KERR. So far as I know, there was none affecting this provision. How-

ever, the committee specifically honored any treaty obligation of the U.S. Government.

Mr. LAUSCHE. By the last section?

Mr. KERR. By the last language in the bill.

Mr. LAUSCHE. Near the middle of page 117 of the report, it is stated:

The President in his tax program recommended that this exemption be eliminated on the grounds that in recent years this has been a subject of abuse.

I assume that that is what the Senator has in mind concerning the abuses perpetrated in owning real estate in foreign countries for the purpose of escaping the payment of taxes.

Mr. KERR. For the purpose of escaping the estate tax.

Mr. LAUSCHE. Yes.

Mr. KERR. The Senator is correct.

Mr. President, I have explained briefly the more significant provisions of the bill. A full explanation of the other provisions in this bill appears to me to be unnecessary at this time. In addition, the committee report before the Senate contains an explanation of each of the provisions in the bill. I am sure that as the debate progresses I will want to delve more deeply into various provisions and I, of course, will be glad to answer any questions to the extent of my information and my physical endurance. I am also attaching to my statement a summary of the bill as amended by the committee which, Mr. President, I ask to have made a part of the RECORD at the end of my remarks.

The PRESIDING OFFICER. Without objection, it is so ordered.

(See exhibit 1.)

Mr. KERR. Mr. President, in conclusion, let me say, Mr. President, that this legislation represents a major step in the revision of our tax structure. It provides a significant stimulus for investments in order to achieve needed economic growth and to help our balance of payments. It wipes out tax haven and other abuse situations in the foreign area and removes serious inequities and loopholes in our domestic tax structure. This tax measure is a necessary initial step in any revision of our tax structure, and I urge all Senators to support its passage.

EXHIBIT 1

SUMMARY OF BILL AS ORDERED REPORTED BY THE SENATE COMMITTEE ON FINANCE

SECTION 1. SHORT TITLE, ETC.

The act is to be cited as the "Revenue Act of 1962."

SECTION 2. INVESTMENT CREDIT

The bill provides a credit against tax liability with respect to investments in certain types of property. It generally is 7 percent (3 percent in the case of certain public utilities) of investments in new tangible personal property (except livestock) and depreciable real property, except buildings and structural components of buildings, used in manufacturing, production, extraction, transportation, communications, and certain other services. No credit is allowed for property with a useful life of less than 4 years, nor generally for replacements (to the extent of insurance proceeds) of property destroyed by fire or other casualty or stolen. For property with a life of 4 to 6 years, one-third of the investment is taken into account; for property of 6 to 8 years, two-

thirds is taken into account; and for property with longer lives, the full amount of the investment is taken into account. Purchases of used property, up to \$50,000 worth, also are eligible for the credit. The credit may offset tax liability in full up to \$25,000, but above that point the credit may not reduce tax liability by more than 25 percent. Any unused credit may be carried back for 3 years (not before June 30, 1962) or forward for 5 years and used in those years to the extent there is sufficient tax liability under the applicable limitation.

The basis of the property (for depreciation or gain or loss on sale) is reduced by the amount of the investment credit, whether or not it can be immediately used to reduce taxes, with appropriate later adjustments if all the credit is not ultimately used. A "recapture rule" is also provided to recover the tax reduction previously allowed as a credit, to the extent property is disposed of in less than its estimated useful life.

This provision is effective for taxable years ending after June 30, 1962, but only with respect to property acquired or to the extent constructed, reconstructed, or erected after that date.

SECTION 3. APPEARANCE WITH RESPECT TO LEGISLATION

A deduction is provided for costs relating to appearances before, presentation of statements to, or communications sent to a legislative body, a legislative committee, or individual legislator (Federal, State, or local), if the expenses are otherwise ordinary and necessary business expenses. A deduction also is allowed for the portion of dues paid to an organization which are used for similar legislative expenses to the extent they are related to the businesses of its members. In addition, the expense of communication of information with respect to legislation between the taxpayer and the organization of which he is a member, and between a taxpayer and its employees and stockholders, is deductible if the matter is of direct interest to the members or taxpayers. This provision does not permit the deduction of expenses incurred for attempts to influence the general public, or segments of the public (by advertising or otherwise), or for expenses concerned with political campaigns. This provision applies to taxable years beginning after December 31, 1962.

SECTION 4. ENTERTAINMENT AND TRAVEL EXPENSES

Deductible expenses for entertainment, amusement, or recreation generally are limited to those directly related to the active conduct of a trade or business, or to those associated with the active conduct of a trade or business. In the case of facilities, a further restriction is imposed to the effect that the facility must be used more than 50 percent for the furtherance of the taxpayer's trade or business (if any depreciation, rent, maintenance, etc., is to be deductible). Club dues are treated the same as facilities. This bill (unlike the House bill) will permit expenses to generate business goodwill to be deductible where a clear business purpose for the expense is established.

A second feature of the provision limits the deduction for business gifts to \$25 per year per individual recipient. In applying the \$25 limitation, however, advertising gifts costing less than \$4 bearing the taxpayer's name are not to be taken into account and signs, display racks, or other promotional material used on the business premises of the recipient also are not to be taken into account. Another exception to the \$25 limitation involves items of tangible personal property which cost not more than \$100 awarded to an employee by reason of length of service or for safety achievement.

A third feature requires an allocation of travel expenses in certain cases where the travel involves both business and personal

purposes. If the travel is for a period longer than 1 week, allocation must be made in all cases where the portion of the time away from home which is for personal purposes exceeds 25 percent of the total time away from home and only the amount allocated to business will be deductible.

In a fourth feature of the provision, rules are set forth providing that the deduction of entertainment or travel expenses will be denied unless they are substantiated (by adequate records) as to the amount, time and place, and the business relationship to the taxpayer of the persons involved.

A fifth feature provides that in the case of traveling expenses, deduction will be allowed for amounts expended for meals and lodging other than amounts which are lavish or extravagant under the circumstances.

This provision applies to taxable years ending after December 31, 1962, for periods after that date.

SECTION 5. DISTRIBUTIONS IN KIND BY A FOREIGN CORPORATION

Distributions in kind from foreign corporations to domestic corporations are treated as having a value equal to the fair market value of the property distributed (and not the adjusted basis of this property in the hands of the distributing corporation where this is lower). The foreign tax credit applicable with respect to such distributions is to be computed by reference to the fair market value of the property. This applies to distributions made after December 31, 1962.

SECTION 6. MUTUAL SAVINGS BANKS, ETC.

Mutual savings banks, domestic building and loan associations, and cooperative banks are allowed under present law to add all of their income to bad debt reserves until reserves (including surplus reserves) reach 12 percent of deposits. In lieu of this, under the bill, these institutions (other than domestic building and loan associations having capital stock outstanding) are to be permitted deductions for additions to bad debt reserves generally of up to 60 percent of their taxable income (before this deduction) or, if larger, an amount bringing their reserves up to 3 percent of improved real property loans, plus a reasonable addition for other loans. (Existing reserves in excess of this amount generally are disregarded.) The bill also provides that the reserves may be accumulated in excess of 3 percent of these loans if the taxpayer's experience shows this is required. In the case of domestic building and loan associations with capital stock outstanding the 60-percent rule described above is not to apply; instead such associations are to be permitted to deduct up to 50 percent of such taxable income. Small new domestic building and loan associations are provided a special additional deduction which is to apply only in their first 10 years of operation. These companies are to be permitted to set aside up to 5 percent of their improved real property loans (which do not total more than \$4 million) rather than 3 percent. Limitations are provided on the overall amounts which may be accumulated in bad debt reserves. The first limitation provides that under the 60-percent alternative (or the 50-percent alternative in the case of stock associations) amounts may not be accumulated after the reserve reaches 6 percent of improved real property loans. The second limitation provides that no deductible additions may be made to bad debt reserves if the total amount accumulated in all reserves equals 12 percent of deposits.

Under the bill, in the case of stock savings and loan associations, distributions to shareholders will be considered as paid first out of already tax-paid funds and, only when these are exhausted, out of reserve funds on which a tax has to be paid by the association at the time of distribution. Also, under the bill, a domestic building and loan association is defined as one which is insured under the

National Housing Act or subject to State or Federal supervision, but only if substantially all of its business consists of accepting savings and investing the proceeds as follows: At least 90 percent of the assets must consist of cash, Government obligations, loans secured by an interest in real property, and loans for the improvement of real property, or share account loans; at least 80 percent of the 90 percent must consist of cash, Government obligations, and loans secured by an interest in real property which is or will become residential real property; and at least 70 percent of the 90 percent must consist of cash, Government obligations, and loans secured by an interest in real property which is or will become residential real property containing one- to four-family units. No part of its investments may be in private corporate stock. In addition, the exemption of Federal savings and loan associations from certain excise taxes is repealed.

Generally, these provisions are effective for taxable years ending after December 31, 1962. The excise tax changes are effective as of December 31, 1962.

SECTION 7. DISTRIBUTIONS BY FOREIGN TRUSTS

Distributions by foreign trusts which are attributable to contributions made by U.S. grantors (or added by U.S. transferors) are to be taxed to any U.S. beneficiaries in substantially the same manner as if the beneficiaries had received this income directly in the year earned rather than later when the distribution is made. However, the additional tax is payable at the time of the actual distribution. For those preferring not to make the calculations required under this "exact method" of taxation, an averaging device is provided. This applies to distributions (accumulated after the effective date of the 1954 Code) made after the date of enactment of the bill.

SECTION 8. MUTUAL FIRE AND CASUALTY INSURANCE COMPANIES

Mutual fire and casualty insurance companies are to be taxed on their "total" income less a deduction for additions to a reserve for protection against losses equal to one-fourth of their underwriting gains plus 1 percent of their insurance claims. After a 5-year interval, the 1 percent set-aside with respect to insurance claims and one-half of the amount attributable to underwriting gains is brought back into the taxable income to the extent not already offset by losses. The remainder, to the extent not offset by losses, will remain in the loss reserve but no amount may be added to this reserve which would build it up to a level of more than 10 percent of the current year's premiums. The bill provides uniform treatment for losses of mutual companies regardless of whether they operate on a deviated-premium basis or on a dividend-paying basis. Concentrated risk companies (those having 40 percent or more of their premium income from windstorm, hail, flood, and so forth, risks, arising in one State or within 200 miles of any point selected by the taxpayer) may set aside an additional amount of underwriting income in the protection-against-loss account, and with respect to this additional amount the 10-percent limitation will not apply but the 5-year limitation will apply.

Companies whose total receipts do not exceed \$150,000 are to be exempt from tax, and companies with total receipts of between \$150,000 and \$600,000 are to be taxed only on their investment income. For those with gross receipts above \$600,000, a special deduction of \$6,000 is provided which decreases as gross receipts rise and disappears at a level of gross receipts of \$1,200,000.

Factory mutual companies are to be taxed like stock companies without the special protection against loss reserve referred to above. However, in computing their underwriting profits they will be permitted to determine their premium income on the basis

of "absorbed" premium deposits (i.e., in general, excluding the portion of the deposit returnable to the person insured). The amount so determined is then increased by 2 percent. Mutual flood insurance companies are to be taxed in the same manner as factory mutual insurance companies. Under a special transitional loss rule, mutual companies which incurred underwriting losses in 5 out of the 6 years preceding 1963 are permitted to carry such losses over and deduct them over a 5-year period. Reciprocal underwriters and interinsurers are in effect permitted to combine the underwriting income of their corporate attorney in fact with their own for most purposes.

These provisions apply to taxable years beginning after December 31, 1962.

SECTION 9. DOMESTIC CORPORATIONS RECEIVING DIVIDENDS FROM FOREIGN CORPORATIONS

Under present law when the income of a foreign subsidiary is distributed to a domestic parent corporation only the income of the subsidiary remaining after tax is treated as a dividend and a foreign tax credit is allowed the parent corporation for that part of the foreign taxes paid by the subsidiary attributable to this income. Under the bill, except in the case of dividends received directly or indirectly from less developed country corporations, the amount included in the tax base of the domestic corporation, if it elects the foreign tax credit, is to be not only the dividend itself but also the tax paid by the foreign corporation as well.

A less developed country corporation generally is a corporation, engaging in a trade or business, which derives 80 percent or more of its gross income from such a country; and has 80 percent or more of its assets (in general) located in such a country. It also includes companies holding 10 percent or more of the stock of the less developed country corporations described, if 80 percent of their income is derived from less developed countries and 80 percent of their assets are either located in less developed countries or are stock or securities of less developed country corporations. It further includes shipping and air transport companies deriving 80 percent of their gross income from ships or aircraft registered under (but not necessarily incorporated under) the laws of a less developed country and having 80 percent or more of their assets in such a business. Where there are two levels of foreign corporations the status of the top-level corporation determines whether or not the gross-up applies.

Also, where a foreign corporation is eligible for the 85-percent intercorporate-dividends-received deduction with respect to income earned in the United States, the 15 percent of this income for which no deduction is allowed is not to be treated as foreign source income for purposes of the foreign tax credit. The subsection of present law making the foreign tax credit available for royalty income received from wholly owned subsidiaries in certain cases is repealed.

These amendments become fully effective for distributions received by domestic corporations after December 31, 1964. In the case of distributions received by domestic corporations before 1965 but in taxable years after December 31, 1962, the new rules are to apply in the case of distributions made out of profits of a foreign corporation accumulated in taxable years beginning after December 31, 1962.

SECTION 10. SEPARATE LIMITATION ON FOREIGN TAX CREDIT FOR CERTAIN INTEREST INCOME

Your committee's amendments provide that the limitation on the foreign tax credit is to be computed separately with respect to certain types of interest income. Also, the "per country" limitation must be used for this special interest income, whether the "per country" or "overall" limitation is used

for other income. The separate computation is required for interest income other than interest derived: (1) From the active conduct of a trade or business, (2) from the conduct of a banking, financing, or similar business, or (3) from a corporation in which the taxpayer has at least a 10-percent stock interest. This is intended to prevent a domestic corporation receiving income from operations abroad which are taxed at a level above the U.S. level of taxation from offsetting these "excess" foreign taxes against interest income, also earned abroad, which is taxed at less than the U.S. level of taxation.

SECTION 11. EARNED INCOME FROM SOURCES OUTSIDE THE UNITED STATES

Under existing law, individuals who are present in a foreign country or countries for 17 out of 18 months may exclude from their U.S. tax base up to \$20,000 per year of income earned abroad. If they are bona fide residents of a foreign country there is no ceiling on this exclusion. In the case of these bona fide foreign residents, a ceiling is to be provided of \$20,000 for the first 3 years they are abroad and \$35,000 thereafter. If an individual makes a statement to a foreign country that he is not a resident and the foreign country grants him tax exemption, the statement is to be conclusive evidence that he is not a bona fide resident of that country for purposes of the U.S. exclusion. Under the provision, contributions made by employers for employee benefits under qualified pension plans with respect to future employment are to be taxable to the employee when he receives these amounts after retirement. Generally these provisions are effective with respect to taxable years ending after December 31, 1962. However, noncash fringe benefits received in 1963 are not to be taken into account in applying the limitation to bona fide residents. In 1964 one-third of the value of such benefits is to be taken into account, in 1965 two-thirds of the value of such benefits is to be taken into account, and thereafter the full value of such benefits is to be taken into account.

SECTION 12. CONTROLLED FOREIGN CORPORATIONS

In the case of controlled foreign corporations, where more than 50 percent of the stock is owned by U.S. shareholders who own 10 percent or more of the stock in these corporations, such shareholders are to report for tax purposes the undistributed earnings of these corporations to the extent they represent (a) income from insuring or reinsuring U.S. risks; (b) increases in earnings invested in U.S. property (generally not related to foreign business); (c) passive types of income; (d) income from purchases from or sales to related "persons" where the goods are produced or grown and the property is sold for use outside of the country of incorporation of the foreign corporation involved; (e) income from services performed for related persons outside of the country of incorporation of the foreign corporation. The last three of these categories comprise what is known as foreign base company income. In these latter three cases, the combination of the three types of income must equal 30 percent of total income before it is taken into account. Where this combined income equals more than 70 percent of the total, then all income is attributed to the shareholders. However, reductions in the income taxed to shareholders are allowed in the case of dividends, interest and gains from sales if these are received from less developed country corporations, to the extent that these earnings are reinvested in less developed country corporations. Exclusions from categories (c), (d), and (e) above are also provided for shipping income and for income from corporations which (as established to the satisfaction of the Treasury) are not availed of to reduce taxes. Undistributed earnings which are taxed to the U.S.

shareholders under any of the above provisions may subsequently be actually distributed to U.S. shareholders without further payment of tax.

The bill also provides a series of relief measures from the above provisions. First, individual shareholders may elect to have the undistributed income which is to be taxed to them treated as if they, the recipients, were domestic corporations (subject to a maximum tax rate of 52 percent and eligible for the foreign tax credit).

Second, if certain minimum amounts of income are distributed (which vary in accordance with foreign effective tax rates) the section on controlled foreign corporations is not to apply. The distributions are as follows:

Effective foreign tax rate:	Minimum distribution (percent)
Under 10 percent.....	90
10 percent up to 20 percent.....	80
20 percent up to 30 percent.....	70
30 percent up to 40 percent.....	60
40 percent up to 42 percent.....	50
42 percent up to 44 percent.....	38
44 percent up to 46 percent.....	26
46 percent up to 47 percent.....	14
Over 47 percent.....	0

For the purpose of computing the above distribution schedule each controlled foreign corporation can be treated separately, each chain of controlled foreign corporations may be treated as a unit, all controlled foreign corporations may be treated as a unit, or all controlled foreign corporations other than less developed country corporations may be treated as a unit. Foreign branches of U.S. corporations also may be taken into account if the third category above is used.

Third, certain export trade income of "Export Trade Corporations" will not be taxable to U.S. shareholders in the case of foreign base company income, i.e., the last three of the five categories of income listed above. An export trade corporation is a controlled foreign corporation deriving 90 percent of its income from sources outside the United States and 75 percent of its income from "export trade income." Export trade income is the income derived from the sale to an unrelated person for use outside the United States of property produced, grown, or extracted in the United States, as well as certain other income related to such sales. The bill provides that the income of a controlled foreign corporation which is taxable to U.S. stockholders (except insofar as it relates to insurance of U.S. risks) is not to include the export trade income of one of these corporations to the extent this export trade income does not exceed 1½ times the export promotion expenses or 10 percent of gross receipts, whichever is lesser. However, for this treatment to apply, the earnings involved must be invested in the export trade business.

SECTION 13. ORDINARY INCOME ON CERTAIN GAINS FROM DEPRECIABLE PROPERTY

In the case of tangible personal property (other than livestock) and depreciable real property, other than buildings and structural components, used in manufacturing, production, extraction, transportation, communications, and certain other services, when such property is sold or exchanged at a gain during a taxable year beginning after December 31, 1962, this gain, to the extent of depreciation attributable to periods after December 31, 1961, is to be treated as ordinary income for tax purposes (instead of capital gain). In the case of dispositions of property during a taxable year beginning after December 31, 1962, other than by sale or exchange, this same treatment is to apply except that the amount of the presumed gain is to be determined by the excess of the fair market value of the property at the time

of its disposition over its then adjusted basis.

This treatment is to apply in the case of most dispositions of property whether or not gain is otherwise recognized. The treatment described above does not apply, however, in the case of gifts, although in the case of charitable contributions the amount of the charitable contribution deduction which may be taken is reduced by the amount which would be treated as ordinary income if this provision were applicable. Other exceptions are provided for property transferred at death, for transfers where no gain is recognized and the basis of the property is carried over to the transferor, and for transfers in like kind exchanges and involuntary conversions to the extent no gain is recognized. In the case of partnership, distribution to partners or sales of partnership interests are taxed to the partners to the extent of the underlying depreciable property in much the same way as if the depreciable property had been sold directly.

The bill also provides that in computing the basis on which depreciation may be taken salvage value may be ignored up to an amount equal to 10 percent of the cost or other basis of the property. Also, under the bill taxpayers are permitted to elect to change their method of depreciation with respect to property coming within the scope of this provision from any declining balance, or sum-of-the-years digit method to a straight-line method.

This provision applies to taxable years beginning after December 31, 1962.

SECTION 14. FOREIGN INVESTMENT COMPANIES

When stock in foreign investment companies is sold, the gain realized by the U.S. shareholders is to be ordinary income (instead of capital gain) to the extent of the taxpayer's share of the earnings and profits of the corporation accumulated in taxable years beginning after December 31, 1962, and during the period in which he held the stock. In the case of stock in a foreign investment company acquired from a decedent, the basis of the stock is not to be increased at the date of death to the extent of the amount which would have been taxed as ordinary income to the decedent had he sold the stock before death. A deduction for estate tax attributable to this amount will be allowed, however, upon subsequent sale of this stock by the heir or legatee.

The companies and shareholders can avoid the treatment described above if the companies distribute 90 percent or more of their taxable income, other than capital gains, designate in a written notice to the shareholders each year (to be mailed to them within 45 days after the close of the taxable year) their ratable share of the capital gains of the corporation and provide such other information as the Treasury requires to enforce this provision. The shareholders, however, must also report as capital gains their share of the capital gains of the corporation, whether the gains are distributed or not. Where these provisions are complied with, the shareholders are permitted to take a foreign tax credit for foreign taxes paid by the company. Under the bill a foreign investment company is permitted to reincorporate (in a tax-free reorganization) as a domestic regulated investment company if it does so before January 1, 1964.

These provisions apply with respect to taxable years beginning after December 31, 1962.

SECTION 15. GAIN FROM SALES OR EXCHANGES OF STOCK IN FOREIGN CORPORATIONS

Where there is a redemption of stock in a controlled foreign corporation or a controlled foreign corporation is liquidated, or where stock in such a corporation is sold, then any gain to the extent it represents earnings and profits of the corporation accumulated in taxable years beginning after

December 31, 1962, is to be taxed to 10 percent or more U.S. shareholders as ordinary income. If the shareholder is a corporation, it is allowed a foreign tax credit for taxes paid to foreign countries in the same manner as in the case of any other dividend.

If the shareholder is an individual, his tax is to be no greater than the smaller of two ceilings. The first ceiling provides that the individual's tax is to be no greater than if the foreign corporation had been a domestic corporation paying the regular 52-percent U.S. tax (offset by any foreign tax credits allowable) which then made a liquidating distribution of the balance to the U.S. shareholder and this balance was subject to capital gains tax. In other words, this ceiling would provide a U.S. tax of 52 percent, against which foreign tax credits could be taken, and on the balance (not over 48 percent of the total) a capital gains tax of not over 25 percent would be paid. Thus, the aggregate maximum tax in this case would be 64 percent (52 percent plus 25 percent of 48 percent). The second ceiling is the amount of tax which would have resulted had the earnings and profits been distributed to the shareholder in the years they were earned. The section also provides that earnings and profits are not to include profits on sales made during a liquidation if the corporation could have qualified for tax-free sales on liquidation if it had been a domestic corporation. The section does not apply to stock of a less developed country corporation which had been held for 10 years at the time of its sale. These provisions apply with respect to sales or exchanges occurring after December 31, 1962.

SECTION 16. SALES AND EXCHANGES OF PATENTS, ETC., TO CERTAIN FOREIGN CORPORATIONS

The committee amendments provide that gain from the sale or exchange after December 31, 1962, of a patent invention, model or design, copyright, secret formula or process, or other similar property, to a foreign corporation by a U.S. person (corporation, individual, etc.) who controls the foreign corporation is to be treated as ordinary income rather than as a capital gain. This provision is not to apply in the case of a patent, etc., transferred to a foreign corporation in exchange for stock or as a contribution to capital if it is established to the satisfaction of the Treasury that the principal purpose of the transfer is to enable the foreign corporation to use the patent, etc., in its own manufacturing operations. This is to apply to taxable years beginning after December 31, 1962.

SECTION 17. TAX TREATMENT OF COOPERATIVES AND PATRONS

Cooperatives are to receive a deduction for patronage dividends paid to their patrons in cash, or by allocations if the patron has the option to redeem the notices of allocation in cash not later than 90 days after they are issued or if he consents to this income being treated as constructively received by him and then reinvested in the cooperative. In either case, under the bill, 20 percent of the value of a patronage dividend which includes qualified allocations must be in the form of cash. The patron, either a member or non-member, may give his consent individually in writing, or, a patron who is a member may also consent by retaining membership in a cooperative after it adopts a bylaw requiring consent by all members and gives written notice of this bylaw to all members. Under a third method, consent may be given by the endorsing and cashing of a qualified check for the 20-percent amount referred to above. If the check for the 20-percent amount is endorsed and cashed by 90 days after the date for filing the tax return the patronage dividend of which the check is part will be deductible by the cooperative with respect to the year in which the patronage occurred. In the case of allocations

which do not qualify, the cooperative will initially be taxed on this type of patronage dividends. However, when such a patronage dividend is redeemed, the cooperative will receive a deduction (or refund of tax) at that time. In the case of allocations which do not qualify, the cooperative will initially be taxed on this type of patronage dividends. However, when such a patronage dividend is redeemed, the cooperative will receive a deduction (or refund of tax) at that time.

Where consent is given, or where the option to receive cash was available, the patron will be required to include the patronage dividends which arise from business activity as taxable income. The patron will also be required to take into account nonqualifying patronage dividends when they are redeemed (assuming they arise from business activity).

In addition, all cooperatives (rather than merely tax-exempt cooperatives as under present law) are given until 8½ months after the end of the year in which patronage occurs to allocate amounts to the accounts of their patrons and in most cases are also given this same period of time for the filing of their own income tax returns. These provisions apply to taxable years of cooperatives beginning after December 31, 1962, and with respect to amounts received by patrons attributable to years of the cooperatives to which the new law applies. The new provisions will not, however, apply to future redemptions of patronage dividends declared when the old law was applicable.

SECTION 18. INCLUSION OF FOREIGN REAL PROPERTY IN GROSS ESTATE

Real property located outside of the United States, in the case of citizens or residents of the United States, is to be included in their tax base for purposes of the Federal estate tax imposed at the time of their death. This provision will be fully effective for decedents dying on or after January 1, 1963. For those dying after the date of enactment of this bill, and before January 1, 1963, real property located outside of the United States will be included in their gross estate only if acquired on or after February 1, 1962.

SECTION 19. REPORTING OF INTEREST, DIVIDEND, AND PATRONAGE DIVIDEND PAYMENTS

The bill provides, in lieu of withholding, for the reporting of most interest, dividend, and patronage dividend payments of \$10 or more per year. These reports must be made to the Government on an annual basis and also to each dividend or interest recipient on an annual basis. The bill provides civil penalties of \$10 for each statement not sent to the Government unless it is shown that the failure is due to reasonable cause. The aggregate penalty in this case is not to exceed \$25,000. Similarly, a civil penalty of \$10 per statement is provided for failure, other than with reasonable cause, to send the statements to the interest or dividend recipients. Here, too, the maximum penalty is \$25,000. These penalties are in addition to criminal penalties in existing law.

SECTION 20. INFORMATION WITH RESPECT TO FOREIGN ENTITIES

A number of changes are made in the annual information return which domestic corporations presently are required to file with respect to their subsidiaries or foreign corporations which they control. The changes are: This return is to be filed not only by corporations but by others as well who control foreign corporations; "control" is defined more broadly by adding some of the constructive ownership rules; information must be provided not only with respect to subsidiaries of foreign corporations but also for other foreign corporations which are further down the chain of ownership; and additional information may be required which is similar or related in nature to that already specified. A ceiling has been placed on the penalty applicable under present law,

to provide that the reduction in the foreign tax credit of a corporation, which would occur for noncompliance with the reporting requirements, may not exceed the income of the foreign corporation with respect to which the failure occurs or \$10,000, whichever is greater.

Present law also requires U.S. citizens or residents who are officers or directors of a foreign corporation within 60 days of its organization or reorganization and also 5-percent shareholders who have this status within 60 days of the organization or reorganization to supply certain information to the Treasury Department with respect to the corporation. This same information is also to be required of U.S. citizens or residents who at some later time become officers, directors, or shareholders with an interest of 5 percent or more. However, in the case of U.S. officers or directors of a foreign corporation, this reporting requirement is to apply only if 5 percent or more of the value of the stock is owned by a U.S. person and the only information these officers or directors are to be required to furnish is the names and addresses of these 5-percent shareholders. Information is not to be required under this provision unless so provided by regulations in effect 90 days before the filing of the information return is required. A penalty provision also is provided.

Generally, these additional information requirements become effective as of January 1, 1963.

SECTION 21. CLEARING OF LAND

In the case of farmers, expenditures incurred during any taxable year in the clearing of land (which would otherwise be chargeable to capital account) may be deducted to the extent of \$5,000 or 25 percent of the taxable income from farming for that year, whichever is the lesser.

SECTION 22. CERTAIN CHARITABLE CONTRIBUTIONS

Where an individual is entitled to (in effect) spread his income over the years to which it is attributable for purposes of determining his tax, he may elect to apply the limitation on charitable contributions (20 percent or 30 percent, whichever is applicable) before the income is spread, and then spread only the income remaining after the charitable deduction.

SECTION 23. SECTION 1371(c)

The effective date of section 1371(c) (relating to husband and wife in community property States) is made effective with respect to taxable years beginning after December 31, 1957, and elections by small business corporations to have their income taxed directly to their shareholders are to be validated if the shareholders so consent within 1 year after the date of enactment of this act.

SECTION 24. LOSSES BY CERTAIN STREET RAILWAY COMPANIES

Net operating losses incurred in 1953 and 1954 by a street railway company in converting from streetcar to bus service, which were not absorbed within the normal 3-year carryback and 5-year carryforward period, are to be treated as a net operating loss occurring in 1959. This will permit these unused losses to be absorbed over the years 1960 through 1964.

SECTION 25. EXEMPTION FOR PENSION TRUST

The union-negotiated pension plan of Local Union No. 435 of the International Hod Carriers' Building and Common Laborers' Union of America is to be treated as a qualified, tax-exempt trust for the period beginning May 1, 1960 and ending April 20, 1961, if it is shown to the satisfaction of the Secretary of the Treasury that the trust was not operated during this period in a manner which would jeopardize the interests of its beneficiaries. This will permit employers to

deduct contributions made to this trust in this period.

SECTION 26. CONTINUATION OF PARTNERSHIP YEAR IN CERTAIN CASES

Your committee's amendments modify the 1939 Code to provide that where one partner dies, in a partnership consisting of two members, the partnership year for the surviving partner is not to close prior to the time the partnership year would have closed if neither partner had died. This provision is to apply only if the surviving partner so elects within 1 year after the date of enactment of this provision. This amendment applies to taxable years of a partnership beginning after December 31, 1946, to which the 1939 Internal Revenue Code applies.

SECTION 27. TREATIES

No provision of this bill is to apply in any case where its application would be contrary to any treaty obligation of the United States.

Mr. KERR. Mr. President, a parliamentary inquiry.

The PRESIDING OFFICER. The Senator from Oklahoma will state it.

Mr. KERR. First, however, if the distinguished junior Senator from Tennessee [Mr. GORE] is in the Chamber—

Mr. PROXMIRE. The Senator from Tennessee will return to the Chamber in a few minutes.

Mr. KERR. Mr. President, I shall repeat my request for unanimous consent that the committee amendments be agreed to en bloc; and that the bill as thus amended be considered as original text for the purpose of further amendments. However, on the assumption that the request will be objected to, I address this parliamentary inquiry to the Chair: What will be the parliamentary procedure with reference to the consideration of the bill as affected by the committee amendments?

The PRESIDING OFFICER. If the unanimous-consent request is objected to, the order of business before the Senate will be the first amendment that has been proposed by the committee.

Mr. KERR. The first committee amendment?

The PRESIDING OFFICER. That is correct.

Mr. KERR. Mr. President, in view of that fact, and the fact that I have been on the floor about 4 hours, I shall yield the floor at this time.

I say to the distinguished Senator from Wisconsin that I shall be in the Chamber repeatedly and shall be happy, from time to time, to answer any questions he may have to the extent of my ability.

Mr. PROXMIRE. Mr. President, I have a series of questions to address to the Senator from Oklahoma. I will appreciate it if he will yield to me later in the day.

The PRESIDING OFFICER. The first committee amendment will be stated.

The LEGISLATIVE CLERK. On page 8, line 2, after the word "Code" and the period, it is proposed to strike out "Whenever" and insert "Except as otherwise expressly provided, whenever".

Mr. DOUGLAS. Mr. President—

The PRESIDING OFFICER. (Mr. FELL in the chair). The Senator from Illinois is recognized.

SUPPORT FOR PRESIDENT'S TAX PROPOSALS

Mr. DOUGLAS. Mr. President, legislative decisions on important matters are not primarily made inside the walls of this Chamber. Such decisions are instead largely made by public opinion outside this Chamber; they are made by public opinion acting on the information primarily furnished to the public by the press.

Over the weekend I began to think that insofar as the struggle over this tax bill is concerned, I was living in a world of Alice in Wonderland—a world in which the stated issues and problems were exactly contrary to the issues really at stake. At times it seems like George Orwell's "1984" with its doublespeak and its contradictory slogans such as "War is peace," and so forth.

The junior Senator from Tennessee [Mr. GORE] and I have been closely associated with this tax bill ever since it came from the House of Representatives and ever since the Senate Finance Committee began its hearings in April. We attended the committee hearings, and we worked in the executive sessions of the committee. In the main, we fought for the original program of the President of the United States.

We saw amendment after amendment submitted which largely would gut the recommendations made by the President. In our minority views, the Senator from Tennessee and I urge—in the main—that the substantial features of the President's original program be returned to the bill and be enacted into law. We intend to fight on the floor of the Senate for those principles.

Therefore, it was quite proper, I believe, for the Senator from Tennessee to object to the request of the Senator from Oklahoma [Mr. KERR] that the committee amendments be agreed to en bloc, for many of the committee amendments would help to wreck the President's original program. Certainly the committee should be required to justify every eviscerating amendment which it proposes.

Mr. President, those are the facts, and I think they will become evident to the country.

PRESS REPORTS MISLEADING

This morning I read in the lead article in the Washington Post—an article which I believe also was printed in the New York Herald Tribune—a statement:

A powerful array of liberal and conservative Senators are lined up to battle today against the administration-sponsored tax revision bill.

(See exhibit 1.)

Mr. DOUGLAS. In an editorial published on Saturday the Washington Post bemoans "the obstructive course of action to which Senators DOUGLAS and GORE appeared to be committed."

(See exhibit 2.)

Mr. DOUGLAS. Mr. President, our course is described by the Washington Post as "an obstructive course of action" because we want to put the President's program into effect.

FUNNY THING HAPPENED ON MY WAY TO THE SENATE

Mr. President, a funny thing happened this noon, when I was on my way

to the Senate. As I came into the Capitol, a reporter gave me a tearsheet from the Wall Street Journal of today. I think the Senator from Wisconsin has already made some reference to it. It reads, in part:

"Liberal Tax Bill Amendments Face Defeat in Senate."

Listen to this, Mr. President—

"Democratic Chiefs To Fight Bid To Restore Proposal That President Had Urged."

In the body of the article which follows those headlines, we find the following:

Senate Democratic leaders plan to employ harsh parliamentary tactics against liberal efforts to restore some of President Kennedy's recommendations to the Senate Finance Committee's version of the tax-revision bill.

(See exhibit 3.)

Mr. DOUGLAS. Mr. President, the Wall Street Journal, with its usual accuracy, is correct in stating that we are trying to restore the original recommendations of the President; and I hope the Washington Post and the New York Herald Tribune will take note of that fact. When the Senator from Oklahoma [Mr. KERR] moves the adoption of gutting amendment after gutting amendment, in an effort to eviscerate the President's tax-revision plan, it will be made abundantly clear that we who are objecting to those proposals are, in the main—and I emphasize the words "in the main"—trying to defend the program of the President of the United States.

FAVOR ADMINISTRATION TAX BILL

On Saturday, the Washington Post took the Senator from Tennessee [Mr. GORE] and me to task, because it said we had joined forces with the Senator from Virginia [Mr. BYRD] in opposing the administration's tax bill, and said this would shock "even the most cynical of political observers."

Mr. President, I hold the Senator from Virginia in high personal esteem. But I suppose the record of the rollcall votes in the Senate in the 14 years that I have been serving here will indicate that in connection with approximately 95 percent of the controverted bills, we have been on opposite sides.

I do not know whether the Senator from Virginia is opposing the administration's tax bill; but certainly the Senator from Tennessee [Mr. GORE] and I are not opposing the administration's tax bill. We are in favor of the administration's tax bill—the original tax bill; and we are against those who would try to destroy it.

I make no apologies for being in agreement with the Senator from Virginia [Mr. BYRD] in regard to the present form of the investment-credit plan. I should like to state the matter the other way; I should like to say that I am greatly pleased that the Senator from Virginia [Mr. BYRD] agrees with the Senator from Tennessee [Mr. GORE] and me in opposing the investment-credit plan in its present form, because the present form of the investment-credit plan is very different from its original form, as I shall demonstrate as I proceed.

I believe we should consider these issues on the basis of their merits, not on the basis of a listing of those who favor them and those who oppose them.

The Senator from Virginia [Mr. BYRD] has always—even when I differed most vigorously with him—treated me with perfect courtesy and kindness; treatment which I have not always received from other quarters; and I wish to pay tribute to him and thank him for the gentility with which he has behaved toward those whose views have differed from his.

I am glad to welcome the Senator from Virginia [Mr. BYRD] to the ranks of those of us who oppose the present form of the investment-credit plan. I am not at all ashamed to be seen going down the street with him on this issue.

We may differ on the issues involved, but as long as he is on the right side on this issue, I will keep in step with him—for a limited period of time. [Laughter.] And I hope that our associations together, fighting this iniquitous investment credit, will gradually lead to a tempering of his own opinions so that he will walk with the Senator from Tennessee and the Senator from Illinois for a longer period of time. We do not expect him to become a fellow traveler of ours, but we hope that he will be at least a limited pedestrian associate. [Laughter.]

TAX REFORM ORIGINAL PURPOSE

Mr. President, one of the tricks of semantics is to alter the terms of reference and to call different things by the same words. We liberals are making our fight to return to the main features of the President's original tax bill. That original bill included not only business stimulation, but tax reform. Those two features were contained in the tax message of the President to the Congress last year. They were embodied in the original administration tax proposals to the House of Representatives last year. But now notice what my good friends

in the Washington Post say this morning.

(See exhibit 4.)

Mr. DOUGLAS. They refer to this bill not as the tax reform bill but as "the investment credit bill," and they are trying to pretend that the present form of the investment credit bill is the form which the President originally advocated, whereas it is not at all, of course.

So, Mr. President, let there be no confusion among the members of the press who sit on high in judgment upon us. Let there be no confusion about this matter. The Senator from Tennessee, the Senator from Illinois, and those who think similarly with us are fighting the pro-administration fight; and I hope that for once the Wall Street Journal is not accurate in its prediction that the "Senate Democratic leaders," in its words, "plan to employ harsh parliamentary tactics against liberal efforts to restore some of President Kennedy's recommendations."

By the very astute parliamentary maneuver of the junior Senator from Tennessee [Mr. GORE], the initiative has been thrown upon the Senator from Oklahoma [Mr. KERR]. It will not be the liberal group which will be proposing amendments to the bill which can be falsely called the administration's bill—

Mr. GORE. Crippling amendments.

Mr. DOUGLAS. Crippling amendments; weakening amendments. No; it will have to be the Senator from Oklahoma who will defend why he is offering crippling amendments to the administration's program though he sits in the chair of the floor leader of the Democratic Party.

Mr. President, I ask unanimous consent that the articles and editorials which I have referred to be printed in the RECORD at the conclusion of my remarks.

The PRESIDING OFFICER. Without objection it is so ordered.

Mr. CURTIS. Mr. President, will the Senator yield for a question?

Mr. DOUGLAS. I yield for a question.

Mr. CURTIS. Can the distinguished Senator tell us whether or not the administration is supporting the provision now in the bill, or in the committee amendments, for the investment credit?

Mr. DOUGLAS. I think it is.

Mr. CURTIS. It is.

Mr. DOUGLAS. I think it is supporting the present form of the investment credit, but I do not think it would object if we returned to the original form.

Mr. CURTIS. Well, it was worse.

Mr. DOUGLAS. No; it was much better, and I shall develop that as I go along.

When the administration proposed this bill a year and a half ago, it was intended to close a few of the loopholes which disgrace our tax system—most conspicuous of which, of course, is the 27½-percent depletion allowance on gas and oil, which is the particular pet of the Senator from Oklahoma—and which cause grave injustices and irregularities in the application of our tax laws. The total amount of revenue which would have been saved to the Treasury, and hence to the people, was, by the terms of the President's original proposal, approximately \$2.3 billion.

We have prepared a summary table which shows the President's original proposals, together with what happened to them in the House, together with what happened to them in the Senate Finance Committee. Here is a record so that we can see who did the dirty work at the crossroads.

I ask unanimous consent that this summary of the evolution, or devolution, or degeneration, of the President's tax bill be printed in the RECORD at this point in my remarks.

There being no objection, the table was ordered to be printed in the RECORD, as follows:

TABLE I.—*Evolution of the Revenue Act of 1962—with pertinent revenue estimates*¹

LOOPHOLE CLOSERS

President's proposals of Apr. 20, 1960	Revenue gain	House bill	Revenue gain	Revenue decrease compared to President's proposal	Finance Committee bill	Revenue gain	Revenue decrease compared to House bill	Revenue decrease compared to President's proposal
	Millions		Millions	Millions		Millions	Millions	Millions
Sec. 4. Expense accounts: Provides that the cost of business entertainment, including club dues, and the maintenance of entertainment facilities (such as yachts and hunting lodges) be disallowed in full as a tax deduction. Restrictions should also be imposed on the amount to be deducted as business gifts, on travel expenses for vacations that are combined with business travel, and on excessive personal living expenses incurred on business travel away from home.	\$250	Under the House bill expenditures for entertainment activities must be directly related to the active conduct of the taxpayer's trade or business and those for entertainment facilities such as yachts must meet an additional test of being primarily in furtherance of the trade or business. Deduction was denied for business gifts in excess of \$25, a standard of "reasonableness" was added to the provisions dealing with traveling expenses, and a good rule requiring substantiation of expenditures was adopted.	\$125	\$125	The Finance Committee added to the directly related test of the House bill a liberalizing test permitting the deduction of entertainment expenditures if they are directly "associated with" the taxpayer's trade or business. In addition, the committee's report is very weak and confusing—quite unlike the report of the House Ways and Means Committee which provided some meaningful guidelines that made the House provision workable and effective.	\$60	\$65	\$190
Sec. 6. Mutual savings banks: The existing bad debt reserve formula of 12 percent of deposits, which has resulted in virtual tax exemption, would be reviewed to assure "non-discriminatory treatment." The Treasury Department Report of July 1961 suggested alternative methods of taxation to produce revenue of between \$150 to \$416 million, at 1963 levels of income, depending upon alternative selected.	150-416	Provided a bad debt reserve deduction of 3 percent of the increase in real estate mortgage loans or, alternatively, a deduction of 60 percent of retained earnings. Technical provisions changed definition of "domestic building and loan association," prevented capital stock savings and loan associations from distributing to stockholders pre-1952 tax-free surplus, removed certain exemptions from excise taxes, and applied realistic rules for computing bad debts resulting from mortgage foreclosures.	200	-----	In the case of capital stock savings and loan associations, the special deduction of 60 percent of earnings was reduced to 50 percent to produce additional revenue of about \$5 million annually. Other changes modified definition of domestic building and loan association, broadened repeal of excise tax exemptions, imposed ceilings on amount of reserves, and took into account tax-free surplus accumulated prior to 1952 to the extent necessary to place all institutions on an equal basis.	205	+5	-----
Sec. 8. Mutual insurance companies Provided for the elimination of the special provisions of existing law which are applicable only to mutual fire and casualty insurance companies, so as to tax such companies on total income in essentially the same manner as stock fire and casualty insurance companies.	50	Provided a modified total income approach which permits a portion of underwriting income to be set aside tax free in a special reserve for protection against losses. Also, provided special rules for concentrated risk companies, reciprocals, factory mutuals, mutual marine companies, and certain small mutuals.	40	10	Changed the order in which losses are to be charged to the special protection against loss reserve. Other changes liberalized the provisions of the House bill relating to concentrated risk companies, reciprocals and certain small mutuals, and provided a special rule for taxing mutual flood insurance companies.	35	5	15
Sec. 13. Gain on depreciable property Gain on sale of depreciable property, both real and personal, should be treated as ordinary income to extent of prior depreciation.	200	Removed real estate from application of provision.	100	100	Same as House bill.	100	0	100
Sec. 17. Cooperatives: Provide that all earnings of a cooperative arising from business activities are taxable to either the cooperative or its patrons. The patrons (and not the cooperative) would pay the tax on patronage distributions in money or noncash allocations meeting certain conditions. The cooperative would be taxable on earnings which are not returned to the patrons.	35	The Ways and Means Committee made several refinements in the bill, none of which affected the revenue estimate. The primary change requires the patron to consent to paying the tax on noncash distributions before he is taxable and the cooperative receives a deduction.	35	0	The Senate Finance Committee made 2 changes in the House bill, none of which affects the revenue estimate. One would require the cooperative to distribute at least 20 percent of its patronage dividends in cash in order to escape tax—this replaces the 20-percent withholding that would have been required under the House bill. The other change prescribes an alternative method for a patron to consent to paying tax on noncash distributions.	35	0	0
Sec. 19. Withholding: Provide for withholding of 20 percent from interest, dividends, and patronage dividends.	880	The Ways and Means Committee made several important refinements in the bill, but none of them affected the revenue estimate. The most important changes were the inclusion of exemptions for nontaxable persons and the extension of the quarterly refund procedures to taxable individuals who are subject to overwithholding.	Same	-----	The Senate Finance Committee deleted the withholding plan and substituted an expanded information reporting plan under which all dividend, interest, or patronage dividend payments of \$10 or more a year must be reported to the Government, with a copy of the information given to the payee.	1 275	605	605
FOREIGN INCOME								
Sec. 12. Controlled foreign corporations: Provide for the elimination of deferral of U.S. tax of foreign subsidiaries.	230	The House bill would eliminate deferral with respect to certain tax haven profits, earnings not reinvested in an existing business in a developed area or in an active business in a less developed area and earnings reinvested in the United States in such a way as to constitute a constructive dividend. However, tax haven profits which were invested in less developed areas would not be covered.	85	145	The Senate Finance Committee restricted its approach to the elimination of deferral for tax haven profits and those earnings invested in the United States. It improved the taxation of tax haven profits by (a) including certain service income and branch sales profits, (b) excluding the profits of certain active businesses from the definition of tax haven profits, and (c) eliminating the "pour over" of developed-area tax haven profits into less developed countries. The committee also added 2 important exceptions for (a) the earnings of certain export trade corporations and (b) the earnings of certain foreign subsidiaries or groups of foreign subsidiaries which distributed specified minimum percentages of their after-tax earnings.	85	0	145

Footnote at end of table.

TABLE I.—*Evolution of the Revenue Act of 1962—with pertinent revenue estimates*¹—Continued

LOOPHOLE CLOSERS

President's proposals of Apr. 20, 1960	Revenue gain	House bill	Revenue gain	Revenue decrease compared to President's proposal	Finance Committee bill	Revenue gain	Revenue decrease compared to House bill	Revenue decrease compared to President's proposal
FOREIGN INCOME—continued	<i>Millions</i>		<i>Millions</i>	<i>Millions</i>		<i>Millions</i>	<i>Millions</i>	<i>Millions</i>
Sec. 9. Gross-up: Provide for gross-up of dividends received by U.S. companies from their foreign subsidiaries so as to correct the inadequacy of the existing foreign tax credit formula under which the combined U.S. and foreign tax may be substantially lower than 52 percent. Under existing law, the disparity between 52 percent and the actual combined rate varies with the actual foreign taxes paid, being highest at 26 percent and gradually diminishing as the foreign tax drops below or rises above 26 percent. Secs. 5, 7, 10, 11, 14, 15, 16, 18, 20, and 27. All other foreign items: (For convenience, section references refer to section numbers in the Senate Finance Committee bill.) (1) Eliminate the tax-free nature of certain distributions by foreign trusts to U.S. beneficiaries (sec. 7). (2) Eliminate the exclusion of income for U.S. citizens residing in developed areas of the world and reduce it to \$20,000 annually for those residing in less developed areas (sec. 11). (3) Eliminate the tax benefits now obtained by U.S. citizens through investments in foreign investment companies (sec. 14). (4) Eliminate the present exclusion of foreign real property from the gross estate of decedents subject to U.S. tax (sec. 18). (5) Improve the information now required regarding U.S.-owned foreign corporations (sec. 20). [No recommendations similar to secs. 5, 10, 15, 16, or 27.] Repeal of dividends received credit and exclusion Repeal of provision excluding first \$50 of dividends and allowing a credit of 4 percent on dividends in excess of \$50.	\$35	With the exception of a 2-year grace period for previously accumulated earnings, the Ways and Means Committee adopted the President's recommendation.	\$35	\$0	The Senate Finance Committee adopted the proposal only with respect to dividends received from operations in developed areas. The existing formula would continue to apply for dividends paid from less developed country earnings.	\$25	\$10	\$10
(1) Eliminate the tax-free nature of certain distributions by foreign trusts to U.S. beneficiaries (sec. 7). (2) Eliminate the exclusion of income for U.S. citizens residing in developed areas of the world and reduce it to \$20,000 annually for those residing in less developed areas (sec. 11). (3) Eliminate the tax benefits now obtained by U.S. citizens through investments in foreign investment companies (sec. 14). (4) Eliminate the present exclusion of foreign real property from the gross estate of decedents subject to U.S. tax (sec. 18). (5) Improve the information now required regarding U.S.-owned foreign corporations (sec. 20). [No recommendations similar to secs. 5, 10, 15, 16, or 27.] Repeal of dividends received credit and exclusion Repeal of provision excluding first \$50 of dividends and allowing a credit of 4 percent on dividends in excess of \$50.	50	The Ways and Means Committee generally adopted the proposals regarding foreign trusts, foreign investment companies, foreign real estate and improved information requirements. As to the earned income exclusion, the committee provided that U.S. citizens residing abroad could annually exclude \$20,000 for the first 3 years of foreign residence and \$35,000 thereafter, without distinction between developed and less developed areas. The committee added provisions increasing the taxation of distributions in kind from foreign corporations (sec. 5), gain on the sale or exchange of stock in foreign corporations (sec. 15) and a provision regarding the relationship between the bill and existing tax treaties (sec. 27).	30	20	The Senate Finance Committee, at the recommendation of the Treasury, added a provision providing for a special computation of the foreign tax credit with respect to certain interest income designed to halt certain flows of capital abroad which are induced by the existing foreign tax credit mechanism (sec. 10) and also added a provision providing for the taxation of gain from the sale of certain patents and other intangible rights to foreign subsidiaries as ordinary income where such gain would otherwise be taxable as capital gain under existing law (sec. 16).	30	0	20
Repeal of provision excluding first \$50 of dividends and allowing a credit of 4 percent on dividends in excess of \$50.	450	Not included in bill.	0	450	Not included in bill.	0	0	45

LOOPHOLE OPENERS

Sec. 2. Investment credit: Investment in new real and personal depreciable property having a useful life of 6 years or more qualified for a credit of 15 percent to the extent the new investment exceeded current depreciation allowances. A 6-percent credit was allowable on new investment between 50 and 100 percent of current depreciation allowances, with a minimum credit of 10 percent on the first \$5,000 of new investment. The credit was not to affect the depreciable cost of the property. Residential property, property used outside the United States, and property used by public utilities (other than transportation) were ineligible. The credit deductible in any one year was limited to 30 percent of tax liability, but the excess could be carried forward for 5 years. The proposed effective date was Jan. 1, 1961.	<i>Billions</i> \$1.7	The House approved the tax credit plan, but made the following changes: (1) Eliminated the "excess approach" in favor of a 7-percent flat across-the-board credit; (2) Excluded all buildings and certain other real property, but made personal property of hotels and motels eligible; (3) Permitted \$50,000 of used property to qualify; (4) Eliminated any limitation on the use of the credit on the taxpayer's first \$25,000 of tax liability; adopted a 25-percent limitation on the tax liability above \$25,000; (5) Approved a 3-percent credit for public utilities; (6) Dropped the useful life requirement to 4 years, but scaled down the benefits of the credit for assets with lives between 4 and 8 years; (7) Moved the effective date up to Jan. 1, 1962.	<i>Billions</i> \$1.395	<i>Millions</i> \$305	The Senate Finance Committee modified the House bill in the following manner: (1) Required that the credit be subtracted from the taxpayer's cost of the property before permitting the taxpayer to compute his depreciation allowance. (2) Disallowed a credit upon the investment of insurance proceeds, and upon the purchase of livestock. (3) Approved a 3-year carry-back of unused credits, in addition to the 5-year carryover. (4) Moved the effective date up to July 1, 1962.	<i>Billions</i> \$1.340	<i>Millions</i> \$55	<i>Millions</i> \$300
Sec. 3. Lobbying expenditures: The President did not recommend that a deduction be allowed for lobbying expenditures and the Treasury Department is opposed to the allowance of any deductions in this area.	-----	The House bill permits business taxpayers to deduct the following lobbying expenditures: the cost of appearing before and communicating with committees of Federal, State, or local legislative bodies, contacting individual legislators, transmitting legislative information between a taxpayer and an organization of which he is a member, and the portion of the dues paid by a member attributable to the carrying on of such activities by the organization.	(*)	-----	The Finance Committee expanded the House provision to cover the cost of sending lobbying material to employees and stockholders.	-----	(*)	-----

¹ All estimates in this table are those of the Treasury except for the investment credit as passed by the House and as passed by the Senate Finance Committee, and the revenue figures for reporting of dividends and interest, where the Joint Committee on Internal Revenue Taxation's figures are used.

² \$670 million (based on 1959 data) \$780 million based on 1960 data; \$880 million for 1963, based on trends from previous years.

³ No estimates available.

ORIGINAL BILL PROVIDED REVENUE GAIN

Mr. DOUGLAS. Mr. President, the President of the United States advanced these proposals for tax reform, but to "sweeten" them and to make them more acceptable to those who had been avoiding the just payment of taxes on income which they had received in the past, he also offered a tax adjustment consisting of a generous tax credit on most forms of net business investment in depreciable property. It was estimated that, on an annual basis, this would lose \$1.7 billion in revenue.

The original plans of the administration thus provided for an overall annual increase in revenues of about \$600 million. But it is probably fair to conclude that, knowing the tendency for tax reform proposals to be whittled away, and indeed to evaporate, as they move through Congress, the administration really would have been satisfied if the loophole closing and the investment credit finally offset each other so that there would have been little or no revenue gain or loss. The basic original aim of the bill was, therefore, first, to effect minor and, it was believed, the less controversial changes in the field of tax reform, and, second, to balance this with an approximately equal reduction in the taxes paid by business and industry. This latter was framed in such a way that it was hoped it would stimulate new investment and the modernization of machinery and equipment.

BILL DISFIGURED BY CONGRESS

In the long-drawn-out process of nearly a year and a half during which this bill has moved slowly through the other body and through the Finance Committee, it has been disfigured almost beyond recognition, and I think it can fairly be said to have been wrecked.

The proposal to repeal the 1954 dividend credit of 4 percent and the exclusion of \$50 of dividends which would have reclaimed \$450 million a year for the Treasury and the people was thrown overboard early.

The main feature on the loophole closing side, namely, the withholding at the source on dividends and interest income paid by institutions, was eliminated by a lopsided vote in our committee—I believe a vote of 12 to 5—and the Senator from Illinois is proud of the fact that he was one of the 5 who voted against the elimination of this withholding method of collecting taxes.

Mr. GORE. Mr. President, will the Senator yield?

Mr. DOUGLAS. Yes, I am glad to yield.

Mr. GORE. Is not the parliamentary situation now such that the withholding provision is in the bill now before the Senate, and the vote on the subject, if the Senate has a vote on the subject, will be on a motion to strike it from the bill?

Mr. DOUGLAS. That is correct, and I will watch that performance with great interest, and it will be interesting to see who votes for the President of the United States and who votes against the President of the United States. The Senator from Tennessee and the Senator

from Illinois will be on the side of the President.

In this connection, it is also interesting to observe that when the President gave out his statement at the White House last week, the one feature of the tax bill which he emphasized was his desire to retain in the tax bill the withholding provision on dividends and interest.

Mr. GORE. Mr. President, will the Senator yield?

Mr. DOUGLAS. It will be interesting to see if some of those in charge of this bill rise in open revolt against the proposal of the President. If they can do it in the name of carrying out the President's program, as they are now trying to do, I can only say that Harry Houdini will have had worthy successors.

Mr. GORE. Mr. President, will the Senator yield?

Mr. DOUGLAS. I am glad to yield.

Mr. GORE. In addition to being curious as to whether that will be done, will not the Senator be anxious to note exactly which of our colleagues will move to strike from the bill the one provision which the President has recommended so strongly?

Mr. DOUGLAS. I will certainly watch that with interest. And I will watch the subsequent rollcall with interest.

A TORNADO OF MAIL

Now, Mr. President, I should like to give a more ample discussion of this withholding feature later. It is estimated that this elimination would lose about \$900 million in revenues from taxes which are owed but not paid in its first full year of operation.

This elimination, which would ultimately cost the people of the United States almost \$1 billion a year, was done at the behest of the most powerful organized mail campaign I suppose I have seen in the 14 years I have served in the Senate. This step was taken by the committee to the accompaniment of a tornado of mail stimulated by the building and loan associations, the banks, and the mutual savings institutions.

I personally received no less than 75,000 letters from my constituents demanding that the withholding provision be eliminated from the bill. While I know it may sound self-righteous—and I believe some of my friends have accused me of being excessively self-righteous—I wish to say that if I can withstand 75,000 letters I think others can do the same.

GRAVE MISCONCEPTION

These letters portrayed gross misconceptions of what the withholding method really was. From one-third to one-half of the correspondents wrote that it was a new tax, to be imposed on dividends and interest, which did not now exist. Why, of course, it is not that. Dividends and interest are income exactly as wages, salaries, and rents are income. They are subject to the income tax laws of the country now, exactly as wages and salaries are subject to the income tax laws of the country. They are income and are equally taxable with wages and salaries.

NOT A NEW TAX

The very fact that so many wrote that this was a new tax which they did not now have to pay was rather strong presumptive evidence that many of these people have not been paying taxes on dividends and interest in the past. If they had been paying taxes on dividends and interest, they would have known it was not a new tax, but was merely a better method of collecting an existing tax.

Incidentally, it would merely use the same method which has been applied for 20 years to wages and salaries. We have had a withholding tax on wages and salaries ever since 1942. When that was put into effect, there was a "hullabaloo" about it. It was said to be unfair. It was said to be administratively impossible to operate. But it was put into effect, nevertheless. We have operated under that law for 20 years. The percentage of evasion of the tax, as I shall show, is very slight, only about 3 percent. There are very few complaints about it. Refunds which are made are made quickly with a minimum of administrative trouble.

I personally thought that the fairness of applying the same methods to dividends and interest which we apply to wages and salaries would so commend itself to the Nation, to the Senate, and to the Finance Committee that there would be no question about its adoption. But, no, it was eliminated from the bill by the Finance Committee by an overwhelming vote. It will be very interesting to see if those who claim to speak in the name of the administration now propose its formal elimination by action of the Senate itself.

NOT A TAX ON CAPITAL BUT ON INCOME

A great many of the correspondents also charged that the withholding method was a tax on capital; that if a man had \$1,000 invested in a building and loan association, the basic tax of 20 percent would be paid on the \$1,000, and that he would have to pay \$200. This, of course, is a ludicrous misunderstanding. The tax is upon income, and not upon capital. If we assume a 4-percent return, the income from \$1,000 of capital investment would be \$40, and the 20-percent tax would be one-fifth of that \$40, or \$8. But a very large proportion of the correspondents thought the tax would be \$200.

As we shall see, the administrative difficulties were grossly exaggerated.

BILL FURTHER EMASCULATED

That I think, was the greatest sin which the Finance Committee committed, but the committee committed other legislative sins as well, and they will have to stand up before the bar of the judgment of the Senate and of public opinion and justify these other legislative crimes which they committed.

For example, under heavy battering from American corporations doing business abroad, the proposed levies based on the earnings of their foreign subsidiaries were progressively softened, although there were some not satisfied even with that, who proposed to eliminate even the emasculated version still remaining.

I may say, also, as a further example, the administration originally proposed that the present provisions as interpreted by the Supreme Court in the case of *Cammarano et al.* against United States as respects lobbying, should be continued. The House weakened these provisions. The Senate Finance Committee went them one better. So, as a result, there has been recommended a great weakening of the lobbying tax deduction provisions, which would play directly into the hands of big business and result in the ordinary taxpayer financing a large portion of the lobbying activities of the big corporations of the country.

Indeed, the savings and loan campaign against the withholding provision would, under the terms of the lobbying proposal, be largely financed by the American taxpayers.

There was also a weakening of the expense account provisions. In the original form, the expense account provisions were quite good. Those were weakened in the House. They were still further weakened by the Senate committee.

I will defy even the most careful lexicographer, or dictionary expert, to tell what the committee means by the expense account provisions it recommends. It is a formula for confusion. Once I nearly said "for deception," but I thought better of that. I will say it is a formula for confusion.

Mr. PROXMIRE. Mr. President, will the Senator yield in respect to the lobbying provision?

Mr. DOUGLAS. Yes; I am glad to yield.

Mr. PROXMIRE. Is it true that the bill, as it came to the Senate from the committee, would provide that businesses could subtract, as an expense of doing business, the cost of lobbying Members of Congress, members of State legislatures, and members of city councils?

LOBBYING EXPENSES TAX DEDUCTIBLE

Mr. DOUGLAS. That is correct. And they could also get others to lobby them directly and make that tax free.

Mr. PROXMIRE. Suppose there were a situation in which a proposed gambling law was before the Congress, or before a city council, and suppose this proposed law would make it easier for the gambling syndicate to operate, in that it would increase profits. It would be possible, then, for them to subtract that item as an expense of doing business. How about the opposition?

Mr. DOUGLAS. The Senator has mentioned a very important point. Under the bill those who have a direct and appreciable business interest in the decision of a legislative body can lobby that body, have their expenses deducted, and under the Senate amendment they could organize campaigns among their stockholders and members. All of that kind of activity would be a business expense.

But if a member of a church who objected to the gambling provision of a law, feeling that it went against public morals, lobbied against that provision, he would not have the benefit of such a tax

deduction, because it could not be said that he had a direct business interest. In other words, the general interest of the citizen and taxpayer, and the general and diffused interest of the consumer would have no deduction supplied to them when lobbying is engaged in in their behalf.

Mr. PROXMIRE. Would the expenses of the League of Women Voters, which certainly is divorced from any pecuniary or financial interest, and whose position on issues is based upon very careful study, analysis, and understanding of what would best serve the public interest, be deductible in any way?

Mr. DOUGLAS. They would not. As I understand, contributions to the League of Women Voters are not tax exempt now. The lobbyist appearing to give testimony in support of the program of the League of Women Voters could not deduct his expenses.

Mr. PROXMIRE. On the basis of the Senator's experience in both the city council of Chicago and in the Senate, and also his broad knowledge of Government in our country, does the Senator feel that the special financial interests are being so consistently defeated by the advocates of the public interest and are suffering so because of the great power of the League of Women Voters, the Civil Liberties Union, and the other pro bono publico groups, that they need that kind of protection in order to provide for their opportunity to defend themselves?

Mr. DOUGLAS. Of course not. One of the gravest weaknesses in modern democracy is the fact that the so-called special and concentrated private interests, in the form of the producing groups, are powerfully organized and can bring to bear great pressures on legislative bodies, whereas the diffused general interest of consumers and small taxpayers is relatively little represented. The obstacles are great to start with because any particular act or bill does not mean to the individual consumer or taxpayer.

GAS BILL GOOD EXAMPLE

Let us consider the gas bill which Senator KERR sponsored. To the gas and oil industry that bill meant \$600 million a year. But to the 30 million householders who use gas to cook and heat it meant on the average only \$20 a year. Very few people will become sufficiently interested in the subject, study it, and then be able to afford to come to Washington to lobby against it when only \$20 a year for each is involved. As a result, the powerful interests of the producing groups are strong and vigorous. The diffused general interest groups are weak.

I sometimes think an analogy is what happened to the Incas of Peru and the Indians of Mexico. The Aztecs and the other Indian tribes outnumbered Cortez and his men 1,000 to 1. But the Indians were divided. They were relatively uninterested. Cortez had firearms, armor, and horses. He overthrew an empire.

The same thing happened in Peru. Time after time in our city councils, State legislatures, and the Congress of the United States, the same thing tends to happen.

There is already a great disparity in strength. The protective devices which

James Madison thought were embodied in the Constitution of the United States, and which he developed in the 10th paper of the *Federalist*, and with respect to which he relied upon conflicting economic interests to offset each other—are what Mr. Galbraith calls the theory of "countervailing power"—no longer operate very fully because we are now getting cross lobbying for example on the part of the National Association of Manufacturers, the American Farm Bureau, and the American Medical Association. All those great groups support each other. The result is a terrific combination against which it is very difficult to stand up and fight successfully.

The lobbying provision in the tax bill would still further intensify that imbalance. I think that is the word. It would make possible a deduction from the tax bills of the wealthy for lobbying expenses, which would be paid for by Uncle Sam, while the weak, general consumer or small taxpayer would have no protection.

In my opinion, the lobbying provision started by the House and completed by the Finance Committee is one of the most inequitable in the bill. The provision appears early in the bill. There will be a yea-and-nay vote on it when the Senator from Oklahoma proposes, as I suppose he will propose, that it be included. We shall then see who is for the big vested interests, the special interests, and selfish interests, and who is for the people.

Mr. PROXMIRE. Is it the conclusion of the Senator from Illinois that at present a most serious weakness in American democracy is the pressure of organized financial interests that use the organized pressure to get special interest legislation at the expense of the public interest?

Mr. DOUGLAS. The Senator is completely correct.

Mr. PROXMIRE. The proposal would aggravate that situation.

Mr. DOUGLAS. That is correct.

Mr. PROXMIRE. Is it not true that the section of the bill about which we are speaking has never been recommended by the Kennedy administration or by the Department of the Treasury?

Mr. DOUGLAS. It has been opposed by the Treasury Department.

Mr. PROXMIRE. They have opposed it. They do not want it. They think it is wrong.

Mr. DOUGLAS. The proposal has been opposed by the administration. In the *Cammarano* case the Supreme Court in a unanimous opinion handed down by Justice Harlan, with no dissenting opinion that I can find, held that the tax system should be neutral so far as lobbying is concerned. The Court held that tax credits should not be given either to those who had a direct business interest or to those who oppose the direct business interest and fight for the general interest. It is the *Cammarano* verdict which the Senate Finance Committee, and to some degree that House Ways and Means Committee, are now seeking to reverse.

Mr. PROXMIRE. In the interest of our friends across the aisle, is it not

true that the Eisenhower administration also opposed that particular provision?

Mr. DOUGLAS. I think that is true.

Mr. PROXMIRE. That is the understanding of the Senator from Wisconsin. Is it not also true that one of the reasons that provision got through the House of Representatives was that it was a new section of the bill on which the House Ways and Means Committee held no hearings. With the kind of closed rule the House had on the bill, there seems to have been a violation of the rules, and if there had been an objection, it would have been possible to block consideration of the tax bill on that basis.

Mr. DOUGLAS. That is my understanding of the parliamentary procedure. There was no testimony on this provision. The House Ways and Means Committee, as I understand, inserted it at the last minute. They asked for a closed rule, which meant that the only motion that could be made, except on final passage, was a motion to recommit, which means that it is necessary to take the bill as a whole or defeat the bill. I am very frank to say that I believe the bill would have been defeated in the House had not some of us gone to certain Members who wanted to oppose the bill in the House and said to them, "We hope you do not defeat the bill in the House. Let it come to the Senate. We hope that we can take this and other features out of the bill on the floor of the Senate." That was not trying to obstruct the bill, as certain writers charge, but trying to help the bill become law.

Mr. PROXMIRE. Therefore we have a provision in the bill which would serve the interests of special vested financial interests. There is no question that it would weaken the already comparatively feeble strength of those who argue for the public interest. It is opposed by the Kennedy administration, and was opposed by the Eisenhower administration, and only got in this bill because of a parliamentary evasion.

Mr. DOUGLAS. That is correct.

Mr. PROXMIRE. I thank the Senator.

THE DEDUCTION FOR CERTAIN LOBBYING EXPENSES OF TAXPAYERS WITH BUSINESS INCOME

Mr. DOUGLAS. Mr. President, section 3 would permit the deduction of certain lobbying expenses by taxpayers with business income. This would depart from a salutary principle which has been part of the income tax law since World War I. It would provide unwarranted tax reduction where it is least needed for reasons which are specious. It would introduce novel distinctions into the tax law, producing new requirements difficult for the Internal Revenue Service to administer. The specific language in which the deduction is cast contains ambiguities which will create continuing uncertainty as to its exact meaning, and, most important, the relationship of this provision to the whole process by which our citizens seek to influence the enactment of legislation at all levels of government was not adequately considered. Section 3 should be deleted from the bill.

Under existing law the costs of efforts to influence legislation are not deductible, a rule applicable to all taxpayers. Whatever the motive for a citizen's efforts to influence legislation, he now bears the whole cost of that effort himself. No part of the expense can be passed on to the Federal Government through an income tax deduction. In the constant competition for legislative favor and results at National, State, and local levels, the Federal Treasury stands neutral—and properly so.

Section 3 would change all that. It would amend section 162 of the Internal Revenue Code of 1954, the section creating the general authority for deduction of the ordinary and necessary expenses of business operation. Section 3 would add a new subsection specifically authorizing deduction of lobbying expenses in certain categories by taxpayers with business income. Only those taxpayers with business income would receive any benefit. All others would still be subject to the existing rule of no tax benefits for lobbying, a result which follows necessarily from incorporation of the amendment in section 162 and one which is specifically spelled out by the House committee report.

SPECIFIC EXAMPLES

Some specific typical examples will bring this into sharper focus. Suppose a measure is being considered, as many have been, involving a proposed change in the standards or testing procedures for food, drugs, or cosmetics. The costs of presenting the views of drug manufacturers and distributors would be deductible. The cost of presentations on behalf of consumers or of disinterested professional or technical advisers would not be. Or suppose that a State legislature is debating a measure designed to decrease stream pollution. Manufacturers who would be adversely affected by its enactment could deduct the cost of opposition. Members of the public interested in pure water for drinking or for recreational uses would have to finance their support of the measure entirely from their own pockets. Or, at the local level, a business owner of a piece of real estate could seek advantageous amendment of the local zoning ordinance deducting the cost of his presentation before the local city council. The owners of nearby residences would not receive this help from the Federal Treasury in preparing the exhibits and briefs necessary for effective opposition.

These are discriminations impossible to justify. Can anyone seriously contend that consideration of legislative proposals affecting business taxpayers is seriously handicapped by absence or weakness of expression of business viewpoints? Is there any evidence that business taxpayers, individually or collectively, are now deterred from expressing themselves on these subjects by the present rule of tax neutrality which permits no deduction for lobbying expenses? To ask these questions is to answer them. Of all viewpoints on legislative proposals, those of business are consistently the most ably represented before the Congress and before State and local legislative bodies. Why then should the cost

of lobbying activities of taxpayers with business income be singled out for this preferential tax reduction? No adequate reason has been given.

Any discrimination at all among citizens in the exercise of their constitutional right to petition their representatives is patently undesirable. Discrimination by preferential tax deduction is magnified as the amounts spent for these purposes increase. Modern efforts to influence legislation cover a wide range of techniques, some of which are very costly. One can send a letter to his Senator for 4 cents. However, to stimulate tens of thousands to do so requires the expenditure of large amounts running sometimes into the hundreds of thousands, even millions, of dollars. But all this is well known. It has been thoroughly documented many times.

LARGE SUMS INVOLVED

The application of section 3 would not be confined to nominal amounts. It would permit the deduction of some very large sums. In addition to provision for deduction of the costs involved in direct contacts with legislators (personal calls and visits, appearances before committees or statements filed with them), the cost of efforts to influence legislation indirectly are also made deductible in some instances. The costs of communications to organization members and to shareholders and employees have all been blanketed in.

When section 3 is applied to today's scene, we find that it will authorize giant corporations to deduct the cost of communicating the views of management officials to hundreds of thousands, even millions, of shareholders and employees, for the purpose of influencing them with respect to current controversial legislative proposals. To use a painfully familiar example, section 3 would authorize deduction of the cost of campaigns designed to produce a flood of letters opposing withholding on dividend income.

Under existing law these sums are not properly deductible—and never have been. To permit deduction now would shift a very large proportion of these heavy costs to the Federal Treasury, a disguised subsidy for which there would be no justification.

The effects of such subsidized efforts to influence legislation indirectly would not be confined to the recipient members, shareholders, and employees. The views expressed and their source would frequently come to the attention of families and friends of the recipients, thereby broadening the scope of the influence subsidized by the Federal Treasury. Of course, the benefits of section 3 as they would apply to these broadcast efforts to influence legislation can only benefit very large organizations. Small business taxpayers, as well as nonbusiness taxpayers, would have little or no use for it and could well suffer from its use where their interests on legislative matters are opposed to those who could take advantage of it.

LIMITATIONS ILLUSORY

True, not all lobbying costs of business taxpayers would be made deductible by section 3. The bill purports to create

limitations which will restrict the kind of expenses for which a deduction can be claimed. Thus, to qualify for the deduction, the legislative proposal must be of "direct interest" to the taxpayer. In addition, specific provisions deny deductions for political campaign expenses or for efforts "to influence the general public, or segments thereof." However, a close inspection raises genuine doubt as to the precise meaning and application of these restrictions. They may, in fact, prove largely illusory.

Thus, one might ask, What subjects are not of "direct interest" to a large corporation? Any measure involving a tax or a change in the regulation of business or the marketing of securities or foreign trade or the terms of employment or labor relations or the monetary system will have some impact on every substantial business enterprise. Is it intended that the cost of testimony or statements or communications to shareholders or employees on this entire range of subjects is to be deductible? Similarly, can the prohibition against deductions for political campaign purposes be really effective? Granted that the cost of a folder urging shareholders to vote for Jim Darkwater will not be deductible, what of the cost of a folder urging a position on the principal issue dividing Darkwater from his opponent Bob Cleanriver? Can issues and the candidates be separated so easily? It is doubtful. Section 3 thus could make slightly veiled political contributions deductible. The benefit would not be universal though. To return for a moment to the anti-water-pollution measure used as an example before, suppose Darkwater is against it and Cleanriver is for it. The former's supporters could deduct the cost of their literature discussing the anti-pollution measure (and thus their support of Darkwater; supporters of Clean-

Obviously, congressional memories are very short. For at least a century Senators and Representatives have regularly inveighed, individually and collectively, against lobbyists and their activities. The need for substantial disclosure by lobbyists, particularly in financial respects, has long been recognized. When a person or organization becomes a lobbyist, he is required to register as such and thereafter to report quarterly his expenditures for these purposes. In spite of these safeguards, every few years some lobbyists become so bold and their overreaching so bad that a special inquiry is required. A prime example was the creation in the 84th Congress of the Senate Special Committee To Investigate Political Activities, Lobbying, and Campaign Contributions. Its report states graphically the kinds of abuses which occur and the large sums of money available to be spent on efforts to influence legislation. Sugar quota bills attract lobbyists like flies and, like flies, their activities are not widely admired. The Senate Foreign Relations Committee is currently beginning an investigation of another group of lobbyists, an inquiry which has grown in large part out of concern for their lucrative finan-

cial arrangements. Nor are problems with lobbyists confined to Washington. Their influence on State legislators and their sometimes questionable methods in State capitols is notorious.

CYNICAL PROVISION

When projected against all this experience, section 3's proposed financial bonanza for one group of lobbyists and their employers seems ironic in the extreme, if not downright cynical.

There is no challenge here to lobbying per se. It is unquestionably legitimate. A constitutionally protected right of our citizens, it often supplies useful information and reactions on pending legislation. However, it would be foolish to exalt it unduly for these reasons. At best, lobbying is a mixed blessing for it is almost always exclusively concerned with self-interest rather than the broad public interest. Fortunately, section 3 presents only a narrow problem, viz, whether or not the lobbying done by one segment of our society—taxpayers with business income—should be entitled to support from the Federal Treasury.

A number of arguments are made in favor of this measure. Some of them have a surface plausibility, but on close analysis none of them holds water. The issue is actually a simple one. We begin with a longstanding rule that all taxpayers, business and nonbusiness, who seek to influence the work of legislative bodies, National, State, or local, pay their own expenses in full without assistance from the Federal tax system. This neutral posture of the tax law is a healthy one and should be defended and strengthened. Legislation affects all our citizens. It is entirely suitable that all who seek to influence that legislation, directly or indirectly, should be treated alike. The expenses of all should be on the same footing as far as the Treasury of the United States is concerned. The only issue here is whether or not to depart from this principle of neutrality and equality. Plainly, the case for such a change has not been and cannot be proved.

Mr. PROXMIRE. Mr. President, will the Senator yield for one more observation?

Mr. DOUGLAS. Certainly.

Mr. PROXMIRE. On page 23 of the committee report the following language occurs:

Your committee's amendment provides, in addition to the categories specified in the House bill, for the deduction of expenses incurred by a taxpayer in carrying on a trade or business if the expenses are in direct connection with the communication of information between the taxpayer and employees or stockholders with respect to legislation, or proposed legislation, of direct interest to the taxpayer.

In other words, the Finance Committee, in addition to all other things, has provided that a corporation can lobby its employees and stockholders in its interest, and therefore considerably aggravates and increases the power of a special interest to get the kind of legislation it wants to achieve.

Mr. DOUGLAS. Yes. For example we know that the pressure against the

withholding feature of this bill was carried out by building and loan associations, and if the lobbying provisions were now law they could have made Uncle Sam pay 52 percent of the cost of lobbying against the bill—52 percent of the cost which they had in circularizing their members, depositors, copartners, or what have you.

Similarly in the Du Pont bill, which the Senator from Tennessee and I opposed at the opening of this session, if the lobbying provisions were in effect the Du Pont Co. could get a refund of expenses incurred in circularizing their stockholders and their employees, in making ex parte statements to them, and in getting them, in turn, to write to the legislators.

There are tremendous possibilities of evil and excessive pressure which these two measures open up; namely, the House amendment permitting the underwriting of direct lobbying, not only by officers, but also of others, of legislative bodies; and the Senate Finance Committee amendment permitting circularization of stockholders and members and depositors, and the like.

Mr. GORE. Mr. President, will the Senator yield?

Mr. DOUGLAS. Yes, I am glad to yield.

Mr. GORE. Does not it go much further, in fact, than the Senator has described? Does not it include research and travel expense items and contacts—whatever that means—not only of congressional committees and Members of Congress, but also of State legislatures, municipal councils, and county governments; indeed, does not this provide for a tax deduction of nationwide lobbying organizations on a permanent basis, from the local level to the national level?

Mr. DOUGLAS. The Senator is correct. Not only does it help finance lobbying and circularization, but, also as he says, the staff work which lies behind it, such as research and legal services and public relations works.

Mr. GORE. And retainer fees.

Mr. DOUGLAS. Yes.

Mr. GORE. Public relations fees.

Mr. DOUGLAS. Yes.

Mr. GORE. Lawyers' fees, accountants' fees, statisticians' fees.

Mr. DOUGLAS. And fees of Washington representatives.

Mr. GORE. Oh, yes.

Mr. DOUGLAS. And of representatives in Springfield and Madison and Albany and Nashville. Also the context with which all of this takes place.

Mr. GORE. With which they succeeding in the Du Pont bill and in the withholding provision of the pending bill in thoroughly misleading the American people.

Mr. DOUGLAS. That is correct.

Mr. GORE. Will the Senator yield for one further question?

Mr. DOUGLAS. Yes; gladly.

Mr. GORE. Is it the Senator's purpose, first, to oppose the adoption of the amendment approved by the Senate Committee on Finance, which makes it worse—

Mr. DOUGLAS. I hope that if the leadership is not able to get it through and if we defeat it, we will then move to strike out the House provision.

EXPENSE ACCOUNT PROVISIONS

The second way in which this bill was gutted was in the matters dealing with expense accounts and entertainment.

THE PROBLEM

That is one of the grossest abuses in American business—the yachts, the hunting lodges, the dinners at the 21 Club, the \$65 tickets to "My Fair Lady," the champagne suppers, the elaborate gifts for which Uncle Sam is the unseen host, picking up to 52 percent of the check, but never getting any credit for being the host.

President Kennedy described this tax giveaway of the deductible expense account as a matter of national concern. He proposed a very liberal limitation. He proposed, for instance, that one could take people out to lunch provided one did not pay more than \$5 or \$7 for the lunch. He would have allowed \$10 for a dinner, which would seem to be enough for anyone except Diamond Jim Brady. He proposed that when individuals traveled they get twice the allowance that a government civil servant is allowed, which is now \$15 a day; he would allow them \$30. On the whole it was a very liberal proposal.

The House took out this restriction and wrote in some language which, so far as the bill is concerned, is rather elliptical, but which is defined in the report, which is said to have the binding force of legislation.

Mr. GORE. Mr. President, will the Senator yield?

Mr. DOUGLAS. I yield.

Mr. GORE. With respect to the President's recommendation of a limit of \$30 per day for expenses while in traveling status, perhaps the Senator would be interested to know that the junior Senator from Tennessee last week accepted an assignment to be one of the U.S. delegates to the United Nations General Assembly, which begins about the 18th of September and runs until some time near Christmas. Upon accepting the assignment the junior Senator from Tennessee, being a prudent man, reasonably, inquired what provision existed for the defrayment of expenses. The junior Senator from Tennessee was advised that he would be provided with a hotel room and \$9 per diem.

Mr. DOUGLAS. And that was to pay for three meals plus taxi fares, plus tips. Is that correct?

Mr. GORE. Whatever else went along.

Mr. DOUGLAS. The Senator from Tennessee is a frugal man; there would not be very much else that would go along.

Mr. GORE. Not on \$9.

Mr. DOUGLAS. But the President is willing to let the business groups have \$30 a day. The House, after careful consideration—I should not say "careful," but rather after long consideration—adopted a provision which, although falling short of the President's recommendations, would go a long way toward a fairer set of rules. It would

permit deduction for entertainment more closely related to the conduct of business but would cut out deductions for many of the highly personal expenditures permitted under present law when the taxpayer can make a showing of some connection between the entertainment and the taxpayer's trade or business.

The allowance of deductions for such essentially personal entertainment has brought the integrity of the entire revenue system into disrepute. The expense account deduction has been a breeding ground for fraud and misrepresentation. It has encouraged disrespect for honest self-compliance with the tax laws among those not in a position to claim such deductions, but who have watched other satisfy their personal amusement tastes at the taxpayers' expense.

What has the Committee on Finance done with the House bill? It has simply pulled the teeth from the proposal, leaving it merely with a dangling tongue—a tongue which is certain to confuse taxpayer and Government official alike as to what it is trying to say. Certainly the vague and almost meaningless standard adopted by the committee will do very little, if anything, to change the style of operation of those who have been living high on their expense accounts at the cost of their fellow citizens.

Mr. GORE. Mr. President, will the Senator from Illinois yield?

Mr. DOUGLAS. I yield.

Mr. GORE. If the Senator will refer to the bill, I shall call his attention to the first amendment which, under the rules of the Senate, will be considered, the item involving expense account abuses. The amendment appears on page 41. Three seemingly innocent little words have been added on page 41, and the same three seemingly innocent little words have been added twice on page 42. Does the Senator find the Senate amendment?

Mr. DOUGLAS. I do.

Mr. GORE. The Senator will notice the words which the Committee on Finance approved as an amendment:

That amendment appears on line 18, page 41.

Mr. DOUGLAS. Yes. The expense must not only be "directly related to the active conduct of the taxpayer's trade or business," as provided in the House language, but also may be only "associated with" the conduct of the business.

Mr. GORE. Mr. President, will the Senator further yield?

Mr. DOUGLAS. I yield.

Mr. GORE. Will not Senators who wish to understand the legal meaning of the words "or associated with" find it necessary to turn to the majority report?

Mr. DOUGLAS. Absolutely. What do we find there?

Mr. GORE. I was about to ask the Senator from Illinois.

FORMULA FOR CONFUSION

Mr. DOUGLAS. We find a formula for confusion. To the degree that it is restrictive, it outlaws things that are already outlawed, but does not outlaw anything that is not now outlawed. In my judgment, you can still have expensive

dinner at the 21 Club or Antoine's; for which the taxpayers will pay 52 percent; you can still have the \$45 dinner and the \$20 lunch; you can still have football tickets for the Rose Bowl or the other bowls; you can have prize fight tickets; you can have tickets to the Kentucky Derby and other races. And Uncle Sam will help foot the bill.

Mr. GORE. The Senator does not mean me, does he?

Mr. DOUGLAS. No, no, no; I refer to those who go in on the expense accounts. I used the word "you" in a plural sense. It was not the equivalent of the German "sie" or the French "vous."

Mr. GORE. Is it not, in fact, very difficult to find any item of personal expense disallowed by the amendment which is deductible under present law?

Mr. DOUGLAS. Personal expense. That's correct.

Mr. GORE. Personal expense deductible under the present law, which would not be deductible under the terms of the majority report as it interprets the words "or associated with"?

Mr. DOUGLAS. I think it outlaws what is already outlawed. It takes a highly virtuous stand against call girls. I do not know whether they are outlawed, but deductions for their employment are outlawed. That is specific. I am not certain that that practice has always been followed in the past; but I wish to pay a compliment to the Senator from Oklahoma and the majority report for this highly virtuous affirmation.

Mr. GORE. Expenses for call girls, if any businessmen have indulged in such on expense accounts, are not deductible under present law, though.

Mr. DOUGLAS. No; they certainly are not. It is possible that at times they have been covered up in general expense items.

Mr. GORE. Why was this strawwoman set up in the majority report?

Mr. DOUGLAS. To give a similitude of virtue which did not exist.

Mr. GORE. If the Senate wishes to come to grips with this problem, when the committee amendment is called up to add the words "or associated with," on page 41, the Senate will want to vote against the adoption of those words.

Mr. DOUGLAS. That is correct. I hope the Senator from Tennessee will blast that amendment from Cape Hatteras to Lubeck, Maine.

TAX DEDUCTIONS FOR PERSONAL EXPENSES

The basic problem is whether this country can continue to afford to permit a small group of taxpayers to take tax deductions for highly personal items such as nightclub hopping, fancy yachts, and swanky country clubs while the great majority of their fellow taxpayers cannot take such deductions. From a practical point of view the concern of the Nation is not only the basic unfairness of this situation—in itself a vital consideration—but it is also the effect that this legally created unfairness has upon those who are discriminated against. It makes them resentful of the law which permits such a situation to exist and encourages them toward laxness in discharging their full tax obligations.

It is quite natural for a customer's wife to feel, "Why should I help keep that fellow on the gravy train—paying for his fancy yacht and swanky country club?" An expansion of this type of thinking could eventually destroy our tax system, the keystone of which is its voluntary character. We rely on each taxpayer to be his own tax assessor. The essential honesty of our citizens and, most important in this context, their respect for our tax laws, has enabled this system of voluntary self-assessment to function most effectively. However, like all good things, the system must be nurtured and protected.

Expense account abuses have become a real threat to the continued effectiveness of our self-assessing system. Much taxpayer distaste has already been voiced against this unwarranted privilege. The danger signals are loud and clear. In his testimony before the House Ways and Means Committee and the Senate Finance Committee, the Secretary of the Treasury documented the situation in great detail with numerous case studies and many samples of editorial comment from all over the country.

Mr. President, I ask unanimous consent to have printed at the conclusion of my statement the Secretary's exhibit which includes a list of some of the deductions claimed and largely received for entertainment and related expenses.

The PRESIDING OFFICER. Without objection, it is so ordered.

(See exhibit 5.)

Mr. DOUGLAS. Mr. President, let us examine a few of these.

A corporation engaged in manufacturing was allowed to deduct \$991,665 in 1959 for yachts, club dues, shipboard conventions, hunting and fishing trips, and parties.

A taxpayer engaged in the insurance business was allowed to deduct \$97,500 for meals, lodging, transportation, entertainment, tickets, books, gifts, et cetera. The amount covered entertainment at vacation resorts, \$6,000 for an apartment, and over \$30,000 for food, beverage, and other entertainment.

A manufacturer was allowed to deduct over \$34,000 spent on liquor, football tickets, parties, and a speedboat. The expenses for liquor totaled \$13,750.

A family-held ship repair corporation was allowed to deduct \$23,758 for a Christmas dinner and party. Uncle Sam paid half the cost of that Christmas party.

An enterprising banker effectively combined sentiment with business when he deducted, as present law permitted, a substantial part of the cost of his debutante daughter's coming-out party on the ground that some of the guests had business connections with him.

In another case, the taxpayer was allowed \$115,000 for entertainment and gifts. His expenses included \$7,500 spent at a resort hotel; \$5,400 for food, liquor, and cigars for his office and farm; and \$8,700 in cash to officers of his closely held corporation for entertainment.

A beverage manufacturer claimed and was allowed \$10,903 for entertaining customers at the Kentucky Derby.

Huge sums are allowed to business taxpayers in connection with maintenance and operation of yachts and other fancy boats. One manufacturer was allowed to deduct \$253,000 for the expense of his yacht. Another was permitted to deduct \$112,000 for such expenses—as well as an additional amount of \$362,000 for a ranch-hunting lodge, nightclub, and other similar expenses. A company in the business of selling fuel was allowed \$93,000 as deductions for a yacht, a fuel products company was allowed \$23,000 and an auto dealer was allowed yacht expenses of \$22,000.

A cake and cookie bakery was allowed \$66,000 for a yacht on which to entertain supermarket and chainstore buyers and branch managers. Despite its rather sad undercurrents, both from the viewpoint of the tax system as well as otherwise, one of the most interesting cases is that in which a mortuary business—vulgarly known as an undertaking establishment—was allowed \$26,495 for yacht expenses in entertaining visiting morticians, clergymen, and for meetings of employees. In other words, the persons running the mortuary business were in the business of shipping bodies; and they wanted to maintain friendly relationships with the recipients of the bodies, and also wished to maintain friendly relationships with the clergymen, so they could get business from them, and also with the other prospective customers of their mortuary business. One can imagine the ghoulish feeling when a prospective customer was invited on board the mortician's yacht. The expense in that connection was a perfectly legitimate business-deductible expense, according to our tax laws—and allowed by the tax laws, so the mortician could build up good will, so that those he entertained would in gratitude let that mortician bury them.

OTHER CASES

These cases could be multiplied by the thousands. Similar large expenditures are constantly being made on hunting and fishing lodges, on elaborate beach resort homes, on exotic island retreats, on extended hunting trips, including plush safaris to far off Africa and India. The first case cited was that of a dairyman who took his family with him so on elaborate safari to Africa, where he had movies taken of the trip. Thereafter, the entire expense of the safari was allowed to be charged or deducted as a business expense, on the theory that the showing of the movies he took on the trip would enable him to sell more milk.

Indeed, just about every kind of human activity in the nature of fun and frolic is being well subsidized on behalf of a privileged few by the average taxpayer who does not happen to be engaged in a trade or business so as to enable him to join in this Government-supported high life. Is it any wonder, then, that such strong taxpayer resentment has developed against the expense account privilege. Clarence Randall, former chairman of the board of one of America's largest steel companies, the Inland Steel Co., has vividly expressed this taxpayer resentment. Let me say

that I suppose he is one of the most conservative men in America. He was chosen by the steel industry to oppose the action taken by President Truman against that industry; and I am sure that all of us remember the vitriolic denunciation Mr. Randall applied to President Truman. I think it can certainly be said that Mr. Randall is a dues-paying, card-carrying, conservative Republican. But what does he say? I think his article appeared in the *Atlantic Monthly*; and in it he is quoted as saying:

Gone are the days when a salesman occasionally wined and dined his favorite customer, or perhaps gave a small theater party. Nowaday, when the deal gets big enough, the company yacht weighs anchor and moves into position, the company plane takes off for a duckblind in Arkansas, or the best hotel in Miami throws open its door to expectant dealers for a week of continuous circus.

The distaff side is cut in, too, on both sides of the deal. How the ladies love it. With jet travel what it is, those who were getting a little tired of White Sulphur may now hope to look in on Capri or the Riviera.

The unseen partner in all this largesse, of course, the man who rides the afterdeck of the company yacht, copilots the duck hunter's plane, sits by while the caviar is spooned out and the crepes suzettes are sizzling, the man who splits the check at the nightspot and hands the big bill to the headwaiter, is none other than Uncle Sam.

But who are the silent underwriters of this frenetic spending? You and I, the general taxpayers. It is we who make up to the U.S. Treasury the revenue lost through expense-account deductions.

Mr. President, an important point to be derived from the foregoing is that all of the expenditures described were deductible under the broad standard of present law which permits the deduction of "all the ordinary and necessary business expenses" of the taxpayer. The fact that there is a business relationship, actual or even only hoped for, between the parties does not prevent them from enjoying the fancy resort living, the cruise on the expensive yacht, or the fancy nightclub. The law does not deny to clergymen and those who will shortly shuffle off this mortal coil the pleasure of being entertained on board the undertaker's yacht at Fort Lauderdale.

ROUND ROBIN RECIPROCITY

Mr. President, suppose company A sells its product to company B. If a sales executive of company A invites his close friend, an executive of company B, to join him for a cruise on his yacht, who can say that the executive of A did not intend to promote the business relationship between the two companies? The fact is that in the usual case the businessman's friends are his business customers or prospects. Under the test of present law, so long as this business connection exists between entertainer and entertained, the parties can enjoy tax deductible vacations in Bermuda, cruises on yachts, and evenings in luxury nightclubs on a tax deductible basis. This can be done on a reciprocal arrangement of "you entertain me and I'll entertain you," with the Treasury paying half the bill for each. In fact, the

Treasury discovered that one club to which businessmen belonged required, as a qualification of membership, that each member give a party, once a year, to all the others, with the result that A would give a party for B, C, D, E, F, G, H, I, J, K, L, M, N—and all the way down to Z; and then B would take up the party-giving burden and would similarly entertain all the other members of the club; and subsequently C and D and all the others would do likewise; and eventually all of them would receive tax deductions. In short, they would have a continuous round of hilarious high living, with Uncle Sam, the unseen host, picking up half the checks.

Business does not have to be discussed nor need the entertainment follow or precede business discussion. The taxpayer need not even be present at the entertainment. Because of absence of restrictions, taxpayers are encouraged to ask, Why should not I deduct my personal pleasures and entertainment, if everyone else can? Because of this, the expense account problem has grown to its present unmanageable proportions.

HOUSE SOLUTION TO THE PROBLEM

The test adopted by the House of Representatives is that the expense of an entertainment activity will not be deductible unless "directly related to the active conduct of the taxpayer's trade or business." Where an expense connected with a facility such as a yacht or a hunting lodge is involved, the taxpayer must also show that the facility "was used primarily for the furtherance of the taxpayer's trade or business." On its face, this standard seems almost as broad as present law and would appear to present many of the same problems.

However, in its report the House Ways and Means Committee has explained its test in a way which provides a number of tangible, practical, and meaningful guidelines: The report states that under its test the taxpayer—

Will have to show more than a general expectation of deriving some income at some indefinite future time from the making of the entertainment-type expenditure; however, he will not be required to show that income actually resulted from each and every expenditure for which a deduction is claimed.

If the expenditure is for entertainment which occurs under circumstances where there is little or no possibility of conducting business affairs or carrying on negotiations or discussions relating thereto, the expenditure will generally be considered not to have been directly related to the active conduct of business. Thus, the absence of the taxpayer or his representative from the entertainment activity ordinarily indicates that the entertainment was not directly related to the conduct of the taxpayer's trade or business. Similarly, if the group of persons entertained is large or the distractions substantial, the cost of the entertainment will not be deductible, in the absence of a clear showing of a direct relationship to the active conduct of the trade or business.

This clear statement of legislative intent coupled with the statutory language provides a workable and reasonable solution to the difficult expense account problem and should go a long way toward reducing the abuses outlined above. However, critics of the House

proposal attacked this crucial committee report statement on the ground that it had no support in the statute.

In view of the broad language of the statute, requiring explanatory implementation to make it useful, this contention is baseless. The true reason for the complaint is the fact that the statute as interpreted by the Ways and Means Committee report has some real teeth in it.

Even so, we are not asking that the business community adopt Spartan standards. The House bill, which we hope will be restored, recognized the general custom of business entertaining at meals in restaurants. It specifically permits the deduction of entertainment presently allowable through furnishing food and drink in restaurants and hotels in an atmosphere conducive to business discussion. No business need be discussed. It thus leaves undisturbed the most significant portion of goodwill entertainment conducted in this country. It strikes only at the high, wide, and fancy living and indulgence in personal pleasures which all taxpayers ought to pay for themselves without Government subsidy.

FINANCE COMMITTEE SOLUTION—FORMULA FOR DECEPTION

The only change in the pertinent House statutory language made by the Finance Committee is, as has been stated by the Senator from Tennessee, the addition of the words "or associated with." Thus, a taxpayer can deduct an entertainment expenditure which is only "associated" with the active conduct of his trade or business, as well as one which is directly related thereto. Since this statutory language is quite similar to that of the House bill—equally broad, in any event—one would reasonably expect again to find a helpful explanation as to what the committee intended to accomplish by its additional phrase "or associated with."

Unfortunately, such is not the case. Unlike the clear, concise, and workable guidelines set forth in the House report the Finance Committee report is a mass of vague, disconnected statements and examples which are destined to spawn controversies so numerous and intense as to make the highly unsatisfactory expense account picture of today seem most pleasant. In addition, the Senate report attempts to paint a picture of virtue and righteousness, but even a casual glance beneath the surface reveals that the virtuous exterior is more illusion than reality. For example, the report states:

Nothing in your committee's bill is to be construed as allowing a deduction for any expense which is against public policy or which violates the public conscience. Deducting an expense incurred for such purpose under the guise of generating "business goodwill" will not be condoned and under your committee's amendment is not deductible. Thus, the cost of liquor purchased for the entertainment of customers and the promotion of goodwill (which under existing law has been held deductible) will be disallowed if the serving of liquor violates the public morals of the community as expressed in local law—

Very few local laws forbid the consumption of liquor. I think there are

only two States in the Union where the sale of liquor is forbidden, but I am not sure that its consumption is forbidden in any State.

Another example of expenses for immoral purposes which have been claimed on tax returns under existing law involves expenditures to provide "call girls" for the purpose of entertaining clients. Under your committee's amendment no deduction whatsoever is to be allowed for expenditures of this nature. In no legitimate sense are they "directly related to or associated with the active conduct" of a trade or business.

COMMITTEE ACTION NO MORAL BROOM

The foregoing suggests that the committee's action will serve as a moral broom to disallow expenditures where liquor is illegal under local law, and where "call girls" are utilized as "business" entertainment. However, expenditures such as these, which violate clearly defined lines of public policy, are not deductible under present law. See *Smith*, 33 T.C. 861 (1960); *R. E. L. Finley*, 27 T.C. 406 (1956); *U.S. v. Winters*, 261 F. 2d 675 (1958). What then will be accomplished under the committee's language? Is it not clear that this is simply a smokescreen thrown up to suggest that abuses are being remedied whereas in actuality little, if anything, is being accomplished beyond present law?

The Finance Committee report stresses the desirability and wholesomeness of "goodwill" entertainment. It states:

Goodwill has long been recognized as a legitimate objective of business entertaining and where the purpose of the expense and its clear relation to a business is firmly established, the expense ordinarily will continue to be deductible.

The report further states:

To eliminate the harshness resulting from the House report, amendment of the language of the House bill is necessary. * * * This new language will permit deduction of expenses for entertainment, amusement, or recreation incurred for the creation or maintenance of business goodwill without regard to whether a particular exception applies. However, this new language will apply only if the taxpayer demonstrates a clear business purpose and shows a reasonable expectation of deriving some income or other benefit to his business as a result of the expenditure. If he meets this test, the expenditure will be considered to be associated with the active conduct of his trade or business; otherwise, the expense will be disallowed under your committee's amendment.

GOOD WILL ALLOWED

A close analysis of these statements makes it eminently clear that expenditures for goodwill have been given preferred status. In these references to "good will," the committee has presented our sophisticated expense account society with a blueprint for continued high living at Government expense. These statements are a readymade formula for deception which will leave the Internal Revenue Service with an impossible enforcement task, for, in effect, almost all entertainment expenditures, both for the creation and maintenance of business goodwill are declared to be henceforth deductible. In stating that the taxpayer must demonstrate a clear business purpose and show a reasonable expectation of deriving some income or other benefit to his business from the making of the entertainment expenditure, the commit-

tee report has added nothing to the requirements of present law. The taxpayer must meet precisely the same test today, but, as hundreds of cases illustrate, such vague and generalized requirements present are so easy to meet as to be practically meaningless.

Furthermore, although the committee report makes numerous references to goodwill, it gives no indication as to what is encompassed by this term. Nowhere is good will defined. How does a businessman go about creating good will—whatever good will is? It seems clear that the sky is the limit. If a businessman—in his judgment—thinks a big yacht may be helpful in developing some customers, does not this committee report language put the official congressional stamp of approval on his deduction of these substantial costs of maintaining and operating such a "business" asset? Is not a revenue agent foreclosed from effectively examining into the matter?

In the light of all the foregoing statements respecting good will, very little is salvaged from the following comment—particularly in view of the illustration given as to what is meant by "vague good will."

Where goodwill generated by the expense is vague or where the possibility of the expenditure resulting in the production of income is remote, no deduction will be permitted. For instance, under present law a taxpayer may deduct expenses of entertaining buyers and others associated with his trade or business even though at the time he does the entertaining he already has more business than he can handle. Under your committee's amendment, however, no deduction will be allowed because, with a large backlog of unfilled orders, such entertainment ordinarily cannot be regarded as being associated with efforts to produce income.

This narrow "exception" to the basic theme of the Finance Committee report that all good-will entertainment is deductible is scant evidence of tightening up present law. Rare indeed is the case where the taxpayer has such a backlog of unfilled orders that his entertainment activities cannot be regarded as being associated with efforts to produce income. It is interesting to note that even in such an extreme case the report hedges the consequences by providing that "ordinarily" the deduction will not be allowed. Moreover, there is a good possibility that entertainment expenditures in such a unique case are not deductible under present law because they are in the nature of capital expenditures. Cf. *James Schulz* (16 T.C. 901). Here again the committee has done nothing more than set up a strawman—to give the illusion that a cutback on existing law is being effected. In reality nothing has been accomplished—except that perhaps another arena for conflict has been created.

The harshness of which the report speaks is that the House provision, as explained by the Ways and Means Committee's report, has some effect and will disallow some entertainment expenditures which are deductible under present law. Presumably that is the purpose of this legislation. However, one must struggle hard to tell which of the above-described cases would be denied deduc-

tion under the Finance Committee report. How much, if anything, would be disallowed to the corporation which spent and deducted almost \$1 million in 1 year for yachts, club dues, shipboard conventions, hunting and fishing trips, and parties? Does not a corporation make such expenditures to develop good will? We have already seen that good-will expenditures are clearly deductible under the Finance Committee report. How about the banker who deducted a substantial part of the cost of his daughter's coming-out party as a business expense? Wasn't he also developing customer good will? Certainly the Government is not, under the Finance Committee report, free to disallow expenses regardless of the form of entertainment the taxpayer may adopt to develop good will. Similarly, in all the other cases set forth above, the taxpayer would appear to be able to continue to deduct all entertainment expenditures.

"RED HERRING"

One further "red herring" in the Finance Committee report should be mentioned. The report states that no deduction will be allowed for entertainment expenses "which under the circumstances in which they are incurred are lavish or extravagant." Here again no standards or guidelines are furnished. What is lavish or extravagant under the circumstances? If the circumstances involve a taxpayer accustomed to entertaining in an elaborate and expensive style, can they be held to be lavish under the circumstances? When does a yacht become an extravagant expenditure? When is it 60 feet in length? One hundred feet in length? When it has more than one mast? Would these criteria vary with the income—or expected income—of the taxpayer? Would a resident of Miami Beach, Fla., be entitled to a bigger and more expensive yacht than a resident of Providence, R.I.? Would a beach home with eight rooms be a lavish facility? What about one with 30 rooms? Would a corporate president be entitled to drink champagne whereas a proprietor of a corner grocery store be restricted to ordinary corn liquor?

Is it not abundantly clear that the so-called test produced by the Finance Committee, superimposed upon the unsatisfactory test of present law, will simply compound existing difficulties? The litigation and controversy which would follow adoption of such meaningless language would even make the present situation seem a happy one. The result would be a real mess. And to what avail? In this posture of things, it seems quite proper to ask: What is wrong with the proposal adopted by the House of Representatives? It is obviously far superior to the Finance Committee's product. We urge the Senate to endorse at least the House provision and again, as it did in 1960, produce a really significant legislative measure to deal with expense account abuses.

When the committee proposes to loosen the House provisions, I hope the amendments will be voted down. Then I hope we can then proceed to the consideration of the original proposals of the President of the United States fixing quantitative limits upon the amounts that can be tax

free. We do not object to these expenditures but we think those who enjoy them should pay for them and that Uncle Sam should not be called upon to be the silent host.

TAXATION OF FOREIGN OPERATIONS

Mr. President, I had intended to discuss the question of foreign operations, but the Senator from Tennessee [Mr. GORE] has devoted himself to this subject and to the provisions of the bill relating to foreign operations.

For this reason I am going to ask unanimous consent that the statements which I have prepared on foreign operations be printed in the RECORD at this point in my remarks.

There being no objection, the statement was ordered to be printed in the RECORD, as follows:

FOREIGN OPERATIONS

I. GENERAL STATEMENT

Except for withholding on dividend and interest income, which was defeated outright, no major aspect of the President's recommendations for tax reform contained in his message to the Congress on April 20, 1961, suffered so badly at the hands of the Finance Committee as did those recommendations relating to the taxation of income and profits earned abroad by U.S. persons.

President Kennedy recommended that American corporations, as well as individual U.S. taxpayers who are "shareholders of closely held" foreign corporations, be taxed each year "on their current share of the undistributed profits" of foreign corporations in which they hold stock and which are "organized in economically advanced countries." At the same time, the President recommended "elimination of the tax haven device anywhere in the world."

The Ways and Means Committee and the House of Representatives moved resolutely, if not altogether perfectly, in the direction indicated by the President.

The Finance Committee, on the other hand, in executive session, by rollcall vote, refused even to consider the President's major recommendations in this area. Instead, the committee proceeded to adopt a watered down tax haven approach to this problem, and then, amendment by amendment, moved further to weaken even that wholly inadequate approach—this, despite the fact that the Secretary of the Treasury had agreed, in testimony before the committee, that anything short of removal of the deferral privilege, whereby U.S. taxation of profits earned abroad may be indefinitely postponed, would be but "piddling" with the problem.

Though the committee has done a fairly creditable job in reviewing and acting on many provisions in the foreign area contained in the House-passed bill, it has materially weakened the grossup provision, section 9, and section 11, which deals with earned income from sources outside the United States. These provisions badly need strengthening. By far the most important provisions, however, are contained in section 12 dealing with controlled foreign corporations. It is here the Senate must surely act if this bill is to come even close to implementing the President's recommendations.

II. TAXATION AND CAPITAL FLOWS

One of the most startling economic phenomena of the past 5 years is the large-scale movement of American capital abroad. Though some of the economic activity represented by this movement may be desirable and may serve to increase exports, much of it directly and materially weakens the base of our economy. Some of this capital is drawn abroad for legitimate economic reasons. Much of it, far too much, is stimulated to move abroad because of faulty U.S. tax provisions.

Several reasons exist, of course, for this unprecedented movement of capital abroad. International barriers of all sorts are being broken down. Convertibility of currency exists in large measure. Electronic communications insure effective control of economic activities anywhere in the world from one central office. The movement of persons and goods has been speeded up and cheapened to a point where distance makes very little difference. American economic style and business organization have made American know-how welcome in most countries. American free world leadership has lent prestige to all things American.

In view of these facts—facts which we may not want to alter, even if we could—it is most inappropriate to set up additional artificial stimuli to the movement of American capital abroad, particularly into activities and in amounts which are contrary to the national interest. Existing law relating to the taxation of economic activities carried out by American interests in foreign countries constitutes just such an artificial stimulus to the movement of capital abroad into areas and activities which pose dangers to the domestic economy and make more difficult a solution of the balance-of-payments problem.

As our tax laws now stand, they constitute a positive subsidy to the movement of American capital abroad. There are numerous ways in which the taxation of profits from foreign operations can be reduced to the extent that it may be more profitable to expend American capital and American know-how in building up the economy of West Germany rather than the economy of West Virginia, or south Italy rather than South Carolina.

The existence of this unhappy circumstance is given implicit verification by virtue of the fact that this bill, in 11 of its 27 sections, deals with the taxation of foreign operations of U.S. taxpayers, both individual and corporate. Unfortunately, having recognized the existence of certain problems, the bill proceeds toward correction of these problems in a most timid and half-hearted manner.

Our tax laws regarding foreign operations are hopelessly out of date. For the most part they stem from rules laid down when the income tax was developed prior to the First World War. Developments in communications, transportation, and even in international politics and political organization have made some of these laws obsolete.

In theory, the United States taxes its citizens wherever they are and from whatever source their income is derived. Although this would seem to preclude the use of the tax laws as a subsidy to draw economic activity abroad, in practice we have nullified theory to a great extent by, first, allowing American interests to operate abroad in subsidiary form without the imposition of any U.S. taxation whatsoever on the profits from those operations until those profits are remitted—often in a form which can take a capital gains rate or no rate at all—and, second, by providing for a credit for foreign income taxes paid against ultimate U.S. taxes on income earned abroad.

It is now well past the time when we should have examined our basic concepts and tax laws in the light of current political and economic realities. It is well past the time when we should have given serious consideration to the need for continuing, through domestic tax law, the subsidization of the strengthening of the economies of the countries of Western Europe, Japan, Canada, and other countries which are, at least for the moment, our political allies and friends, but which are now, and in the foreseeable future will continue to be, our fierce economic competitors.

In reexamining our tax laws relating to foreign economic activities, there are three

considerations which must, in the light of today's conditions, be kept in mind. These are (1) equity, always important to any tax system but doubly so in a voluntary system such as ours, (2) domestic economic health, particularly in these times of persistently high unemployment, and (3) the balance of payments.

III. TAX EQUITY

Equity in taxation is a subject to which lipservice is paid from time to time. Everyone claims to be in favor of equity, but many define equity in strange and tortured ways. Generally speaking, if a dollar earned by a particular type of taxpayer in any economic activity, in any geographical area, pays the same tax as another dollar earned under other circumstances by similar types of taxpayers we can say that tax equity has been achieved.

Of course, from time to time preferences are given to certain types of operations, certain areas, and certain organizations, but when this is done it should be done consciously, and deliberately, in the full knowledge of what is being done, and with the accomplishment of definite objectives in mind. When a subsidy is voted—and a subsidy can be awarded a taxpayer by giving him a tax preference just as surely as it can be awarded by way of a cash payment—it should be voted to accomplish a proper national or social goal, not done accidentally, or as a private giveaway.

For example, there is no question that the average homeowner receives better tax treatment than the average renter of living quarters. But the Congress has deliberately provided this because it is considered socially desirable to foster homeownership.

In certain other instances tax advantages are given inadvertently, or because of reasons which are no longer valid. Certain of our laws dealing with the taxation of the profits and income earned abroad by American taxpayers, both corporate and individual, directly and through technically foreign subsidiaries, fall in each of these two categories.

Business decisions today are often made on the basis of tax consequences. Many decisions as to what operations should be moved abroad are made on the basis of tax consequences. Many foreign operations are set up in order to avoid taxes, in a virtual maze of interlocking and overlapping organizations, confusing to customers and operators alike. This is hardly in keeping with concepts of equity or even good business management.

The best way to achieve tax equity, particularly in the field, is to seek tax neutrality, that is, to seek to have tax laws such that economic decisions are made on the basis of economic criteria, not on tax consequences. Unfortunately, the bill reported by the Finance Committee, although it recognizes the existence of inequity does little to deal with it effectively. Under terms of this bill, operations carried on abroad will still receive favored tax treatment as compared with the same type of operation carried on here at home.

IV. DOMESTIC ECONOMIC HEALTH

It has been clearly recognized by government at all levels—Federal, State, and local—as well as by foreign governments, that taxation and tax differentials influence economic decisions. For that reason, we have seen some of our State and local government units offer various types of tax concessions when negotiating with industries to relocate. Some foreign governments have made concessions, including allowing new concerns to operate tax free for a specified number of years. The results of this type of stimulus can be clearly seen in Puerto Rico.

When the United States arbitrarily and unilaterally gives tax concessions to domestic industry, provided that industry will move abroad, the results are certainly foresee-

able—and we are seeing them now. The end result is the weakening of our economy. But for some reason, many seem to feel that loss of capital and productive facilities is good for the United States, although bad for other countries.

The tax stimulus to the movement of productive facilities abroad is a subject which has been widely discussed for some years. For example, a study made by the American Management Association in 1960 and reported in *Business Week* for December 31, 1960, showed that, "because of tax differentials, the reinvestment of foreign earnings over a 3-year period can provide 'roughly double the rate of profit accumulation for reinvestment that is possible under domestic tax schedules.'"

With 52 percent domestic corporate tax rate, and with tax-haven countries having rates running down almost to zero in some instances on sales, service, and holding company income originating in third countries, the temptation to move facilities abroad, accumulate profits for reinvestment for a period of years, and only then begin to repatriate dividends on which an inadequate U.S. tax would finally be paid, could hardly be resisted. In fact it has not been resisted and we have seen a rapid acceleration of the buildup of American direct investment abroad during the past 5 years.

Our total private investment abroad now exceeds \$50 billion, and is increasing at the rate of about \$5 billion per year. In the field of direct investment, and particularly with reference to tax-haven devices it is noteworthy that, according to some authorities, two-thirds of our tax-haven companies have been established within the past 5 years.

The movement of productive facilities abroad has already reached serious proportions, but even more alarming is the increasing tempo of this movement. The loss of jobs, the loss of productive facilities needed for defense and other purposes, cannot be taken lightly. It is altogether too easy for a manufacturer, when he is faced with a labor problem or with extensive replacement of machinery, to pull up stakes and move a large part of his production to a foreign country.

In this country, contrary to the practice everywhere else in the world, the direct regulation of the outflow of capital and productive facilities has always been resisted. Such direct regulation may be necessary if we are to reach a real solution. But at the very least, we must not directly and positively encourage such an outflow by giving tax concessions to those who operate abroad and thereby build up the economies of foreign countries while tearing down our own. At the very least, we should remove the tax incentive which now exists to go abroad.

There will be, even with the enactment of the tightest possible tax provisions, a continuing flow of direct investment capital and productive facilities abroad in response to economic stimuli. This will not be interfered with by this, or any other similar bill. There will also be a continuation of the outflow of other forms of capital—portfolio and short term. These latter outflows have been troublesome during the past few years and require direct and specific regulation. This bill touches only direct investment, and touches that ever so tenderly.

Criticism has been leveled at those who wish to remove the tax incentive to take American industry and productive facilities abroad. It has been alleged that this is a new type of protectionism—a new type of isolationism.

This criticism is unwarranted, and represents the most blatant type of reverse doublethink. There is no thought, insofar as this legislation is concerned, of doing anything more than removing a positive stimulus and subsidy for American plants to be moved abroad. Of course, it may well be

that this is not enough. It may be that tax neutrality may not be sufficient to slow to a tolerable rate this widespread movement of capital abroad.

Those who believe in freer trade, and who support in general the President's recommendations for legislation to improve our reciprocal trade system which has served us so well for the past 28 years, certainly cannot legitimately be accused of economic isolationism merely because they wish to achieve tax neutrality, and terminate a hurtful subsidy.

The most cruel competition which an American producer can be forced to undergo is competition from American-type goods with well-known American brand names, produced abroad by American-owned subsidiaries which have achieved rapid growth because of the ability to dodge U.S. taxes and plow back practically all earnings, with these products distributed throughout this country through a well-established chain of wholesale and retail outlets. With a further lowering of tariffs contemplated by the trade bill now before the Finance Committee, it is certainly most inequitable to continue to give these foreign but American-owned producers, continued tax advantages when they are competing directly with U.S. production, either in American or in foreign markets.

V. BALANCE OF PAYMENTS

It has become so fashionable to discuss any problem in terms of its effect on the balance of payments that one might properly look with suspicion on some arguments which attempt to tie balance-of-payments considerations to any possible subject matter. This has been much overdone. In the case of legislation directly affecting the flow of capital funds abroad, however, balance-of-payments considerations are certainly pertinent.

The balance-of-payments problem has been with us for some years, but has been recognized as being acute by the general public and most Government officials for only about 3 years. Prior to that time, many still talked of the dollar gap and of means of increasing the flow of capital abroad.

Although the balance-of-payments problem seems likely to be brought under control within the near future—and it must be brought under control within the next 2 or 3 years if we are to be able to avoid the use of rather drastic control methods—the problem is still acute and must be attacked from all quarters. This includes, but is not limited to, a close examination of investments made abroad by U.S. taxpayers. Those sections of the bill dealing with the taxation of profits gained from activities carried on abroad by American taxpayers will affect the balance of payments specifically and directly.

There are three principal types of capital outflows which are of concern in the balance-of-payments picture. Only one, that is, direct investment outflows, will be affected by the provisions of this bill. The other two, portfolio investment and short-term flows, will be little affected and must probably be dealt with in ways other than tax changes. The simplest way to deal with all three, of course, is by some system of direct licensing of capital outflows. Since we have traditionally resisted this type of regulation, however, we must be doubly sure that our tax laws are not weighted in the wrong direction. This bill does not go far enough in that regard. It does not subject income and profits earned abroad to as heavy an income tax as income and profits earned in the United States. But it does move, though haltingly and timidly, in the right direction.

There can be no question as to the effect of capital outflows on the balance of payments in the short run. There can be, of course, some question as to the long-range effects of capital outflows, particularly direct investment flows.

As to the long-range effect of direct investment outflows, the effect on the balance of payments may eventually be positive. But, with an acute situation which must be corrected within 2 or 3 years, it is not advisable to wait for a period of years, perhaps as long as 12 to 15 years according to Treasury Department analyses, for current direct foreign investment to assist in correcting the present imbalance.

Bearing in mind that direct foreign investment is accelerating, and that the net overall balance-of-payments deficit this year is expected to be in the neighborhood of \$1.5 billion, an alteration of investment flows in the order of a few hundred million dollars would be significant.

Reliable estimates indicate that the complete removal of the deferral privilege would, by slowing down direct investment outflows and by speeding up repatriation of earnings, decrease the balance-of-payments deficit by about \$400 million annually. This bill, of course, would not be nearly so beneficial. In its present form it would be of little assistance. A good, tight, tax haven bill would assist in the balance of payments in the order of \$200 to \$300 million.

VI. SPECIFIC PROVISIONS

The best and indeed the only sure way to achieve substantial equity, guard against the untoward weakening of American industry and assist in the solution of the balance-of-payments problem through taxation is to tax American taxpayers annually on income and profits earned anywhere in the world. This would restore neutrality as to taxation, allowing economic forces to play their proper role in economic decisions relating to investment choices at home or abroad. This would insure that the corporation which helps to build up a depressed area in the United States would be treated as fairly by the Federal Government as the corporation which builds up the economy of Western Europe. The most important section of the subject bill dealing with foreign operations has, however, been drawn up on the theory that the partial elimination of tax-haven advantages is sufficient.

There is no question that the complete elimination of tax-haven operations would help materially. It is through the combination of a sales subsidiary, a service subsidiary, and a holding company located in a tax-haven country, Switzerland, for example, that the U.S.-owned manufacturing company in Germany—or other relatively high tax foreign country—is able to reduce its German tax to a rate well below the stated rate of 51 percent. If tax havens are made less profitable from a tax standpoint, the manufacturing operations which support them will have to be justified on economic grounds, not on grounds of tax avoidance, whether the taxes avoided are United States or foreign.

The Finance Committee, by approving even these imperfect provisions, does recognize that certain changes in existing law should be made.

1. It is recognized that numerous abuses exist in the operation of certain types of corporations organized in certain low-tax countries. While this tax haven problem is recognized, it is not completely corrected.

2. It is recognized that many individual U.S. citizens are living abroad for the purpose, or with the result, of escaping proper U.S. taxation. But the provisions of the bill are sufficient to deal with the problem. It will still be highly profitable, under the terms of this bill, for a U.S. citizen to live abroad and thereby avoid paying his fair share of the cost of U.S. and free world defense and essential Government services.

3. It is recognized that there are numerous abuses in setting up foreign trusts for the purpose of escaping U.S. taxation.

4. It is recognized that there have been abuses in the liquidation of foreign corpora-

tions, with the result that accumulated ordinary income is being brought into the country in a form which allows it to be taxed at the low capital gains rate, if at all.

5. It is recognized that the U.S. estate tax has been avoided by some through the device of investing in foreign real estate, even in contemplation of death.

6. It is recognized that the law as now written allows both a partial credit and a deduction for foreign income and related taxes. For some reason, presumably because it is recognized that tax reductions do act as subsidies to draw capital investment abroad, the committee allows this double benefit to be continued in less developed countries.

7. It is recognized that present law does not require sufficiently stringent reporting of foreign economic activities of American interests.

In order for the bill to be really meaningful in correcting the imperfections in existing law which have been recognized, however, certain minimum changes must be made.

1. Section 12—Controlled foreign corporations

(a) This entire section, embodying as it does the tax haven approach, ought to be deleted and have substituted therefor the complete removal of the deferral privilege. Language to accomplish this objective exists in amendment 6-19-62—A to H.R. 10650, previously offered.

(b) The tax haven approach, if sufficiently rigorous, does represent a step forward. Should the Senate decide to proceed with this approach, this section should be amended in at least the following ways:

1. The de minimus rule should be restored to 20 percent.

2. The exception for export trade income of "Export Trade Corporations" should be deleted.

3. The exception for dividend and interest income from less developed countries, together with profits realized from the sale of investments in less developed countries, should be deleted.

2. Section 9—The gross-up

This provision should be made applicable to income from subsidiary corporations operating anywhere in the world, as provided by the House-passed bill. There is no equity in allowing both a deduction and a partial credit for income taxes paid to certain countries. The operation of existing law in this area is capricious and even perverse, and is not a suitable vehicle for a subsidy, should it be felt that a subsidy is needed or desirable.

3. Section 11—Income earned abroad

There is no equity in allowing individual U.S. citizens living abroad, either temporarily or on a more permanent bona fide basis, to pay less taxes than citizens and residents here at home. All benefit from services rendered by both the U.S. Government and the government of their host countries. All should contribute toward the cost of U.S. and free world protection. It is particularly inappropriate to allow a phasing-in of taxes on fringe benefits.

WITHHOLDING OF BASIC TAX ON DIVIDENDS AND INTEREST

Mr. DOUGLAS. Mr. President, I come now to the worst legislative crime committed by the Finance Committee, namely the deletion of the withholding provision on dividends and interest.

In striking out of the tax bill the plan for withholding the basic tax on dividend and interest payments, the committee is, in effect, indicating that it condones the intolerable gap in the payment of taxes on dividends and interest,

in many cases the result of outright and willful evasion. The Secretary of the Treasury estimates that in 1963 the gap between the dividends and interest that should be included on tax returns, and those that actually are, will exceed \$3.7 billion.

In my own judgment, it is probably nearer \$4 billion. The truth of the matter is that close to \$4 billion paid out in dividends and interest is not reported by the recipients, and therefore no taxes are paid upon it, even though it is received. Part of this is unconscious avoidance; part of it is conscious evasion.

REVENUE LOSS OVER \$1 BILLION

The Government will lose in revenue almost \$1.1 billion in 1963—\$440 million of taxes owed on dividends and \$650 million of taxes owed on interest.

Withholding would collect about \$880 million of this \$1.1 billion. Withholding combined with the other collection and enforcement procedures available to the Internal Revenue Service would close nearly the entire gap. Without withholding, and with the automatic data processing system which has been so much heralded, less than a fourth of the gap can be closed, or not more than \$250 million can be collected, but even this cannot be accomplished until the Internal Revenue Service's new automatic data processing system becomes fully operational in 1967.

As I mentioned earlier in my address, in 1942 Congress put into effect the withholding plan on wages and salaries.

LITTLE WAGE EVASION OR AVOIDANCE

This has been in operation for 20 years. Only 3 percent of the taxes due on wages go unpaid. On the other hand, in 1960 more than 11 percent of the dividends which should have been reported on the tax returns of individuals were not so reported. The situation is even more intolerable in regard to interest. Slightly more than one-third—to be precise, 34 percent—of interest paid out was not reported as income. No taxes were paid upon that percentage.

WHY DOUBLE STANDARD

Why should we have this double standard, Mr. President? Withholding at the source occurs on wages and salaries, the recipients of which have much lower incomes than the average recipient of dividends and interest. In regard to wages and salaries there is virtually no tax evasion. Those in the low income group pays their taxes, as they should, of course. But as a result of the failure to withhold taxes on dividends and interest, a goodly proportion of those in the upper income group do not pay their taxes.

Who are these people who do not pay their taxes on interest and dividends? The Internal Revenue Bureau made a study of 6,000 to 8,000 cases. They found that about 70 percent of the nonreported dividends were received by individuals having more than \$10,000 of income. In respect to nonreported interest, only 30 percent of it was received by people having less than \$5,000 income a year, and approximately 30 percent was received

by those who had more than \$10,000 a year income.

I ask again, Mr. President, if a withholding system is appropriate for those who are in the lower income group, the wage earners, to make sure that they pay their taxes, what possible excuse can there be for not applying it to help collect the taxes on dividends and interest

from the many individuals with higher incomes who escape those taxes today?

Mr. President, I ask unanimous consent that two tables prepared by the Secretary of the Treasury may be printed in the Record at this point.

There being no objection, the tables were ordered to be printed in the Record, as follows:

TABLE 1.—Number of individual income tax returns with dividends and amount of dividends in 1959

[Dollars in thousands]

Adjusted gross income	Number of returns with dividends ¹	Dividends on returns ¹	All returns	Adjusted gross income, all returns	Number of returns with dividends as a percent of all returns	Dividends on returns as a percent of adjusted gross income
Taxable returns:						
Under \$5.....	1,142,168	\$675,392	23,415,117	\$71,434,488	4.9	0.9
\$5 to \$10.....	2,008,754	1,253,645	19,305,707	133,012,206	10.4	3.9
\$10 to \$20.....	1,369,308	1,731,510	3,909,998	49,701,599	35.0	3.5
\$20 to \$50.....	518,881	2,219,331	723,682	20,846,984	71.7	10.6
\$50 to \$100.....	101,520	1,416,317	114,711	7,549,453	88.5	18.8
\$100 to \$200.....	20,492	845,098	21,940	2,844,906	93.4	29.7
\$200 to \$500.....	4,598	508,843	4,776	1,361,923	96.3	37.4
\$500 to \$1,000.....	700	190,677	717	478,154	97.6	39.9
\$1,000 and over.....	261	263,463	265	545,633	98.5	48.3
Nontaxable returns.....	781,696	610,118	12,774,384	17,319,633	6.1	3.5
Total.....	5,948,378	9,714,394	60,271,297	305,094,979	9.9	3.2

¹ Covers domestic and foreign dividends before dividend exclusions. Does not include data for form 1040A returns which do not specify the amount of dividends received.
Source: Treasury Department, Office of Tax Analysis.

TABLE 2.—Number of individual income tax returns with interest and amount of interest in 1959

Adjusted gross income class	Number of returns with interest	Interest on returns (thousands)	Average amount of interest	All returns	Adjusted gross income (thousands)	Number of returns with interest as a percent of all returns	Interest as percent of adjusted gross income
Taxable returns.....	7,829,849	\$3,754,177	\$479	\$47,496,913	\$287,775,346	16.5	1.3
Under \$5.....	2,076,348	732,695	353	23,415,117	71,434,488	8.9	1.0
\$5 to \$10.....	3,502,941	1,145,505	327	19,305,707	133,012,206	18.1	1.9
\$10 to \$20.....	1,643,381	857,445	522	3,909,998	49,701,599	42.0	1.7
\$20 to \$50.....	491,763	631,422	1,284	723,682	20,846,984	68.0	3.0
\$50 to \$100.....	91,923	243,484	2,649	114,711	7,549,453	80.1	3.2
\$100 to \$200.....	18,472	90,428	4,895	21,940	2,844,906	84.2	3.2
\$200 to \$500.....	4,142	36,469	8,805	4,776	1,361,923	86.7	2.7
\$500 to \$1,000.....	647	10,193	15,754	717	478,154	90.2	2.1
\$1,000 and over.....	232	6,536	28,172	265	545,633	87.5	1.2
Nontaxable returns.....	1,443,845	641,241	444	12,774,384	17,319,633	11.3	3.7
Total.....	9,273,694	4,395,418	474	60,271,297	305,094,979	15.4	1.4

Source: Office of the Secretary of the Treasury, Office of Tax Analysis.

Mr. DOUGLAS. Mr. President, I wish to discuss each of these tables a little.

In 1959 there were 60.3 million individual income tax returns filed in this country. Only 7.8 million of the taxable returns included any interest. In other words in only 13 percent of the income returns listed any interest.

The figures I am giving will be quoted to the nearest 100,000.

There were 2.1 million returns in which interest was reported which had under \$5,000 of income, or 3½ percent of the total number of taxpayers. The interest which they received was only 1 percent of the total income received by the entire group of those below \$5,000. They received approximately 17 percent of the total amount of interest paid out.

There were about 650,000 returns with incomes of over \$20,000 a year on which interest was reported. These comprised only 1 percent of the total number of tax returns, but they received about 55 percent of the interest reported.

The table indicates that the recipients of interest in the main belong to the upper income brackets and not to the lower income brackets. Everyone knows this to be a fact.

DIVIDENDS RECEIVED BY UPPER INCOME GROUPS

The situation is even more marked in respect to dividends. Only 6 million returns showed the receipt of any dividends, out of the 60.3 million returns which were filed. A little less than 10 percent of the returns, therefore, showed any dividends received.

Those returns with total gross incomes of under \$5,000 were 1,142,000 in number or not quite 2 percent of the entire number of returns, and the dividends which were reported received were less than 1 percent of the total income received by those whose returns showed incomes of less than \$5,000.

If we include those returns with incomes from \$5,000 to \$10,000, we would get a total of only 3.1 million or 3.2 million out of the 60.3 million returns, or

about 5 percent of the total. In other words, only 5 percent of the income recipients were in the \$5,000 to \$10,000 class and at the same time received dividends, and the dividends which they received were only 20 percent, roughly, of the total dividends paid out.

EIGHTY PERCENT OF DIVIDENDS GO TO THOSE WITH INCOMES OF \$10,000 OR MORE

To put it the other way—and this is the important point—80 percent of the dividends went to those who filed returns with incomes of more than \$10,000.

I remember that the Secretary of the Treasury under the administration of Mr. Eisenhower, Mr. Humphrey, stated that the recipients of dividends and interest are now no more wealthy than anyone else, that wealth had been so democratized in this country that those who owned stock were like everyone else. That is not true.

I wish to present another very interesting fact. Those with taxable returns of over \$1 million a year got 48 percent of their income from dividends.

NOT WIDOWS AND ORPHANS WHO GET LARGE DIVIDENDS

So, Mr. President, the failure to require withholding applies to those in the upper income brackets of society, in the main, and not to those in the lower or middle income brackets. It is not the widows and the orphans who get these sums, in whose name the piteous appeals are made that there should be no withholding of the taxes they owe. Instead, it is the recipients of large incomes who in the main are involved.

I wish to say also that I am well aware that in a large percentage of the cases the failure to pay taxes on dividends and interest is not intentional, but is rather a result of the fact that the interest paid on savings bank accounts and the dividends or interest or whatever one might call it paid by the building and loan associations are more or less automatically added to the capital and to the account of the individual, and are not drawn out by the individual into a separate checking or savings account.

The recipient often does not spend those amounts for current consumptive purposes. Therefore it is quite possible that he (or she) would not regard them as income. They are income nevertheless, because they go to increase the capital holdings of the individual. What he does is tacitly to acquiesce in their reinvestment. In those cases I certainly do not charge any conscious fraud.

But when we get up into the upper income brackets and find the reception of large amounts of dividends which are not reported and upon which taxes are not paid, and large amounts of interest which are received but not declared, then we get into a more dubious field. Whether that is evasion, avoidance, or downright fraud, the fact remains that those are sums owed by individuals to the Treasury, and their failure to pay those amounts increases the burden upon the honest taxpayers who pay every cent they owe.

I therefore hope that when the committee moves to strike the withholding provisions from the House bill, the Sen-

ate will show its sense of fairness by rejecting the amendment.

SUPPORT PRESIDENT ON WITHHOLDING

I wish again to emphasize that that is the one point the President of the United States emphasized last week in his statement to the press and to the Nation. He said he wanted the withholding provisions retained. God grant that this body may have courage enough to stand up for the payment of these taxes against the powerful forces of the building and loan associations, and the mutual savings banks, and God grant that the leadership of the Democratic Party may stand fast behind the President and not try to strike that provision from the bill.

AUTOMATIC DATA PROCESSING NO SUBSTITUTE

It is said that since we provide for the automatic data processing of the payment of dividends and interest, that will remove the necessity for withholding. Let me point out that the Commissioner of Internal Revenue, Mr. Mortimer Caplin, an extremely able, high-minded, and conscientious man—the man who actually does the job of collecting our taxes—has carefully studied both the withholding plan and the expanded information-reporting program and has concluded that information reporting, even when coupled with the Service's new automatic data-processing system, cannot be an alternative to withholding. This is because an ADP information return system in itself will not collect one penny in taxes.

All it can do is to identify possible discrepancies between the amounts received by the individual and the amounts declared by the individual. But it does not collect the taxes on any difference. That will have to be done through the ordinary collection and enforcement procedures available to the Internal Revenue Service.

The figures tell the story themselves. If we use the estimate for 1959 of the gap in the reporting of taxes on dividends and interest at \$850 million, withholding alone would recover \$650 million at a cost of approximately \$19 million. The remaining \$200 million could be recovered in large part by the ADP system, combined with a reasonable enforcement effort for an estimated additional cost of \$29 million. In other words, the entire gap could be closed through a combination of withholding and enforcement for a cost of only \$48 million.

To close the entire gap without withholding would be physically impossible and economically unfeasible. It would mean contacting 12 million people for the purpose of checking discrepancies in their dividend-and-interest reporting turned up by ADP. This is three times as many people as the Service contacts today in its total enforcement program. It would cost \$400 million to collect the \$850 million by this method, more than eight times the cost if withholding were used.

Even if we were to collect all of the \$650 million, the dollar equivalent to the results under withholding, it would cost \$200 million to collect this amount, or more than 10 times what it would cost un-

der withholding. In addition, the Internal Revenue Service's present enforcement staff, which through its activities collects about \$3.5 billion annually, would almost have to be doubled to collect the additional \$650 million. The resulting imbalance in enforcement effort is one of that cannot be reconciled with any sound concept of tax administration.

To look at the matter realistically, and within the concept of a sensible and effective use of equipment and enforcement manpower, based on 1959 data, the information-reporting system adopted by the committee can be expected to recover only \$200 million.

These figures, which were compiled by the Commissioner and his staff after careful study of the matter, conclusively prove that the information-reporting system adopted by this committee is not a substitute for withholding.

Even apart from its complete ineffectiveness as a tool for closing the more than \$1 billion gap in the reporting of taxes on dividends and interest, the information-reporting plan adopted by the committee is at best a clumsy and burdensome substitute for the relatively simple withholding plan adopted by the House. Under withholding, a payer of dividends or interest would merely be required to deduct a flat 20 percent from its payments to persons who have not filed exemption certificates and then make one lump-sum payment to the Government each quarter. The payers will not have to make out individual withholding receipts for each recipient nor will they be required to submit any detailed records to the Government.

MORE REDTAPE IN REPORTING PROVISIONS

The Senator from Virginia [Mr. Byrd], who is opposed to the withholding system, and to whom the alleged alliance between the Senator from Illinois and the chairman of our committee does not extend on that point, but who has a rugged sense of individual honesty and integrity, insisted that if we did not adopt the withholding system, we should impose a thorough reporting system. He insisted that all dividends and interest in excess of \$10 each quarter be reported to the Government and to the individual recipient.

Under that plan let us see what would happen. At the end of the year each payer would be required to add up all the dividend or interest payments it has made to a person during the year and, if they equal or exceed \$10 in the aggregate, make out an information return showing the name and address of that person and how much was paid to him during the year. Then this information must be filed with the Government and a copy given to the recipient. This means that the payer must make a reasonable effort to obtain the current address and account numbers for each of its depositors or stockholders. Translated into numbers, payers of dividends and interest will be required to complete and file with the Government 100 million pieces of paper each year and then distribute an additional 100 million copies to their depositors or stockholders.

The savings and loan industry has admitted that this information reporting plan will involve heavier administrative costs for them than withholding. They got themselves into their present fix. Their witnesses testified that we should not have withholding but instead automatic data processing. The Senator from Virginia [Mr. BYRD] with his strict sense of integrity, insisted that this be done. It will be done if the committee has its way, although I suspect that efforts will be made to weaken this position along the line.

MORE PAPERWORK THAN WITHHOLDING

If it is done, the banks and the savings and loan institutions will have to do infinitely more paper work than they would have been compelled to go through under the withholding plan. Already some of them are beginning to understand the situation. The Senator from Oklahoma spoke of a beartrap. I wish to compliment him on a very witty speech he made about me last week, when he said that one should beware of praying for something because sometimes he gets what he prays for. I thought that was a good joke on me and I compliment the Senator on his wit. We can say that the same thing applies to savings and loan associations and to the banks. They asked for automatic processing rather than withholding. The Senator from Virginia said, "All right, you will take it." They got it. Now the beartrap has closed on them and the Senator from Oklahoma may well quote to them, "Be careful what you pray for. You may get it."

Mr. KERR. Mr. President, will the Senator yield?

Mr. DOUGLAS. I yield.

Mr. KERR. When they wake up and realize what has come about, they may feel like the fellow who had a bone in his throat and thought he had a nice mesh of fish.

Mr. DOUGLAS. I am glad the Senator admits it. This was one of the few occasions when the Senator from Oklahoma and the Senator from Illinois voted together. I wish to compliment the Senator for opposing the elimination of the withholding provision. There were not many of us. The Senator from Oklahoma was one of them. This will be one of the things which he will be able to plead before St. Peter.

Now I should like to discuss—and I will try not to take too much time—the administrative provisions of the withholding system, because there has been a great deal of misrepresentation and distortion.

SIMPLE PLAN TO ADMINISTER

Basically, the plan is very simple. The institution which pays interest, dividends, or patronage dividends would be required to deduct a flat 20 percent from these payments and remit the total amount to the Government once a quarter. The plan includes several relief provisions which would insure that individuals and other taxpayers who owe little or no tax on their dividend and interest income will not be unduly harmed by withholding. These three basic objections have been made to the

plan: it would hurt many people with low incomes who depend on their dividend and interest income for living expenses; it would result in a maze of paperwork and confusion for the taxpayer; and it would impose heavy burdens on the paying institutions. We have already pointed out that withholding would be far less burdensome to the payers than the new information reporting plan. The other two objections are equally groundless.

WITHHOLDING WOULD NOT HURT LOW-INCOME INDIVIDUALS

There have been repeated accusations that withholding will unfairly deprive low-income people of funds which they need to meet their living expenses. This is just not true.

CHILDREN AND LOW INCOME GROUPS EXEMPT

In the first place, we have shown that there are very few of those in the low income brackets who get dividends, and not a great many who get interest. Those with such low incomes that they do not owe any taxes could completely avoid withholding in almost every case merely by filing simple exemption certificates with the paying institutions. Children under 18 would be exempt from withholding regardless of their tax status. There can be no hardship for these people, since withholding will not even apply.

QUARTERLY REFUNDS

It is true that there would be some people who, although they owe some tax, would be subject to overwithholding. These people, however, can obtain quarterly refunds of the overwithheld tax merely by filing a simple refund claim.

I should like to point out that in the case of wages and salaries, the wage and salary worker can get a refund only once a year. The withholding plan for dividends and interest would provide a refund once a quarter. It would give those who receive dividends and interest a refund once a quarter.

Furthermore, it has been found that 37 million recipients of wages and salaries ask for refunds. Those refunds are completed within 3 or 4 weeks, which is a most extraordinary performance by the Internal Revenue Service. They get their money back within a month. This is done on a volume of 37 million claims. I wish to make that clear. The average return is \$142. Under the withholding plan for dividends and interest, only about one-fifth as many refunds will have to be made.

Under such a withholding plan as is now in effect for wages and salaries, 14.3 percent of the taxes collected by wage withholding must be refunded; the comparable figure for dividend and interest withholding would be only 5.5 percent, and most of this will be returned quarterly.

MOST ELDERLY EXEMPT

A great many crocodile tears have been shed about the elderly, how they will be heavily penalized under the withholding plan. I do not believe that we fully realize the exemptions which are now given for tax purposes for those over the age of 65.

DOUBLE PERSONAL EXEMPTION

The ordinary exemption is \$600 per person. It is double for those over 65 years of age. The husband would get an exemption of \$1,200, and his wife, if over 65, would get an exemption of \$1,200. The total exemption, therefore, would be \$2,400.

RETIREMENT INCOME CREDIT

Then, in addition, there is a little known tax credit exemption for retirement income. This is not known by the average person. When we found out about it in the Finance Committee it came with a good deal of surprise to many of us. A person over the age of 65 can get a \$240 tax credit, which is the equivalent of a \$1,200 deduction, on amounts received from dividends and interest, rents, royalties, and pensions. The wife would get it for any such amounts received in her name. Assuming, then, that they both get the \$240 tax credit, or the equivalent of a deduction of \$1,200 each, thus, added to the double exemption of \$2,400, would make the first \$4,800 of income totally tax exempt.

ELDERLY COUPLE NEEDS \$5,300 IN INTEREST OR \$6,100 IN DIVIDENDS TO BE TAXABLE

In addition to this, there is the 10 percent standard deduction. This means that those who receive \$5,300 from interest, will pay no taxes at all, and would therefore be exempt from withholding. Those who receive \$6,100 from dividends would, in addition to these three deductions, get a dividend credit of 4 percent under existing law, which would mean that their income would have to be \$6,100 before they would be liable to pay a single dollar in taxes. Therefore, those who receive less than these sums would have no withholding applied to them at all.

NO WITHHOLDING ON ELDERLY EXCEPT FOR THOSE WITH LARGE INCOMES

Let us see how much capital they would have to have to get these incomes. If a couple received the maximum social security benefit of \$2,178 and also interest income of \$3,200 a year, the \$3,200 of interest at 4 percent would represent a savings account of about \$80,000. In other words, those receiving the maximum social security benefit and having \$80,000 in savings at 4 percent would not be liable for a single cent in income taxes; therefore, there would be no withholding in their case.

If they received dividends, then their amount would be even greater. Of course, if they do not have any social security and get the \$5,100 at 4 percent, that would be roughly \$125,000. The \$6,100 at a dividend rate of 4 percent would be over \$150,000. So they would not exactly be paupers. Neither widows nor orphans nor old people would be injured by withholding. It is clear that hardship to low income individuals and the aged cannot be used as an excuse for abandoning withholding. There is just no such hardship. Furthermore, withholding would be a simple and efficient means for an individual to pay his taxes on dividends and interest.

NO MAZE OF CONFUSION

It has been claimed that withholding will result in a maze of confusion for the American taxpayers. For the great majority of taxpayers, the only burden caused by withholding would be two additional computations on the tax return—those involved in a simple schedule. In addition to entering the amount of his dividends and interest on the return as at present, the taxpayer would, as a result of withholding, be required to divide this amount by 4, and then add these two amounts together to determine the amount of his dividends and interest to be reported as income and the amount of credit he would be permitted for the withheld tax. This is the extent of the "maze of confusion" for the taxpayer.

For many taxpayers, withholding would actually reduce their paperwork by eliminating the necessity for filing quarterly estimated tax returns.

Those who raise this objection completely ignore the fact that most Americans already operate under a much more complicated withholding system on their wages, with no maze of confusion. It is ignoring reality to say that they will not be able to adapt to the much simpler system for withholding on dividends and interest.

Mr. KEFAUVER. Mr. President, will the Senator from Illinois yield?

Mr. DOUGLAS. I yield.

Mr. KEFAUVER. I have appreciated that part of the Senator's learned address which I have heard. As to withholding, was not the same scare raised about the same type of withholding of the tax on wages in 1940?

Mr. DOUGLAS. I was not then a Member of Congress, being otherwise occupied; but from reading the CONGRESSIONAL RECORD, I know that is true.

Mr. KEFAUVER. I had the privilege of being a Member of Congress. I remember that all the same points were raised, with even more force and vehemence at that time, about the withholding of taxes on salaries, than has been raised about the withholding of taxes on dividends and interest. I have the feeling that with the very liberal amendments which have been suggested, the people would find it even less onerous than they have found the withholding of taxes on salaries to be, and that system has worked out quite well, as we all know.

Mr. DOUGLAS. I thank the Senator from Tennessee. That is exactly my opinion.

ONLY TAX EVADERS AND AVOIDERS WILL BE HURT

Who will be hurt? The people who will be hurt are those who fail to pay the taxes due on their dividend and interest income. They should not obtain exemption by denying to the rest of the community the taxes which they owe.

Perhaps one reason behind the campaign against withholding is that the savings institutions of the Nation get an automatic snowballing of capital from the interest or dividends which they credit to the accounts of the individuals, which are never checked out into the demand deposits of the individual, and

which automatically are added to capital. To the degree that taxes are not paid upon those accounts—and I think they must run into many, many millions of dollars a year—they increase the capital assets of the institutions and enable those assets to snowball much more rapidly by thus using money really owed to the community. In other words, the savings institutions are getting a large degree of their growth on the taxes avoided and evaded by their members.

Mr. President, I ask unanimous consent that a question and answer sheet which I have prepared on withholding contained in a previous Senate speech be printed at the end of my remarks.

The PRESIDING OFFICER. Without objection, it is so ordered.

(See exhibit 6.)

INVESTMENT CREDIT

Mr. DOUGLAS. Mr. President, I had intended to discuss the question of the investment credit at some length, but the Senator from Wisconsin [Mr. PROXMIER] delivered one of the most extraordinary and learned speeches on any tax subject that has ever been delivered in the Senate on the question of the investment credit. I was not privileged to hear all of that speech, but I read it yesterday with close attention, and no fairer, more concise, and yet more accurate, description of the present proposal has ever been given.

Anyone who studies the Proxmire speech of Saturday can only be driven to the conclusion that this is a field which needs to be covered much more carefully than the committee has done.

So I am going to ask unanimous consent that the statements which I have prepared on the investment credit be printed in the RECORD at this point in my remarks. I urge every Member of the Senate and every member of the press to read the great speech of the Senator from Wisconsin.

The PRESIDING OFFICER. Without objection the statements were ordered to be printed in the RECORD, as follows:

THE INVESTMENT CREDIT—THE OPENING OF ANOTHER LOOPHOLE

WHAT THE INVESTMENT CREDIT IS

1. The bill in its present form provides a tax credit of 7 percent on amounts invested in new tangible depreciable property, other than buildings, which is subject to a depreciation life of more than 8 years. There are certain limitations which can be briefly stated: (a) If the life of the property is less than 4 years, no credit will be granted; (b) if the life is from 4 to 6 years, only one-third of the credit (2⅓ percent) will be granted; (c) if the life is from 6 to 8 years, then two-thirds of the credit (4⅔ percent) will be granted. The credit for used property is limited to the first \$50,000 of investment.

2. The bill also provides a 3-percent credit for regulated private utilities such as telephone and domestic telegraph, gas and electric companies.

3. The investment credit can be offset dollar for dollar against taxes owed up to \$25,000 but above that amount may not reduce tax liability by more than 25 percent.

4. The Long amendment adopted by the Finance Committee slightly reduces the effect of these tax credits in later years by providing that the basic cost of the asset

shall not exceed the value of the asset minus the investment credit. Thus, depreciation is limited to 93 percent of the original cost of the asset (97 percent for utilities).

The Department of Commerce estimates that the production of durable equipment in 1961 amounted to \$25.5 billion. A 7-percent reduction in this would amount to \$1¾ billion annually. This would be reduced in practice by the lower rate for the private utilities, the exceptions listed above, and the Long amendment.

It is probably safe to estimate the initial loss of revenue from this feature of the bill at somewhere between \$1.1 billion to \$1.4 billion. We personally believe it will amount to not far from \$1.3 billion.

This measure is advocated by the majority as a means of stimulating industry to improve its plant and machinery, reduce its costs, and by stimulating investment to expand employment and reduce unemployment.

Here it should be noted that the tax credit originally proposed by the administration was on net additional investment, or the amount invested in industry over and above that allowed for depreciation. There would have been strong grounds for supporting such a proposal or one which would have given the credit to increases in investment over the average for a previous 3- or 5-year period. But during its consideration by the House Ways and Means Committee, this proposal was vulgarized almost beyond recognition. Instead of being a bonus for net additional investment or for increased investment, it was transformed into a credit for all investment (aside from buildings) or what may be termed gross investment. Thus, if a company invests less than the physical depreciation of its machinery and equipment, it will still get a 7-percent credit, or a 14-percent tax deduction on this gross investment. To repeat, an actual decrease in investment as compared with the years prior to July 1, 1962, will be rewarded.

WOULD THE INVESTMENT CREDIT APPRECIABLY STIMULATE INVESTMENT?

In other words, by giving the rewards on average gross investment rather than on marginal net investment any possible stimulus to added investment is greatly reduced and in our judgment is very slight indeed. We are confirmed in this opinion by the results of the McGraw-Hill survey in the spring of 1962. The question asked by McGraw-Hill was as follows:

"If the administration's program of tax incentives for investment were enacted, how much would this increase your capital expenditures in 1962?"

In reply to this, business as a whole indicated that it would raise its 1962 plans by only about 1 percent, or about \$300 million. Nine out of every ten companies which replied stated that they would not use such a program in 1962.

Since the bonus under the proposed investment credit will amount to about \$1.1 to \$1.4 billion, this would mean that, out of every dollar which the Government will lose in taxes, less than 30 cents will find its way into increased investment in American industry. This is a very high price to pay for a little stimulus.

The National Industrial Conference Board made a special survey in late March and early April 1962 of the 1,000 largest manufacturing corporations in the United States to determine what effect the 7-percent investment credit would have upon their capital investment. While the influence of the credit on the plans of the companies varied somewhat from industry to industry, the results were that only 8 percent of those responding said they would revise their capital spending for the balance of 1962 if the credit were enacted by mid-1962. Seventeen per-

cent of the reporting companies said they would increase their investments in 1963 if the credit were enacted by the end of the current session of Congress. But the prospective change in the dollar volume of capital spending in 1963 as a result of the credit would be as small as 1 percent.

As the report of the survey states:

"Overall, * * * the increase in 1963 outlays expected on account of the investment tax credit may be small in relation to its potential. In more than half of the industries covered, moreover, the imputed difference was less than 1 percent."¹

There are already more than adequate funds available for investment on the part of corporations which they are refusing to use for this purpose. Thus the July 1962 Survey of Current Business, issued by the Department of Commerce (p. 24), shows that in 1961 American corporations had acquired \$43.1 billion of corporate funds² but invested only \$31.3 billion in equipment and inventories.³ In this one year, therefore, they piled up nearly \$12 billion in liquid assets. There were also very large accumulations of liquid assets in preceding years, amounting to about \$5 billion in 1960 and an equal amount in 1959.⁴ If business conditions did not cause American corporations to invest these huge sums in past years, there is little prospect that the extra bonus of \$1.3 billion will be translated into investment. What is more likely to happen is that the overwhelming proportion will also pass into the cash reserves and swell them still further. There would seem to be little prospect that the investment credit will have any real stimulative effect. It will increase the power and wealth of the already powerful and wealthy.

We should also realize that a very large percentage of plant and equipment now lies idle and unutilized primarily because there is not adequate demand for the goods which could be produced at the prices charged.

The McGraw-Hill index of plant utilization is now at approximately 85 percent. Even though the 15 percent which now lies idle is partially composed of a "standby" reserve or is markedly obsolete, it is still true that the percentage of plant utilized is 5 or 6 percent short of what would be used under full employment. Can it be maintained that, if good machinery and equipment is thus allowed to lie idle because of a shortage in effective demand relative to prices, a bonus on investment would stimulate a still further increase in machinery and equipment? For would not this still further increase the already high percentage of idle equipment?

In addition, it should be realized that, while the purpose of the investment credit is to stimulate economic growth and to help business to compete more effectively in foreign markets, it would in fact be given all the way across the board without regard to the quality or social need for the investment. Thus, the credit would be available for such investments as a new ski-lift at Sun Valley or in Vermont, an escalator in a department store, new farm machinery to spread fertilizer on lands which are already overproducing, klieg lights in a burlesque house, and martini-mixing machines in a bar. Other investments of an even more

questionable nature would receive the bonus.

It is hard to see how this increases our efficiency as compared with other countries or whether this serves meaningful economic growth.

The 3-percent credit which is to go to utilities would be completely wasted and is wholly unnecessary.

The rate of return of the private utilities is regulated by both State and Federal bodies. If regulation is properly carried out, then any favorable tax consequences of the credit would be offset by reductions in the rates charged to consumers.

If not properly carried out, it would be an outright gift to the private utilities, for it would merely increase their rate of return above that set by the regulatory bodies.

In addition, the 3-percent credit for utilities has nothing to do with other stated purposes of the credit, namely, to help modernize industry or to make it more competitive in world markets.

WHO HAS BEEN GETTING THE TAX CUTS?

Let us also note the way in which tax benefits and reductions have been made during these last 8 years. In 1954, accelerated depreciation, with the double declining balance and the sum of the digits methods, was authorized by Congress. This amounted to an initial loss of revenue to the Government of at least \$2 billion a year. This went to the industrial corporations and to the industrialists. At the same time the \$50 dividend exclusion and the 4 percent credit were passed in 1954 which gave \$400 million a year more to the owners of common stocks. This summer the Treasury has issued a new Bulletin F., permitting machinery and equipment to be depreciated much more rapidly. It is estimated that this will reduce business taxes by approximately \$1.5 billion a year. All of these taken together come to just short of \$4 billion a year.

Now we have this provision for the investment credit which will give the investors in machinery and equipment at least another \$1.3 billion annually. Thus, in 8 years we have decreased the annual tax burden on industry by over \$5 billion a year. This, of course, goes to the upper income groups in society who own the overwhelming proportion of the stock of American corporations.

During this period the low- and middle-income groups have received virtually nothing in the way of tax cuts. It is about time that the United States was less partial in its distribution of favors. This is true both on economic and ethical grounds.

INVESTMENT CREDIT A FORM OF THE TRICKLE-DOWN THEORY

The basic way in which investment is stimulated and the economy moved forward is not by granting incentives for increased capital expenditures at a time when the existing plant and equipment is not fully used, but by increasing the demand for the products which the existing plant and equipment can produce which, in turn, will stimulate investment. In other words, the investment credit proposed is really a form of the trickle-down theory of economics which has largely been shown to be ineffective in the past. We believe instead in the theory that purchasing power should be built from the bottom up.

INVESTMENT CREDIT OPENS UP ANOTHER LOOPHOLE

Finally, the investment credit would open up more tax loopholes and would be quickly extended to other fields.

As nearly as possible a proper tax system should be neutral in the way it treats both income and expenditures. If we could have an absolutely just tax system it would probably make no distinctions as to the amount of tax to be paid on income or deductions for expenditures, no matter where the funds

were derived or for what they were spent. It is the failure to carry out this principle which has so eroded our present tax system and which has made it so unjust.

For example, income from a wage or salary, in general, is taxed at the full rate, but income from oil, or from stock options, or from the cutting of timber, or from dividends, or from gains on the stock market, or from the sale of real property, among others, is taxed at lower rates and has special privileges not afforded to income from a wage or salary.

On the expenditure side, money spent for entertainment expenses, for business expense accounts, including yachts, club dues, and so forth, are deductible from taxable income, while the expenses of an ordinary person driving to and from work, or the payment of rent, or expenditures for the recreation or education of one's children are not deductible. These privileges for deductions and allowances go almost entirely to the strong, the powerful, and the well-to-do, and favor high-income groups and unearned income as opposed to low income groups and earned income.

The main purpose of tax reform is to try to modify or to do away with some of these inequities and privileges in the tax laws.

What the investment credit does is to say that for social purposes we should give a special tax privilege for funds used to buy most kinds of depreciable property. At least as good a case can be made that society would be as wise to allow deductions for money spent for the education of children, for a future pension, or for preventive medicine rather than for capital investment.

Every legislator is pressed almost daily by some constituent or interest group to vote for a tax reduction for their particular interest. Once we start on this road it is almost impossible to stop. For this reason alone it is very unwise to give a special deduction for funds which are spent in this particular way; namely, for capital investment. It would be equally unwise to give deductions for most of these other proposals.

If the 7-percent tax credit is allowed on machinery and equipment, it will be only a short time before it will be granted on plant and buildings, and this will amount to another revenue loss of not far from \$1.5 billion. Indeed, proposals to this effect have already been made. Residential construction would not be left behind for long and this would take another \$1.5 billion away from our revenue. It would also be inevitable that the principle of H.R. 10 would find its way into enactment, and moneys devoted to purchasing voluntary retirement plans would be exempted from taxation. So would expenditures to educate children in college.

The final result would be that only income spent for current consumption would be taxed. This would be a kind of sales tax which would be highly regressive in nature and would weigh proportionately far more heavily upon those with lower or middle incomes than upon those with large resources. State and local taxation is already highly regressive. This is only made bearable by the fact that Federal taxation is progressive and hence introduces a kind of rough proportionality over the range of most incomes. To make Federal taxation also regressive or less progressive would in our opinion be grossly unjust. And yet that is precisely the end result toward which the opening of these loopholes would tend. We cannot acquiesce in these tendencies however well intentioned they may be.

NOT ORIGINAL CREDIT

Mr. DOUGLAS. The present investment credit differs very markedly from the original investment credit proposed by President Kennedy and the administration. The original proposal was for

¹ The Business Record, National Industrial Conference Board, August 1962, p. 19.

² Made up as follows (in billions of dollars): Retained profits, \$7.3; depreciation, \$24.8; sale of stocks, \$4.5; sale of bonds, \$5.1.

³ Made up of \$29.6 billion in plant and equipment and \$1.8 billion in inventories.

⁴ John K. Landrum seems to come to the same general conclusion, although with somewhat smaller increases in liquid funds. See his Corporate Profits and Cash Flow supplement to testimony before Joint Economic Committee, Aug. 10, 1962, p. 1.

a 15 percent investment credit on amounts invested in excess of depreciation charges, plus 6 percent on amounts invested between 50 percent of depreciation and 100 percent of depreciation.

Let me illustrate what that proposal was. Suppose a company invested \$150,000 and that its depreciation charges were \$100,000. The original proposal would have provided to this company an investment credit of 15 percent on the \$50,000, excess of the actual investment over the \$100,000 of depreciation, or \$7,500, and 6 percent on the difference between the 50-percent depreciation and the 100-percent depreciation, or \$3,000. So the total investment credit would have been \$10,500.

ORIGINAL CREDIT ON NET INVESTMENT

The emphasis throughout was placed upon net investment—investment in excess of depreciation. It was designed to stimulate net investment, or what perhaps could be called, in economic terms, a form of marginal investment. I think it would have been still better if the investment credit had been paid on the increase in the amount of investment over the average for a preceding period of years. That would have been truly a stimulation of additional or marginal investment.

Mr. GORE. Mr. President, will the Senator yield?

Mr. DOUGLAS. I yield.

Mr. GORE. Is it not true that under either the provisions of the original investment credit proposal or the suggestion which the able Senator has just now made, a specific treatment would be provided? Either of the provisions would be designed strictly for the encouragement of investment in improved plant and production facilities?

Mr. DOUGLAS. Exactly so.

Mr. GORE. Over and beyond the normal depreciation allowance therefor?

Mr. DOUGLAS. That is correct.

Mr. GORE. But as the provision now comes to the Senate, it is available to anyone for almost any purpose—slot machines or elevators in downtown garages. Can the Senator think of any particular facility that would not qualify?

Mr. DOUGLAS. The credit would be pretty broadly granted. Quantitatively, the present provision is for a 7-percent investment credit on what can be termed gross investment in machinery and equipment—the credit is for gross investments even though they are less than the depreciation, and even though the investment is less than it has been in preceding years.

Mr. LAUSCHE. Mr. President, will the Senator from Illinois yield?

Mr. DOUGLAS. I am glad to yield.

Mr. LAUSCHE. Does the right to obtain the credit have any relationship in this bill to the depreciation fund which has been established?

Mr. DOUGLAS. None at all.

Mr. LAUSCHE. In other words, the depreciation allowance would be granted, regardless of that?

Mr. DOUGLAS. That is correct.

Mr. LAUSCHE. And I assume it would be granted in anticipation that it would be used to replace obsolete and worn out equipment; is that true?

Mr. DOUGLAS. That is correct.

Mr. LAUSCHE. But this credit would be made available on the basis of the amounts which normally would have been reinvested out of the depreciation account, as well as out of the new investments induced because of the credit?

Mr. DOUGLAS. That is absolutely correct.

Mr. President, let us consider a firm with \$100,000 of depreciation. If it invested only \$50,000 it would be allowed a credit of 7 percent of that amount, or \$3,500, even though it failed by 50 percent to meet the actual depreciation charges. If last year it invested \$75,000 and this year reduced that investment to \$50,000, it would get its 7 percent of the \$50,000. In other words, it would get a 7-percent credit of its gross investment, not net investment, not increased investment, but total investment, regardless of whether it was made—as in most cases it would have been—whether the credit was in the law or not.

CORPORATIONS HAVE AMPLE INVESTMENT FUNDS

I believe it should be noted—as the Senator from Wisconsin [Mr. PROXMIRE] pointed out in his very able speech on Saturday—that the cash and liquid funds of U.S. corporations are “running out of their ears.” The July 1962 Survey of Current Business shows, on page 24, that in 1961, American corporations had acquired \$43.1 billion of corporate funds but invested only \$31.3 billion in equipment and inventories. In this one year, therefore, they piled up nearly \$12 billion in liquid assets. There were also very large accumulations of liquid assets in preceding years, amounting to about \$5 billion in 1960 and an equal amount in 1959. If business conditions did not cause American corporations to invest these huge sums in past years, there is little prospect that the extra bonus of \$1.3 billion—which this investment credit would give—will be translated into investment. What is more likely to happen is that the overwhelming proportion will also pass into the cash reserves and swell them still further. There would seem to be little prospect that the investment credit will have any real stimulative effect. It will increase the power and wealth of the already powerful and wealthy.

As I think the chairman of the committee once said, there would be a big subsidy to big business. I want to applaud the chairman of the committee for making that statement.

We should also realize, as the Senator from Wisconsin [Mr. PROXMIRE] pointed out, that a very large percentage of plant and equipment now lies idle and unutilized primarily because there is not adequate demand for the goods which could be produced at the prices charged.

The McGraw-Hill index of plant utilization is now at approximately 85 percent—meaning that 15 or 16 percent now lies idle. Even though the 15 percent which now lies idle is partially composed of a standby reserve or is markedly obsolete, it is still true that the percentage of plant utilized is 5 or 6 percent short of what would be used under full employment. Can it be maintained that, if good machinery and equipment

is thus allowed to lie idle because of a shortage in effective demand relative to prices, a bonus on investment would stimulate a still further increase in machinery and equipment? For would not this still further increase the already high percentage of idle equipment?

In addition, it should be realized that, while the purpose of the investment credit is to stimulate economic growth and to help business to compete more effectively in foreign markets, it would in fact be given all the way across the board without regard to the quality or social need for the investment. Thus, the credit would be available for such investments as a new ski-lift at Sun Valley or in Vermont, an escalator in a department store, new farm machinery to spread fertilizer on lands which are already overproducing, klieg lights in a burlesque house, and martini-mixing machines in a bar. Other investments of an even more questionable nature would receive the bonus. Indeed, there might be investments in depreciable equipment in places of even more questionable reputation—in houses which are not homes; and they would receive the bonus.

It is hard to see how this increases our efficiency as compared with other countries or whether this serves meaningful economic growth.

WHO HAS BEEN GETTING THE TAX CUTS?

Let us also note the way in which tax benefits and reductions have been made during these last 8 years. In 1954, accelerated depreciation, with the double declining balance and the sum of the digits methods, was authorized by Congress. This amounted to an initial loss of revenue to the Government of at least \$2 billion a year.

Although this may be made up later by the individual investments, there is an ultimate net loss to the Treasury, because of the fact that the initial loss never is made up subsequently. During these early years there is a postponement or forgiveness.

This \$2 billion a year—and I believe that is a modest figure to use in that connection—went to the industrial corporations and to the industrialists. At the same time the \$50 dividend exclusion and the 4-percent credit were passed in 1954 which gave \$400 million a year more to the owners of common stocks. This summer the Treasury has issued a new Bulletin F, permitting machinery and equipment to be depreciated much more rapidly. It is estimated that this will reduce business taxes by approximately \$1.5 billion a year. All of these taken together come to just short of \$4 billion a year.

Let me say, in connection with the revision of Bulletin F, that I do not object to it, because I think the previous allowance given for obsolete machinery and equipment did not sufficiently take care of actual obsolescence, and therefore it is proper to have the allowance made sufficient to take care of obsolescence. But I understand that the Senator from Oklahoma claimed, earlier today, that because one approves of that revision of Bulletin F, one must also approve of the proposed investment credit. However, I

disagree, for certainly those are two entirely different things.

Now we have this provision for the investment credit which will give the investors in machinery and equipment at least another \$1.3 billion annually. Thus, in 8 years we have decreased the annual tax burden on industry by over \$5 billion a year. This, of course, goes to the upper income groups in society who own the overwhelming proportion of the stock of American corporations.

During this period the low- and middle-income groups have received virtually nothing in the way of tax cuts. It is about time that the United States was less partial in its distribution of favors. This is true both on economic and ethical grounds.

INVESTMENT CREDIT A FORM OF THE TRICKLE-DOWN THEORY

Mr. President, in my judgment, the basic way in which investment is stimulated and the economy moved forward is not by granting incentives for increased capital expenditures at a time when the existing plant and equipment is not fully used, but by increasing the demand for the products which the existing plant and equipment can produce which, in turn, will stimulate investment. In other words, the investment credit proposed is really a form of the trickle-down theory of economics which has largely been shown to be ineffective in the past. I would have expected this theory to be advanced from the other side of the aisle, because from the time of Hamilton, the Republican Party has believed in giving wealth and power to those who already have wealth and power, on the theory that they know what is best for mankind, and also that the favors they will receive will be passed down. But the historical principles of the Democratic Party from Jackson on have been to build up purchasing power from the bottom, on the theory that if the great mass of Americans are made prosperous, whether they be wage workers, salaried employees, small businessmen, farmers, or professional men, the rest of society becomes prosperous because there is an effective demand for goods, and there will be a stimulation in demand, investment, production, invention, and the rest.

BELIEVE IN SHARING THE BURDENS

This was not only the theory of Jackson; it was the theory of William J. Bryan when he remade the Democratic Party. That tradition was carried on by Woodrow Wilson, Franklin Roosevelt, and Harry Truman. I would dislike to see it abandoned now by the congressional leaders of the Democratic Party. We do not favor class antagonism. As the Senator from Louisiana said the other day, we are not wealth sharers; we do not believe in sharing the wealth; but we believe in sharing the burdens and we believe that the burdens should be shared in some proportion to ability to pay. We believe that purchasing power should, in the main, be built from the bottom up.

There is one final point on which I wish to speak.

Mr. PROXMIRE. Mr. President, before the Senator leaves that subject, will he yield briefly?

Mr. DOUGLAS. I yield.

Mr. PROXMIRE. In addition to the opposition to the investment credit on the very firm ground to which the Senator has referred as the trickle-down theory, is it not also true that there is opposition to the investment credit on the part of highly conservative people of very high integrity, on the ground that this is an unconscionable subsidy or giveaway because it provides for depreciation in excess of 100 percent, which is in violation of sound tax principles, and the only other such exception in our tax laws is in regard to mineral depletion?

Mr. DOUGLAS. That is true. Many conservatives of great integrity, such as the distinguished Senator from Virginia, object to the plan on the ground that they regard it as an unconscionable subsidy. The Senator from Louisiana [Mr. Long] persuaded the Finance Committee to adopt an amendment which somewhat mitigated the effect when he provided that the 7 percent could not be taken in depreciation, or, in other words, that the basis be reduced to 93 percent.

Mr. PROXMIRE. That is, depreciation would be 107 percent, instead of 114 percent.

Mr. DOUGLAS. I think the Long amendment would permit no more than 107 percent.

Mr. PROXMIRE. The conclusion of the Senator from Wisconsin—and I have gone over this question very carefully with a number of economists—is that unless the Long amendment should be extended to 86 percent—in other words, the base should have to be reduced, not to 93 percent, but to 86 percent, there would still be a depreciation in excess of 100 percent.

Mr. DOUGLAS. I believe that the Senator from Wisconsin is correct.

Mr. PROXMIRE. I would like to ask the Senator one other question—because I think this point was not adequately developed by the Senator from Wisconsin when he spoke on this subject the other day—and that is with regard to the justification for investment credit for utilities.

Mr. DOUGLAS. I am pleased the Senator from Wisconsin has mentioned that. There is a 3-percent investment credit for most utilities, though, interestingly enough, the report, on page 155, points out that gas pipelines are to get 7 percent. I think the Senator from Tennessee, earlier in the afternoon, got the Senator from Oklahoma to admit that.

NO JUSTIFICATION FOR UTILITIES

What justification can there be for investment credit to private utilities regulated by public regulatory bodies? The public regulatory bodies have to allow a rate which will not only meet operating expenses, but also rate of return on capital investment sufficient to induce adequate investment. It is very rare that a return of less than 7½ percent is allowed on the rate basis. In

other words, there is already a guaranteed return to the electrical companies, telephone, gas, and pipeline utilities. Three of these are to be given an additional 3 percent and the gas pipelines are to get 7 percent. Trust the big gas operators to get in with all four feet in the trough.

It is said that this subsidy could be recovered later by reducing rates. That would be somewhat difficult to bring about. There are 51 different regulatory bodies in this country. We all know that the regulatory bodies, in a large percentage of cases, are controlled by the groups which they are supposed to regulate. It is very dubious whether there would be a reduction in rates comparable to the subsidy granted, and this would, therefore, largely be a windfall. It will probably mean more than \$200 million a year to the private utilities of the Nation. This is indeed an unjustifiable giveaway.

A.T. & T. DOES NOT WANT IT

Let it be said about one of the great utilities, the American Telephone & Telegraph Co., that it does not want the subsidy. I heard the two Senators from Tennessee make a very eloquent analysis of how A.T. & T. would profit from the satellite communications system which Congress established. I started on the fence in that discussion. My mind was not made up. As the discussion went on, I became convinced however that they were correct. I am very proud that I stayed with them and walked the last mile, even though it was to defeat and apparent disaster.

But we should give the A.T. & T. its due. They stand to invest next year over \$2½ billion on their planned investments which they worked out long before this proposal was made, and they stand to collect about \$75 million in subsidies if this provision goes through. But the leaders of A.T. & T. had the courage and public spirit to come before our Finance Committee and say they did not want the money, that they would feel ashamed in taking the money, that it was not necessary for them to make the investment they were going to make. So they deserve much credit, and when they are arraigned before St. Peter, and perhaps the two Senators from Tennessee are the prosecuting attorneys, in mitigation of the sentence which St. Peter might pass upon them, they can plead the fact that, on the question of investment credit, they stood up like public-spirited men and said they did not want the subsidy.

Mr. GORE. Mr. President, will the Senator yield?

Mr. DOUGLAS. I yield.

Mr. GORE. In any prospective or possible fanciful proceeding before St. Peter, the Senator from Tennessee would like to be a defender.

Mr. DOUGLAS. Probably we shall all be defendants.

Finally, Mr. President, we talk a great deal about closing loopholes. The President started with a very modest plan to close a few of the loopholes. Most of them are still open.

LOOPHOLES REMAIN

The lobbying loophole has been widened. The loophole of the 4 percent dividend credit is to be continued. The loophole on depreciable real estate is not to be closed. The loophole on non-collection of taxes on dividends and interest is still to remain. The expense account loopholes still largely remain. A lobbying loophole has been opened up.

Most of the great loopholes are to continue. But the investment credit will add another loophole. It will not only be a loophole, but also it will be a direct inducement for other loopholes.

Mr. President, as nearly as possible a proper tax system should be neutral in the way it treats both income and expenditures. If we could have an absolutely just tax system it would probably make no distinctions as to the amount of tax to be paid on income or deductions for expenditures, no matter where the funds were derived or for what they were spent. It is the failure to carry out this principle which has so eroded our present tax system and which has made it so unjust, against which the present Assistant Secretary of the Treasury, Mr. Stanley Surrey, has been the most scholarly and the most authoritative crusader as a private student.

For example, income from a wage or salary, in general, is taxed at the full rate, but income from oil, or from stock options, or from the cutting of timber, or from dividends, or from gains on the stock market, or from the sale of real property, among others, is taxed at lower rates and has special privileges not afforded to income from a wage or salary.

On the expenditure side, money spent for entertainment expenses, for business expense accounts, including yachts, club dues, and so forth, are deductible from taxable income, while the expenses of an ordinary person driving to and from work, or the payment of rent, or expenditures for the recreation or education of one's children are not deductible. These privileges for deductions and allowances go almost entirely to the strong, the powerful, and the well-to-do, and favor high income groups and unearned income as opposed to low income groups and earned income.

The main purpose of tax reform is to try to modify or to do away with some of these inequities and privileges in the tax laws.

What the investment credit does is to say that for social purposes we should give a special tax privilege for funds used to buy most kinds of depreciable property. At least as good a case can be made that society would be as wise to allow deductions for money spent for the education of children, for a future pension, or for preventive medicine rather than for capital investment.

Every legislator is pressed almost daily by some constituent or interest group to vote for a tax deduction for their particular interest. Once we start on this road it is almost impossible to stop. For this reason alone it is very unwise to give a special deduction for funds which are spent in this particular way; namely, for capital investment. It would be equally

unwise to give deductions for most of these other proposals.

OTHER LOOPHOLES PROPOSED

Mr. President, the other day I wrote this:

If the 7-percent tax credit is allowed on machinery and equipment, it will be only a short time before it will be granted on plant and buildings.

Since then I am told an amendment has been proposed to extend the credit to plant and buildings. This would mean another \$20 or \$25 billion a year, and would result in the further tax loss of \$1.5 billion.

If this credit is to be granted on machinery and equipment, it is argued, why not on buildings? Are they not as much a part of capital as is machinery?

If this were to be done, factories, shops, and barns would soon follow, and it would be only a little time before it would be proposed for residential construction. That would take more hundreds of millions of dollars from our tax revenues.

H.R. 10 IN OFFING

Furthermore, we have already seen the proposed reintroduction of the Keogh bill, otherwise known as H.R. 10, which would give deductions for payments of sums into voluntary retirement funds by self-employed persons. This might be called the doctors' and lawyers' amendment.

This was all set to go through the Senate last year, during the month of September. It had been reported by the Finance Committee. The Treasury Department did not oppose it at that time. The way was greased.

The junior Senator from Tennessee and the Senator from Illinois served notice that if it were proposed they would give it thorough discussion. I suppose, had we done so, that would have been called a filibuster by the proponents, and the steamroller would have been put into action, but so long as we had enough strength we would have resisted that procedure. Since there was great pressure for adjournment, it was decided not to bring up H.R. 10. It has since resided in what Grover Cleveland would call innocuous desuetude ever since.

Only a few days ago the distinguished minority leader [Mr. DIRKSEN] issued a press release saying that he was going to revive it, although I am told he made a statement some years ago that H.R. 10 would plow a tremendous hole in our revenue system and would ultimately lose \$3½ billion in revenue.

That issue is coming up, and those who favor a 7-percent-investment credit cannot logically deny to the lawyers and doctors an exemption for amounts contributed to voluntary pension funds, although we have seen that there is quite a liberal tax exemption for pensions later.

And if H.R. 10 goes into effect similar exemptions will be proposed for the purchase of other voluntary plans, for laying up sums of money to send children to college, and for accumulating funds for medical expenses.

The final result would be that only income spent for current consumption

would be taxed. This would be a kind of sales tax which would be highly regressive in nature and would weigh proportionately far more heavily upon those with lower or middle incomes than upon those with large resources. State and local taxation is already highly regressive. This is only made bearable by the fact that Federal taxation is progressive and hence introduces a kind of rough proportionality over the range of most incomes. To make Federal taxation also regressive or less progressive would in our opinion be grossly unjust. And yet that is precisely the end result toward which the opening of these loopholes would tend. We cannot acquiesce in these tendencies however well intentioned they may be.

PANDORA'S BOX

Pandora's box, already partly open, will be wide open, and all the evils of exemption will flood forth upon the Senate floor. It will require the ingenuity and oratory of the Senator from Oklahoma, having opened the door for tax favors for investment in machinery and equipment, to bar the door for private pension plans, for education and all the rest.

If anyone can take an illogical position and get away with it, it is my good friend from Oklahoma. Logical consistency has never restrained him, and I am sure it will not restrain him now. If he gets the 7-percent-investment credit and the eloquent Senator from across the aisle proposes H.R. 10, or the Keogh bill, this will add to the amusement and gaiety of the Senate and of the Nation as the Senator from Oklahoma strives to distinguish between the two. I am sure that in his characteristic fashion, like Houdini, he will escape from the logical irons which will encircle him, but it will be an extraordinary exercise in lock breaking when he does.

I think he did it a couple of years ago. I think the Senator from Oklahoma has been on both sides of H.R. 10. I remember that at one time he made a point of order against a ruling I made. I happened to be the Presiding Officer at the time. His appeal killed H.R. 10.

Then upon occasion I think he supported H.R. 10. I understand that this year he will oppose H.R. 10.

Mr. KERR. Mr. President, will the Senator yield?

Mr. DOUGLAS. I am glad to yield for a question but not for a speech, because I cannot speak as well as does the Senator. I will yield for a question.

Mr. KERR. If the Senator illustrates by setting forth an occasion on which he and I were on both sides of H.R. 10—

Mr. DOUGLAS. No, I was not on the opposite side. I made a parliamentary ruling.

Mr. KERR. Then we are on opposite sides now. By reason of the position that the Senator from Oklahoma took on that occasion and then reversed himself, would it not necessarily follow that the Senator from Illinois likewise reversed himself, since we are still on opposite sides of the question?

Mr. DOUGLAS. No; I happened to be in the chair, and though I was opposed to H.R. 10—

Mr. KERR. I thought the action was premeditated.

Mr. DOUGLAS. I ruled that the motion of the sponsors of H.R. 10 was in order. The Senator from Oklahoma appealed from the ruling of the Chair, and my parliamentary ruling was reversed. I voted to uphold the appeal from the Chair.

Mr. KERR. I beg the Senator's pardon. I believe the Senator voted against upholding the appeal.

Mr. DOUGLAS. That is right. I voted for my own ruling.

Mr. KERR. I can understand that. I compliment the Senator on his consistency.

Mr. DOUGLAS. Exactly. Now the Senator is accusing me of being self-righteous again.

Mr. KERR. Oh, not again—still.

Mr. DOUGLAS. When I am in the chair, I do not rule according to what I have done. I rule according to what I think are the equities in the parliamentary law of the case. I try to adhere to what I consider to be right—to my own hurt, if that be necessary—but I do not take advantage of parliamentary subterfuge to achieve my own purpose.

Mr. KERR. Mr. President, will the Senator yield?

Mr. DOUGLAS. I will yield for a question, but not for a speech, because I am no match for the Senator in verbal quickness.

Mr. KERR. Is the Senator taking the position that he was any more accurate in the ruling he made than the Senator from Oklahoma was in the appeal from the ruling of the Chair, in view of the fact that the Senator from Oklahoma did not agree with the ruling which the Senator made?

Mr. DOUGLAS. I do not wish to be led into digression with regard to bygone days. I merely wish to say that the Senator from Oklahoma has been on all sides of H.R. 10, just as my good friend, the minority leader, has been on all sides of H.R. 10. I think he is now about to make the full reversal—a revolving-door type of movement—and having made the revolution two or three times, he is about to come around again.

Mr. KERR. Mr. President, will the Senator yield for a question?

Mr. DOUGLAS. The Senator may ask a question, but not make a speech.

Mr. KERR. If the Senator from Illinois states that the Senator from Oklahoma was opposed to him before when a parliamentary situation was proposed to him, and he is now opposed to the Senator from Oklahoma on a legislative situation, if they were on opposite sides then and on opposite sides now, has not the Senator from Illinois made as complete a revolution?

Mr. DOUGLAS. No. I intend to vote against the Keogh bill, or H.R. 10. If the Senator from Oklahoma opposes H.R. 10, I will support him. I shall support not only the Senator from Virginia [Mr. BYRD] when he is right, but also the Senator from Oklahoma [Mr. KERR] when he is right.

Mr. KERR. Praise God.

Mr. DOUGLAS. It does not happen very often. Once in a while the Senator from Oklahoma is right.

Mr. KERR. A new day has dawned.

CONCLUSION

Mr. DOUGLAS. Mr. President, on balance, the bill as reported by the Finance Committee is a poor one. Although there are worthwhile sections in the bill these are hardly sufficient to outweigh those sections which are, either in whole or in part, faulty.

As we have already pointed out, many of the President's major recommendations have been ignored or watered down. The committee has chosen to strike the withholding provision, which was passed by the other body. It has failed to include in the bill such obviously needed reforms as the repeal of the dividend credit and exclusion as recommended by the President. In almost every instance, expense accounts and foreign operations, for example, where the committee did approve a section or provision recommended by the President and adopted by the House, that provision has been materially weakened.

As if the emasculation of many of the President's major recommendations were not enough, the Finance Committee has added, by way of afterthought, several rather petty addenda to the bill. Sections 21 through 26 really have no place in this bill. Some of these additions are really private bills masquerading as general legislation, while others are of such minor consequence that they have far too little stature to warrant their consideration in this bill when so many more important subjects are being left to a later, more general, tax reform bill.

The Senate must now proceed to a painstaking examination of each provision contained in the bill.

Thank the Lord, the junior Senator from Tennessee [Mr. GORE] refused to give unanimous consent to have the amendments of the committee agreed to en bloc. They will now have to be considered individually. The burden of proof will pass from those of us who are trying to defend the President's program to those who are trying to defeat the President's program. The issues at stake can then be shown in their real light.

Possibly the press may wake up as to who is defending the President and who is opposing the President. I hope that the Wall Street Journal is not correct in its prophecy of this morning that the Democratic leadership will move "with harsh parliamentary tactics against liberal efforts to restore some of President Kennedy's recommendations to the Senate Finance Committee version of the tax bill."

Mr. MANSFIELD. Mr. President, will the Senator yield?

Mr. DOUGLAS. I yield.

Mr. MANSFIELD. That statement was read this morning by the Senator from Wisconsin. I stated at the time that I had not seen the story and that the allegations contained in it were not true. I had not discussed the subject with the Senator from Minnesota [Mr. HUMPHREY], whose name was mentioned, or with the Senator from Florida [Mr. SMATHERS], with whom I would discuss it along with the Senator from Minnesota. I do not know what the source of the story was. I can only say that the

story is untrue. No agreement was made. No procedure was agreed to.

I did see a staff reporter of the Wall Street Journal about 1 o'clock on Saturday, at which time he asked me what procedure would be followed in connection with the bill. My answer was that I did not know.

Mr. DOUGLAS. I thank the Senator from Montana. I am greatly reassured by his statement. I think it is excellent.

Now I appeal to the leadership of the Democratic Party in the Senate to help us restore the President's original proposal and get a Kennedy tax bill through the Senate.

Mr. President, I yield the floor.

EXHIBIT 1

[From the Washington Post, Aug. 27, 1962]

COALITION OPENS FIGHT ON TAX BILL—LIBERALS GET HELP OF CONSERVATIVES TO REVAMP PLAN

(By Andrew J. Glass)

A powerful array of liberal and conservative Senators are lined up to battle today against the administration-sponsored tax-revision bill.

Although acting from different motives, the two groups have a common aim: To scuttle President Kennedy's tax legislation unless their views prevail.

In opposition on the left are such liberal stalwarts as Senators PAUL H. DOUGLAS, Democrat, of Illinois, ALBERT GORE, Democrat, of Tennessee, EUGENE MCCARTHY, Democrat, of Minnesota, and WILLIAM PROXMIRE, Democrat, of Wisconsin.

Joining them from the other side of the political spectrum are such figures as Senator HARRY F. BYRD, Democrat, of Virginia, chairman of the Senate Finance Committee, and Senator JOHN J. WILLIAMS, Republican, of Delaware, the ranking GOP member on the finance group.

The liberals are primarily upset by the billion-dollar business investment credit provision. From their standpoint, this is a giveaway from an administration that already has been overly kind to business while being repaid with abuse.

These Senators are also out to put the toughly written administration expense account clause in the Senate version of the bill and enact the House-passed 20 percent withholding on dividends and interest.

For differing reasons, the conservative camp is also unhappy over the 7½ percent investment credit to business. As the Senate tax bill now reads, it will cost the Treasury upwards of \$750 million a year in lost revenue, they maintain.

Adamantly opposed to budgetary deficits, the faction led by BYRD feels the investment credit must go if the measure is to retain its "fiscal responsibility."

This double-barreled attack is sure to pose new problems for Senate Majority Leader MIKE MANSFIELD (Democrat, of Montana). His timetable now calls for at least a full week on the complex 390-page tax measure.

So far, MANSFIELD has declined to state the leadership's position on a host of amendments to the tax bill being offered from both the left and the right.

His strategy is to try to fashion a behind-the-scenes compromise that will lead to passage of the Kennedy measure with its loophole-closing provisions, at least, intact.

On the rest of it, including the key investment credit provision, predictions were, at best, hazardous. But it looked like the investment credit, which has the support of ROBERT S. KERR (Democrat, of Oklahoma), would make it and the withholding attempt would fail.

"The President proposes, the Congress disposes," Senator MANSFIELD said, indicating

that the leadership would be playing its cards carefully right up to the actual voting.

EXHIBIT 2

[From the Washington Post, Aug. 25, 1962]

A VERY HAPPY UNION

It has often been observed that politics makes strange bedfellows, but even the most cynical observers must be somewhat astonished by the decision of Senators DOUGLAS and GORE to join forces with Senator HARRY F. BYRD in opposing the administration's tax bill and especially by Senator DOUGLAS' characterization of this strange coalition as "a very happy union which promises increased strength as we move along."

As supporters of the administration's original tax proposals, we share the Senators' dissatisfaction with the emasculated creature that was hatched by the Finance Committee. It is true that the investment-credit plan has been "vulgarized almost beyond recognition" and that it is now more a credit for gross, rather than net, new investment. And we agree that information returns are not a substitute for the dividend-interest withholding provisions which the Senate Finance Committee eliminated in a cowardly abrogation of its duty to strengthen the enforcement of existing tax laws. Nor are we happy with the toothless provisions of the House and Senate bills which deal with expense accounts and lobbying expenditures.

But none of these shortcomings seems to justify the obstructive course of action to which Senators DOUGLAS and GORE appear to be committed. The investment credit provisions will stimulate economic activity after personal income taxes are cut, and however weak the loophole-closing provisions are, they constitute steps in the right direction.

Tax reform in a representative democracy can proceed only at snail's pace. And progress will be even slower if its liberal supporters insist upon tossing the baby out with the bath water.

EXHIBIT 3

[From the Wall Street Journal, Aug. 27, 1962]

LIBERAL TAX BILL AMENDMENTS FACE DEFEAT IN SENATE—DEMOCRATIC CHIEFS TO FIGHT BID TO RESTORE PROPOSALS THAT PRESIDENT HAD URGED—DEBATE WILL RESUME TODAY

WASHINGTON.—Senate Democratic leaders plan to employ harsh parliamentary tactics against liberal efforts to restore some of President Kennedy's recommendations to the Senate Finance Committee's version of the tax revision bill.

In an attempt to complete Senate action on the measure before the Labor Day weekend, the Democratic leadership—acting with the tacit acquiescence of the administration—will try to table, or kill, most, if not all of the Kennedy proposals being offered by liberal Democratic Senators as amendments to the bill. Because a tabling motion is not debatable, this tactic tends to accelerate action by the slow-moving Senate. Debate on the measure began Saturday afternoon and will continue today.

The seemingly incongruous spectacle of Mr. Kennedy's chief Senate lieutenants using a parliamentary buzz saw to cut down the President's tax proposals stems from a realistic appraisal of the Senate situation by Majority Leader MANSFIELD, Democrat, of Montana; Assistant Majority Leader HUMPHREY, Democrat, of Minnesota, and Senator KERR, Democrat, of Oklahoma, floor manager of the bill.

They believe the Finance Committee version of the bill is the most the administration can hope for in the Senate, even though it resembles the original Kennedy tax program far less than the measure passed by the House last March. In fact, the final ver-

sion of the bill most likely to emerge from a Senate-House conference is expected to be along the lines of the Finance Committee measure.

MOVE TO SAVE TAX CREDIT

Rather than expend their energy during this week's Senate debate in a time-consuming and fruitless drive to adopt such Kennedy proposals as the House-passed plan for 20 percent tax withholding on dividends and interest income, Senators MANSFIELD and HUMPHREY want to concentrate on saving the one big administration provision that survived in the Finance Committee. This is a tax credit that would permit businessmen to reduce their tax payments by as much as 7 percent of the cost of newly purchased equipment.

The Democratic leaders probably will be able to kill all the liberal-sponsored amendments without much trouble and retain the investment credit with a bit more difficulty. What really worries them is a last-ditch effort to attach to the tax bill a long-stalled measure that would permit self-employed persons to claim tax deductions for their contributions to pension funds. It is entirely conceivable the Democratic leaders will fail in an attempt to table this Treasury-opposed measure, cosponsored by Representative KEOGH, Democrat, of New York, and Senator SMATHERS, Democrat, of Florida.

Apart from the fight over the Keogh-Smathers bill, the effort to rewrite the Finance Committee's tax revision bill on the Senate floor will be spearheaded by Senators DOUGLAS, Democrat, of Illinois, and GORE, Democrat, of Tennessee, the Finance Committee's two most liberal members.

In an unusual alliance, they will join Chairman HARRY BYRD, Democrat, of Virginia, of the Finance Committee to try to strip the investment credit from the bill. Conservative BYRD agrees with Liberals GORE and DOUGLAS that the tax relief scheme is a windfall for certain businessmen. But the Democratic leaders, with some Republican help, including probable support from Minority Leader DIRKSEN, Republican, of Illinois, believe they can keep the investment credit in the bill with some 10 votes to spare.

LIBERALS HAVE FOUR MAIN GOALS

Aside from their monetary alliance with Senator BYRD to fight the investment credit, Senators DOUGLAS and GORE will be occupied mainly with trying to restore some of Mr. Kennedy's original recommendations. These will be their four major efforts:

Restoration of the dividend and interest withholding scheme. Under Senator BYRD's leadership, the Finance Committee adopted an alternative plan that would require financial institutions and corporations to report to both the taxpayer and the Government their dividend or interest payments of \$10 or more to one person in 1 year.

Adoption of Mr. Kennedy's original proposal that income by U.S.-owned foreign subsidiaries be subject to U.S. taxation in the year it which it is earned; taxation of such income currently is deferred until it is returned to this country in the form of dividends to the parent corporation. Both the House and the Senate committee adopted less sweeping plans, intended primarily to subject to immediate taxation the income of what the Treasury calls "tax haven" operations—nonmanufacturing subsidiaries located in low-tax countries for the purpose of avoiding immediate taxation in the United States.

Restoration of the House-passed provision imposing relatively tight restrictions on tax deductions for business entertainment intended to generate good will among customers and clients. The Senate committee bill would permit considerable leeway in claiming entertainment costs as tax deduction as long as the costs are associated with the taxpayer's trade or business.

And elimination of an administration-opposed provision, contained in both the House and Senate committee bills, permitting businessmen to claim tax deductions for a wide variety of lobbying expenses.

Because the dividend and interest withholding provision has been so stoutly advocated by the administration and was championed by Mr. Kennedy as recently as his news conference last week, Senator MANSFIELD is somewhat reluctant to use the tabling procedure against it. The tabling motion in this case might be offered by Senator BYRD rather than a member of the leadership.

In any event, the leadership is anxious to avoid a rollcall vote on withholding. Because the proposal is certain to be killed on the Senate floor, the Democratic leaders see no reason why their party's Senators should be forced to go on record regarding such a politically unpopular scheme in an election year.

But the leadership probably will feel no qualms in moving to table the rest of the Douglas-Gore proposals or the scores of other amendments that have been drafted.

Since his election as majority leader 19 months ago, Senator MANSFIELD has made increasing use of the tabling motion. Its advantages are twofold. It chokes off debate without the often difficult negotiations needed to obtain a unanimous agreement for some kind of debate limitation. And it tends to obscure the issue on a politically touchy matter: A Senator voting to table the withholding plan can argue he isn't actually voting against the proposal. In parliamentary terms, a motion to lay an amendment on the table is a procedural step that has the effect of preventing a vote on the substance of the amendment—a delicate distinction some Senators cite when it comes to explaining their votes.

But the tabling motion is so abrupt a maneuver it sometimes ruffles the feathers of the Senator it is used against. Consequently, extensive use of the tabling motion this week might widen the breach in the Senate between the Democratic leadership and the liberal bloc that was opened during the vain filibuster against the communications satellite bill.

The Treasury's position amid this intra-party bickering in the Senate is an ambiguous and embarrassed one.

Treasury officials privately agree with the Senate leadership's appraisal that the Finance Committee bill cannot be significantly changed on the Senate floor. Moreover, they are eager to win passage of any bill that contains the investment credit for business.

But these same officials are loath to discourage the liberal efforts to promote Mr. Kennedy's original recommendations. Treasury Secretary DILLON informed Senator GORE recently the administration would do nothing to oppose his fight on the Senate floor.

The one area where the Treasury, the Senate leadership and the liberals can find common cause without qualification is in opposition to the Keogh-Smathers bill giving tax relief to self-employed persons. But so many other Senators have given their doctor and lawyer constituents commitments of support for the House-passed bill that even this united front may not be able to stop the measure.

DIRKSEN UPSETS APPLECAKE

Democratic leaders hope Senators pledged to support the Keogh-Smathers bill will find their way free to table its introduction as an amendment to the tax revision bill, on the ground it should be considered separately. But this tactic is by no means foolproof. Nor is it certain that the Keogh-Smathers proposal, if adopted by the Senate, could be eliminated from the final version of the bill by the Senate-House conference.

Actually, Senator SMATHERS, who often opposes the administration, although a member of the leadership team by virtue of his post as Democratic caucus secretary, had almost decided not to offer his bill as an amendment to the tax-revision measure. But Senator DIRKSEN upset the applecart last week with his surprise announcement he would propose the measure as a tax-bill amendment if nobody else did. Now, there is speculation Senator SMATHERS may try to beat the Republican leader to the punch.

If this effort fails, the future for the Keogh-Smathers bill isn't bright. Senator MANSFIELD probably would delay bringing up the measure, approved last year by both the House and the Senate Finance Committees, for Senate debate until the closing days of the session. Then even the threat of a liberal filibuster might be enough to kill the bill, as it did in 1960. And if the bill did manage to win final congressional passage as a separate measure, it might be cut down by a Presidential veto.

EXHIBIT 4

[From the Washington Post, Aug. 27, 1962]

SIX IMPORTANT BILLS

President Kennedy is urging the enactment of six measures which would promote long-term economic growth and strengthen our educational and social security systems. We have given our endorsement to each of these measures, the present status of which is as follows:

1. The Trade Expansion Act: This bill would encourage the expansion of international trade by granting the President authority to negotiate for the reduction of tariff barriers. It has passed the House and stands a good chance of enactment by the Senate notwithstanding the efforts of protectionist forces to weaken it through crippling amendments.

2. Investment credit: The investment credit provision of the Revenue Act of 1962 as passed by the House would stimulate investment by permitting businesses to reduce their taxes by as much as 7 percent of the cost of newly purchased equipment. A somewhat weaker version of this provision has been approved by the Senate Finance Committee as part of a tax bill that will face a hard fight on both the floor of the Senate and in the conference committee.

3. Youth employment opportunity: This legislation would establish a Conservation Corps to provide employment in our national parks and forests for youths who have left school before finishing and a program of part-time public service work for those who remain at home. The Senate passed a bill embodying similar provisions 3 years ago and is expected to approve the current legislation. Unfortunately the House version is bottled up in Representative HOWARD SMITH's Rules Committee.

4. Public works acceleration: The Senate has passed a bill providing \$750 million to be used immediately for public works and urban renewal projects and an additional \$750 million which is to be expended under standby authority when the rate of unem-

ployment exceeds a critical level. A House version of the bill provides \$900 million for immediate use and a coordinator charged with setting up a reserve "shelf" of public works. Democratic leaders in the House now believe that they have a sufficient number of votes to carry this measure next week.

5. Federal backstop to unemployment compensation: This legislation would extend for 1 year the emergency program, which expired at the end of June, for assisting those persons who have exhausted their unemployment benefits. Chairman WILBUR MILLS of the Ways and Means Committee has begun hearings, and it is believed that his committee will recommend an extension. But the measure is expected to meet strong opposition in the Senate Finance Committee.

6. Federal aid to higher education: Measures which would provide Federal assistance to public and private institutions of higher learning were passed by large majorities in both Houses, but final action has been delayed by a deadlocked conference committee. At issue is the constitutionality of grants which the House bill would authorize for church-affiliated institutions.

All of these measures command widespread public support, and yet only the trade bill seems to be assured of passage at this time. What is required is more resolute action on the part of the majority leadership in the Congress and stronger voices from the grassroots.

EXHIBIT 5

EXPENSES FOR TRAVEL, ENTERTAINMENT, AND BUSINESS GIFTS

(Analysis of some court decisions and administrative cases allowing deductions of entertainment and related expenses)

INTRODUCTION

Collected here are summaries of judicial decisions and administrative cases which illustrate the type of expenditures for entertainment and related items which are allowed as business deductions under present law.

Recently the National Office of the Internal Revenue Service requested district offices to submit cases involving expenditures for parties, business gifts, yachts, hunting lodges and similar items which would illustrate how a relatively slight business element is sufficient to require a revenue agent to allow the deduction of an essentially personal type of expenditure under present law. The cases collected here are typical of expenditures for entertainment which are claimed and allowed in a large number of cases.

These cases show that stricter enforcement procedures cannot solve the problem. Stricter enforcement can only require more detailed documentation of amounts expended and the purpose of the expenditure. But, as these exhibits show, this documentation already exists in a large number of these cases. And where the documentation exists, the present law requires that the entertainment expenses be fully allowed. When existing law allows the cost of a safari to Africa, undertaken by a hunting enthusiast and his wife, to be deducted on the ground that it provides advertising for dairy milk, one can-

not expect revenue agents to successfully question the business necessity for duck hunting or nightclubbing with business associates.

Excerpts from the reports of two revenue agents, submitted in connection with this study, highlight the situation under existing law. One revenue agent reports that:

"The president and one vice president (of the taxpayer corporation) are father, and son. The father and son own memberships in the ——— Club, ——— Country Club, and various supper clubs. The corporation pays all dues and entertainment expenses. It is, however, believed that the entertainment involves friends, and that the officers are in turn entertained by the same people whom they entertain when they pay the bill. Each member of the club is supposed to give a party once each year for the others.

"It has proven impossible to prove such entertainment and parties as personal expense because the officers can always point to some of the parties who were supposedly instrumental in their having obtained some (business).

"One thing is ever present with this taxpayer. A trip to Las Vegas, Nev.; Havana, Cuba; or some other place has always been opportune to attend some New York's Day bowl game or other affair, yet the trip was to see some concern about selling."

Another revenue agent states:

"The president of the corporation is a gun collector and hunting enthusiast. Each year he goes on a hunting trip to Wyoming in the company plane or car (with four hunting companions).

"The four hunting companions were from * * * firms who may be instrumental in the award of contracts * * * and are hunting enthusiasts themselves as well as friends of the president.

"It has further come to the attention of the examiner that officers' salaries are held to a minimum * * *, but the expenses of the above nature are paid in behalf of the officer. It should be added that all events of the trip and associations of the companions are carefully documented and reported to the firm to avoid possible trouble in connection with the deduction.

"Under present law there has been found no basis for disallowance of the expense."

Administrative cases No. 1 through No. 41 were submitted as part 3 of the entertainment expense study presented to the House Ways and Means Committee last year. Cases No. 42 through No. 60 further illustrate the basic expense account problem. These cases are samples from subsequent audits. In cases No. 42 through No. 54 substantially the entire amount claimed as a deduction was allowed. Cases No. 55 through No. 60 are examples of a great number of cases where a substantial portion of the deduction claimed is disallowed because the expenses are purely personal with no business connection but the remainder is allowed because a slight business connection is shown. Of course, to the extent that cases of this kind are not examined by a revenue agent, the entire amount claimed, including the purely personal part, is effectively deducted.

Analysis of court cases involving deductions for entertainment and related expenses

Case No.	Type of business	Type of expense	Amount			Summary of facts
			Claimed by taxpayer	Allowed by Commissioner	Allowed by court	
1	Dairy.....	Safari to Africa.....	\$16,818	\$1,200	\$16,448	In 1950, the taxpayer, a closely held corporation engaged in the business of processing and distributing milk and milk products, paid the expenses for an African hunting safari for its principal shareholder-president and his wife. The president was an experienced hunter. The trip, which included stays at London, Paris, and Rome, lasted approximately 6 months. Taxpayer received publicity as the sponsor of the trip, both in the newspapers and by the exhibition of motion pictures and hunting trophies. The Tax Court concluded that the taxpayer's primary intent was to publicize the business and was not to benefit the officer and his wife. The court allowed the deduction of expenses in full by the taxpayer. (<i>Sanitary Farms Dairy, Inc.</i> , 25 T.C. 463 (1955).)
2	Brewing company.....	Cabin cruiser.....	10,481	6,785	10,481	Cabin cruiser expense incurred during the years 1949 and 1950. President of company testified that the cruiser was used solely to hold sales meetings and to entertain customers and distributors; that it was especially necessary to own a cruiser because company's plant was located in a slum area where it was not feasible to conduct sales meetings or to meet with customers and distributors; that there was a constant need to generate goodwill. "Customarily on weekends they took a group of distributors or take out people or large dealers fishing down to the islands if the weather permitted." The Tax Court allowed the deduction in full. (<i>Cleveland-Sandusky Brewing Corp.</i> , 30 T.C. 539 (1958).)
3	Diversified manufacturing.	Redecorating principal officer's residence.	10,000	None	(¹)	Taxpayer corporation reimbursed its principal shareholder-officer for a portion of the cost of refurbishing the 1st floor of his residence. Taxpayer deducted this reimbursement, contending that this residence was used for entertaining its customers and thus served its business purposes. The jury was instructed that there was nothing wrong with the use of a private residence for a business purpose if it was ordinary and necessary. The court said that the question for the jury was whether a business advantage was expected and whether it was realized.
		Swimming pool adjacent to residence.	6,600	1,650	-----	Taxpayer also claimed depreciation on a swimming pool constructed on land which it owned. The pool was adjacent to the shareholder-officer's residence and could be entered only from that residence. The jury was instructed to find for the taxpayer if it was satisfied that, as taxpayer contended, the pool was purchased for business use and in anticipation of benefits to the business. (<i>Doughboy Industries, Inc. v. United States</i> , 4 A.F.T.R. 2d 5021 (W.D. Wis. 1959).)
4	Manufacturer of witch hazel.	Yacht.....	10,949	None	9,789	The taxpayer, an individual engaged in manufacturing witch hazel, purchased a yacht for the entertainment of customers and potential customers. The yacht was used to encourage such persons to visit taxpayer's plant. Although the Commissioner disallowed the expenses as personal, they were for the most part allowed by the Board of Tax Appeals because of the business relationship which the taxpayer had established. (<i>E. E. Dickinson</i> , 8 B.T.A. 722 (1927).)
5	Horse racing secretary and handicapper.	Yacht and entertainment.	2,000	None	2,000	Taxpayer, an individual engaged in the occupation of scheduling and making other arrangements for horse races and handicapping horses, entertained racing officials, track owners, horsemen and turf writers by arranging dinners and theater parties and providing recreation aboard his yacht. The court found that taxpayer's business was highly competitive. The expenses for entertainment claimed as a deduction by taxpayer were held to be expended for the purpose of promoting taxpayer's business. Taxpayer's effort to maintain friendly relations with those entertained was viewed as essential to his continued success. The deductions claimed were allowed in full. (<i>Charles J. McLennan</i> , T.C. Memo. Op. Docket No. 4757 (June 25, 1945), ¶ 45, 217 P-H T.C. Memo.)
6	Manufacturing paints and related products.	Cabin cruiser.....	28,039	2,000	21,029	Taxpayers were general partners engaged in the business of manufacturing, buying, and selling paints and related products. They claimed a deduction for fiscal years 1952-53 for the operating expenses and depreciation of a boat. The boat was principally used for entertaining financiers, suppliers, and other persons with whom the partnership had business dealings. It was also used for testing work in connection with marine paints and for the personal pleasure of the taxpayers and their families. The court allowed 75 percent of the boat expense as a business deduction. (<i>Greenberg v. Riddell</i> , 4 A.F.T.R. 2d 5040 (S. D. Cal. 1959).)
7	Automobile dealer.....	do.....	992	0	310	Taxpayer was 1 of 2 partners in a partnership selling used cars at retail. The partnership maintained a cabin cruiser which was used partly for business purposes and partly for personal recreation. The Tax Court stated: "An expense of this nature, where reasonably related to the operation of the business, may be deducted as an ordinary and necessary expense. * * * Except for generalities, the criteria upon which the petitioner's basis for determining whether they were business or personal expenses were not disclosed in his testimony." Nevertheless, with respect to taxable year 1949, the court allowed about 1/4 of the claimed expense. (<i>Charles M. Kilborn</i> , 29 T.C. 102 (1957).)
8	Solicits and writes insurance.	Vacation camp.....	1,833	None	1,629	Taxpayer, an individual engaged in the general insurance business, owned a vacation cottage which was used partly for family vacation and partly to entertain customers and prospective customers. Taxpayer frequently held stag parties for businessmen on weekends. Recreation took the form of boating, eating, drinking, and playing poker. The cottage was on a lake and boating facilities were maintained by the taxpayer. The property was sold in 1944 at a loss. Taxpayer claimed a deduction for 75 percent of the loss and 75 percent of the depreciation for that year. The Tax Court found that the property was used 3/4 of the time in taxpayer's business and allowed 3/4 of the loss and depreciation as a business expense deduction. (<i>Walter O. Kraft</i> , T.C. Memo. Op. Doc. No. 14975 (June 22, 1949), ¶ 49, 159 P-H T.C. Memo.)
9	Actor.....	Entertainment.....	1,687	None	1,687	Taxpayer, a professional actor, incurred expenses for theater tickets, luncheons, suppers, and other entertainment which he provided to a variety of individuals for purposes of publicity and public relations and to enable him to secure theatrical engagements more easily. The Board of Tax Appeals sustained the Commissioner's disallowance but was reversed on appeal. The circuit court noted that this entertainment tended to promote the taxpayer's popularity and thereby to increase his income from acting; the expenses were therefore held to be ordinary and necessary. The court said "As the word 'necessary' is used here, we think it means 'appropriate' and 'helpful.'" (<i>Blackmer v. Commissioner</i> , 70 F. 2d 255 (2d Cir. 1934).)

¹ Jury verdict in favor of taxpayer for 95 percent of refunds claimed.

Summary analysis of tax cases involving deductions for entertainment and related expenses

Case No.	Type of business	Type of expense	Amount		Tax year or period	Summary of facts
			Claimed	Allowed		
1	Manufacturer-----	Hunting lodge-----	\$61,146 71,206 55,065	\$61,146 71,206 55,065	1956 1957 1958	Closely held corporate taxpayer maintains a luxurious hunting lodge which had a 1958 tax basis of over \$230,000 and is constantly maintained by caretaker and wife. Streams stocked with trout, small game raised by farmers for purpose of stocking, and large deer population. Log maintained showing names and dates representatives of customers are entertained. Lodge also used for entertainment of key personnel of taxpayer. Log indicates use by 500 to 600 persons annually.
2	do-----	Maintenance of resort facilities on sub-tropical island. Airplane expense----- Airplane depreciation---	353,713 90,666 20,439	269,666 90,666 15,277	Sept. 30, 1957	Taxpayer, a domestic manufacturing corporation, owns luxurious facilities on a sub-tropical island. The principal use of the property is for entertainment of executives and key personnel of customer firms. Fishing cruisers are maintained and air transportation furnished guests. The chairman of the board, who is the controlling stockholder, and other officers and key employees accompanied by their families spent considerable time at island. Adjustment was made for amounts considered personal expenses of these officers and employees.
3	Supplier-----	Yacht----- Ranch-hunting lodges----- Nightclub expenses----- Other entertainment-----	----- ----- ----- -----	111,804 116,440 128,249 119,647	1953-54 1953-59 1954-59 1953-59	Taxpayer's stock is owned by 2 individuals. Yacht was used by company for fishing parties for customers and company personnel. Yacht expenses shown are only for 1953 and 1954; it is estimated that operating expenses, exclusive of depreciation, are \$75,000 per year. Ranch properties are leased by taxpayer from stockholder and from others and are used by customers for hunting and fishing. Nightclub expense was paid by company to a club owned by stockholder to cover charges made by company executives and sales personnel (\$23,000 of this amount was charged at club by stockholder). Parties are held at club during Christmas season and cost of each party ranges from \$8,000 to \$14,000. Each year the company finances a hunting trip to Canada for executive personnel and customers and minimum cost is \$5,000 to \$6,000 for a party of 8 to 12 men. Corporate expenditures which were not allowed as a deduction included over \$20,000 paid for addition to personal residence of stockholder and over \$9,000 for vacation trips to Europe and Africa by stockholder and family. Item of "other entertainment" represents reimbursement for travel and entertainment by stockholder.
4	Insurance-----	Meals----- Lodging----- Transportation----- Food and beverage for entertainment----- Tickets----- Conventions----- Apartment----- Gifts----- Other----- Auto-----	25,000 20,000 30,000 30,000 2,000 1,000 6,000 10,500 3,000 10,000	----- ----- ----- ----- ----- ----- ----- ----- ----- -----	1957	Individual taxpayer travels widely while visiting insurance agency offices. At each office the taxpayer entertains office personnel lavishly for the apparent purpose of establishing good management-employee relations. Taxpayer also lavishly entertains management personnel at Florida vacation resorts. The disallowance of \$40,000 of expense was based on either lack of substantiation or claim stated in wrong year; it was not based on failure to establish a business relationship for the expense.
5	Food products-----	Hunting trip-----	137,500 12,211 14,325	97,500 12,211 14,325	1951 ----- 1952	The trip was given considerable coverage by the newspapers. Films of the trip were exploited successfully in connection with taxpayer's business. The deduction was allowed based on decision of the Tax Court on a similar issue.
6	Supplier-----	Gifts----- ----- Entertainment-----	10,521 9,304 5,941 51,259 44,230 23,898	10,521 9,304 5,941 38,444 33,172 17,924	1953 ----- 1955	President of closely held corporate taxpayer traveled extensively with officers of a customer to various plants, conventions, and on the "horse show circuit." On these occasions he entertained officials of customer at cocktail parties, dinners, etc. Taxpayer contended that it was essential to maintain close personal relations with officers and employees of its customer. It was taxpayer's policy to give gifts to key employees of customer. Entertainment expense of \$44,230 for 1954 is typical and was expended as follows: Local hotels and clubs----- \$7,500 Out-of-town hotels and clubs----- 14,000 Cash to officers, entertainment----- 8,700 Transportation----- 1,000 Food, liquor, cigars for office and farm----- 5,400 Florida hotel expense----- 7,500
7	Sales of steel equipment	Farm resort golf party---	20,000 5,000	20,000 5,000	1958 1958	Most of the expenditures were made by the president of taxpayer. Corporate taxpayer expended \$20,000 to maintain a large plantation and farm type residence in a resort area for entertainment of top echelon executives of various large customers of the taxpayer. The expenditure of \$5,000 was for a golf party for executives of various customers of the taxpayer. This same situation existed in prior years and was accepted.
8	Mortuary business-----	Yacht----- ----- Cottage expense and entertainment----- Personal residence and entertainment-----	11,455 11,096 12,776 4,424 12,271 14,686 10,762 23,758	8,591 8,322 9,582 2,875 7,362 8,811 6,457 23,758	1955 1956 1957 1955 1955 1956 1957 1956	Yacht owned by this closely held corporation was used to entertain visiting morticians, clergymen, and for meetings of employees. Taxpayer prepares and ships bodies to other areas for burial. Personal residence of principal shareholder has an office and residence is used for business meetings and entertainment of business guests.
9	Ship repair-----	Christmas party-----	23,758	23,758	1956	Taxpayer is a closely held family corporation. During the Christmas season of 1956 the corporation gave a dinner at a large hotel, which was attended by customers of the firm and business acquaintances of the corporate executives. The cost of the affair was allowed as deduction on the ground that the purpose for the expenditure was to create goodwill and to enhance the repute of the corporation.
10	Beverage manufacturer	Kentucky derby-----	10,903	10,903	Apr. 30, 1958	Customers and their wives are entertained by derby parties such as breakfasts and luncheons, etc.; by furnishing box seats and tickets for the derby; and entertainment at the derby.
11	Textile manufacture-----	Plantation resort-----	34,258 31,950 29,022 32,924	22,839 21,300 14,511 16,462	Sept. 3, 1955 Sept. 1, 1956 Aug. 31, 1957 Aug. 30, 1958	The corporation leased a plantation from a stockholder of the corporation for an annual rental of \$1. The stated purpose of the lease was to provide the corporation with a place to entertain customers and business associates. Although it appeared that some business purpose was served by the rental of the plantation it was determined a portion of the expenditures to be personal to the stockholder. The disallowed portions of the deductions were taxed to the stockholder.
12	Food products-----	Guesthouse in resort area	13,500 14,300	13,500 14,300	Feb. 28, 1959 Feb. 28, 1960	Taxpayer corporation is located on west coast and most of its sales are made through brokers from the eastern United States and Europe. While they are out on the west coast, the brokers expect the sellers to provide them a place to stay and taxpayer established that the purchase of the guesthouses was for this purpose. The taxpayer also established that the facilities were used by its sales representatives for making sales.
13	Coal and iron mining---	Cottage in Canada-----	11,983 10,509	11,983 10,504	1959 1960	Cottage on bay in Canada was used to entertain people connected with ingot steel industry. 87 persons were entertained in 1960.

Summary analysis of tax cases involving deductions for entertainment and related expenses—Continued

Case No.	Type of business	Type of expense	Amount		Tax year or period	Summary of facts
			Claimed	Allowed		
14	Steel products.....	Residence, Miami Beach..	\$33,206	\$28,706	Apr. 30, 1956	The taxpayer, which is located in the Midwest asserted that lavish entertainment is essential in obtaining business and it established a Miami residence for this purpose. The 2 principal officers and their wives are usually present at the residence when entertaining customers. Deductions allowed include depreciation on residence, food, liquor, boat expense, and salaries of service employees and entertainment. Disallowance was made for amounts deemed to be personal expense.
15	Hosiery mill.....	Beach house and boat....	25,367 32,713	25,367 32,713	1957 1958	Expense of beach house and boat maintained by corporate taxpayer to entertain business guests was allowed in full.
16	Mineral products.....	Summer home and residence.	40,256 42,858 36,696	20,128 21,429 18,348	1956 1957 1958	Closely held corporate taxpayer located in Midwest maintains a summer home in Maine and a residence in midwestern city. Principal stockholder and wife spend 2½ months each summer at the Maine home and entertain high officials (and wives) of customers. The property in Midwest is used to entertain visiting buyers and is used occasionally by president of company and his wife.
17	Roadbuilding equipment.	Club expense..... Liquor..... Season football tickets..... Convention expenses.....	6,700 13,750 2,004 4,250	6,700 13,750 2,004 4,250	1959 and 1960 1959 and 1960 1959 and 1960 1959 and 1960	These expenses are incurred primarily by the top 3 officers of the company. In general, the club expenses are for lunches, dinners, parties, and convention expense on behalf of customers. The liquor is purchased for the bar in the office and is kept for customers who drop in. Expense for conventions are for various groups who have their conventions in the taxpayer's home city; however, a good share is for conventions that the officers attend in resort cities.
		Convention.....	1,400	1,400	1959	Expenses for tractor demonstration attended by corporate taxpayer's principal officer-shareholder and his wife. A purported business reason for the wife's travel was established based on allowance of expenses for similar travel in the past.
		Travel to construction job of one of taxpayer's customers.	2,600	2,600	1960	Such shareholder and his wife traveled to Alaska with customer and wife. Expense of wife was allowed based on representation that customer would not go without his wife and his wife would not go without such shareholder's wife.
		Speedboat.....	1,410	1,410	1959-60	Speedboat was used exclusively at officer-shareholder's personal cottage, yet a log was kept which showed that the boat was used solely for the pleasure and convenience of customers of the taxpayer corporation.
		Party.....	675	675	1960	Christmas party given by such officer-shareholder cost \$850. It was claimed that most of guests were business customers or potential customers. Accordingly \$675 of the \$850 was claimed and allowed as a business expense of taxpayer.
		Las Vegas vacation.....	1,500	1,500	1960	Officer-shareholder and wife accompanied customer and wife to Las Vegas for 12-day vacation. Taxpayer paid the expenses for the 4 individuals. Officer-shareholder asserted that he would not have made the trip except for business purposes and that his wife's presence was required by the customer and his wife.
18	Manufacturer of equipment.	Lease of hunting lodge..	175,000	175,000	1956 1957 1958	Taxpayer leases a hunting lodge and duck hunting preserve for a minimum rental of \$1,800 per month. It is engaged in manufacture of equipment and has its products distributed by several firms located throughout the United States. Customers of each firm are entertained at the hunting preserve. A log is maintained and it disclosed no personal use by stockholders. Taxpayer shares expenses of lodge with 2 other taxpayers. The total expenditure claimed for this lodge by the 3 taxpayers for the years 1953-59 is \$666,000 and it appears that most of this expense was allowed.
19	Manufacturer.....	Yacht.....	272,640	253,035	Feb. 28, 1954 Feb. 28, 1955 Feb. 28, 1956	Taxpayer, in addition to other large entertainment expenses, maintained a yacht primarily for the purpose of entertaining dealers who sell taxpayer's products. The disallowed portion of the expenses was for the estimated personal use by taxpayer's officers.
20	Automobile dealer.....	-----do-----	290 6,204 7,401 10,761	0 0 7,401 10,761	1946 1947 1948 1949	Corporation purchased yacht for purpose of providing free rides to customers upon purchase of an automobile. Log maintained indicated passengers were customers. No boat trips were made unless the principal stockholder was aboard. This case was settled by stipulation while in a docketed state in Tax Court.
21	Cake and cookie bakery.....	-----do-----	18,000 22,000 26,000 20,907	18,000 22,000 26,000 16,943	1957 1958 1959 (2)	Taxpayer sells cakes and cookies to grocery stores. The yacht was used exclusively to entertain supermarket and chainstore buyers and branch managers on deep-sea-fishing trips for promotion purposes.
22	Shoe manufacturer.....	-----do-----	20,907	16,943	(2)	Purpose of expenditure was stated to be the use of the boat to demonstrate to customers a non-skid-sole sneaker made by taxpayer. Used at various Atlantic and gulf coast ports.
23	Automobile dealer.....	Yacht expense.....	(2)	22,692	1956	The taxpayer maintained a guest list record which disclosed that the yacht was used for entertainment of old customers, officials of an automobile manufacturer, automobile dealers, and prospective customers.
24	Oil and refining corporation.	Hunting trip..... Fishing trip.....	1,240 3,855	1,240 3,855	1958 1959	Elk hunting trip for party of 6. Fishing trip to Canada for party of 11. These trip expenses were incurred to entertain officers and managers of various oil and pipeline companies from which taxpayer acquired its crude oil.
25	Auto dealer.....	Airplane.....	20,000	20,000	1958	Used for entertainment, travel, advertising. Records support claimed deduction for depreciation and maintenance of airplane used in entertaining customers and prospective customers.
26	Metals manufacturer.....	Yacht expense.....	7,999	5,500	1957	Boat was acquired in order to create a more intimate relationship between this corporation, through its officers, and its sources of supply. The amount allowed represented the portion spent which related to business purposes.
27	Sale of fuel.....	Hotels, restaurants, boat club, parties, gifts, etc.	60,000	40,000	1958	The amounts claimed included expense-paid vacations for officials and employees of customers at resort cities in Florida. The taxpayer contended that such entertainment served to maintain and increase its sales volume.
28	-----do-----	Yacht.....	34,189 24,063 34,787	34,189 24,063 34,787	Sept. 30, 1957 Sept. 30, 1958 Sept. 30, 1959	The yacht, which was acquired by the corporate taxpayer in 1954 at a cost of \$80,314, is used for sales promotion purposes. Customers and prospective customers are frequently entertained on it. When used for nonbusiness purposes, either by taxpayer's officers or by other persons, a rental charge of \$250 per day is made, which is credited to the yacht expense account.
29	Food products.....	Yacht and resort residence.	26,031	23,491	Oct. 31, 1958	Corporate taxpayer is owned by 2 individuals, is located in a Midwestern State and maintains a residence in Miami, Fla. The taxpayer established that the Florida residence is maintained for the use of personnel of customers and prospective customers and must be staffed and available for use all through the year. The taxpayer contended that the Florida residence and yacht were used to great advantage with suppliers, who expedited delivery schedules, and were helpful also in persuading larger packers to place orders. A sufficient business element was considered to be present and the deduction was allowed under present law.
30	Consultant to manufacturer.	Duck hunting club.....	4,211	4,211	1957	Individual taxpayer served as consultant to manufacturing company with annual compensation of \$25,000. Expense was incurred for entertaining customers of company at a duck hunting club owned by taxpayer.
31	Lawyer.....	Yacht.....	6,475	6,475	1958	The taxpayer is engaged in the litigation of claims as a specialist. In 1950 he acquired a cabin cruiser. The cost of the maintenance and operation of this boat in 1958 amounted to \$6,975. Of this amount the taxpayer claimed and was allowed \$6,475 as an ordinary and necessary business expense on a showing that the boat was used primarily for entertaining clients and business executives for the purpose of establishing professional contacts.

1 Approximate.

2 Not available.

Summary analysis of tax cases involving deductions for entertainment and related expenses—Continued

Case No.	Type of business	Type of expense	Amount		Tax year or period	Summary of facts
			Claimed	Allowed		
32	Exclusive sales representative.	Entertainment.....	\$55,000	\$53,645	1959	Corporate taxpayer, a manufacturer's sales representative, leased the yacht in 1959 for \$1,000 per month from a partnership consisting of 2 individuals who are officers of taxpayer. Partnership was formed in 1959 and acquired yacht in April of that year. Corporation rents the yacht back to the partnership for 2 months each year at a monthly rental of \$1,250. Yacht expense and entertainment expense are incurred to maintain good will with customers of the taxpayer.
		Yacht.....	13,710	8,710	1959	
33	Processing cloth.....	Residence.....	21,183	8,472	1955, 1956, 1957	It was determined that 40 percent of the amount paid by the corporate taxpayer to its president-shareholder was to reimburse him for entertaining business guests of the corporate taxpayer and thus was allowable. No guest register was maintained but taxpayer was able to establish that customers were entertained at the president's residence. Disallowances were based in part on lack of substantiation and in part on failure to relate some expenses to a business purpose. The expense of a hotel suite maintained by the taxpayer was allocated between business and nonbusiness use. Gifts and football tickets for taxpayer's customers were allowed in full.
		Entertainment.....	32,015	23,101	1955, 1956, 1957	
		Hotel suite.....	7,200	3,600	1955, 1956, 1957	
		Gifts.....	3,300	3,300	1955, 1956, 1957	
		Football tickets.....	1,246	1,246	1955, 1956, 1957	
34	Wholesaler.....	Promotion.....	49,329	(⁴)	1957, 1958, 1959	Taxpayer corporation is a wholesale supplier primarily serving utilities, contractors, and local governments. The expenses claimed are for the alleged purpose of increasing taxpayer's sales. Those expenses which are related to business or potential business with local governments will be disallowed as contrary to public policy.
		Football tickets.....	31,963		1957, 1958, 1959	
		Food and beverages.....	124,600		1957, 1958, 1959	
35	Buying and selling of corporations.	Resort residence and luxury apartment.	\$21,399	\$8,559	1956	The corporate taxpayer's business is that of buying and selling corporations. The taxpayer seeks bargain purchases of controlling stock in other corporations.
			16,478	6,591	1957	
36	Manufacturer.....	Yacht expenses.....	13,795	13,795	Apr. 30, 1955	Corporate taxpayer, located in northeastern State acquired the yacht in 1954 and used it during the summer predominantly for the recreation of employees. During the winter it is moved to Florida and is used to entertain various business associates, distributors, suppliers, etc., visiting there on vacation.
			32,527	32,527	Apr. 30, 1956	
			34,404	34,404	Apr. 30, 1957	
37	Selling and servicing new and used cars.	Yacht.....	8,337	5,796	1955	Corporate taxpayer claimed 100 percent of the depreciation and expenses incurred in operating a yacht. Log records maintained were not complete. Many affidavits were submitted by customers which stated that they were guests on the boat and that they received a "sales pitch" while aboard. The taxpayer's president took the boat to Florida each year for a personal vacation which lasted about 3 months. On several of these trips the president was accompanied by a business associate and many vacationing business associates were entertained. Expenses were allowed for portion deemed attributable to business.
			17,641	12,530	1956	
			15,282	10,270	1957	
			10,474	6,946	1958	
38	Shipbuilding.....	Yachts.....	292,627	211,204	1955	Corporation owns several yachts. One of the yachts was primarily experimental. The others were used primarily for entertaining customers and prospective customers.
			354,258	293,330	1956	
			285,617	247,671	1957	
			201,450	176,046	1958	
39	Oil and gas.....	Lodge and boat expense.	23,219	19,737	1956-59	The individual taxpayers are located in a midwestern city. The lodge and boats were used to entertain investors from New York whom taxpayers sought to interest in development of oil and gas properties. Taxpayers also entertained local representatives of oil companies and drillers to encourage their participation in development of oil and gas properties.
40	Construction of roads...	Pleasure resort.....	77,697	53,000	1959 and 1960	The taxpayer corporation is engaged in heavy construction and sale of construction supplies. Its customers are Federal, State and local governments, other contractors, and the general public. The taxpayer acquired a resort estate which is maintained and serviced at a cost approximating \$40,000 per year. The estate has facilities for hunting, boating, and fishing. The purpose of maintaining the estate is to create good will among the various people with whom the taxpayer has business dealings and is specifically used when it is attempting to negotiate or secure a contract. The disallowance of a portion of the expense covers preferential dividends and expenses which are contrary to public policy.
41	Transformer manufacturer.	Entertainment at private clubhouse.	127,067	127,067	Sept. 30, 1959	These deductions consist of depreciation, wages, and other expenditures made in connection with the taxpayer corporation's private clubhouse which is used for the entertainment of customers and prospective customers.
42	Automobile dealer.....	Boat.....	5,681	4,545	1957	Taxpayer owned a boat which was used principally to entertain customers. Taxpayer's records established that most of the persons entertained on the boat subsequently purchased automobiles from the taxpayer. Also, it was established that taxpayer's president regularly lived on the boat. A portion of the claimed expenses was disallowed as personal and taxed as income to the president.
			6,421	5,136	1958	
43	Manufacturers' representative.	Yacht.....	1,956	1,956	1956	Taxpayer's yacht log showed that a majority of the dozen trips out of port was to participate in races. Most of the business entertainment was conducted while the boat was in port. The amount claimed and allowed was 50 percent of the operating expenses and depreciation.
44	Manufacturer.....	Boat.....	3,257	3,257	1958	The boat was purchased in 1958 and sold in 1960. It was used to entertain customers and prospective customers 9 times in 1958, 13 times in 1959, and 6 times in 1960. Deductions included expenses for gas, oil, and entertainment, and depreciation.
			3,985	3,985	1959	
			2,154	2,154	1960	
45	General contractor.....	Yacht.....	2,212	2,212	1959	Taxpayer's yacht was used to entertain customers on fishing trips. Taxpayer maintained a log of the trips made and the persons on board.
46	Banker.....	Country club entertainment.	3,000	3,000	1960	Taxpayer held a debut for his daughter. Approximately 1/4 of the guests had business connections with the taxpayer. Deduction claimed and allowed was approximately 25 percent of the cost of the debut.
47	Manufacturers of automobile accessories.	Yachts, club dues and related expenses, shipboard conventions, hunting and fishing trips, parties.	993,565	991,665	1959	Taxpayer corporation did not maintain a separate travel and entertainment account. Additional yacht expenses and airplane expenses were also spread among various accounts. The only expense disallowed was the purchase price of 1 share of stock in a country club. All other expenses were allowed because taxpayer maintained detailed records, fully documenting all expenses.
48	Physician.....	Travel to Europe.....	1,182	1,182	1960	Taxpayer spent 6 of 22 days in Europe attending a medical congress at which he delivered a paper and presided at one of the meetings. Taxpayer was accompanied by his wife and 2 children. The expenses attributable to taxpayer were allowed as a deduction because he was improving his specialized professional skills.
49	Territorial sales manager for insurance company.	Entertainment; football games; fishing expeditions; theaters.	2,802	2,802	1959	Taxpayer sells insurance for several companies. He entertains present and past customers, as well as prospective customers, contending that it is not feasible to stop entertaining once a person has been sold a policy. Taxpayer entertained about 25 times in 1960 but fewer than 30 different individuals were entertained.
			1,967	1,967	1960	

⁴ Under examination.

Summary analysis of tax cases involving deductions for entertainment and related expenses—Continued

Case No.	Type of business	Type of expense	Amount		Tax year or period	Summary of facts
			Claimed	Allowed		
50	Whisky distillers-----	Yacht-----	\$49,641	\$43,325	1959	Taxpayer corporation purchased and outfitted a yacht. A log and guest register were maintained to show the extent to which the yacht was used to entertain customers and others having some connection with the taxpayer's business.
		Tickets-----	600	600		
		Club dues-----	975	975		
		Conventions-----	15,000	15,000		
		Gifts-----	7,280	5,284		
51	Sales of medical equipment.	Other petty cash-----	14,323	7,000	1960	Taxpayer corporation was allowed its entire operating expenses for a yacht because the yacht log disclosed date of each trip, passengers' names on each trip, and their business association to taxpayer. All expenses fully documented and no trips of a nonbusiness nature were found.
		Yacht-----	3,949	3,949		
52	Manufacturer-----	-----do-----	75,290	72,070	1953	Taxpayer corporation purchased a yacht to entertain visiting officials of other companies and for rental to its officers below operating costs. The Service charged a portion of the difference to the taxpayer's president as a dividend. Also taxpayer leased from its president his personal residence and automobile to provide food and lodging to its guests when the president was away.
			114,600	106,032	1954	
			82,751	74,933	1955	
		Residence-----	9,600	9,600	1953	
53	Manufacturer-----	Tickets for sporting events, etc.	3,000	3,000	1959 and 1960	Most of the expenses claimed were allowed, based on proof by the taxpayer they were connected with his business.
		Convention, Bermuda, etc.	12,000	11,150	1959 and 1960	
		Gifts-----	2,000	2,000	1959 and 1960	
		Resort fishing expenses--	15,700	10,600	1959	
			10,000	7,200	1960	
54	Petroleum production, refining and marketing.	Club dues-----	8,000	6,150	1959 and 1960	Taxpayer company maintained several resort area facilities including several yachts for business conferences, and entertainment. Taxpayer also maintained an apartment used by company employees and representatives. In addition, taxpayer incurred costs for various conventions and club dues to a number of dinner clubs, country clubs, etc., for business purposes. The expense disallowed was a nondeductible capital expenditure.
		Resort property, yachts, apartment, and entertainment.	104,422	100,577	1957	
55	Dairy-----	Resorts, racing events, clubs, tickets, parties, gifts, yachts, etc.	90,000 102,900 106,100 104,400	60,000 65,000 68,000 64,000	1957 1958 1959 1960	The taxpayer, a closely held corporation, deducted amounts for sale promotion expenses, including home phone bills, hotel bills for wives of shareholders, resort trips for families of shareholders, racing tickets, etc. The officers engaged in large-scale entertaining and kept few detailed records. 3 of the officers charged the costs of 17 clubs to the corporation in addition to the costs of 3 yachts, 1 of which was owned by an officer. The taxpayer maintained that the boats were used for business purposes but no logs were kept to establish this use. Some officers had 2 company automobiles in their personal possession. Adjustments were proposed for lack of substantiation, considering the presumptively personal nature of the expenses.
56	Petroleum-----	Trip to Europe-----	12,614	None	1959	Taxpayer toured Europe with his wife to set up a refinery and secure oil leases. No business was actually transacted. Taxpayer claimed deductions for the hotel expenses of himself, his wife, and his daughter as the basis of discussing oil business or other family business matters. Included in the expenses claimed were purchases of clothes, theater tickets, drugs, candy, barber and beauty shop treatments, etc. Other deductions claimed were air transportation for his wife and daughter; expenses incurred in the management of his daughter's trust and investments; country club charges incurred by taxpayer and his family allegedly in connection with discussions of business; expenses for the importation of cigars, some of which were given to business associates; expenses for entertainment and meals at night clubs and restaurants during which proposed oil deals were discussed; automobile expenses, many of which were incurred by taxpayer's wife and daughters; and gift expenses, including various and sundry items of small value which the taxpayer himself distributed to employees on special occasions. Taxpayer alleges that all activity outside his home is business motivated, such as seeking investments, discussing oil deals, and looking after his income-producing properties. Disallowances were based upon the revenue agents determination that the claimed deductions had been made for purely personal items to the extent of the disallowed amounts.
		Hotel expense-----	15,950	6,500		
		Air transportation-----	5,812	2,500		
		Country clubs-----	4,146	2,300		
		Cigars-----	840	400		
		Night clubs and restaurants.	4,500	3,800		
		Car expense-----	7,500	6,500		
		Gifts-----	2,000	1,800		
57	Independent oil operator.	Lodging-----	952	690	1959	Taxpayer's business depends on the ability to acquire bargain properties through his contacts in the oil industry. Taxpayer claimed sums for travel, liquor, hunting and fishing facilities, and club dues. Of these sums expended, taxpayer allocated a portion to business and a portion to personal, based upon his personal opinions. Disallowances were based upon the revenue agent's determination that a greater portion of the claimed expenditures were properly allocable to personal rather than business purposes.
		Automobile-----	3,468			
		Food and beverage for entertaining.	5,128	3,211		
		Airplane-----	350	327		
		Club dues-----	1,200	750		
		Fishing camp-----	4,395	2,744		
		Liquor-----	1,086	558		
		Miscellaneous-----	828	250		
			17,407	8,530		
		Lodging-----	816	647	1960	
		Automobile-----	3,646	2,000		
		Food and beverage for entertaining.	5,920	3,690		
		Airplane-----	792	685		
		Club dues-----	1,200	750		
		Fishing camp-----	4,109	2,562		
		Liquor-----	1,473	640		
		Miscellaneous-----	160	100		
			18,116	11,064		
58	Petroleum sales-----	Promotion-----	7,326	3,663	1958	Taxpayer is a closely held corporation. Taxpayer acquired riding horses which he entered in various shows. Taxpayer's name was listed on the programs, and was displayed on horse trailers and equipment carriers. Taxpayer's return included deductions for board, room, and training of the horses and riding lessons for its president's daughter, who rode them in the shows. Taxpayer's return also included nominal winnings of the horses. Taxpayer claimed the expenses were business connected, but half of them were disallowed. The cost of the horses was treated as a dividend to the president.
59	Physician-----	Entertainment-----	2,605 2,385 2,648	1,564 1,400 1,596	1958 1959 1960	The taxpayer maintained an office in his home. He built an addition to his residence including a recreation hall, barbecue area, and swimming pool, allegedly to promote his practice. No records were maintained to show the business use of these facilities. Expenses were disallowed for the personal use of the facilities by the taxpayer's spouse and social acquaintances. Taxpayer's expenditures appeared to be largely personal in nature. He was able to establish a business connection only for the amounts allowed.
60	Manufacturer-----	Resorts, conventions, clubs, tickets, gifts, etc.	23,200 24,700 23,100	3,700 4,100 4,000	1958 1959 1960	

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EXPENSES FOR TRAVEL, ENTERTAINMENT, AND BUSINESS GIFTS

(Compilation of current comments in newspapers and periodicals relating to expense accounts and business gifts)

FOREWORD

In recent years, the millions of taxpayers who are not so fortunate as to have an expense account and who, incidentally, are the bulwark of our tax system, have been reading and hearing more and more of expense account abuses. Collected here are excerpts from articles published in magazines, trade journals, and newspapers, which illustrate the public's growing concern with this problem.

The portrait presented by these articles is that of a privileged class which has become known as the expense account society—a society made up of individuals who, because of the liberality of our tax laws, practically live on expense accounts. According to many of these commentators, there are very few of the necessities of life, such as meals and lodging, or even of the luxuries, such as vacations at fancy resorts, club memberships, and cruises, that such taxpayers cannot somehow deduct on tax returns as business expenses. These articles describe people who can "charge" almost everything to the company; the type of taxpayer who, when questioned about his return, would say "I have no personal life—all I do is for the company."

EXPENSE ACCOUNTS

"The Myth of the Magic Expense Account," Clarence B. Randall, *Dun's Review*, August 1960, pages 39-41:

"Certain it is that entertaining by business in this country is now itself big business. Some companies are more widely known for their parties than they are for their products. The occasions for business entertainment range all the way from two for lunch in the executive dining room to several thousand in the ballroom for the big hotel, with name bands, and orchids flown in from Hawaii for the ladies.

"Gone are the days when a salesman occasionally wined and dined his favorite customer, or perhaps gave a small theater party. Nowadays, when the deal gets big enough, the company yacht weighs anchor and moves into position, the company plane takes off for a duck blind in Arkansas, or the best hotel in Miami throws open its doors to expectant dealers for a week of continuous circus.

"The distaff side is cut in, too, on both sides of the deal. How the ladies love it. With jet travel what it is, those who were getting a little tired of White Sulphur may now hope to look in on Capri or the Riviera.

"The unseen partner in all this largesse, of course, the man who rides the afterdeck of the company yacht, copilot the duck hunters' plane, sits by while the caviar is spooned out and the crepes suzettes are sizzling, the man who splits the check at the nightspot and hands the big bill to the head-waiter, is none other than Uncle Sam. Lights would go dim along the Strip in Las Vegas and chorus girls would be unemployed from New York to Los Angeles if it were not for that great modern invention, the tax deduction.

"But who are the silent underwriters of this frenetic spending? You and I, the general taxpayers. It is we who make up to the U.S. Treasury the revenue lost through expense account deductions.

"This orgiastic abuse of the expense account is by no means universal, or even in a broad sense characteristic of our business community today. It is, however, a spectacular and alarming trend participated in

by enough companies and individuals to put all of us upon caution for the good reputation of businessmen as a class.

"So far, expense-account entertainment is held somewhat in check by two factors.

"First of all, the best companies—those who value the good opinion of thoughtful people—reject it. They behave with dignity and self-restraint in relationships with their customers.

"Secondly—and this is altogether discreditable—in some of those companies that practice excesses, the president himself has no part in it. He just passes the word to the general auditor not to bear down. And the dirty work is delegated to the younger men.

"It is disturbing that business does not put its own house in order while there is still time, that it does not speak out boldly against expense account abuses. The whole purpose of a trade association, or of any nationwide industrial organization, is to provide a collective voice on matters of mutual concern. The trouble is that we use that voice steadily against others, but seldom turn it inward toward ourselves.

"If we cannot correct these things ourselves, we can hardly protest if Government steps into to do it for us.

"But beyond these moral overtones, and the damage currently being done to the good name of business in the eyes of the general public, comes a practical question. Do these practices, in fact, pay off? There would seem to be serious reason to doubt whether lavish display and heavyhanded entertaining are really worth the cost, whether in the long run they actually sell the merchandise.

"On the law of chances, there are probably as many men who will be offended, even insulted, by overexpenditure to win their favors as there are those who will be impressed.

"Sometimes the use of entertainment and gifts reaches the point where it crosses the line of proper customer relationships altogether and becomes commercial bribery. A set of golf clubs at Christmas to the third assistant purchasing-agent, or a carton of cigarettes with a \$100 bill tucked inside, is completely venal. Business purchased by such means has too precarious a base to be enduring.

"In the long run, the product must sell itself. It takes on no added value from exposure to neon lights, nor is it likely that its special virtues can be explained more clearly at 2 in the morning than at 2 in the afternoon. If it is insufficient in quality or uncertain in delivery, no amount of entertaining can long conceal those basic deficiencies.

"Objective students of the current business scene must view this phenomenon of the reckless use of expense-account money with considerable dismay. They would be hard to convince that extravagant parties make a significant contribution to the Nation. Party or no party, the commodity to be sold remains the same, having no greater utility for the buyer afterward than before, and no greater profit potential for the seller. To say these things, however, is something of a waste of breath, for those on the lunatic fringe of industry who commit the excesses are not given to taking serious thought for the welfare of the economy or for the preservation of the private enterprise system in the midst of the great world struggle in which we are engaged.

"They seldom pause to speculate on what image of the American free economy their conduct creates in the minds of men from the new countries who come to study our way of life. From Pakistan to Nigeria, from Ecuador to Indonesia, the battle is on between socialism and free enterprise. Which will be the basis for developing untapped industrial strength? We are the models upon whom men who wish to preserve private initiative in their economics base their hopes.

"We cannot be too careful in what we teach them. They imitate the bad as readily as they do the good, and they may easily attribute our success to the wrong causes." (Reprinted by permission from *Dun's Review* and *Modern Industry*, August 1960. Copyright, 1960, Dun & Bradstreet Publications Corp.)

"Expense Account Caviar," Lucius Beebe, *San Francisco Chronicle*, March 20, 1961, page 36:

"If the new administration in Washington would like to come by a program of readjustment which would evoke rousing cheers from all but a very small segment of the American people, it could hit upon nothing more felicitous than the often promised but never yet actually inaugurated crackdown on executive expense account.

"The expense account society that has been brought into existence by the past attitude of the Treasury toward this aspect of the national business structure is not only one that costs the Federal Government a good deal of money—how much let Sylvia Porter tell you—but is a much resented affront to a great many people who are themselves unable to swell it in expensive resorts, restaurants and foreign travel tax free and out of various corporate pockets on the slim excuse that they are doing company business.

"There are precious few Americans of private means who can or will patronize restaurants where the luncheon tab for the chef's suggestion can come to \$45 for two, but such plush premises as the Four Seasons in New York are jammed to the reservation desks with expense account patrons paying \$200 for dinner for five.

"This is the aspect of expense-account civilization that is most distasteful to people of ordinary means and prudent ways with money, even if they have it in ample abundance. Probably corporate expense accounts are the greatest single inflationary agency in the entire national economy, in addition to which well-upholstered jerks preempting the best of everything in restaurants, theaters, nightclubs and airplanes are a damned poor advertisement for big business. They make more enemies among a class of people naturally sympathetic to corporate vastness than all the radical agitators and Socialists put together.

"An abatement of the expense-account society could win the Government wild plaudits from a great many taxpayers who, by indirection, are tired of picking up the tab every time some crumbbum with an executive title, who couldn't treat a friend to a Coke on his own money, decides he wants a week in New York with a suite at the St. Regis and ringside tables at El Morocco every evening."

"Life at Uncle Sam's Expense," the *Economist*, April 4, 1959, pages 234, 237:

"The maximum tax that an American could be charged by the Federal Government on his income this year would be 87 percent, but few are so rich and so ingenious as to be caught in that top bracket. The minimum he could pay depends less on the actual income he receives than on his deftness in charging items off against the expense account allowed him by his employer (who then deducts it from the cost of doing business) or in seeking his own loopholes in the tax laws and ordering his life so as to take advantage of them. Many people do both. Living on an expense account is a recognized technique, loopholes in the law are many.

"The man who dines only at the best restaurants, and takes his clients to see only the most popular plays might, were he paying the full bill himself, persuade his wife to cook supper and then take his guests around the corner to the cinema. But the privilege of writing these gestures off, either

on the company's expense account or from his own taxable income, makes a different man of him. He becomes a free spender, bigger than life size, and headwaiters bow, while the bill is ultimately delivered to Uncle Sam.

"The effect is felt by more than the individual taxpayer. Critics charge that the interaction of expense account habits and income tax rules distorts the price system and weakens the moral fiber of the country. The evidence offered includes such trends as the climbing prices of beefsteaks and theater tickets, the seagoing convention, and the recently disclosed business interest in ladies whose telephone numbers can be bought.

"The annual convention is, of course, no novelty. For years these holiday jaunts, masked as educational meetings and therefore properly chargeable to the costs of doing business, have helped to support big resort hotels with convenient golf courses. This year however, the Furness Bermuda Line reports that 26 percent of its cruise bookings in 1959, as compared with 18 percent in 1958, will be convention business. The growing popularity of holding conventions at sea is said to be due to the fact that more members attend educational meetings on board ship just because there are no golf courses attached.

"The Ohio State University School of Journalism recently questioned 600 presidents of big industrial, insurance, commercial, and banking firms on their tax-deductible Christmas giving; under promise of anonymity nearly a quarter of them responded and, with considerable acrimony, some of them described the custom bluntly as 'black-mail' which they could neither approve nor escape. In their world, such gifts ranged from trinkets to Cadillacs, and on to the loan of a yacht, liquored, fueled, and girded. Thus far there is no evidence of a concerted move to end even the most flamboyant of these practices; indeed, no reliable study exists to tell the whole story or to clear the reputation of the business firms which keep free of purple fringes."

"High on the Hog," editorial, the Nation, December 17, 1960, page 467:

"Business entertainment no longer gets business, Mr. Auchincloss, lawyer-novelist, pointed out, since everyone 'is perfectly aware that his host is passing the bill onto Uncle Sam in the form of a business deduction.' 'The vice of the system is not in its attempted bribery,' said Mr. Auchincloss, 'but in the privilege of a few to dine and wine at the expense of the taxpayer.' He proposed that Congress disallow the cost of entertainment as a business expense.

"The racket has reached such proportions that in some cases it is scarcely necessary for a business executive to earn a salary—he can live like a millionaire on his expense account."

"There's No Business Like Lunch Business," William K. Zinsser, New York Times magazine, March 20, 1960, page 60:

"With expense accounts, many have found they can eat well—and make money at it.

"What the country really needs is more restaurants, for that is where much of the Nation's business is transacted. The 'business lunch,' that lavish exercise in spending the boss' money, has fastened such a grip on our cities that to lunch with someone for pleasure is almost indecent.

"Many, in fact, rely on these daily banquets to tide them over the next 24 hours. By careful planning, week after week, a man can literally eat himself into solvency. 'If he eats on the expense account every day, he saves about \$6. That's \$30 a week, or \$1,500 a year, tax free—the equivalent of several thousand dollars more in salary. Of course, if the man puts in an expense account when actually he went out alone and had a hot dog, he can make \$12 a day.'

"This form of chicanery is so common that many a company bookkeeper has been startled to see that two employees took the same client to different restaurants for lunch the same day. Influential columnists believe that they are listed on four or five expense accounts every noon.

"Presidents of companies do not, on the whole, eat business lunches. But in all lower strata, business lunches are almost routine. One elderly ad man, asked how frequently he ate on his or somebody else's expense account, looked amazed at the naivete of the question. 'Why, I haven't paid for my lunch,' he said, 'in 31 years.'

"Expense Accounts," Richard Gehman, Cosmopolitan, March 1957, pages 44-47:

"Today we live in what has been called the Era of the Expense Account. Ever since World War II, the expense account has been playing an increasingly important part in our lives and our economy.

"The extent to which the expense account has influenced the economy is indicated by the fact that multimillion-dollar businesses have been founded and now exist almost solely by virtue of the expense account. The increased traffic in restaurants and in liquor, unusual foods, jewelry, flowers, leather goods, books and other luxury items is directly traceable to the new American habit of blithely charging off nearly everything in sight to expenses.

"Food, drink and expensive gifts are not the only items that turn up regularly on expense accounts. Some men also feel justified in putting down upkeep of their homes, entertainment in their homes, clothes for their wives, and services provided for business associates—services such as furnishing chartered planes or railroad cars, limousines and chauffeurs, or supplying private secretaries complete with typewriters and dictating machines.

"Giving expense accounts to its salesmen and executives has three distinct advantages for a corporation.

"First, it saves money. Most larger companies now pay a 52-percent corporate tax. When a salesman spends a dollar in attempting to cajole a customer into buying the company's product, it actually costs the company only 48 cents.

"Second, it enables the company to reward or remunerate its employees without making them subject to further personal income taxes.

"Third, it enables the company to get more work out of its employees. The man who has no expense account works a given number of hours each day; his evenings are free. The man who is expected to entertain clients and prospects usually does it after business hours.

"But the expense account economy does not work exclusively to the benefit of the large corporation. The small businessman may benefit from the structure of the tax laws, too. By incorporating himself, even the man with a modest income can live on a scale comparable to that of a maharajah * * * and, in general, enjoy himself at the Government's expense.

"Actually, the expense account has created a new upper class—a group of men who, while paying themselves relatively small salaries, actually can live as though their incomes equaled those of oil barons.

"Expense account spending first reached a peak during World War II,' says a Pennsylvania manufacturer * * * 'in my opinion, it's helped contribute to inflation, by jacking up prices far out of reason.'

"Under the expense account economy, human behavior is sometimes subjected to severe stress.

"I've known of several cases in which an expense account at the office caused trouble in the home,' says an advertising agency executive. He points out that a young man who takes clients to the Colony, Le Pavillon,

and other high-priced restaurants for lunch, merrily charging the \$35-for-two tabs to his company, leads a schizophrenic existence.

"Unless the young man's moral fiber is stronger than most men's, he is bound to react unfavorably. So is his wife; at lunch, munching a cheese sandwich, she cannot be blamed for thinking bitterly of her husband, at that moment eating pheasant in Twenty-One. She is bound to be jealous; she is bound to demand to be taken along on his expense account sprees.

"The expense account may cause other domestic difficulties * * * the husband and wife may actually find themselves living on a higher standard than they can afford.

"Many people who operate on expense accounts augment their incomes by falsifying. It is not uncommon for a man, signing a tab in a restaurant where he is known, to put down an amount double the size of the check and take the remainder of the money for himself.

"We're meeting in Siam, bring the wife," Eugene D. Fleming, Cosmopolitan, May 1960, page 60:

"Ever see a business meeting on a tropical beach? Or a million-dollar contract signed at a cocktail party? Or a salesman's wife taking part in company policy? Conventions in exotic places are the newest travel bonanza. Best of all, the cost is tax deductible.

"Day in and night out during 1960, from the Roosevelt Hotel in Cedar Rapids, Iowa, to the sunbaked villas of the Italian Riviera; at millionaire playgrounds in the Caribbean, such as Laurence Rockefeller's elegant Dorado Beach Hotel; on board luxury cruise ships; and at world-famed spas like French Lick, Ind., whose two golf courses and three pools make thinking less fatiguing, some 16 million Americans from every walk of life—salesmen, executives, horticulturists, railway surgeons—will be discussing common problems, making valuable contacts, closing multimillion-dollar deals—and drinking like the well was going dry.

"Ten million of these travelers are freely associated joiners who attend over 20,000 get-togethers, ranging from that of the American Medical Association to the Concatenated Order of Hoo-Hoo, a national lumberman's fraternity. In addition, 6 million businessmen fly hither and yon to sop up corporate wisdom (among other things) at over 60,000 company conventions. These steadfast pursuers of conclaves spend well over a billion dollars on convention-going travel alone.

"Convention travel, it seems, knows no bounds. * * * Delegates would certainly rather spend a week in Paris than in Chicago, the reasoning goes. The traveltime is only a difference of hours, and just a tax deductible, so why not meet there? Bring your wife, of course. She'll love it."

"An Unknown Side of Resource Allocation, the Invisible Hand of Tax Exemption," Norman B. Ture, Challenge, November 1960, pages 8-10:

"The tax treatment of expense accounts is about the most thorny problem in the income tax. The typical situation which causes so much furor involves a company's sales representative who spends lavishly in an effort to secure or retain a customer. Caribbean cruises, theater tickets, a season's box at sporting events, expensive gifts, are a few examples. For a company's executives, there may be country club memberships, use of the company's cars, hunting lodges, perhaps even a home—all at the company's expense.

"Entertainment expenses which show up on the expense account often include those incurred on behalf of the employee's wife and the spouse of the prospective customer. Exciting journeys with gun and camera through what used to be darkest Africa show up on the company's tax return as sales

expenses. The cost of the boss' honeymoon has been known to appear in the same way.

"To the extent that these expenses are allowed as deductions, the Government—therefore, all of us—pays the bill for the goods and services provided for the employee, his sales prospects and others loaded into his expense account. Those on the receiving end do not include the value of these goods and services in their taxable income.

"The company, in other words, is allowed a deduction for a cost of producing income, but the recipients of these expenditures do not report them as income. This creates an anomaly. Though what is cost to one economic entity (in this case the company) must be income to some other (in this case the recipient), this is not always so from the point of view of the Federal income tax.

"Why not just disallow all such deductions? If this were done, clearly this type of sales promotion would cost the company considerably more. With the present corporation income tax rate of 52 percent, every deductible dollar on an expense account costs the company only 48 cents. Remove the deduction and the cost shoots up—a dollar of expense is then a full dollar of cost.

"Where should the line be drawn? The statute's 'ordinary and necessary' rule for deductions is not much help in many cases. What is ordinary in one line of business is frequently extraordinary in another. In fact, the courts interpret 'ordinary' to mean not unique in the business community—rather than customary in a particular business. On this basis, it is hard to conceive of an expense which could not qualify as ordinary.

"If 'ordinary' won't do as a criterion for deductibility, what about 'necessary'? Necessity might seem to be an easier test to apply. But how should one distinguish between the legitimacy of an expense and the necessity for it?

"The African safari, for example, had a legitimate business purpose; it did indeed contribute to sales promotion, or so it was ruled. Was it necessary, however? Most of us would answer, unhesitatingly, that it was not. But what kind of objective criteria are we to use in deciding that the expense of this trip was not as necessary as an equal expenditure on some other activity which produced the same effect on sales?

"Because of these difficulties in applying the vague language of the Internal Revenue Code, this kind of sales promotion effort meets with extremely liberal tax treatment. This situation encourages the allocation of a greater volume of resources to lavish sales promotion methods than would otherwise occur. Moreover, this result was not contemplated when the Internal Revenue Code was framed.

"The frivolous—and well-publicized—activities for which tax deductions are claimed, offends Congressmen and Senators just as greatly as novelists and TV scenario writers. The apparent disinclination to amend the tax law in this area, however, does not imply approval of its results. It is rather, evidence of the difficulties in making a change which will conform with legitimate business requirements."

"I'll Just Sign, Those Big-Figure Expense Accounts," *Newsweek*, May 20, 1957, pages 87-92:

"While U.S. prosperity rests on a solid base of production and sales, its facade is brightened considerably by a host of 'deductibles'—the appurtenances, from first-class fares to crepes suzette, that many employees can rarely afford on their own incomes but can enjoy when traveling on an expense account.

"Nothing on the U.S. business scene has provoked more elbow digs and thigh slapping than the expense account, including racy bits about traveling salesmen who are among its chief devotees.

"More people are spending more money on the company cuff than at any other time, at a rate that would astound 'swindle-sheet' artists of a decade ago.

"Some 80 percent of luncheons served at top Manhattan restaurants like '21' Le Pavillon, and Chambord are expensed. On the Florida Gold Coast, expense accounts are the backbone of the winter economy. Without expense accounts, big yacht basins like Fort Lauderdale's Bahia Mar might be almost deserted."

"The Conventions—Work, Hard Play," *Business Week*, May 16, 1959, pages 176-182: "Last week some 200 members and guests of the Magazine Publishers Association spent 3 days luxuriating at the Greenbrier, posh resort hotel at White Sulphur Springs, W. Va. (pictures).

"What drew them was MPA's 40th annual spring meeting—plus the golf, tennis, swimming, fine food, and secluded luxury that ever since the war have been luring an increasing share of conventioning Americans to the resort hotels.

"The American penchant for conventions—increasingly bearing the more elegant label of 'conferences'—has reached its de luxe flowering in these rural spas that once were the exclusive domain of wealthy families and dowagers who are moving over for the growing number of expense-account guests.

"When the resort hotels—safely secluded from the hurly-burly of the metropolitan areas—got into the convention business they introduced a new note. The flamboyance and commercialism of many of the older shows was replaced by a few days of luxurious living, spiced with refined business contacts and high-level formal programs. Business deals, to be sure, are sometimes started or even concluded, but such trafficking is frowned on except in private, friendly conversation.

"This special type of resort hotel convention is the elite one * * * And the gatherings are kept smallish both by the limits of the hotel's facilities and the fact that they draw mostly from higher, bigger-expense-account echelons of business.

"The magazine publishers' confab at The Greenbrier last week was thoroughly typical of the resort hotel convention. The MPA devoted the first day to committee reports and pressing industry problems. In the evening, special committees met.

"For the rest of the time, it was half work, half play.

"The talks—serious, sometimes valuable and interesting—serve as a psychic payoff for the enjoyment of the other half of the meeting—the hard play in the afternoon. This conscience factor helps account for the remarkably high attendance at formal meetings."

"Visit to the World of Expense Accounts," Russell Lynes, *New York Times Magazine*, February 24, 1957, page 17:

"The expense account—its wry pleasures, its hangovers, its bonanzas and its abuses—has become one of the uneasy national jokes of our time.

"Since not all of us can sink oil wells and have a benign Government smile on our profits and bemoan our losses, we find ways of charging our appetite for luxury to 'the company,' which, in the final analysis, is charging it to our neighbors' tax bills.

"A system of rewards is obviously essential to the successful operation of the capitalist system. The trouble, if it is a trouble, is that the rewards that are represented by the private use of the company plane, the company car and the company shooting lodge do not seem like rewards for performance; they seem to a great many people like special privilege, and that, in a very real sense, is what they are meant to look like.

"The tax structure seems to create one ethic for certain business men whose services are

greatly in demand by corporations and another for the rest of us.

"Seen from a distance, the group portrait of expense-account society presents a rather curious picture. To a great many people it it inevitably looks, and will continue to look, like the society of kept men."

"Expense Account Scandal" *U.S. News & World Report*, January 25, 1960, pages 50-54 (copyright 1960):

"An expense-account scandal—\$1.5 billion in size—is starting now to get special attention from this country's tax collectors.

"The scandal grows out of the use of business-expense accounts to evade taxes by hiding taxable income. Income that should be taxed, but is not taxed, is estimated at \$1.5 billion or more a year. Tax loss is reported to exceed \$700 million a year.

"One of the partners in an accounting firm comments: 'I don't think the Internal Revenue Service is exaggerating the extent of the expense-account scandal. There isn't any doubt that the total of money being taken as tax deductions is enormous.'

"Phony branch offices. A growing practice, tax men say, is for a small firm to maintain an unused office as a 'front' in a resort area. This gives executives an excuse to deduct travel expenses for visits ostensibly made to the branch office. Actually, these visits can be a cloak for personal vacation trips."

BUSINESS GIFTS

Printers' Ink, September 2, 1960, pages 44-45:

"During World War II the sharp rise in the regular corporate income tax rate, capped off for a time by an excess-profits tax, had brought industry's generosity, largely at Uncle Sam's expense, to an all-time high.

"Now a reaction, quiet, but all pervasive, has set in. The regular tax rate is still high, and our Treasury still picks up most of the tab for corporate gifts, but there is a difference. The change in attitude and practice is really a product of the times. * * *

"Two effects have been noticed. One is the decision by some companies that they will not permit their employees to accept any gifts at all or, in some cases, any gifts of more than nominal value. Some businesses have stopped giving gifts to customers. In other instances, some former gift-givers have replaced their largesse to individuals with donations to charity in the name of business friends.

"Corporate gift-giving is conducted on a scale estimated to have grown from \$200 million in 1950 to almost a billion dollars this year, with the average cost per gift now about \$7.

"What the corporate gift buyer must do now is try to find a middle defensible ground between the lush gift that has caused so much public eyebrow-raising and the gift with so little intrinsic value that it would stir up more ill will than good will in the mind of the recipients."

Spirits, October 1960, pages 13, 40:

"Over \$1 billion, or about 10 percent of all expenditures for alcoholic beverages in the United States, may come out of the corporate treasury.

"As for gift buying, the every-man-for-himself land of estimate has to be entered once more. Sales Management, the magazine of marketing, which surveyed 900 American industrial companies in spring-summer, 1960, about their gift giving proclivities, put it succinctly when it said: 'In the absence of exact reporting, marketers must guesstimate the national gift-incentive volume.' *Esquire* puts it at \$2.5 billion. (The people over at *Fortune* set the entire market at \$2.2 billion.) The Business Goodwill Advisory Council is more cautious; the SM report continued, 'almost \$300 million, not counting liquor and purchases at retail stores.' The international news magazine for sales and marketing executives, has

stated that "Today corporate gift-giving adds up to a \$300-million industry at Christmas time." "Industrial and commercial buying apparently fell off to some extent primarily because of the payola scandals that rocked the Nation."

"It is clear that there is a reaction to business entertainment, if only through a few voices."

"It is also clear that there is an 'expense-account audience' that helps pay the distiller's bills to the tune of hundreds of millions of dollars each year."

The Reporter, December 25, 1958, pages 20, 21:

"During a year-long study recently completed by the School of Journalism at Ohio State University, the presidents of the country's 500 largest industries, 50 major merchandise, 50 big insurance companies, and 50 biggest banks were polled."

"Nearly a quarter of them replied. They spoke their minds in the bluntest of blunt language. They used words like 'blackmail' and 'sucker' and 'shakedown.' They told of gifts ranging from trinkets to Cadillacs to \$280,000 in cash to 'the loan of a yacht—liquored, fueled, and girlled.'"

"Nearly half of the big industrialists say their companies give to customers, suppliers, prospects, public officials, newspaper people, and others. Yet 7 out of 10 don't like the idea. (Six of ten flatly disapprove, 1 out of 10 has serious misgivings.)"

"Why this difference between what companies do and what their presidents believe in? Very simple: money. Nine out of ten say they give 'for business benefit' or to 'meet competition.' The 10th gives as a gesture of good will."

"What is the most expensive gift—which you personally know about—that any company has given to gain a benefit? the company presidents were asked. Examples of their replies:

"Midwestern appliance dealer: 'A trip to Jamaica.'"

"Oil refiner: 'Fifteen shares of stock, cost \$3,500.'"

"Heavy equipment manufacturer: 'Cadillac to get shipping contract.'"

"Ore producer: 'Boat trips and other gifts, \$4,000 to \$5,000.'"

"Life insurance man: 'Trip to Europe.'"

"Ore refiner: 'Furnace for a brandnew house.'"

"Mentioned most often were hi-fis, television sets, automobiles (with Cadillacs far outnumbering other makes), cases of whisky, fancy luggage, trips, hotel accommodations, and lavish entertainment."

Fortune, editorial note, October 1959, page 108: "And does the business gift really express the spirit of Christmas? Since everybody knows it is written off as a business expense, its qualification as a token of affection or esteem would seem to be highly dubious. In any case the practice is a nuisance, and can turn out to be a source of embarrassment to both sides."

Business Record, November 1959, pages 503-508:

"Giving Christmas gifts to customers and other business friends is a practice that most of the 291 manufacturing firms participating in this month's survey of business practices strongly oppose in principle. Typical is the attitude of one construction materials producer who regards 'the giving of Christmas gifts for business purposes as a most unhealthy practice, which in its worst form borders on bribery, and in its lesser form is a useless business expense.'"

"Even more outspoken in his disapproval is one company president who states that 'the giving of Christmas gifts on the part of business is becoming a racket, and we shall do everything we can to discourage it.'"

"To the extent that business gifts 'are intended to influence the placement of an or-

der, they are a source of embarrassment to the recipient,' according to respondents."

"A small minority of the firms surveyed maintain that there is nothing inherently wrong with the practice of Christmas business gifts."

"Another group of companies, while agreeing with the sentiment of business Christmas remembrances, replies that 'our Christmas greetings to customers are very well expressed through the medium of a Christmas card.'"

"While most responding companies would prefer not to participate in giving or receiving business Christmas gifts, almost half do send out gifts at Christmas time. Considerations of precedence and competition are most often cited by respondents to explain their continuation of Christmas giving."

Sales Management, September 10, 1959:

"How 448 companies spent their gift dollars:

	Percent
"Up to \$2-----"	4.4
\$2.01 to \$5-----"	11.0
\$5.01 to \$10-----"	62.3
\$10.01 to \$20-----"	7.6
\$20.01 to \$50-----"	5.5
More than \$50-----"	9.2

"When does a gift become a bribe?"

"Sales Management's eighth annual survey put this question to 758 executives and 385 respondents set down a dollar dividing line. Below that mark, they believe, business gifts are friendly remembrances. Above it lies extravagance and bribery."

"The 385 specific amounts and number of mentions divided into: \$5-\$10—28; \$5-49; \$10—113; \$10-\$15—18."

American Lumberman, November 24, 1958, pages 62, 80:

"Cash to contractor's favorite charity is replacing loot to individual builders. Dealers give new views on holiday gift problem."

"Who killed Santa Claus?"

"That is a question that some contractors may be asking themselves next month. More and more dealers say they are getting awfully tired of the insidious seasonal shakedown commonly known as the Christmas gift."

"A coast-to-coast check of dealers by American Lumberman indicates that many dealers are gradually calling a halt to promiscuous gifts to contractors at the holiday season."

"Adverse dealer comments on gift giving ranged from 'a necessary evil' and 'parasitic expense' to 'vicious cycle, which should be brought to a stop.'"

"Most dealers admitted that they go along with the idea of gift giving simply because it is expected. Other dealers feel more strongly."

"Eliminating gifts to contractors wouldn't hurt their business a bit, several dealers predicted, admitting that once started, gift giving is a hard practice to stop."

Purchasing magazine, December 1957, pages 75, 76, 77, 328:

"A total of 75.6 percent of the P.A.'s (purchasing agents) and 76 percent of the sales managers would 'like to see gift giving eliminated entirely'."

"The fact is gifts are a waste of money in many cases. Although half the sales managers surveyed said they bought gifts for their customers, less than 20 percent of them believed sales and earnings would be hurt if they cut out the practice. In other words, over half the companies that give gifts to customers don't do it on an economic basis."

"Just about everyone in sales and purchasing agrees that a really big gift—particularly cash—is, in effect a bribe."

Business Week, November 28, 1959, pages 161, 162:

"This is the time of year when the question of giving Christmas gifts to business associates often crops up."

"It's always been a ticklish problem, but made doubly so this year because of the current scandals concerning 'payola' and business bribes in general. For in making a Christmas gift, the question is often raised whether the gift isn't really made for services rendered or anticipated."

"That's one reason quite a few business executives don't accept such presents and a growing number of businessmen simply don't give business Christmas gifts."

Time, December 1, 1958, page 74:

"Hardly anyone anywhere celebrates Christmas more impressively—or does retailers more good—than the U.S. businessman. * * * The list has grown so long that today the Santas-in-pinstripes spend something like \$1 billion on yuletide cheer: \$300 million for liquor, the rest for a stockingful of loot ranging from \$2.50 puddings to \$2,500 pianos. The giving is not necessarily due to an excess of Christmas spirit; businessmen simply think they must. * * * 'Giving business Christmas presents is like drinking at lunch. Nobody wants to, but everyone's scared not to.' Now at last, the tide is turning. The company Christmas present, like the office party, is on its way down."

"Companies have found that the present produces some king-sized headaches. Some companies spend \$100,000 or more on gifts alone each Christmas."

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EXHIBIT VI.—GAIN ON SALE OF DEPRECIABLE REAL ESTATE

A. "Excessive Tax Allowances on Depreciable Real Estate and Recommended Remedial Action."

B. "Examples of Cases in Which Real Estate Was Sold After Depreciation Allowances Had Substantially Exceeded Actual Decline in Value."

C. "Example of Relationship Between Depreciation and Nontaxable Cash Flow in a Typical Projection."

D. "Analysis of Real Estate Corporation Prospectuses."

E. "Projections of Cash Flow and Taxable Income by Noncorporate Real Estate Syndicates Based on Actual Prospectuses."

EXHIBIT 6

[From the CONGRESSIONAL RECORD, MAY 21, 1962]

PROPOSED WITHHOLDING ON TAXES OWED ON DIVIDENDS AND INTEREST INCOME

(Excerpts from speech of Hon. PAUL H. DOUGLAS, of Illinois, in the Senate of the United States, Monday, May 21, 1962)

Mr. DOUGLAS. Mr. President, last week I reported that I had received approximately 50,000 communications from my State in opposition to the method of collecting the income taxes already owed on dividends and interest by withholding a basic 20 percent at the source. I report today that the deluge of mail still continues.

I believe the vast proportion of the people who write these letters are misinformed about the nature of the problem and misinformed about the degree of difficulty which they would experience. So once again I take the opportunity of speaking about this subject not merely to the Senate, but also to the country through the medium of the CONGRESSIONAL RECORD.

AMOUNTS AVOIDED OR EVADED ARE HUGE

I do not believe the people generally realize the amount of money which is lost to the Treasury by reason of the failure of those who receive dividends and interest income fully to report the amounts which they receive. As we all know, there is a withholding tax imposed on wages and salaries, and the percentage of avoidance and evasion on the income because of the method of collection is very small indeed.

The Treasury has now issued revised estimates, taking account of all criticisms, with respect to the gap between the dividends and interest paid and the amounts which are reported by the recipients on their income tax returns.

For the year 1959 the gap is reported at \$3.8 billion. The amount of taxes owed on the amount paid in dividends and interest, either evaded or avoided, is estimated at \$880 million. The amount which it is estimated withholding would have collected is \$700 million.

The estimate for 1960, which I hinted at in my statement of last week and which has now been confirmed, is that the gap between dividends and interest paid and the amounts reported on income tax returns came to \$4.4 billion; and that the amount of taxes owed, either evaded or avoided, came

to \$1,040 million. The estimated amount which withholding would have collected is \$830 million.

ONE BILLION, ONE HUNDRED MILLION DOLLARS WILL BE LOST IN 1963

It is now estimated that for the year 1963 the gap will amount to between \$4.9 billion and \$5.2 billion; that the amount of taxes which will be owed and either evaded or avoided, will come to \$1,150 million; and that withholding would collect \$910 million.

These are enormous sums. Because such large amounts are owed but not paid and because the tax is evaded or avoided, the burden upon those who pay their taxes becomes correspondingly heavier. I am frank to say that unless we close this great loophole or sluiceway any reduction in taxes sought by other portions of the tax bill really cannot be appreciable in amount. If withholding on taxes owed on dividends and interest income is killed, there will not be very much to share among other claimants for reduced taxation.

It will be virtually impossible then for the investment credit tax to go through. I am not very keen about that provision.

But even if we were not to have investment credit, we could not get any other reductions in the form of a decrease in the corporate tax, a decrease in the tax on small business, or a decrease in the excise taxes. So the very center of the tax bill is the question of withholding.

The Treasury's estimate that \$1.1 billion in taxes already owed on income from dividends and interest in the calendar year 1963 will be evaded or avoided represents a scandalous situation.

WITHHOLDING IS TEST OF CONCERN FOR FISCAL SOUNDNESS

I am absolutely amazed that many of the same individuals and same groups who are constantly criticizing the size of our national debt, who are demanding that the budget be balanced, and who appeal for fiscal soundness are fighting this proposal.

The \$1.1 billion in taxes avoided and the \$900 million in taxes per year which withholding would collect may be small potatoes to them but it is a big amount to me.

The test of their real concern about fiscal soundness will come when we vote in the Finance Committee or on the floor of the Senate on the withholding provision.

COMMON MISCONCEPTIONS

I should like to emphasize that the Treasury's proposal to withhold the taxes already owed on dividends and interest income at the source is very simple.

Although these may seem somewhat repetitious, I wish to repeat again answers to some of the major misconceptions. Among these major misunderstandings are the following:

First. It is not a new tax. I emphasize that point again. Although from one-third to one-half of the people who write me think it is a new tax, it is not a new tax. It is merely a better method of collecting an existing tax. The taxes are now owed but \$1.1 billion is escaping taxation.

Second. That it would hurt the widows, the orphans, the low-income groups, and the old folks.

Those under 18 would be exempt. Those who owe no tax would be exempt. Those who are overwithheld against—and this would be a very small relative number—could get quarterly refunds. This is a privilege which is four times better than that given to the 37 million wage and salaried people who are overwithheld against and must wait until the end of the year for their refunds.

Third. That it is a tax on the individuals, savings or principal rather than a tax on the interest or dividend.

This is not true. On a savings account of \$100 with interest at 4 percent, the

amount withheld would be 80 cents. That is 20 percent of \$4. It would not be \$20, as much of the information put out by the savings institutions have led people to believe.

Fourth. That it would cost too much to administer.

This is not true. It would cost the Treasury between 2 and 3 percent of the amount collected. It would cost the paying institutions about 30 cents per \$100 withheld, or three-tenths of 1 percent.

Fifth. That the Treasury's automatic data processing system—ADP—would be an adequate substitute for withholding. This is not true. In the first place ADP would not go in effect fully until 1967. Between now and then some \$4 billion in taxes owed would be lost. After that about \$700 million a year would be lost, for ADP would collect, at best, only \$200 to \$250 million of the \$900 million which would be collected by withholding.

Finally, ADP would merely provide information to the Treasury. It would not collect taxes. The paying institutions would have to provide the names, addresses, and amounts for 250 million payments. This would be much more paperwork for the institutions than would be required by withholding.

Of the 250 million reporting slips, the Treasury estimates that there would be about 15 million discrepancies when these were matched against the individual taxpayers accounts.

AUTOMATIC DATA PROCESSING NO SUBSTITUTE

Agents would then have to collect the amounts and check out the discrepancies. This would require an increase in the number of existing agents by about 70 percent.

Because of these facts, automatic data processing would cost more, recover less, and require more paperwork than would the very simple method of withholding proposed in the Treasury's bill.

There has been so much misinformation about the proposal to withhold at the source on dividends and interest that with the help of my administrative assistant, Mr. Shuman, I have prepared a question and answer sheet on this subject.

This answers in detail some of the major misunderstandings about withholding.

Mr. President, as I have prepared a sort of catechism on withholding, I shall ask myself a series of questions and then answer them.

WITHHOLDING ON DIVIDENDS AND INTEREST AT THE SOURCE—IS IT A NEW TAX?

Question. Is this a new tax?

Answer. No. Taxes are already owed on income from dividends and interest. It is merely a better method of collection.

Question. Why do we need withholding?

Answer. Because so many people are not paying the taxes they owe on interest and dividend income.

Question. How much is this?

Answer. The Treasury calculations show that the gap between dividends and interest paid out in the United States and the amounts which appear on income tax returns was about \$3.8 billion in 1959, and is estimated at \$4.4 billion for 1960 and between \$4.9 and \$5.2 billion in 1963.

Question. What is wrong about this?

Answer. This is tax evasion or avoidance. People who actually pay their taxes have higher taxes than they would have if those who evade or avoid them paid their taxes.

Question. How much revenue does the Treasury lose because of this?

Answer. In 1959 they lost about \$880 million. In 1960, over \$1.0 billion. For 1963 the estimate is \$1.15 billion.

Question. Would withholding on dividends and interest at the source help?

Answer. Yes, it would. It would collect 80 percent or more of the taxes now evaded or avoided. In fact, the Treasury has fur-

nished me with the following information about this.

Mr. President, I ask unanimous consent that a brief table, the substance of which I have already given, be printed at this point in the RECORD.

There being no objection, the table was ordered to be printed in the RECORD, as follows:

Year	Gap between dividends and interest paid and amounts reported on income tax returns	Amount of taxes owed on these amounts which are evaded or avoided	Amount which withholding would collect
	<i>Billions</i>	<i>Billions</i>	<i>Millions</i>
1959.....	\$3.8	\$0.880	\$700
1960.....	4.4	1.040	830
1963 (estimate)....	\$4.9- 5.2	1.150	910

EXEMPTION CERTIFICATE, WIDOWS, ORPHANS, OLD FOLKS, LOW-INCOME GROUPS

Mr. DOUGLAS. Mr. President, the next question: Would this system penalize the widows, orphans, the old folks, and low-income groups?

Answer. No. The proposal would provide exemptions from withholding for these groups if they owed no tax.

Question. How would it work for children?

Answer. Any child under 18 would be exempt from withholding merely by certifying to the paying institution that the child was under 18.

Question: What about those other 18?

Answer. Any person over 18 who "reasonably expects" to have no tax liability would also become exempt merely by filing a statement with the paying institution to that effect.

Question. Does this include those over 65?

Answer. Of course. Any one over 18—including those over 65—could get an exemption if he owed no tax.

Question. How would one file the exemption certificate?

Answer. He files it with the paying institution—the bank, the savings and loan or building association, or the company paying dividends.

Question. What will the form say?

Answer. It will be an affidavit on which the person merely says that he "reasonably expects" not to be liable for taxes on these amounts.

Question. Will the exemption be permanent?

Answer. The Treasury is recommending that it be made permanent so that the individual need not file again in the second or third year. Of course, if his tax status changes and he becomes taxable, he could no longer claim exemption.

SPECIAL TAX PROVISIONS FOR OLD PEOPLE

Question. Do not older people now have a number of tax privileges in the law which mean that they have to have considerably more income than those under 65 before they owe any tax at all?

Answer. That is correct, and this means that virtually all the low-income older people would be exempt entirely from withholding.

Question. What are these provisions now in the law which reduce the taxes of older people?

Answer. There are many of them.

Question. Would you be specific?

Answer. Yes. First of all, when one reaches age 65, the \$600 exemption per person is doubled. Thus, a couple both over 65 would receive four \$600 exemptions instead of two, and their total exemption on this score alone would be \$2,400 instead of \$1,000.

Question. Do they still receive the standard 10-percent deduction?

Answer. Yes, they do. They can subtract 10 percent of their adjusted gross income or a larger amount if they itemize their deductions.

Question. What about pensions and retirement income?

Answer. As you know, social security payments and railroad retirement payments are already tax exempt. In addition there is a "retirement income credit" for other retirement income.

Question. What does this include?

Answer. It includes income from other pension, interest, dividends, rent, and royalties.

Question. How much is the retirement income credit?

Answer. It amounts to 20 percent of retirement income up to \$240 in taxes per person.

Question. Is this a deduction or a credit against the actual tax owed?

Answer. This is a tax credit. If an individual's taxes were \$240 he could then apply the retirement income credit against this amount and he would owe no taxes at all.

Question. Does this apply to both man and wife?

Answer. Yes, it does, provided the wife's income is from these sources.

Question. This could mean a double credit or a total of \$480?

Answer. That is correct and this is equal to a deduction of another \$2,400.

Question. What about other tax credits or deductions allowed in the law? Do the older people also get to take advantage of these?

Answer. They certainly do. In the case of dividends received, there is an initial deduction or exclusion of \$100 per couple—\$50 apiece—from gross income. Then there is a 4-percent tax credit of 4 percent of the dividends—up to a total of 4 percent of taxable income.

Question. Then a retired couple over 65 with all their income from dividends and interest would need a sizable income before they were taxable at all?

Note this, Mr. President.

Answer. Yes. They could get \$6,100 in dividends or \$5,333 in interest before they owed any tax whatsoever.

Question. Then withholding would not affect very many old people?

Answer. Not at all. Most of them would be exempt.

Question. How many would be exempt?

Answer. Approximately 75 to 80 percent.

Question. What proof do you have for making that statement?

Answer. Treasury figures show that of the approximately 15 million persons aged 65 or over in this country only a little over 3 million are subject or liable for any Federal income tax.

WHAT ABOUT MEDICAL EXPENSE DEDUCTIONS

Question. When one is over 65, cannot medical expenses be deducted from one's income?

Answer. Yes. The medical expenses can be itemized. The 3-percent limitation which applies to those under 65 does not apply here.

Question. What is the 3-percent limitation for those under 65?

Answer. They can only deduct medical expenses if they exceed 3 percent of the taxpayer's adjusted gross income, and they can deduct only those expenses which exceed this 3 percent.

Question. What is the rule then, for those over 65?

Answer. If either the taxpayer or his spouse is over 65, the 3-percent limitation does not apply. He can deduct the medical expenses for himself and for his spouse and his father and mother, including, of course, the amounts paid for medical insurance.

Question. Is there an upper limit to these medical deductions?

Answer. Yes. It amounts to \$5,000 for a single taxpayer and \$10,000 for those filing joint returns or returns as head of a household.

Question. What if they are disabled?

Answer. The limit is raised. If one person is 65 or over and disabled, the upper limit is \$15,000. If both are 65 and over and disabled, the upper limit is doubled and would be \$30,000.

These medical expenses, if incurred, are in addition to all the other deductions which I have mentioned.

Question: Who is considered to be disabled?

Answer. Under the law anyone is considered to be disabled for tax purposes if he is unable to engage in substantial gainful activity because of a mental or physical impairment.

Question. What proportion of the medical expenses of the aged are deducted?

Answer. In the latest year for which the figures were analyzed, about 90 percent of the medical expenses of those over 65 who itemized their deductions were deducted.

Question. How does this compare with those under 65?

Answer. Only about 65 percent of the medical expenses were deducted by those taxpayers under 65 who itemized their deductions.

COST OF ANTIWITHOLDING CAMPAIGN

Question. Are not some of the savings institutions fighting this withholding provision very hard?

Answer. Yes. I have received about 50,000 letters and cards in a 3- or 4-week period opposing it.

These protests are still pouring in.

Question. Is this an inspired campaign?

Answer. It certainly is. Many letters say the savings institution told them to write. Other include the letter or literature the savings institutions have sent out to them. Some say they have received four or five letters from institutions urging them to write to me. I have collected many examples of full-page ads opposing withholding.

Question: Is not this campaign costly to the savings institutions?

Answer. Of course, it is. It takes a 4-cent stamp for each letter to hundreds of members of the institutions. In my judgment it is costing some of these institutions more than the administrative cost of withholding would be for 3 or 4 years in the future.

Question. Are the letters you have received well informed?

Answer. No. From one-third to one-half of those who give a reason for their opposition to withholding believe this is a new tax.

Question. This would tend to show that many of these people probably do not now pay the taxes they owe if they think this is a new tax?

Answer. That is correct. In itself it shows why we need to withhold at the source on these amounts.

I do not know of any stronger argument, really, than that so large a proportion of the protestants on this issue think it is not taxed, which is in itself a confession that they have not paid the tax in the past.

Question. Is there other misinformation in these letters?

Answer. Yes. Many have been misled to think it will hurt the old people, or the children, or the orphans, or the widows, or the low-income groups, all of whom would be exempt if they owed no tax.

Mr. President, it is extraordinary how widow and orphans always appear in these piteous appeals, as do the low-income groups, all of whom would be exempt if they paid no tax.

Question. Do some think the 20-percent tax is 20 percent of the savings instead of merely 20 percent of the interest on their savings?

Answer. Yes. As you know, the tax already owed and which would be collected is only 20 percent of the interest or dividend paid, not 20 percent of the principal.

That is the third time that I have said this, but it is necessary to say it over and over and over again.

Question. Can you give an example?

Answer. Yes. If a person has \$100 in a savings account and receives interest at 4 percent, he would receive \$4 interest. The withholding would be only 20 percent of the \$4 or 80 cents, not 20 percent of \$100 or \$20.

FARFETCHED EXAMPLES

Question. Some of the examples that have been used about how people might suffer from withholding are pretty farfetched?

Answer. Yes. We have been told over and over again how a retired couple, both over 65, receiving \$5,000 a year in income from dividends, would be overwithheld against.

Question. Is this true?

Answer. No. As I pointed out, a married couple, both over age 65, receiving their total income from dividends would have to receive about \$6,100 before they were subject to any tax. They would be exempt.

Question. A couple with \$5,000 in dividends a year would not exactly be paupers in any event, would they?

Answer. No. With a 4-percent return they would have an investment of about \$125,000. I doubt that anyone with investments of that amount would be harmed by withholding even if he were not exempt.

They tend to be exempt if they are married.

Question. But in this case, withholding would not even apply to them?

Answer. That is correct. They would not even come under the withholding provisions.

WAGE AND SALARY WITHHOLDING

Question. How would withholding on dividends and interest compare with withholding on wages and salaries?

Answer. Some 60 million people are now withheld against on their wages and salaries.

Question. How many would be withheld against on dividends and interest?

Answer. The Treasury estimates about 22 million people.

Question. Are many wage and salaried people overwithheld against?

Answer. Yes. About 37 million or over 60 percent of the total are overwithheld against.

Question. How many would be overwithheld against under dividend and interest withholding?

Answer. About 2 million altogether, or 10 percent compared with 60 percent under wage and salary withholding.

Question. What proportion of these would have large amounts overwithheld?

Answer. Only about 1 million of the 2 million who were overwithheld against under dividend and interest withholding would have more than \$10 of overwithholding per year, and they could receive quarterly refunds. That is \$2.50 a quarter, or a monthly amount of 83⅓ cents.

QUARTERLY REFUNDS

Question. Could they get refunds?

Answer. Yes; they could, and they could get them quarterly.

Question. How?

Answer. Those who are overwithheld against in the amount of \$10 or more per year could apply in the first quarter for a refund to the District Internal Revenue Office.

Question. Where would they get the refund forms?

Answer. The Treasury plans to distribute these as widely as possible. They plan to make them available at the offices of the Internal Revenue Service, at post offices, at banks, and at savings and loan, and other savings institutions.

Question. How long would it take for them to get their money?

Answer. About 3 to 4 weeks. That is the time required for the 37 million cases of overwithholding for wage and salaries.

Question. What about the other quarters?

Answer. In the second and third quarters the Treasury would send the individual the form. It would be automatic and he would not forget to apply.

Question. What about the fourth quarter?

Answer. If he had money coming back he merely would file his yearly income tax return as soon after January 1 as he wanted to and would get a check in 3 to 4 weeks.

Question. Would this continue in the following year?

Answer. The Treasury is proposing that the refund procedure be the same in the following years. The exemption certificates would be permanent.

Question. Do wage and salaried people get a quarterly refund?

Answer. No, they do not. They get it only once a year.

Question. Then the procedure for refunds for dividend and interest is better than for those on wages and salaries?

Answer. Four times better. Perhaps I should say four times easier. They would get preferential treatment.

Question. If the wage and salaried person is subject to withholding, why should it not apply to income from dividends and interest?

Answer. There is no just reason why the taxes now owed on dividend and interest income should not be subject to withholding just as the basic tax on income from wages and salaries is withheld.

Question. In fact, doesn't this make it easier rather than more difficult for the honest taxpayer?

Answer. Yes. Often people spend their income when they receive it and then have to borrow money to pay their taxes at the end of the year. The pay-as-you-go principle is certainly more convenient for most people. It would be more convenient on dividends and interest than on wages and salaries.

FARMER'S REFUNDS

Question. Do not farmers who buy gasoline and pay the Federal tax get a refund?

Answer. They do, if they use the gasoline and oil in their tractors or other farm machinery.

Question. How many of these refunds are there a year?

Answer. About 1 million.

Question: Have these people been inconvenienced or have they complained about this procedure?

Answer. Not to my knowledge. They get it quickly and have made no or few complaints.

Question. The number of refunds under dividend and interest withholding would be about the same number, would it not?

Answer. Yes. And after it was in effect, there would be few complaints about it.

Question. And what about the 37 million people who get refunds from wage and salary withholding?

Answer. They have certainly not complained to any extent. I do not believe I have received a single letter this entire year from anyone who has complained about this.

ADMINISTRATIVE COST SMALL

Question. Would it not cost more to collect the \$900 million by withholding than it would be worth?

Answer. No. The Treasury estimates it would cost about \$20 million to collect the \$900 million or between 2 and 3 percent of the amount collected.

Question. But would it not cost the banks and savings institutions too much to withhold?

Answer. No. The best estimates, which were given by private bankers in our hear-

ings, were that it would cost the savings institutions about 30 cents for each \$100 of taxes withheld, and the taxes paid, of course, are only one-fifth of the amount of income received, or about three-tenths of 1 percent after the system was in effect.

MIGHT COST LESS THAN PRESENT EDUCATIONAL CAMPAIGN

Question. Some of the savings institutions say that their present system of informing their members that they actually owe taxes on dividends and interest is enough. They say that the present educational campaign will collect much of the \$1.1 billion which will be lost.

Answer. Well, this campaign has been going on for some time and the results have been nil. In fact, the gap between the amount of dividend and interest paid out in the United States and the amount reported on income tax returns has been growing rather than decreasing.

Question. If we had withholding this cost would be cut out?

Answer. Yes; it would. And even if institutions felt they should inform their members about how much they withheld—and that is not required by law—this would cost no more than the present ineffective educational campaign.

PROCEDURE FOR PAYING INSTITUTION SIMPLE

Question. Would not withholding mean a lot of extra work for the paying institution?

Answer. No.

Question. Why?

Answer. In the first place the saving institution would merely send 20 percent of the total amounts of dividends and interest withheld to the Treasury.

Question. Would they not have to list each person by name, address, and the amount withheld?

Answer. No. No names. No addresses. No individual amounts. If a company paid out \$100,000 in dividends, it would merely send a check for 20 percent to the Treasury.

Question. What about posting the interest to the account of the individual saver? Would that not be troublesome?

Answer. No. The savings institutions would merely credit the savers account with 80 percent of the interest earned.

Question. So if a person earned \$1 merely credit his account with 80 cents? Is that correct?

Answer. Yes; there would only be one posting, as there is now one posting—and this is done by machine.

Question. The cost to the institution would be small?

Answer. Yes. About 30 cents for each \$100 of taxes withheld even if they performed other services in connection with the withholding.

SIMPLE GROSS UP PROCEDURE FOR TAXPAYER

Question. Would the paying institution have to send a notice to the individual giving the amount it withheld?

Answer. No. They might do this as a service but they would not be required to do it.

Question. Why not?

Answer. Because on the yearly income tax form there would be a new space which would make it possible for the taxpayer to compute the amount withheld without actually receiving a notice from the paying institution.

Question. How would this work?

Answer. Let us take an example of a person who earned \$100 of interest from a bank. The bank, of course, would credit his account in the amount of \$80.

Question. Is he now required to report the income he receives from dividends and interest?

Answer. Yes.

Question. Then would it be a new requirement that he list such income on his tax return?

Answer. No. He is required by law to do it now.

Question. How would he do it under withholding?

Answer. First he would enter \$80 in the appropriate space on the tax return. On the next line he would take 25 percent or one-quarter of the \$80. This would be \$20, or the amount withheld.

Question. You mean he—the taxpayer—could compute the amount withheld actually being told the amount by the bank?

Answer. Yes. Merely by taking 25 percent of the amount he received from the bank he would find out the amount withheld. That is, 20 percent of the total amount of dividends and would equal 25 percent of the 80 percent distributed to the individual.

Question. Then he would know the amount received—\$80—and the amount withheld—\$20?

Answer. Yes.

Question. What would he do next?

Answer. He would include the \$100 in the amount of income he received in that year along with the other income he had from salary, wages, et cetera.

Question. Would he get credit for the \$20 withheld?

Answer. Yes. He would enter the \$20 in the space already provided on the tax form for the amounts withheld from his wage, salary, interest, dividends, et cetera.

Question. What would this new space on his income tax return look like?

Answer. In the example I have given it would look like this:

Line 1. Enter amount received from dividends and interest.....	\$80
Line 2. Take 25 percent or one-quarter of amount on line 1.....	20

Line 3. Add lines 1 and 2, total.... 100

Question. That seems simple enough.

Answer. It is simple and would make it unnecessary for the paying institutions to provide any information in addition to that they now provide.

WHY AUTOMATIC DATA PROCESSING WOULD BE NO SUBSTITUTE FOR WITHHOLDING

Question. Would not the new automatic data processing system of the Treasury be an adequate substitute for withholding?

Answer. No it would certainly not be.

Question. Why not?

Answer. In the first place, it will not come into effect fully until 1967. Even then it would collect only about \$200 to \$250 million of the \$900 million which withholding would collect.

Question. Would this \$900 million per year be lost to the Treasury in the meantime?

Answer. Yes; much of it would be. In fact, between now and 1967 the Treasury would lose about \$4 billion in revenues which are owed if we relied on automatic data processing as a substitute for withholding.

Question. Would automatic data processing simplify procedures for the savings institutions?

Answer. No; not in the area of dividend and interest payments.

Question. Why not?

Answer. The savings institutions would have to report the amounts paid by them to their members, which they would not have to do under withholding.

Question. How much paperwork would be involved?

Answer. The institutions would send about 250 million different reporting slips to the Treasury each year with names, addresses, account numbers, and the amounts withheld.

Question. What would the Treasury do with them?

Answer. The Treasury would then have to match them against each and every taxpayer's account.

Question. What would this show?

Answer. It would give about 15 million discrepancies which the Treasury agents would have to check out.

Question. Then automatic data processing would give information to the Treasury, but it would not collect the taxes?

Answer. Right.

Question. Would the Treasury need new agents to collect the amounts owed?

Answer. It most certainly would. It would need to increase its agents by about 70 percent, just to do this job alone—or a total—to collect as much as under withholding—of about 13,000 new agents. Mr. President, we can imagine the resentment which would be created when all those new agents began to call on the people, to make the collections.

Question. Would not the reporting requirements for savings institutions be greater if automatic data processing were used, instead of withholding?

Answer. Certainly. The paperwork would be many times as great for the paying institution.

Question. Would not Congress have to provide money for the new agents?

Answer. It certainly would; and in the past the Congress has been very reluctant to add anything like the number of new agents the Treasury has said it needed.

WITHHOLDING IS TEST OF TAX REFORM

Mr. President, this is one of the most important issues now before the Senate and the country. I hope Senators and the press and the public will inform themselves on the real situation. This is really the Rubicon. If we do not cross this Rubicon, we shall not collect much added revenue; we shall have very little to distribute in the form of decreased taxes; and any hope for a more comprehensive tax reform and loophole closing bill for next year will go down the drain.

How can we plug the other loopholes if we cannot put into effect a system which merely will mean that those who already owe taxes will pay them? This is the easiest of all methods.

PASSAGE OF THE POLL TAX RESOLUTION IN THE HOUSE OF REPRESENTATIVES—TRIBUTE TO SENATOR HOLLAND

Mr. MANSFIELD. Mr. President, it is my understanding that this afternoon, the House of Representatives, by an overwhelming vote—far more than required—passed the resolution calling for a constitutional amendment to abolish the poll tax in the United States. I take this occasion to express my gratitude and thanks to the distinguished Senator from Florida [Mr. HOLLAND], who began the crusade, if I may call it that, 13 or 14 years ago to abolish the poll tax by constitutional amendment. It was a long, hard, and bitter fight. It caused much difficulty, personally and otherwise. But I should like on this occasion to congratulate him for his obstinacy, his determination, and the fact that after 13 or 14 years, at long last, the resolution has passed both Houses; and now the results rest with the States.

THE RAILROAD MERGER PROBLEM

Mr. KEFAUVER. Mr. President, there is presently moving across our

land one of the broadest and boldest attempts at economic concentration in the history of our Nation. I refer to the railroad merger proposals which are pending, or soon to be presented, before the Interstate Commerce Commission for approval. Already more than 75 percent of the Nation's rail assets are involved in these proceedings. Encouraged by a law which has no real, definitive merger guidelines or criteria, and further encouraged by a regulatory body which up to this time refuses to make any overall investigation or establish any basic standards for approval, the mergers are being pushed rapidly along, first in one direction, then in another, depending upon where the financial alliances can best be obtained. The result has been a hodgepodge of irresponsible planning, resulting in the abandonment of basic concepts of competition and antimonopoly, and leading to a possible serious shrinkage of our rail plant at a time when our country needs to grow and defend its world position at all cost.

The Subcommittee on Antitrust and Monopoly of which I am chairman has recently completed some 9 days of hearings in connection with this pending rail merger problem, and particularly with respect to the merits of S. 3097, which I introduced in the Senate April 3, 1962. This legislation which was cosponsored by 13 Senators, including the majority leader and the majority whip, would defer until 1964 any approval by the Interstate Commerce Commission of those major rail mergers which would result in a substantial lessening of rail competition or a tendency toward monopoly, excepting those mergers involving bankrupt railroads, or where such transactions were necessary and essential to the maintenance of adequate railroad transportation facilities. Also excepted was any railroad with assets under \$200 million.

The bill is designed to give Congress and the Interstate Commerce Commission the opportunity to consider anti-monopoly standards as permanent rail merger safeguards—not now guaranteed by the law—and to review the whole merger problem with a view to developing additional public interest criteria which must be met before this vast reorganization of our rail transportation network is allowed to proceed.

THE INADEQUACY OF OUR APPROACH TO BIG RAIL MERGERS

Mr. President, the testimony, exhibits, and other materials obtained in these hearings before the subcommittee have convinced me that our present approach with respect to these vast consolidations in the rail industry, both in law, and by administrative procedure, is wholly inadequate to assure the American people that a healthy, balanced, competitive rail network will result. The bulk of the railroad industry now appears determined to combine and consolidate its major trunkline systems with the announced intention of reducing trackage, diminishing schedules, eliminating terminals and other facilities, laying off workers, and most important, destroying to the greatest extent possible competi-

tive rail operations in most of the productive areas of the United States. The hearings have amply demonstrated that neither the Interstate Commerce Commission, nor the administration, is presently equipped to cope with this great transportation problem, and that if these large trunkline mergers are allowed to go forward, without a general investigation and analysis of their long-range impact on our competitive business society and upon our economic growth, we may be making a very grave and irreversible error. In short, these presently proposed mergers may well be the first long step toward a single or double railroad system for this country, controlled by private investment and regulated by a regulatory body which may become subservient to such private interests. With this first step, we may be crossing the threshold of private, competitive enterprise, and entering the domain of private government. Certainly, this is a transition for which no Member of this body would want the responsibility.

From 1920 to 1940, there were sensible plans proposed for merged rail systems based among other things on the preservation of competition and the creation of economic balance. The Interstate Commerce Commission was given the authority to approve mergers in conformity with these plans and to give to the railroads immunity from the anti-trust laws. The railroad community had every opportunity to cooperate with the Commission in working out an orderly consolidation program during these years, but instead it frustrated the Commission's work, declined to submit any substantial mergers for approval and took extraordinary advantage of a loophole in the Interstate Commerce Act allowing railroads to combine through stock control, leases and other arrangements without having to conform to any plans or to obtain the Commission's approval. Many of the larger eastern and western systems which exist today were developed through the use of these holding company devices under this loophole in the 1920 act.

There were, of course, some practical obstacles to effecting a plan for a railroad network, including the lack of power in the Commission to compel or enforce mergers after determining that the proposed alignment was in harmony with the Commission's plan. Nevertheless, the essential point, Mr. President, is that during this great, growing period of our American economic life, the railroads could have developed themselves into strong, healthy, and competitive private systems under the imprimatur of the Interstate Commerce Commission and with the blessing of Congress and much of the competitive imbalances and financial and operational deficiencies which exist today in the railroad industry could have been eliminated. The law was adequate, and the experts were sufficient, to effectuate a soundly conceived revamping of our rail plant in accordance with public interest standards, if the railroads and their financial backers had cooperated in this venture.

When the holding company loophole was eliminated in 1933, the railroad in-

dustry pushed for a transportation merger policy which would not only relieve the Commission of responsibility for effecting, or suggesting, an orderly consolidation plan, but would leave in the Commission only the bare power to accept or reject voluntary proposed rail mergers on a case-by-case basis in accordance with certain very general and weak public interest criteria. This policy was enacted into law in the Transportation Act of 1940 and it is the present policy under which this vast proposed railway reorganization will be processed today. Noticeably absent from this policy were the fundamental prerequisites that rail competition should be preserved and that monopolistic combinations should not be created in this industry. Absent, too, were adequate standards and safeguards relating to the protection of areas and communities, the promotion of economic growth, the effect on our national defense, and the preservation of necessary lines and facilities. In addition, the effect of increased economic power through rail mergers upon other modes of transportation was something not specifically contemplated by this act.

However, despite this lack of definitive legislative intent, with respect to the positive role to be played by the Interstate Commerce Commission in rail mergers, the Commission, when faced with this rash of huge consolidations over the past 2 years, should have initiated its own general merger investigation, formulated general, regulative policy in this direction, and established some guides so that the carriers would not go to the expense of thousands, and perhaps millions, of dollars and man-hours of work presenting cases only to be rejected. According to Commissioner William H. Tucker, the Commission in section 17(3) of the Interstate Commerce Act (49 U.S.C. 17(3)) has the power to coordinate merger proposals by regions, to make independent investigations and pilot studies secondary to such merger proceedings, and to create special professional task forces to explore all the public interest factors involved in these merger proposals. In addition, Commissioner Tucker says that the Commission has the power to formulate rail merger policy and guide merger considerations.

Instead of meeting the rail merger issue, the Interstate Commerce Commission has refused to make over all investigations, has continued to consider each merger proposal on a piecemeal basis, has introduced its economic experts only in extreme cases, and has declined to seek from the Congress any additional legislation or direction which would assure it of greater participation in these merger plans being presented by the rail industry. In fact, before the Senate Antitrust and Monopoly Subcommittee, Chairman Rupert L. Murphy urged that the Congress not depart from the voluntary case-by-case approach.

THE BREAKDOWN IN THE VOLUNTARY, PIECEMEAL METHOD OF MERGER APPROVAL—THE PENNSYLVANIA-CENTRAL MERGER

Mr. President, the testimony before the Senate Antitrust and Monopoly Sub-

committee clearly demonstrated that the piecemeal, unguided, hands-off procedure of the Commission in meeting this giant reorganization of the rail industry is seriously breaking down. An extraordinary example of such breakdown lies in the eastern merger situation. There, according to the subcommittee hearings, two major applications—the B. & O.-C. & O. proposal and the N. & W.-Nickle Plate-Wabash proposal—are continuing to be processed separately and unrelated to other merger proposals, but are nevertheless conditioned upon the approval of a recently proposed merger between the New York Central and Pennsylvania railroads. Although the B. & O.-C. & O. and the N. & W.-Nickle Plate-Wabash plans might each be beneficial to the public interest, standing alone, and completely separate and distinct from any controls or influences by either the New York Central or the Pennsylvania, the people may not be entitled to these new systems unless the giant Pennsylvania-New York Central merger—which could well not be in the public interest—is permitted to go forward by the Commission.

This is the industry's package for the East. It involves every eastern road, large or small, in one way or another. In effect, the industry is saying to the Interstate Commerce Commission—buy the Pennsy-Central combination, involving a massive concentration of assets and financial power, and an equally massive shrinking of our eastern rail plant, or there will not be any eastern rail mergers in the public interest. That is essentially what the chairman of the board of the Pennsylvania told the Antitrust and Monopoly Subcommittee at the hearings on July 3. The testimony, in part, went as follows:

Mr. SYMES. * * * But one thing for sure, we won't get any merger if we are going to try hold the one over here for the one back here, and I say it is this simple. If the C. & O.-B. & O. is approved, that is going to help the Nickel Plate case, and if that is approved, it is going to help our case, going to go right around the circle.

Mr. TURNER. That is right. * * * If you don't take the Pennsylvania-Central, you don't get the other mergers. Isn't it just about that simple?

Mr. SYMES. I think that is probably right, and that is the way it should be.

Mr. TURNER. Now, the ICC—

Mr. SYMES. I am gambling that that is what it is going to be.

Mr. TURNER. The ICC is entrusted with the public interest. It has to decide these mergers in the public interest. It now has before it three mergers, some of which may be perfectly good in the public interest, but it has no alternative but to buy the package or nothing at all. Isn't that a fact?

Mr. SYMES. It is the fact, and it is up to the ICC to decide.

Now, Mr. President, this proposed Pennsylvania-New York Central merger, which began its presentation last week before the Interstate Commerce Commission, has many shortcomings. Competent experts testified before the Antitrust and Monopoly Subcommittee that this combination of properties would result in \$5.4 billions in assets, exceeded in the United States only by General Motors, American Telephone & Telegraph, Standard Oil of New Jersey, four insurance companies and three banks.

and reasonable proposal which has been made on this delicate but vexatious question.

As the Senator from Minnesota has pointed out, the Soviet Union has demonstrated beyond peradventure that it will not accept on-site inspection within the Soviet Union. It may be that the nature of Soviet closed society is such that it is impossible politically, from an internal standpoint, to accept on-site inspection. That I do not know. It may be that for some other reason they are unwilling to accept inspection. Whether they wish to continue such underground tests I do not know.

At any rate, as the Senator has said, President Kennedy has demonstrated beyond any doubt which any person in the world could reasonably entertain his sincerity and his honesty in regard to the attaining of an agreement to bring to an end the contamination of the world's atmosphere. It happens that in the last proposal the President is proposing an agreement which deals with the medium in which the tests have the greatest meaning as to weapons development and also the medium from which the hazard from fallout is the greatest.

So, though this last step would not be the total and comprehensive ban, it would perhaps go four-fifths of the way. It would be a very significant step.

I am pleased that the President has made this proposal, though I cannot express any expectation as to what the Soviets will do. I think humanity the world over, including the Russian citizens, would be benefited if they should accept the proposal.

I thank the Senator for his able address.

Mr. HUMPHREY. I thank the distinguished Senator from Tennessee for his remarks.

The Senator from Tennessee [Mr. GORE] was one of the first in the Congress who recommended and advocated that our efforts in this field of nuclear weapons test prohibition be centered upon what is now called the limited test ban; namely, the limitation of tests and the banning of tests in the atmosphere, under water, and in space.

The Senator from Tennessee was an adviser to the American delegation at Geneva in the year 1958, if my memory is correct. After having been there for some weeks he returned to the United States. While he was on his return trip it was my good fortune to meet with him very briefly in Paris. I was on my way to serve in that post as adviser to our delegation after the Senator from Tennessee had left.

The Senator at that time informed me that it was his view that the Soviets would not agree to a general, overall, comprehensive test ban treaty including underground tests. He also indicated to me, which was proved to be very true later on, that there were certain limitations to our capacity to detect certain underground tests.

Therefore it might be well that we would hesitate on that particular matter. In substance, the Senator reported to the then President of the United States, Mr. Eisenhower, and the Secre-

tary of State, Mr. Dulles, that we should take the initiative on the limited test ban. He has been a firm and staunch advocate of it. Time after time on this floor I have joined him in making that recommendation. I am sure that both of us today feel that the proposal which has been advanced so completely in every one of its details is a worthy proposal because, as the Senator has said, it affects primarily the area in which new weapons can be developed. In other words, the environment of the atmosphere, outer space, or under water is where new weapon technology can be most fully developed, as compared with underground testing. That type of treaty would surely slow down the contamination of the atmosphere.

I wish to join with the Senator in commending the President again for his initiative.

I repeat that if there is one iota of sincerity in the leadership of the Soviet Union to slow down the arms race, this is the opportunity that they have to accept this constructive proposal. Let those of us in this body say as loudly as we can that the proposal is not only in the interest of the United States and our people, but also it is in the interest of the Soviet Union and the people of Russia, because they, too, are in the northern belt, so to speak, in which radioactive fallout is the heaviest. It surely is in the interest of all humanity.

I think the proposal will demonstrate once again to the world that this country, while strong, unafraid, and the most powerful nation on the face of the earth, is ready to walk the path of peace, if there is any willingness on the part of any nation to join us, because negotiations, if they are to be meaningful, must be between more than one party. They must be between at least two parties. In the present instance there are 18 nations represented there designated by the United Nations to try to find some way to slow down the arms race and in particular the nuclear arms race. I hope and pray that it will be possible. It is to the credit of our country that we have taken the initiative.

Mr. GORE. I wish to thank the Senator for his generous reference. It has been a pleasure to work with the distinguished chairman of the Subcommittee on Disarmament. His contributions have been great and frequent.

I should like to add one further thought. It may well be that events and technology of our time have passed a bit beyond underground tests. At least they do not now loom as importantly as they did 2 or 3 years ago.

Mr. HUMPHREY. I thank the Senator. He is so right.

EXHIBIT 1

MINNESOTA ACTS ON IODINE IN MILK (By Donald Janson)

MINNEAPOLIS, August 23.—Minnesota's farmers kept dairy cows out of the pasture today. It was the start of the first statewide program in the United States to reduce the amount of radioactive iodine 131 that nuclear testing puts into milk.

In sufficient quantities iodine 131 can cause thyroid cancer, particularly in children. All iodine tends to concentrate in the thyroid glands in the neck.

The Minnesota programs calls for shifting milk cows from pasture to dry hay and other feed that has been aged at least 21 days. Iodine 131 decays rapidly enough to lose its radiation punch in this length of time.

Levels of iodine 131 in milk here are not at danger levels. The new program is precautionary. State officials do not want to take a chance on any sharp rise in radioactivity levels as a result of Soviet testing that was resumed this month.

According to the Federal Radiation Council an iodine 131 level in excess of 100 micro-microcuries a liter of milk a day is the peril point.

The effects of the Soviet series have not been measured yet. However, when the Soviet Union conducted its previous series last fall iodine 131 levels here jumped. Fallout attributed to U.S. tests in the Southwest also accumulates here.

Last week the iodine 131 count at eight sampling stations in Minnesota averaged 46 micromicrocuries, at times ranging up to 100. Last month the level was about the same, at times measuring slightly over 100 at some stations.

FORTY PERCENT OF FARMERS TAKE PART

Although no complete tabulation has been made yet, indications today were that about 40 percent of the State's dairy farmers already were participating in the voluntary program to remove cows from pasture.

More are signing up. Duane Wilson, Minnesota's commissioner of agriculture, said that most producer groups and processors in the State would participate to some degree.

Herman Birdsall, controller of the Twin City Milk Producers Association, representing 2,575 farmers who supply fluid milk to the Minneapolis-St. Paul area, said that about half of those in his association might comply.

Those who do will be paid a premium to compensate for increased costs of feed, labor, and fencing. The association has passed the cost of this premium on to dairies, and some dairies have passed it on to retailers. An expected retail price increase of a cent a quart for milk, however, did not go into effect today at most stores here.

Dr. Warren R. Lawson, chief of the radiation section of the Minnesota Department of Health, said that 80 percent participation by farmers would be necessary to keep iodine 131 levels below guidelines established by the Federal Radiation Council "if we get any large amount of Russian fallout."

INTAKE NEAR PERIL POINT

The Council puts the danger level at 36,500 micromicrocuries a year, an average of 100 a day. The Federal testing station here showed that residents of the Twin Cities who drank a quart of milk a day would have accumulated 33,000 in the 11 months ended August 1.

To check the effectiveness of the aged-feed program, the Minnesota Department of Agriculture is beginning a daily collection of milk samples from both participants and nonparticipants. The samples will be analyzed by the State department of health.

In case of danger, the unprotected milk would be held off the market or blended with the "clean" milk to reduce its iodine 131 content to a harmless level.

The program will continue until further notice. This probably will be late October, when cows in this area are normally taken off pasture and put in barns for the winter.

Standby programs such as Minnesota's are being considered in other States. So is another approach—to divert to such manufactured dairy products as butter and cheese the milk from any area within a State that is hard hit by fallout.

Iodine 131 loses much of its radioactivity by the time butter and cheese reach the consumer.

REVENUE ACT OF 1962

The Senate resumed the consideration of the bill (H.R. 10650) to amend the Internal Revenue Code of 1954 to provide a credit for investment in certain depreciable property, to eliminate certain defects and inequities, and for other purposes.

Mr. PROXMIRE. Mr. President, earlier today I engaged in a colloquy with the Senator from Oklahoma [Mr. KERR], the Senator in charge of the bill. At that time I made clear that I wished to ask further questions of the Senator in charge of the bill. It was my understanding that the distinguished Senator from Oklahoma said in his prepared statement that he would be happy to answer questions of any Senator. I have been present in the chamber all afternoon waiting to do that. A few minutes ago, before the distinguished Senator left the floor, I told him that I wished he would remain so I could ask him questions. He said he would not be able to answer questions tonight. I said I would ask them tomorrow.

He said, "We may get around to that tomorrow."

I wish to make clear that I feel very strongly that questions should be answered on the bill, because I think it will be very hard to justify some of the provisions in the bill.

There is no Senator—and I feel emphatic about this—in the Senate who is better able to justify the bill than is the Senator from Oklahoma. If he cannot justify it, I think nobody can justify it. But since I cannot interrogate the Senator from Oklahoma tonight, I should like to reinforce the point I was seeking to make when I questioned him before. I should like to read the colloquy between myself and the Senator from Oklahoma, and then put the facts from the survey of current business of the U.S. Department of Commerce into the Record to support my position. I quote now from a colloquy that took place at about 1:30 o'clock this afternoon:

I should like to ask the Senator how he explains the fact that we do not have an unfavorable balance of trade but have a highly favorable balance of trade. The favorable balance of trade in the first half of 1962, seasonally adjusted to an annual basis, is \$4.8 billion.

Even if we should leave out of consideration foreign aid and military spending, the commercial favorable balance of trade is \$2.2 billion, which means that other nations have an unfavorable balance of trade vis-a-vis us to that extent. In other words, we are winning. We are competing far more effectively abroad than other nations. The statistics prove it.

Mr. KERR. I say to the Senator from Wisconsin that his figures are erroneous and his conclusions inaccurate.

Mr. PROXMIRE. I call the Senator's attention to the statistics from the Department of Commerce.

Mr. KERR. Let me answer the Senator's question.

Mr. PROXMIRE. The Senator challenged my figures. I am giving the source. Does the Senator want the facts, or not?

Mr. KERR. If I did I would not go to the Senator from Wisconsin for them.

Mr. PROXMIRE. I ask the Senator to go to the U.S. Department of Commerce for them. That is my source.

Mr. KERR. The Senator from Oklahoma will take his pitcher to whatever well he chooses.

Mr. PROXMIRE. I am sure he will.

Mr. KERR. Yes. The balance of trade, overall, that is when one gives effect to items such as foreign aid, military expenditures, investments of American financial institutions abroad, is a deficit.

Mr. PROXMIRE. The Senator is completely wrong.

Mr. KERR. Not a credit position.

Mr. PROXMIRE. The facts contradict the Senator completely.

Mr. KERR. I say to the Senator, "I will finish my speech, and then you finish yours."

Mr. President, I wish to finish my speech by putting into the Record the facts. First, I ask unanimous consent that a table, the source of which is the U.S. Department of Commerce Survey of Current Business entitled "U.S. Balance of Payments, 1958 to 1962" be printed at this point in the Record.

There being no objection, the table was ordered to be printed in the Record, as follows:

U.S. balance of payments, 1958-62

(In billions of dollars)

	1958-60 average	1961		1962, 1st half ¹
		Full year	2d half ¹	
Commercial exports...	17.4	17.7	17.8	18.1
Government aid-financed exports ² ...		2.2	2.4	2.6
Imports.....	-14.3	-14.5	-15.5	-15.9
Surplus on trade...	3.1	5.4	4.7	4.8
Services rendered.....	7.0	7.7	7.8	8.2
Services received ³	-5.9	-6.3	-6.5	6.5
Surplus on services.....	1.1	1.4	1.3	1.7
Surplus on trade and services.....	4.2	6.8	6.0	+6.5
Military outlays ⁴	-2.9	-2.5	-2.4	-2.0
Economic grants.....	-1.6	-1.9	-4.0	-3.2
Loans ⁵	-8	-9		
Total Government outlays.....	-5.3	-5.3	-6.4	-5.2
Private long-term capital:				
Inflow.....	.3	.6	.1	.3
Outflow.....	-2.4	-2.5	-2.8	-2.5
Net.....	-2.1	-1.9	-2.7	-2.2
Total Government outlays and private long-term capital.....	-7.4	-7.2	-9.1	-7.4
Basic deficit.....	3.2	.4	3.0	.9
Private short-term capital:				
Recorded outflow.....	-.6	-1.5	-1.2	-.8
Errors and omissions.....	.1	-.6	-.4	.5
Net.....	-.5	-2.1	-1.6	-.3
Overall deficit.....	3.7	2.5	4.6	1.2

¹ Seasonally adjusted, raised to annual rate.

² Excluding shipments under military aid programs.

³ Including private remittances and Government pensions.

⁴ Net of sales of military equipment.

⁵ Net of repayments.

NOTE.—Details may not add to totals because of rounding.

Source: U.S. Department of Commerce, Survey of Current Business. Figures for the 1st half of 1962 are educated guesses based on preliminary and incomplete data.

Mr. PROXMIRE. Mr. President, I wish to point out that what the table shows is that we have a commercial export surplus, that is, a favorable bal-

ance of trade of \$2.2 billion. If we add to that our favorable balance from services rendered, that is, the excess of services rendered as compared with services received, we have an additional favorable balance of \$1.7 billion, for a total commercial surplus or favorable balance of \$3.9 billion.

The Senator from Oklahoma [Mr. KERR], in the colloquy, used the following phrase:

With reference to the purchases of borrowers from American-supported financial institutions there is a deficit.

What he was referring to, of course, is that our capital in loans goes abroad, and if we allow for that, the Senator from Oklahoma said, there is a deficit total overall in the commercial account.

Well, the fact is that the Senator from Oklahoma is completely wrong on that point. The facts show that even if we assume that every single penny we loan abroad is expended in our country and results in exports, we still would have a net favorable balance of trade after all the American capital is assumed to be spent in this country, which it is not; but giving him the full length and breadth of his assumption, we still would have a favorable balance of \$1.4 billion, because our net long-term capital outflow is \$2.2 billion. Our short-term capital outflow net is \$300 million, for a total of \$2.5 billion. If we subtract that \$2.5 billion from the \$3.9 billion, we find that we have not an unfavorable, but a total, overall, commercial favorable balance of \$1.4 billion. So that the hard, cold, stubborn fact that won't go away is that by the test of the market in world trade we are in fact competing successfully.

Mr. President, I think it is extremely important to recognize that—because unfortunately the fallacious idea has gotten abroad in our country that our economy cannot compete with nations overseas. The facts, when examined carefully, show that we are competing very effectively. We are not losing. As I said, we are winning. We are winning in trade throughout the world.

We are selling more abroad than our rivals are, on any basis of comparison. We are competing very well. What I wish to emphasize is that we are competing well without benefit of the investment credit.

Furthermore, when we take into account the fact that the President of the United States and the Secretary of the Treasury very wisely provided for vast improvement in our depreciation schedule, to the extent of \$1½ billion, which is substantially more than the investment credit would amount to, we can see that the competitive position of American industry has already this year been even further improved.

I wish to question the distinguished Senator from Oklahoma tomorrow. I believe that—not from the standpoint of courtesy, which is not important—but from the standpoint of the merits of this controversial and complex bill, certain questions which are pertinent to the bill should be answered by the Senator in charge of the bill, who is as capable as

any Senator of answering the questions. For those reasons the answers should be given before we proceed further with the consideration of the bill.

Mr. HUMPHREY. Mr. President, will the Senator yield?

Mr. PROXMIRE. I yield.

Mr. HUMPHREY. Mr. President, what is the pending question?

The PRESIDING OFFICER. The question is on agreeing to the committee amendment on page 8, line 2.

Mr. PROXMIRE. I suggest the absence of a quorum.

The PRESIDING OFFICER. The clerk will call the roll.

The legislative clerk proceeded to call the roll.

Mr. HUMPHREY. Mr. President, I ask unanimous consent that the order for the quorum call be rescinded.

The PRESIDING OFFICER. Without objection, it is so ordered.

Mr. HUMPHREY. Mr. President, I suggest the absence of a quorum.

The PRESIDING OFFICER. The clerk will call the roll.

The legislative clerk proceeded to call the roll.

Mr. HUMPHREY. Mr. President, I ask unanimous consent that the order for the quorum call be rescinded.

The PRESIDING OFFICER. Without objection, it is so ordered.

COMMITTEE MEETINGS DURING SENATE SESSION TOMORROW

Mr. HUMPHREY. Mr. President, I ask unanimous consent that the Committee on the Judiciary may be permitted to meet during the session of the Senate tomorrow.

The PRESIDING OFFICER. Is there objection? The Chair hears none, and it is so ordered.

On request of Mr. HUMPHREY, and by unanimous consent, the Committee on Commerce was authorized to meet during the session of the Senate tomorrow.

REVENUE ACT OF 1962

The Senate resumed the consideration of the bill (H.R. 10650) to amend the Internal Revenue Code of 1954 to provide a credit for investment in certain depreciable property, to eliminate certain defects and inequities, and for other purposes.

Mr. HUMPHREY. Mr. President, so that the Senate may be informed, a discussion has taken place between the Senator in charge of the bill, the Senator from Oklahoma [Mr. KERR], and the chairman of the committee, the Senator from Virginia [Mr. BYRD], the Senator from Tennessee [Mr. GORE], the Senator from Wisconsin [Mr. PROXMIRE], and other Senators relating to the procedure which it is hoped will be followed tomorrow. That procedure will be as follows:

Senators who are deeply interested in the amendments to the bill will examine each of the committee amendments and separate from them those which are controversial in terms of the need of extra debate. The other committee amendments, those which are not of a controversial nature, will be offered and will

be agreed to en bloc, so that the bill will stand as new text or as a new bill with the exception of those amendments which will be excluded from the understanding as of tomorrow.

Mr. GORE. Mr. President, will the Senator from Minnesota yield?

Mr. HUMPHREY. I yield.

Mr. GORE. The bill contains about 175 committee amendments. Most of them are minor. It is the consensus, as the Senator from Minnesota has correctly stated, that with the exception of six or eight amendments it will be possible to agree to the remaining amendments en bloc. And between now and the time when the Senate meets tomorrow, I and other Senators will go through this 400-page bill and will try to develop with the chairman of the committee, the Senator from Virginia [Mr. BYRD], the Senator from Oklahoma [Mr. KERR], and other Senators an agreement along this line.

Mr. PROXMIRE. Mr. President, will the Senator from Minnesota yield for a parliamentary inquiry?

Mr. HUMPHREY. I yield for that purpose.

Mr. PROXMIRE. I should like to ask the Presiding Officer whether it would be in order to accept some of the committee amendments and thus amend the bill, with the understanding that the bill would then be considered as original text, subject to further amendment. Is that parliamentarily possible, and would that be acceptable?

The PRESIDING OFFICER (Mr. HICKEY in the chair). The Chair understands that the proposal made by the acting majority leader is just such as the Senator from Wisconsin has outlined, and the Chair understands that the proposal is that that be ordered by unanimous consent.

Mr. PROXMIRE. I thank the Chair.

Mr. HUMPHREY. Mr. President, that is the purpose of the suggestion to which the Senator from Tennessee and I addressed ourselves—namely, that the Senate would agree to these amendments en bloc—with the major controversial amendments excluded. Then we would have, for all practical purposes, a new text; and the remaining amendments could be considered in connection with it, as amendments to that new text.

The PRESIDING OFFICER. That is in accordance with the understanding of the Chair.

Mr. HUMPHREY. Mr. President, I thank all Senators for their cooperation.

Mr. DIRKSEN. Mr. President, if the Senator from Minnesota will yield, I should like to suggest that I hope the amendments in the print will be listed and identified in such a way that will be easy for Senators to understand them, so there will not be any difficulty or objection to amendments because of any misunderstanding by Senators as to exactly what the amendments are. So I think a list should be made.

Mr. GORE. I will work with the chairman of the committee, the Senator from Virginia [Mr. BYRD], the Senator from Oklahoma [Mr. KERR], the Senator from Minnesota [Mr. PROXMIRE], the Senator from Illinois [Mr. DOUGLAS], the

Senator from Delaware [Mr. WILLIAMS], and other Senators, so that if an agreement is reached—and I am sure one will be—we shall prepare a list by means of which Senators can be guided.

Mr. DIRKSEN. And also a list of the major amendments on which separate action is sought.

MESSAGE FROM THE HOUSE

A message from the House of Representatives, by Mr. Bartlett, one of its reading clerks, announced that the House had passed, without amendment, the joint resolution (S.J. Res. 29) proposing an amendment to the Constitution of the United States relating to the qualifications of electors.

The message also announced that the House had agreed to the amendment of the Senate to the bill (H.R. 11040) to provide for the establishment, ownership, operation, and regulation of a commercial communications satellite system, and for other purposes.

ADJOURNMENT UNTIL 10 A.M. TOMORROW

Mr. HUMPHREY. Mr. President, I move that the Senate do now adjourn, in accordance with the order previously entered, until tomorrow, at 10 a.m.

The motion was agreed to; and (at 7 o'clock and 2 minutes p.m.) the Senate adjourned, under the order previously entered, until tomorrow, Tuesday, August 28, 1962, at 10 a.m.

NOMINATIONS

Executive nominations received by the Senate August 27, 1962:

U.S. COAST GUARD ACADEMY

The following-named person to be a member of the permanent commissioned teaching staff of the U.S. Coast Guard Academy with the permanent grade of lieutenant in the U.S. Coast Guard.

Roderick M. White.

IN THE ARMY

The following-named officer for promotion in the Regular Army of the United States, under the provisions of title 10, United States Code, sections 3284 and 3299:

To be major, Army Medical Specialist Corps
Jaakkola, Irma L., M10095.

The following-named officers for promotion in the Regular Army of the United States, under the provisions of title 10, United States Code, sections 3284 and 3298:

To be first lieutenants

Ferrari, Robert G., O89691.
Haight, Barrett S., O87152.

The following-named person for appointment in the Regular Army by transfer, in the grade specified, under the provisions of title 10, United States Code, sections 3283, 3284, 3285, 3286, 3287, 3288, and 3290:

To be first lieutenant, Medical Service Corps
Proe, John D. (infantry) O86664.

The following-named persons for appointment in the Regular Army of the United States, in the grades specified, under the provisions of title 10, United States Code, sections 3283, 3284, 3285, 3286, 3287, and 3288:

To be captains

Alderman, Nathaniel, Jr., O4021310.
Anderson, John H., O2207390.

Cook, Duncan S., O4034383.
 Fite, Richard A., O967710.
 Harris, Charles M., O2097057.
 Harris, Herbert D., O4009884.
 Horta-Merly, Juan, O4028565.
 Jones, Albert P., O1926754.
 McCurdy, Jasper M., O1925652.
 Mendes, Benjamin J., Jr., O4038937.
 O'Grady, Eugene J., O985238.
 Rutkowski, Joseph F., O1936070.
 Sutton, Larry L., O2265250.
 Wagner, Richard J., O4059391.
 Whipple, Ward J., O978530.

To be first lieutenants

Andre, David H., O5203830.
 Bernard, Richard A., O5206643.
 Campbell, Kenneth H., O5308214.
 Clarke, Robert G., O5400448.
 Clemons, Damon L., O5403602.
 Dick, Laurin L., O5405128.
 Durham, James A., O4084860.
 Griffiths, Allyn C., Jr., O5206207.
 Grim, Richard A., O5305259.
 Hines, Frank E., O5305879.
 Ivey, Charles E., O5507803.
 Langer, Joseph A., Jr., O5301530.
 McNamara, Michael J., O5000374.
 McReynolds, Samuel O., O5401449.
 Moldaschel, William A., O5509278.
 Nock, Jean A., Jr., O4069492.
 Perry, Robert P., O5001462.
 Ray, Thomas L., Jr., O5305215.
 Roberts, Hollis L., O5200011.
 Robinson, Charles W., O5300124.
 Rogers, Hugh K., Jr., O5303149.
 Simpson, Robert B., O4063208.
 Spence, Ray L., O4049502.
 Townsend, Robert F., O4052876.
 Walsh, Thomas A., Jr., O5508433.

To be second lieutenants

Andrews, Raymond G., O5306383.
 Bolton, Peter A., O5000752.
 Conte, Richard E., O5005624.
 Gillette, Samuel G., O6307460.
 Grant, Lawrence M., Jr., O5309625.
 Griffey, Joseph P., O5208840.
 Haas, Steven L., O5309324.
 Hamby, Larry B., O5213244.
 Harvell, Kenneth E., O5403651.
 Hunt, John W., O5309815.
 Junod, Joseph J., O5209857.
 Karsteter, Robert B., O5401701.
 King, Stanley L., Jr., O5006123.

Kinkade, David R., O5705363.
 Michie, Richard L., O5512018.
 Mylks, Herbert W., O5210908.
 Paquette, Edward H., O5308913.
 Paradowski, Charles E., O5403166.
 Peters, Shelton V., O5404237.
 Rogers, Martin M., O5510511.
 Vinci, Frank, Jr., O5211469.
 Wharton, Gerald M., O5211184.
 Willms, Walter R., O5412312.
 Wolfarth, William M., Jr., O5310259.

The following-named persons for appointment in the Regular Army of the United States, in the grades and corps specified, under the provisions of title 10, United States Code, sections 3283, 3284, 3285, 3286, 3287, 3288, 3289, 3290, 3291, 3293, 3294, and 3311:

To be captains, Chaplain

Floyd, William R., O2003168.
 Johnson, Kermit D., O2274589.

To be captains, Dental Corps

Auzins, Janis, Jr., O5500647.
 Call, Robert I., O2211948.
 Kennemer, Thomas O., Jr., O4062586.
 Urick, Howard B., O2205634.

To be captains, Medical Corps

Hernandez-Fragoso, Ignacio, O5213679.
 Hinckley, Robert F., O4046342.
 Hughes, Charles R., O5312888.
 Jackson, John K., Jr., O1880831.
 Molina y Vedia, Marcel, O2309691.
 Pappas, Michael T., O5213024.
 Park, Robert C., O2291916.
 Shroyer, Joseph M., O2309863.

To be captain, Medical Service Corps

Barnett, Lacy C., O1878565.

To be captain, Veterinary Corps

Keel, James E., O2295309.

To be first lieutenants, Army Nurse Corps

Christ, Nancy M., N2304803.
 Glor, Beverly A. K., N2303633.

To be first lieutenants, Chaplain

Blunt, Kenneth L., O5500455.
 Hyde, Patrick H., O5407755.
 Kieschnick, Alton R., O5501028.

To be first lieutenants, Dental Corps

Gary, Ralph R., O5003455.
 Hirsch, Edward H., O5004867.
 Hirsch, Herbert I., O5206837.

Rodenburg, Carl E., O5012677.

To be first lieutenants, Medical Corps

Burton, Thomas H., O2305101.
 Cooper, Edgar L., O2300670.
 Hutchison, William A., O2305187.
 Levy, Morris S., O2300692.

To be first lieutenant, Women's Army Corps

Lipner, Lois, L5004860.

To be second lieutenants, Army Nurse Corps

Garfall, Gloria M., N2304927.
 Irvine, Leona R., N5407064.
 Rolfe, Agnes O., N5407457.

To be second lieutenant, Medical Service Corps

Anderson, Charles H., O4070138.

To be second lieutenants, Women's Army Corps

Bradford, Loyce A., L2304804.
 Frisk, Helen E., L2304921.

The following-named distinguished military students for appointment in the Medical Service Corps, Regular Army of the United States, in the grade of second lieutenant, under the provisions of title 10, United States Code, sections 3283, 3284, 3285, 3286, 3287, 3288, and 3290:

Katsuyoshi, Charles M.
 Kreuter, Robert H., Jr.
 Zimmerman, Harry R.

The following-named distinguished military students for appointment in the Regular Army of the United States in the grade of second lieutenant, under the provisions of title 10, United States Code, sections 3283, 3284, 3285, 3286, 3287, and 3288:

Adams, Paul G.	Lindsay, Larry A.
Brazil, Daniel S.	McBroom, Billy W.
Burns, Frank L.	McKay, Donald M., Jr.
Carlson, John P.	McTernan, Bernard
Carver, Troy V.	Machus, Robert J.
Cooper, Fredrick C.	Memec, Carl J.
Crume, Thomas E.	Pinon, Richard A.
Edwards, William W.	Sakamoto, Shiori
Fivian, James A.	Simpson, Benjamin E.
Florreich, James H.	Simpson, Patrick J.
Frost, Leonard D., Jr.	Smith, Hubert G.
Goodfellow, Michael P.	Stenning, Simon A. J.
Hagedorn, Ronald S.	Taylor, John V., Jr.
Hill, Thomas F.	O5516869.
Hunter, Paul C.	Tinberg, Larry R.

Digest of CONGRESSIONAL PROCEEDINGS

INTEREST TO THE DEPARTMENT OF AGRICULTURE

OFFICE OF
BUDGET AND FINANCE

(For information only;
should not be quoted
or cited)

Issued August 29, 1962
For actions of August 28, 1962
87th-2d, No. 154

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HIGHLIGHTS: House Rules Committee reported rule to send farm bill to conference. Several Senators defended Under Secretary Murphy against recent criticism. House passed appropriations continuation resolution. House began debate on public works acceleration bill. Rep. Johnson, Wis., inserted Secretary's statement criticizing CED farm policy report. Senate subcommittee voted to report roads bill. Senate committee reported measure for designation of National School Lunch Week.

HOUSE

- 1. APPROPRIATIONS.** Passed without amendment H. J. Res. 864, the appropriations continuation resolution to make temporary appropriations until September 30, 1962, for those departments and agencies whose annual appropriation bills have not yet been enacted. p. 16847
- 2. FARM PROGRAM.** The Rules Committee reported a resolution to send to conference H. R. 12391, the proposed Food and Agriculture Act of 1962. p. 16922
Rep. Johnson, Wis., criticized the farm policy proposals of the Committee for Economic Development and inserted a statement by Secretary Freeman criticizing these proposals. pp. 16909-12
- 3. COMMITTEES.** Rep. Marshall resigned from, and Rep. Smith, Iowa., was elected to, the Appropriations Committee. p. 16847
- 4. PUBLIC WORKS.** Began debate on H. R. 10113, the public works acceleration bill. pp. 16855-95

5. PARKS. Rep. Aspinall, Rep. Rutherford, and Rep. Saylor urged enactment of S. 2429, to revise the boundaries of the Virgin Islands National Park, St. John, V.I. pp. 16896-7
6. MILK. Rep. Halpern discussed the radioactive contamination of milk and said, "The problem of radioactive fallout is clearly a Federal responsibility." pp. 16918-20
7. PERSONNEL; VETERANS. Received from the Defense Department a proposed bill "to exempt certain Reserve officers of the Army or Air Force from the dual compensation restrictions of the Economy Act of June 30, 1962, as amended"; to Armed Services Committee. p. 16921

SENATE

8. FARM PROGRAM. Sens Morse, Burdick, Humphrey, Ervin, Sparkman, and Carroll commended the integrity, honesty, and public service of Under Secretary Murphy, and defended him against recent criticism relative to his role in the Estes case. pp. 16803-8
9. ROADS. The Subcommittee on Public Roads of the Public Works Committee voted to report to the full committee with amendments H. R. 12135, the road authorization bill. The "Daily Digest" states that one of the amendments would "add \$10 million for fiscal 1963 for forest roads and trails."
10. SCHOOL LUNCH. The Judiciary Committee reported without amendment S. J. Res. 211, providing for the designation of a week each year as National School Lunch Week (S. Rept. 1929). p. 16752
11. FORESTRY. The Interior and Insular Affairs Committee voted to report with amendment (but did not actually report) S. 2387, to authorize the establishment of the Canyonlands National Park, Utah. p. D778
Sen. Cooper submitted an amendment intended to be proposed to H. R. 8355, authorizing executive agencies to grant easement in, over, or upon real property of the U. S., so as to exclude lands reserved, dedicated, or acquired for national forest purposes. pp. 16753-4
12. TAXATION. Continued debate on H. R. 10650, the proposed Revenue Act of 1962 (pp. 16767-803, 16808-9, 16814-46). Agreed to the committee amendment relating to taxation of cooperatives, but deferred until later consideration of the committee amendment relating to deductions for farmers for land-clearing expenses (See Digest 150 for a summary of these amendments)(pp. 16767-90).
13. AMERICAN SAMOA. Agreed to the conference report on H. R. 10062, to extend the application of certain laws to American Samoa (see Digest 150 for an explanation of the bill as reported out of conference). p. 16813-4
14. LOANS. Agreed to the House amendments to S. 3327, to make certain federally impacted areas eligible for assistance under the public facility loan program. This bill will now be sent to the President. p. 16814
15. TRANSPORTATION. The Commerce Committee voted to report (but did not actually report) with amendment S. 3509, to place transactions involving unifications or acquisitions of control of freight forwarders under regulation of the Interstate Commerce Act. p. D778

Staff contended that present policy of Commission is in error for three major reasons:

"The use of liberalized depreciation results in a tax saving or reduction and not in tax deferral.

"There is nothing in the legislative history of section 167 that requires the Commission to allow a natural gas company more taxes than actually payable, or that requires the customers of a natural gas company to advance capital to that company.

"There is no similarity of purpose or applicability between accelerated amortization of defense facilities under section 168 of the Internal Revenue Code and liberalized depreciation under section 167 of that code."

Commission staff also discussed "economic impact on the consumer arising from the use of the normalization method (present policy) and the benefits to be derived by the natural gas company and the consumer by the change over to the flow-through method."

Mr. PROXMIRE. The second action of the Commission staff which I wish to bring to the attention of the Senate occurred last Tuesday, August 21, 1 day after the Alabama-Tennessee brief was filed. I am referring now to the so-called Pemex case. In this action the staff asked the Commission to dismiss applications to build a \$225 million natural gas pipeline from Texas through Mexico to southern California.

The staff introduced the motion to dismiss the applications on two grounds: First—and I am now quoting from the staff brief:

It is obvious that the proposals contained in the applications, if certificated, would have an immediate inflationary impact of immeasurable proportions upon field prices generally.

Secondly, the staff pointed out that the planned uses of the gas are "inferior uses and are to be permitted only on a positive showing that the public interest requires them." In other words, the staff argued that there are better uses—uses having higher priority—for the gas than the use for which the applicants wanted the gas.

In this case, then, the Commission staff was not only representing the consumer in arguing against an unnecessary price rise, but also attempting to prevent the long-range misallocation of our gas resources.

Mr. President, both these examples show the Commission staff actively engaged in upholding the public interest. They are not standing back and letting the case be decided on the narrow issues that may be raised by the adversaries. Rather the staff has conducted its own study and investigation and has made recommendations, supported by evidence and logic. This shows that an active, able staff in an independent agency can go a long way toward providing essential representation of the public interest in regulatory proceedings.

Naturally, the staff needs the support and encouragement of the Commission. I am sure that without the support of the FPC's able chairman, Mr. Joseph Swidler, it would not have been possible for the staff to develop and present these two outstanding briefs. I congratulate Mr. Swidler for his wisdom and foresight in supporting his staff in these endeavors—and I congratulate the staff for their fine work in the two cases I have referred to.

Mr. President, I ask unanimous consent that the article from the August 23, Wall Street Journal be printed at this point in the RECORD.

There being no objection, the article was ordered to be printed in the RECORD, as follows:

FPC ATTORNEYS OPPOSE GASLINE ACROSS MEXICO

WASHINGTON.—Federal Power Commission attorneys asked the FPC to dismiss applications to build a \$225 million natural gas pipeline from Texas through Mexico to southern California.

Staff lawyers said it was "pointless" to continue hearings on the proposal because it "flies in the face of two very fundamental policy concepts of the Commission." For one thing, they said, it would have "an immediate inflationary impact of immeasurable proportions" on gas prices. For another, it would "promote inferior uses of a limited supply of natural gas."

The 1,600-mile pipeline ultimately would carry about 380 million cubic feet of natural gas daily from Texas fields for Southern California Edison Co. to use in driving steam-powered electric generators. Edison would buy about 82 percent of the gas from Humble Oil & Refining Co., subsidiary of Standard Oil Co. (New Jersey).

MEXICAN GAS WOULD BE ADDED

From Texas fields, the gas would move to the Mexican border in a \$12 million pipeline to be built by Tennessee California Gas Transmission Co., a subsidiary of Tennessee Gas Transmission Co. The gas would be picked up by Petroleos Mexicanos, an agency of the Mexican Government that proposes to build \$165 million of pipeline facilities; Mexican-produced gas would be added to the load.

At the California border, California Gas Transmission Co., another Tennessee Gas subsidiary, would take over and distribute the gas to five Edison generating stations through \$48 million of pipeline.

An Edison spokesman in Los Angeles said he was "still convinced the pipeline is a very sound project." He said the company wouldn't comment further until the report asking the dismissal had been studied. Humble and Tennessee Gas officials declined to comment on the recommendation.

Hearings on the proposed project began in April but have been recessed until October 2. The FPC could rule on the staff's dismissal motion before the hearings reconvene. The companies have 10 days to challenge the motion. Commission attorneys said the companies "have presented all of their evidence and it falls short of justifying the proposed project. A failure to dismiss at this juncture will only result in a waste of time and money."

The staff lawyers said the price Edison proposes to pay is 2 to 3½ cents a thousand cubic feet more than the "area price" ceiling of 18 cents a thousand cubic feet the FPC set for the Texas area. To channel a large amount of gas to one consumer at a high price, the lawyers asserted, would "increase demands on a limited supply of gas" and "have the effect of propelling field prices upward."

CONSERVING NATURAL GAS

"In addition to its concern with maintaining stable gas prices," the lawyers stated, "the Commission is equally concerned with conserving natural gas * * * where other fuels are in ample abundance to meet inferior fuel demands of industry generally and of steam-electric plants particularly."

The lawyers said Edison's proposed use of the gas "is far more prolific than in typical boiler fuel cases * * * in its present form, this case very simply involves the transference of tremendous gas reserves from producing fields directly to burner tips for use

in the steam generation of electricity. There are to be no complementary benefits to domestic and commercial gas users—because no such users are contemplated to receive service."

The attorneys said "there is no assertion by Edison that oil, as an alternate fuel, is not available in quantities sufficient to satisfy all of its needs" not met by Southern California Gas Co., Southern Counties Gas Co., and Pacific Lighting Gas Supply Co., west coast gas distributors who oppose the project because they claim it will rob them of their principal customer, Edison.

The staff also challenged Edison estimates it could save \$173 million over the next 20 years by buying its gas directly from Texas. The FPC attorneys said the company's cost estimates of the Pemex project gas were low and were compared with "unreasonably high estimates" of the cost of gas from existing suppliers.

Edison's savings estimates, the lawyers added, are based also on "the belief that this Commission will permit uncontrolled price increases in the cost of gas in the field. If this be so, then [Edison's estimates] may have a certain validity. However, any prediction of future field prices premised on the assumption this Commission will permit field prices to barrel along at ever higher levels is patently ridiculous."

The attorneys charged, "It is the inflationary forces set in motion by companies like Edison that causes the prices of future acquisitions of gas by others to be at even higher plateaus. When these forces are kept under control, anticipated long-range savings would no longer be a motivation to large industrial companies attempting to obtain and hoard their own supply of natural gas * * * to the detriment of the remainder of the gas-consuming public."

Attacking contentions that the project would promote petroleum exploration in Mexico, the FPC staff commented, "building a pipeline to induce exploration seems to be a reversal of the usual practice of finding commercial deposits of gas or oil and then constructing the pipeline to take the product to market." They asserted that evidence of much petroleum deposits in the path of the pipeline was "quite sketchy. In any event, there is no prognostication that a pipeline passing through Mexico will stimulate the development of gas reserves equivalent to the 2½ trillion cubic feet of Texas-produced gas which Edison proposes to burn in its boilers."

The FPC staff also struck out at assertions that the project would bolster competition in the California fuel market. "Any competition engendered by the Pemex project will be unfair competition," they charged. "The existing gas distribution companies and interstate gas pipelines would simply be outdistanced in the race for industrial customers * * * so eagerly sought by the promoters of Pemex."

The PRESIDING OFFICER. Is there further morning business? If not, morning business is closed.

REVENUE ACT OF 1962

Mr. KERR. Mr. President, I ask that the Chair lay before the Senate the unfinished business.

Without objection, the Senate resumed the consideration of the bill (H.R. 10650) to amend the Internal Revenue Code of 1954 to provide a credit for investment in certain depreciable property, to eliminate certain defects and inequities, and for other purposes.

The PRESIDING OFFICER (Mr. LAUSCHE in the chair). The question is on agreeing to the committee amendment on page 8, in lines 2 and 3.

Mr. KERR. Mr. President, after consultation with the distinguished Senator from Tennessee [Mr. GORE], the Senator from Illinois [Mr. DOUGLAS], the Senator from Delaware [Mr. WILLIAMS], and the Senator from Virginia [Mr. BYRD], I should like to propound a unanimous-consent request; namely, that the following amendments—which I shall designate specifically in a moment—are not agreed to by this unanimous-consent request—

Mr. DOUGLAS. Mr. President, will the Senator from Oklahoma yield for a moment?

Mr. KERR. I yield.

Mr. DOUGLAS. The Senator from Oklahoma means the following committee amendments; does he not?

Mr. KERR. That is correct.

Mr. President, I was saying that I wish to propound the following unanimous-consent request: That the following committee amendments are to be considered in succession, following consideration of the amendment to section 2, which is to be offered by the senior Senator from Virginia [Mr. BYRD]; that all other committee amendments are agreed to en bloc and are to be considered as part of the original text of the bill, and subject to further amendment; and that after consideration by the Senate of the 11 amendments which I shall not specifically identify—being committee amendments—and after they are acted on by the Senate, the entire bill then shall be considered as part of the original text, and subject to further amendment.

The specific amendments to be excepted from this agreement, as heretofore stated, are as follows:

First. The committee amendment on page 41, in line 18, through page 42, in line 4, and page 42, in line 7, being the expense account amendment.

Second. The committee amendment eliminating entirely section 482 of the bill. This section would have strengthened the allocation formula in section 482 of the code; and the committee amendment is on page 52, line 1, through page 57, in line 22.

Third. The gross-up committee amendment, on page 121, in line 3, through page 127, in line 1.

Fourth. The withholding committee amendment, on page 307, line 9, through page 369, line 19.

Fifth. The clearing land committee amendment, on page 381, line 16, through page 384, line 24.

Sixth. The charitable contributions amendment, on page 385, line 1, through page 386, line 6.

Seventh. The determination of the number of stockholders committee amendment, on page 386, line 7, through page 388, line 10.

Eighth. The committee amendment on the Twin Cities Street Railway, on page 388, line 11, through page 389, line 14.

Ninth. The committee amendment on the pension plan for the Hod Carriers Union, on page 389, line 15, through page 390, line 8.

Tenth. The committee amendment on the surviving partner in a two-man

partnership, on page 390, line 9, through page 391, line 21.

Eleventh. The committee amendment on page 305, in lines 23 and 24.

Mr. GORE. Mr. President, will the Senator from Oklahoma yield?

Mr. KERR. I yield.

Mr. GORE. The last six amendments are not major ones, except the very last one, which is the—

Mr. KERR. I think the Senator from Tennessee means the last seven.

Mr. GORE. Yes, except the last one, which has been temporarily requested by the senior Senator from Ohio. They are proposed additions to the bill or so-called riders to the bill—

Mr. KERR. They are not completely related to the other parts of the bill.

Mr. GORE. That is correct. So this proposed agreement will reduce the number of controversial committee amendments to five major subject matters; and, in addition, the agreement will make it in order, before action on any of these exceptions to the en bloc agreement, for the chairman of the committee to offer an amendment to section 2.

Mr. SMATHERS. Mr. President, will the Senator from Oklahoma yield for a question?

Mr. KERR. I yield.

Mr. SMATHERS. The amendment the able chairman of the committee expects to offer deals with the investment credit provision, does it not?

Mr. KERR. That is correct; and it is one of the amendments which, under the proposed unanimous-consent agreement, will become part of the original text of the bill, and subject to further amendment.

Mr. JAVITS. Mr. President, will the Senator from Oklahoma yield for a question?

Mr. KERR. I yield.

Mr. JAVITS. What will be the situation of Senators who wish to amend section 12, relating to controlled foreign corporations?

Mr. KERR. As I understand, any Senator who wishes to have any part of the bill amended will be in a position identically the same as that he would be in either if this unanimous-consent request is agreed to or if it is not agreed to. Ordinarily a unanimous-consent agreement is made in regard to all committee amendments—in other words, that they be agreed to en bloc and considered part of the original text to the bill, and subject to further amendment. But such a unanimous-consent request, when made yesterday, was objected to.

The unanimous-consent agreement now being requested is proposed after consultation with Senators who lodged the objection yesterday.

The result of this unanimous-consent agreement, if entered into, will be that all of the committee amendments, except the 11 committee amendments specifically excepted, will be agreed to en bloc, and of course, will be subject to amendment by any Member, but not until the committee amendments which have not been agreed to and have not, by means of this agreement, been made part of the original text, and subject to

amendment, have been acted upon, whereupon, after the action on all the committee amendments is completed, the ones agreed to will be part of the original text; and then the entire bill, as it then will stand, will be subject to amendment, the same as though the request made yesterday had been agreed to.

Mr. JAVITS. In dealing with those 11 amendments, would it be more efficient to complete our action on them before other amendments are offered?

Mr. KERR. That would be in order.

Mr. JAVITS. Perhaps I misunderstood the Senator.

Mr. KERR. Then let me address a parliamentary inquiry to the Chair: When a committee amendment is not made a part of the original text, is not that amendment open to amendment when the Senate is considering it?

The PRESIDING OFFICER. The answer is in the affirmative.

Mr. JAVITS. Mr. President, a parliamentary inquiry: When amendments are offered to amendments which have not been made part of the original text, are not such amendments therefore limited to amendments in the second degree—which means only one amendment or no substitute?

The PRESIDING OFFICER. As a general rule, amendments in the second degree are always in order.

Mr. JAVITS. And therefore, in the case of amendments which are not incorporated in the bill as part of the original text, there would be the possibility of only one amendment, which would itself be a second-degree amendment?

The PRESIDING OFFICER. One amendment to the amendment.

Mr. JAVITS. Yes.

Let me ask the Senator from Oklahoma whether among the 11 committee amendments enumerated is included the entire committee amendment with regard to controlled foreign corporations—section 12?

Mr. KERR. No, it is not.

Mr. JAVITS. So that would be in the original text of the bill, as covered by the unanimous-consent request?

Mr. KERR. Yes.

Mr. JAVITS. Does the proposed agreement also include the savings and loan provision?

Mr. KERR. Yes.

Mr. JAVITS. So that one, too, under this agreement, would be made part of the original text?

Mr. KERR. Yes.

Mr. DOUGLAS. Mr. President, will the Senator from Oklahoma yield for a clarification and explanation of a point?

The PRESIDING OFFICER (Mr. Young of Ohio in the chair). Does the Senator from Oklahoma yield to the Senator from Illinois?

Mr. KERR. I yield.

Mr. DOUGLAS. In the original discussions with the Senator from Oklahoma, it was proposed by the Senator from Tennessee [Mr. GORE] and myself that the lobbying provision would also have to be proposed as a committee amendment. It will be noticed, upon a

close reading of the RECORD, that this one is not now included in the exceptions.

Mr. KERR. Yes.

Mr. DOUGLAS. And this has been done with the full agreement of the Senator from Tennessee [Mr. GORE] and myself.

I think perhaps it is appropriate, however, that the RECORD should show why we agreed to this. It will be remembered that the original House bill made no alteration in the law concerning deductions for lobbying. The House Ways and Means Committee, at the last moment, without anyone really knowing what had happened, added a provision which permitted deductions for direct lobbying by business interests which had a business concern in legislation. This legitimized tax deductions for direct lobbying on the part of officers, employees, and other representatives, and mass representation before not only Congress, but State legislatures, local councils, county bodies, and the like.

The Senate Finance Committee endorsed this provision and went it one better. It also permitted deductions for expenses connected with all communications on legislation between officers of the companies, stockholders, members, and employees, so that a company could circularize its stockholders, employees, and associates against a measure and get them to lobby and charge this as a business lobbying deduction. In other words, it would have permitted as a deduction from taxable income expenses in connection with efforts made by building and loan associations and certain mutual savings banks to strike out the withholding plan, and would legitimize and have the Treasury pay 52 percent of the expenses of DuPont Co. in connection with efforts in favor of the DuPont tax bill which Congress passed so overwhelmingly in the early part of the year.

Likewise, it would permit the deduction of expenses by A.T. & T. in getting the satellite communications bill through Congress so that Uncle Sam would pick up 52 percent of those costs.

In the opinion of some of us, this is a gross abuse, and we object not only to the Senate amendment, but to the House provision.

Therefore, for technical reasons, in order to have one vote taken instead of two, we have agreed to the committee amendment on this point with the understanding that at an appropriate time I shall offer an amendment to strike both the House and the Senate provisions.

I will say in advance we will not prolong the discussion on this point. I think it could well be concluded, in view of the adequate discussion which we had yesterday in 1½ or 2 hours. On behalf of the Senator from Tennessee, the Senator from Wisconsin, and myself, I am ready to agree to a limitation of 2 hours on this amendment when such a request is made, and I hope no motion to table will be entered against it.

Mr. MANSFIELD. Mr. President, will the Senator yield?

Mr. DOUGLAS. I yield.

Mr. MANSFIELD. I think the Senator is more than fair. If it is agreeable, I would like to give favorable consideration to a limitation of 2 hours on that particular amendment.

Mr. DOUGLAS. It is understood, I hope, that this exclusion of the lobbying provision from the agreement which is now being made does not mean in any degree that those who are opposed to both lobbying amendments have folded their tents and withdrawn from the battle. Quite the contrary, is true; we are going to take the field and do our best. In the meantime, I strongly urge Members of the Senate, of the press, and citizens to read the debate of yesterday on lobbying, because I think these provisions are indefensible.

At present the law is neutral so far as lobbying is concerned. The law does not permit deductions either by special business interests or advocates of the general interest. But this amendment would permit the special interests to take their deductions, but would not permit the individual citizen to get the deduction. It would be difficult for him to do that, anyway; but this is a one-sided furnishing of additional weapons to those who already have nearly all the resources.

I do not think the conscience of the country can long stand these two amendments.

I make this explanation so that we can know exactly where the lines of battle are drawn and what the issues are.

I thank the Senator from Oklahoma for giving me permission to make this statement.

The PRESIDING OFFICER. Is there objection to the unanimous-consent request? The Chair hears none, and it is so ordered.

The amendments agreed to en bloc are as follows:

At the top of page 2, in the table of contents, to strike out:

"Sec. 1. Short title, etc.

(a) Short title.

(b) Table of contents.

(c) Amendment of 1954 code.

"Sec. 2. Credit for investment in certain depreciable property.

(a) Allowance of credit.

(b) Rules for computing credit.

(c) Certain corporate acquisitions.

(d) Clerical amendments.

(e) Effective date.

"Sec. 3. Appearances, etc., with respect to legislation.

(a) In general.

(b) Effective date.

"Sec. 4. Disallowance of certain entertainment, etc., expenses.

(a) Denial of deduction.

(b) Traveling expenses.

(c) Effective date.

"Sec. 5. Amount of distribution where certain foreign corporations distribute property in kind.

(a) Amount distributed.

(b) Basis.

(c) Dividends received from certain foreign corporations.

(d) Credit for foreign taxes.

(e) Effective date.

"Sec. 6. Amendment of section 482.

(a) In general.

(b) Clerical amendment.

(c) Effective date.

"Sec. 7. Distributions of foreign personal holding company income.

(a) Definition of foreign personal holding company.

(b) Amount of undistributed income.

(c) Effective date.

"Sec. 8. Mutual savings banks, etc.

(a) Reserves for losses on loans.

(b) Foreclosure on property securing loans.

(c) Definition of domestic building and loan association.

(d) Clerical amendments.

(e) Repeal of exemption from communications and transportation of persons taxes.

(f) Effective dates.

"Sec. 9. Distributions by foreign trusts.

(a) Definitions.

(b) Accumulation distributions of foreign trusts.

(c) Allocation of accumulation distributions to preceding years.

(d) Amounts treated as received in prior years.

(e) Special rules for foreign trusts.

(f) Information returns with respect to foreign trusts.

(g) Failure to file information returns.

(h) United States person defined.

(i) Technical amendments.

(j) Effective date.

"Sec. 10. Mutual insurance companies (other than life, marine, and certain fire insurance companies), etc.

(a) Imposition of tax.

(b) Taxable investment income.

(c) Statutory underwriting income or loss.

(d) Mutual fire insurance companies operating on basis of premium deposits.

(e) Election of certain mutual companies to be taxed on total income.

(f) Technical amendments, etc.

(g) Effective date.

"Sec. 11. Domestic corporations receiving dividends from foreign corporations.

(a) Entire amount of foreign tax to be taken into account.

(b) Inclusion in gross income of amount equal to taxes deemed paid.

(c) Determination of source of dividends received from certain foreign corporations.

(d) Repeal of section 902(d).

(e) Technical amendments.

(f) Effective date.

"Sec. 12. Earned income from sources without the United States.

(a) Limitation on amount and type of income excluded.

(b) Computation of employees' contributions.

(c) Effective date.

"Sec. 13. Controlled foreign corporations.

(a) In general.

(b) Technical and clerical amendments.

(c) Effective date.

"Sec. 14. Gain from dispositions of certain depreciable property.

(a) In general.

(b) Change in method of depreciation.

(c) Salvage value of personal property.

(d) Special rule for charitable contributions of section 1245 property.

(e) Technical amendments.

(f) Effective date.

- "Sec. 15. Foreign investment companies.
 (a) Treatment of sale of stock of foreign investment companies.
 (b) Conforming amendments.
 (c) Effective date.
- "Sec. 16. Gain from certain sales or exchanges of stock in certain foreign corporations.
 (a) Treatment of gain from the redemption, cancellation, or sale of stock in certain corporations.
 (b) Clerical amendment.
 (c) Effective date.
- "Sec. 17. Tax treatment of cooperatives and patrons.
 (a) In general.
 (b) Technical amendments.
 (c) Effective dates.
- "Sec. 18. Inclusion of foreign real property in gross estate.
 (a) Amendments to include foreign real property.
 (b) Effective date.
- "Sec. 19. Withholding of income tax at source on interest, dividends, and patronage dividends.
 (a) In general.
 (b) Credits against income tax for tax withheld.
 (c) Interest and dividends paid to nonresident aliens, etc.
 (d) Credit for States and tax exempt organizations.
 (e) Other technical amendments.
 (f) Effective dates.
- "Sec. 20. Information with respect to certain foreign entities.
 (a) Information to be furnished by individuals, domestic corporations, etc., with respect to certain foreign corporations.
 (b) Information as to organization or reorganization of foreign corporations and as to acquisitions of their stock.
 (c) Civil penalty for failure to file return.
 (d) Technical amendments.
 (e) Effective date.
- "Sec. 21. Treaties."
 And, in lieu thereof, to insert:
- "Sec. 1. Short title, etc.
 (a) Short title.
 (b) Table of Contents.
 (c) Amendment of 1954 code.
- "Sec. 2. Credit for investment in certain depreciable property.
 (a) Allowance of credit.
 (b) Rules for computing credit.
 (c) Deduction for unused credit."
 (d) Certain corporate acquisitions.
 (e) Statutes of limitations and interest relating to investment credit carrybacks.
 (f) Technical amendment.
 (g) Clerical amendments.
 (h) Effective date.
- "Sec. 3. Appearances etc., with respect to legislation.
 (a) In general.
 (b) Effective date.
- "Sec. 4. Disallowance of certain entertainment, etc., expenses.
 (a) Denial of deduction.
 (b) Traveling expenses.
 (c) Effective date.
- "Sec. 5. Amount of distribution where certain foreign corporations distribute property in kind.
 (a) Amount distributed.
 (b) Basis.
 (c) Dividends received from certain foreign corporations.
 (d) Effective date.

- "Sec. 6. Mutual savings banks, etc.
 (a) Reserves for losses on loans.
 (b) Foreclosure on property securing loans.
 (c) Definition of domestic building and loan association.
 (d) Clerical amendments.
 (e) Repeal of exemption from certain excise taxes.
 (f) Deduction for dividends or interest paid on deposits.
 (g) Effective dates.
- "Sec. 7. Distribution by foreign trusts.
 (a) Definitions.
 (b) Accumulation distributions of foreign trusts.
 (c) Allocation of accumulation distributions to preceding years.
 (d) Amounts treated as received in prior years.
 (e) Special rules for foreign trusts.
 (f) Information returns with respect to foreign trusts.
 (g) Failure to file information returns.
 (h) United States person defined.
 (i) Technical amendments.
 (j) Effective date.
- "Sec. 8. Mutual insurance companies (other than life, marine, and certain fire and flood insurance companies), etc.
 (a) Imposition of tax.
 (b) Taxable investment income.
 (c) Statutory underwriting income or loss.
 (d) Exemption from tax.
 (e) Mutual fire insurance companies operating on basis of premium deposits.
 (f) Election of certain mutual companies to be taxed on total income.
 (g) Technical amendments, etc.
 (h) Effective date.
- "Sec. 9. Domestic corporations receiving dividends from foreign corporations.
 (a) Foreign taxes deemed paid by domestic corporations.
 (b) Inclusion in gross income of amount equal to taxes deemed paid.
 (c) Determination of source of dividends received from certain foreign corporations.
 (d) Technical amendments.
 (e) Effective date.
- "Sec. 10. Separate limitation on foreign tax credit with respect to certain interest income.
 (a) Limitation on foreign tax credit.
 (b) Effective date.
- "Sec. 11. Earned income from sources without the United States.
 (a) Limitation on amount and type of income excluded.
 (b) Computation of employees' contributions.
 (c) Effective date.
- "Sec. 12. Controlled foreign corporations.
 (a) In general.
 (b) Technical and clerical amendments.
 (c) Effective date.
- "Sec. 13. Gain from dispositions of certain depreciable property.
 (a) In general.
 (b) Change in method of depreciation.
 (c) Salvage value of personal property.
 (d) Special rule for charitable contributions of section 1245 property.

- (e) Computation of taxable income for purposes of limitation on percentage depletion deduction.
 (f) Technical amendments.
 (g) Effective dates.
- "Sec. 14. Foreign investment companies.
 (a) Treatment of sale of stock of foreign investment companies.
 (b) Conforming amendments.
 (c) Effective date.
- "Sec. 15. Gain from certain sales or exchanges of stock in certain foreign corporations.
 (a) Treatment of gain from the redemption, cancellation, or sale of stock in certain foreign corporations.
 (b) Clerical amendment.
 (c) Effective date.
- "Sec. 16. Sales and exchanges of patents, etc., to certain foreign corporations.
 (a) Treatment of gain as ordinary income.
 (b) Clerical amendment.
 (c) Effective date.
- "Sec. 17. Tax treatment of cooperatives and patrons.
 (a) In general.
 (b) Technical amendments.
 (c) Effective dates.
- "Sec. 18. Inclusion of foreign real property in gross estate.
 (a) Amendments to include foreign real property.
 (b) Effective date.
- "Sec. 19. Reporting of interest, dividend, and patronage dividend payments of \$10 or more during a year.
 (a) Returns regarding payment of dividends.
 (b) Returns regarding payment of patronage dividends.
 (c) Returns regarding payment of interest.
 (d) Penalties for failure to file information returns.
 (e) Penalties for failure to furnish statements to persons with respect to whom returns are filed.
 (f) Technical amendments.
 (g) Clerical amendments.
 (h) Effective dates.
- "Sec. 20. Information with respect to certain foreign entities.
 (a) Information to be furnished by individuals, domestic corporations, etc., with respect to certain foreign corporations.
 (b) Information as to organization or reorganization of foreign corporations and as to acquisitions of their stock.
 (c) Civil penalty for failure to file return.
 (d) Technical amendments.
 (e) Effective date.
- "Sec. 21. Expenditures by farmers for clearing land.
 (a) Allowance of deduction.
 (b) Clerical amendment.
 (c) Effective date.
- "Sec. 22. Charitable contributions made from income attributable to several taxable years.
 (a) Treatment for purposes of part I of subchapter Q.
 (b) Effective date.
- "Sec. 23. Effective date of section 1371(c) of the Internal Revenue Code of 1954.
 (a) In general.
 (b) Election and consent by corporations; consents by shareholders.

(c) Tolling of statutes of limitations.

"Sec. 24. Certain losses sustained in converting from street railway to bus operations.

(a) In general.

(b) Unused conversion loss defined.

(c) Treatment of unused conversion loss.

(d) Regulations.

"Sec. 25. Pension plan of Local Union Numbered 435, International Hod Carriers' Building and Common Laborers' Union of America.

"Sec. 26. Continuation of a partnership year for surviving partner in a two-man partnership where one dies.

(a) Close of taxable year of two-man partnership when one partner dies.

(b) Effective date, etc.

"Sec. 27. Treaties."

On page 8, line 2, after the word "Code" and the period, to strike out "Whenever" and insert "Except as otherwise expressly provided, whenever".

In section 2, on page 8, line 12, after the word "section", where it appears the second time, to strike out "40" and insert "39"; on page 11, at the beginning of line 3, to insert "carryback or"; after line 16, to strike out:

"(b) 5-YEAR CARRYOVER OF UNUSED CREDITS.—

"(1) ALLOWANCE OF CREDIT.—If the amount of the credit determined under subsection (a) (1) for any taxable year exceeds the limitation provided by subsection (a) (2) for such taxable year (hereinafter in this subsection referred to as 'unused credit year'), such excess shall be added to the amount allowable as a credit by section 38 for each of the 5 succeeding taxable years to the extent not taken into account for taxable years intervening between the unused credit year and such succeeding taxable year.

"(2) LIMITATIONS.—The amount of the unused credit which may be added under paragraph (1) for any succeeding taxable year shall not exceed the amount by which the limitation provided by subsection (a) (2) for such taxable year exceeds the sum of—

"(A) the credit allowable under subsection (a) (1) for such taxable year, and

"(B) the amounts which, by reason of this subsection, are added to the amount allowable for such taxable year and attributable to taxable years preceding the unused credit year."

And, in lieu thereof, to insert:

"(b) CARRYBACK AND CARRYOVER OF UNUSED CREDITS.—

"(1) ALLOWANCE OF CREDIT.—If the amount of the credit determined under subsection (a) (1) for any taxable year exceeds the limitation provided by subsection (a) (2) for such taxable year (hereinafter in this subsection referred to as 'unused credit year'), such excess shall be—

"(A) an investment credit carryback to each of the 3 taxable years preceding the unused credit year, and

"(B) an investment credit carryover to each of the 5 taxable years following the unused credit year,

and shall be added to the amount allowable as a credit by section 38 for such years, except that such excess may be a carryback only to taxable years ending after June 30, 1962. The entire amount of the unused credit for an unused credit year shall be carried to the earliest of the 8 taxable years to which (by reason of subparagraphs (A) and (B)) such credit may be carried, and then to each of the other 7 taxable years to the extent that, because of the limitation contained in paragraph (2), such unused credit may not be added for a prior taxable year to which such unused credit may be carried.

"(2) LIMITATION.—The amount of the unused credit which may be added under paragraph (1) for any preceding or succeeding taxable year shall not exceed the amount by which the limitation provided by subsection (a) (2) for such taxable year exceeds the sum of—

"(A) the credit allowable under subsection (a) (1) for such taxable year, and

"(B) the amounts which, by reason of this subsection, are added to the amount allowable for such taxable year and attributable to taxable years preceding the unused credit year.

"(3) EFFECT OF NET OPERATING LOSS CARRYBACK.—To the extent that the excess described in paragraph (1) arises by reason of a net operating loss carryback, subparagraph (A) of paragraph (1) shall not apply.

"(4) TAXABLE YEARS BEGINNING BEFORE JULY 1, 1962.—For purposes of determining the amount of an investment credit carryback that may be added under paragraph (1) for taxable years beginning before July 1, 1962, and ending after June 30, 1962, the amount of the limitation provided by subsection (a) (2) is the amount which bears the same ratio to such limitation as the number of days in such year after June 30, 1962, bears to the total number of days in such year."

On page 16, after line 15, to insert:

"(4) CERTAIN REPLACEMENT PROPERTY.—For purposes of paragraph (1), if section 38 property is placed in service by the taxpayer to replace property which was—

"(A) destroyed or damaged by fire, storm, shipwreck, or other casualty, or

"(B) stolen,

the basis of such section 38 property (in the case of new section 38 property), or the cost of such section 38 property (in the case of used section 38 property), which (but for this paragraph) would be taken into account under paragraph (1) shall be reduced by an amount equal to the amount received by the taxpayer as compensation, by insurance or otherwise, for the property so destroyed, damaged, or stolen, or to the adjusted basis of such property, whichever is the lesser. No reduction in basis or cost shall be made under the preceding sentence in any case in which the reduction in qualified investment attributable to the substitution required by section 47(a)(1) with respect to the property so destroyed, damaged, or stolen (determined without regard to section 47(a)(4)) is greater than the reduction described in the preceding sentence."

On page 20, line 13, after "(3)" to strike out "Carryovers" and insert "Carrybacks and Carryovers", and in line 16, after the word "the" to insert "carrybacks and".

On page 20, after line 18, to insert:

"(4) PROPERTY DESTROYED BY CASUALTY, ETC.—No increase shall be made under paragraph (1) and no adjustment shall be made under paragraph (3) in any case in which—

"(A) any property is disposed of, or otherwise ceases to be section 38 property with respect to the taxpayer, on account of its destruction or damage by fire, storm, shipwreck, or other casualty, or by reason of its theft,

"(B) section 38 property is placed in service by the taxpayer to replace the property described in subparagraph (A), and

"(C) the reduction in basis or cost of such section 38 property described in the first sentence of section 46(c)(4) is greater than the reduction in qualified investment which (but for this paragraph) would be made by reason of the substitution required by paragraph (1) with respect to the property described in subparagraph (A)."

On page 25, after line 9, to insert:

"(6) LIVESTOCK.—Livestock shall not be treated as section 38 property."

On page 25, line 16, after the word "after", to strike out "December 31, 1961" and insert "June 30, 1962"; in line 18, after the word "after", to strike out "December 31, 1961"

and insert "June 30, 1962"; in line 24, after the word "after", to strike out "December 31, 1961" and insert "June 30, 1962"; on page 26, line 4, after the word "after", to strike out "December 31, 1961" and insert "June 30, 1962"; on page 28, line 4, after the word "of", to insert "(other than by reason of its destruction or damage by fire, storm, shipwreck, or other casualty, or its theft)"; in line 16, after the word "credit" to insert "carrybacks or"; on page 29, line 4, after "section 46 (d))", to strike out "engaged in the business of leasing property" and insert "who is a lessor of property"; in line 25, after the word "property", to insert "If a lessor makes the election provided by this subsection with respect to any property, then, under regulations prescribed by the Secretary or his delegate, subsection (g) shall not apply with respect to such property and the deductions otherwise allowable under section 162 to the lessee for amounts paid to the lessor under the lease shall be adjusted in a manner consistent with the provisions of subsection (g)."; on page 31, after line 16, to insert:

"(g) ADJUSTMENTS TO BASIS OF PROPERTY.—

"(1) IN GENERAL.—The basis of any section 38 property shall be reduced, for purposes of this subtitle other than this subpart, by an amount equal to 7 percent of the qualified investment as determined under section 46(c) with respect to such property.

"(2) CERTAIN DISPOSITIONS, ETC.—If the tax under this chapter is increased for any taxable year under paragraph (1) or (2) of section 47(a) or an adjustment in carrybacks or carryovers is made under paragraph (3) of such section, the basis of the property described in such paragraph (1) or (2), as the case may be (immediately before the event on account of which such paragraph (1), (2), or (3) applies), shall be increased by an amount equal to the portion of such increase and the portion of such adjustment attributable to such property."

On page 32, at the beginning of line 9, to strike out "(g)" and insert "(h) CROSS REFERENCE.—"; at the beginning of line 10, to insert:

"(c) DEDUCTION FOR UNUSED CREDIT.—Part VI of subchapter B of chapter 1 (relating to itemized deductions for individuals and corporations) is amended by adding at the end thereof the following new section:

"SEC. 181. DEDUCTION FOR CERTAIN UNUSED INVESTMENT CREDIT

"'If the amount of the credit determined under section 46(a)(1) for any taxable year exceeds the limitation provided by section 46(a)(2) for such taxable year and if the amount of such excess has not, after the application of section 46(b), been allowed to the taxpayer as a credit under section 38 for any taxable year, then an amount equal to the amount of such excess not so allowed as a credit shall be allowed to the taxpayer as a deduction for the first taxable year following the last taxable year in which such excess could under section 46(b) have been allowed as a credit. If a taxpayer dies or ceases to exist prior to the first taxable year following the last taxable year in which the excess described in the preceding sentence could under section 46(b) have been allowed as a credit, the amount described in the preceding sentence, or the proper portion thereof, shall, under regulations prescribe by the Secretary or his delegate, be allowed to the taxpayer as a deduction for the taxable year in which such death or cessation occurs.'"

On page 33, at the beginning of line 10, to strike out "(c)" and insert "(d)"; after line 22, to insert:

"(e) STATUTES OF LIMITATIONS AND INTEREST RELATING TO INVESTMENT CREDIT CARRYBACKS.—

"(1) ASSESSMENT AND COLLECTION.—Section 6501 (relating to limitations on assessment and collection) is amended by redesigning—

nating subsection (j) as subsection (k), and inserting after subsection (i) the following new subsection:

"(j) INVESTMENT CREDIT CARRYBACKS.—In the case of a deficiency attributable to the application to the taxpayer of an investment credit carryback, such deficiency may be assessed at any time before the expiration of the period within which a deficiency for the taxable year of the unused investment credit which results in such carryback may be assessed."

"(2) CREDIT OR REFUND.—Subsection (d) of section 6511 (relating to limitations on credit or refund) is amended by adding after paragraph (3) thereof the following new paragraph:

"(4) SPECIAL PERIOD OF LIMITATION WITH RESPECT TO INVESTMENT CREDIT CARRYBACKS.—

"(A) PERIOD OF LIMITATION.—If the claim for credit or refund relates to an overpayment attributable to an investment credit carryback, in lieu of the 3-year period of limitation prescribed in subsection (a), the period shall be that period which ends with the expiration of the 15th day of the 40th month (or 39th month, in the case of a corporation) following the end of the taxable year of the unused investment credit which results in such carryback, or the period prescribed in subsection (c) in respect of such taxable year, whichever expires later. In the case of such a claim, the amount of the credit or refund may exceed the portion of the tax paid within the period provided in subsection (b) (2) or (c), whichever is applicable, to the extent of the amount of the overpayment attributable to such carryback."

"(B) APPLICABLE RULES.—If the allowance of a credit or refund of an overpayment of tax attributable to an investment credit carryback is otherwise prevented by the operation of any law or rule of law other than section 7122, relating to compromises, such credit or refund may be allowed or made, if claim therefor is filed within the period provided in subparagraph (A) of this paragraph. In the case of any such claim for credit or refund, the determination by any court, including the Tax Court, in any proceeding in which the decision of the court has become final, shall not be conclusive with respect to the investment credit, and the effect of such credit, to the extent that such credit is affected by a carryback which was not in issue in such proceeding."

"(3) INTEREST ON UNDERPAYMENTS.—Section 6601(e) (relating to interest on underpayment, nonpayment, or extensions of time for payment, of tax) is amended to read as follows:

"(e) INCOME TAX REDUCED BY CARRYBACK.—

"(1) NET OPERATING LOSS CARRYBACK.—If the amount of any tax imposed by subtitle A is reduced by reason of a carryback of a net operating loss, such reduction in tax shall not affect the computation of interest under this section for the period ending with the last day of the taxable year in which the net operating loss arises."

"(2) INVESTMENT CREDIT CARRYBACK.—If the credit allowed by section 38 for any taxable year is increased by reason of an investment credit carryback, such increase shall not affect the computation of interest under this section for the period ending with the last day of the taxable year in which the investment credit carryback arises."

"(4) INTEREST ON OVERPAYMENTS.—Section 6611(f) (relating to interest on overpayments) is amended to read as follows:

"(f) REFUND OF INCOME TAX CAUSED BY CARRYBACK.—

"(1) NET OPERATING LOSS CARRYBACK.—For purposes of subsection (a), if any overpayment of tax imposed by subtitle A results from a carryback of a net operating loss, such overpayment shall be deemed not to have been made prior to the close of the

taxable year in which such net operating loss arises."

"(2) INVESTMENT CREDIT CARRYBACK.—For purposes of subsection (a), if any overpayment of tax imposed by subtitle A results from an investment credit carryback, such overpayment shall be deemed not to have been made prior to the close of the taxable year in which such investment credit carryback arises."

"(f) TECHNICAL AMENDMENT.—Section 1016(a) (relating to adjustments to basis) is amended—

"(1) by striking out the period at the end of paragraph (18) and inserting in lieu thereof a semicolon; and

"(2) by adding after paragraph (18) the following new paragraph:

"(19) to the extent provided in section 48(g) in the case of property which is or has been section 38 property (as defined in section 48(a));"

On page 37, after line 23, to strike out:

"(d) CLERICAL AMENDMENT.—Part IV of subchapter A of chapter 1 is amended by inserting after the heading and before the table of sections the following:"

On page 38, after line 2, to insert:

"(g) CLERICAL AMENDMENTS.—

"(1) Part IV of subchapter A of chapter 1 is amended by inserting after the heading and before the table of sections the following:"

After line 7, to insert:

"(2) The table of sections for part IV of subchapter A of chapter 1 is amended by striking out

"Sec. 38. Overpayments of tax."

and inserting in lieu thereof

"Sec. 38. Investment in certain depreciable property."

"Sec. 39. Overpayments of tax."

"(3) The table of sections for part VI of subchapter B of chapter 1 is amended by adding at the end thereof the following:

"Sec. 181. Deduction for certain unused investment credit."

At the beginning of line 14, to strike out "(e)" and insert "(h)"; in line 16, after the word "after", to strike out "December 31, 1961" and insert "June 30, 1962".

In section 3, on page 39, line 18, after the word "taxpayer", to strike out "or"; in line 23, after the word "organization", to insert a comma and "or"; after line 23, to insert:

"(C) in direct connection with communication of information between the taxpayer and an employee or stockholder with respect to legislation or proposed legislation of direct interest to the taxpayer."

On page 43, line 1, after the word "this", to strike out "chapter." and insert "chapter, but such term does not include—

"(A) an item having a cost to the taxpayer not in excess of \$4.00 on which the name of the taxpayer is clearly and permanently imprinted and which is one of a number of identical items distributed generally by the taxpayer,

"(B) a sign, display rack, or other promotional material to be used on the business premises of the recipient, or

"(C) an item of tangible personal property having a cost to the taxpayer not in excess of \$100 which is awarded to an employee by reason of length of service or for safety achievement."

After line 21, to insert:

"(c) TRAVELING.—In the case of any individual who is traveling away from home in pursuit of a trade or business or in pursuit of an activity described in section 212, no deduction shall be allowed under section 162 or section 212 for that portion of the expenses of such travel otherwise allowable under such section which, under regulations prescribed by the Secretary or his delegate,

is not allocable to such trade or business or to such activity. This subsection shall not apply to the expenses of any travel away from home which does not exceed one week or where the portion of the time away from home which is not attributable to the pursuit of the taxpayer's trade or business or an activity described in section 212 is less than 25 percent of the total time away from home on such travel."

On page 44, at the beginning of line 11, to strike out "(c)" and insert "(d)"; on page 45, at the beginning of line 8, to strike out "(d)" and insert "(e)"; on page 46, line 20, after the word "section", to strike out "(c)" and insert "(d)"; on page 47, after line 7, to strike out:

"(6) EMPLOYEE AND STOCKHOLDER BUSINESS MEETINGS.—Expenses directly related to business meetings of employees or stockholders."

And, in lieu thereof, to insert:

"(6) EMPLOYEE, STOCKHOLDER, ETC., BUSINESS MEETINGS.—Expenses incurred by a taxpayer which are directly related to business meetings of his employees, stockholders, agents, or directors."

On page 48, at the beginning of line 7, to strike out "(e)" and insert "(f)"; at the beginning of line 13, to strike out "(f)" and insert "(g)"; at the beginning of line 19, to strike out "(g)" and insert "(h)"; on page 49, line 6, after the word "including", to strike out "a reasonable allowance for amounts expended for meals and lodging" and insert "amounts expended for meals and lodging other than amounts which are lavish or extravagant under the circumstances"; at the beginning of line 12, to strike out "June 30, 1962" and insert "December 31, 1962".

In section 5, on page 51, after line 15, to strike out:

"(d) CREDIT FOR FOREIGN TAXES.—Section 902(a) (relating to credit for foreign taxes) is amended by adding at the end thereof the following new sentence: 'For purposes of this subsection and subsection (b), the amount of any distribution in property other than money shall be the amount determined by applying section 301(b) (1) (B).'"

At the beginning of line 22, to strike out "(e)" and insert "(d)".

At the top of page 58, to strike out:

"Sec. 7. Distributions of foreign personal holding company income."

"(a) DEFINITION OF FOREIGN PERSONAL HOLDING COMPANY.—So much of subsection (a) of section 552 (relating to definition of foreign personal holding company) as precedes paragraph (2) is amended to read as follows:

"(a) GENERAL RULE.—For purposes of this subtitle, the term "foreign personal holding company" for a taxable year beginning after December 31, 1962, means any foreign corporation if—

"(1) GROSS INCOME REQUIREMENT.—At least 20 percent of its gross income (as defined in section 555(a)) for the taxable year is foreign personal holding company income (as defined in section 553). For purposes of this paragraph, there shall be included in the gross income the amount includible therein as a dividend by reason of the application of section 555(c) (2); and"

"(b) AMOUNT OF UNDISTRIBUTED INCOME.—Subsection (a) of section 556 (relating to undistributed foreign personal holding company income) is amended to read as follows:

"(a) DEFINITION.—For purposes of this part—

"(1) If the foreign personal holding company income of a foreign personal holding company exceeds 80 percent of its gross income, "undistributed foreign personal holding company income" of such company is its taxable income adjusted in the manner provided in subsection (b), minus the dividends paid deduction (as defined in section 561).

"(2) If the foreign personal holding company income of a foreign personal holding company does not exceed 80 percent of its gross income, the "undistributed foreign personal holding company income" of such company is that amount which bears the same ratio to—

"(A) its taxable income adjusted in the manner provided in subsection (b), minus the dividends paid deduction (as defined in section 561), as

"(B) its foreign personal holding company income bears to its gross income."

"(c) EFFECTIVE DATE.—The amendments made by this section shall apply only in respect of taxable years of foreign corporations beginning after December 31, 1962."

On page 59, at the beginning of line 19, to change the section number from "8" to "6"; on page 60, line 17, after the word "largest", to insert a comma and "but the amount determined under this subparagraph, when added to the amount determined under subparagraph (A), shall in no case be greater than the amount by which 12 percent of the total deposits or withdrawable accounts of depositors of the taxpayer at the close of such year exceeds the sum of its surplus, undivided profits, and reserves at the beginning of such year (taking into account any portion thereof attributable to the period before the first taxable year beginning after December 31, 1951)"; on page 61, line 3, after "(2)", to strike out "60 Percent and insert "Percentage"; after line 5, to strike out:

"(A) an amount equal to 60 percent of the taxable income for such year, over"

And, in lieu thereof, to insert:

"(A) an amount—

"(i) in the case of a taxpayer other than a taxpayer described in clause (ii), equal to 60 percent of the taxable income for such year, or

"(ii) in the case of a domestic building and loan association having capital stock with respect to which any distribution of property (as defined in section 317(a)) is not allowable as a deduction under section 591, equal to 50 percent of the taxable income for such year, over

In line 20, after the word "such", to strike out "year." and insert "year, but the amount determined under this paragraph shall not exceed the amount necessary to increase the balance (as of the close of the taxable year) of the reserve for losses on qualifying real property loans to 6 percent of such loans outstanding at such time."; on page 62, line 6, after "(3)" to strike out "3 percent" and insert "percentage"; in line 11, after the word "loans", to strike out "to 3 percent of such loans outstanding at such time." and insert "to an amount equal to—

"(A) 3 percent of such loans outstanding at such time, plus

"(B) in the case of a taxpayer which is a new company and which does not have capital stock with respect to which distributions of property (as defined in sections 317 (a)) are not allowable as a deduction under section 591, an amount equal to—

"(i) 2 percent of so much of the amount of such loans outstanding at such time as does not exceed \$4,000,000, reduced (but not below zero) by

"(ii) the amount, if any, of the balance (as of the close of such taxable year) of the taxpayer's supplemental reserve for losses on loans.

For purposes of subparagraph (B), a taxpayer is a new company for any taxable year only if such taxable year begins not more than 10 years after the first day on which it (or any predecessor) was authorized to do business as an organization described in subsection (a)."

On page 64, line 21, after the word "paragraph", to strike out "(3)" and insert "(3) (A)".

On page 65, after line 10, to insert:

"(5) CERTAIN PRE-1952 SURPLUS.—If after the application of paragraph (3), the opening balance of the reserve described in paragraph (2) (B) is less than the amount described in paragraph (3) (B), then, for purposes of this subsection, the term 'pre-1963 reserves' includes so much of the surplus, undivided profits, and bad debt reserves (determined as of December 31, 1962) attributable to the period before the first taxable year beginning after December 31, 1951, as does not exceed the amount by which such opening balance is less than the amount described in paragraph (3) (B). For purposes of the preceding sentence, the surplus, undivided profits, and bad debt reserves attributable to the period before the first taxable year beginning after December 31, 1951, shall be reduced by the amount thereof which is attributable to interest which would have been excludable from gross income under section 22(b) (4) of the Internal Revenue Code of 1939 (relating to interest on governmental obligations) or the corresponding provisions of prior laws. Notwithstanding the second sentence of paragraph (1), any amount which, by reason of the application of the first sentence of this paragraph, is allocated to the reserve described in paragraph (2) (B) shall not be treated as a reserve for bad debts for any purpose other than determining the amount referred to in subsection (b) (1) (B), and for such purpose such amount shall be treated as remaining in such reserve."

On page 66, at the beginning of line 14, to strike out "(5)" and insert "(6)"; on page 67, line 10, after the word "section", to strike out "8" and insert "6"; in line 17, after the word "section", to strike out "8" and insert "6"; on page 73, after line 4, to strike out:

"(19) DOMESTIC BUILDING AND LOAN ASSOCIATION.—The term 'domestic building and loan association' means a domestic building and loan association, a domestic savings and loan association, and a Federal savings and loan association, which—

"(A) is an insured institution (within the meaning of section 401(a) of the National Housing Act (12 U.S.C., sec. 1724 (a)), or

"(B) is subject by law to supervision and examination by State or Federal authority having supervision over such associations,

if substantially all of its business consists of accepting savings and investing the proceeds (i) in loans secured by an interest in real property which is (or, from the proceeds of the loan, will become) residential real property, and (ii) in other loans, to the extent such other loans would be authorized to be made by a Federal savings and loan association under section 5(c) of the Home Owners' Loan Act, as amended (12 U.S.C., sec. 1464(c))."

And, in lieu thereof, to insert:

"(19) DOMESTIC BUILDING AND LOAN ASSOCIATION.—The term 'domestic building and loan association' means a domestic building and loan association, a domestic savings and loan association, and a Federal savings and loan association—

"(A) which either (i) is an insured institution (within the meaning of section 401(a) of the National Housing Act (12 U.S.C., sec. 1724(a)), or (ii) is subject by law to supervision and examination by State or Federal authority having supervision over such associations;

"(B) substantially all of the business of which consists of acquiring the savings of the public and investing in loans described in subparagraph (C);

"(C) at least 90 percent of the amount of the total assets of which (as of the close of the taxable year) consists of (i) cash, (ii) obligations of the United States or of a State or political subdivision thereof, and stock or obligations of a corporation which is an instrumentality of the United States

or of a State or political subdivision thereof, (iii) loans secured by an interest in real property and loans made for the improvement of real property, (iv) loans secured by a deposit or share of a member, and (v) property acquired through the liquidation of defaulted loans described in clause (iii);

"(D) of the assets of which taken into account under subparagraph (C) as assets constituting the 90 percent of total assets—

"(i) at least 80 percent of the amount of such assets consists of assets described in clauses (i) and (ii) of such subparagraph and of loans secured by an interest in real property which is (or, from the proceeds of the loan, will become) residential real property or loans made for the improvement of residential real property; and

"(ii) at least 70 percent of the amount of such assets consists of assets described in clauses (i) and (ii) of such subparagraph and of loans secured by an interest in real property which is (or, from the proceeds of the loan, will become) residential real property containing 4 or fewer family units, or loans made for the improvement of residential real property containing 4 or fewer family units;

"(E) not more than 18 percent of the amount of the total assets of which (as of the close of the taxable year) consists of assets other than those described in clause (i) of subparagraph (D), and not more than 27 percent of the amount of the total assets of which (as of the close of the taxable year) consists of assets other than those described in clause (ii) of subparagraph (D), except that the 18 percent and 27 percent limitations contained in this subparagraph shall be increased by the number, if any, of percentage points (including any fraction of a percentage point) by which 10 percent exceeds the percentage of the total assets consisting of assets described in clauses (i) and (ii) of subparagraph (C); and

"(F) except for property described in subparagraph (C), none of the assets of which consists of stock of any corporation."

On page 76, after line 18, to strike out:

"(c) REPEAL OF EXEMPTION FROM COMMUNICATIONS AND TRANSPORTATION OF PERSONS TAXES.—Notwithstanding any other provision of law, Federal savings and loan associations shall not be exempt as such from the taxes imposed by section 4251 (relating to excise tax on communications) and section 4261 (relating to excise tax on transportation of persons) of the Internal Revenue Code of 1954."

And, in lieu thereof, to insert:

"(e) REPEAL OF EXEMPTION FROM CERTAIN EXCISE TAXES.—

"(1) AMENDMENT TO HOME OWNERS' LOAN ACT.—Section 5(h) of the Home Owners' Loan Act, as amended (12 U.S.C. sec. 1464 (h)), is amended to read as follows:

"(h) EXEMPTION FROM DISCRIMINATORY STATE AND LOCAL TAXATION.—No State, county, municipal, or local taxing authority shall impose any tax on such associations or their franchise, capital, reserves, surplus, loans, or income greater than that imposed by such authority on other similar local mutual or cooperative thrift and home financing institutions."

"(2) CERTAIN DOCUMENTARY STAMP TAXES.—Section 4382(a) (2) (relating to exemptions from documentary stamp taxes) is amended to read as follows:

"(2) DOMESTIC BUILDING AND LOAN ASSOCIATION AND MUTUAL DITCH OR IRRIGATION COMPANIES.—Shares or certificates of stock issued by domestic building and loan associations and cooperative banks, to the extent such shares or certificates represent deposits or withdrawable accounts; or shares or certificates of stock and certificates of indebtedness issued by mutual ditch or irrigation companies."

"(f) DEDUCTION FOR DIVIDENDS OR INTEREST PAID ON DEPOSITS.—Section 591 (relating to deduction for dividends paid on deposits) is amended—

"(1) by striking out 'and domestic building and loan associations' and inserting in lieu thereof the following: 'domestic building and loan associations, and other savings institutions chartered and supervised as savings and loan or similar associations under Federal or State law'; and

"(2) by inserting after 'dividends' the following: 'or interest'.

On page 78, at the beginning of line 16, to strike out "(f)" and insert "(g)"; on page 79, after line 3, to insert:

"(3) The amendment made by subsection (c) shall apply to taxable years beginning after the date of the enactment of this Act."

After line 6, to strike out:

"(3) Subsection (c) of this section shall apply—

"(A) in the case of the tax imposed by section 4251 of the Internal Revenue Code of 1954, with respect to amounts paid pursuant to bills rendered after June 30, 1962; and

"(B) in the case of the tax imposed by section 4261 of such Code, with respect to transportation beginning after June 30, 1962."

And, in lieu thereof, to insert:

"(4) Subsection (e) of this section shall become effective on January 1, 1963, except that—

"(A) in the case of the tax imposed by section 4251 of the Internal Revenue Code of 1954, such subsection shall apply only with respect to amounts paid pursuant to bills rendered after December 31, 1962; and

"(B) in the case of the tax imposed by section 4261 of such Code, such subsection shall apply only with respect to transportation beginning after December 31, 1962."

On page 80, at the beginning of line 4, to change the section number from "9" to "7"; in line 22, after "(C)", to strike out "Subsection (a) (3) of this section" and insert "Paragraph (3)"; on page 81, line 7, after the word "Foreign", to strike out "estates and"; on page 81, line 12, after the word "means", to strike out "a foreign trust (as defined in section 7701 (a) (31)) to which money or property has been transferred" and insert "that portion of a foreign trust (as defined in section 7701 (a) (31)) attributable to money or property transferred"; on page 90, line 17, after the word "made", to strike out "in taxable years of trusts beginning".

On page 91, at the beginning of line 1, to change the section number from "10" to "8"; in the heading at the beginning of line 3, to insert "Or Flood"; on page 91, in the heading, in line 12, after the word "Fire", to insert "Or Flood"; on page 92, line 7, after the word "a", to strike out "fire" and insert "fire, flood"; after line 9, to strike out:

"(1) NORMAL TAX.—A normal tax of 25 percent of the mutual insurance company taxable income, or 50 percent of the amount by which such taxable income exceeds \$6,000, whichever is the lesser; plus"

And, in lieu thereof, to insert:

"(1) NORMAL TAX.—

"(A) TAXABLE YEARS BEGINNING BEFORE JULY 1, 1963.—In the case of taxable years beginning before July 1, 1963, a normal tax of 30 percent of the mutual insurance company taxable income, or 60 percent of the amount by which such taxable income exceeds \$6,000, whichever is the lesser;

"(B) TAXABLE YEARS BEGINNING AFTER JUNE 30, 1963.—In the case of taxable years beginning after June 30, 1963, a normal tax of 25 percent of the mutual insurance company taxable income, or 50 percent of the amount by which such taxable income exceeds \$6,000, whichever is the lesser; plus"

On page 94, after line 8, to strike out:

"(A) NORMAL TAX.—A normal tax of 25 percent of the taxable investment income, or 50 percent of the amount by which such taxable income exceeds \$3,000, whichever is the lesser; plus"

And, in lieu thereof, to insert:

"(A) NORMAL TAX.—

"(i) TAXABLE YEARS BEGINNING BEFORE JULY 1, 1963.—In the case of taxable years beginning before July 1, 1963, a normal tax of 30 percent of the taxable investment income, or 60 percent of the amount by which such taxable income exceeds \$3,000, whichever is the lesser;

"(ii) TAXABLE YEARS BEGINNING AFTER JUNE 30, 1963.—In the case of taxable years beginning after June 30, 1963, a normal tax of 25 percent of the taxable investment income, or 50 percent of the amount by which such taxable income exceeds \$3,000, whichever is the lesser; plus"

On page 95, line 7, after the word "over", to strike out "\$75,000" and insert "\$150,000"; in line 8, after the word "than", to strike out "\$125,000" and insert "\$250,000"; in line 12, after the word "over", to strike out "\$75,000" and insert "\$150,000"; at the beginning of line 13, to strike out "\$125,000" and insert "\$250,000"; in line 16, after the word "over", to strike out "\$75,000" and insert "\$150,000"; in line 17, after the word "to", to strike out "\$50,000" and insert "\$100,000"; in line 23, after the word "a", to strike out "fire" and insert "fire, flood"; on page 96, in line 5, after the word "of", to strike out "\$75,000" and insert "\$150,000"; in line 6, after the word "of", to strike out "\$300,000" and insert "\$600,000"; on page 97, line 7, after the word "a", to strike out "fire" and insert "fire, flood"; after line 11, to insert:

"(f) SPECIAL TRANSITIONAL UNDERWRITING LOSS.—

"(1) COMPANIES TO WHICH SUBSECTION APPLIES.—This subsection shall apply to every mutual insurance company which has been subject to the tax imposed by this section (as in effect before the enactment of this subsection) for the 6 taxable years immediately preceding January 1, 1963, and has incurred an underwriting loss for at least 5 of such 6 taxable years.

"(2) REDUCTION OF MUTUAL INSURANCE COMPANY TAXABLE INCOME.—For purposes of this part, the mutual insurance company taxable income for the taxable year with respect to a company described in paragraph (1) shall be the mutual insurance company taxable income for the taxable year (determined without regard to this subsection) reduced by the amount by which—

"(A) the sum of the underwriting losses of such company for the 6 taxable years prior to January 1, 1963, reduced by the underwriting gain for such years, exceeds

"(B) the total amount by which the mutual insurance company taxable income was reduced by reason of this subsection for prior taxable years.

"(3) For purposes of this subsection—

"(A) The term 'underwriting loss' means statutory underwriting loss, computed without any deduction under section 824(a).

"(B) The term 'underwriting gain' means statutory underwriting income, computed without any deduction under section 823(c) or any deduction under section 824(a).

"(4) YEARS TO WHICH SUBSECTION APPLIES.—This subsection shall apply with respect to any taxable year beginning after December 31, 1962, and before January 1, 1968, for which the taxpayer is subject to the tax imposed by subsection (a)."

On page 99, at the beginning of line 1, to strike out "(f)" and insert "(g)".

On page 102, in the heading, in line 16, after the word "Than", to strike out "\$900,000" and insert "\$1,200,000"; in line 23, after the word "exceed", to strike out "\$900,000" and insert "\$1,200,000"; on page 103, line 2,

after the word "exceeds", to strike out "\$300,000" and insert "\$600,000"; in line 4, after the word "which", to strike out "\$900,000" and insert "\$1,200,000"; in line 22, after the word "exceeds", to strike out "50" and insert "40"; in line 24, after the word "exceeds", to strike out "50" and insert "40"; on page 104, line 12, after the word "losses", to strike out "arising in any one State" and insert "arising, either in any one State or within 200 miles of any fixed point selected by the taxpayer"; on page 105, after line 6, to strike out:

"(A) first, an amount equal to the excess of the statutory underwriting loss for the taxable year over the underwriting loss (as defined in paragraph (6)) for the taxable year."

And, in lieu thereof, to insert:

"(A) first, an amount equal to the excess (if any) of the deduction allowed under subsection (a) for the taxable year over the underwriting gain (within the meaning of subsection (a) (1)) for the taxable year."

In line 18, after the word "the", to strike out "underwriting loss" and insert "statutory underwriting loss (reduced by the amount referred to in subparagraph (A))"; on page 108, after line 21, to strike out:

"(6) UNDERWRITING LOSS DEFINED.—For purposes of paragraph (1), the term 'underwriting loss' means the amount by which—

"(A) the deductions which would be taken into account in computing taxable income under section 832 if the taxpayer were subject to the tax imposed by section 831, reduced by the sum of (i) the deductions provided in section 822(c), and (ii) the deduction for dividends to policyholders provided by section 832(c) (11), exceeds

"(B) the amount referred to in section 823(a) (1) (A)."

On page 113, after line 8, to strike out:

"(d) SPECIAL RULE.—For purposes of computing the deduction provided in section 824(a) and the additions to the account provided by section 824(c) with respect to any reciprocal electing to be subject to the limitation provided in subsection (b), such limitation shall not be taken into account."

And, in lieu thereof, to insert:

"(d) SPECIAL RULE.—In applying section 824(d) (1) (D), any amount which was added to the protection against loss account by reason of an election under this section shall be treated as having been added by reason of section 824(a) (1) (A)."

On page 114, line 10, after the word "which", to strike out "a reciprocal was allowed a credit" and insert "credit or refund to the reciprocal resulted"; after line 18, to insert:

"(d) EXEMPTION FROM TAX.—Section 501 (c) (15) (relating to exemption from tax of certain mutual insurance companies) is amended by striking out '\$75,000' and in lieu thereof inserting '\$150,000'."

At the beginning of line 23, to strike out "(d)" and insert "(e)"; on page 115, line 11, after the word "fire", to insert "or flood"; on page 117, at the beginning of line 16, to strike out "(e)" and insert "(f)"; on page 118, at the beginning of line 15, to strike out "(f)" and insert "(g)"; on page 119, after line 18, to strike out:

"(4) CLERICAL AMENDMENT.—The table of parts for subchapter L is amended by striking out the portion referring to part II and inserting in lieu thereof the following:

"Part II. Mutual insurance companies (other than life and certain marine insurance companies and other than fire insurance companies which operate on basis of perpetual policies or premium deposits)."

And, in lieu thereof, to insert:

"(4) CLERICAL AMENDMENTS.—

"(A) The table of parts for subchapter L is amended by striking out the portion re-

ferring to part II and inserting in lieu thereof the following:

"Part II. Mutual insurance companies (other than life and certain marine insurance companies and other than fire or flood insurance companies which operate on basis of perpetual policies or premium deposits)."

"(B) The heading to section 831 is amended to read as follows:

"Sec. 831. Tax on insurance companies (other than life or mutual), mutual marine insurance companies, and certain mutual fire or flood insurance companies."

"(C) The table of sections for part III of subchapter L is amended by striking out the portion referring to section 831 and inserting in lieu thereof the following:

"Sec. 831. Tax on insurance companies (other than life or mutual), mutual marine insurance companies, and certain mutual fire or flood insurance companies."

On page 120, at the beginning of line 15, to strike out "(g)" and insert "(h)"; in line 16, after the word "subsection", to strike out "(e)" and insert "(f)"; on page 121, at the beginning of line 1, to change the section number from "11" to "9".

On page 127, line 7, after the word "From" to insert the word "Certain"; in line 14, at the beginning of the line, to strike out "902" and insert "902(a)(1)"; in line 15, after the word "section", strike out "957(a)" and insert "960(a)(1)(C)"; on page 128, after line 12, to strike out:

"(d) REPEAL OF SECTION 902(d). Subsection (d) (relating to special rules for certain wholly owned foreign corporations) is hereby repealed."

At the beginning of line 16, to strike out "(e)" and insert "(d)";

In the line after line 19, after the word "from" to insert "certain";

On page 129, line 2, after the word "section", strike out "902" and insert "902(a)(1) or 960(a)(1)(C)";

After line 5, to strike out:

"(4) Section 902 is amended by striking out subsection (c) and inserting in lieu thereof the following:

"(d) CROSS REFERENCES.—

"(1) For inclusion in gross income of an amount equal to taxes deemed paid under this section, see section 78.

"(2) For reduction of credit with respect to dividends paid out of accumulated profits for years for which certain information is not furnished, see section 6038."

At the beginning of line 9, to change the subsection letter from "(f)" to "(e)".

On page 130, after line 12, to insert a new section, as follows:

"Sec. 10. Separate limitation on foreign tax credit with respect to certain interest income.

"(a) LIMITATION ON FOREIGN TAX CREDIT.—Section 904 (relating to limitations on foreign tax credit) is amended by redesignating subsection (f) as subsection (g) and by inserting after subsection (e) the following new subsection:

"(f) APPLICATION OF SECTION IN CASE OF CERTAIN INTEREST INCOME.—

"(1) IN GENERAL.—The provisions of subsections (a), (c), (d), and (e) of this section shall be applied separately with respect to—

"(A) the interest income described in paragraph (2), and

"(B) income other than the interest income described in paragraph (2).

"(2) INTEREST INCOME TO WHICH APPLICABLE.—For purposes of this subsection, the interest income described in this paragraph is interest other than interest—

"(A) derived from any transaction which is directly related to the active conduct of a trade or business in a foreign country or a possession of the United States,

"(B) derived in the conduct of a banking, financing, or similar business, or

"(C) received from a corporation in which the taxpayer owns at least 10 percent of the voting stock.

"(3) OVERALL LIMITATION NOT TO APPLY.—The limitation provided by subsection (a) (2) shall not apply with respect to the interest income described in paragraph (2). The Secretary or his delegate shall by regulations prescribe the manner of application of subsection (e) with respect to cases in which the limitation provided by subsection (a) (2) applies with respect to income other than the interest income described in paragraph (2).

"(4) TRANSITIONAL RULES FOR CARRYBACKS AND CARRYOVERS.—

"(A) CARRYBACKS TO YEARS PRIOR TO REVENUE ACT OF 1962.—Where, under the provisions of subsection (d), taxes (i) paid or accrued to any foreign country or possession of the United States in any taxable year beginning after the date of the enactment of the Revenue Act of 1962 are deemed (ii) paid or accrued in one or more taxable years beginning on or before the date of enactment of the Revenue Act of 1962, the amount of such taxes deemed paid or accrued shall be determined without regard to the provisions of this subsection. To the extent the taxes paid or accrued to a foreign country or possession of the United States in any taxable year described in clause (i) are not, with the application of the preceding sentence, deemed paid or accrued in any taxable year described in clause (ii), such taxes shall, for purposes of applying subsection (d), be deemed paid or accrued in a taxable year beginning after the date of the enactment of the Revenue Act of 1962, with respect to interest income described in paragraph (2), and with respect to income other than interest income described in paragraph (2), in the same ratios as the amount of such taxes paid or accrued with respect to interest income described in paragraph (2), and the amount of such taxes paid or accrued with respect to income other than interest income described in paragraph (2), respectively, bear to the total amount of such taxes paid or accrued to such foreign country or possession of the United States.

"(B) CARRYOVERS TO YEARS AFTER REVENUE ACT OF 1962.—Where, under the provisions of subsection (d), taxes (i) paid or accrued to any foreign country or possession of the United States in any taxable year beginning on or before the date of the enactment of the Revenue Act of 1962 are deemed (ii) paid or accrued in one or more taxable years beginning after the date of the enactment of the Revenue Act of 1962, the amount of such taxes deemed paid or accrued in any year described in clause (ii) shall, with respect to interest income described in paragraph (2), be an amount which bears the same ratio to the amount of such taxes deemed paid or accrued as the amount of the taxes paid or accrued to such foreign country or possession for such year with respect to interest income described in paragraph (2) bears to the total amount of the taxes paid or accrued to such foreign country or possession for such year; and the amount of such taxes deemed paid or accrued in any year described in clause (ii) with respect to income other than interest income described in paragraph (2) shall be an amount which bears the same ratio to the amount of such taxes deemed paid or accrued for such year as the amount of taxes paid or accrued to such foreign country or possession for such year with respect to income other than interest income de-

scribed in paragraph (2) bears to the total amount of the taxes paid or accrued to such foreign country or possession for such year."

"(b) EFFECTIVE DATE.—The amendments made by subsection (a) shall apply with respect to taxable years beginning after the date of the enactment of this Act, but only with respect to interest resulting from transactions consummated after April 2, 1962."

On page 134, at the beginning of line 16, to change the section number from "12" to "11"; on page 138, after line 18, to insert:

"(6) TEST OF BONA FIDE RESIDENCE.—A statement by an individual who has earned income from sources within a foreign country to the authorities of that country that he is not a resident of that country, if he is held not subject as a resident of that country to the income tax of that country by its authorities with respect to such earnings, shall be conclusive evidence with respect to such earnings that he is not a bona fide resident of that country for purposes of subsection (a) (1).

"(7) CERTAIN NONCASE REMUNERATION.—If an individual who qualifies under subsection (a) (1) receives compensation from sources without the United States (except from the United States or any agency thereof) in the form of the right to use property or facilities, the limitation under paragraph (1) applicable with respect to such individual—

"(A) for a taxable year ending in 1963, shall be increased by an amount equal to the amount of such compensation so received during such taxable year;

"(B) for a taxable year ending in 1964, shall be increased by an amount equal to two-thirds of such compensation so received during such taxable year; and

"(C) for a taxable year ending in 1965, shall be increased by an amount equal to one-third of such compensation so received during such taxable year."

On page 141, after line 3, to strike out:

"Sec. 13. Controlled foreign corporations.

"(a) IN GENERAL.—Part III of subchapter N of chapter 1 (relating to income from sources without the United States) is amended by adding at the end thereof the following new subpart:

"Subpart F—Controlled Foreign Corporations.

"Sec. 951. Amounts included in gross income of United States persons.

"Sec. 952. Subpart F income defined.

"Sec. 953. Investment of earnings in non-qualified property.

"Sec. 954. Controlled foreign corporations.

"Sec. 955. Rules for determining stock ownership.

"Sec. 956. Exclusion from gross income of previously taxed earnings and profits.

"Sec. 957. Special rules for foreign tax credit.

"Sec. 958. Adjustments to basis of stock in controlled foreign corporations and of other property.

"Sec. 951. Amounts included in gross income of United States persons.

"(a) AMOUNTS INCLUDED.—

"(1) IN GENERAL.—If a foreign corporation is a controlled corporation on any day of a taxable year beginning after December 31, 1962, every United States person (as defined in section 7701(a)(30)) who owns (within the meaning of section 955(a)) stock in such corporation on the last day, in such year, on which such corporation is a controlled foreign corporation shall include in his gross income, for his taxable year in which or with which such taxable year of the corporation ends—

"(A) his pro rata share (determined under paragraph (2)) of the corporation's subpart F income for such year, and

“(B) his pro rata share (determined under section 953(a)(2), of the corporation's increase in earnings invested in nonqualified property for such year (but only to the extent not excluded from gross income under section 956(a)(2)).

“(2) PRO RATA SHARE OF SUBPART F INCOME.—The pro rata share referred to in paragraph (1)(A) in the case of any United States persons is the amount—

“(A) which would have been distributed with respect to the stock which such person owns (within the meaning of section 955(a)) in such corporation if on the last day, in its taxable year, on which the corporation is a controlled foreign corporation it had distributed pro rata to its shareholders an amount (i) which bears the same ratio to its subpart F income for the taxable year, as (ii) the part of such year during which the corporation is a controlled foreign corporation bears to the entire year, reduced by

“(B) the amount of any distribution received by any other United States person during such year as a dividend with respect to such stock.

“(3) LIMITATION ON AMOUNT OF PRO RATA SHARE OF INVESTMENT IN NONQUALIFIED PROPERTY INCLUDED IN GROSS INCOME.—For purposes of paragraph (1)(B), the pro rata share of any United States person in the increase of the earnings of a controlled foreign corporation invested in nonqualified property shall not exceed an amount (A) which bears the same ratio to his pro rata share of such increase (as determined under section 953(a)(2)) for the taxable year, as (B) the part of such year during which the corporation is a controlled foreign corporation bears to the entire year.

“(b) LESS THAN 10 PERCENT OWNERSHIP.—No person shall be required to include any amount in gross income under subsection (a) unless he can be considered, by applying the rules of ownership of section 955 (b), as owning, directly or indirectly, on any day during the taxable year of the corporation on which it was a controlled foreign corporation, 10 percent or more of the total combined voting power of all classes of stock, or of the total value of shares of all classes of stock, of such corporation.

“(c) COORDINATION WITH ELECTION OF A FOREIGN INVESTMENT COMPANY TO DISTRIBUTE INCOME.—A United States person who, for his taxable year, is a qualified shareholder (within the meaning of section 1247(c)) of a foreign investment company with respect to which an election under section 1247 is in effect shall not be required to include in gross income, for such taxable year, subpart F income of such company.

“Sec. 952. Subpart F income defined.

“(a) IN GENERAL.—

“(1) ITEMS TAKEN INTO ACCOUNT.—For purposes of this subpart, the term “subpart F income” means, in the case of any controlled foreign corporation, the sum of—

“(A) income derived from insurance of United States risks (as determined under subsection (b)),

“(B) income from United States patents, copyrights, and exclusive formulas and processes (as determined under subsection (c)), and

“(C) the net foreign base company income (as determined under subsection (d)), except that this subparagraph shall apply only in the case of a controlled foreign corporation in which 5 or fewer United States persons own, by applying the rules of ownership of section 955(b), more than 50 percent of the total combined voting power of all classes of stock entitled to vote.

“(2) EXCLUSION OF UNITED STATES INCOME.—Subpart F income does not include any item includible in gross income under this chapter (other than this subpart) as income derived from sources within the United

States of a foreign corporation engaged in trade or business in the United States.

“(3) NOT TO EXCEED EARNINGS AND PROFITS.—The subpart F income of any controlled foreign corporation for any taxable year shall not exceed the earnings and profits of such corporation for such year.

“(b) INCOME FROM INSURANCE OF UNITED STATES RISKS.—

“(1) GENERAL RULE.—If a controlled foreign corporation receives premiums or other consideration in respect of any reinsurance or the issuing of any insurance or annuity contract—

“(A) in connection with property in, or residents of, the United States, or

“(B) in connection with property not in, or nonresidents of, the United States as the result of any arrangement whereby another corporation receives a substantially equal amount of premiums or other consideration in respect of any reinsurance or the issuing of any insurance or annuity contract in connection with property in, or residents of, the United States,

then for purposes of subsection (a)(1)(A), the term “income derived from the insurance of United States risks” means that income which (subject to the modifications provided by subparagraphs (A), (B), and (C) of paragraph (2)) would be taxed under subchapter L of this chapter if such corporation were a domestic corporation.

“(2) SPECIAL RULES.—For purposes of paragraph (1)—

“(A) In the application of part I of subchapter L, life insurance company taxable income is the gain from operations as defined in section 809(b).

“(B) A corporation which would, if it were a domestic corporation, be taxable under part II of subchapter L shall apply paragraph (1) as if it were taxable under part III of subchapter L.

“(C) The following provisions of subchapter L shall not apply:

“(i) Section 809(d)(4) (operations loss deduction).

“(ii) Section 809(d)(5) (certain nonparticipating contracts).

“(iii) Section 809(d)(6) (group life, accident, and health insurance).

“(iv) Section 809(d)(10) (small business deduction).

“(v) Section 817(b) (gain on property held on December 31, 1958, and certain substituted property acquired after 1958).

“(vi) Section 832(b)(5) (certain capital losses).

“(D) “Gross amounts” to the extent provided in section 809(c)(1) and (2), less “increase in certain reserves” as defined in section 809(d)(2), and “premiums earned” as defined in section 832(b)(4) shall be taken into account only to the extent they are in respect to any reinsurance or the issuing of any insurance or the issuing of any insurance or annuity contract described in paragraph (1).

“(E) All items of income (other than those taken into account under subparagraph (D)) and all items of expenses, losses, and deductions shall be properly allocated or apportioned under regulations prescribed by the Secretary or his delegate.

“(c) INCOME FROM UNITED STATES PATENTS, COPYRIGHTS, AND EXCLUSIVE FORMULAS AND PROCESSES.—

“(1) GENERAL RULE.—For purposes of subsection (a)(1)(B), the term “income from United States patents, copyrights, and exclusive formulas and processes” means the amount of gross rentals, royalties, or other income derived from the license, sublicense, sale, exchange, use, or other means of exploitation of patents, copyrights, and exclusive formulas and processes—

“(A) substantially developed, created, or produced in the United States, or

“(B) acquired from any United States person which, directly or indirectly, owns or controls, or is owned or controlled by, or is under common ownership or control with, the controlled foreign corporation,

less the cost and expense allowance defined in paragraph (2).

“(2) COST AND EXPENSE ALLOWANCE.—An allowance shall be made, in accordance with regulations prescribed by the Secretary or his delegate, for ordinary and necessary expenses incurred by the controlled foreign corporation in the receipt or production of the income described in paragraph (1), including taxes and any amortization or depreciation of the cost to such corporation of such property or rights described in paragraph (1), but not including any production, manufacturing, or similar expenses incurred in the use or other means of exploitation of such property or rights.

“(3) DETERMINATION OF INCOME FROM USE.—The income from use or other means of exploitation by the controlled foreign corporation of the property or right described in paragraph (1) shall be the amount which would be obtained as a gross rent, royalty, or other payment in an arm's length transaction with an unrelated person for similar use or exploitation, of the property or right.

“(d) NET FOREIGN BASE COMPANY INCOME.—For purposes of subsection (a)(1)(C), the term “net foreign base company income” means—

“(1) the foreign base company income for the taxable year, determined under subsection (c), reduced by

“(2) the increase in investment in qualified property in less developed countries for the taxable year, determined under subsection (f).

“(e) FOREIGN BASE COMPANY INCOME.—

“(1) IN GENERAL.—For purposes of subsection (d)(1), the term “foreign base company income” means the foreign personal holding company income (as defined in section 553) for the taxable year, modified and adjusted as provided in this subsection.

“(2) CERTAIN SALES INCOME INCLUDED.—The term “foreign base company income” includes foreign base company sales income if, for the taxable year, such income is equal to at least 20 percent of the gross income of the foreign corporation (not including for this purpose other foreign base company income under this subsection). For purposes of this paragraph, the term “foreign base company sales income” means income (whether in the form of profits, commissions, fees, or otherwise) derived in connection with the purchase of personal property from a related person and its sale to any person, or the purchase of personal property from any persons and its sale to a related person, where—

“(A) the property which is purchased is manufactured, produced, grown, or extracted outside the country under the laws of which the controlled foreign corporation is created or organized, and

“(B) the property is sold for use, consumption, or disposition outside such foreign country.

For purposes of the preceding sentence, a person is a related person with respect to the controlled foreign corporation if he, directly or indirectly, owns or controls, or is owned or controlled by, or is under common ownership or control with, the controlled foreign corporation.

“(3) RENTS INCLUDED WITHOUT REGARD TO 50-PERCENT LIMITATION.—All rents shall be included in foreign base company income without regard to whether or not such rents constitute more than 50 percent of gross income.

“(4) INSURANCE AND PATENT INCOME EXCLUDED.—The term “foreign base company income” does not include any income derived

from insurance of United States risks (as determined under subsection (b)) or income from United States patents, copyrights, and exclusive formulas and processes (as determined under subsection (c)).

"(5) INCOME OF CERTAIN BANKS AND BANK-CONTROLLED CORPORATIONS EXCLUDED.—The term "foreign base company income" does not include—

"(A) the income of any corporation described in section 552(b) (relating to exception for banks and exempt corporations), or

"(B) the income of any foreign corporation if 50 percent or more of the fair market value of its outstanding stock is owned directly or indirectly by a domestic corporation which is either organized under section 25(a) of the Federal Reserve Act (12 U.S.C., secs. 611–631), or has an agreement or understanding with the Board of Governors of the Federal Reserve System under section 25 of the Federal Reserve Act (12 U.S.C., secs. 601–604), if all of the stock (except qualifying shares) of the domestic corporation is owned by a national or State bank which is a member of the Federal Reserve System.

"(6) SPECIAL RULE WHERE FOREIGN BASE COMPANY INCOME IS LESS THAN 20 PERCENT OR MORE THAN 80 PERCENT OF GROSS INCOME.—For purposes of this subsection—

"(A) If the foreign base company income (determined without regard to paragraph (7)) is less than 20 percent of gross income, no part of the gross income of the taxable year shall be treated as foreign base company income.

"(B) If the foreign base company income (determined without regard to paragraph (7)) exceeds 80 percent of gross income, the entire gross income of the taxable year shall be taken into account in determining foreign base company income.

"(7) DEDUCTIONS TO BE TAKEN INTO ACCOUNT.—The foreign base company income for the taxable year shall be reduced so as to take into account deductions (including taxes) properly allocable to such income.

"(f) INVESTMENT IN QUALIFIED PROPERTY IN LESS DEVELOPED COUNTRIES.—

"(1) GENERAL RULE.—For purposes of subsection (d) (2), the increase in investment in qualified property in less developed countries for any taxable year is the amount by which—

"(A) the aggregate amount of property described in sections 953(b) (2) (C) and (D) and property (including money) which is located outside the United States and is ordinary and necessary for the active conduct of a qualified trade or business described in section 953(b) (3) (A) (ii) held at the close of the taxable year, exceeds

"(B) the aggregate amount of property described in subparagraph (A) held at the close of the preceding taxable year.

"(2) INVESTMENTS AFTER CLOSE OF YEAR.—Under regulations prescribed by the Secretary or his delegate, a controlled foreign corporation may elect to make the determinations under subparagraphs (A) and (B) of paragraph (1) as of the close of the 75th day after the close of each taxable year.

"(3) AMOUNT ATTRIBUTABLE TO PROPERTY.—The amount taken into account under paragraph (1) with respect to any property shall be its adjusted basis, reduced by any liability to which the property is subject.

"Sec. 953. Investment of earnings in nonqualified property.

"(a) GENERAL RULES.—For purposes of this subpart—

"(1) AMOUNT OF INVESTMENT.—The amount of earnings of a controlled foreign corporation invested in nonqualified property at the close of any taxable year is the aggregate amount of such property held at the close of the taxable year, to the extent such amount does not exceed the sum of (A) the earnings and profits for the taxable

year, and (B) the earnings and profits accumulated for prior taxable years beginning after December 31, 1962.

"(2) PRO RATA SHARE OF INCREASE FOR YEAR.—In the case of any United States person, the pro rata share of the increase for any taxable year in the earnings of a controlled foreign corporation invested in a nonqualified property is the amount determined by subtracting—

"(A) his pro rata share of the amount determined under paragraph (1) for the close of the preceding taxable year, reduced by amounts paid during the taxable year to which section 956(c) (1) applies, from

"(B) his pro rata share of the amount determined under paragraph (1) for the close of the taxable year.

"(3) AMOUNT ATTRIBUTABLE TO PROPERTY.—The amount taken into account under paragraph (1) or (2) with respect to any property shall be its adjusted basis, reduced by any liability to which the property is subject.

"(b) NONQUALIFIED PROPERTY DEFINED.—For purposes of this subpart—

"(1) GENERAL RULE.—The term "nonqualified property" means any money or other property (tangible or intangible) acquired after December 31, 1962, which is not qualified property.

"(2) QUALIFIED PROPERTY.—The term "qualified property" means—

"(A) Any money or other property which is located in the United States, but only if ordinary and necessary for the active conduct of a qualified trade or business (as determined under paragraph (3)) carried on by the controlled foreign corporation.

"(B) Property which would qualify under subparagraph (A) except for the fact that it is located in the United States, but only of such property is—

"(i) obligations of the United States, money, or deposits with persons carrying on the banking business;

"(ii) property purchased in the United States for export to, or for use in, foreign countries; or

"(iii) any loan arising in connection with the sale of property if the amount of such loan outstanding at no time during the taxable year exceeds the amount which would be ordinary and necessary to carry on the trade or business of both the lending corporation and the borrowing United States person had the sale been made between unrelated persons.

"(C) Stock owned by the controlled foreign corporation in another controlled foreign corporation in which it owns at least 10 percent of the voting stock and 10 percent of the value of all classes of stock and in which it together with four or fewer United States persons, owns, directly or indirectly, more than 50 percent of the voting stock (unless under the laws of a less developed country such percentage of ownership is not permitted, in which case such lesser percentage as is permitted); but this subparagraph shall apply only if—

"(i) substantially all of the property of such other controlled foreign corporation is ordinary and necessary for the active conduct of a trade or business engaged in by it almost wholly within a less developed country or countries, and

"(ii) such other controlled foreign corporation is created or organized under the laws of one of such countries in which it is so engaged.

"(D) Any investment which is required because of restrictions imposed by a less developed country, and any investment which, when made, was so required and which would result in substantial losses if withdrawn.

"(3) QUALIFIED TRADE OR BUSINESS.—

"(A) A trade or business is a qualified trade or business if such trade or business (or substantially the same trade or business)—

"(i) is carried on by the controlled foreign corporation outside the United States and has been so carried on by such corporation, while controlled by substantially the same United States persons since December 31, 1962, or during the 5-year period ending with the close of the preceding taxable year, or

"(ii) is carried on by the controlled foreign corporation almost wholly within a less developed country or countries.

"(B) A trade or business which is a qualified trade or business for a corporation in which the controlled foreign corporation owns at least 80 percent of the total combined voting power of all classes of stock entitled to vote and at least 80 percent of the total value of all classes of stock shall be treated as a qualified trade or business for the controlled foreign corporation if such percentage of stock was owned continuously since December 31, 1962, or during the 5-year period ending with the close of the preceding taxable year.

"(4) SITUS OF CERTAIN PROPERTY.—Property which is an obligation of, or pledges and guarantees made with respect to obligations of, United States persons shall be considered as property located in the United States.

"(5) LESS DEVELOPED COUNTRY DEFINED.—The term "less developed country" means (in respect of any foreign corporation) any foreign country (other than an area within the Sino Soviet bloc) or any possession of the United States, with respect to which on the first day of the taxable year, there is in effect an Executive order by the President of the United States designating such country or possession as an economically less developed country for purposes of this subpart. For purposes of the preceding sentence, an overseas territory, department, province, or possession may be treated as a separate country. No designation shall be made under this paragraph with respect to Australia, Austria, Belgium, Canada, Denmark, France, Germany (Federal Republic), Hong Kong, Italy, Japan, Liechtenstein, Luxembourg, Monaco, Netherlands, New Zealand, Norway, Union of South Africa, San Marino, Sweden, Switzerland, United Kingdom.

"SEC. 954. Controlled foreign corporations.

"(a) GENERAL RULE.—For purposes of this subpart, the term "controlled foreign corporation" means any foreign corporation of which more than 50 percent of the total combined voting power of all classes of stock entitled to vote is owned, directly or indirectly (within the meaning of section 955 (b)), by United States persons on any day during the taxable year of such foreign corporation.

"(b) SPECIAL RULE FOR INSURANCE.—For purposes only of taking into account income described in section 952(a) (1) (A) (relating to income derived from insurance of United States risks), the term "controlled foreign corporation" includes not only a foreign corporation as defined by subsection (a) but also one of which more than 25 percent of the total combined voting power of all classes of stock is owned, directly or indirectly (within the meaning of section 955 (b)), by United States persons on any day during the taxable year of such corporation, if the gross amount of premiums or other consideration in respect of reinsurance or the issuing of insurance or annuity contracts in connection with property in, or residents of, the United States, exceeds 75 percent of the gross amount of all premiums or other consideration in respect of all risks.

"(c) SPECIAL RULE FOR CERTAIN LESS DEVELOPED COUNTRIES.—In the case of any foreign corporation to which section 953(b) (2) (C) applies, the maximum percentage of ownership permitted under the laws of a less developed country shall be considered, in lieu of the more than 50 percent requirement in subsection (a), the percentage required

under subsection (a) in order for the corporation to be classified as a controlled foreign corporation.

"Sec. 955. Rules for determining stock ownership

"(a) FOR PURPOSES OF SECTION 951(a).

"(1) GENERAL RULE. For purposes of section 951(a), stock owned means—

"(A) stock owned directly, and

"(B) stock owned with the application of paragraph (2).

"(2) STOCK OWNERSHIP THROUGH FOREIGN ENTITIES.—For purposes of subparagraph (B) of paragraph (1), stock owned, directly or indirectly, by or for a foreign corporation, foreign partnership, or foreign trust or foreign estate (within the meaning of section 7701(a)(31)) shall be considered as being owned proportionately by its shareholders, partners, or beneficiaries. Stock considered to be owned by a person by reason of the application of the preceding sentence shall, for purposes of applying such sentence, be treated as actually owned by such person.

"(3) SPECIAL RULE FOR MUTUAL INSURANCE COMPANIES.—For purposes of applying paragraph (1) in the case of a foreign mutual insurance company, the term "stock" shall include any certificate entitling the holder to voting power in the corporation.

"(b) OTHER PROVISIONS. For purposes of sections 951(b), 952(a)(1)(C), and 954, section 318(a) (relating to constructive ownership of stock) shall apply to the extent that the effect is to subject a United States person to the requirement of section 951(a), to treat 5 or fewer United States persons as owning more than 50 percent of all classes of stock entitled to vote of a controlled foreign corporation, or to make a foreign corporation a controlled foreign corporation under section 954, except—

"(1) In applying paragraph (1)(A) of section 318(a), stock owned by a nonresident alien individual (other than a foreign trust or foreign estate) shall not be considered as owned by a citizen or by a resident alien individual.

"(2) In applying the first sentence of subparagraphs (A) and (B), and in applying clause (i) of subparagraph (C), of section 318(a)(2)—

"(A) if a partnership, estate, trust, or corporation owns, directly or indirectly, more than 50 percent of the total combined voting power of all classes of stock entitled to vote of a corporation, it shall be considered as owning all the stock entitled to vote, and

"(B) if a partnership, estate, trust, or corporation owns, directly or indirectly, more than 50 percent of the total value of shares of all classes of stock of a corporation, it shall be considered as owning the total value of all of the outstanding stock of such corporation. The application of this subparagraph shall not have the effect of increasing voting power of a partner, beneficiary, or shareholder, for purposes of subparagraph (A).

"(3) Stock owned by a partnership, estate, trust, or corporation, by reason of the application of the second sentence of subparagraphs (A) and (B), and the application of clause (ii) of subparagraph (C), of section 318(a)(2), shall not be considered as owned by such partnership, estate, trust, or corporation, for the purposes of applying the first sentence of subparagraphs (A) and (B), and in applying clause (i) of subparagraph (C), of section 318(a)(2).

"(4) In applying clause (i) of subparagraph (C) of section 318(a)(2), the 50-percent limitation contained in subparagraph (C) shall not apply.

"Sec. 956. Exclusion from gross income of previously taxed earnings and profits.

"(a) EXCLUSION FROM GROSS INCOME OF UNITED STATES PERSONS.—For purposes of this chapter, the earnings and profits for a tax-

able year of a foreign corporation attributable to amounts which are, or have been, included in the gross income of a United States person under section 951(a) shall not, when—

"(1) such amounts are distributed to, or

"(2) such amounts would, but for this subsection, be included under section 951(a) (1)(B) in the gross income of,

such person (or any other United States person who acquires from any person any portion of the interest of such United States person in such foreign corporation, but only to the extent of such portion, and subject to such proof of the identity of such interest as the Secretary or his delegate may by regulations prescribe) directly, or indirectly through a chain of ownership described under section 955(a), be again included in the gross income of such United States person (or of such other United States person).

"(b) EXCLUSION FROM GROSS INCOME OF CERTAIN FOREIGN SUBSIDIARIES.—For purposes of section 951(a), the earnings and profits for a taxable year of a controlled foreign corporation attributable to amounts which are, or have been, included in the gross income of a United States person under section 951(a), shall not, when distributed through a chain of ownership described under section 955(a), be also included in the gross income of another controlled foreign corporation in such chain for purposes of the application of section 951(a) to such other controlled foreign corporation with respect to such United States person (or to any other United States person who acquires from any person any portion of the interest of such United States person in the controlled foreign corporation, but only to the extent of such portion, and subject to such proof of identity of such interest as the Secretary or his delegate may prescribe by regulations).

"(c) ALLOCATIONS OF DISTRIBUTIONS.—For purposes of subsections (a) and (b), section 316(a) shall be applied by applying paragraph (2) thereof, and then paragraph (1) thereof—

"(1) first to earnings and profits attributable to amounts included in gross income under section 951(a)(1)(B) (or which would have been included except for section 956(a)(2)),

"(2) then to earnings and profits attributable to amounts included in gross income under section 951(a)(1)(A) (but reduced by amounts not included under section 951(a)(1)(B) because of the exclusion in section 956(a)(2)), and

"(3) then to other earnings and profits.

"(d) DISTRIBUTIONS EXCLUDED FROM GROSS INCOME NOT TO BE TREATED AS DIVIDENDS.—Except as provided in section 957(a)(3), any distribution excluded from gross income under subsection (a) shall be treated, for purposes of this chapter, as a distribution which is not a dividend.

"Sec. 957. Special rules for foreign tax credit.

"(a) TAXES PAID BY A FOREIGN CORPORATION.—

"(1) GENERAL RULE.—For purposes of subpart A of this part, if there is included, under section 951(a), in the gross income of a domestic corporation any amount attributable to earnings and profits—

"(A) of a foreign corporation at least 10 percent of the voting stock of which is directly owned by such domestic corporation, or

"(B) of a foreign corporation at least 50 percent of the voting stock of which is directly owned by a foreign corporation at least 10 percent of the voting stock of which is in turn directly owned by such domestic corporation,

then, under regulations prescribed by the Secretary or his delegate, such domestic corporation shall be deemed to have paid the same proportion of the total income, war

profits, and excess profits taxes paid (or deemed paid, if, paragraph (4) applies) to a foreign country or possession of the United States for the taxable year which the amount of earnings and profits of such foreign corporation so included in gross income of the domestic corporation bears to the entire amount of the total earnings and profits of such foreign corporation for such taxable year.

"(2) TAXES PREVIOUSLY DEEMED PAID BY DOMESTIC CORPORATIONS.—If a domestic corporation receives a distribution from a foreign corporation, any portion of which is excluded from gross income under section 956, the income, war profits, and excess profits taxes paid or deemed paid by such foreign corporation to any foreign country or to any possession of the United States in connection with the earnings and profits of such foreign corporation from which such distribution is made shall not be taken into account for purposes of section 902, to the extent such taxes were deemed paid by such domestic corporation under paragraph (1) for any prior taxable year.

"(3) TAXES PAID BY FOREIGN CORPORATION AND NOT PREVIOUSLY DEEMED PAID BY DOMESTIC CORPORATION.—Any portion of a distribution from a foreign corporation received by a domestic corporation which is excluded from gross income under section 956(a) shall be treated by the domestic corporation as a dividend, solely for purposes of taking into account under section 902 any income, war profits, or excess profits taxes paid to any foreign country or to any possession of the United States, on or with respect to the accumulated profits of such foreign corporation from which such distribution is made, which were not deemed paid by the domestic corporation under paragraph (1) for any prior taxable year.

"(4) TAXES PAID BY A FOREIGN SUBSIDIARY.—If subparagraph (A) of paragraph (1) applies with respect to an amount included in gross income under section 951(a) for a taxable year, then such amount shall be considered a dividend for purpose of the application of section 902(b).

"(5) INCLUSION IN GROSS INCOME.—"For inclusion in gross income of amount equal to taxes deemed paid under paragraph (1), see section 78.

"(b) SPECIAL RULES FOR FOREIGN TAX CREDIT IN YEAR OF RECEIPT OF PREVIOUSLY TAXED EARNINGS AND PROFITS.—

"(1) INCREASE IN SECTION 904 LIMITATION.—In the case of any taxpayer who—

"(A) either (i) chose to have the benefits of subpart A of this part for a taxable year in which he was required under section 951(a) to include in his gross income an amount in respect of a controlled foreign corporation, or (ii) did not pay or accrue for such taxable year any income, war profits or excess profits taxes to any foreign country or to any possession of the United States, and

"(B) chooses to have the benefits of subpart A of this part for the taxable year in which he receives a distribution or amount which is excluded from gross income under section 956(a) and which is attributable to earnings and profits of the controlled foreign corporation which was included in his gross income for the taxable year referred to in subparagraph (A), and

"(C) for the taxable year in which such distribution or amount is received, pays, or is deemed to have paid, or accrues income, war profits, or excess profits taxes to a foreign country or to any possession of the United States with respect to such distribution or amount,

the applicable limitation under section 904 for the taxable year in which such distribution or amount is received shall be increased as provided in paragraph (2), but such increase shall not exceed the amount of such

taxes paid, or deemed paid, or accrued with respect to such distribution or amount.

"(2) AMOUNT OF INCREASE.—The amount of increase of the applicable limitation under section 904(a) for the taxable year in which the distribution or amount referred to in paragraph (1)(B) is received shall be an amount equal to—

"(A) the amount by which the applicable limitation under section 904(a) for the taxable year referred to in paragraph (1)(A) was increased by reason of the inclusion in gross income under section 951(a) of the amount in respect of the controlled foreign corporation, reduced by

"(B) the amount of any income, war profits, and excess profits taxes paid, or deemed paid, or accrued to any foreign country or possession of the United States which were allowable as a credit under section 901 for the taxable year referred to in paragraph (1)(A) and which would not have been allowable but for the inclusion in gross income of the amount described in subparagraph (A).

"(3) CASES IN WHICH TAXES NOT TO BE ALLOWED AS DEDUCTIONS.—In the case of any taxpayer who—

"(A) chose to have the benefits of subpart A of this part for a taxable year in which he was required under section 951(a) to include in his gross income an amount in respect of a controlled foreign corporation, and

"(B) does not choose to have the benefits of subpart A of this part for the taxable year in which he receives a distribution or amount which is excluded from gross income under section 956(a) and which is attributable to earnings and profits of the controlled foreign corporation which was included in his gross income for the taxable year referred to in subparagraph (A),

no deduction shall be allowed under section 164 for the taxable year in which such distribution or amount is received for any income, war profits, or excess profits taxes paid or accrued to any foreign country or to any possession of the United States on or with respect to such distribution or amount.

"(4) INSUFFICIENT TAXABLE INCOME.—If an increase in the limitation under this subsection exceeds the tax imposed by this chapter for such year, the amount of such excess shall be deemed an overpayment of tax for such year.

"Sec. 958. Adjustments to basis of stock in controlled foreign corporation and of other property.

"(a) INCREASE IN BASIS.—Under regulations prescribed by the Secretary or his delegate, the basis of a United States person's stock in a controlled foreign corporation, and the basis of property of a United States person by reason of which he is considered under section 955(a)(2) as owning stock of a controlled foreign corporation, shall be increased by the amount required to be included in his gross income under section 951(a) with respect to such stock or with respect to such property, as the case may be, but only to the extent to which such amount was included in the gross income of such person.

"(b) REDUCTION IN BASIS.—

"(1) IN GENERAL.—Under regulations prescribed by the Secretary or his delegate, the adjusted basis of stock or other property with respect to which a United States person receives an amount which is excluded from gross income under section 956(a) shall be reduced by the amount so excluded.

"(2) AMOUNT IN EXCESS OF BASIS.—To the extent that an amount excluded from gross income under section 956(a) exceeds the adjusted basis of the stock or other property with respect to which it is received, the amount shall be treated as gain from the sale or exchange of property."

"(b) TECHNICAL AND CLERICAL AMENDMENTS.—

"(1) Section 551(b) (relating to foreign personal holding company income included in gross income of United States shareholders) is amended by adding at the end thereof the following new sentence: "The amount included in the gross income of any United States shareholder for any taxable year under the preceding sentence shall be reduced by such shareholder's proportionate share of the undistributed personal holding company income which is included in his gross income under section 951(a)(1)(A) (relating to amounts included in gross income of United States persons) for such taxable year as his pro rata share of the subpart F income of the company."

"(2) Section 901 (relating to foreign tax credit) is amended by striking out 'section 902' and inserting in lieu thereof 'sections 902 and 957'."

"(3) Section 902(e) is amended to read as follows:

"(e) CROSS REFERENCES.—

"(1) For application of subsections (a) and (b) with respect to taxes deemed paid in a prior taxable year by a United States person with respect to a controlled foreign corporation, see section 957.

"(2) For reduction of credit with respect to dividends paid out of accumulated profits for years for which certain information is not furnished, see section 6038."

"(4) Section 904(f) is amended to read as follows:

"(f) CROSS REFERENCES.—

"(1) For increase of applicable limitation under subsection (a) for taxes paid with respect to amounts received which were included in the gross income of the taxpayer for a prior taxable year as a United States person with respect to a controlled foreign corporation, see section 957(b).

"(2) For special rule relating to the application of the credit provided by section 901 in the case of affiliated groups which include Western Hemisphere trade corporations for years in which the limitation provided by subsection (a)(2) applies, see section 1503(d)."

"(5) The table of subparts for part III of subchapter N of chapter 1 is amended by adding at the end thereof the following:

"Subpart F. Controlled foreign corporations."

"(6) Section 1016(a) (relating to adjustments to basis) is amended—

"(A) by striking out the period at the end of paragraph (18) and inserting in lieu thereof a semicolon; and

"(B) by adding after paragraph (18) the following new paragraph:

"(19) to the extent provided in section 958 in the case of stock in controlled foreign corporations (or foreign corporations which were controlled foreign corporations) and of property by reason of which a person is considered as owning such stock."

"(c) EFFECTIVE DATE.—The amendments made by this section shall apply with respect to taxable years of foreign corporations beginning after December 31, 1962, and to taxable years of United States persons within which or with which such taxable years of such foreign corporations end."

And, in lieu thereof, to insert:

"Sec. 12. Controlled foreign corporations.

"(a) IN GENERAL.—Part III of subchapter N of chapter 1 (relating to income from sources without the United States) is amended by adding at the end thereof the following new subparts:

"Subpart F—Controlled Foreign Corporations.

"Sec. 951. Amounts included in gross income of United States shareholders.

"Sec. 952. Subpart F income defined.

"Sec. 953. Income from insurance of United States risks.

"Sec. 954. Foreign base company income.

"Sec. 955. Withdrawal of previously excluded subpart F income from qualified investment.

"Sec. 956. Investment of earnings in United States property.

"Sec. 957. Controlled foreign corporations; United States persons.

"Sec. 958. Rules for determining stock ownership.

"Sec. 959. Exclusion from gross income of previously taxed earnings and profits.

"Sec. 960. Special rules for foreign tax credit.

"Sec. 961. Adjustments to basis of stock in controlled foreign corporations and of other property.

"Sec. 962. Election by individuals to be subject to tax at corporate rates.

"Sec. 963. Receipt of minimum distributions by domestic corporations.

"Sec. 964. Miscellaneous provisions.

"Sec. 951. Amounts included in gross income of United States shareholders.

"(a) AMOUNTS INCLUDED.—

"(1) IN GENERAL.—If a foreign corporation is a controlled foreign corporation for an uninterrupted period of 30 days or more during any taxable year beginning after December 31, 1962, every person who is a United States shareholder (as defined in subsection (b)) of such corporation and who owns (within the meaning of section 958(a)) stock in such corporation on the last day, in such year, on which such corporation is a controlled foreign corporation shall include in his gross income, for his taxable year in which or with which such taxable year of the corporation ends—

"(A) the sum of—

"(i) except as provided in section 963, his pro rata share (determined under paragraph (2)) of the corporation's subpart F income for such year, and

"(ii) his pro rata share (determined under section 955(a)(3)) of the corporation's previously excluded subpart F income withdrawn from investment in less developed countries for such year; and

"(B) his pro rata share (determined under section 956(a)(2)) of the corporation's increase in earnings invested in United States property for such year (but only to the extent not excluded from gross income under section 959(a)(2)).

"(2) PRO RATA SHARE OF SUBPART F INCOME.—The pro rata share referred to in paragraph (1)(A)(i) in the case of any United States shareholder is the amount—

"(A) which would have been distributed with respect to the stock which such shareholder owns (within the meaning of section 958(a)) in such corporation if on the last day, in its taxable year, on which the corporation is a controlled foreign corporation it had distributed pro rata to its shareholders an amount (i) which bears the same ratio to its subpart F income for the taxable year, as (ii) the part of such year during which the corporation is a controlled foreign corporation bears to the entire year, reduced by

"(B) the amount of distributions received by any other person during such year as a dividend with respect to such stock, but only to the extent of the dividend which would have been received if the distribution by the corporation had been the amount (i) which bears the same ratio to the subpart F income of such corporation for the taxable year, as (ii) the part of such year during which such shareholder did not own (within the meaning of section 958(a)) such stock bears to the entire year.

“(3) LIMITATION ON PRO RATA SHARE OF PREVIOUSLY EXCLUDED SUBPART F INCOME WITHDRAWN FROM INVESTMENT.—For purposes of paragraph (1)(A)(ii), the pro rata share of any United States shareholder of the previously excluded subpart F income of a controlled foreign corporation withdrawn from investment in less developed countries shall not exceed an amount (A) which bears the same ratio to his pro rata share of such income withdrawn (as determined under section 955(a)(3)) for the taxable year, as (B) the part of such year during which the corporation is a controlled foreign corporation bears to the entire year.

“(4) LIMITATION ON PRO RATA SHARE OF INVESTMENT IN UNITED STATES PROPERTY.—For purposes of paragraph (1)(B), the pro rata share of any United States shareholder in the increase of the earnings of a controlled foreign corporation invested in United States property shall not exceed an amount (A) which bears the same ratio to his pro rata share of such increase the corporation is a controlled foreign corporation bears to the entire year.

“(b) UNITED STATES SHAREHOLDER DEFINED.—For purposes of this subpart, the term “United States shareholder” means, with respect to any foreign corporation, a United States person (as defined in section 957(d)) who owns (within the meaning of section 958(a)), or is considered as owning by applying the rules of ownership of section 958(b), 10 percent or more of the total combined voting power of all classes of stock entitled to vote of such foreign corporation.

“(c) COORDINATION WITH ELECTION OF A FOREIGN INVESTMENT COMPANY TO DISTRIBUTE INCOME.—A United States shareholder who, for his taxable year, is a qualified shareholder (within the meaning of section 1247(c)) of a foreign investment company with respect to which an election under section 1247 is in effect shall not be required to include in gross income, for such taxable year, any amount under subsection (a) with respect to such company.

“(d) COORDINATION WITH FOREIGN PERSONAL HOLDING COMPANY PROVISIONS.—A United States shareholder who, for his taxable year, is subject to tax under section 551(b) (relating to foreign personal holding company income included in gross income of United States shareholders) on income of a controlled foreign corporation shall not be required to include in gross income, for such taxable year, any amount under subsection (a) with respect to such company.

“Sec. 952. Subpart F income defined.

“(a) IN GENERAL.—For purposes of this subpart, the term “subpart F income” means, in the case of any controlled foreign corporation, the sum of—

“(1) the income derived from the insurance of United States risks (as determined under section 953), and

“(2) the foreign base company income (as determined under section 954).

“(b) EXCLUSION OF UNITED STATES INCOME.—Subpart F income does not include any item includible in gross income under this chapter (other than this subpart) as income derived from sources within the United States of a foreign corporation engaged in trade or business in the United States.

“(c) LIMITATION.—For purposes of subsection (a), the subpart F income of any controlled foreign corporation for any taxable year shall not exceed the earnings and profits of such corporation for such year reduced by the amount (if any) by which—

“(1) an amount equal to—

“(a) the sum of the deficits in earnings and profits for prior taxable years beginning after December 31, 1962, plus

“(B) the sum of the deficits in earnings and profits for taxable years beginning after December 31, 1959, and before January 1,

1963 (reduced by the sum of the earnings and profits for such taxable years); exceeds

“(2) an amount equal to the sum of the earnings and profits for prior taxable years beginning after December 31, 1962, allocated to other earnings and profits under section 959(c)(3).

For purposes of the preceding sentence, any deficit in earnings and profits for any prior taxable year shall be taken into account under paragraph (1) for any taxable year only to the extent it has not been taken into account under such paragraph for any preceding taxable year to reduce earnings and profits of such preceding year.

“(d) SPECIAL RULE IN CASE OF INDIRECT OWNERSHIP.—For purposes of subsection (c), if—

“(1) a United States shareholder owns (within the meaning of section 958(a)) stock of a foreign corporation, and by reason of such ownership owns (within the meaning of such section) stock of any other foreign corporation, and

“(2) any of such foreign corporations has a deficit in earnings and profits for the taxable year,

then the earnings and profits for the taxable year of each such foreign corporation which is a controlled foreign corporation shall, with respect to such United States shareholder, be properly reduced to take into account any deficit described in paragraph (2) in such manner as the Secretary or his delegate shall prescribe by regulations.

“Sec. 953. Income from insurance of United States risks.

“(a) GENERAL RULE.—For purposes of section 952(a)(1), the term “income derived from the insurance of United States risks” means that income which—

“(1) is attributable to the reinsurance or the issuing of any insurance or annuity contract—

“(A) in connection with property in, or liability arising out of activity in, or in connection with the lives or health of residents of, the United States, or

“(B) in connection with risks not included in subparagraph (A) as the result of any arrangement whereby another corporation receives a substantially equal amount of premiums or other consideration in respect to any reinsurance or the issuing of any insurance or annuity contract in connection with property in, or liability arising out of activity in, or in connection with the lives or health of residents of, the United States, and

“(2) would (subject to the modifications provided by paragraphs (1), (2), and (3) of subsection (b)) be taxed under subchapter L of this chapter if such income were the income of a domestic insurance corporation. This section shall apply only in the case of a controlled foreign corporation which receives, during any taxable year, premiums or other consideration in respect of the reinsurance, and the issuing, of insurance and annuity contracts described in paragraph (1) in excess of 5 percent of the total of premiums and other consideration received during such taxable year in respect of all reinsurance and issuing of insurance and annuity contracts.

“(b) SPECIAL RULES.—For purposes of subsection (a)—

“(1) In the application of part I of subchapter L, life insurance company taxable income is the gain from operations as defined in section 809(b).

“(2) A corporation which would, if it were a domestic insurance corporation, be taxable under part II of subchapter L shall apply subsection (a) as if it were taxable under part III of subchapter L.

“(3) The following provisions of subchapter L shall not apply:

“(A) Section 809(d)(4) (operations loss deduction).

“(B) Section 809(d)(5) (certain non-participating contracts).

“(C) Section 809(d)(6) (group life, accident, and health insurance).

“(D) Section 809(d)(10) (small business deduction).

“(E) Section 817(b) (gain on property held on December 31, 1958, and certain substituted property acquired after 1958).

“(F) Section 832(b)(5) (certain capital losses).

“(4) The items referred to in—

“(A) section 809(c)(1) (relating to gross amount of premiums and other considerations),

“(B) section 809(c)(2) (relating to net decrease in reserves),

“(C) section 809(d)(2) (relating to net increase in reserves), and

“(D) section 832(b)(4) (relating to premiums earned on insurance contracts),

shall be taken into account only to the extent they are in respect of any reinsurance or the issuing of any insurance or annuity contract described in subsection (a)(1).

“(5) All items of income, expenses, losses and deductions (other than those taken into account under paragraph (4)) shall be properly allocated or apportioned under regulations prescribed by the Secretary or his delegate.

“SEC. 954. FOREIGN BASE COMPANY INCOME.

“(a) FOREIGN BASE COMPANY INCOME.—For purposes of section 952(a)(2), the term “foreign base company income” means for any taxable year the sum of—

“(1) the foreign personal holding company income for the taxable year (determined under subsection (c) and reduced as provided in subsection (b)(5)),

“(2) the foreign base company sales income for the taxable year (determined under subsection (d) and reduced as provided in subsection (b)(5)), and

“(3) the foreign base company services income for the taxable year (determined under subsection (e) and reduced as provided in subsection (b)(5)).

“(b) EXCLUSIONS AND SPECIAL RULES.—

“(1) EXCLUSION OF CERTAIN DIVIDENDS, INTEREST, AND GAINS FROM QUALIFIED INVESTMENTS IN LESS DEVELOPED COUNTRIES.—For purposes of subsection (a), foreign base company income does not include—

“(A) dividends and interest received during the taxable year from investments which at the time of receipt are qualified investments in less developed countries (as defined in section 955(b)), or

“(B) if the gains from the sale or exchange during the taxable year of investments which at the time of sale or exchange are qualified investments in less developed countries exceed the losses from the sale or exchange during the taxable year of such qualified investments, the amount by which such gains exceed such losses.

The preceding sentence shall apply only to the extent that the sum of the dividends and interest described in subparagraph (A) and the amount described in subparagraph (B) does not exceed the increase for the taxable year in qualified investments in less developed countries of the controlled foreign corporation (as determined under subsection (f)).

“(2) EXCLUSION OF CERTAIN SHIPPING INCOME.—For purposes of subsection (a), foreign base company income does not include income derived from, or in connection with, the use (or hiring or leasing for use) of any aircraft or vessel in foreign commerce, or the performance of services directly related to the use of any such aircraft or vessel.

“(3) SPECIAL RULE WHERE FOREIGN BASE COMPANY IS LESS THAN 30 PERCENT OR MORE THAN 70 PERCENT OF GROSS INCOME.—For purposes of subsection (a)—

"(A) If the foreign base company income (determined without regard to paragraphs (1) and (5)) is less than 30 percent of gross income, no part of the gross income of the taxable year shall be treated as foreign base company income.

"(B) If the foreign base company income (determined without regard to paragraphs (1) and (5)) exceeds 70 percent of gross income, the entire gross income of the taxable year shall, subject to the provisions of paragraphs (1), (2), (4), and (5), be treated as foreign base company income.

"(4) EXCEPTION FOR FOREIGN CORPORATIONS NOT AVAILED OF TO REDUCE TAXES.—For purposes of subsection (a), foreign base company income does not include any item of income received by a controlled foreign corporation if it is established to the satisfaction of the Secretary or his delegate with respect to such item that the creation or organization of the controlled foreign corporation receiving such item under the laws of the foreign country in which it is incorporated does not have the effect of substantial reduction of income, war profits, or excess profits taxes or similar taxes.

"(5) DEDUCTIONS TO BE TAKEN INTO ACCOUNT.—For purposes of subsection (a), the foreign personal holding company income, the foreign base company sales income, and the foreign base company services income shall be reduced, under regulations prescribed by the Secretary or his delegate, so as to take into account deductions (including taxes) properly allocable to such income.

"(c) FOREIGN PERSONAL HOLDING COMPANY INCOME.—

"(1) IN GENERAL.—For purposes of subsection (a)(1), the term "foreign personal holding company income" means the foreign personal holding company income (as defined in section 553), modified and adjusted as provided in paragraphs (2), (3), and (4).

"(2) RENTS INCLUDED WITHOUT REGARD TO 50 PERCENT LIMITATION.—For purposes of paragraph (1), all rents shall be included in foreign personal holding company income without regard to whether or not such rents constitute 50 percent or more of gross income.

"(3) CERTAIN INCOME DERIVED IN ACTIVE CONDUCT OF TRADE OR BUSINESS.—For purposes of paragraph (1), foreign personal holding company income does not include—

"(A) rents and royalties which are derived in the active conduct of a trade or business and which are received from a person other than a related person (within the meaning of subsection (d)(3)), or

"(B) dividends, interest, and gains from the sale or exchange of stock or securities derived in the conduct of a banking, financing, or similar business, or derived from the investments made by an insurance company of its unearned premiums or reserves ordinary and necessary for the proper conduct of its insurance business, and which are received from a person other than a related person (within the meaning of subsection (d)(3)).

"(4) CERTAIN INCOME RECEIVED FROM RELATED PERSONS.—For purposes of paragraph (1), foreign personal holding company incomes does not include—

"(A) dividends and interest received from a related person which (i) is organized under the laws of the same foreign country under the laws of which the controlled foreign corporation is created or organized, and (ii) has a substantial part of its assets used in its trade or business located in such same foreign country;

"(B) interest received in the conduct of a banking, financing or similar business from a related person engaged in the conduct of a banking, financing, or similar business if the businesses of the recipient and the payor are predominantly with persons other than related persons; and

"(C) rents, royalties, and similar amounts received from a related person for the use of, or the privilege of using, property within the country under the laws of which the controlled foreign corporation is created or organized.

"(d) FOREIGN BASE COMPANY SALES INCOME.—

"(1) IN GENERAL.—For purposes of subsection (a)(2), the term "foreign base company sales income" means income (whether in the form of profits, commissions, fees, or otherwise) derived in connection with the purchase of personal property from a related person and its sale to any person, the sale of personal property to any person on behalf of a related person, the purchase of personal property from any person and its sale to a related person, or the purchase of personal property from any person on behalf of a related person where—

"(A) the property which is purchased (or in the case of property sold on behalf of a related person, the property which is sold) is manufactured, produced, grown, or extracted outside the country under the laws of which the controlled foreign corporation is created or organized, and

"(B) the property is sold for use, consumption, or disposition outside such foreign country, or, in the case of property purchased on behalf of a related person, is purchased for use, consumption, or disposition outside such foreign country.

"(2) CERTAIN BRANCH INCOME.—For purposes of determining foreign base company sales income in situations in which the carrying on of activities by a controlled foreign corporation through a branch or similar establishment outside the country of incorporation of the controlled foreign corporation has substantially the same effect as if such branch or similar establishment were a wholly owned subsidiary corporation deriving such income, under regulations prescribed by the Secretary or his delegate the income attributable to the carrying on of such activities of such branch or similar establishment shall be treated as income derived by a wholly owned subsidiary of the controlled foreign corporation and shall constitute foreign base company sales income of the controlled foreign corporation.

"(3) RELATED PERSON DEFINED.—For purposes of this section, a person is a related person with respect to a controlled foreign corporation, if—

"(A) such person is an individual, partnership, trust, or estate which controls the controlled foreign corporation;

"(B) such person is a corporation which controls, or is controlled by, the controlled foreign corporation; or

"(C) such person is a corporation which is controlled by the same person or persons which control the controlled foreign corporation.

For purpose of the preceding sentence, control means the ownership, directly or indirectly, of stock possessing more than 50 percent of the total combined voting power of all classes of stock entitled to vote. For purposes of this paragraph, the rules for determining ownership of stock prescribed by section 958 shall apply.

"(e) FOREIGN BASE COMPANY SERVICES INCOME.—For purposes of subsection (a)(3), the term "foreign base company services income" means income (whether in the form of compensation, commissions, fees, or otherwise) derived in connection with the performance of technical, managerial, engineering, architectural, scientific, skilled, industrial, commercial, or like services which—

"(1) are performed for or on behalf of any related person (within the meaning of subsection (d)(3)), and

"(2) are performed outside the country under the laws of which the controlled foreign corporation is created or organized.

The preceding sentence shall not apply to income derived in connection with the performance of services which are directly related to the sale or exchange by the controlled foreign corporation of property manufactured, produced, grown, or extracted by it and which are performed prior to the time of the sale or exchange, or of services directly related to an offer or effort to sell or exchange such property.

"(f) INCREASE IN QUALIFIED INVESTMENTS IN LESS DEVELOPED COUNTRIES.—For purposes of subsection (b)(1), the increase for any taxable year in qualified investments in less developed countries of any controlled foreign corporation is the amount by which—

"(1) the qualified investments in less developed countries (as defined in section 955(b)) of the controlled foreign corporation at the close of the taxable year, exceeds

"(2) the qualified investments in less developed countries (as so defined) of the controlled foreign corporation at the close of the preceding taxable year.

"Sec. 955. Withdrawal of Previously Excluded Subpart F Income From Qualified Investment.

"(a) GENERAL RULES.—

"(1) AMOUNT WITHDRAWN.—For purposes of this subpart, the amount of previously excluded subpart F income of any controlled foreign corporation withdrawn from investment in less developed countries for any taxable year is an amount equal to the decrease in the amount of qualified investments in less developed countries of the controlled foreign corporation for such year, but only to the extent that the amount of such decrease does not exceed an amount equal to—

"(A) the sum of the amounts excluded under section 954(b)(1) from the foreign base company income of such corporation for all prior taxable years, reduced by

"(B) the sum of the amounts of previously excluded subpart F income withdrawn from investment in less developed countries of such corporation determined under this subsection for all prior taxable years.

"(2) DECREASE IN QUALIFIED INVESTMENTS.—For purposes of paragraph (1), the amount of the decrease in qualified investments in less developed countries of any controlled foreign corporation for any taxable year is the amount by which—

"(A) the amount of qualified investments in less developed countries of the controlled foreign corporation at the close of the preceding taxable year, exceeds

"(B) the amount of qualified investments in less developed countries of the controlled foreign corporation at the close of the taxable year,

to the extent the amount of such decrease does not exceed the sum of the earnings and profits for the taxable year and the earnings and profits accumulated for prior taxable years beginning after December 31, 1962. For purposes of this paragraph, if qualified investments in less developed countries are disposed of by the controlled foreign corporation during the taxable year, the amount of the decrease in qualified investments in less developed countries of such controlled foreign corporation for such year shall be reduced by an amount equal to the amount (if any) by which the losses on such dispositions during such year exceed the gains on such dispositions during such year.

"(3) PRO RATA SHARE OF AMOUNT WITHDRAWN.—In the case of any United States shareholder, the pro rata share of the amount of previously excluded subpart F income of any controlled foreign corporation withdrawn from investment in less developed countries for any taxable year is his pro rata share of the amount determined under paragraph (1).

“(b) QUALIFIED INVESTMENTS IN LESS DEVELOPED COUNTRIES.—

“(1) IN GENERAL.—For purposes of this subpart, the term “qualified investments in less developed countries” means property which is—

“(A) stock of a less developed country corporation held by the controlled foreign corporation, but only if the controlled foreign corporation owns 10 percent or more of the total combined voting power of all classes of stock of such less developed country corporation;

“(B) an obligation of a less developed country corporation held by the controlled foreign corporation, which, at the time of its acquisition by the controlled foreign corporation, has a maturity of 5 years or more, but only if the controlled foreign corporation owns 10 percent or more of the total combined voting power of all classes of stock of such less developed country corporation; or

“(C) an obligation of a less developed country.

“(2) COUNTRY CEASES TO BE LESS DEVELOPED COUNTRY.—For purposes of this subpart, property which would be a qualified investment in less developed countries, but for the fact that a foreign country has, after the acquisition of such property by the controlled foreign corporation, ceased to be a less developed country, shall be treated as a qualified investment in less developed countries.

“(3) INVESTMENTS AFTER CLOSE OF YEAR.—For purposes of this subpart, a controlled foreign corporation may, under regulations prescribed by the Secretary or his delegate, elect to treat property described in paragraph (1) or (2) which was acquired after the close of the taxable year and on or before the close of the following taxable year, or on or before such day after the close of the following taxable year as such regulations may prescribe, as having been acquired on the last day of the taxable year.

“(4) AMOUNT ATTRIBUTABLE TO PROPERTY.—The amount taken into account under this subpart with respect to any property described in paragraph (1) or (2) shall be its adjusted basis, reduced by any liability to which such property is subject.

“(c) LESS DEVELOPED COUNTRY CORPORATIONS.—

“(1) IN GENERAL.—For purposes of this subpart, the term “less developed country corporation” means a foreign corporation which is created or organized under the laws of a less developed country and which during the taxable year is engaged in the active conduct of one or more trades or businesses and—

“(A) 80 percent or more of the gross income of which for the taxable year is derived from sources within less developed countries; and

“(B) 80 percent or more in value of the assets of which on each day of the taxable year consists of—

“(i) property used in such trades or businesses and located in less developed countries,

“(ii) money, and deposits with persons carrying on the banking business.

“(iii) stock, and obligations which, at the time of their acquisition, have a maturity of 5 years or more, of any other less developed country corporation,

“(iv) an obligation of a less developed country,

“(v) an investment which is required because of restrictions imposed by a less developed country, and

“(vi) property described in section 956 (b) (2).

For purposes of subparagraph (A), the determination as to whether income is derived from sources within less developed countries shall be made under regulations prescribed by the Secretary or his delegate.

“(2) SHIPPING COMPANIES.—For purposes of this subpart, the term “less developed country corporation” also means a foreign corporation—

“(A) 80 percent or more of the gross income of which for the taxable year consists of—

“(i) gross income derived from, or in connection with, the using (or hiring or leasing for use) in foreign commerce of aircraft or vessels registered under the laws of a less developed country, or from, or in connection with, the performance of services directly related to use of such aircraft or vessels, or from the sale or exchange of such aircraft or vessels, and

“(ii) dividends and interest received from foreign corporations which are less developed country corporations within the meaning of this paragraph and 10 percent or more of the total combined voting power of all classes of stock of which are owned by the foreign corporation, and gain from the sale or exchange of stock or obligations of foreign corporations which are such less developed country corporations, and

“(B) 80 percent or more of the assets of which on each day of the taxable year consists of (i) assets used, or held for use, for or in connection with the production of income described in subparagraph (A), and (ii) property described in section 956(b) (2).

“(3) LESS DEVELOPED COUNTRY DEFINED.—For purposes of this subpart, the term “less developed country” means (in respect of any foreign corporation) any foreign country (other than an area within the Sino-Soviet bloc) or any possession of the United States with respect to which, on the first day of the taxable year, there is in effect an Executive order by the President of the United States designating such country or possession as an economically less developed country for purposes of this subpart. For purposes of the preceding sentence, an overseas territory, department, province, or possession may be treated as a separate country. No designation shall be made under this paragraph with respect to Australia, Austria, Belgium, Canada, Denmark, France, Germany (Federal Republic), Hong Kong, Italy, Japan, Liechtenstein, Luxembourg, Monaco, Netherlands, New Zealand, Norway, Union of South Africa, San Marino, Sweden, Switzerland, United Kingdom. After the President has designated any foreign country or any possession of the United States as an economically less developed country for purposes of this subpart, he shall not terminate such designation (either by issuing an Executive order for that purpose or by issuing an Executive order under the first sentence of this paragraph which has the effect of terminating such designation) unless, at least 30 days prior to such termination, he has notified the Senate and the House of Representatives of his intention to terminate such designation.

“Sec. 956. Investment of earnings in United States property.

“(a) GENERAL RULES.—For purposes of this subpart—

“(1) AMOUNT OF INVESTMENT.—The amount of earnings of a controlled foreign corporation invested in United States property at the close of any taxable year is the aggregate amount of such property held, directly or indirectly, by the controlled foreign corporation at the close of the taxable year, to the extent such amount would have constituted a dividend (determined after the application of section 955(a)) if it had been distributed.

“(2) PRO RATA SHARE OF INCREASE FOR YEAR.—In the case of any United States shareholder, the pro rata share of the increase for any taxable year in the earnings of a controlled foreign corporation invested in United States property is the amount determined by subtracting his pro rata share of—

“(A) the amount determined under paragraph (1) for the close of the preceding taxable year, reduced by amounts paid during such preceding taxable year to which section 959(c) (1) applies, from

“(B) the amount determined under paragraph (1) for the close of the taxable year. The determinations under subparagraphs (A) and (B) shall be made on the basis of stock owned (within the meaning of section 958(a)) by such United States shareholder on the last day during the taxable year on which the foreign corporation is a controlled foreign corporation.

“(3) AMOUNT ATTRIBUTABLE TO PROPERTY.—The amount taken into account under paragraph (1) or (2) with respect to any property shall be its adjusted basis, reduced by any liability to which the property is subject.

“(b) UNITED STATES PROPERTY DEFINED.—“(1) IN GENERAL.—For purposes of subsection (a), the term “United States property” means any property acquired after December 31, 1962, which is—

“(A) tangible property located in the United States;

“(B) stock of a domestic corporation;

“(C) an obligation of a United States person; or

“(D) any right to the use in the United States of—

“(i) a patent or copyright,

“(ii) an invention, model, or design (whether or not patented),

“(iii) a secret formula or process, or

“(iv) any other similar property right, which is acquired or developed by the controlled foreign corporation for use in the United States.

“(2) EXCEPTIONS.—For purposes of subsection (a), the term “United States property” does not include—

“(A) obligations of the United States, money, or deposits with persons carrying on the banking business;

“(B) property located in the United States which is purchased in the United States for export to, or use in, foreign countries;

“(C) any obligation of a United States person arising in connection with the sale or processing of property if the amount of such obligation outstanding at no time during the taxable year exceeds the amount which would be ordinary and necessary to carry on the trade or business of both the other party to the sale or processing transaction and the United States person had the sale or processing transaction been made between unrelated persons;

“(D) any aircraft, railroad rolling stock, vessel, motor vehicle, or container used in the transportation of persons or property in foreign commerce and used predominantly outside the United States;

“(E) an amount of assets of an insurance company equivalent to the unearned premiums or reserves ordinary and necessary for the proper conduct of its insurance business attributable to contracts which are not contracts described in section 953(a) (1); and

“(F) an amount of assets of the controlled foreign corporation equal to the earnings and profits accumulated after December 31, 1962, and excluded from subpart F income under section 952(b).

“(c) PLEDGES AND GUARANTEES.—For purposes of subsection (a), a controlled foreign corporation shall, under regulations prescribed by the Secretary or his delegate, be considered as holding an obligation of a United States person if such controlled foreign corporation is a pledgor or guarantor of such obligation.

“Sec. 957. Controlled foreign corporations; United States persons.

“(a) GENERAL RULE.—For purposes of this subpart, the term “controlled foreign corporation” means any foreign corporation of which more than 50 percent of the total

combined voting power of all classes of stock entitled to vote is owned (within the meaning of section 958(a)), or is considered as owned by applying the rules of ownership of section 958(b), by United States shareholders on any day during the taxable year of such foreign corporation.

“(b) SPECIAL RULE FOR INSURANCE.—For purposes only of taking into account income described in section 953(a) (relating to income derived from insurance of United States risks), the term “controlled foreign corporation” includes not only a foreign corporation as defined by subsection (a) but also one of which more than 25 percent of the total combined voting power of all classes of stock is owned (within the meaning of section 958(a)), or is considered as owned by applying the rules of ownership of section 958(b), by United States shareholders on any day during the taxable year of such corporation, if the gross amount of premiums or other consideration in respect of the reinsurance or the issuing of insurance or annuity contracts described in section 953(a) (1) exceeds 75 percent of the gross amount of all premiums or other consideration in respect of all risks.

“(c) CORPORATIONS ORGANIZED IN UNITED STATES POSSESSIONS.—For purposes of this subpart, the term “controlled foreign corporation” does not include any corporation created or organized in the Commonwealth of Puerto Rico or a possession of the United States or under the laws of the Commonwealth of Puerto Rico or a possession of the United States if—

“(1) 80 percent or more of the gross income of such corporation (computed without regard to section 931) for the 3-year period immediately preceding the close of the taxable year (or for such part of such period immediately preceding the close of such taxable year as may be applicable) was derived from sources within the Commonwealth of Puerto Rico or a possession of the United States; and

“(2) 50 percent or more of the gross income of such corporation (computed without regard to section 931) for such period, or for such part thereof, was derived from the active conduct within the Commonwealth of Puerto Rico or a possession of the United States of any trades or businesses constituting the manufacture or processing of goods, wares, merchandise, or other tangible personal property; the processing of agricultural or horticultural products or commodities (including but not limited to livestock, poultry, or furbearing animals); the catching or taking of any kind of fish or the mining or extraction of natural resources, or any manufacturing or processing of any products or commodities obtained from such activities; or the ownership or operation of hotels. For purposes of paragraphs (1) and (2), the determination as to whether income was derived from sources within the Commonwealth of Puerto Rico or a possession of the United States and was derived from the active conduct of a described trade or business within the Commonwealth of Puerto Rico or a possession of the United States shall be made under regulations prescribed by the Secretary or his delegate.

“(d) UNITED STATES PERSON.—For purposes of this subpart, the term “United States person” has the meaning assigned to it by section 7701(a) (30) except that—

“(1) with respect to a corporation organized under the laws of the Commonwealth of Puerto Rico, such term does not include an individual who is a bona fide resident of Puerto Rico, if a dividend received by such individual during the taxable year from such corporation would, for purposes of section 933(1), be treated as income derived from sources within Puerto Rico,

“(2) with respect to a corporation organized under the laws of the Virgin Islands,

such term does not include an individual who is a bona fide resident of the Virgin Islands and whose income tax obligation under this subtitle for the taxable year is satisfied pursuant to section 28(a) of the Revised Organic Act of the Virgin Islands, approved July 22, 1954 (48 U.S.C. 1642), by paying tax on income derived from all sources both within and outside the Virgin Islands into the treasury of the Virgin Islands, and

“(3) with respect to a corporation organized under the laws of any other possession of the United States, such term does not include an individual who is a bona fide resident of any such other possession and whose income derived from sources within possessions of the United States is not, by reason of section 931(a), includible in gross income under this subtitle for the taxable year.

“Sec. 958. Rules for determining stock ownership.

“(a) DIRECT AND INDIRECT OWNERSHIP.—

“(1) GENERAL RULE.—For purposes of this subpart (other than sections 955(b) (1) (A) and (B), 955(c) (2) (A) (ii), and 960(a) (1)), stock owned means—

“(A) stock owned directly, and

“(B) stock owned with the application of paragraph (2).

“(2) STOCK OWNERSHIP THROUGH FOREIGN ENTITIES.—For purposes of subparagraph (B) of paragraph (1), stock owned, directly or indirectly, by or for a foreign corporation, foreign partnership, or foreign trust or foreign estate (within the meaning of section 7701(a) (31)) shall be considered as being owned proportionately by its shareholders, partners, or beneficiaries. Stock considered to be owned by a person by reason of the application of the preceding sentence shall, for purposes of applying such sentence, be treated as actually owned by such person.

“(3) SPECIAL RULE FOR MUTUAL INSURANCE COMPANIES.—For purposes of applying paragraph (1) in the case of a foreign mutual insurance company, the term “stock” shall include any certificate entitling the holder to voting power in the corporation.

“(b) CONSTRUCTIVE OWNERSHIP.—For purposes of sections 951(b), 954(d) (3), and 957, section 318(a) (relating to constructive ownership of stock) shall apply to the extent that the effect is to treat any United States person as a United States shareholder within the meaning of section 951(b), to treat a person as a related person within the meaning of section 954(d) (3), or to treat a foreign corporation as a controlled foreign corporation under section 957, except that—

“(1) In applying paragraph (1) (A) of section 318(a), stock owned by a nonresident alien individual (other than a foreign trust or foreign estate) shall not be considered as owned by a citizen or by a resident alien individual.

“(2) In applying the first sentence of subparagraphs (A) and (B), and in applying clause (i) of subparagraph (C), of section 318(a) (2), if a partnership, estate, trust, or corporation owns, directly or indirectly, more than 50 percent of the total combined voting power of all classes of stock entitled to vote of a corporation, it shall be considered as owning all the stock entitled to vote.

“(3) Stock owned by a partnership, estate, trust, or corporation, by reason of the application of the second sentence of subparagraphs (A) and (B), and the application of clause (ii) of subparagraph (C), of section 318(a) (2), shall not be considered as owned by such partnership, estate, trust, or corporation, for purposes of applying the first sentence of subparagraphs (A) and (B), and in applying clause (i) of subparagraph (C), of section 318(a) (2).

“(4) In applying clause (i) of subparagraph (C) of section 318(a) (2), the phrase “10 percent” shall be substituted for the

phrase “50 percent” used in subparagraph (C).

“(5) The second sentence of subparagraphs (A) and (B), and clause (ii) of subparagraph (C), of section 318(a) (2) shall not be applied so as to consider a United States person as owning stock which is owned by a person who is not a United States person.

“Sec. 959. Exclusion from gross income of previously taxed earnings and profits.

“(a) EXCLUSION FROM GROSS INCOME OF UNITED STATES PERSONS.—For purposes of this chapter, the earnings and profits for a taxable year of a foreign corporation attributable to amounts which are, or have been, included in the gross income of a United States shareholder under section 951(a) shall not, when—

“(1) such amounts are distributed to, or

“(2) such amounts would, but for this subsection, be included under section 951(a) (1) (B) in the gross income of,

such shareholder (or any other United States person who acquires from any person any portion of the interest of such United States shareholder in such foreign corporation, but only to the extent of such portion, and subject to such proof of the identity of such interest as the Secretary or his delegate may by regulations prescribe) directly, or indirectly through a chain of ownership described under section 958(a), be again included in the gross income of such United States shareholder (or of such other United States person).

“(b) EXCLUSION FROM GROSS INCOME OF CERTAIN FOREIGN SUBSIDIARIES.—For purposes of section 951(a), the earnings and profits for a taxable year of a controlled foreign corporation attributable to amounts which are, or have been, included in the gross income of a United States shareholder under section 951(a), shall not, when distributed through a chain of ownership described under section 958(a), be also included in the gross income of another controlled foreign corporation in such chain for purposes of the application of section 951(a) to such other controlled foreign corporation with respect to such United States shareholder (or to any other United States shareholder who acquires from any person any portion of the interest of such United States shareholder in the controlled foreign corporation, but only to the extent of such portion, and subject to such proof of identity of such interest as the Secretary or his delegate may prescribe by regulations).

“(c) ALLOCATION OF DISTRIBUTIONS.—For purposes of subsections (a) and (b), section 318(a) shall be applied by applying paragraph (2) thereof, and then paragraph (1) thereof—

“(1) first to earnings and profits attributable to amounts included in gross income under section 951(a) (1) (B) (or which would have been included except for subsection (a) (2) of this section),

“(2) then to earnings and profits attributable to amounts included in gross income under section 951(a) (1) (A) (but reduced by amounts not included under section 951(a) (1) (B) because of the exclusion in subsection (a) (2) of this section), and

“(3) then to other earnings and profits.

“(d) DISTRIBUTIONS EXCLUDED FROM GROSS INCOME NOT TO BE TREATED AS DIVIDENDS.—Except as provided in section 960(a) (3), any distribution excluded from gross income under subsection (a) shall be treated, for purposes of this chapter, as a distribution which is not a dividend.

“Sec. 960. Special rules for foreign tax credit.

“(a) TAXES PAID BY A FOREIGN CORPORATION.—

"(1) GENERAL RULE.—For purposes of subpart A of this part, if there is included, under section 951(a), in the gross income of a domestic corporation any amount attributable to earnings and profits—

"(A) of a foreign corporation at least 10 percent of the voting stock of which is owned by such domestic corporation, or

"(B) of a foreign corporation at least 50 percent of the voting stock of which is owned by a foreign corporation at least 10 percent of the voting stock of which is in turn owned by such domestic corporation,

then, under regulations prescribed by the Secretary or his delegate, such domestic corporation shall be deemed to have paid the same proportion of the total income, war profits, and excess profits taxes paid (or deemed paid) by such foreign corporation to a foreign country or possession of the United States for the taxable year on or with respect to the earnings and profits of such foreign corporation which the amount of earnings and profits of such foreign corporation so included in gross income of the domestic corporation bears to—

"(C) if the foreign corporation at least 10 percent of the voting stock of which is owned by such domestic corporation referred to in subparagraph (A) or (B) is not a less developed country corporation (as defined in section 902(d)) for such taxable year, the entire amount of the earnings and profits of such foreign corporation for such taxable year, or

"(D) if the foreign corporation at least 10 percent of the voting stock of which is owned by such domestic corporation referred to in subparagraph (A) or (B) is a less developed country corporation (as defined in section 902(d)) for such taxable year, the sum of the entire amount of the earnings and profits of such foreign corporation for such taxable year and the total income, war profits, and excess profits taxes paid by such foreign corporation to foreign countries or possessions of the United States for such taxable year.

"(2) TAXES PREVIOUSLY DEEMED PAID BY DOMESTIC CORPORATION.—If a domestic corporation receives a distribution from a foreign corporation, any portion of which is excluded from gross income under section 959, the income, war profits, and excess profits taxes paid or deemed paid by such foreign corporation to any foreign country or to any possession of the United States in connection with the earnings and profits of such foreign corporation from which such distribution is made shall not be taken into account for purposes of section 902, to the extent such taxes were deemed paid by a domestic corporation under paragraph (1) for any prior taxable year.

"(3) TAXES PAID BY FOREIGN CORPORATION AND NOT PREVIOUSLY DEEMED PAID BY DOMESTIC CORPORATION.—Any portion of a distribution from a foreign corporation received by a domestic corporation which is excluded from gross income under section 959(a) shall be treated by the domestic corporation as a dividend, solely for purposes of taking into account under section 902 any income, war profits, or excess profits taxes paid to any foreign country or to any possession of the United States, on or with respect to the accumulated profits of such foreign corporation from which such distribution is made, which were not deemed paid by the domestic corporation under paragraph (1) for any prior taxable year.

"(b) SPECIAL RULES FOR FOREIGN TAX CREDIT IN YEAR OF RECEIPT OF PREVIOUSLY TAXED EARNINGS AND PROFITS.—

"(1) INCREASE IN SECTION 904 LIMITATION.—In the case of any taxpayer who—

"(A) either (i) chose to have the benefits of subpart A of this part for a taxable year in which he was required under section 951(a) to include in his gross income an amount in respect of a controlled foreign corpora-

tion, or (ii) did not pay or accrue for such taxable year any income, war profits, or excess profits taxes to any foreign country or to any possession of the United States, and

"(B) chooses to have the benefits of subpart A of this part for the taxable year in which he receives a distribution or amount which is excluded from gross income under section 959(a) and which is attributable to earnings and profits of the controlled foreign corporation which was included in his gross income for the taxable year referred to in subparagraph (A), and

"(C) for the taxable year in which such distribution or amount is received, pays, or is deemed to have paid, or accrues income, war profits, or excess profits taxes to a foreign country or to any possession of the United States with respect to such distribution or amount.

the applicable limitation under section 904 for the taxable year in which such distribution or amount is received shall be increased as provided in paragraph (2), but such increase shall not exceed the amount of such taxes paid, or deemed paid, or accrued with respect to such distribution or amount.

"(2) AMOUNT OF INCREASE.—The amount of increase of the applicable limitation under section 904(a) for the taxable year in which the distribution or amount referred to in paragraph (1)(B) is received shall be an amount equal to—

"(A) the amount by which the applicable limitation under section 904(a) for the taxable year referred to in paragraph (1)(A) was increased by reason of the inclusion in gross income under section 951(a) of the amount in respect of the controlled foreign corporation, reduced by

"(B) the amount of any income, war profits, and excess profits taxes paid, or deemed paid, or accrued to any foreign country or possession of the United States which were allowable as a credit under section 901 for the taxable year referred to in paragraph (1)(A) and which would not have been allowable but for the inclusion in gross income of the amount described in subparagraph (A).

"(3) CASES IN WHICH TAXES NOT TO BE ALLOWED AS DEDUCTION.—In the case of any taxpayer who—

"(A) chose to have the benefits of subpart A of this part for a taxable year in which he was required under section 951(a) to include in his gross income an amount in respect of a controlled foreign corporation, and

"(B) does not choose to have the benefits of subpart A of this part for the taxable year in which he receives a distribution or amount which is excluded from gross income under section 959(a) and which is attributable to earnings and profits of the controlled foreign corporation which was included in his gross income for the taxable year referred to in subparagraph (A),

no deduction shall be allowed under section 164 for the taxable year in which such distribution or amount is received for any income, war profits, or excess profits taxes paid or accrued to any foreign country or to any possession of the United States on or with respect to such distribution or amount.

"(4) INSUFFICIENT TAXABLE INCOME.—If an increase in the limitation under this subsection exceeds the tax imposed by this chapter for such year, the amount of such excess shall be deemed an overpayment of tax for such year.

"Sec. 961. Adjustments to basis of stock in controlled foreign corporation and of other property.

"(a) INCREASE IN BASIS.—Under regulations prescribed by the Secretary or his delegate, the basis of a United States shareholder's stock in a controlled foreign corporation, and the basis of property of a United States shareholder by reason of which he is consid-

ered under section 958(a)(2) as owning stock of a controlled foreign corporation, shall be increased by the amount required to be included in his gross income under section 951(a) with respect to such stock or with respect to such property, as the case may be, but only to the extent to which such amount was included in the gross income of such United States shareholder. In the case of a United States shareholder who has made an election under section 962 for the taxable year, the increase in basis provided by this subsection shall not exceed an amount equal to the amount of tax paid under this chapter with respect to the amounts required to be included in his gross income under section 951(a).

"(b) REDUCTION IN BASIS.—

"(1) IN GENERAL.—Under regulations prescribed by the Secretary or his delegate, the adjusted basis of stock or other property with respect to which a United States shareholder or a United States person receives an amount which is excluded from gross income under section 959(a) shall be reduced by the amount so excluded. In the case of a United States shareholder who has made an election under section 962 for any prior taxable year, the reduction in basis provided by this paragraph shall not exceed an amount equal to the amount received which is excluded from gross income under section 959(a) after the application of section 962(d).

"(2) AMOUNT IN EXCESS OF BASIS.—To the extent that an amount excluded from gross income under section 959(a) exceeds the adjusted basis of the stock or other property with respect to which it is received, the amount shall be treated as gain from the sale or exchange of property.

"Sec. 962. Election by individuals to be subject to tax at corporate rates.

"(a) GENERAL RULE.—Under regulations prescribed by the Secretary or his delegate, in the case of a United States shareholder who is an individual and who elects to have the provisions of this section apply for the taxable year—

"(1) the tax imposed under this chapter on amounts which are included in his gross income under section 951(a) shall (in lieu of the tax determined under section 1) be an amount equal to the tax which would be imposed under section 11 if such amounts were received by a domestic corporation, and

"(2) for purposes of applying the provisions of section 960 (relating to foreign tax credit) such amounts shall be treated as if they were received by a domestic corporation.

"(b) ELECTION.—An election to have the provisions of this section apply for any taxable year shall be made by a United States shareholder at such time and in such manner as the Secretary or his delegate shall prescribe by regulations. An election made for any taxable year may not be revoked except with the consent of the Secretary or his delegate.

"(c) SURTAX EXEMPTION.—For purposes of applying subsection (a)(1), the surtax exemption provided by section 11(c) shall not exceed, in the case of any United States shareholder, an amount which bears the same ratio to \$25,000 as the amounts included in his gross income under section 951(a) for the taxable years bears to his pro rata share of the earnings and profits for the taxable year of all controlled foreign corporations with respect to which such United States shareholder includes any amount in gross income under section 951(a).

"(d) SPECIAL RULE FOR ACTUAL DISTRIBUTIONS.—The earnings and profits of a foreign corporation attributable to amounts which were included in the gross income of a United States shareholder under section 951(a) and with respect to which an election under this section applied shall, when such

earnings and profits are distributed, notwithstanding the provisions of section 959(a)(1), be included in gross income to the extent that such earnings and profits so distributed exceed the amount of tax paid under this chapter on the amounts to which such election applied.

"Sec. 963. Receipt of minimum distributions by domestic corporations.

"(a) GENERAL RULE.—In the case of a United States shareholder which is a domestic corporation and which consents to all the regulations prescribed by the Secretary or his delegate under this section prior to the last day prescribed by law for filing its return of the tax imposed by this chapter for the taxable year, no amount shall be included in gross income under section 951(a)(1)(A)(i) for the taxable year with respect to the subpart F income of a controlled foreign corporation, if—

"(1) in the case of a controlled foreign corporation described in subsection (c)(1), the United States shareholder receives a minimum distribution of the earnings and profits for the taxable year of such controlled foreign corporation;

"(2) in the case of controlled foreign corporations described in subsection (c)(2), the United States shareholder receives a minimum distribution with respect to the consolidated earnings and profits for the taxable year of all such controlled foreign corporations; or

"(3) in the case of controlled foreign corporations described in subsection (c)(3), the United States shareholder receives a minimum distribution of the consolidated earnings and profits for the taxable year of all such controlled foreign corporations.

"(b) MINIMUM DISTRIBUTIONS.—For purposes of this section, a minimum distribution with respect to the earnings and profits for the taxable year of any controlled foreign corporation or corporations shall, in the case of any United States shareholder, be its pro rata share of an amount determined in accordance with the following table:

If the effective foreign tax rate is (percentage):	The required minimum distribution of earnings and profits is (percentage):
Under 10-----	90
10 or over but less than 20-----	80
20 or over but less than 30-----	70
30 or over but less than 40-----	60
40 or over but less than 42-----	50
42 or over but less than 44-----	38
44 or over but less than 46-----	26
46 or over but not more than 47-----	14
Over 47-----	0

"(c) AMOUNTS TO WHICH SECTION APPLIES.—

"(1) FOREIGN SUBSIDIARIES.—Subsection (a)(1) shall apply to amounts which (but for the provisions of this section) would be included in the gross income of the United States shareholder under section 951(a)(1)(A)(i) by reason of its ownership, within the meaning of section 958(a)(1)(A), of stock of a controlled foreign corporation.

"(2) CHAIN OF CONTROLLED FOREIGN CORPORATIONS.—Subsection (a)(2) shall apply to amounts which (but for the provisions of this section) would be included in the gross income of the United States shareholder under section 951(a)(1)(A)(i) —

"(A) by reason of its ownership, within the meaning of section 958(a)(1)(A), of stock of a controlled foreign corporation, and

"(B) to the extent that the United States shareholder so elects, by reason of its ownership, within the meaning of section 958(a)(2), of stock of any other controlled foreign corporation (on account of its ownership of the stock described in subparagraph (A) or of stock described in this subparagraph), but only if there is taken into account the earnings and profits of such foreign corpora-

tion, whether or not a controlled foreign corporation, by reason of which the United States shareholder owns, within the meaning of section 958(a)(2), stock of such controlled foreign corporation.

"(3) ALL CONTROLLED FOREIGN CORPORATIONS.—Except as provided in paragraph (4), subsection (a)(3) shall apply to amounts which (but for the provisions of this section) would be included in the gross income of the United States shareholder under section 951(a)(1)(A)(i) —

"(A) by reason of its ownership, within the meaning of section 958(a)(1)(A), of stock of all controlled foreign corporations in which it owns stock within the meaning of such section, and

"(B) by reason of its ownership, within the meaning of section 958(a)(2), of stock of all controlled foreign corporations in which it owns stock within the meaning of such section, but only if there is taken into account the earnings and profits of each foreign corporation, whether or not a controlled foreign corporation, by reason of which the United States shareholder owns, within the meaning of section 958(a), stock of any of such controlled foreign corporations.

"(4) EXCEPTIONS AND SPECIAL RULES.—

"(A) LESS DEVELOPED COUNTRY CORPORATIONS.—If the United States shareholder so elects, subsection (a)(3) and paragraph (3) of this subsection shall not apply to amounts which would be included in the gross income of such shareholder under section 951(a)(1)(A)(i) by reason of its ownership, within the meaning of section 958(a), of stock of controlled foreign corporations which are less developed country corporations (as defined in section 955(c)). This subparagraph shall not apply with respect to a less developed country corporation if, by reason of the ownership of the stock of such corporation, the United States shareholder owns, within the meaning of section 958(a)(2), stock of any other controlled foreign corporation which is not a less developed country corporation. Except as provided in the preceding sentence, an election under this subparagraph may be made only with respect to all controlled foreign corporations which are less developed country corporations and with respect to which the domestic corporation making the election is a United States shareholder.

"(B) FOREIGN BRANCHES.—In applying subsection (a)(3) and paragraph (3) of this subsection, if a United States shareholder so elects, all branches maintained by such shareholder in foreign countries, the Commonwealth of Puerto Rico, or possessions of the United States shall, under regulations prescribed by the Secretary or his delegate, be treated as wholly owned subsidiary corporations of such shareholder organized under the laws of such foreign countries, the Commonwealth of Puerto Rico, or possessions of the United States, as the case may be. Each branch so treated shall, for purposes of this section, be considered to have distributed to the United States shareholder all of its earnings and profits for the taxable year. This subparagraph shall not apply to a branch maintained by a United States shareholder in the Commonwealth of Puerto Rico or a possession of the United States unless—

"(i) such branch would be a controlled foreign corporation (as defined in section 957) if it were incorporated under the laws of the Commonwealth of Puerto Rico or the possession of the United States, as the case may be, and

"(ii) the gross income of the United States shareholder for the taxable year includes income derived from sources within the Commonwealth of Puerto Rico and possessions of the United States.

"(C) BLOCKED FOREIGN INCOME.—If a United States shareholder so elects, the provisions of subsection (a)(3) and of paragraph (3) of this subsection shall not apply

with respect to any foreign corporation, if it is established to the satisfaction of the Secretary or his delegate that the earnings and profits of such foreign corporation could not have been distributed to United States shareholders who own (within the meaning of section 958(a)) stock of such foreign corporation because of currency or other restrictions or limitations imposed under the laws of any foreign country.

"(d) EFFECTIVE FOREIGN TAX RATE.—For purposes of this section, the term "effective foreign tax rate" means—

"(1) with respect to a single controlled foreign corporation, the percentage which—

"(A) the income, war profits, or excess profits taxes paid or accrued to foreign countries or possessions of the United States by the controlled foreign corporation for the taxable year on or with respect to its earnings and profits for the taxable year, is of

"(B) the sum of (i) the earnings and profits of the controlled foreign corporation described in subparagraph (A) and (ii) and the taxes described in subparagraph (A); and

"(2) with respect to two or more foreign corporations, the percentage which—

"(A) the total income, war profits, or excess profits taxes paid or accrued to foreign countries or possessions of the United States by such foreign corporations for the taxable year on or with respect to the total earnings and profits of such foreign corporations for the taxable year, is of

"(B) the sum of (i) the total earnings and profits of such foreign corporations described in subparagraph (A) and (ii) the taxes described in subparagraph (A).

For purposes of the preceding sentence, in the case of any United States shareholder, the computation of the effective foreign tax rate applicable with respect to any controlled foreign corporation or corporations shall be made without regard to distributions made by such controlled foreign corporation or corporations to such United States shareholder.

"(e) SPECIAL RULES.—

"(1) YEAR FROM WHICH DISTRIBUTIONS ARE MADE.—For purposes of this section, the second sentence of section 902(c)(1) shall apply in determining from the earnings and profits of what year distributions are made by any foreign corporation, except that the Secretary or his delegate may by regulations provide a period in excess of 60 days in lieu of the 60-day period prescribed in such section.

"(2) INSUFFICIENT DISTRIBUTIONS.—If—

"(A) a United States shareholder, in making its return of the tax imposed by this chapter for any taxable year, applies the provisions of this section with respect to any controlled foreign corporation,

"(B) it is subsequently determined that this section did not apply with respect to such controlled foreign corporation for such taxable year due to the failure of the United States shareholder to receive a minimum distribution with respect to such controlled foreign corporation, and

"(C) such failure is due to reasonable cause, then a subsequent distribution made with respect to such controlled foreign corporation may, if made at a time and in a manner prescribed by the Secretary or his delegate by regulations, be treated, for purposes of this chapter, as having been made for, and received in, the taxable year of the United States shareholder for which such shareholder applied the provisions of this section.

"(3) AFFILIATED GROUPS OF CORPORATIONS.—An affiliated group of corporations which is eligible to make a consolidated return under section 1501 for the taxable year, may, if it so elects, be treated as a single United States shareholder for purposes of applying this section for the taxable year.

"(f) REGULATIONS.—The Secretary or his delegate shall prescribe such regulations as he may deem necessary to carry out the provisions of this section, including regulations for the determination of the amount of foreign tax credit in the case of distributions with respect to the earnings and profits of two or more foreign corporations.

"Sec. 964. Miscellaneous provisions.

"(a) EARNINGS AND PROFITS.—For purposes of this subpart, the earnings and profits of any foreign corporation, and the deficit in earnings and profits of any foreign corporation, for any taxable year shall be determined according to rules substantially similar to those applicable to domestic corporations, under regulations prescribed by the Secretary or his delegate.

"(b) BLOCKED FOREIGN INCOME.—Under regulations prescribed by the Secretary or his delegate, no part of the earnings and profits of a controlled foreign corporation for any taxable year shall be included in earnings and profits for purposes of sections 952, 955, and 956, if it is established to the satisfaction of the Secretary or his delegate that such part could not have been distributed by the controlled foreign corporation to United States shareholders who own (within the meaning of section 958(a)) stock of such controlled foreign corporation because of currency or other restrictions or limitations imposed under the laws of any foreign country.

"(c) RECORDS AND ACCOUNTS OF UNITED STATES SHAREHOLDERS.—

"(1) RECORDS AND ACCOUNTS TO BE MAINTAINED.—The Secretary or his delegate may by regulations require each person who is, or has been, a United States shareholder of a controlled foreign corporation to maintain such records and accounts as may be prescribed by such regulations as necessary to carry out the provisions of this subpart and subpart G.

"(2) TWO OR MORE PERSONS REQUIRED TO MAINTAIN OR FURNISH THE SAME RECORDS AND ACCOUNTS WITH RESPECT TO THE SAME FOREIGN CORPORATION.—Where, but for this paragraph, two or more United States persons would be required to maintain or furnish the same records and accounts as may be required by regulations under paragraph (1) with respect to the same controlled foreign corporation for the same period, the Secretary or his delegate may by regulations provide that the maintenance or furnishing of such records and accounts by only one such person shall satisfy the requirements of paragraph (1) for such other persons.

"Subpart G—Export Trade Corporations
"Sec. 970. Reduction of subpart F income of export trade corporations.

"Sec. 971. Definitions.

"Sec. 972. Consolidation of group of export trade corporations.

"Sec. 970. Reduction of subpart F income of export trade corporations.

"(a) EXPORT TRADE INCOME CONSTITUTING FOREIGN BASE COMPANY INCOME.—

"(1) IN GENERAL.—In the case of a controlled foreign corporation (as defined in section 957) which for the taxable year is an export trade corporation, the subpart F income (determined without regard to this subpart) of such corporation for such year shall be reduced by an amount equal to so much of the export trade income (as defined in section 971(b)) of such corporation for such year as constitutes foreign base company income (as defined in section 954), but only to the extent that such amount does not exceed whichever of the following amounts is the lesser:

"(A) an amount equal to $1\frac{1}{2}$ times so much of the export promotion expenses (as defined in section 971(d)) of such corporation for such year as is properly allocable to the export trade income which constitutes foreign base company income of such corporation for such year, or

"(B) an amount equal to 10 percent of so much of the gross receipts for such year (or, in the case of gross receipts arising from commissions, fees, or other compensation for its services, so much of the gross amount upon the basis of which such commissions, fees, or other compensation is computed) accruing to such export trade corporation from the sale, installation, operation, maintenance, or use of property in respect of which such corporation derives export trade income as is properly allocable to the export trade income which constitutes foreign base company income of such corporation for such year.

The allocations with respect to export trade income which constitutes foreign base company income under subparagraphs (A) and (B) shall be made under regulations prescribed by the Secretary or his delegate.

"(2) OVERALL LIMITATION.—The reduction under paragraph (1) for any taxable year shall not exceed an amount which bears the same ratio to the increase in the investments in export trade assets (as defined in section 971(c)) of such corporation for such year as the export trade income which constitutes foreign base company income of such corporation for such year bears to the entire export trade income of such corporation for such year.

"(b) INCLUSION OF CERTAIN PREVIOUSLY EXCLUDED AMOUNTS.—Each United States shareholder of a controlled foreign corporation which for any prior taxable year was an export trade corporation shall include in his gross income under section 951(a)(1)(A) (ii), as an amount to which section 955 (relating to withdrawal of previously excluded subpart F income from qualified investment) applies, his pro rata share of the amount of decrease in the investments in export trade assets of such corporation for such year, but only to the extent that his pro rata share of such amount does not exceed an amount equal to—

"(1) his pro rata share of the sum of (A) the amounts by which the subpart F income of such corporation was reduced for all prior taxable years under subsection (a), and (B) the amounts not included in subpart F income (determined without regard to this subpart) for all prior taxable years by reason of the application of section 972, reduced by

"(2) the sum of the amounts which were included in his gross income under section 951(a)(1)(A)(ii) under the provisions of this subsection for all prior taxable years.

"(c) INVESTMENTS IN EXPORT TRADE ASSETS.—

"(1) AMOUNT OF INVESTMENTS.—For purposes of this section, the amount taken into account with respect to any export trade asset shall be its adjusted basis, reduced by any liability to which the asset is subject.

"(2) INCREASE IN INVESTMENTS IN EXPORT TRADE ASSETS.—For purposes of subsection (a), the amount of increase in investments in export trade assets of any controlled foreign corporation for any taxable year is the amount by which—

"(A) the amount of such investments at the close of the taxable year, exceeds

"(B) the amount of such investments at the close of the preceding taxable year.

"(3) DECREASE IN INVESTMENTS IN EXPORT TRADE ASSETS.—For purposes of subsection (b), the amount of decrease in investments in export trade assets of any controlled foreign corporation for any taxable year is the amount by which—

"(A) the amount of such investments at the close of the preceding taxable year (reduced by an amount equal to the amount of net loss sustained during the taxable year with respect to export trade assets), exceeds

"(B) the amount of such investments at the close of the taxable year.

"(4) SPECIAL RULE.—A United States shareholder of an export trade corporation may, under regulations prescribed by the

Secretary or his delegate, make the determinations under paragraphs (2) and (3) as of the close of the 75th day after the close of the years referred to in such paragraphs in lieu of on the last day of such years. An election under this paragraph made with respect to any taxable year shall apply to such year and to all succeeding taxable years unless the Secretary or his delegate consents to the revocation of such election.

"Sec. 971. Definitions.

"(a) EXPORT TRADE CORPORATION.—For purposes of this subpart, the term 'export trade corporation' means—

"(1) IN GENERAL.—A controlled foreign corporation (as defined in section 957) which satisfies the following conditions:

"(A) 90 percent or more of the gross income of such corporation for the 3-year period immediately preceding the close of the taxable year (or such part of such period subsequent to the effective date of this subpart during which the corporation was in existence) was derived from sources without the United States, and

"(B) 75 percent or more of the gross income of such corporation for such period constituted gross income in respect of which such corporation derived export trade income.

"(2) SPECIAL RULE.—If 50 percent or more of the gross income of a controlled foreign corporation in the period specified in subsection (a)(1)(A) is gross income in respect of which such corporation derived export trade income in respect of agricultural products grown in the United States, it may qualify as an export trade corporation although it does not meet the requirements of subsection (a)(1)(B).

"(b) EXPORT TRADE INCOME.—For the purposes of this subpart, the term "export trade income" means net income from—

"(1) the sale to an unrelated person for use, consumption, or disposition outside the United States of export property (as defined in subsection (e)), or from commissions, fees, compensation, or other income from the performance of commercial, industrial, financial, technical, scientific, managerial, engineering, architectural, skilled, or other services in respect of such sales or in respect of the installation or maintenance of such export property;

"(2) commissions, fees, compensation, or other income from commercial, industrial, financial, technical, scientific, managerial, engineering, architectural, skilled, or other services performed in connection with the use by an unrelated person outside the United States of patents copyrights, secret processes and formulas, goodwill, trademarks, trade brands, franchises, and other like property acquired or developed and owned by the manufacturer, producer, grower, or extractor of export property in respect of which the export trade corporation earns export trade income under paragraph (1);

"(3) commissions, fees, rentals, or other compensation or income attributable to the use of export property by an unrelated person or attributable to the use of export property in the rendition of technical, scientific, or engineering services to an unrelated person; and

"(4) interest from export trade assets described in subsection (c)(4).

For purposes of paragraph (3), if a controlled foreign corporation receives income from an unrelated person attributable to the use of export property in the rendition of services to such unrelated person together with income attributable to the rendition of other services to such unrelated person, including personal services, the amount of such aggregate income which shall be considered to be attributable to the use of the export property shall (if such amount cannot be established by reference to transactions between unrelated persons) be that part of such

aggregate income which the cost of the export property consumed in the rendition of such services (including a reasonable allowance for depreciation) bears to the total costs and expenses attributable to such aggregate income.

“(c) EXPORT TRADE ASSETS.—For purposes of this subpart, the term “export trade assets” means—

“(1) working capital reasonably necessary for the production of export trade income,

“(2) inventory of export property held for use, consumption, or disposition outside the United States,

“(3) facilities located outside the United States for the storage, handling, transportation, packaging, or servicing of export property, and

“(4) evidences of indebtedness executed by persons, other than related persons, in connection with payment for purchases of export property for use, consumption, or disposition outside the United States, or in connection with the payment for services described in subsections (b) (2) and (3).

“(d) EXPORT PROMOTION EXPENSES.—For purposes of this subpart, the term “export promotion expenses” means the following expenses paid or incurred in the receipt or production of export trade income—

“(1) a reasonable allowance for salaries or other compensation for personal services actually rendered for such purpose,

“(2) rentals or other payments for the use of property actually used for such purpose,

“(3) a reasonable allowance for the exhaustion, wear and tear, or obsolescence of property actually used for such purpose, and

“(4) any other ordinary and necessary expenses of the corporation to the extent reasonably allocable to the receipt or production of export trade income.

No expense incurred within the United States shall be treated as an export promotion expense within the meaning of the preceding sentence, unless at least 90 percent of each category of expenses described in such sentence is incurred outside the United States.

“(e) EXPORT PROPERTY.—For purposes of this subpart, the term “export property” means any property or any interest in property manufactured, produced, grown, or extracted in the United States.

“(f) UNRELATED PERSON.—For purposes of this subpart, the term “unrelated person” means a person other than a related person as defined in section 954(d) (3).

“Sec. 972. Consolidation of group of export trade corporations.

“For purposes of this subpart and subpart F of this part, a United States shareholder of a controlled foreign corporation which is an export trade corporation may, under regulations prescribed by the Secretary or his delegate, treat as a single controlled foreign corporation—

“(1) such controlled foreign corporation,

“(2) all controlled foreign corporations which are export trade corporations and 80 percent or more of the total combined voting power of all classes of stock entitled to vote of which is owned by such controlled foreign corporation; and

“(3) all controlled foreign corporations which are export trade corporations and 80 percent or more of the total combined voting power of all classes of stock entitled to vote of which is owned by controlled foreign corporations described in paragraph (2).’

“(b) TECHNICAL AND CLERICAL AMENDMENTS.—

“(1) Section 901 (relating to foreign tax credit) is amended by striking out ‘section 902’ and inserting in lieu thereof ‘sections 902 and 960’.

“(2) Section 904(g) (as redesignated by section 10(a) of this Act) is amended to read as follows:

“(g) CROSS REFERENCES.—

“(1) For increase of applicable limitation under subsection (a) for taxes paid with respect to amounts received which were included in the gross income of the taxpayer for a prior taxable year as a United States shareholder with respect to a controlled foreign corporation, see section 960(b).

“(2) For special rule relating to the application of the credit provided by section 901 in the case of affiliated groups which include Western Hemisphere trade corporations for years in which the limitation provided by subsection (a) (2) applies, see section 1503(d).’

“(3) The table of subparts for part III of subchapter N of chapter 1 is amended by adding at the end thereof the following:

“Subpart F. Controlled foreign corporations.

“Subpart G. Export trade corporations.’

“(4) Section 1016(a) (relating to adjustments to basis) is amended by adding after paragraph (19) (as added by section 2(f) of this Act) the following new paragraph:

“(20) to the extent provided in section 961 in the case of stock in controlled foreign corporations (or foreign corporations which were controlled foreign corporations) and of property by reason of which a person is considered as owning such stock.’

“(c) EFFECTIVE DATE.—The amendments made by this section shall apply with respect to taxable years of foreign corporations beginning after December 31, 1962, and to taxable years of United States shareholders within which or with which such taxable years of such foreign corporations end.”

On page 246, line 1, to change the section number from “14” to “13”.

On page 246, line 13, after the word “of” where it occurs the first time, to strike out “after the date of the enactment of the Revenue Act of 1962” and insert “during a taxable year beginning after December 31, 1962”.

On page 247, line 4, after the word “adjustments”, to strike out “for taxable years beginning” and insert “attributable to periods”; in line 13, after the word “any” to strike out “taxable year” and insert “period”, in line 15, after the word “such”, to strike out “taxable year” and insert “period”.

On page 251, line 18, after the word “may”, to strike out “within such period after the date of the enactment of the Revenue Act of 1962” and insert “on or before the last day prescribed by law (including extensions thereof) for filing his return for his first taxable year beginning after December 31, 1962”.

At the top of page 254, to insert:

“(e) COMPUTATION OF TAXABLE INCOME FOR PURPOSES OF LIMITATION ON PERCENTAGE DEPLETION DEDUCTION.—Section 613(a) (relating to percentage depletion) is amended by inserting after the second sentence thereof the following new sentence: ‘For purposes of the preceding sentence, the allowable deductions taken into account with respect to expenses of mining in computing the taxable income from the property shall be decreased by an amount equal to so much of any gain which (1) is treated under section 1245 (relating to gain from disposition of certain depreciable property) as gain from the sale or exchange of property which is neither a capital asset nor property described in section 1231, and (2) is properly allocable to the property.’”

On page 254, at the beginning of line 15, to strike out “(e)” and insert “(f)”; on page 256, after line 23, to strike out:

“(f) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 1961, and ending after the date of the enactment of this Act.”

And, in lieu thereof, to insert:

“(g) EFFECTIVE DATES.—The amendments made by this section (other than the amendments made by subsection (c)) shall apply

to taxable years beginning after December 31, 1962. The amendments made by subsection (c) shall apply to taxable years beginning after December 31, 1961, and ending after the date of the enactment of this Act.”

On page 257, at the beginning of line 9, to change the section number from “15” to “14”; in line 15, after the word “section”, where it appears the second time, to strike out “14” and insert “13”; in line 21, after the word “exchange”, to insert “(or a distribution which, under section 302 or 331, is treated as an exchange of stock)”; on page 268, after line 14, to strike out:

“(B) excluding such earnings and profits which were taxed to such taxpayer under section 951 or under section 551.”

And, in lieu thereof, to insert:

“(B) excluding such earnings and profits attributable to any amount previously included in the gross income of such taxpayer under section 951 (but only to the extent the inclusion of such amount did not result in an exclusion of any other amount from gross income under section 959).”

On page 259, line 14, after the word “corporation” to insert “which, for any taxable year beginning after December 31, 1962, is—”.

In line 24, after the word “Act”, to insert “as limited by paragraphs (2) through (10) (except paragraph (6)(C) and paragraphs (12) through (15) of section 3(c) of such Act)”, and on page 260, line 6, after the word “section” to strike out “955” and insert “958”.

On page 261, line 16, after the word “the” where it occurs the second time, to strike out “accumulated earnings and profits of such company” and insert “earnings and profits of such company accumulated after December 31, 1962”.

On page 262, line 10, after the word “Foreign”, to strike out “Investment” and insert “Investment Companies”; after line 16, to insert:

“(g) NONAPPLICATION OF SECTION 367 IN CERTAIN CASES.—Section 367 shall not apply in respect of a foreign investment company described in paragraph (1) of subsection (b) which is a party to a reorganization in which all of its properties are acquired before January 1, 1964, by a domestic corporation which is a regulated investment company under section 851 for its first taxable year ending after the reorganization, but only if such foreign investment company made the election described in section 1247 with respect to its taxable years beginning after December 31, 1962.”

On page 263, line 3, to change the letter “(g)” to “(h)”.

On page 263, line 20, after the word “of” where it occurs the first time, to strike out “30” and insert “45”; in line 23, after the word “capital”, to strike out “gains” and insert “gain”, and on page 264, line 1, after the word “capital” to strike out “losses” and insert “loss of the taxable year”.

On page 264, line 14, after the word “of” to strike out “capital gains over losses” and insert “the net long-term capital gains over the net short-term capital loss”.

On page 265, line 10, after the word “of” to strike out “capital gains over losses” and insert “the net long-term capital gains over the net short-term capital loss”.

On page 266, line 9, after the word “person”, to insert “(as defined in section 7701 (a) (30))”.

At the top of page 267, to strike out:

“(d) ADJUSTMENTS.—Under regulations prescribed by the Secretary or his delegate, proper adjustment shall be made—

“(1) in the earnings and profits of the electing foreign investment company, and

“(2) the adjusted basis of stock of such company held by qualified shareholders,

to reflect the inclusion in gross income by such shareholders of undistributed capital gains.”

And in lieu thereof, to insert:

"(d) TREATMENT OF DISTRIBUTED AND UN-DISTRIBUTED CAPITAL GAINS BY A QUALIFIED SHAREHOLDER.—Every qualified shareholder of a foreign investment company for any taxable year of such company with respect to which an election pursuant to subsection (a) is in effect shall include, in computing his long-term capital gains—

"(1) for his taxable year in which received, his pro rata share of the distributed portion of the excess of the net long-term capital gain over the net short-term capital loss for such taxable year of such company, and

"(2) for his taxable year in which or with which the taxable year of such company ends, his pro rata share of the undistributed portion of the excess of the net long-term capital gain over the net short-term capital loss for such taxable year of such company.

"(e) ADJUSTMENTS.—Under regulations prescribed by the Secretary or his delegate, proper adjustment shall be made—

"(1) in the earnings and profits of the electing foreign investment company and a qualified shareholder's ratable share thereof, and

"(2) in the adjusted basis of stock of such company held by such shareholder,

to reflect such shareholder's inclusion in gross income of undistributed capital gains.

"(f) ELECTION BY FOREIGN INVESTMENT COMPANY WITH RESPECT TO FOREIGN TAX CREDIT.—A foreign investment company with respect to which an election pursuant to subsection (a) is in effect and more than 50 percent of the value (as defined in section 851(c)(4)) of whose total assets at the close of the taxable year consists of stock or securities in foreign corporations may, for such taxable year, elect the application of this subsection with respect to income, war profits, and excess profits taxes described in section 901(b)(1) which are paid by the foreign investment company during such taxable year to foreign countries and possessions of the United States. If such election is made—

"(1) the foreign investment company—

"(A) shall compute its taxable income, for purposes of subsection (a)(1)(A), without any deductions for income, war profits, or excess profits taxes paid to foreign countries or possessions of the United States, and

"(B) shall treat the amount of such taxes, for purposes of subsection (a)(1)(A), as distributed to its shareholders;

"(2) each qualified shareholder of such foreign investment company—

"(A) shall include in gross income and treat as paid by him his proportionate share of such taxes, and

"(B) shall treat, for purposes of applying subpart A of part III of subchapter N, his proportionate share of such taxes as having been paid to the country in which the foreign investment company is incorporated, and

"(C) shall treat as gross income from sources within the country in which the foreign investment company is incorporated, for purposes of applying subpart A of part III of subchapter N, the sum of his proportionate share of such taxes and any dividend paid to him by such foreign investment company.

"(g) NOTICE TO SHAREHOLDERS.—The amounts to be treated by qualified shareholders, for purposes of subsection (f)(2), as their proportionate share of the taxes described in subsection (f)(1)(A) paid by a foreign investment company shall not exceed the amounts so designated by the foreign investment company in a written notice mailed to its shareholders not later than 45 days after the close of its taxable year.

"(h) MANNER OF MAKING ELECTION AND NOTIFYING SHAREHOLDERS.—The election provided in subsection (f) and the notice to shareholders required by subsection (g) shall

be made in such manner as the Secretary or his delegate may prescribe by regulations."

On page 270, at the beginning of line 13, to change the letter from "(e)" to "(1)".

On page 271, in the language following line 2, after the word "company" to insert the word "stock".

On page 271, line 21, after the word "of" where it occurs the first time, to strike out "paragraphs (1) and (2)" and insert "paragraph (1)".

On page 274, at the beginning of line 3, to change the section number from "16" to "15"; in line 11, after the word "section", where it appears the first time, to strike out "15" and insert "14"; after line 11, to strike out:

"SEC. 1248. GAIN FROM CERTAIN SALES OR EXCHANGES OF STOCK IN CERTAIN FOREIGN CORPORATIONS.

"(a) REDEMPTIONS AND LIQUIDATIONS.—If a foreign corporation redeems its stock in an exchange to which section 302(a) applies, or if a foreign corporation cancels its stock in a complete or partial liquidation in an exchange to which section 331 applies, then the gain of a United States person (as defined in section 7701(a)(30)) from the exchange of such stock shall be included in the gross income of such person as a dividend, to the extent of such person's proportionate share of the earnings and profits of the foreign corporation accumulated after February 28, 1913.

"(b) SALES AND OTHER EXCHANGES.—If a United States person (as defined in section 7701(a)(30)) sells or exchanges stock in a foreign corporation, then the gain recognized on the sale or exchange of such stock shall be considered as gain from the sale or exchange of property which is not a capital asset, to the extent of such person's proportionate share of the earnings and profits of the foreign corporation accumulated during the period the stock sold or exchanged was held by such person.

"(c) LIMITATIONS.—

"(1) CONTROLLED FOREIGN CORPORATIONS.—Subsections (a) and (b) shall apply only if the foreign corporation the stock of which is sold or exchanged (A) is a controlled foreign corporation (as defined in section 954) at the time of the sale or exchange, or (B) was such a controlled foreign corporation at any time during the 5-year period ending on the date of the sale or exchange.

"(2) 10 PERCENT OWNERSHIP.—Subsections (a) and (b) shall apply only to a United States person who can be considered, by applying the rules of constructive ownership of section 955(b), as being the owner, directly or indirectly, of 10 percent or more of the total combined voting power of all classes of stock entitled to vote of the foreign corporation at the time of the sale or exchange, or at any time during the 5-year period ending on the date of the sale or exchange.

"(3) ELIMINATION FROM EARNING AND PROFITS OF AMOUNTS INCLUDED IN GROSS INCOME UNDER SECTION 951.—In determining the amount to be considered a dividend under subsection (a), or as gain from the sale or exchange of property which is not a capital asset under subsection (b), the United States person's proportionate share of earnings and profits of the foreign corporation shall be reduced by the amount previously included in the gross income of such person under section 951, with respect to the stock sold or exchanged, but only to the extent such amount did not result in an exclusion from gross income under section 956.

"(4) REDEMPTIONS TO PAY DEATH TAXES.—Subsections (a) and (b) shall not apply to distributions to which section 303 (relating to distributions in redemption of stock to pay death taxes) applies.

"(5) ADDITIONAL CONSIDERATION IN CERTAIN REORGANIZATIONS.—Subsection (b) shall not apply to gain recognized on exchanges to which section 356 (relating to receipt of additional consideration in certain reorganizations) applies.

"(6) TREATMENT OF AMOUNTS WHICH ARE ORDINARY INCOME, ETC., UNDER OTHER PROVISIONS.—Subsections (a) and (b) shall not apply with respect to any amount to the extent that such amount is, under any other provision of this title, treated as—

"(A) a dividend,

"(B) gain from the sale of an asset which is not a capital asset, or

"(C) gain from the sale of an asset held for not more than 6 months.

"(d) TAXPAYER TO ESTABLISH EARNINGS AND PROFITS.—Unless the taxpayer establishes the amount of the earnings and profits of the foreign corporation to be taken into account under subsections (a) and (b), all gain from the sale or exchange shall be considered a dividend under subsection (a), or as gain from the sale or exchange of property which is not a capital asset under subsection (b), whichever applies."

And, in lieu thereof, to insert:

"SEC. 1248. GAIN FROM CERTAIN SALES OR EXCHANGES OF STOCK IN CERTAIN FOREIGN CORPORATIONS.

"(a) GENERAL RULE.—If—

"(1) a United States person sells or exchanges stock in a foreign corporation, or if a United States person receives a distribution from a foreign corporation which, under section 302 or 331, is treated as an exchange of stock, and

"(2) such person owns, within the meaning of section 958(a), or is considered as owning by applying the rules of ownership of section 958(b), 10 percent or more of the total combined voting power of all classes of stock entitled to vote of such foreign corporation at any time during the 5-year period ending on the date of the sale or exchange when such foreign corporation was a controlled foreign corporation (as defined in section 957),

then the gain recognized on the sale or exchange of such stock shall be included in the gross income of such person as a dividend, to the extent of the earnings and profits of the foreign corporation attributable (under regulations prescribed by the Secretary or his delegate) to such stock which were accumulated in taxable years of such foreign corporation beginning after December 31, 1962, and during the period or periods the stock sold or exchanged was held by such person while such foreign corporation was a controlled foreign corporation.

"(b) LIMITATION ON TAX APPLICABLE TO INDIVIDUALS.—

"(1) IN GENERAL.—In the case of an individual, the tax attributable to an amount included in gross income as a dividend under subsection (a) shall not be greater than the tax described in paragraph (2) or in paragraph (3), whichever is lesser.

"(2) DOMESTIC CORPORATION LIMITATION.—If the stock sold or exchanged is a capital asset (within the meaning of section 1221) and has been held for more than 6 months, a tax equal to the sum of—

"(A) a pro rata share of the excess of—

"(1) the taxes that would have been paid by the foreign corporation with respect to its income had it been taxed under this chapter as a domestic corporation (but without allowance for deduction of, or credit for, taxes described in clause (ii)), for the period or periods the stock sold or exchanged was held by the United States person in taxable years beginning after December 31, 1962, while the foreign corporation was a controlled foreign corporation, adjusted for distributions and amounts previously included in gross income of a United States shareholder under section 951, over

"(ii) the income, war profits, or excess profits taxes paid by the foreign corporation with respect to such income; and

"(B) an amount equal to a tax that would result by including in gross income the amount described in subsection (a), reduced by the excess of the taxes described in paragraph (A)(i) over the taxes described in paragraph (A)(ii), as gain from the sale or exchange of a capital asset held for more than 6 months.

"(3) ANNUAL DISTRIBUTION LIMITATION.—A tax equal to the aggregate of the taxes which would have been attributable to the amount described in subsection (a) had it been included in the gross income of the individual as a dividend in the year or years in which earned by the foreign corporation, adjusted for losses and distributions as provided by regulations prescribed by the Secretary or his delegate.

"(c) SPECIAL RULES.—For purposes of this section, the following amounts shall be excluded, with respect to any United States person, from the earnings and profits of a foreign corporation:

"(1) AMOUNTS INCLUDED IN GROSS INCOME UNDER SECTION 951.—Earnings and profits of the foreign corporation attributable to any amount previously included in the gross income of such person under section 951, with respect to the stock sold or exchanged, but only to the extent the inclusion of such amount did not result in an exclusion of an amount from gross income under section 959.

"(2) GAIN REALIZED FROM THE SALE OR EXCHANGE OF PROPERTY IN PURSUANCE OF A PLAN OF COMPLETE LIQUIDATION.—If a foreign corporation adopts a plan of complete liquidation in a taxable year of a foreign corporation beginning after December 31, 1962, and if section 337(a) would apply if such foreign corporation were a domestic corporation, earnings and profits of the foreign corporation attributable (under regulations prescribed by the Secretary or his delegate) to any net gain from the sale or exchange of property.

"(3) LESS DEVELOPED COUNTRY CORPORATIONS.—Earnings and profits accumulated by a foreign corporation while it was a less developed country corporation (as defined in section 955(c)), if—

"(A) the foreign corporation qualified as a less developed country corporation for all taxable years of such corporation beginning after December 31, 1962, for which the country under the laws of which the foreign corporation was created or organized (or, in the case of a less developed country corporation within the meaning of section 955(c)(2), for which the country under the laws of which the aircraft or vessels described therein were registered) was designated a less developed country under section 955(c)(3); and

"(B) the stock sold or exchanged was owned for a continuous period of at least 10 years, ending with the date of the sale or exchange, by the United States person who sold or exchanged such stock.

In the case of stock sold or exchanged by a corporation, if United States persons who are individuals, estates, or trusts (each of whom owned within the meaning of section 958(a), or were considered as owning by applying the rules of ownership of section 958(b), 10 percent or more of the total combined voting power of all classes of stock entitled to vote of such corporation) owned, or were considered as owning, at any time during the 10-year period referred to in subparagraph (B) more than 50 percent of the total combined voting power of all classes of stock entitled to vote of such corporation, this paragraph shall apply only if such United States persons owned, or were considered as owning, at all times during the remainder of such 10-year period more than 50 percent of the total combined voting power of all classes of stock entitled to

vote of such corporation. For purposes of this paragraph, stock owned by a United States person who is an individual, estate, or trust which was acquired by reason of the death of the predecessor in interest of such United States person shall be considered as owned by such United States person during the period such stock was owned by such predecessor in interest, and during the period such stock was owned by any other predecessor in interest if between such United States person and such other predecessor in interest there was no transfer other than by reason of the death of an individual.

"(4) UNITED STATES INCOME.—Any item includible in gross income of the foreign corporation under this chapter as income derived from sources within the United States of a foreign corporation engaged in trade or business in the United States.

"(5) AMOUNTS INCLUDED IN GROSS INCOME UNDER SECTION 1247.—If the United States person whose stock is sold or exchanged was a qualified shareholder (as defined in section 1247(c)) of a foreign corporation which was a foreign investment company (as described in section 1246(b)(1)), the earnings and profits of the foreign corporation for taxable years in which such person was a qualified shareholder.

"(d) EXCEPTIONS.—This section shall not apply to—

"(1) distributions to which section 303 (relating to distributions in redemption of stock to pay death taxes) applies;

"(2) gain realized on exchanges to which section 356 (relating to receipt of additional consideration in certain reorganizations) applies; or

"(3) any amount to the extent that such amount is, under any other provision of this title, treated as—

"(A) a dividend,

"(B) gain from the sale of an asset which is not a capital asset, or

"(C) gain from the sale of an asset held for not more than 6 months.

"(e) TAXPAYER TO ESTABLISH EARNINGS AND PROFITS.—Unless the taxpayer establishes the amount of the earnings and profits of the foreign corporation to be taken into account under subsection (a), all gain from the sale or exchange shall be considered a dividend under subsection (a), and unless the taxpayer establishes the amount of foreign taxes to be taken into account under subsection (b)(2), the limitation of such subsection shall not apply."

On page 284, line 21, after the word "after", to strike out "the date of the enactment of this Act" and insert "December 31, 1962".

At the top of page 285, to insert a new section, as follows:

"SEC. 16. SALES AND EXCHANGES OF PATENTS, ETC., TO CERTAIN FOREIGN CORPORATIONS.

"(a) TREATMENT OF GAIN AS ORDINARY INCOME.—Part IV of subchapter P of chapter 1 (relating to special rules for determining capital gains and losses) is amended by adding after section 1248 (as added by section 15 of this Act) the following new section:

"SEC. 1249. GAIN FROM CERTAIN SALES OR EXCHANGES OF PATENTS, ETC., TO FOREIGN CORPORATIONS.

"(a) GENERAL RULE.—Except as provided in subsection (c), gain from the sale or exchange after December 31, 1962, of a patent, an invention, model or design (whether or not patented), a copyright, a secret formula or process, or any other similar property right to any foreign corporation by any United States person (as defined in section 7701(a)(30)) which controls such foreign corporation shall, if such gain would (but for the provisions of this subsection) be gain from the sale or exchange of a capital asset or of property described in section 1231, be considered as gain from the sale or ex-

change of property which is neither a capital asset nor property described in section 1231.

"(b) CONTROL.—For purposes of subsection (a), control means, with respect to any foreign corporation, the ownership, directly or indirectly, of stock possessing more than 50 percent of the total combined voting power of all classes of stock entitled to vote. For purposes of this subsection, the rules for determining ownership of stock prescribed by section 958 shall apply.

"(c) EXCEPTION.—This section shall not apply to gain realized from the sale or exchange for stock or contribution to capital of property described in subsection (a) where it is established to the satisfaction of the Secretary or his delegate that the principal purpose of the transfer is to enable the foreign corporation to use such property in its own manufacturing operations."

"(b) CLERICAL AMENDMENT.—The table of sections for such part IV is amended by adding at the end thereof the following:

"Sec. 1249. Gain from certain sales or exchanges of patents, etc., to foreign corporations."

"(c) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 1962."

In section 17, on page 290, at the beginning of line 10, to insert "For purposes of subsections (b)(1) and (c)(2)(A), a qualified check issued during the payment period shall be treated as an amount paid in money during such period if endorsed and cashed on or before the 90th day after the close of such period."; on page 297 after line 7, to insert "Such term does not include any written notice of allocation which is paid as part of a patronage dividend or as part of a payment described in section 1382(c)(2)(A), unless 20 percent or more of the amount of such patronage dividend, or such payment, is paid in money or by qualified check."; in line 18, after the word "writing", to strike out "or"; on page 298, line 2, after the word "such", to strike out "bylaw" and insert "bylaw, or

"(C) if neither subparagraph (A) nor (B) applies, endorsing and cashing a qualified check, paid as a part of the patronage dividend or payment of which such written notice of allocation is also a part, on or before the 90th day after the close of the payment period for the taxable year of the organization for which such patronage dividend or payment is paid."

At the top of page 300, to insert:

"(4) QUALIFIED CHECK.—For purposes of this subchapter, the term 'qualified check' means only a check (or other instrument which is redeemable in money) which is paid as a part of a patronage dividend, or as a part of a payment described in section 1382(c)(2)(A), to a distributee who has not given consent as provided in paragraph (2)(A) or (B) with respect to such patronage dividend or payment, and on which there is clearly imprinted a statement that the endorsement and cashing of the check (or other instrument) constitutes the consent of the payee to include in his gross income, as provided in the Federal income tax laws, the stated dollar amount of the written notice of allocation which is a part of the patronage dividend or payment of which such qualified check is also a part. Such term does not include any check (or other instrument) which is paid as part of a patronage dividend or payment which does not include a written notice of allocation (other than a written notice of allocation described in paragraph (1)(A))."

On page 300, line 24, after "(c)", to insert "or a qualified check which is not cashed on or before the 90th day after the close of the payment period for the taxable year for which the distribution of which it is a part

is paid"; on page 301, after line 18, to strike out:

"(3) Section 6044 (relating to returns regarding patronage dividends) is amended to read as follows:

"SEC. 6044. RETURNS REGARDING PATRONAGE DIVIDENDS.

"Any organization to which part I of subchapter T of chapter 1 (relating to tax treatment of cooperatives) applies which pays amounts described in section 1382(b), or (in the case of an organization described in section 1381(a)(1)) amounts described in section 1382(c)(2), shall, when required by regulations of the Secretary or his delegate, make a return showing

"(1) the name and address of each patron to whom it has made such payments during the calendar year; and

"(2) the amount of such payments to each patron."

On page 302, at the beginning of line 8, to strike out "(4)" and insert "(3)"; on page 303, at the beginning of line 4, to strike out "(5)" and insert "(4)"; at the beginning of line 6, to strike out "(6)" and insert "(5)".

In section 20, on page 373, line 5, after the word "and", to strike out "957" and insert "960"; at the beginning of line 21, to strike out "subsection" and insert "paragraph"; after line 24, to insert:

"(2) LIMITATION.—The amount of the reduction under paragraph (1) for each failure to furnish information with respect to a foreign corporation required under subsection (a)(1) shall not exceed whichever of the following amounts is the greater:

"(A) \$10,000, or

"(B) the income of the foreign corporation for its annual accounting period with respect to which the failure occurs."

On page 374, at the beginning of line 9, to strike out "(2)" and insert "(3)"; in line 22, after the word "section", to strike out "956" and insert "960"; on page 376, line 2, after the word "apply", to strike out "except that clause (i) of section 318(a)(2)(C) shall be applied without regard to the 50 percent limitation contained in such section." and insert "except that—

"(A) the second sentence of subparagraphs (A) and (B), and clause (ii) of subparagraph (C), of section 318(a)(2) shall not be applied so as to consider a United States person as owning stock which is owned by a person who is not a United States person, and

"(B) in applying clause (i) of subparagraph (C) of section 318(a)(2), the phrase '10 percent' shall be substituted for the phrase '50 percent' used in subparagraph (C)."

On page 377, line 10, after the word "is", to strike out "an officer or director of a foreign corporation on January 1, 1963" and insert "on January 1, 1963, an officer or director of a foreign corporation, 5 percent or more in value of the stock of which is owned by a United States person,"; on page 378, line 10, after the word "laws", to insert a comma and "except that in the case of persons described only in subsection (a)(1) the information required shall be limited to the names and addresses of persons described in subsection (a)(2)"; in line 15, after "(a)", to strike out "(2) and (3)"; on page 379, after line 5, to insert:

"(e) LIMITATION.—No information shall be required to be furnished under this section with respect to any foreign corporation unless such information was required to be furnished under regulations which, on the date on which the United States citizen, resident, or person becomes liable to file a return required under subsection (a)—

"(1) if such liability arises on or after January 1, 1963, and before March 1, 1963, have been in effect since January 1, 1963 (but only if such regulations were prescribed before December 1, 1962), or

"(2) if such liability arises on or after March 1, 1963, have been in effect for at least 90 days."

On page 379, at the beginning of line 18, to strike out "(e)" and insert "(f)"; in the second line of the material after line 18, after the word "sections", to strike out "6678" and insert "6679"; on page 380, line 3, after the word "adding", to strike out "at the end thereof" and insert "after section 6678 (as added by section 19(e) of this Act)"; at the beginning of line 6, to change the section number from "6678" to "6679"; on page 381, at the beginning of the line after line 9, to change the section number from "6678" to "6679".

On page 391, at the beginning of line 22 to change the section number from "21" to "27"; after line 22, to strike out:

"Section 7852(d) of the Internal Revenue Code of 1954 (relating to treaty obligations) shall not apply in respect of any amendment made by this Act."

And, in lieu thereof, to insert:

"No provision of this Act shall apply in any case where its application would be contrary to any treaty obligation of the United States."

Mr. KERR. Mr. President, yesterday I occupied the floor for about 4 hours, some considerable part of the time devoted to answering questions from the distinguished Senator from Wisconsin. Later in the day, as I went by his chair, he asked me if I would again yield. I explained to him that some degree of physical fatigue had set in and I did not want to again take the floor, but that I would be happy to do so today. I now have the floor, Mr. President, and I am happy to yield to the Senator from Wisconsin for a question.

Mr. PROXMIRE. I thank the Senator for yielding.

I want to ask the Senator from Oklahoma how he can maintain that we need investment credit for the purpose of increasing the modernization of American equipment and machinery in view of the fact that the McGraw-Hill survey shows we are going to have this year the biggest investment in plant and equipment in the history of our country. They expect, on the basis of their survey, which has been very accurate in the past, for it to be even bigger in 1963, 1964, and 1965. Furthermore, they say that 70 percent of this investment is going to be in modernization. So without the investment credit, and even without the new depreciation provisions, we are going to have the greatest improvement in the modernization of our plant we have ever had in our history, and the expectation is that plant is going to be automated even more rapidly in the next 3 or 4 years.

Since the most authoritative evidence is that industry is going to break all records in modernization, how can the Senator from Oklahoma maintain that we need investment credit for the purpose of increasing the modernization of American equipment and machinery?

Mr. KERR. Mr. President, the position of the Senator from Oklahoma is this: America has come of age in a new world, a world we have helped create, of which we are a part, and of which, with reference to the free nations of the world, we are the leaders. We are confronted with the reality of a revived, re-

surgent, vital, dynamic, expanding industrial workshop in Western Europe, which, as of today, in countries with a population equal to our own, is united in an economic union, which union is in the process of negotiating with the United Kingdom to become a part of it. The Senator from Oklahoma is hopeful that those negotiations will be successful, and that the United Kingdom will become a part of the Common Market. The Senator from Oklahoma entertains this wish because he believes it will be to the advantage of the United States of America for that to be accomplished.

The Senator from Oklahoma believes that this economic union in Western Europe, especially if and when the United Kingdom becomes a part of it, will be a third world power, with an industrial, population, and resource strength superior to that of Russia and with an industrial potential superior to that of both Russia and China. The Senator from Oklahoma believes it will be a great barrier—and I believe one of the two invincible barriers—against Communist aggression and world domination either by Communist Russia or Communist China or both.

Yet, great as are those advantages, the competitive position between the United States of America and that great industrial workshop in Western Europe will be something which will be fought out over a period of years, during which the fiercest industrial competition which has ever taken place in this world will occur.

It is the hope of the Senator from Oklahoma that the United States will emerge, shall I say, triumphant in that great competitive and economic struggle. If it is to do so, the rate of growth we have had, the rate of growth we now have, and the rate of growth we foresee under the present environment of our industrial complex, in the opinion of the Senator from Oklahoma, will not be adequate in the elements of encouragement and stimulant which it contains to permit and to bring about that desired growth in our own industrial workshop which will enable us to hold our own in that tremendously fierce and enduring competition.

The Senator from Oklahoma does not believe that we should wait until that competition has reached the point that it is evident that the great industrial workshop emerging in Europe, the overall rate of growth of which is at this time much higher than our own, to take those actions which will insure the opportunity for the certainty that America's industrial growth will be maintained at a rate that will never permit our position industrially and competitively, both for the domestic market within this country and for the world market in the channels of trade and commerce of the free world, to be jeopardized.

Therefore, the Senator from Oklahoma thinks that a stitch in time will save nine, that action in time will insure the achievement of this objective, for which I know the Senator from Wisconsin devoutly hopes.

If there is disagreement between the Senator from Wisconsin and the Senator from Oklahoma, it is not as to the objective to be achieved but is as to whether this provision is either necessary or helpful to the achieving of that objective. The Senator from Oklahoma thinks it is. The Senator from Wisconsin thinks it is not. I have full respect for the Senator's position and for his ability to make it clear. I simply do not agree with it.

Mr. PROXMIRE. Is it not true that with the changes in the depreciation schedule which the Treasury Department has now provided, any firm can depreciate any piece of equipment or machinery as rapidly as it wishes, and in the future for the first time will have an opportunity to write it off against taxes; provided only that it can show it actually does depreciate and actually does use up the equipment that rapidly? So although the new depreciation schedule which has gone into effect has not had an effect yet at stimulating the American economy, it would seem to be just about as far as one could go without providing an extraordinary, excessive advantage for manufacturers.

Mr. KERR. The first question the Senator asked the Senator from Oklahoma would answer in the affirmative. Since the Senator then qualified his question, the Senator from Oklahoma will have to answer in the negative.

The fact about the business is, Mr. President, even giving effect to the new depreciation guidelines, the representative tax life, with reference to a comparison between the United States and the nations of Europe, would be roughly as follows: in Belgium 8 years, in Canada 10 years, in France 10 years, in West Germany 10 years, in Italy 10 years, in the Netherlands 10 years, in Sweden 5 years, in the United States 12 years, in Japan 16 years, and in the United Kingdom 27 years.

Giving effect to the new guidelines in the last order, to which the Senator has referred, the depreciation allowance in the first year would be as follows: in Belgium 22½ percent, in Canada 30 percent, in France 25 percent, in West Germany 20 percent, in Italy 25 percent, in Japan 43.4 percent, in The Netherlands 26.2 percent, in Sweden 30 percent, and in the United Kingdom 39 percent.

The average for all those foreign countries is a 29 percent depreciation deduction, initial investment allowance, the first year. That is an average of 29 percent. In the United States, after giving effect to the new depreciation guidelines, the percentage is 16.7 percent.

Mr. DOUGLAS. Mr. President, will the Senator yield?

Mr. KERR. That compares to the overall average which I have just stated, as to which I read the details, of 29 percent in the nine foreign countries which are competitive to us.

Mr. DOUGLAS. Mr. President, will the Senator yield?

Mr. PROXMIRE. Mr. President—

Mr. KERR. I should be delighted to yield to my friend from Illinois, but the Senator from Wisconsin, after the Sen-

ator from Oklahoma talked to him yesterday and explained to him he was not exhausted, but tired, and would be glad to yield to him this morning, took the floor of the Senate and expressed regret over the fact that the Senator from Oklahoma had seen fit to leave the Chamber and not permit himself to be interrogated by the Senator from Wisconsin.

Mr. DOUGLAS. I understand and withdraw my request.

Mr. KERR. I say to my friend from Illinois, after I have fully satisfied the Senator from Wisconsin I shall have no higher pleasure than to yield to the Senator from Illinois for such questions as he wishes to ask.

Mr. DOUGLAS. It is always a great pleasure to engage in colloquy with the Senator from Oklahoma. I think his implicit reproof to me is correct. I shall not try to inject myself in this discussion.

Mr. PROXMIRE. Mr. President, I wish to make it clear that the Senator from Wisconsin merely stated exactly what happened. The Senator from Oklahoma said he preferred to be interrogated this morning. I put that in the RECORD. I thought that was a perfectly reasonable request. I said I would regret it very much if there were not an opportunity to interrogate the Senator from Oklahoma, who is in charge of the consideration of the bill, before the Senate takes action.

Mr. KERR. I would not miss it for the world.

Mr. PROXMIRE. So the Senator from Oklahoma and the Senator from Wisconsin agree on this.

Now, to get back to the Senator's answer, I merely wish to point out to the Senator from Oklahoma that whereas there may be in the difference in depreciation opportunities to which the Senator adverts, it is very interesting to note that the countries which can charge off the largest amount of their equipment in the first year—and the United Kingdom is a conspicuous example—have been growing more slowly than others.

The investment credit has not helped them. They have been doing worse not better than countries that have no investment credit. Sweden can charge off the life of assets in an average of 5 years; Belgium 8 years. Those countries have been growing more slowly than has the United States, not more rapidly. So the empirical evidence shows—

Mr. KERR. With reference to Sweden, we know that it is a Socialist country in which, so far as we know, all or much of the industry is owned by the Government. It is a Socialist government. The Senator from Oklahoma believes that any Socialist government will slow down the industrial development within it. That is inherent in socialism. This country, with even more shackles around it than it has now, will outgrow any Socialist country in the world.

The United Kingdom has had a slower rate of growth. I cannot imagine more trouble than the United Kingdom has had economically in the past 15 years. As I read my history, late in the 19th

century there was a great celebration in England. It was the 50th anniversary of the great Queen. People came from around the world and joined in a tribute to the great Queen and to the mighty empire over which she reigned.

England was the predominant military power in the world. It was said that the sun never set upon her dominions and her possessions. England was the predominant financial power in the world. England was the predominant industrial power in the world. Her mighty fleet which ruled the waves made it possible for countless thousands of boats and ships to ply the seven seas, bringing from her colonies around the world raw materials which were fed into the maw of her industrial machines, out of which poured the mighty production which gave her a predominant position industrially and financially, and supported her in achieving her predominant military position in the world.

While that celebration was under way, a citizen of England was a resident in our country. I know he must have been thrilled by the great celebration going on in his native land and by the tribute being paid to the great queen upon her 50th anniversary. But he looked down the years and saw that the day would come when his mother country would be stripped of her colonies and when the foundation for the mighty position she occupied would no longer exist. Rudyard Kipling then penned the immortal words of the "Recessional":

God of our fathers, known of old,
Lord of our far-flung battle line
Beneath whose awful hand we hold
Dominion over palm and pine,
Lord God of Hosts, be with us yet,
Lest we forget, lest we forget!

He said:

The tumult and the shouting dies,
The captains and the kings depart,
Still stands Thine ancient sacrifice,
An humble and a contrite heart.
Lord God of Hosts, be with us yet,
Lest we forget—lest we forget!

Today I honor England, equal with the honor I pay any nation on this earth, other than the proud and mighty Nation under the Western stars, beneath the flag of Old Glory.

But England no longer rules the waves. Her financial institutions are no longer the dominant power in finance. Her industrial workshop no longer causes the channels of trade and commerce to tremble or stand in awe and respect. The star that was then in its zenith above the United Kingdom and shone with such brilliance upon the magnificent celebration of the 50th anniversary of the great queen has long since left its zenith and started its inexorable descent down the Western horizon.

It is my hope that it will never set, because she has a proud and glorious history and record. But her colonies have been stripped from her. She has had the fight of her life to survive. Be it said to her credit, her courage has never failed or dimmed. The ingenuity and resourcefulness of her people have never been impaired.

But she is competing today with our Nation. Today the star of America is in

the zenith, and our light shines far above the seven seas and the channels of trade and commerce around the world. It is well, because we now bear the burden of world leadership of the free world. Ours is the dominant industrial workshop on the earth. We are the center of financial strength and power in our world. We are the proud possessors of mighty fleets in the air, on the ocean, and under the waters of the ocean that make the world livable here and in other free areas.

How can the distinguished Senator from Wisconsin seek to impose upon us shackles that would hold our progress to the rate of advance yet to be made by the brave and gallant nation yonder on that island, after the sources of her wealth, her power, and her strength have been stripped from her? There is no basis of comparison, nor could we possibly endure the thought of shackling ourselves to a position in which we could march forward at no greater pace of progress than England is able to maintain.

Mr. PROXMIRE. Mr. President, will the Senator yield?

Mr. KERR. I yield. I was about to describe conditions in both Belgium and Holland.

Mr. PROXMIRE. Mr. President, I do not like to puncture the Senator's magnificent oratorical balloon—

Mr. KERR. Have at it.

Mr. PROXMIRE. I will have at it.

Mr. KERR. I ask no quarter and give none.

Mr. PROXMIRE. The Senator has made an attack on the investment credit in trying to defend it, that demolishes his own position. The fact is that England was rising. England was reaching the zenith before she had the investment credit and before she had the advantages of quick depreciation. Since she adopted that method of subsidy—this particular method of tax advantage for manufacturers—she has gone down, as the Senator has so eloquently described. Whenever we raise this point—whether it be in relation to Belgium, the Netherlands, England, or Sweden—there is always an alibi. It is said that this country or that country is a Socialist country, or that it has lost its colonies.

They have had one kind of problem or another. The fact remains that they adopted investment credit, and they have not grown as rapidly as we have.

Mr. KERR. The decline started before they adopted the measure. They adopted the measure in an effort to hold the decline as they started up the hill with some degree of success. The Senator's observations on history are not supported by the record. However, I yield for a question, not a speech.

Mr. PROXMIRE. Is it the Senator's position that although we are winning the trade competition, although we have a new depreciation schedule, we must follow the same kind of tax privilege and tax advantage that our world competitors do, no matter how unjustifiable and discriminatory they may be? I ask the Senator if this is not the same old story that we have encountered in our experience in our own States, the argument that we must adopt whatever regressive form of taxation a nearby State has

adopted if we are to permit our manufacturers, in Oklahoma or in Wisconsin, to compete successfully? Is it not the same old discredited argument that we have to have a tax system, no matter how regressive it may be, in order to put our industry on the same basis? Finally, I wish to ask the Senator—

Mr. KERR. I wish the Senator would ask these questions one at a time. The Senator has already asked three. I will try to answer two of them. First, as of now, certainly, we are not winning the trade war. The Senator has been quoting figures on the floor about our advantage with reference to imports and exports, totally ignoring many of the elements of the picture relating to export dollars in contrast to the dollars we import.

The Senator has used various figures about how much more we sell than we buy. He took offense yesterday because I did not accept the figures of the Department of Commerce in this connection. About 2 years ago the distinguished chairman of our committee became suspicious of the figures that were being given to the committee with reference to how much this country was exporting and how much it was importing. Witnesses came before our committee and told us:

The figures of the Department of Commerce show that we have a \$4 billion favorable trade balance.

The distinguished senior Senator from Virginia said:

Let us analyze these statements. How much of this supposedly \$4 billion trade balance is due to the agricultural and other products we export after we give them away?

Mr. PROXMIRE. Mr. President—

Mr. KERR. Let me answer the Senator's question. He can stand up as long as I can.

Mr. PROXMIRE. The Senator has asked a rhetorical question. I wish to answer it.

Mr. KERR. The Senator from Virginia asked that question of the witness. The witness said, "I do not know."

The Senator from Virginia said, "Go and get the answer."

The witness came back and disclosed that about \$2 billion to \$2½ billion of that supposedly advantageous or favorable trade balance was by reason of what we had given away.

Mr. ROBERTSON. Mr. President, will the Senator yield?

Mr. KERR. I yield.

Mr. ROBERTSON. On grains?

Mr. KERR. Yes.

Mr. ROBERTSON. Six billion nine hundred million dollars, for soft currency, which is equal to a giveaway.

Mr. KERR. Yes. That has been included in the figures of the Commerce Department, representing to the American people what our favorable balance was in connection with trade and commerce. Because of the fight made by the Finance Committee, under the able leadership of its distinguished chairman, the Commerce Department began using a different basis for the figures that it publishes.

However, even as of now, when they issue their monthly figures on what our

exports and imports are, they include in the exports what we give away.

Finally, when they get down to the things that go out for dollars, as contrasted with the imports that come in and are paid for in dollars, they give the figures in their quarterly reports. But even in those reports they include our agricultural exports, which are sold at the world market. Cotton, for example, is sold at 8½ cents a pound less than American textile mills pay for it. Feed grains are sold at a greatly reduced price.

Mr. ROBERTSON. Mr. President, will the Senator yield?

Mr. KERR. I yield.

Mr. ROBERTSON. On wheat, our export subsidy is 65 cents a bushel.

Mr. KERR. On wheat, it is 65 cents a bushel. Yet the dollar we receive from the sale of agricultural products at giveaway prices are included in the Commerce Department's reports with reference to our trade balance, imports and exports. If we strip from that statement the billions of dollars of agricultural exports that we send out, for which we receive some dollars, but which are sold at from 25 percent to 35 percent below the domestic market, we find emerging an entirely different picture.

As of now, the Department of Commerce says we have a favorable trade balance, I believe, running at the rate of \$2 billion for 1962. The Senator from Oklahoma has not had time to go beneath the surface, as the Senator from Virginia has so often done in asking questions at Finance Committee hearings, and as the distinguished junior Senator from Virginia [Mr. ROBERTSON] has indicated in connection with the prices that we get for these exports, even though they pay us a part of their value in dollars.

Therefore, the Senator from Oklahoma does not regard as valid in this debate, and in determining the position of the American industrial workshop relative to that in Western Europe, the figures of the Department of Commerce. They are not an accurate presentation of the actual picture.

When we finally strip the issue down to what this country buys and sells, we see that what we buy we pay for at 100 cents on the dollar, and Senators will find that instead of having a rosy picture of a big balance in favor of our country, we have a sad picture, an anemic picture, one which can be corrected only by a vast increase in the efficiency in the economy of our industrial workshop and its productivity.

As I said yesterday, aside from whatever the relationship may be, if we continue to give away our products or sell them at 50 cents on the dollar, we can keep a certain number of dollars coming into this country. However, there are Senators who think the day will come when either by choice or necessity we shall abandon that process. In the meantime it is the hope of the Senator from Oklahoma that we will develop a situation which will enable us to survive and maintain the convertibility of the dollar which we now maintain, without being forced into international fiscal bankruptcy, as I related it yesterday with

respect to the decline in our gold reserve and the increase of the claims against it.

With reference to the last question of the Senator from Wisconsin, about this being the same as the contest between the various States—

Mr. PROXMIRE. Before the Senator gets to that, does he wish to yield for one further question?

Mr. KERR. I am simply answering the Senator's questions one at a time. I will finish answering the last one.

Mr. PROXMIRE. The Senator just finished saying he had finished.

Mr. KERR. No; I said:

Now, with reference to the last question of the Senator.

Mr. PROXMIRE. That is correct. I simply wanted to ask a further question with respect to the question the Senator just answered, if he will permit. Does the Senator deny that the Department of Commerce shows that we have a surplus in trade of \$4.8 billion in the first half of 1962?

Mr. KERR. Yes; I deny that it shows that.

Mr. PROXMIRE. I have the figures right here.

Mr. KERR. If the Senator will look at them, they show that we are going at that rate for the year.

Mr. PROXMIRE. That is correct.

Mr. KERR. That was not what the Senator asked.

Mr. PROXMIRE. Seasonally adjusted.

Mr. KERR. That was not in the Senator's question.

Mr. PROXMIRE. On an annual basis.

Mr. KERR. That was not in the Senator's question.

Mr. PROXMIRE. If we take out Government aid of exports, we take \$2.6 billion from that balance.

Mr. KERR. No; we have an annual rate of that.

Mr. PROXMIRE. An annual rate of that.

Mr. KERR. The Senator ought to read what the rate is.

Mr. PROXMIRE. If we add in the services rendered surplus, of \$1.7 billion; we have an annual favorable trade in the commercial area alone, leaving out the Government giveaway of \$3.9 billion. If we subtract from that the \$2.5 billion, which is all we have loaned abroad, capital long and short term from our private institutions, we have a surplus of \$1.5 billion, even assuming that all we have loaned abroad has come back and has been spent here and has benefited our export business.

I submit that on this basis, in the first half of 1962, we are winning; we are doing a better job in trade than other nations throughout the world.

Mr. KERR. Surely; but in that annual rate of \$1.5 billion is included \$1.1 billion of agricultural products we are selling.

Mr. PROXMIRE. Government aid or financed exports.

Mr. KERR. That is not Government aid exports. The Senator ought to know what he is looking at. The Senator from Oklahoma does not admit its au-

thenticity. What it says does not include sales of agricultural products that we make for dollars, not loaned, which are sold at from 25 to 40 percent discount. Did not the Senator know that?

Mr. PROXMIRE. The position of the Senator from Wisconsin is that this is included in the figures here; and this is not commercial export; it is Government-financed aid export.

Mr. KERR. No, they are not Government financed at all. We sell those products for cash, but we sell them at a discount.

Mr. PROXMIRE. They are Government sales, though. They are Government export.

Mr. KERR. That is Government aid.

Mr. PROXMIRE. It is Government export. The figure is for Government export.

Mr. KERR. The Senator said it was Government aid export.

Mr. PROXMIRE. Well, it is not commercial export.

Mr. YOUNG of North Dakota. Most of our exports of wheat are for dollars. It is private trade in itself, but is subsidized by the Government. There is a separate subsidy. It is export trade but not for the Government.

Mr. KERR. It is not included in that figure. What they actually get was included in that figure of the Department of Commerce.

So if we strip it all down bare, naked, we have a deficit. Any time we want to give this "stuff" away, we can do so.

I wrote a book 3 or 4 years ago. I found out that it was not too great a success in selling. But it was the easiest thing to give away that I ever saw. The same is true of our agricultural products.

The Senator from Oklahoma said that we have built an industry and a workshop that will bring things into the channels of trade and commerce and world competition and will produce an adequate inflow of dollars to offset what goes out for the stuff we buy; what goes out for what our tourists spend overseas; for what goes out that we spend in other countries in connection with our armed services; for what goes out in the form of loans of dollars that do not have to be spent here. Why treat a patient until he can stand up for an hour a day but never will get any better than that?

I used to know a doctor, a very dear friend of mine. He said, "Do you understand my concept of treating illness?"

I said, "Yes, you treat your patients so that they will neither die nor ever get well."

That is the kind of prescription the Senator from Wisconsin is offering. He wants to give an economic prescription that will let American industry barely get up off its knees, but never be able to stand erect and take its rightful place in the economic battles of this great new world in which we have come of age, and which we helped to create.

Mr. PASTORE. Mr. President, will the Senator from Oklahoma yield for a question?

Mr. KERR. I am delighted to yield.

Mr. PASTORE. Is the Senator from Oklahoma saying categorically that insofar as the balance of trade being in our

favor is concerned, it is merely a fiction?

Mr. KERR. The Senator from Oklahoma tried to explain very carefully what he was saying.

Mr. PASTORE. I am very much interested in the subject; I am not being critical at all.

Mr. KERR. I know the Senator is not being critical.

Mr. PASTORE. I am not trying to be impertinent. The Senator's view is very optimistic. He believes that the balance of trade is in our favor. The point has been made that some things are being sold at a discount, which are being included in what they are actually selling, and that is balancing the trade to our favor. But that is only a fiction, and not a truth.

Mr. KERR. If the Senator from Wisconsin [Mr. PROXMIRE] can understand these figures, he is far better than the Senator from Oklahoma.

The actual situation is this: I said that aside from Government aid exports and Government financing, the balances are now in our favor to the tune of \$1,500 million or \$1,200 million a year.

Mr. PROXMIRE. They are in our favor to the extent of \$3.9 billion a year even if we include the export of American capital, and even if we assume that it is all spent here.

Mr. KERR. The Department of Commerce advised me last night that aside from what we were giving away, we had a favorable balance of about \$2 billion, at the annual rate, for this year. But included in that amount are the dollars we receive for the agricultural products we sell at a discount.

I have been trying all morning to get from the Department of Agriculture the exact figures with respect to our total exports of agricultural products at a discount. I have not been able to get that information, but I expect to receive it during the day and shall place it in the RECORD. I am of the opinion that it exceeds the \$2 billion, which, according to the estimates I received from the Department of Commerce, is our favorable trade balance for this year, including the dollars we receive for the agricultural products we sell at a discount.

Mr. PASTORE. Then the Senator says we are selling our agricultural commodities at a discount. Does he mean that foreign consumers are able to buy those commodities at cheaper prices than the prices which American consumers pay?

Mr. KERR. I say that a foreign textile mill can buy American cotton—

Mr. PASTORE. I know about cotton.

Mr. KERR. At 8½ cents a pound under what domestic textile mills pay.

Mr. PASTORE. I realize that.

Mr. KERR. Foreign users are buying our wheat for about 65 cents a bushel below the domestic price.

Mr. PASTORE. In other words, American commodities are being sold abroad at a price cheaper than the price the American consumer has to pay for them?

Mr. KERR. That is correct.

Mr. PASTORE. I am familiar with the cotton situation, because that case is pending before a Government agency.

It is one in which we and the declining textile industry in this country are deeply interested. Up until now, a decision has not been forthcoming.

There is very little for us in the United States to brag about, when we are boasting about what we are selling abroad, when what we are selling there is being sold to foreign consumers at a cheaper price than the price at which it is being sold to American consumers. Certainly we have very little to brag about in that situation, and it gives no pleasure to me.

Mr. KERR. I understand; and that is what the Senator said when he said he did not believe we needed an economic doctor which would prescribe for us the kind of medicine that would barely keep us alive, but never would permit us to become as strong and as powerful as we can become with the proper economic environment.

Mr. PROXMIRE. Does the Senator from Oklahoma deny that the McGraw-Hill survey and the National Industrial Conference survey and the Wall Street Journal survey all show—after interrogating businesses all over the country—that they consider that the investment credit will have little or no effect on the investments they make; and according to the survey made by the National Industrial Conference Board, such additional investments would be made only in the amount of approximately \$300 million, but at a cost of \$1 billion in Federal revenue?

Mr. KERR. I say to the Senator from Wisconsin that my confidence in myself is such that I think I know more about the economics of the American industrial establishment than do the editors of McGraw-Hill or the Wall Street Journal—and what was the other one the Senator from Wisconsin named?

Mr. PROXMIRE. I say to the Senator—

Mr. KERR. The Senator from Wisconsin named three papers. What were they?

Mr. PROXMIRE. It was a survey of the top executives of each of these companies. They were asked what effect the proposed investment credit would have on their companies. The Wall Street Journal asked 68 of the leading business executives in the country. Only one said he would change his policy in regard to industrial plant and equipment. The National Industrial Conference Board asked 1,000. The Senator from Oklahoma is a very successful businessman; but he is only one, and I doubt that he knows more than 1,000 people—although that is possible.

Mr. KERR. I say to the Senator from Wisconsin that I do not know what McGraw-Hill said. I am like the young fellow that a well-known poet wrote about. This young fellow was trying to get a girl to marry him, but she was not satisfied with the economic situation he could offer her, and she was trying to encourage him to exert greater effort than he was capable of.

She said she wished he could be like Ben Franklin.

She said 'at Ben Franklin was awfully poor, But full of ambition an' brains;
An' studied philosophy all his hull life,
An' see what he got for his pains!

He brought electricity out of the sky,
With a kite an' a bottle an' key,
An' we're owing him more'n anyone else
For all the bright lights 'at we see.

Jane Jones she honestly said it was so!
Mebbe he did—
I dunno!
O'course what's allers been hinderin' me
Is not havin' any kite, lightnin', er key.

I do not know what McGraw-Hill said. But I know what the economic facts of life are, and I know what industrial executives in this country have told me. I know what the railroad industry has said; I know what the textile industry has said; I know what the chemical industry has said; I know what the coal industry has said; and I know what the shoe industry has said.

Mr. PROXMIRE. They want a windfall.

Mr. KERR. They say, "We need this additional incentive to enable us to build facilities to quickly and effectively compete for the domestic market and in the world market."

The Senator from Wisconsin can call it a windfall if he likes; it is immaterial to the Senator from Oklahoma. I simply do not agree with him.

I think it is a constructive piece of tax legislation which, in conjunction with the revision of the depletion formula recently announced, will arm the industrial workshop in this country with the economic weapons to enable it to survive and to prosper. Mere survival, Mr. President, is inadequate.

Mr. PROXMIRE. These hundreds of executives were asked the question: If the administration's program of tax incentives for investment purposes were enacted, how much would it cause them to increase their capital expenditures in 1962?

In reply, business as a whole indicated that it would raise its 1962 plans by only about 1 percent or about \$300 million. Nine out of every ten companies which replied stated that they would not use such a program. That was exactly the same answer that the National Industrial Conference Board got, and it was exactly the same answer that the Wall Street Journal got.

Although the Senator from Oklahoma is one of the most successful businessmen in the country, I submit that these people, who have the responsibility of determining the capital investment plans of their own companies, understand their companies' plans even better than does the Senator from Oklahoma.

Mr. KERR. I think I understand them better than the Senator from Wisconsin does.

Mr. PROXMIRE. I am sure the Senator is endowed with ample self-confidence.

Mr. KERR. And the plans for 1962 were not made in the middle of 1962 or in the spring of 1962. The plans of these companies for their expansion in 1962 were made in 1960 or in 1961.

Mr. PROXMIRE. May I say to the Senator—

Mr. KERR. Just a minute. If any one of us is going to make a speech in my time, it is myself. I will answer the Senator's questions, but I will not yield any further for speeches.

As for the question the Senator from Wisconsin referred to, I do not know when they were asked it. But this investment credit was not then a reality. There are some conservative businessmen in this country who do not respond to that which is not in existence. They knew there was certain opposition to this investment credit last year. They knew there was strong opposition to it this year. Why would they respond to a stimulant which had not been provided at that time?

Mr. PROXMIRE. That was not the question—

Mr. KERR. The Senator from Wisconsin can speculate all he wants to. But the evidence the Senator from Oklahoma has is that industry—if and when this credit becomes the law and becomes available to industry—will respond. That is my conviction. The Senator from Wisconsin may have a different one. If he does, I am happy to have him tell the Senate so; but I am going to ask him to do it in his own time, not in my time.

(At this point Mr. PELL took the chair as Presiding Officer.)

Mr. PROXMIRE. Does the Senator from Oklahoma deny that the great business organizations and associations of the country came before the Finance Committee and opposed this windfall which business would thus receive?

Mr. KERR. Yes, I deny that—

Mr. PROXMIRE. Does the Senator from Oklahoma deny that they came before the committee?

Mr. KERR. No, I do not deny that they came before us.

Mr. PROXMIRE. Or that they opposed the investment credit?

Mr. KERR. I admit that some of them opposed it. But I deny that any of them opposed it as a windfall or that it is a windfall. When the Senator from Wisconsin includes the word "windfall" in his question, I answer in the negative.

Mr. PROXMIRE. But the Senator from Oklahoma does not deny that they opposed it?

Mr. KERR. There were some who opposed it, and they are as shortsighted as the Senator from Wisconsin.

Mr. PROXMIRE. Does the Senator from Oklahoma dispute that this investment credit would "sock" the budget for a \$1 billion or \$1.4 billion tax cut which the responsible business organizations oppose?

Mr. KERR. Well, Mr. President, that is a question of interpretation. The Government spends a couple of billion dollars a year in the development of water and soil resources. If one were so shortsighted as to look at only the budget for that year, he would consider that the budget had been "socked" for \$2 billion. But if he would look at what that \$2 billion expenditure would do, if he would look at vast areas in this country whose economies have been built up, following this kind of investment, and if he would see the tremendous inflow of taxes which comes to the Government from economies thus encouraged and thus provide a foundation for coming into existence and growing and expanding, he would have a concept of the situation similar to that which the Sen-

ator from Oklahoma has of this investment credit.

It is true that for the first full year the Treasury would lose in excess of \$1 billion current revenue. But, Mr. President, that will not be a loss. That will be an investment by this Government in a stronger base for growth and progress and greater prosperity. And on that foundation will develop a stronger economy. From that investment will come greater returns; and I hope I have the ability to look beyond the immediate moment, and to see what is out yonder that will come from so constructive a move as I regard this investment credit.

Mr. PROXMIRE. Then is the Senator from Oklahoma making the usual argument that if Government taxes are cut and reduced—although, according to the responsible businessmen, the stimulation of business which will result will be far less than the amount of the tax cut—the Government will, somehow, get back more than the amount of the tax cut? If so, why not eliminate or reduce all taxes, balance the budget and retire the national debt?

Mr. KERR. If the Senator has the intelligence I think he has, he understood what I said; and if he did not, he can read it in the Record, and he does not need to put an interpretation on it that was not given by the Senator from Oklahoma. The Senator from Oklahoma made a very clear statement that he believes this to be a sound Government policy whereby the Treasury would receive one billion and a quarter dollars less the first year, but thereby promote a greater growth, and a foundation for increased prosperity and increased tax revenue which in the long run will bring in far more for the economy than it would presently lose in revenue. That is what the Senator from Oklahoma believes. The Senator will not argue about it, but if the Senator from Wisconsin wants to ask another question, the Senator from Oklahoma will answer it.

Mr. PROXMIRE. I want to understand what the Senator said. So the Treasury will raise revenues by losing taxes?

Mr. KERR. The Senator heard what I said.

Mr. PROXMIRE. Is the Senator aware of the fact that the oil industry will get favored treatment because gas pipelines get a 7-percent investment credit, although I understand they are utilities regulated by the Federal Power Commission. Why the favoritism for the oil industry?

Mr. KERR. That shows the ignorance of the Senator from Wisconsin.

Mr. PROXMIRE. It is in the report.

Mr. KERR. The oil industry does not own any gas pipelines. They run from it as they would run from the plague. They got rid of them when the Supreme Court held that independent producers were utilities when they held gas pipelines. The oil companies do not own any interstate gas pipelines, because if they did they would become regulated utilities.

The 7 percent the Senator is talking about has nothing to do with oil companies. His reference to gas pipelines

instead is concerned with interstate gas transporters, who are public utilities, and who are under the regulation of the Federal Power Commission, which has without exception compelled the interstate gas pipeline carriers to pass on to the consumers any savings that they get by such a situation as a tax credit.

Mr. PROXMIRE. Would the Senator deny that the Phillips Co. puts gas into the pipelines and therefore would benefit from this kind of arrangement?

Mr. KERR. I guess the Senator from Wisconsin is an authority in the Phillips Petroleum Co. The Senator from Oklahoma is not, but he would make this little suggestion to the Senator from Wisconsin: If he would really like to know whether the Phillips Petroleum Co. is in interstate gas pipelines or not, he can find out from them. I would wager him a Coca-Cola that they do not own a foot of interstate gas pipeline.

Mr. PROXMIRE. But the fact is that the pipelines are regulated by the Federal Power Commission.

Mr. KERR. But they are not owned by the oil companies.

Mr. PROXMIRE. But they are regulated public utilities.

Mr. KERR. That is what I said.

Mr. PROXMIRE. Yet they get a 7-percent credit.

Mr. KERR. Not on interstate gas pipelines. They do not own them.

Mr. PROXMIRE. The pipelines, according to the committee report on page 155—

Mr. KERR. The Senator ought to read what is in the bill. Maybe he would know what he is talking about.

Mr. PROXMIRE. One has to read the report to find the interpretation of the bill. I read the bill.

Mr. KERR. The Senator ought to read one of them. There is not anything in the report that is not in the bill.

Mr. PROXMIRE. On page 155 of the report, next to the last sentence on the page reads:

Specific examples of qualifying property which normally would be used as an integral part of one of the specified activities are blast furnaces, oil and gas pipelines, and railroad tracks and signals.

This is the paragraph which refers to the 7-percent credit—oil and gas pipelines.

Mr. KERR. But the Senator did not say oil and gas pipelines. He asked me about gas pipelines.

Mr. PROXMIRE. Well—

Mr. KERR. Well.

Mr. PROXMIRE. Gas pipelines. Then I wish to discuss oil pipelines—

Mr. KERR. If the Senator knows anything about it, I will be glad to discuss it; if not, I will be glad to enlighten him.

Mr. PROXMIRE. I asked how the Senator justified the fact that gas and oil pipelines—

Mr. KERR. No. The Senator asked if the oil industry was not getting a windfall out of the 7-percent credit on gas pipelines. I said they are not because they do not own any.

Mr. PROXMIRE. Will not the gas pipelines get a windfall?

Mr. KERR. The gas pipelines will not, because any reduction they get they pass on to the consumers under the regulations of the Federal Power Commission. The consumers in Wisconsin will get the windfall.

Mr. PROXMIRE. Why do they not get the same treatment as any other utility that is regulated?

Mr. KERR. If the Senator from Wisconsin would look into it, he would find that gas interstate pipelines are regulated by the Federal Power Commission in Washington. He would find further that private utilities are regulated within the State where located.

Mr. PROXMIRE. I know that.

Mr. KERR. The Senator does not know that?

Mr. PROXMIRE. I do know that.

Mr. KERR. If the Senator does know that, he knows that the regulatory bodies in the States do not necessarily follow the same guidelines or formula of regulation that are followed by the Federal Power Commission, that the regulatory practices of the Federal Power Commission are not binding on State commissions, and that the regulatory practices of the State commissions are not binding on the Federal Power Commission.

Mr. PROXMIRE. Then why should not the gas pipelines get the same 3-percent investment credit that other regulated utilities get instead of a further preferential 7 percent?

Mr. KERR. In the first place, oil pipelines are not under the Federal Power Commission.

Mr. PROXMIRE. I know.

Mr. KERR. The Senator asked me a question, and I told him. I informed him, because I told him something he did not know, and I am happy to do that.

Mr. PROXMIRE. I thank the Senator from Oklahoma.

Mr. DOUGLAS. Mr. President, does the Senator from Oklahoma feel he has sufficient strength to answer a few questions which the Senator from Illinois would like to ask?

Mr. KERR. I will risk it.

Mr. DOUGLAS. Is the Senator from Oklahoma aware of the fact that the 7-percent credit is to be paid on all investment even though that investment is less than the actual depreciation upon the machinery and equipment?

Mr. KERR. I do not understand the question.

Mr. DOUGLAS. Suppose a company has a \$100,000 of depreciation but invests only \$70,000. Will it not receive a 7-percent credit on the \$70,000, or \$4,900 as a direct credit against its taxes, despite the fact that it is not actually physically meeting its depreciation costs?

Mr. KERR. If I understand the bill—

Mr. DOUGLAS. If the Senator knows the answer, I would appreciate his giving it to me.

Mr. KERR. If I understand it, I will give it.

Mr. DOUGLAS. Good.

Mr. KERR. And that will be in line with what the Senator from Oklahoma has always done.

Mr. DOUGLAS. That is correct.

Mr. KERR. If I understand the bill, it gives anyone making an investment in certain depreciable property a credit up to, but not exceeding, 7 percent against taxes, but there are very distinct limitations on the amount of credit that the taxpayer gets.

Mr. DOUGLAS. Now would the Senator answer my question, namely, is the Senator aware of the fact—

Mr. KERR. Will the Senator refer to the provision in the bill that he is asking about?

Mr. DOUGLAS. I am referring to the 7-percent credit.

Mr. KERR. Will he point it out in the bill?

Mr. DOUGLAS. The bill contains some 300 pages.

Mr. KERR. This part does not cover 300 pages.

Mr. DOUGLAS. The Senator from Oklahoma can give a direct answer to this question. There are various interlocked points in the bill. Is the Senator from Oklahoma aware of the fact that this 7-percent credit is to be given for all investment even though that investment is less than the actual depreciation upon the machinery and equipment? In other words, is the Senator aware that this tax credit is to be given for gross investment, and not net investment over and above depreciation?

Mr. KERR. It is on the gross investment the taxpayer makes in those items with reference to which the tax credit is applicable.

Mr. DOUGLAS. That is right.

Mr. KERR. That is correct.

Mr. DOUGLAS. That is correct; even though the gross investment were less than the depreciation.

Mr. KERR. That is correct.

Mr. DOUGLAS. I thank the Senator from Oklahoma. Is the Senator aware that this 7-percent credit would be given even though there were a decrease in the investment made, compared with previous years?

Mr. KERR. That is correct, but it would be applicable only to new investment.

Mr. DOUGLAS. That is correct. Now, is the Senator aware that this would be a very great difference from the original investment credit proposed by the administration and the Treasury Department, which was to be a 15-percent credit on net investment over and above 100 percent depreciation, plus a 6-percent allowance on the amount between 50 and 100 percent.

Mr. KERR. I would say this: I am not entirely familiar with all of the details of the original request by the administration. I am sure it is a matter of record. If the Senator wants to put it in the RECORD, he may do so.

I will say also that the Treasury Department has made it quite apparent that it is very much in favor of the passage of the bill with the investment credit provision which is to be provided.

Mr. DOUGLAS. I may say to my good friend, I had experts make an analysis of the progress of this bill.

Mr. KERR. Mr. President, I do not yield for a reading of the progress of the bill.

Mr. DOUGLAS. Would the Senator be willing to turn to pages 16700 and 16701 of the RECORD for yesterday, which lies on his desk? This is a question, as to whether the Senator would be willing to turn to those pages.

Mr. KERR. I am not willing to turn to them and to have the Senator from Illinois read to me. If the Senator wishes to read to the Senate—

Mr. DOUGLAS. I do not want to read. I want to ask a question.

Mr. KERR. If the Senator has a question, let us hear it.

Mr. DOUGLAS. Will the Senator tell me—as shown on page 16701—whether the original bill did not provide for a 15 percent credit on net investment over and above depreciation?

Mr. KERR. I rather think it did.

Mr. DOUGLAS. Yes.

Mr. KERR. I do not have to read what the Senator has there to know about it.

Mr. DOUGLAS. Fine. At first the Senator said he did not know about it.

Mr. KERR. I did not know what the question was.

Mr. DOUGLAS. I am glad he now does.

Mr. KERR. The Senator finally got around to asking a question.

Mr. DOUGLAS. Is the Senator aware that as this bill has gone through Congress it has been changed vitally from the original proposal by the administration?

Mr. KERR. There has been substantial change.

Mr. DOUGLAS. That is correct.

Mr. KERR. That was done by the Ways and Means Committee of the House and by the House of Representatives.

Mr. DOUGLAS. That is correct.

Mr. KERR. And by the Finance Committee of the Senate.

Mr. DOUGLAS. Is the Senator aware of the fact that—

Mr. KERR. Does the Senator from Illinois hold the Senator from Oklahoma responsible for that?

Mr. DOUGLAS. No.

Mr. KERR. I thank the Senator.

Mr. DOUGLAS. I merely wished to know whether the Senator was aware of it, that is all.

Is the Senator from Oklahoma aware of the fact that even though a business should reduce its investment from that of previous years it would still get a 7-percent tax credit on the investment which it made?

Mr. KERR. I believe I answered that question.

Mr. DOUGLAS. How did the Senator answer it?

Mr. KERR. If the Senator does not know he can read the RECORD tomorrow.

Mr. DOUGLAS. Does the Senator know how he answered it?

Mr. KERR. Yes; I know how I answered it.

Mr. DOUGLAS. How did the Senator answer it?

Mr. KERR. I answered it as I gave it.

Mr. DOUGLAS. Does the Senator—

Mr. KERR. And in that regard, with reference to the position of the Treasury Department, I will read to the Senator

from the report of the Committee on Finance, at page 10:

The Secretary of the Treasury in his appearance before your committee stated:

"The central element in the bill is the tax credit for investment in depreciable machinery and equipment."

At another point he said, with respect to the investment credit:

"This matter has top priority in the agenda for tax reform. As chief financial officer of the Nation, I do not lightly regard tax abatements on the scale proposed here. I urge this legislation because it will make a real addition to growth consistent with the principles of a free economy; because it will provide substantial help in alleviating our balance-of-payments problem, both by substantially increasing the relative attractiveness of domestic as compared with foreign investment and by helping to improve the competitive position of American industry in markets at home and abroad; and because, far from adding to the forces responsible for alternative recessions and recoveries, it will be of major assistance in strengthening our present recovery and enabling us to attain a higher rate of growth and sustained full employment. Early action will resolve uncertainty or hesitancy and begin at once a strong and lasting incentive for modernization of the productive facilities of our national economy."

Mr. DOUGLAS. Now, may I say, I admire—

Mr. KERR. I will say to the Senator from Illinois that that is the position of the Senator from Oklahoma.

Mr. DOUGLAS. I understand. Now will the Senator answer my question?

Mr. KERR. If the Senator from Illinois does not like this bill, he is at perfect liberty to offer any amendment he wishes to offer. If he favors the original administration proposal, he can offer it as a substitute for the provision recommended. If he is against this provision, he can fight it. But the Secretary of the Treasury in that statement made clear the position of the administration, and that is the position of the Senator from Oklahoma.

Mr. DOUGLAS. I admire the voice of the Senator from Oklahoma.

Mr. KERR. I thank the Senator.

Mr. DOUGLAS. And his stentorian presence. But now would the Senator from Oklahoma answer my question? Does the Senator realize that even though a firm should decrease its investment, it would still get the 7-percent credit on the gross investment which it would make?

Mr. KERR. Yes. I told the Senator that twice. I told the Senator that it was only with reference to the investment it made after the effective date of the bill, and not only if the firm makes a lesser investment, but also if it makes a greater investment.

Mr. DOUGLAS. Then how can it be said that this would stimulate investment, when it would reward a firm for making a lesser investment?

Mr. KERR. Well, I will say this to the Senator from Illinois: There are none so blind as those who refuse to see. It just might be, I say to the distinguished Senator, that without this provision, instead of making a lesser investment, the taxpayer might not make any investment. Had that ever occurred to the Senator as being possible?

Mr. DOUGLAS. It has never occurred in the past for American industry as a whole.

Mr. KERR. Oh, now—

Mr. DOUGLAS. American industry has made huge investments.

Mr. KERR. Who is the Senator to say what has never occurred in the minds of industrial investors since 1789?

Mr. DOUGLAS. I did not say that; it is always the Senator from Oklahoma who makes those judgments.

Mr. KERR. The Senator just made one, and I challenged it.

Mr. DOUGLAS. Is the Senator aware of the fact that there have been enormous investments in machinery and equipment by American industry in the past without the 7 percent credit?

Mr. KERR. Yes.

Mr. DOUGLAS. And that even though there were no increase in the investment, the firms would get the 7-percent credit in the future, under the proposal.

Mr. KERR. For the fourth time, the answer is "Yes."

Mr. DOUGLAS. Yes.

Mr. KERR. Yes.

Mr. DOUGLAS. And that in these cases it will amount to a complete windfall?

Mr. KERR. The answer to that is "No."

Mr. DOUGLAS. A windfall of hundreds of millions of dollars for investments that would have been made anyway, in the absence of the provision.

Mr. KERR. That is an argument, not a question.

Mr. DOUGLAS. Is the Senator aware of that fact?

Mr. KERR. I am aware.

Mr. DOUGLAS. Good. Is the Senator aware of that fact?

Mr. KERR. I am aware.

The answer to the Senator's question about it being a windfall is "No."

Regardless of how much information I give to my friend, I am compelled to observe that he is not always aware.

Mr. DOUGLAS. I am sure that the Senator from Oklahoma feels that, but I have the feeling that the Senator from Illinois may be aware of more things than the Senator from Oklahoma sometime is willing to give him credit for.

Mr. KERR. Then our self-adoration is probably on a par.

Mr. DOUGLAS. I would not like to think that was so.

Mr. KERR. I would not like to think it was not.

Mr. DOUGLAS. Will the Senator from Oklahoma come back to the point? Is the Senator aware of the fact that even though a firm made no increase in investment, even though there were a decrease—

Mr. KERR. One at a time.

Mr. DOUGLAS. Is the Senator aware of the fact that even though a firm made no increase in its investment the firm or the corporation would receive the 7-percent investment credit?

Mr. KERR. I have answered that in the affirmative four times. Now I am glad the Senator has asked it the fifth time, because I am going to qualify the answer.

Mr. DOUGLAS. Oh?

Mr. KERR. Because the 7 percent is not always the applicable figure.

Mr. DOUGLAS. That is the rough figure.

Mr. KERR. That is not always the accurate figure or the applicable figure.

The Senator from Oklahoma is aware that although a taxpayer might make no greater investment after the bill is enacted, and although an investor might make a smaller investment than he had previously made, before the effectiveness of the law, he still would get the applicable tax credit with reference to the investment he made. Now, that is the fifth time I have answered the question for the Senator.

Mr. DOUGLAS. That is fine.

Mr. KERR. If he were aware, it seems that it should break through his consciousness that I had answered it.

Mr. DOUGLAS. The Senator tried not to answer the question a number of times.

Mr. KERR. No. The Senator did not ask that question. He came over here with a bunch of insertions that he made, to which I did not pay any attention when he made them, and I have not paid any more attention to them today.

Mr. DOUGLAS. I want to know how the Senator can maintain that the proposal would be a stimulant to investment in cases in which the firm actually invests less than it did before, or would not invest the amount of the depreciation, or cases in which there is a net capital loss.

Mr. KERR. The Senator answered that question awhile ago when he told the Senator from Illinois that it was entirely possible that, without the stimulant, the firm might not make any investment.

Mr. DOUGLAS. What I have said is true of industry as a whole.

Mr. KERR. That is true of the situation to which the Senator from Oklahoma referred.

Mr. DOUGLAS. In industry as a whole about \$27 billion annually has been invested without the 7-percent credit.

Mr. KERR. The bill applies to individual taxpayers on the basis of the position of the taxpayer with reference to the law.

Mr. DOUGLAS. Does not the Senator think that in order to reach a small group of margin-of-decision firms, vast subsidies would be paid to firms which would make such investments anyway?

Mr. KERR. Will the Senator repeat his question?

Mr. DOUGLAS. Does not the Senator feel that in order to affect a few firms on the margin of decision, the 7-percent investment credit would be applied across the board to all firms, most of which would make investments anyway. Therefore would not the proposal constitute a bonus or windfall?

Mr. KERR. The Senator from Oklahoma does not any more agree that that is the way in which the bill would work than that the revised formula of depreciation would work that way. The Senator from Oklahoma thinks that both would stimulate increased investment by American investors, especially

in our industrial workshop. He thinks that is an objective devoutly to be hoped for.

Mr. DOUGLAS. Is the Senator from Oklahoma aware of the fact that last year the resources of American corporations increased by approximately \$43 billion, which came from depreciation funds?

Mr. KERR. From what?

Mr. DOUGLAS. And from profits, the sale of stocks, and the sale of bonds. The physical investment in industry during that time amounted, however, to only about \$31 billion; so the cash assets of corporations increased by approximately \$12 billion in a year. The corporations did not invest those cash balances in industry, but put them interest into Government bonds and securities. If they had those amounts of cash, why did they not invest them? Does the Senator think the added \$1,300 million yearly tax credit this bill provides would be put into investment, or would it increase the cash resources of corporations whose cash resources are already overflowing, and which would not invest in industry because they do not think there is sufficient effective consumer demand?

Mr. KERR. If the Senator from Illinois would confine himself to asking questions instead of making speeches, we could get along better. But if that is the way he wants to operate, it is all right.

Mr. DOUGLAS. I have been following a worthy example.

Mr. KERR. The Senator from Oklahoma does not know the exact figures with reference to the matters mentioned by the Senator from Illinois, but he does not dispute them. But as American industries did have \$12 billion in liquidating assets last year which they did not invest in increasing their efficiency and their productive capacity, it might well be because there was not adequate stimulant or encouragement for them to do so. If firms have adequate stimulant and encouragement, the Senator from Oklahoma contemplates the expenditure of portions of that amount, or perhaps all of it, by those companies to improve their competitive position and efficiency of operation, rather than investing the money in Government bonds. If the situation which the Senator from Illinois describes exists, it is an argument in favor of the proposed legislation rather than against it.

Mr. COOPER. Mr. President, will the Senator yield?

Mr. KERR. I yield to the Senator from Kentucky.

Mr. COOPER. I intervene with some reluctance in this joust between giants, but I believe the Senator from Illinois asked whether the Senator from Oklahoma was aware of the fact that if a company actually reduced its investment in plant—

Mr. KERR. No, he did not say that. He assumed that a company might make a smaller investment this year than last year. He assumed that it might make a smaller investment than it had planned.

Mr. COOPER. If that state of facts existed, the credit would be available.

Also companies might invest the same amount that they invested last year. Is it the conception of the chairman of the committee that, looking at the total of investments all over the country, regardless of the fact that one company might not invest as much as it did last year, or might even reduce its plans to invest this year, or might invest the same amount, the total investment of all companies would be increased throughout the country? Is that the argument of the Senator from Oklahoma?

Mr. KERR. That is the position, belief, and conviction of the Senator from Oklahoma.

Mr. COOPER. All of that, of course, must be based upon assumption. I know the Senator has developed the point before, but there must be some basic assumptions which leave the Senator and the committee—

Mr. KERR. A majority of the committee.

Mr. COOPER. Yes.

Mr. KERR. It was a divided committee on that provision.

Mr. COOPER. I understand. The point that I understand the Senator is making is that in the totality of investment made by all taxpayers, whatever changes might be made in some cases that would lower investment by a specific taxpayer or even keep the level the same as it was last year, the investment would be increased. The Senator's argument is that in considering the investments of companies all over the country, the Senator believes that the credit would increase the total of investments.

Mr. KERR. There is not the slightest question of doubt in the mind of the Senator from Oklahoma that what he has said is correct. The tax credit would be a stimulant to all industry. It would be a stimulant to marginal industries. It would be a stimulant to industries that have a larger cash flow than they have an investment program.

One of the amazing facts of our economy is that the spread between capital investment and cash flow is increasing and has been for some months—that is, the amount of cash flow available for investors is larger than the amount being invested.

Mr. DOUGLAS. It would increase the cash flow by diminishing the tax.

Mr. KERR. The Senator from Oklahoma thinks that the best possible way to reverse the trend and bring about a situation in which industry would increase its capital expenditures in more efficient facilities and more efficient capacities is to provide the proposed stimulant, because, as of now, in the judgment of the Senator from Oklahoma, companies do not have adequate encouragement to cause them to make the investment in a capital expenditure program that is required to enable us to achieve a position as a national industrial workshop equal to or superior to any other in the world.

Mr. DOUGLAS. Even though they receive that 7 percent on investments which they would make anyway?

Mr. KERR. Even though they receive that 7 percent on investments that they would make anyway.

Mr. DOUGLAS. Which would mean around \$27 billion.

Mr. KERR. Just as they get depreciation on investments that they would make anyway.

Mr. DOUGLAS. The depreciation is on investments which they made in the past.

Mr. KERR. And make this year, and that they would make anyway. Just as we would reduce the base on income that a person would get anyway. Just as we would say, "Let us reduce the corporate rate." We would reduce it on income they would have anyway. The Senator from Oklahoma does not think it is any crime for the Government to improve the economic environment of the American taxpayer.

Mr. DOUGLAS. Does the Senator—

Mr. KERR. Just a moment. The Senator from Oklahoma thinks that the power to tax is the power to destroy. The Senator from Oklahoma thinks the responsibility of government in fashioning its tax structure is one whereby it should do so on a basis that will be the most conducive to expansion and increase in efficiency and increase in productivity. Therefore, the Senator from Oklahoma favors what he believes to be a constructive measure.

Mr. DOUGLAS. Does the Senator from Oklahoma have a high opinion of the business judgment of the leaders of the American Telephone & Telegraph Co.?

Mr. KERR. I would rather not indulge in personalities, except as between me and the Senator from Illinois.

Mr. DOUGLAS. Does the Senator from Oklahoma have the same high opinion of the ability of the managers of A.T. & T. that the Senator from Illinois has?

Mr. KERR. The Senator from Oklahoma declines to indulge in personalities with respect to any industrial unit.

Mr. DOUGLAS. Is the Senator from Oklahoma aware of the fact that the representatives of A.T. & T. came before the committee and said that although they would get at least \$75 million of the investment credit, they thought it was immoral and they thought it was wrong and that it would not increase investments in the slightest, and that they urged the Senate to turn down this measure? Is the Senator aware of that fact?

Mr. KERR. No; he is not aware of that fact.

Mr. DOUGLAS. The Senator reads the RECORD, I am sure.

Mr. KERR. The Senator from Oklahoma denies it. The Senator from Oklahoma stood on this floor for 6 weeks, during which time he heard the Senator from Illinois describe A.T. & T. as a giant monopoly seeking to crush all competition.

Mr. DOUGLAS. No, no. I must rise to a point of personal privilege.

Mr. KERR. The Senator from Oklahoma is astounded to find that A.T. & T. officials have a new champion, upholding them for their high morality and their great judgment.

Mr. DOUGLAS. I rise to a point of personal privilege.

Mr. KERR. It seems to me that he would rather fashion facts to meet his argument instead of fitting his argument to the facts.

Mr. DOUGLAS. Since the Senator has quoted the Senator from Illinois, I would suggest that if he will examine the RECORD he will find that the only part I took in the debate on satellite communications was to ask certain questions of the Senators from Tennessee and, I believe, the Senator from Louisiana [Mr. LONG], for a very brief period. I was on the fence until I became convinced by the arguments of the two Senators from Tennessee and the Senator from Oregon [Mr. MORSE] and the Senator from Louisiana [Mr. LONG]. However, I do want to say—

Mr. KERR. Just a moment. I have the floor. I want to say that when the Senator got off the fence he surely did so as vigorously as anybody I ever saw get off a fence. I remember hearing him say he joined these greater fighters in their battle for righteousness.

Mr. DOUGLAS. At the end; that is right; that is correct.

Mr. KERR. I have never seen a man do so with greater zeal and more vigor and, I must say, with what appeared to be more enthusiasm and agreement than I have ever seen any man display.

Mr. DOUGLAS. In all this I made no reflection upon the officials of the A.T. & T. I make no reflection on the motives of the Senator from Oklahoma, with whom I have clashed for 12 long years.

Mr. KERR. For 14 years.

Mr. DOUGLAS. I believe it began in 1950, when he tried to jam the gas bill through.

Mr. KERR. And did.

Mr. DOUGLAS. And did; and we were saved by the veto of a President. Then the Senator tried to get at the Federal Power Commission.

Mr. KERR. I was not saved by the veto. The Senator from Illinois was.

Mr. DOUGLAS. I was saved by the veto; exactly so. Thank God we had a President in Harry Truman who vetoed that bill. Now if we may depart from history and come to the present—

Mr. KERR. Let us never depart from history, because even the present is history in the making.

Mr. DOUGLAS. Very good. Is not the Senator aware of the fact that officials of the A.T. & T. testified against the investment credit and said it was a windfall, and that even though it would give them \$75 to \$100 million, they were opposed and did not favor it? I appeal to the chairman to say if they did not so testify.

Mr. KERR. The Senator need not appeal to the chairman. If the Senator were to ask me the question whether I am aware of the fact that a, one, a single, representative of A.T. & T. appeared before the committee and opposed this feature of the bill, the answer is "yes."

Mr. DOUGLAS. I am glad the Senator admits it. He has retreated.

Mr. KERR. Not at all. I answered no to the Senator's question before because he put statements into the mouths of officials of A.T. & T. and asked me if

I did not know that they had said so and so. I said I did not know it.

Mr. DOUGLAS. Did they not state—

Mr. KERR. No.

Mr. DOUGLAS. The Senator does not know what I am asking.

Mr. KERR. He did. They did not.

Mr. DOUGLAS. I mean the man who appeared before the committee. Did he not represent A.T. & T.?

Mr. KERR. Yes; but the Senator said "they." "He" is singular not plural.

Mr. DOUGLAS. In other words, you imply he was not the representative of A.T. & T., although they sent him here. In other words, the medieval philosophers who calculated how many angels could dance on the point of a pin, have a successor in the Senator from Oklahoma.

Mr. KERR. When the Senator from Illinois knows not what else to say he refers to some memory he has of the classics or poetry, in which he takes refuge. I hope he may be happy.

Mr. DOUGLAS. I asked a specific question. I shall document it this afternoon. Did not a representative of A.T. & T. testify against the bill?

Mr. KERR. Stop right there.

Mr. DOUGLAS. No; I will not stop. Did he not—

Mr. KERR. I will yield no further. If the Senator asks whether a representative appeared in opposition to this provision, the answer is "Yes."

Mr. DOUGLAS. May I ask the next question?

Mr. KERR. This is the first time the Senator from Illinois has asked the Senator from Oklahoma if a representative appeared.

Mr. DOUGLAS. Was he not the representative of A.T. & T.?

Mr. KERR. He was the one, so far as I know, who came before the committee, but he was still singular.

Mr. DOUGLAS. Did he not say that A.T. & T. did not want the \$75 million?

Mr. KERR. I told the Senator he appeared in opposition to the bill. I do not know what he said. It is in the record. If the Senator wants to spend the afternoon reading it, he may do so.

Mr. DOUGLAS. We will find it.

Mr. KERR. The Senator from Oklahoma does not let an A.T. & T. representative make up his mind. He tries to make up his own mind.

Mr. DOUGLAS. The Senator would give them \$75 million even though they do not want it.

Mr. KERR. I want the Senator from Illinois to make up his mind too.

Mr. DOUGLAS. I try to.

Mr. KERR. The Senator from Illinois says he said it and, therefore, I should accept it. I am not persuaded to do something because someone has said it. I make up my own mind.

Mr. DOUGLAS. There is a good deal of contrasuggestion there.

Mr. KERR. Contra what?

Mr. DOUGLAS. Suggestion.

Mr. KERR. I misunderstood the last part of the Senator's statement.

Mr. DOUGLAS. The Senator from Oklahoma is not as unfamiliar with the

English language as he pretends to be.

Mr. KERR. I did not say I was unfamiliar with it. I merely did not hear what the Senator said. I was sure it could not be what I thought the Senator said. I got the "contra" part, and the rest was not clear.

Mr. DOUGLAS. We will meet again at Philippi.

Mr. KERR. I hope we will meet in Washington before that.

Mr. LAUSCHE. Mr. President, will the Senator yield?

Mr. KERR. I yield.

Mr. LAUSCHE. In the minority views, filed by the Senator from Virginia [Mr. BYRD] and other Senators, it is stated that the U.S. Chamber of Commerce, the National Manufacturers Association, the AFL-CIO, the American Farm Bureau Federation, and the Farmers Union are opposed to the bill through testimony or letters. I should like to know if that is the fact.

Mr. KERR. I must say to my good friend from Ohio that my regard for the veracity and accuracy of the chairman of this committee is such that I would endorse the factual attributes of any statement that he made.

The Senator from Ohio need never ask me if a statement made by that great man is accurate.

Mr. LAUSCHE. It delights me to hear the Senator from Oklahoma make that statement, because I hold him in that same high esteem. I do not mean to imply that their positions ought to be determinative.

Mr. KERR. I never knew the Senator from Ohio to let anyone else prescribe his position; and certainly the Senator from Oklahoma does not.

Mr. LAUSCHE. Neither do I intend to. However, it is a consideration that must be given in trying to evaluate the relative arguments made on the subject.

Mr. KERR. The Senator from Ohio may be influenced by such considerations as he desires and believes are justified. That is a right which every Senator has, a right which I would not take away from him if I could, and could not if I would.

Mr. LAUSCHE. I may say that while the discussions have grown a bit sharp and hot, they have been very informative to those who have been listening, and at times very entertaining.

Mr. KERR. Oh, they have been informative even to those who have participated.

Mr. LAUSCHE. I thank the Senator.

Mr. KERR. Mr. President, I yield the floor.

Mr. GORE. Mr. President, will the Senator from Oklahoma yield?

Mr. KERR. Oh, with pleasure; for a question.

Mr. GORE. In connection with the liquidity position of the U.S. corporations—

Mr. KERR. Would the Senator from Tennessee use language I can understand?

Would a page bring me a dictionary? I should like to answer the Senator's question, but I should like to have him

use the English language with which I am familiar.

Mr. GORE. Very well. In reference to the cash position—

Mr. KERR. Oh, I know what that is.

Mr. GORE. I daresay better than any other Member of the Senate.

Mr. KERR. No, but well enough.

Mr. GORE. Is the Senator from Oklahoma aware that U.S. corporations in the year 1961 increased or bettered their cash position by approximately \$12 billion?

Mr. KERR. The Senator from Oklahoma will not need the dictionary now. The Senator from Tennessee has stated his question in language I can understand.

The Senator from Oklahoma, in answer to a question by the Senator from Illinois [Mr. DOUGLAS], said that he had not been aware that that was the fact, but that if the Senator from Illinois stated it as a fact, the Senator from Oklahoma would accept it as a fact; and the Senator from Oklahoma certainly has equal respect for the Senator from Tennessee. So the Senator from Tennessee may proceed with his questions on the assumption that the Senator from Oklahoma has taken his word and the word of the Senator from Illinois to the effect that that is the fact.

Mr. GORE. Would the Senator from Oklahoma permit me to give him those particular facts?

Mr. KERR. I thought the Senator had already given them to me. He gave the figure \$12 billion in his question.

Mr. GORE. I wish to elucidate.

Mr. KERR. If the Senator wishes to elucidate, why does he not wait until I take my seat? If he wishes to ask me a question, why does he not ask me a question?

Mr. GORE. I should like very much to give the Senator the benefit—

Mr. KERR. Do not go beyond that. Did they have less or more than that?

Mr. GORE. In 1961, corporations acquired \$43,100 million of corporate funds, but invested only \$31,300 million in plant, equipment, and increased inventory.

Mr. KERR. The Senator has weakened his position, because that does not leave a net of \$12 billion.

Mr. GORE. I deducted \$31 billion from \$43 billion.

Mr. KERR. But the Senator gave the figures as \$43.1 billion and \$31.3 billion.

Mr. GORE. The Senator from Oklahoma is correct; the difference is \$11.8 billion.

Mr. KERR. If we are to insist on accuracy, let us indulge it.

Mr. GORE. I was not attempting to split hairs; I was trying to round off a figure.

Mr. KERR. Two hundred million dollars would be quite a sizable hair.

Mr. GORE. I was trying to round the figure in general terms.

American corporations were \$12 billion better off in their cash and liquid assets position at the end of 1961 than at the beginning of 1961.

I should like to read to the Senator from Oklahoma what Mr. McElroy, a

leading businessman and former Secretary of Defense, said.

Mr. KERR. The Senator from Oklahoma is not interested in what Mr. McElroy said. If the Senator from Tennessee has a question, I will yield to him to ask it. If he wishes to ask it, I will answer it. If he does not, I will take my seat.

Mr. GORE. Would the Senator from Oklahoma be willing to express his agreement or disagreement with a—

Mr. KERR. No; I told the Senator from Illinois [Mr. DOUGLAS] I did not wish to indulge in personalities. The Senator from Tennessee can have a position without putting it in someone else's words.

Mr. GORE. Is the Senator from Oklahoma aware that this leading businessman stated to the Committee on Ways and Means—

Mr. KERR. The Senator from Oklahoma is not interested in what a leading businessman said to the Committee on Ways and Means. If the Senator from Tennessee has a question, I will yield for it; if he does not, I will yield the floor.

Mr. GORE. I have a question.

Mr. KERR. Let us have it.

Mr. GORE. How does the Senator maintain that U.S. corporations, which have steadily increased and bettered their cash position, in a way yet undefined will be encouraged to spend vast amounts of money in improved plant and facility because they are given a little tax subsidy that would but further increase their cash position?

Mr. KERR. I am glad the Senator asked a question and brought in the last phrase, "a little." The way this discussion has been taking place for some time, the Senator from Oklahoma thought the Senator from Tennessee thought it was an awfully big one.

I believe the Senator from Tennessee was in the Chamber when the Senator from Illinois asked the identical question. I shall give the Senator from Tennessee the identical answer.

Mr. GORE. I was not in the Chamber when the question was asked.

Mr. KERR. Then I shall give the identical answer anyway.

Mr. GORE. Good.

Mr. KERR. The Senator from Oklahoma, in answer to that question from the Senator from Illinois, said this: If it is a fact that American business corporations increased their liquid assets in 1961 by approximately \$12 billion and kept them liquid, rather than investing them in improved or more efficient machinery and facilities, in the judgment of the Senator from Oklahoma it was because they did not think they could do so and make a greater profit than they could get by using that cash to invest in Government bonds or some other low-yield securities.

The Senator from Oklahoma thinks it is the business of Government, if possible, to improve the environment in which these industries operate, so that they will be encouraged to invest their money in improved plant and facilities, in more efficient facilities, because that is the objective we seek first by the Treasury's

new depreciation formula, and second by the tax credit.

What the Senator from Tennessee has stated as the basis for his question would indicate that the expansion of American industry had slowed down; that its cash flow exceeded its investments and the expenditures to improve productivity, efficiency, and competitive position. The Senator from Oklahoma thinks they should be encouraged to spend their money to improve their productivity, their efficiency, and their competitive position, rather than to hoard it or to invest it in Government bonds.

The Senator from Tennessee will remember the parable of the talents, in which the master had three servants, to one of whom he gave five talents, to another of whom he gave two talents, and to the third, one talent, and then he departed on a journey.

When he returned, he got a report. The first servant said, "You gave me five talents. I used them. Here are the five talents you gave me and five in addition." That servant was appropriately rewarded.

The second servant said, "You gave me two talents. Here are the two, and another two besides, which I have acquired by using the two you gave me." And that servant was appropriately commended and rewarded.

Then the servant to whom the master had given one talent came in and said, "I knew you were a hard taskmaster; that you gathered where you had not sown. I was afraid. So I took the talent and buried it; I hoarded it." That servant was discharged as an unfaithful servant.

I think this Government in handling the development of the tax environment of our industry should arrange it so that industry does not want to hoard its liquid assets, except what is necessary to maintain a safe reserve. I think the Government should provide a tax structure which will encourage industry to do that which the servant who had the five talents and the servant who had the two talents did—namely, go out and use them to increase what they had, for the benefit of themselves and for the benefit of their masters.

I do not believe we should maintain an environment which will make business want to hoard its assets and bring about the situation which the Senator from Tennessee and the Senator from Illinois have described.

Mr. GORE. But the amendment the Senator from Oklahoma supports would increase the amount hoarded.

Mr. KERR. No; the Senator from Tennessee is very much mistaken. He knows so little about the response of industry to a stimulant. When we increase the profitability of investment, make it possible for businesses to acquire more productive facilities at less cost, we stimulate them to improve their equipment, to increase their efficiency, and to expand their productivity.

Mr. GORE. I agree—

Mr. KERR. Well, that is where I stand on this amendment and on this bill.

Mr. GORE. The great stimulus for investment lies in the hope of a profit from that investment, not in the hope of a tax subsidy, not in the hope of a gimmick, such as this, to increase the board of the particular segments of industry that are in a position to take advantage of it.

If we increase the demand in this country for consumer goods, if we stimulate the economy to provide full employment, thereby developing a climate in which industries can make investments with the hope and the confidence and the expectation of earning profits, rather a tax subsidy, then the economy will be stimulated a thousand times more than it would be by a device such as this one. I am glad the Senator from Oklahoma has put his finger on a fundamental economic fact.

Mr. KERR. Well, if I did, I was not aware of it; and I do not think the Senator from Tennessee would be any more aware of it.

I interpret the result of this amendment differently from the way my good friend, the Senator from Tennessee, does. I think if we reduce the cost of productive machinery, we encourage the taxpayers to build it. I think if we make the tax environment more profitable for a taxpayer, he may respond by making a greater effort. As I said yesterday, I do not regard this amendment as a subsidy. I do not regard a reduction in tax as a subsidy. I do not regard—

Mr. GORE. The Senator from Oklahoma called this just what it is.

Mr. KERR. I did not interrupt the Senator from Tennessee when he asked questions or made a speech.

Mr. GORE. Very well; go ahead.

Mr. KERR. I do not regard any tax reduction as a subsidy. First of all, I think the Government should reduce its taxes whenever it can operate at less expense and thereby make it possible to reduce taxes. I think the Government should reduce its taxes whenever it is justified in believing that by so doing it will bring about a more dynamic economy. If I did not, I would not have helped to bring about the elimination of the excess-profits tax. We had that tax during World War II and during the Korean war; but as soon as we reached the point where we could remove that awful burden from the back of our industry, we did so.

I believe that with the enactment of this tax investment credit, encouragement will be given to American industry to expand, to be able to compete more effectively for the markets at home and abroad. And I say to the Senator from Tennessee that if it does, more jobs will be provided.

I do not want the Government to have to provide jobs. I want full employment just as much as the Senator from Tennessee or any other Senator does. But I want it in a free economy. I want it on the basis of employment by free, private competitive enterprise. I want it on the basis of having our Government make it possible to encourage the expansion of industry. Thereby, more jobs will be created. Thereby, our industry will be able to compete more effectively

for the domestic market. Thereby, more jobs will be provided. Thereby, our industry will find it possible to compete more effectively in the markets of the world. Thereby, more jobs can be created and employment can be increased; and perhaps we shall then reach—on the basis of a free, competitive enterprise economy—the happy objective of full employment.

Mr. GORE. Mr. President, will the Senator from Oklahoma yield?

Mr. KERR. I yield for a question.

Mr. GORE. Will the Senator from Oklahoma yield for a comment?

Mr. KERR. No. If the Senator from Tennessee wishes to make a comment, I shall sit down.

Mr. MORSE. Mr. President, I am going to raise a point of order. I do not like to raise a point of order against two such dear friends as the Senators who now are occupying the floor; but I wish to raise the point of order that there must be no failure to follow the rule that a Senator who has the floor can yield only for a question.

The PRESIDING OFFICER (Mr. BURDICK in the chair). Such a point of order will be sustained. A Senator who has the floor can yield only for a question.

Mr. GORE. Mr. President, will the Senator from Oklahoma yield for a question?

Mr. KERR. I yield for a question.

Mr. GORE. In making the reference, as the distinguished Senator from Oklahoma did, to the need for increasing production facilities, did the Senator from Oklahoma have clearly in mind that the problem with which we are plagued now is the existence of idle production facilities? Did he have clearly in mind that what the country needs is sufficient stimulation of the economy to put to use the production facilities we already have, and thereby increase the possibility of improvement and expansion of those production facilities?

Mr. KERR. I think we shall put our present production facilities into full use or into fuller use and more efficient productive facilities into fuller use if industry in this country has production facilities which will enable it to compete more effectively for the domestic market and for the world market.

I know there is idle industrial capacity. I also know that there are billions of dollars of imports of commodities produced by industrial facilities in other countries, owned by nationals of those countries and owned to some extent by Americans who have gone to those countries to build productive facilities. I know that that migration of industry has brought about the situation whereby we have idle machines in this country. And I want to stop that migration of American industries to other shores and other countries. I want to bring about a condition whereby the idle machines we have, augmented by more efficient ones than can be built, will enable American industries to compete more effectively for our domestic market and for the world market. And I think this amendment is the way to do it.

I recognize the right of the Senator from Tennessee to disagree. I am not

offended by that disagreement. I do not think it is a reflection on the Senator from Tennessee that I do not agree with him, nor do I think it a reflection on me that the Senator from Tennessee does not agree with me. There is that difference of opinion between us. It is a clear-cut and simple one, but a distinct one; and that is all there is to this.

Mr. GORE. Mr. President, will the Senator from Oklahoma yield for a question?

Mr. KERR. Yes.

Mr. GORE. A moment ago, when the Senator from Oklahoma referred to tax reduction, was he aware that in the opinion of the junior Senator from Tennessee he was accurately characterizing the so-called investment credit? I think it is nothing more than a thinly veiled tax reduction for the segments of industry which can take advantage of the so-called investment credit.

Mr. KERR. I was not aware that the Senator from Tennessee believed it was a tax reduction, because I have heard the Senator from Tennessee refer to it as a "subsidy"; and I have heard the Senator from Tennessee refer to it today as a "subsidy."

I am glad to know that the Senator from Tennessee acknowledges that it is a tax reduction. That is what the Senator from Oklahoma believes it to be, but the Senator from Oklahoma knows that under the provisions of the bill it is available only to those taxpayers who comply with this provision and spend certain sums of money on their plant facilities and depreciable property, and the Senator from Oklahoma thinks if they are going to spend it, they are going to spend it on more modern and efficient plant facilities and equipment.

Mr. GORE. Does the Senator know that as the result of a survey conducted by McGraw-Hill on a large number of industrial establishments the report was made that if the investment credit provision were enacted, an increase of only 1 percent in planned investment in plant facilities would be made as a result?

Mr. KERR. The Senator from Tennessee has addressed to the Senator from Oklahoma nearly the same question that the Senator from Wisconsin asked, but the Senator from Wisconsin said the McGraw-Hill survey stated it found that the investment credit would bring an increase of only 1 percent in 1962. It may be that the Senator from Tennessee refers to a different McGraw-Hill survey. I do not know. It may be that if the Senator from Tennessee is referring to the same one referred to by the Senator from Wisconsin, it was with reference to the year 1962.

Mr. GORE. I believe the Senator from Oklahoma in quoting the junior Senator from Wisconsin has quoted him more accurately than the Senator from Tennessee stated. If I said 1963—

Mr. KERR. The Senator did not say 1963. He left it open. He asked me if I was aware of the fact that McGraw-Hill said that enactment of this law would bring about only an increase of 1 percent in investment by American industry.

Mr. GORE. This year.

Mr. KERR. Ah now, I took the word of the Senator from Wisconsin for that. I take the word of the Senator from Tennessee for it. I answered the question of the Senator from Wisconsin. I answer the Senator from Tennessee the same way, that investment credit was talked about all last year, and has been talked about all this year. I know, and I think the Senator from Tennessee does, that business does not respond to a stimulant that is talked about but does not exist. How could American business sometime in 1962 respond to a stimulant not yet in existence and with reference to which they do not know whether it will come into existence or not?

The Senator from Oklahoma answered the Senator from Wisconsin by saying that plans for expansion for 1962 by American industry were made in 1960 and 1961; and certainly to go around now asking, "How much are you going to do this year in connection with this proposal?" would fail to bring about an accurate response or an accurate picture of the long-term effect of this legislation.

Mr. GORE. Will the Senator yield for a question?

Mr. KERR. Yes.

Mr. GORE. Then why, I ask the Senator, does he give it to them this year?

Mr. KERR. I say this, Mr. President—

Mr. GORE. The Senator has just explained here in detail—

Mr. KERR. The Senator asked me a question. Why does he not let me answer? The Senator from Oregon [Mr. MORSE] will make a point of order if the Senator does not let me answer the question.

Mr. GORE. Very well.

Mr. KERR. This bill was introduced last year in the House. They wrestled with it for nearly as long as Jacob wrestled with the angel, and left it probably in the same impaired condition. I do not know. I know that the Senate Finance Committee was wrestling with it all of this year. It came from the House with an effective date of January 1, 1962. It was the amendment of the Senator from Oklahoma, after he had wrestled with the Senator from Tennessee for months, and saw it could not possibly become effective until after the midpart of the year, that made it effective after the middle of 1962. I say if the Senator continues his wrestling until the year is over and we do not enact it until next year, the Senator from Oklahoma will be in favor of starting it in 1963. There must be an effective date if we are to have an effective piece of legislation.

The Senator from Tennessee and other Senators could wrestle and wrestle and wrestle here throughout the spring, and the summer, and the fall, and even until the foliage is in sere and yellow leaf, before we could enact legislation; but to do so we must have an effective date. The Senator from Tennessee is not trying to change the effective date; he is trying to destroy the provision. He is trying to eliminate it.

Mr. GORE. Correct.

Mr. KERR. If he fails in that effort, I hope he will not be too unhappy if those who prevail fix an effective date.

Mr. GORE. Then the Senator maintains that even though it will not, and by the rules of business which he knows so well would not and could not—

Mr. MORSE. Mr. President, I raise the point of order that the Senator from Tennessee is out of order.

Mr. GORE. I am stating a question.

Mr. KERR. I think the Senator has the right to make a point of order. I have asked the Senator from Tennessee to ask questions. I would like to have the Chair make a ruling.

The PRESIDING OFFICER. The Senator from Oklahoma has the floor and he may yield only for a question.

Mr. GORE. Does the Senator yield for a question?

Mr. KERR. I yield for a question.

Mr. GORE. Well, the Senator maintains, does he not—

Mr. KERR. Well, the Senator maintains. I will answer that part of the question, and I hope successfully.

Mr. GORE. The Senator's maintenance against all logic—

Mr. KERR. Oh, I want to say I know the Senator from Tennessee had none, pointing at himself. I did not think he would talk about it on this floor. I do not claim—

The PRESIDING OFFICER. The Senator can yield only for a question.

Mr. KERR. Well, I do not have to yield to myself for a question. I yield to myself for an observation.

I want to say, sir, I do not attempt to deny logic to the Senator from Tennessee, nor can I concede or agree with the inference or statement that he alone possesses it.

Mr. GORE. Now will the Senator yield for a question?

Mr. KERR. Yes.

Mr. GORE. In maintaining that even though the investment credit could not, and under the laws and practices of economics and business would not, result in any substantial increase in investment either in 1962 or 1963, does he not go straight into the face of a statement to the contrary, that this is not a tax reduction in the nature of a windfall?

Mr. KERR. The answer to the Senator's question, is "No." The Senator from Oklahoma believes that even if the effect of this bill were to be limited to 1 percent or less this year—

Mr. GORE. Will the Senator—

Mr. KERR. He will not.

Mr. GORE. Will the Senator let me correct that statement?

Mr. KERR. No. If the Senator asked a question, I want to answer it. I do not want the Senator to get into the clutches of a point of order. [Laughter.]

The Senator from Oklahoma acknowledged the statement of the Senator from Tennessee that McGraw-Hill indicated a fact, not that the Senator from Oklahoma agreed to it, and answered his question on the assumption that it was correct. He did not thereby state it was correct, or maintain it was correct. The review or survey, which the Senator finally admitted when the Senator from

Oklahoma corrected him, was with reference to the year 1962, not with reference to the year 1963.

The Senator from Oklahoma maintains that this cannot be effective until it is enacted; that if and when it is enacted it will have an effect immediately, and more so each year thereafter. Therefore, the Senator from Oklahoma says that in his judgment the effect would be far greater in 1963 than in 1962, and that it would be greater in 1964 than in 1963. That is the belief and the conviction of the Senator from Oklahoma. It is not binding on the Senator from Tennessee. I am aware of the fact that it is persuasive with the Senator.

Mr. GORE. Is the Senator aware that the survey by the National Industrial Conference Board of 1,000 leading industrial establishments showed an anticipated increase in outlay of only 1 percent for 1963?

Mr. KERR. No. The Senator from Oklahoma is not aware of that. What outfit was that?

Mr. GORE. The National Industrial Conference Board.

Mr. KERR. Mr. President, I suppose the Senator from Oklahoma will have to live out his life in his unenlightened condition. I do not have the benefit of the surveys of these organizations to which the Senator from Tennessee refers, nor am I bound by them. I must say to the Presiding Officer and to the Senators present that I have struggled and managed to get along pretty well thus far without being sustained by their surveys, advice, and counsel, or their prescription for my Senatorial action and behavior.

I am glad to know the source of those of the Senator from Tennessee. But I was not aware of them. Believe me, I was not. I hope the Senator will not hold it against me.

Mr. GORE. Would the Senator be affected in his opinion by additional facts which could be brought to bear upon this subject, or is he fixed in his opinion?

Mr. KERR. I am pretty well fixed in my opinion, but, I must say, no more so than is the Senator from Tennessee.

I would hope I would never become either impervious to or unconscious or allergic to fact.

I wish to say that I have been amazed at the absence of them on the part of many people.

Mr. GORE. Did the Senator hear, in the testimony before the Senate Finance Committee, the president of American Electric Power Co., Inc., say that a 7-percent tax credit would mean for his company, with respect to plans already made and which would be carried out whether the bill is passed or not, a 30-percent reduction in that company's taxes?

Mr. KERR. The Senator from Oklahoma heard the testimony of Mr. Donald Cook of the American Electric Power Co., Inc. I did know he was the president of it. I will take the Senator's word for that.

What greatly impressed the Senator from Oklahoma about the testimony of Mr. Cook was that he said that the enactment of the law would bring about

a great stimulation of construction and expansion of productive facilities by his corporation, and that it would pass on to its customers every penny of benefit it got out of the application of the tax credit.

Therefore, if the Senator is making his position on the basis of the testimony of Mr. Cook of the American Electric Power Co., Inc., he will have to abandon his statement that this would constitute a windfall, because that distinguished gentleman said two things. First, he said that this would cause his company to increase the development of its facilities, to speed up the expansion of construction and development, and to make services available to more people at an earlier date. Second, he said it would result in passing on to the consumers every dollar saved by reason of the operation of the law.

If that is true—and I have no reason to doubt it—it would not be a windfall to the corporation but it would be a benefit to the economy of the area in which the corporation operates and to every consumer it serves.

Mr. GORE. The Senator would not mind, would he, if the junior Senator from Tennessee took with a grain of salt the prospective benefits to American consumers from the investment credit provision?

Mr. KERR. The Senator from Oklahoma does not care what the Senator from Tennessee takes with his intellectual diet. The Senator would say not to take too much, because the Senator from Oklahoma remembers what happened to the wife and daughter of a certain Biblical character who took too much salt.

Mr. GORE. Mr. President, will the Senator yield for one final question?

Mr. KERR. The Senator would yield for a question even if it were not a final question, to his good friend from Tennessee.

Mr. GORE. If it be true, as Mr. Donald Cook testified, that a 7-percent investment tax credit for American Electric Power Co., Inc., would result in a 30-percent reduction in taxes, what, in the informed and enlightened opinion of the distinguished senior Senator from Oklahoma, would a 7-percent tax credit for gas and oil pipelines mean by way of tax reduction for gas and oil pipelines?

Mr. KERR. The Senator from Oklahoma does not have the answer to that question. As he has so definitely made clear on this floor, they are entirely different in operation.

The Senator from Tennessee is aware of the fact that interstate pipelines owned by interstate carriers are subject to the regulatory control of the Federal Power Commission, whose record has demonstrated clearly that it compels these interstate carriers to pass on to their consumers all the savings that they make.

With reference to the testimony of the distinguished Mr. Cook, of American Electric Power Co., Inc., I regret the last observation the Senator from Tennessee made about him. The Senator from

Oklahoma was a country lawyer for many years, and one of the first things he learned about the practice of law was that a lawyer could not impeach the testimony of his own witness nor question the veracity of his own witness. I am sorry that the Senator from Tennessee did that with reference to the statement by the distinguished Mr. Cook, whereby he sought to establish a fact by him in one regard and then made the statement that he took with a grain of salt—which I would interpret to mean a good deal of doubt—the other statements by the witness whose testimony he himself brought into the discussion.

Mr. GORE. Mr. President, will the Senator yield for the next final question?

Mr. KERR. Ah, Mr. President, I knew that would not be the last question. I yield for a question.

Mr. GORE. And this will be the last question. If the gas and oil pipelines and electric utilities are going to pass on to the consumers the benefits they receive under the bill, how, then, will those utilities be stimulated to invest more money?

Mr. KERR. Well, I remember, Mr. President, when Mr. Cook was before the committee he made the statement that this credit would result in expanded construction by his corporation, increased service to his consumer customers, and an increase in the base of the industrial development of the area he served. He said it would make that possible and at the same time would make it possible for him to pass on to his consumers the savings which came to him by reason of the application of the credit.

Now, if the Senator from Tennessee does not believe it, or does not understand it as it was so ably given to him by Mr. Cook, who was speaking with reference to his own company and his own operation, I doubt if the Senator from Oklahoma would have the ability to explain it to the Senator from Tennessee in such a way as to make it more easily understood.

But even though I did make it so crystal clear that the Senator from Tennessee understood and believed it, there is great doubt in my mind that he would vote for that provision in the bill.

THE BILLIE SOL ESTES CASE—ATTACKS UPON UNDER SECRETARY OF AGRICULTURE CHARLES S. MURPHY

Mr. MORSE. Mr. President, for some time past I have read in the newspapers, by way of trial by newspaper, criticisms, innuendoes, and attacks upon the Under Secretary of Agriculture Charles S. Murphy relative to the Billie Sol Estes case.

I wish to say at the very outset of the statement I am about to make that I do not know what the facts are in connection with the Billie Sol Estes case with respect to any relationships that anyone in the Department of Agriculture may have had with him, including the Under Secretary of Agriculture, Charles S. Murphy.

I share the point of view that the evidence is pretty clear that Billie Sol Estes

has polluted the stream of good government, that he has performed a great disservice to himself, to his family, and to any government officials, who may have unfortunately come under his corrupt influence.

When I have great confidence in a man, based upon years of friendship with him and an opportunity to observe him in many official relationships during my years in the Senate, I do not walk out on him and run for cover when he is subjected to trial by newspaper. For me the test of friendship, in part, arises when a friend is under attack. One should then make known what he knows about that friend.

This does not mean that when one makes known what he knows about a friend, he therefore underwrites anything about which he does not know. Nor does it mean that any proof or solid evidence which may be developed ought be ignored.

But I wish to say, as I make my comments about the Under Secretary of Agriculture today, that all my experiences with Mr. Murphy over the years have led me to believe that I have been dealing with a fine Christian gentleman of great integrity, of dedication to the public service, and of complete honesty in carrying out the obligations of whatever government post he has held.

In the capacity of a character witness this afternoon on the floor of the Senate, I wish to make that statement about the Under Secretary of Agriculture, Charles S. Murphy. I am glad that at long last he will have an opportunity to testify in person today before an appropriate Senate committee which is looking into the Billie Sol Estes case.

But I think Mr. Murphy is due from those who have been closely associated with him in various official relationships the statement that I now make. I believe that Charles S. Murphy is an honest man of great integrity. He has served his country in post after post in a dedicated fashion. It may very well be that by negligence or oversight he has made some mistake, although I doubt it. But I shall follow where the facts lead in that respect, as I seek to follow where the facts lead in respect to all issues which come before me in the Senate.

I know Charles S. Murphy. I know the great services he rendered the people of our country and this Government during the war. I know of his services under the Truman administration.

When I saw in newspapers the many innuendoes and snide attacks upon him which would be best characterized as smear tactics that are commonplace in American journalism, I proceeded to make such inquiry as I could in regard to Charles S. Murphy. I satisfied myself that unless there is some evidence of which I have not been made aware, Charles S. Murphy has been victimized in recent weeks. I do not stand by in silence when I feel that a wrong may be done to a friend.

Mr. President, I wrote a letter to a group of mutual friends of Mr. Murphy. I shall read a copy of that letter:

Under Secretary of Agriculture Charles S. Murphy is a longtime personal friend of mine. His record of dedicated honest public service has been outstanding. However, I am concerned about the impression which may have been created as a result of his name being drawn into the discussion of the Billie Sol Estes case.

Therefore, I shall appreciate it if you will send me very promptly for public use on the floor of the Senate, if it becomes necessary for me to make a speech in his defense, your evaluation of him and his service as Under Secretary of Agriculture.

With kind personal regards,

Sincerely yours,

WAYNE MORSE.

For the next few minutes I propose to discuss some of the replies which I received to my letter. First, I should like to put into the RECORD some biographical material in regard to Mr. Murphy as an individual and in his capacity as a public servant.

CHARLES S. MURPHY

Charles S. Murphy is the No. 2 man in the administration of the Department of Agriculture, and has a general supervisory function for all its activities and agencies. These agencies include the Agricultural Stabilization and Conservation Service and 15 others.

In addition to the general supervisory functions, he has been assigned special responsibilities.

He has direct supervision of the Foreign Agricultural Service. This includes responsibility for the Department's activities in maintaining and expanding sales of U.S. agricultural commodities in foreign markets as well as administration of a major part of the food-for-peace program under Public Law 480.

Mr. Murphy is chairman of the Budget Committee of the Department of Agriculture and President of the Commodity Credit Corporation.

He has been assigned special responsibility for supervising the commodity programs of the Department. This includes fixing support prices and acreage allotments for tobacco, rice, peanuts, cotton, wheat, feed grains, and other commodities. It also includes policies relating to management and disposition of Government stocks of agricultural commodities, and the purchase and distribution of commodities for the school lunch program as well as the direct distribution program for providing foods to needy persons.

Under Secretary Murphy coordinates and reviews the Department's staff work on major legislative proposals and reviews all departmental reports on legislation, of which there are about 800 each year.

He is a member, and usually acts as chairman, of the Program Review Board of the Department and also supervises its extensive civil defense activities.

He reviews all marketing orders and marketing order amendments before they are issued. There are several hundred of these each year.

Mr. Murphy is the Department's representative on the Trade Policy Committee, which is the Cabinet committee responsible for making recommendations to the President on foreign trade matters.

He serves as Acting Secretary in the absence of the Secretary of Agriculture.

Mr. Murphy is a former special counsel to President Harry S. Truman. He also is a former assistant legislative counsel to the Senate, and in this position specialized in drafting agricultural legislation.

Since 1953 he has practiced law in Washington, D.C. His residence is Annapolis, Md.

Mr. Murphy was born August 20, 1909, in Wallace, N.C., where he attended public schools. He received an A.B. degree from

Duke University at Durham, N.C., in 1931 and an LL.B. in 1934. He worked his way through school as a laborer and clerk in the post office. He was admitted to the North Carolina bar in 1934.

In 1934 he became a law assistant in the Office of the U.S. Senate Legislative Counsel, serving in this post for 2 years. For the next 11 years he was assistant legislative counsel to the Senate.

His duties were to help Senators and senatorial committees draft bills and committee reports, and to advise them on legal matters.

Many of us who served in the Senate during the tenure of Charles Murphy as legislative counsel know what an able lawyer he is and know what a dedicated servant he is to the public weal. I am sure many in the Senate share my very high appraisal of this fine man.

As a specialist in agricultural legislation he helped draft the Agricultural Adjustment Act of 1938, prepared committee reports on agriculture, and assisted in the drafting of other important farm bills.

In 1947 he became administrative assistant to President Truman. In 1950 he was advanced to the position of special counsel to the President, where he acted as the principal staff assistant on legislation—including farm legislation.

Since 1953 Mr. Murphy has practiced law as a member of the Washington, D.C., firm of Morison Murphy, Clapp & Abrams. He was admitted to the Supreme Court bar in 1944 and to the District of Columbia bar in 1947. From 1957 to 1960 he was counsel to the Democratic National Advisory Council.

Mr. BURDICK. Mr. President, will the Senator yield?

Mr. MORSE. I yield.

Mr. BURDICK. I wish to say that I, too, have known Charlie Murphy since the days of the Truman administration. I have known him as an able lawyer and able administrator, and as a man of unimpeachable integrity. I am happy this afternoon to associate myself with the remarks of the Senator from Oregon.

Mr. MORSE. I thank the Senator from North Dakota very much. The Senator comes from a great agricultural State. He is one of the great leaders in the Senate and in the solution of agricultural problems. He is familiar with the agricultural record of Charles Murphy. I am not surprised, but I am certainly pleased to know that he shares my evaluation of Mr. Murphy.

During the 1960 national campaign he was an adviser to Senator LYNDON B. JOHNSON, now Vice President.

Mr. Murphy operates a 750-acre farm—with tobacco as the principal crop—near Durham, N.C., with a brother, R. B. Murphy, who lives on the farm and manages it.

The Under Secretary is a member of the American Bar Association, the North Carolina Bar Association, the Federal Bar Association, and the District of Columbia Bar Association. From 1956 to 1958 he was president of the National Capital Democratic Club. He also belongs to the Order of Coif, which is the honorary scholastic fraternity of the legal profession in standard law schools of the country; Delta Sigma Phi; Pi Gamma Mu; and Omicron Delta Kappa.

Mr. Murphy married Kate Chestney Graham, of Durham, N.C., in 1931. They have three children. One daughter, Courtenay, is married to Whitney

Slater and lives in Arlington, Va. Westbrook, their 20-year-old son, is a junior at Duke University. Another daughter, Betty, 12, lives at home. She attends Annapolis Junior High School.

Mr. President, in the last few months there has been considerable comment in the press concerning Mr. Murphy. On August 24 he issued the following statement in regard to some of these press stories. I quote that statement, as follows:

In the past few days, there has been considerable comment in the press concerning my part in the handling of the business of the Department of Agriculture relating to the affairs of Billie Sol Estes, now under investigation by the Senate Committee on Government Operations. On July 3, 1962, I requested an opportunity to appear and testify before the committee on this matter. I am sure that opportunity will be accorded to me in time, and that principles of fairness and justice will preclude any conclusions or judgments until I have had that opportunity.

All of the matters which I dealt with concerning Estes came to me in the normal course of my duties as Under Secretary of Agriculture. I dealt with all of them strictly on the merits as I saw them. No pressures or improper influences had any effect on my decisions. When this case came to my attention in the fall of 1961, it was extremely complex and difficult under the legal and administrative law principles involved. It was handled by me solely with the twofold objective of protecting the interest of the Government and affording fair and equitable consideration to the rights of private citizens. It is the essence of free, democratic government that the rights of every citizen be protected.

I believe the record shows that, notwithstanding the difficulties, we did succeed in accomplishing our objective of fully protecting the interest of the Government while giving due consideration to the rights to which all citizens are entitled.

Mr. President, as I said, I do not purport to know what may have transpired in the Department of Agriculture, in any office, including Mr. Murphy's, or in any other, with regard to the Billie Sol Estes case. However, I certainly would not be able to live with my conscience seeing a friend of mine under the type of attack which Mr. Murphy has been subjected to in the recent past, if I remained silent for any reason, including the possibility that speaking out in defense of a friend might ultimately result in some kind of reflection upon me, because he might conceivably be found guilty of some sort of negligence.

I speak today, when public opinion eyes will be focused on Mr. Murphy as he testifies before the Senate committee, because, in my judgment, a friend stands up for a friend when he is satisfied that his association with that friend justifies the kind of high opinion and esteem that I have for the integrity of Mr. Murphy. I am glad that others share my point of view concerning the character and integrity and the devoted public service of Mr. Murphy.

Yesterday I had a rather long long-distance telephone conversation with one of the great Americans of our history, a former President of the United States, the incomparable Harry S. Truman. We talked about Mr. Murphy. I paraphrase him, but accurately, when I

say that ex-President Truman authorized me to say on the floor of the Senate this afternoon that he knows Charles Murphy to be an honest man through and through. That, of course, is typical Truman language. He went on to discuss the great services that Charles Murphy rendered to him in his White House appointment capacity when he was President of the United States. He left no room for doubt in my conversation with him yesterday of his complete confidence in the honesty, integrity, and character of Charles S. Murphy.

One of the letters that I wrote—they were identical in composition and I have already read it into the RECORD—was one addressed to Mr. Herschel D. Newsom, master of the National Grange. I have the following reply from him:

HON. WAYNE L. MORSE,
U.S. Senate:

We are happy to know that you intend to express in the Senate your confidence in Under Secretary of Agriculture Charles S. Murphy. Counsel of National Grange and I have known Charlie Murphy for many years both in and out of public office as an able, sincere, and conscientious lawyer and administrator of unimpeachable integrity. We believe that he is serving our farmers and all of our people well and faithfully as Under Secretary of Agriculture and that you are to be commended for bringing this fact to the attention of the Senate.

HERSCHEL D. NEWSOM,
Master of the National Grange.

Mr. President, I received a reply from Alexander Nunn, of the Progressive Farmer, which reads as follows:

I have worked rather closely with Charles Murphy for the last 2 years. I have found him completely honest, fairminded, and alert—a thoroughly dedicated public servant. He has an invaluable background of experience combined with good judgment. He inspires confidence and teamwork. We cannot afford to lose him from Agriculture.

ALEXANDER NUNN,
Executive Editor, Progressive Farmer.

Mr. President, I also have another communication from Alexander Nunn, executive editor of the Progressive Farmer. The letter is dated August 27, 1962, and is a copy of a letter which he wrote to a colleague in the Senate. However, Mr. Nunn authorized me to read the contents of the letter. I shall not read the name of the colleague unless at a later hour he authorizes the use of his name.

Mr. ERVIN. Mr. President, will the Senator from Oregon yield?

Mr. MORSE. I yield.

Mr. ERVIN. I do not know whether the Senator is referring to me or not. This morning I received a letter from Mr. Harry B. Caldwell, of my State of North Carolina, concerning Charlie Murphy. I do not know whether I am the Senator to whom the Senator from Oregon has referred.

Mr. MORSE. Not in this letter. I do have a copy of the letter to which the Senator from North Carolina refers. I was about to refer to the other letter, but without using the Senator's name.

Mr. ERVIN. If the Senator from Oregon is referring to me, he is at perfect liberty to use my name.

Mr. MORSE. I would expect that courtesy from the Senator from North

I wish to commend the Senator from Oregon for what he has said in Mr. Murphy's behalf. I have been privileged to know Mr. Murphy, who is a native of my State, for many years. I do not know of any human being who possesses a higher degree of integrity than does he.

Mr. MORSE. Mr. President, I thank the Senator from North Carolina for his great testimonial—for it can properly be so characterized. It has come from a Member of the Senate who probably is in the best position to say what he has said, because not only does he know Mr. Murphy as one of the two North Carolina Senators, and not only has he had many associations with Mr. Murphy in North Carolina relationships, but, in addition, the Senator from North Carolina is a former justice of the North Carolina Supreme Court, and he knows what due process is, and he is familiar with the requirements of fair procedure. Not only has he expressed his personal opinion in regard to the character and the dedicated public service of Mr. Murphy, but the Senator from North Carolina has also given here on the floor of the Senate an unanswerable legal opinion, in my judgment, because what he has said as a member of the committee itself is that Mr. Murphy has insisted upon a fair hearing and has insisted upon the application of the principles of due process in connection with the consideration of the Billie Sol Estes case, as he would in connection with the consideration of any other case.

It all adds up to the fact that we simply must insist that all the facts are before us before any judgment is rendered. This is the very essence of judicial process in this country. If those who render decisions did not insist on that kind of implementation in the administration of justice, then, Mr. President, you and I would not have any legal rights, because whenever those in positions of decision do not carry out, as the Senator from North Carolina [Mr. ERVIN] has so clearly implied and stated here this afternoon, the guarantees of due process, then we are rightless people. We have lost the rights so cherished and precious to freemen.

I want to thank the Senator from North Carolina [Mr. ERVIN] from the very bottom of my heart for doing what any of us who know him would expect him to do—to have the courage to stand up here this afternoon to bespeak his keen concern over what has been said about Mr. Murphy and his relations to Billie Sol Estes.

I yield now to the Senator from Minnesota [Mr. HUMPHREY] with the same understanding that I do not lose my right to the floor.

Mr. HUMPHREY. Mr. President, first, I wish to commend the Senator from North Carolina for what I consider to be one of the most profound statements with respect to due process and justice under law that I have heard in this body. I think the RECORD should note that two of our most experienced legal minds in the Senate have taken the position that Mr. Murphy has acted

within what we call due process of law and administrative procedures in the actions that are now under investigation.

I also wish to say that I have known Mr. Murphy for a number of years as a friend, as a Government official, and as a lawyer. His record is without blemish. He has demonstrated through years of public service a faithfulness to public duty which should commend him to anyone.

There is a tendency these days in American public life to make a judgment before the evidence is in. As the Senator from Oregon and the Senator from North Carolina have pointed out, Mr. Murphy has not had a chance to defend himself against charges and counter charges, many of which contradict themselves, leaving Mr. Murphy as the sort of fall guy, or as they say in the vernacular, holding the bag.

I only hope, before a judgment is rendered, one who has given so many years to public life, and has taken on so many responsibilities in two administrations, will have a chance to be heard and show his record, word, and performance.

Every one of us has called upon administrative officers to review cases for constituents. Do not forget that, I cannot help but express a note of concern that administrative officers who are asked, at the request of Senators or Representatives, to do something, may later be accused of having given a special privilege or favor, when there was no such desire on the part of either the Member of Congress or the administrative officer. I have had citizens from my State come to my office. I do not have a chance to give them a political blood test, or run them through a test of morals and character. If they come in as responsible citizens so far as I know, and ask me to do something for them that seems to be within the spirit and intent of the law, I pick up the telephone, call up the appropriate officer, and ask, in my name as a Senator of the United States, if something can be done. If those officers do not give us at least a friendly response, we are the first to criticize them. If they look into the question and try to ascertain whether or not something can be done, and later on we find the constituents were unworthy or were crooks or were violating the law at least in spirit, we point at the administrative officer.

I think we ought to recognize that we all share the burdens and responsibilities of government, and it is not fair to single out a man, before he has been heard, for any unfair condemnation or treatment.

I make this statement after hearing two Senators speak for Mr. Murphy. I did not know his name was going to be mentioned. I have been disturbed over the fact that his name has been mentioned in the press, and he has not been given a chance to reply. Perhaps he now will be given a chance.

I express my respect to the able Senator from Oregon for his willingness to speak out in this matter, and to the Senator from North Carolina, who is a member of the committee that heard some of the evidence. The Senator from

North Carolina is a jurist second to none, and as a lawyer he has a sense of fair play. Their testimony means much to me, and I know it will to Mr. Murphy.

Mr. MORSE. I thank the Senator very much for the statement he has made. I expected it of him. I appreciate it. I am sure it has greatly strengthened the record I am seeking to make here this afternoon.

Mr. President, I have two more letters I wish to read, and then will yield the floor. I express my appreciation to the Senator from Nevada [Mr. CANNON] and the Senator from Virginia [Mr. BYRD] for their cooperation in making it possible for me to make this statement.

The next letter is one also in reply to my letter of August 22. It is dated August 27, 1962, and reads as follows:

NATIONAL COUNCIL OF FARMER CO-OPERATIVES,
Washington, D.C., August 27, 1962.
Hon. WAYNE MORSE,
U.S. Senate,
Washington, D.C.

DEAR SENATOR MORSE: I have discussed your letter of August 22 with leaders in our organization who feel that we should heed Mr. Murphy's own appeal that no conclusions be drawn with respect to his official action in the Estes case until he has been heard.

I feel this is a wise admonition and one which is in line with our mutual friend's being willing to let the facts speak for themselves.

Kindest personal regards,
Sincerely,
HOMER L. BRINKLEY,
Executive Vice President.

My last letter, one I received from Claude R. Wickard, former Administrator of REA, and recognized as one of the great agricultural leaders of our time and our century, reads as follows:

DEAR SENATOR: As a member of President Kennedy's National Agricultural Advisory Commission, I have been in a good position to observe the outstanding public service of the Honorable Charles S. Murphy in his position as Under Secretary of Agriculture. He is performing the duties of this office with efficiency, effectiveness, courtesy, and in keeping with the highest ethics.

His service is exactly the kind to be expected from a man of great ability, a deep sense of responsibility of public office, and the highest integrity.

In acknowledgement of your own honorable record of public service and with very best wishes, I am,

Most sincerely yours,
CLAUDE R. WICKARD.

I took these few moments today to make this statement in behalf of Mr. Murphy out of my sincere friendship for him, as I said at the beginning, my personal knowledge of his record in many official capacities, and my satisfaction of his dedication to the public interest. I did it because, finding a friend in whom I had the confidence that I have in Mr. Murphy, under the type of public attack being made, I could do no less.

I want to say, as I close, I will sleep better tonight with my conscience than I would have if I had hesitated or failed to speak out when a friend is under attack.

Mr. SPARKMAN and Mr. CARROLL addressed the Chair.

Mr. MORSE. I yield first to the Senator from Alabama. Then I will yield to the Senator from Colorado.

Mr. SPARKMAN. I commend the Senator from Oregon for speaking as he has. I have followed the press reports from time to time. I often wondered when Charlie Murphy was going to be given an opportunity to answer these charges.

I have known Charlie Murphy for a great many years. I have known him to be a man of ability, a man dedicated to whatever work he undertakes.

I understand the Senator has put some letters into the RECORD.

Mr. MORSE. May I interrupt the Senator a moment? The Senator was not in the Chamber, and I said that I was going to put in the RECORD a copy of a letter which was sent to a colleague of mine, but because I had not had an opportunity to talk to that colleague I was omitting his name from the RECORD. I am ahead of the Senator, I think. I believe he is about to refer to the letter. The letter is in the RECORD, but the Senator's name was not used in connection with it, because I would not deal with my colleagues in that way.

Mr. SPARKMAN. I was going to ask the Senator to permit that letter to go into the RECORD, because it is a fine letter. I am not sure the Senator identified the writer.

Mr. MORSE. Yes, I identified the writer. I think the letter ought to be in the RECORD now, offered by the Senator from Alabama, himself. My previous reading of it, I believe, should stand, because I made certain comments at the time I read it, but I would appreciate it very much if the Senator would insert the letter in the RECORD at this point.

Mr. SPARKMAN. The letter to me was from Alexander Nunn, who is the executive editor of the *Progressive Farmer*. The *Progressive Farmer* is one of the leading farm publications. It is one of the best farm publications in the entire United States.

Mr. Nunn, who is a friend of mine, a citizen of my State, has written a very strong letter to me. I presume that is the letter the Senator put in the RECORD.

Mr. MORSE. Yes.

Mr. SPARKMAN. Did the Senator put in the RECORD a copy of the letter which the editor of the *Progressive Farmer* wrote to the President?

Mr. MORSE. Yes. I put that letter in, too.

Mr. SPARKMAN. I am glad the Senator did.

I should like to read one sentence, for I think it is significant.

We believe that Secretary Freeman and his associates are doing more than any other USDA team in our lifetime to fight skillfully and effectively the battles of working farmers.

The letter is signed by the entire editorial board of the *Progressive Farmer*.

Mr. MORSE. I thank the Senator from Alabama very much. I appreciate his statement. I hope he will understand why I did not use his name heretofore, since I did not have his permission to do so.

Mr. SPARKMAN. That is very fine. I am glad the Senator put the letters in the RECORD.

Mr. CARROLL. Mr. President, will the Senator yield?

Mr. MORSE. Mr. President, I yield to the Senator from Colorado with the understanding that I shall not lose my right to the floor by so doing, although I will seek to give up the floor as soon as I can.

Mr. CARROLL. Mr. President, I rise also to commend the able Senator from Oregon. I have not heard his full presentation about Charles Murphy, but I assume he has been discussing the background of Charles Murphy. I believe he, years ago, was a legislative draftsman for the U.S. Senate.

Mr. MORSE. He was assistant general counsel in our legislative drafting service.

Mr. CARROLL. That was my impression. Some 10 years ago I first knew Charles Murphy intimately, when he was a special counsel for President Truman. I can say without hesitation or equivocation that I have never met a more conscientious public servant. He was a quiet and studious scholar, on the legislative side of the President. He was not, as we used to say in those days, on the political side of the White House, rather he was on the counseling side, the legislative drafting side. He was a quiet, unassuming, intelligent man, a dedicated public servant of excellent character and integrity.

I, too, have wondered, as I have read the articles in the newspapers, when Charles Murphy would be given an opportunity to be heard, to present his side of the case. I am happy to be able to say that as I walked through the corridors toward the Senate Chamber today I accidentally met the chairman of the permanent Subcommittee on Investigations [Mr. McCLELLAN] and I asked, "When is Charles Murphy going to be given an opportunity to testify?" He said, "This afternoon. There is one other witness to appear before him, and Charles Murphy will be second." I have forgotten the name of the first witness.

Mr. MORSE. I have pointed that out.

Mr. CARROLL. I am happy that the Senator from Oregon has done so.

I wish to associate myself with the Senator's remarks. I think this is the time to speak. When we find men we know to be dedicated public servants, we should try to help lay the foundation; to help pave the way for a fair hearing, so that they may present their testimony fully. They should not be prejudged, but should be given a fair opportunity to present their side of the matter.

I join with the Senator from Oregon in this presentation, which he has made in his usual courageous fashion.

Mr. MORSE. I thank the Senator from Colorado very much. He states my case more eloquently than I can myself.

Mr. President, I yield the floor.

provide a credit for investment in certain depreciable property, to eliminate certain defects and inequities, and for other purposes.

Mr. BYRD of Virginia. Mr. President, it is the understanding of the Senator from Virginia that it is in order to offer an amendment to the pending bill to strike the investment tax credit provision, and that such an amendment will be the pending question. I offer the amendment on behalf of myself and other Senators.

The PRESIDING OFFICER (Mr. HICKEY in the chair). The amendment will be stated for the information of the Senate.

The LEGISLATIVE CLERK. On page 8, beginning with line 8, it is proposed to strike out all through line 16 on page 38.

Mr. BYRD of Virginia. Mr. President, I have already discussed this amendment at length. I will make a very brief additional statement.

I wish to state again that I am opposed to the investment credit because it is discriminatory, because its value and its need as a stimulant to the so-called economic growth are both questionable and doubtful, and because it would substantially increase the budget deficit.

Since the bill passed the House, the administration has issued regulations substantially expediting depreciation deductions. This, it is estimated, will lose \$1.5 billion of tax revenue. The investment credit would reduce the revenue by \$1.2 billion, thus making a total of \$2.7 billion, all of which, as it now appears, probably would be added to the public debt.

For the first time in my nearly 30 years of membership on the Senate Committee on Finance, I have found it necessary to present individual views on a bill reported by the committee. In those individual views I was joined by the Senator from Tennessee [Mr. GORE], the Senator from Delaware [Mr. WILLIAMS], and the Senator from Nebraska [Mr. CURTIS].

Mr. SALTONSTALL. Mr. President, will the Senator yield for a question?

Mr. BYRD of Virginia. I yield.

Mr. SALTONSTALL. The Senator used the word "discriminatory." Could the Senator go into that a little more fully? I have in mind particularly the question in regard to a firm, let us say, which needed to enlarge its building a little further to improve its facilities, which, as I understand it, would not be given any benefit, although a firm which had the bricks and mortar but needed a new machine would get benefit of the provision, even though the two firms might be competing against each other.

Mr. BYRD of Virginia. The Senator from Massachusetts is correct to a certain extent. This provision would not apply to buildings. It would apply only to equipment and machinery. It would be discriminatory in the sense that some companies would install machinery and other companies, perhaps, would not. That would make it discriminatory.

It would be discriminatory in another respect. That is, if no profits were made by a company, then the company could

REVENUE ACT OF 1962

The Senate resumed the consideration of the bill (H.R. 10650) to amend the Internal Revenue Code of 1954 to

not take the tax credit. In my judgment, it would be to the advantage of the big companies, of the wealthy companies, which usually have a profit on which to take the tax credit. The struggling, smaller companies might not have a profit. In that event, they would not get one cent from the investment tax credit provision.

Mr. SALTONSTALL. Then the Senator's opposition to this business incentive, so-called, is because he feels it would not be fair, because it would bring about a great reduction in the revenues of the Government, and because in his opinion it would not bring a business incentive.

Mr. BYRD of Virginia. That covers one of the objections. Another objection is that it is another "gadget" to be added to our tax laws.

The Senator from Virginia thinks that the best encouragement is provided by the regular depreciation base as it now exists. This is better than going into another method—a tax credit—which, as the Senator from Massachusetts knows, is entirely different from a tax deduction through depreciation.

I think what the businessmen desire, so far as I can ascertain their desire—incidentally, practically all of the big business organizations opposed this tax credit provision—is liberalization of the regular depreciation schedule and then, if possible, a reduction of the corporation income tax rate. They do not wish for us to go into a new field which would be applicable, I would say, only to a minority of corporations.

Mr. SALTONSTALL. And the new provision, if put into force, would be very difficult to administer fairly, because of the various questions involved, as to what would come within the provision and what would not.

Mr. BYRD of Virginia. I think that is correct, although it is confined to machinery and equipment. For example, slot machines and gambling devices would come under that provision. After going into the question very thoroughly, I did something which, as I have said, I have never done in 30 years. I thought the proposal was so important, since it would lead into another field, that with three other members of the Senate Finance Committee I brought in minority views against the position of the committee. The investment credit provision was adopted in the committee by a vote of 10 to 7.

Mr. SALTONSTALL. As the Senator brought out, the proposal might be discriminatory. It would not be fair, because it would not give everyone the same treatment.

Mr. BYRD of Virginia. The provision would not apply equally. My dear friend the Senator from Oklahoma [Mr. KERR], said that the provision was not a subsidy. I say that it would be a subsidy because one would obtain a certain benefit for doing a certain thing. It would be just as much a subsidy as payments to farmers for not planting. Businessmen would be required to do a certain thing in order to get the special benefit, whether it is called subsidy or something else. I do not think that is the right course.

Furthermore, if the provision were applied to machinery and equipment, I think it would have to apply also to buildings, because it is not logical that a businessman or a corporation should put new machinery into an antiquated building. If the provision were applied to buildings, it would add another \$500 million to \$800 million to the deficit.

Mr. SALTONSTALL. From our point of view in Massachusetts, the provision would seem to me not to be fair. I hope I am correct. Many of our buildings are old. Many of our buildings would have to be remodeled in order to be useful for the installation of new machinery. If I read the amendment correctly, the provision would not help those industries at all.

Mr. BYRD of Virginia. It would not help the company in reference to the building at all.

Mr. SALTONSTALL. I thank the Senator.

Mr. GORE. Mr. President, will the Senator yield?

Mr. BYRD of Virginia. I yield.

Mr. GORE. The Senator has referred to the proposal as a new "gimmick" in a tax law. I think that is a point that has not been sufficiently emphasized. Does not the proposal in fact provide a credit directly against, not taxable income, but against taxes owed?

Mr. BYRD of Virginia. It would be a credit against taxes owed. In other words, it would not be a deduction. It would be a tax credit. After a corporation or a businessman ascertained what he owed, he would receive a credit against his tax. It would be entirely different from the deduction under the regular system of depreciation.

Mr. GORE. That is why the Senator calls the proposal a gimmick. It is not an ordinary provision by which taxable income is determined.

Mr. BYRD of Virginia. As the Senator from Tennessee brought out when I first presented the question in the minority views, under the House bill it would result in giving a 114-percent deduction. This is because the investment credit is taken on income taxed at a rate of up to 52 percent. It would amount to twice as much as a regular expense deduction.

Mr. GORE. In other words, the provision would give to those fortunate enough to take advantage of it a deduction of more than 100 percent of the amounts contained herein.

Mr. BYRD of Virginia. The Senator is correct.

Mr. GORE. Was there not ample testimony before our committee that the cash position of American corporations was unusually good—in fact, better than at any other time in our history?

Mr. BYRD of Virginia. I think it was. The Senator from Tennessee brought out the fact that the U.S. Chamber of Commerce, the National Association of Manufacturers, the American Farm Bureau, and the Farmers Union were among the opponents of the measure. The AFL-CIO representative made one of the most masterly presentations against the proposal of all the witnesses who appeared.

Mr. GORE. If there is a need for more production facilities—and the cash

position of American business is now the best in history—how can we assume that if by the proposed tax reduction, tax subsidy, tax benefit, windfall, or whatever we wish to call it, we should improve their cash positions, the result would be a vast amount of investment in plant?

Mr. BYRD of Virginia. I do not think we can. I do not think that will be the deciding factor. If a company receives 7 percent credit to put in new machinery a businessman would be very unwise to make that controlling point. He must have need for the machinery. If he has need for it, he can put it in and take off in his tax return the regular depreciation, which has now been substantially expedited.

Mr. GORE. Is it not the fact that the recent liberalization in the depreciation schedules made depreciation as rapid as anyone could realistically advocate?

Mr. BYRD of Virginia. I think so. We shall lose \$1,500 million in 1 year. The amount will probably increase as the years go by.

Mr. GORE. In order to summarize, I ask the Senator if we have a great deal of idle plant capacity and unused production facilities now, if there is ample cash reserves in American business to build whatever new plant and facilities economic conditions will justify, and if the depreciation schedules have been revised within the past few weeks so as to be as generous as anyone has ever advocated, so far as I know, what justification is there to pile on top of the generous depreciation and cash reserves the proposed \$1,300 million windfall to those in a position to take advantage of it?

Mr. BYRD of Virginia. I do not see any justification for it. The Senator from Tennessee and I have frequently discussed the point. The action we took in bringing in minority views was not taken without due study. I repeat that it was the first time in 30 years that I have submitted minority views.

What disturbs me is that the big giants of the industry, that always have a profit, could take the tax credit. But the struggling young industries which are trying to compete with the giants frequently do not make a profit, and therefore they could not deduct the credit. It would be a dead loss for such companies.

Mr. GORE. What justification is there for providing a 7-percent tax credit to gas and oil pipeline utilities that are regulated and that are assured by the regulations of a reasonable return on investment?

Mr. BYRD of Virginia. I do not see any justification.

MESSAGE FROM THE HOUSE

A message from the House of Representatives, by Mr. Maurer, one of its reading clerks, announced that the House had passed the bill (S. 3327) to make certain federally impacted areas eligible for assistance under the public facility loan program, with amendments, in which it requested the concurrence of the Senate.

The message also announced that the House had passed the following bills and joint resolution, in which it requested the concurrence of the Senate:

H.R. 11099. An act to amend the Public Health Service Act to provide for the establishment of an Institute of Child Health and Human Development, and for other purposes;

H.R. 12577. An act to place authority over the trust powers of national banks in the Comptroller of the Currency;

H.R. 12628. An act to provide additional funds under section 202(a)(4) of the Housing Act of 1959, and to amend title V of the Housing Act of 1949, in order to provide low and moderate cost housing, both urban and rural, for the elderly;

H.R. 12899. An act to amend section 5155 of the Revised Statutes relating to bank branches which may be retained upon conversion or consolidation or merger; and

H.J. Res. 864. Joint resolution making continuing appropriations for the fiscal year 1963, and for other purposes.

HOUSE BILLS AND JOINT RESOLUTION REFERRED

The following bills and joint resolution were severally read twice by their titles and referred, as indicated:

H.R. 11099. An act to amend the Public Health Service Act to provide for the establishment of an Institute of Child Health and Human Development, and for other purposes; to the Committee on Labor and Public Welfare.

H.R. 12577. An act to place authority over the trust powers of national banks in the Comptroller of the Currency;

H.R. 12628. An act to provide additional funds under section 202(a)(4) of the Housing Act of 1959, and to amend title V of the Housing Act of 1949, in order to provide low and moderate cost housing, both urban and rural, for the elderly;

H.R. 12899. An act to amend section 5155 of the Revised Statutes relating to bank branches which may be retained upon conversion or consolidation or merger; to the Committee on Banking and Currency.

H.J. Res. 864. Joint resolution making continuing appropriations for the fiscal year 1963, and for other purposes; to the Committee on Appropriations.

Subsequently, Mr. HAYDEN, from the Committee on Appropriations, reported favorably, without amendment, the above joint resolution, and submitted a report (No. 1978) thereon, which report was ordered to be printed, and the joint resolution placed on the calendar.

THE NEED FOR A CENSUS OF ENGINEERS AND SCIENTISTS

Mr. CANNON. Mr. President, several times during the past few months I have addressed the Members of this body on a subject that I consider to be of critical importance to the national security—the continuing shortage of scientists and engineers.

Recently available statistics on the enrollment and graduation of engineering students in our colleges and universities have not only borne out the seriousness of this problem, they have shown that the situation is continuing to worsen.

For example, recent studies made by the Engineering Manpower Commission estimated that the proportion of engineering students among incoming fresh-

men—which has been steadily dropping—would continue to drop, probably below 7 percent. Data now available from the Office of Education show the actual figure to be 6.6 percent.

In absolute figures, the number of freshmen enrolled in engineering in 1961 stood at almost the same number that enrolled in 1960, roughly 67,500. The number of engineers graduating in 1961 was 36,000, compared with 42,000 in 1951.

To me it seems nothing less than to be courting national disaster if we continue to let this trend go on without taking some steps to rectify the situation.

This same problem also appears to greatly concern President Kennedy and some time ago at his press conference, he dutifully stated the situation, much as I have just done, and assigned several Government agencies the task of investigating the problem and making recommendations concerning its solution.

It was at his news conference of last January 19; and this is what the President said:

One of the most critical problems facing the nation is the inadequacy of the supply of scientific and technical manpower.

And he went on:

Because of the seriousness of this problem for the long-range future of the United States, I have asked my Science Advisory Committee, in cooperation with the Federal Council for Science and Technology, to review available studies and other pertinent information, and to report to me as quickly as possible on the specific measures that can be taken within and without the Government to develop the necessary well-qualified scientists and engineers and technicians. * * * In undertaking this task the Committee will draw on the advice and assistance of individuals and agencies, including the National Academy of Sciences, which will shortly begin at my request a new study of scientific and technical manpower utilization.

Yet, 6 months later, after this precise directive from the President himself, virtually nothing concrete has been done. The most the Federal Council of Science and Technology can point to is a vague reference to a committee.

The "new study of scientific technical manpower utilization," supposedly being undertaken by the National Academy of Sciences, is equally lost in the bureaucratic mire.

If one investigates further, he runs into a veritable thicket of studies, projections, reports, and assessments—all of which add up to little more than a series of endless dialogs between well-meaning but ineffectual individuals and groups who have been talking this way to one another for 10 years or more.

But this is no time to indulge in unproductive recriminations. There is much too important a matter at stake. The essential question is: Why has nothing been done? Why is our scientific and technical manpower problem stuck on dead center, despite urgent pleas from the President himself?

One reason, I would like to suggest, is that no one seems to know where to start. Statistics in this field have become sterile and meaningless. Projections of future

engineering graduates by the Bureau of Labor Statistics, for example, are based on a questionable study that is already 10 years old. Vitally important information such as the number of technicians in industry compared to the number of engineers, can only be guessed at. We do not even know the number of full-time students enrolled at the technical institutes in the United States.

Once we emerge from the academic halls, the available information becomes even more meager. It seems almost unbelievable that we can know our reserves of a raw material such as plutonium or iron ore down to a gnat's hair, but when it comes to another of our most precious resources—our priceless engineering and scientific talent—we have only the foggiest notion as to where these people are or what they are doing.

The nearest thing we have to an evaluation of our scientific and technical personnel is the register which the law requires the National Science Foundation to maintain. However, this register is admittedly incomplete and underfunded and depends for its information on gleanings from the records of the various technical societies. As a starting point for any realistic appraisal of our engineering and scientific talent it is obviously insufficient. Even though some progress has been made by the register recently, the efforts do not represent the kind of inventory that we ought to have.

As long ago as May of 1959 this so-called register was sharply criticized by the House Committee on Science and Astronautics. Typical of the comments voiced at that time was the criticism of William A. Douglass, president of Careers, Inc., who said:

I don't see how this Nation can properly assess its most key manpower resources if it is to rely on the scanty information presently available to it.

The Committee on Science and Astronautics of the House said in a report issued September 11, 1959:

The Register of Scientists and Technicians is too incomplete, too far behind time, and places too little emphasis on practical experience to be of broad value. It has been alleged that the manpower studies themselves, based on incomplete information, cannot provide adequate data for either current purposes or as a means of anticipating national scientific needs.

Over 2 years ago the National Science Foundation gave a grant to the Engineers Joint Council to restudy the national register in the light of the new need for more detailed and factual national engineering manpower information. A special committee of the Engineers Joint Council was formed to carry out the study. In summary this was the conclusion of that study:

First. That a national register of engineers was impossible to maintain in a useful up-to-date form and was not recommended.

Second. That a register might be beneficial as a source of information concerning the characteristics of the members of the engineering profession, and

Third. That great value could be gained from a comprehensive survey which would accurately reveal the char-

tant tool to help us decide what our actual posture is, where we can obtain these people, how we can increase the pipeline supply, and how we can best utilize them.

Mr. PROXMIRE. The Senator from Nevada could not be more correct. That is why I submitted to the NASA authorization bill the Proxmire amendment to provide for a scientific manpower study by a presidentially appointed Commission. Certainly one is needed; and until we establish these priorities, this situation constitutes our great danger and our Achilles' heel.

I thank the Senator from Nevada very much for his excellent statement.

Mr. CANNON. I thank the Senator from Wisconsin.

Mr. YARBOROUGH. Mr. President, will the Senator from Nevada yield?

Mr. CANNON. I yield to the Senator from Texas.

Mr. YARBOROUGH. I wish to join in congratulating the Senator from Nevada for his contribution to our consideration of the important subject we have been discussing.

I wish to say that as a member of the Veterans' Affairs Subcommittee, I realize the necessity for the kind of study the Senator from Nevada has mentioned. I also wish to state that is one of the reasons why those of us who have co-authored the GI Bill of Rights have been pushing so hard for its passage and enactment, because experience has shown that among the GI's who go to college, the percentage who engage in scientific studies is greater than the percentage among other groups, because many of the GI's worked with engineering or science while they were in the service. Therefore, when they enter college, many of them engage in scientific or engineering studies—and in a higher percentage than is true of any other comparable group of college students.

In connection with these studies, has the Senator from Nevada studied the shortage of medical doctors, and have his studies encompassed the field of medicine?

Mr. CANNON. No. This is the third of a series of talks I have made on this subject; and they have been specifically related to the fields of engineering and science. They do not relate to the medical field.

Mr. YARBOROUGH. Mr. President, again I wish to commend the Senator from Nevada.

I should like to say that medicine is another field in which we are lagging behind in training. Four years ago our medical schools graduated, annually, 7,000 medical doctors; but in the same year the Russian Soviets graduated 16,000—more than double our number. Of those 16,000, 14,000 were for domestic use; but 2,000 were trained in the languages, the mores, the customs, and the religions of the underdeveloped countries, and were pledged in advance to practice medicine in those countries, and to live with the people there, and to live in whatever type of housing the people there are accustomed to live in. Such doctors have a proclivity, as do our peo-

ple, to live in good housing, both when overseas and at home. But they were required to pledge in advance that when they went overseas they would live in the type of housing that the people of those countries are accustomed to live in.

Furthermore, in that year our country had to license 1,700 doctors who had come from abroad—in addition to the 1,600 graduates of American medical schools who were licensed in that year. The licensing of those doctors from abroad was necessary in order to make up the doctor shortage we faced. So I wish to point out that a lag also exists in the field of education in medical science.

Certainly I shall support the Senator's efforts to have a survey made of our educational and scientific needs, including the need for more doctors. In that connection, determination should be made of the number available at home and the number we can spare for service in other parts of the world where improved medical care is so greatly needed.

I congratulate the Senator from Nevada for his leadership in this field and for the very informative speeches he has been making on this subject.

Mr. CANNON. I thank the Senator from Texas.

Mr. President, I yield the floor.

MESSAGE FROM THE HOUSE

A message from the House of Representatives, by Mr. Maupér, one of its reading clerks, announced that the House had agreed to the amendment of the Senate to the bill (H.R. 10743) to amend title 38, United States Code, to provide increases in rates of disability compensation, and for other purposes, with an amendment, in which it requested the concurrence of the Senate.

The message also announced that the House had agreed to the amendment of the Senate to each of the following bills of the House:

H.R. 1388. An act for the relief of Tai Ya Lim; and

H.R. 11257. An act to amend section 815, article 15, of title 10, United States Code, relating to nonjudicial punishment, and for other purposes.

The message further announced that the House had severally agreed to the amendments of the Senate to the following bills and joint resolution of the House:

H.R. 5532. An act to amend the Armed Services Procurement Act of 1947;

H.R. 10431. An act to revise, codify, and enact title 37 of the United States Code, entitled "Pay and Allowances of the Uniformed Services";

H.R. 10432. An act to amend title 39, United States Code, to codify certain recent public laws relating to the postal service and to improve the Code;

H.R. 10433. An act to amend title 10, United States Code, to codify recent military laws, and to improve the Code;

H.R. 10931. An act to revise and codify the general and permanent laws relating to and in force in the Canal Zone and to enact the Canal Zone Code, and for other purposes; and

H.J. Res. 677. Joint resolution relating to the admission of certain adopted children.

ENROLLED BILLS AND JOINT RESOLUTION SIGNED

The message also announced that the Speaker had affixed his signature to the following enrolled bills and joint resolution, and they were signed by the President pro tempore:

S. 1606. An act to authorize the Federal Power Commission to exempt small hydroelectric projects from certain of the licensing provisions of the Federal Power Act;

S. 3574. An act to extend the International Wheat Agreement Act of 1949;

S.J. Res. 29. Joint resolution proposing an amendment to the Constitution of the United States relating to the qualifications of electors;

H.R. 3801. An act to authorize the Secretary of the Army and the Secretary of Agriculture to make joint investigations and surveys of watershed areas for flood prevention or the conservation, development, utilization, and disposal of water, and for flood control and allied purposes, and to prepare joint reports on such investigations, and surveys for submission to the Congress, and for other purposes; and

H.R. 7638. An act for the relief of Kim Hyung In Comstock.

APPLICATION OF CERTAIN LAWS TO AMERICAN SAMOA—CONFERENCE REPORT

Mr. HUMPHREY. Mr. President, on behalf of the Senator from Washington [Mr. JACKSON], I submit a report of the committee of conference on the disagreeing votes of the two Houses on the amendments of the Senate to the bill (H.R. 10062) to extend the application of certain laws to American Samoa. I ask unanimous consent for the present consideration of the report.

The PRESIDING OFFICER. The report will be read, for the information of the Senate.

The legislative clerk read the report. (For conference report, see House proceedings of August 23, 1962, pp. 16265-16266, CONGRESSIONAL RECORD.)

The PRESIDING OFFICER. Is there objection to the present consideration of the report?

There being no objection, the Senate proceeded to consider the report.

Mr. HUMPHREY. Mr. President, as passed by the House, H.R. 10062 authorized the Governor of American Samoa to request Federal departments, corporations, or agencies to extend, without reimbursement, scientific and technical assistance to promote the welfare of the territory. The bill also authorized the extension, upon application by the Governor, of several public laws applicable in other U.S. territories to Samoa. They are the National School Lunch Act, the Vocational Education Act, the Library Services Act, and the Public Health Service Act.

The Senate passed the bill in a somewhat different form. The principal difference in the Senate version was that the request for technical assistance would be made by the Secretary of the Interior, rather than by the Governor of American Samoa; and the programs extended through the various laws I have just mentioned would become effective upon enactment of the bill.

The House conferees and the Senate conferees have agreed that authority to request technical assistance from other departments shall rest with the Secretary of the Interior, instead of the Governor of Samoa. It has also been agreed that benefits from the School Lunch Act and the other acts included in the bill shall not become effective except upon request of the Secretary of the Interior made to the Secretary of Agriculture and to the Secretary of Health, Education, and Welfare.

I present this report on behalf of the distinguished junior Senator from Washington [Mr. JACKSON].

The PRESIDING OFFICER. The question is on agreeing to the report. The report was agreed to.

ELIGIBILITY OF CERTAIN FEDERALLY IMPACTED AREAS FOR ASSISTANCE UNDER PUBLIC FACILITY LOAN PROGRAM

Mr. SPARKMAN. Mr. President, I request that the Chair lay before the Senate amendments of the House of Representatives to S. 3327.

The PRESIDING OFFICER laid before the Senate the amendments of the House of Representatives to the bill (S. 3327) to make certain federally impacted areas eligible for assistance under the public facility loan program, which were, to strike all after the enacting clause and insert:

That paragraph (4) of section 202(b) of the Housing Amendments of 1955 is amended by inserting immediately after "Act" the following: "or in the case of a community in or near which is located a research or development installation of the National Aeronautics and Space Administration".

And to amend the title so as to read:

An Act to make eligible for assistance under the public facility loan program certain areas where research or development installations of the National Aeronautics and Space Administration are located.

Mr. SPARKMAN. Mr. President, I move that the Senate concur in the House amendments.

The motion was agreed to.

REVENUE ACT OF 1962

The Senate resumed the consideration of the bill (H.R. 10650) to amend the Internal Revenue Code of 1954 to provide a credit for investment in certain depreciable property, to eliminate certain defects and inequities, and for other purposes.

INVESTMENT CREDIT

Mr. SMATHERS. Mr. President, the most important measure contained in the tax bill now before the Senate is the proposal to allow a 7-percent credit against taxes on investment in machinery and equipment.

This proposal has been criticized by those who, in my judgment, should most support it.

It has been called a bonanza for business, a tax giveaway, a theoretical scheme that will not work in practice, and a shotgun approach in an area where sharpshooting is called for, or precisely

the opposite, a rifle shot where a scatter gun is needed.

These criticisms do not stand up under close examination of the facts, because the investment credit is none of these things.

I believe it is an important part of the effort to stimulate our economy, to provide more jobs, to end the balance-of-payments deficits and the gold drain, and to give our Nation the means, in the years ahead, to meet head on whatever foreign challenges and domestic requirements we may have to face.

I do not have to tell the Senate of our need for a faster rate of economic growth. We all know that more than 4 million people are out of work in the United States today. We all know that millions of jobs must be created for those people, millions more for the new workers coming into the labor force in this decade, and still more millions to provide for the older workers whose skills are made obsolete by advancing technology.

The only way to get these jobs is by a more rapid rate of growth, for only through economic expansion can our industry operate at a level to sustain full employment under such conditions.

We all know that in recent years our growth rate has been lagging, and we have been outstripped in speed of economic expansion by the industrial nations of Western Europe, by Japan, and even by the Soviet Union.

We all know where this losing race will lead if we continue to be satisfied with an economy operating at slow speed. Every year of delay, every year when we do not act to speed our growth at least to keep pace, not only with our allies, but with other nations far less friendly, brings us closer to the point where our vaunted economic superiority could become a thing of the past. What would happen if that were allowed to occur no one cares to contemplate. We must not and, I am confident, we will not allow it to occur.

One of the most effective measures we have in stimulating growth is the investment credit. It will add momentum to our current recovery by stimulating the capital goods and allied industries, with multiplying effects throughout the economy. It will reach into every nook and cranny of our industrial economy to stimulate modernization of our productive facilities, increasing national productivity, and broadening our industrial base. Greater productivity means greater output, more sales at home and abroad, development of new products, new markets, and more jobs.

The credit will increase our level of productive investment, and this is directly related to our rate of economic growth. During the 1950's, West Germany's proportion of investment in machinery and equipment—as a percentage of gross national product—was roughly twice that of the United States, and her annual rate of economic growth was also twice that of the United States. I will not burden Senators with statistics, since I believe they all have seen them, but I will say that the other industrial nations of Europe which have had more rapid growth

than we have devoted a larger portion of their resources to such investment, and had higher rates of growth.

This is true of almost every single nation in Western Europe—the United Kingdom is the major exception—and of Japan as well.

Even more startling, if we take statistics and examine them more closely, we find that those with the highest investment had the most rapid growth.

The correlation between investment and growth rates in this regard is so nearly perfect as to startle even those familiar with the general trend.

I mentioned that the investment credit will help to increase our sales abroad. This is the second major reason it is needed. It is no secret that those same nations which have been growing so proudly have also been exporting at a very high rate, with the result that they have been piling up surpluses in their balances of international payments.

Our own country, meantime, has been running a persistent balance-of-payments deficit—a deficit which, in the last 4 years, has totaled well over \$13 billion, and included drains on our gold stocks during that time totaling almost \$6 billion. Though we do have a substantial trade surplus, the overall deficit is continuing and the gold drain is continuing.

Our gold stocks now are lower than they have been at any time in more than two decades. They are dropping all the time. The only effective way to stem the gold flow is to eliminate the continuing deficit in our financial relations with other nations. The only way to do that—short of abandoning our national commitments for the defense and development of the free world—is to expand our export surplus, to sell more goods abroad.

The aim of President Kennedy's trade program is to allow us to negotiate mutual tariff reduction with the Common Market and other nations, to assure that our goods can maintain access to vital export markets abroad. But it is not enough to maintain access to these markets. Our goods must be competitive and our producers must be able to outsell foreign producers, both in export markets and here at home.

The higher level of domestic investment which Japan and the industrial nations of Europe have been maintaining has resulted in more rapid modernization of their productive equipment than of ours. This has led to higher productivity, greater efficiency, and lower unit costs added to their initial advantage of lower wage costs.

The consequence has been increasingly aggressive competition. As a result, their share of world markets has been increasing, while ours has been decreasing.

Certainly, we are selling more abroad than they. We are selling more all the time, but their share of the markets has been growing faster than ours. Consequently, our relative competitive position has been declining—at the very time when it is more important than ever for

us to increase our share of world markets.

If we were able to increase our exports only 10 to 15 percent without a commensurate rise in imports, we would be able to wipe out our payments deficit and stop pouring more and more dollars—and gold—into European Central Banks. This is the second major reason for the investment credit. Not only will it stimulate growth, but also it will help assure that our goods are priced competitively. Thus it will be a significant stimulus to export sales and a significant barrier against undue inroads into our domestic markets by imports. This is the most promising avenue for improvement in our international economic position.

Finally, the investment credit, by increasing productive efficiency and thereby lowering costs, provides a strong antidote to any inflationary pressure which may arise again in the future.

The investment credit, then, is basic to our entire economic health, international and domestic. It will help to provide more jobs. It will promote price stability and lessen the possibility of inflation. It will speed our rate of economic growth. It will help in the continuing struggle to balance our international accounts and protect our vital gold reserves. In short, it will serve to move us forward on the road to reaching all of our national economic goals.

Against this background, what have been the criticisms of the investment credit?

It has been pictured as a costly subsidy or windfall to business—a giveaway, which is discriminatory in its application to different industries and different companies.

It has been pictured as a poor incentive, which just will not work as a stimulus, an incentive that is not necessary in view of the recently completed reform of depreciation guidelines.

It is also pictured as a costly, wasteful measure which just will not do what it was designed to do, and even if it did, would be superfluous.

Let us examine those charges one by one. The facts refute them.

Is the investment credit a business windfall? No, it is not a business windfall. In order to benefit from the credit, business must invest in equipment and machinery. The amount of benefit increases directly with the amount of investment. It is not a windfall, but a specific economic stimulus for investment which will not be received unless investment has, in fact, been made. Neither will it be expensive. The \$1 billion expected cost in the first year, according to estimates, may be fully recovered in revenue as a result of the added push to economic expansion in the first year after enactment. As time goes by, the ramifying consequences of a higher investment level will spread throughout the economy, more than compensating for the future costs of the credit.

Is it a giveaway to business—a reward for businessmen who follow Government policy?

No. It is a soundly conceived economic proposal aimed at making sure that business has the funds it needs to finance modernization.

As such, the credit will clearly achieve its objective of encouraging higher rates of business investment. To suggest otherwise—to argue that the credit will not, in fact, work—is to assert that American businessmen are totally irrational.

The credit will work because it will mean cash in hand for business—cash which will find its way back into still further new investment.

The credit will work because it will improve the profitability of investment.

The credit will work because it will shorten the period over which business will recover the cost of investment, and shorten commensurately, the period over which investment capital is risked.

What do the opponents of the credit believe businessmen consider when they are making investment decisions? Do they not ask themselves whether they have the money? Whether the expenditure promises an adequate return? Whether there is a good chance that they will be able to recover the cost of the outlay in a reasonable period of time?

These are, of course, exactly the questions they ask. Enactment of the investment credit will increase the possibility of affirmative answers in a significant number of cases. This is precisely what is meant when supporters of the credit say it will stimulate investment: That enactment of the credit will mean more affirmative investment decisions.

Critics of the credit claim that the credit will be a windfall to those who would have gone ahead anyhow with capital improvements. Even for these firms, however, the additional stimulus of the credit will tend to increase such spending beyond the level which otherwise would have been the limit.

The aim of the credit is to tip the scales in favor of investment in the marginal cases; situations in which the investment decision would have been “no” rather than “yes” but for the faster cost recovery and higher profitability that the credit will make possible.

It is these marginal decisions which may make or break our American growth and our fundamental economic strength in the years ahead. Our competitors in Europe and elsewhere have learned this lesson.

Nearly all of them provide some form of direct stimulus to investment similar to the one now proposed here.

One further point deserves to be made concerning the “windfall” aspect of giving the credit to those who have already made investments since mid-year—or who would be making them, credit or no, in the years ahead.

Is it not true that the credit will provide such businesses, as well as those whose decisions were marginal and thus directly influenced by the credit, with the funds on hand for future investment which might otherwise not have been undertaken?

Another charge made against the credit is that it is discriminatory, favor-

ing one industry against another and one company over another.

In a certain sense this is true—and it is also appropriate.

The benefits of the credit will, in fact, be larger for those industries and those companies which invest the most. But this is as it should be because the credit is intended both to stimulate and to help finance more rapid modernization and expansion. It should therefore go where the most modernizing and expanding is being done. That is where it will go.

While a variety of alternative plans for stimulation of investment have been put forth, in recent months, in one quarter or another, the investment credit, upon analysis, emerges clearly as the most attractive and sensible possible choice.

Some have suggested that the credit is overly generous—frosting on the cake when the Treasury has already taken steps to increase the flow of internally-generated business funds for investment by shortening the lives of depreciable equipment from those previously set forth in Internal Revenue's Bulletin F.

If, however, we have a need—and we surely do—to make the tax treatment of investment in this country comparable to that given investment abroad, depreciation revision is not enough.

We need to make investment incentives here as great, at least, as the average available abroad for two reasons.

First, we need to spur modernization in this country for the health and growth of the American economy and to assure that we have efficient businesses producing at competitive prices. This point I have already touched upon. But there is another reason—also related to both domestic and international economic considerations.

If American businessmen find they can get a faster, more profitable return on their investment in other nations, they are going to invest in other nations.

Such investment overseas, induced in no small measure by our relatively unfavorable tax treatment of investment in this country, hurts the American economy in every way.

It means the export of jobs, along with capital and factories, thus adding to our unemployment problem, impairing our economic health and stunting our economic growth.

In addition, the export of capital hurts our balance of payments directly and the fact that American capital is being used to finance the production of goods for sale and use overseas cuts into the potential volume of exports from this country, thus indirectly also worsening our balance of payments.

Enactment of the investment credit will reduce the relative tax advantage for investment overseas because the credit—and this point should be understood clearly—will apply only and solely to investment in the United States. This is one of the reasons why it is preferable, as a tax inducement for investment, to various forms of accelerated depreciation which, in certain circumstances, can apply to investment in foreign countries.

There are other reasons, also, for preferring the credit to accelerated de-

preciation. I have studied them with care because, I was myself, at one time, an advocate of further acceleration of depreciation. The principal reason is just this: The credit gives more stimulation to investment per dollar of tax revenue lost to the Government than would a similar loss to the Government in the form of accelerated depreciation.

The credit, as opposed to higher depreciation writeoffs, is also relatively more favorable to small corporations, in the 30-percent tax bracket, and to unincorporated businesses whose tax rate is less than 52 percent.

A depreciation deduction of 14 percent would be roughly comparable to the 7-percent credit for a corporation in the 52-percent bracket. But a 14-percent deduction would save a small corporation only \$42 in taxes on a \$1,000 investment, as compared with \$70 under the credit.

It is worth noting, in passing, that there are other features of the pending legislation which have also been tailored with the requirements of small businesses in mind.

One is the permissible use of the credit, subject to a \$50,000 annual limitation, on purchases of used equipment, which is typically bought by the small firm which cannot afford brandnew equipment. Another is the provision extending the credit to leased equipment.

I hope that the facts I have mentioned convince Senators, as they convince me, that we urgently need the credit in the United States today, to spur growth, to provide more jobs, to lessen our international balance-of-payments deficit and to protect our gold reserves.

The credit is no hasty improvisation, but a carefully thought-out policy designed to use our tax law selectively as an economic stimulus tailored to our present and future needs.

The investment credit is based on an understanding of business methods and practice. It is vitally necessary—together with the revision of depreciation guidelines—if our producers are to have tax treatment comparable to that of their foreign competitors.

Depreciation revision alone does not do the job. In the fierce competition for foreign markets that has already begun, it will not be enough to be almost competitive. A price that is almost low enough to meet competition is still too high. The efforts made to lower it, unless they include measures complete enough to do the job, remain only token efforts, and this is no time for token efforts.

American business needs the additional margin of competitive potential which the investment credit promises. Without it, our producers will be laboring under a severe handicap as they attempt to maintain a major place in the rapidly evolving new world of trade. With it, they will have room to use their drive, creativity, business enterprise and plain know-how to keep the United States for many years to come in its present position as the major trading nation and the major industrial nation of the entire world.

Mr. JAVITS. Mr. President, will the Senator yield?

Mr. SMATHERS. I am happy to yield to my friend the able Senator from New York.

Mr. JAVITS. I shall vote against the motion to strike out the proposed equipment tax credit. I have given the subject a great deal of thought, as has my dear friend and colleague from Florida. As the Senator knows, I have had many years of experience with industry and business, both on the legal and the management sides. It is my view that though business is not now very enthusiastic about the credit, the reason for its lack of enthusiasm convinces me that the provision should remain in the bill. Its lack of enthusiasm is attributable to the idea of business that the proposal would become a very uncertain quantity since it is incorporated in a tax bill, and therefore would be subject to the winds of politics. I think its usefulness will be so validated and it will have such a material effect upon the rate of acquisition of new equipment as to imbed itself into tax law very firmly, because it is constructive.

The American industrial plant is undermachined and becoming rapidly very much out of date; and I know my colleague, as he stated, feels the same way. Not only am I in favor of the proposed investment credit, but also I think our formula for depreciation must be revised much more along the German and Swedish models than along our own. We have nothing to lose. The proposal is indispensable to our effort in the cold war to have the American industrial machine occupy the position it occupied after World War I and World War II.

It should lead the world. Anything we can do to bring that about will strengthen our country and materially strengthen its economy.

Productivity is the basis of the economy. We can always find ways and means to deal with the problems of people if there is available money that is worth something in terms of tangible production upon which to build social solutions to social problems. But if we do not have the basic production, we are really in trouble. That is the danger that we run.

So I am very much pleased with the committee report. I know that the vote was close. I know that there is a great deal of opposition to the proposal. I am pleased that the committee left in the bill the proposed equipment tax credit. I know that business is not enthusiastic about it, but I think business is wrong. I think business will be enthusiastic about it once it begins to use the credit and sees how useful it really is, especially—and this is the paramount consideration, in my view—since it would be useful in the national interest. I am very glad that my colleague has made that declaration. I have given the subject a great deal of thought. It has been one of the issues in the bill that has worried me most. For the reasons I have stated, I have come to the conclusion that the provision should be supported, and not rejected.

Mr. SMATHERS. I thank the able Senator from New York for that ex-

pression. The fact that he has had great experience in business, which I venture to say is equal to that of any Senator on either side of the aisle, should strengthen in great measure the opinions of those who support the investment credit provision. I entirely agree with the Senator in his statement that at least at the outset the business community was not enthusiastic about it. Primarily for the reason which he described business felt that the proposal was something of a rather temporary nature. Businessmen did not know how long the provision would remain in the law. They were a little uncertain about its future.

However, in recent weeks, as we have discussed the proposed investment credit provision in the committee and elsewhere, and as the business community itself discussed it, I have found that many businessmen who first came to me expressing great doubt about it have now become convinced of its worth and its desirability. In some instances, those who had previously asked me to vote against it have now in effect made a 180-degree turn, recognizing that the provision could serve a very useful purpose in modernizing their equipment in the productive machinery of our Nation. So I thank the Senator for his comments. I greatly appreciate them.

Mr. SPARKMAN. Mr. President, will the Senator yield to me?

Mr. SMATHERS. I am happy to yield to the distinguished Senator from Alabama.

Mr. SPARKMAN. I have given a great deal of thought to the proposal, not only during the pendency of the bill, but prior thereto. It happens that the Senator from Florida [Mr. SMATHERS], the Senator from New York [Mr. JAVITS], and I are all members of the Small Business Committee. Senators will recall that approximately 4 or 5 years ago we unanimously recommended not exactly a provision such as the one proposed, but a measure which I believe had something to do with the proposal being included in the bill. We were interested in small business, but we could not legislate for small business as a class. So we introduced a bill proposing that any business which plowed back into itself a part of its earnings would be able to deduct for tax purposes such amount of reimbursement, not to exceed 20 percent of its earnings, or \$30,000, whichever was the lesser. We introduced the bill at that session of the Congress and in a succeeding session of Congress.

In the early part of last year the staff members of the Small Business Committee talked with representatives of the Treasury Department in an effort to gain approval of the plan now before the Senate.

They finally said, "We cannot go along with that, but we can go along with this investment credit of 8 percent"—I bet it was originally. I certainly agree with the statement that this can be an incentive for replacing wornout or certainly badly depreciated property. I am no expert in these matters, but I am rather of the opinion that one of the troubles from which the steel industry is suffering today is the need for new equipment. In fact, I believe Mr. Blough said

as much, at the time we were asked to help them replace old equipment so that they could compete with foreign production of steel.

I know that the textile industry, or certain segments of it, have for a long time been plagued with the need for replacing equipment. I do not say that this is the perfect solution, but certainly I believe that it ought to provide a tremendous incentive to business to keep up to date, and thereby maintain productivity and thereby be able to compete on the world market.

Mr. JAVITS. Mr. President, will the Senator yield further?

Mr. SMATHERS. I yield.

Mr. JAVITS. The Senator from Alabama, who so ably heads the Select Committee on Small Business, has had a great deal to do with this matter, and certainly he is entitled to all the credit that is entailed in connection with it, because he was first in the field.

I should like to say, on the question of imports, that, interestingly enough, this provision in the pending bill ties in with the trade bill, because we can take the attitude that we will go along—I am drawing on my memory now—with the situation, according to the estimates, that 40 percent of American machinery and equipment is out of date, considering modern means, when person after person and some of our own colleagues in the Senate come back from Europe and say they have seen a rolling mill or a textile mill or a shoe factory which out-automates anything that we have here. However, I am in favor of meeting that competition by replacing obsolete equipment, and not by meeting it with protective devices.

All of this is directly in point to this particular issue. Unless we are willing to do this in order to encourage that kind of ability, we will go to the other kind, which is protectionism, which will certainly materially weaken the posture of this country in respect of the cold war.

Mr. SMATHERS. Mr. President, I thank the Senator from New York and the Senator from Alabama for their comments. I am very much interested in their comments. I know that when, under the able leadership of the Senator from Alabama, and with the cooperation of the Senator from New York, we devised what we thought was an original concept to keep the economy moving, it is the same concept, as the Senator from Alabama has pointed out, which has developed into this investment credit provision in the pending bill.

Mr. SPARKMAN. There may be some misunderstanding about it. Of course there is a limit on the amount of the investment credit, I believe.

Mr. SMATHERS. Yes; there is a tax limit. The tax credit may offset tax liability in full up to \$25,000, but above that point the credit may not reduce tax liability by more than 25 percent, in any one taxable year. However, any unused credit may be carried back for 3 years or forward for 5 years.

Mr. SPARKMAN. How much is it?

Mr. SMATHERS. There is no specific dollar limitation on the investment credit. However, there is a specific dol-

lar limitation in the case of purchasers of used property. The limitation here is \$50,000. The 7 percent is applied to this \$50,000.

Mr. SPARKMAN. That is another provision.

Mr. SMATHERS. The limit there is \$50,000. This, of course, would be a great stimulant to small business.

Mr. SPARKMAN. I believe \$25,000 is the limit.

Mr. PROXMIRE. There is no limit. The limit of \$25,000 would be provided by the Proxmire amendment. A.T. & T., for example, would get \$75 million.

Mr. SPARKMAN. An official of the Treasury told me it was \$25,000.

Mr. PROXMIRE. Twenty-five percent of the income over \$25,000. A.T. & T. would get \$75 million. There is really no limit.

Mr. SMATHERS. There is no specific dollar limit, on the investment credit because what we are trying to do is to stimulate the economy by encouraging business to rid itself of obsolete machinery and equipment. The bigger the order for machinery in a textile mill or in a shoe mill or by A.T. & T., the more jobs will be created, and the more money will be circulated. The fact that there is no limit does not make it undesirable. I believe it makes it even more desirable.

Mr. PASTORE. Mr. President, will the Senator yield?

Mr. SMATHERS. I yield.

Mr. PASTORE. I could not agree with the Senator from Florida more.

Mr. JAVITS. Mr. President, will the Senator yield?

Mr. SMATHERS. I yield to the Senator from New York.

Mr. JAVITS. I believe the Senator from Florida has put his finger on something that is critically important. We have the concept of absolutes in the way of money without realizing that we are in big business, and that the very size of our whole effort must be proportioned to what we do about it; \$75 million in absolute terms is a great deal of money, but not in terms of a \$500 billion economy; and when we compare it with the thousand-billion dollar production in the Atlantic community, which is the production we are talking about, it is mighty small. The American people, in my opinion, are not frightened by the fact that they earn an annual average of \$6,000 or \$7,000 or \$8,000 and that we are talking about \$100 million or \$1 billion. They have enough wisdom to realize that it is necessary to deal with that kind of economy to give them the security of both jobs and peace that they send us here to create for them in the best way we can.

Mr. SMATHERS. Mr. President, I suggest the absence of a quorum.

The PRESIDING OFFICER. The clerk will call the roll.

The legislative clerk proceeded to call the roll.

Mr. SMATHERS. Mr. President, I ask unanimous consent that the order for the quorum call be rescinded.

The PRESIDING OFFICER. Without objection, it is so ordered.

Mr. WILLIAMS of Delaware. Mr. President, I am a cosponsor of the

amendment offered by the Senator from Virginia [Mr. BYRD] to strike from the bill that section which would provide the 7 percent investment credit. If the investment credit provision is allowed to stand in the bill it will represent a tax reduction of approximately one-quarter billion dollars for American industry. It represents a tax reduction of a quarter of a billion dollars at a time when the only manner in which we can finance it is by a further increase of the national debt and by borrowing the money because we are already operating at a deficit.

I, as much as any other Member of the Senate, look forward to the time when we can cut taxes. However, we should not cut income taxes for corporations or individuals on borrowed money. The Senator from Florida and those who have engaged in colloquy with him state that the proposal would put this money into the spending stream and would thereby help our economy. I am very much surprised to find the Kennedy administration now advocating the trickle-down theory, that they favor a tax reduction for some of the major corporations of this country in the hope that a little of this money will trickle down and help the employees and stockholders and the economy in general. If we are going to give a tax reduction to employees and we want to put money into their hands let us do it with a bona fide tax reduction and reduce taxes for all taxpayers. Let us not pass a tax reduction on to corporations and then say we hope some of it will trickle down to the working man and to the people in the lower tax brackets.

Much has been said in the last several years about the trickle-down theory. I am surprised now to see it embraced so ardently by the Kennedy administration and by some in this country who have heretofore denounced it.

Mr. JAVITS. Mr. President, will the Senator from Delaware yield?

Mr. WILLIAMS of Delaware. I yield.

Mr. JAVITS. I think we want to have the issue clear as between us. I shall not support this proposal on the trickle-down theory, because I agree with the Senator about that. I think it is a very expensive way to spend tax money. But I certainly would appreciate having the views of the Senator on the more fundamental question, to me, of remachining American industrial plants and giving inducements for that purpose.

I am aware of the Senator's extraordinarily fine leadership in respect to depreciation. I pay him all honor for that. I think that is a very potent factor in what we are trying to accomplish. Nevertheless, I feel that the 7-percent tax credit must be discussed in these terms. The Senator has a right to his views as to the trickle-down theory, and I think he has made a legitimate point about the administration.

I was only explaining the view of one Senator on his side of the aisle as to why I would favor this proposal, because I feel that even though there is a little improvement in depreciation, and I would willingly join with the Senator from Delaware, who has shown extraor-

dinary leadership in getting more of a depreciation system for equipment, a system more along the European line, which is designed to encourage business to remachine, I still feel that with this opportunity available, it is so important in terms of re-equipping American industry that, to me, it outweighs any other consideration. I shall take that position.

I agree with the Senator from Delaware that the system should not be justified, and I do not think it could be justified, on the trickle-down theory, because that is a very expensive way to spend tax money.

Mr. WILLIAMS of Delaware. I only repeat the argument that has been made that this benefit would accrue to the working man and other taxpayers. The only way that could happen would be to accept the trickle-down theory.

I agree with the Senator from New York that our present depreciation schedules are outmoded. I was a strong supporter of the administration's recent action in revising schedule F and have been advocating this revision for the past several years.

I would even go further and modify the existing depreciation schedules under our existing laws if we had the money. I made this suggestion in committee and discussed with the Treasury Department my view that a more appropriate method of helping American industry at this time, rather than starting a complicated 7 percent tax credit, would be to liberalize the depletion rates in the framework of our existing law. Why not just change the existing depreciation schedule. For instance, I suggested that rather than doubling the depreciation on a declining balance method, we change to 2½ times. This would allow all taxpayers to write off their investments on a more rapid basis. But it would keep this change confined to the basic principle which has always been a part of our tax structure; namely, that we would never, under any circumstances, allow an individual taxpayer to write off more than 100 percent of the original cost of the item.

One of the basic objections to this current proposal is that with the 7 percent investment credit a taxpayer can claim as depreciation 114 percent of the cost. There is no argument about that. That is the mechanics of the proposal.

In addition, it is very complicated. The staff has prepared an explanation of this investment credit as it was reported out of committee. The Treasury proposal has been changed two or three times. When the President first proposed the investment credit, I asked the staff of the Joint Committee on Internal Revenue Taxation to prepare a report as soon as possible to show taxpayers how the investment credit would work; it required five pages. The formula in the pending bill is just as complicated. The only taxpayers who will use this complicated method will be the corporations which are large enough to keep their tax returns continuously open and which have a group of tax experts on their regular payrolls to figure taxes at all times. If a taxpayer claims this

credit and then sells the piece of equipment 6 years later he will have to go back and recompute his tax returns and open them for those 6 years because he can keep but one-third of the tax credit.

If he sells the equipment within 4 years he will lose all of the tax credit and will have to recompute his return accordingly.

The average small taxpayer who does not employ an accountant on his payroll 12 months a year will not reopen his tax returns voluntarily for this claim. This proposal is even too complicated for a Harvard professor to understand.

Mr. PROXMIRE. Mr. President, will the Senator from Delaware yield?

Mr. WILLIAMS of Delaware. I yield.

Mr. PROXMIRE. I should like to ask a question on the point so ably raised by the Senator from New York. Is it not true that the McGraw-Hill survey asked hundreds of businessmen whether they would use the tax credit, apropos the Senator's argument with respect to remachining and bringing up to date their equipment; and is it not true that the overwhelming majority said, "No"; and that the conclusion was that this proposal would have a very slight effect upon increasing modernization of equipment—about 1½ percent?

Mr. WILLIAMS of Delaware. Yes; small companies would pass it by almost entirely because they do not understand the complications of getting the credit.

Mr. PROXMIRE. Is it not also true that the National Industrial Conference made a similar survey and asked a thousand businessmen whether in 1962 they would use the proposed tax credit?

Mr. WILLIAMS of Delaware. That is true. Any provision which is so complicated that it requires the experts of the committee to devote 5 pages to an explanation of it is too complicated for the average taxpayer and is of no benefit to him.

Mr. PROXMIRE. Is it not also true that McGraw-Hill found that in the coming year the plans of business are to spend more on investment in plant and equipment than ever before in history—more than \$1 billion more—and that 30 percent of that will be for modernization, without the investment credit?

Mr. WILLIAMS of Delaware. That is correct. I would support a liberalization of the present depreciation schedule, but I would want it done within the framework of the existing law so that every taxpayer, whether he be a farmer in Nebraska, Delaware, or Wisconsin, or a small businessman in any State, could compute his own tax return and know what he was paying. Why propose something so complicated that no one can understand it?

Mr. Walter A. Slowinski, speaking in behalf of the Chamber of Commerce of the United States, told the committee:

The chamber again recommends against the adoption of this novel and untried preferential tax credit subsidy for business. It is also unnecessarily complex, and it will be difficult to administer.

Mr. AIKEN. Mr. President, will the Senator from Delaware yield?

Mr. WILLIAMS of Delaware. I yield. Mr. AIKEN. Under this proposal, could an American business concern get credits for modernizing or reequipping a plant which it owned in another country?

Mr. WILLIAMS of Delaware. It is my understanding that it could if the machinery is bought in this country. If it were a subsidiary, I see no reason why that could not be done.

Mr. AIKEN. Suppose an American company decided to modernize its plant in this country, but purchased outside the United States the equipment for modernizing the plant. Would that company then be entitled to the credit?

Mr. WILLIAMS of Delaware. I see nothing in the bill to prevent it.

Mr. AIKEN. We know that most American manufacturers now have plants in other countries. If they were retooling, would they get credits regardless of whether they purchased the tools in the United States or bought them abroad?

Mr. WILLIAMS of Delaware. I have checked with the staff, and the answer is: Yes, they would get the credit, regardless of whether the tools were bought in this country or abroad.

Mr. AIKEN. Will the Senator consult with the staff member in regard to refitting plants owned in another country by another concern?

I realize that most of the plants in other countries are already modernized. But if they wished to install new equipment, would this credit be allowed if they used American equipment to modernize plants overseas?

Mr. WILLIAMS of Delaware. I am advised that if the equipment were purchased overseas and were used in plants in the United States, the 7-percent credit would still be allowed. If the equipment were purchased abroad and were used abroad the 7-percent credit would not be allowed.

Mr. AIKEN. But suppose a plant abroad was refitted with equipment purchased in the United States: Would the credit then be allowed?

Mr. WILLIAMS of Delaware. I am advised by the staff that it would not.

Mr. AIKEN. Then there would be no incentive to use American machine tools, regardless of whether a plant in the United States or a plant overseas was being refitted.

Mr. GORE. Mr. President, on the question of agreeing to this amendment, I ask for a rollcall vote.

Mr. WILLIAMS of Delaware. Mr. President, I join in the request for the yeas and nays.

Mr. SMATHERS. What amendment is this?

Mr. WILLIAMS of Delaware. The Byrd-Williams amendment.

The PRESIDING OFFICER (Mr. BURDICK in the chair). Is there a sufficient second?

The yeas and nays were ordered.

Mr. KEATING. Mr. President, will the Senator from Delaware yield?

Mr. WILLIAMS of Delaware. I yield.

Mr. KEATING. Does the amendment involve discrimination between com-

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panies—for example, between a company which has already modernized its plant and one which modernizes it after this law goes into effect? Would a company which has already modernized its plant be able to obtain the benefit of this investment credit? It would not be able to, would it?

Mr. WILLIAMS of Delaware. That is correct; a plant which does its modernizing before the effective date of the bill would not obtain any credit.

Mr. KEATING. What is the effective date of the bill?

Mr. WILLIAMS of Delaware. As the bill came from the committee the date was July 1, 1962.

Mr. KEATING. So modernizing completed prior to July 1 of this year would get no credit of this sort?

Mr. WILLIAMS of Delaware. That is correct. On the other hand, if the earnings during these years were not such as to enable them to claim the investment credit they could not use any of it.

Mr. KEATING. How long is the bill to continue in effect?

Mr. WILLIAMS of Delaware. Presumably indefinitely.

Mr. KEATING. That is the point I was about to make. If this credit fails, there is no guarantee that it will be repealed.

Mr. WILLIAMS of Delaware. No, no termination date is provided.

Mr. KEATING. But once enacted, it never would be terminated, would the Senator agree?

Mr. WILLIAMS of Delaware. I venture to say that it would soon be recognized for what it is; namely, an unwarranted windfall or subsidy, too complex in nature. Therefore it may well be repealed. Such a step could delay the long overdue correction of our depreciation rates.

I believe that if we are to do anything to change the depreciation formula we should do it in a way which will be understandable to the taxpayers, and we should also apply it to the construction of new buildings. But as the amendment now stands it does not apply to the construction of new buildings. But what good would new machinery be if it were installed in an old, obsolescent building? Unless this provision is applied across the board I do not believe we shall be accomplishing anything of any significant importance. But regardless of that weakness, a tax loss of \$1 billion or \$1.5 billion annually would be caused.

While this 7 percent investment credit as recommended by the Kennedy administration does not apply to building it does apply to racehorses and bulls. I am even advised that this tax credit would apply to the purchase price of allegators and snakes when purchased in the course of a business. Who says the New Frontier does not have ideas?

Mr. KEATING. Is it the experience of the Senator from Delaware that once tax loopholes—which is what I believe this amendment is—are established in the law, it is extremely difficult to get them taken out of the law?

Mr. WILLIAMS of Delaware. Yes. Furthermore, the Chamber of Commerce of the United States recognized this

point as it opposed this credit. That organization certainly represents American industry, and one might think it would favor an amendment which would result in a tax reduction of \$1 billion or \$1.5 billion to American business. However, the Chamber of Commerce of the United States opposes the provision and calls it a "subsidy." It says it does not want American business to be accused of getting such a subsidy. They recognize that subsidies are bound to be accompanied by greater government control of business.

Mr. KEATING. Mr. President, I thank the Senator from Delaware very much for the points he has made and the information he has provided.

I think the tax credit is essentially a gimmick. It would add a new provision to our tax code; and if it did not work, it never would be repealed. Over the years, it could be a multibillion dollar blunder. There is no such thing as a temporary tax or a temporary tax credit.

Mr. President, in the last year I have received a grand total of six letters favoring the investment credit. This shows something of the enthusiasm with which it has been greeted by taxpayers. I would much prefer to see real rate reform, which would help little people as well as big, before we take a step like this.

The investment credit before us is an unproven experiment few people want, and that will cost over a billion dollars. It is part of a tax reform bill which will add substantially to our budget deficit at a time when, although the President promised a balanced budget, the fiscal 1963 budget is deep in the red.

This credit may be good; I am not saying it is necessarily bad. But I doubt very much that it is good enough to warrant a \$1 billion increase in the national debt.

One final word: Depreciation is a tried and practical way to stimulate investment. I support the steps which have been taken to liberalize depreciation treatment. This is an established method. I think we should stick by it. If we need further depreciation reforms—either through legislation or through administrative action—let us do it. This would be far better than taking a gamble on a new tax gimmick which may not work, which will be with us forever, and which will cost the taxpayers of the Nation—big and little—at least a billion dollars a year.

Mr. WILLIAMS of Delaware. Mr. President, Mr. Harold Scaff, chairman of the tax committee of the National Association of Manufacturers, opposed this tax credit; he said:

Investment credit would simply provide reduction in effective tax rates for taxpayers who use their income and other funds as the Government thinks is best for the economy at a particular time.

There has been a tendency to promote and discuss the investment tax credit apart from the price which it would exact in terms of other changes in the tax law. Even without the exaction of such a price, we would oppose the credit for the reasons set forth in the appendix attached hereto. Very simply, we believe that tax reductions should be afforded by direct means. We would take this position even if, in our opinion, all of

the other provisions of H.R. 10650 constituted sound tax policy.

Mr. MILLER. Mr. President, will the Senator from Delaware yield to me?

Mr. WILLIAMS of Delaware. I yield.

Mr. MILLER. The Senator from Delaware knows there is a great deal of talk about making cuts in the tax rates, next year. Suppose next year Congress decides to cut the corporation and the individual tax rates. Is it the opinion of the Senator from Delaware that the investment credit would remain on the statute books, notwithstanding such further cuts?

Mr. WILLIAMS of Delaware. Presumably so. But I am sure that if this investment credit is enacted it will be taken into consideration when a decision is made on the question of whether to reduce the corporate tax rates. One cannot get around the fact that this is a tax cut of \$1.25 billion or \$1.5 billion for the benefit of American industry. A comparable reduction is not given to any other type of taxpayer—although it would go to all partnerships and individuals who purchase new equipment.

This provision will not accelerate the modernization of American industry. This is just a windfall on a discriminatory basis.

Suppose two competitive companies each invest \$10 million in new equipment during 1962. One purchases its equipment in June and the other purchases its equipment in July. One company will get a \$700,000 tax credit or windfall; the other company will get nothing.

Mr. MILLER. But if this amendment is enacted into law and remains on the statute books, and if next year a further reduction is made in the corporate tax rates, the result will be to compound the tax relief for one particular group in the American economy. In short, if next year a 3-percent tax-rate reduction is made across the board, taxpayers who were able to take advantage of this provision would have, in total, a 5-percent tax reduction—which would frustrate the congressional intent.

Mr. WILLIAMS of Delaware. Yes. Furthermore, if the intention is to have such tax relief why is it proposed that it be confined to machinery but not applied to new buildings? If the principle is sound why not have it apply across the board to everyone?

I think this amendment is only an entering wedge for the beginning of subsidies for the benefit of certain segments of American industry.

Mr. MILLER. Is it the understanding of the Senator from Delaware that the proponents of the amendment advocate it on the ground of the need for growth in our economy?

Mr. WILLIAMS of Delaware. Yes; they claim they want to increase the productive capacity of the American economy so that it will be better able to compete with the European Common Market. But if we accept that as a reason then I ask by what line of reasoning did the administration recommend that the investment credit apply to the purchase of racehorses, with the result that

one who purchased a \$100,000 racehorse would automatically receive a tax credit of \$7,000—in other words, a tax reduction of \$7,000. Just how would that enable the American economy better to compete with the European Common Market? Under the livestock provision bulls and even alligators are included.

Mr. MILLER. Along the same line, I was distressed to discover that the proposed tax credit would apply to the purchase of racehorses, but would not apply to the purchase of breeding livestock. I can see a greater relationship to growth of the economy by having the amendment apply to the purchase of breeding livestock than I can to having it apply to the purchase of racehorses.

Mr. WILLIAMS of Delaware. It did apply to both the purchase of racehorses and the purchase of bulls. But as the bill is before us the special tax reduction which would have been allowed those who purchase these bulls and racehorses has been stricken out. That provision was stricken out in the Senate committee. But as the bill now stands this investment credit would be allowed to those who purchase slot machines and all other types of gambling devices, barroom equipment, and all types of equipment used at racetracks. On the other hand, if a farmer in Iowa needed a new barn he would not be eligible for the tax credit. This administration considers racehorses, bulls, and gambling devices more essential than barns and warehouses or a new manufacturing plant.

Buildings necessary to house the equipment of a manufacturer would not be covered. On the other hand, if a man wished to start a gambling joint in one of the States in which gambling is legal all the equipment for the gambling joint would be covered by the special tax reduction on the premise that it would help our economy compete better with the European Common Market.

Mr. MILLER. Mr. President, I realize the validity of the point the Senator from Delaware is making, and I understand that he has pointed out that the proponents of this amendment anticipate that it will help the growth of our economy. But, as I recall, earlier today the Senator from Illinois pointed out that there may be a situation in which a taxpayer may invest in new equipment, but the investment may not even be equal to the amount of depreciation taken on his tax return; and in such a case it could well be that a corporation which had \$200,000 of taxable income last year or this year might have only \$150,000 of taxable income when it took advantage of the investment credit based on the \$200,000 of taxable income in the previous year. In other words, the corporation might have gone backward, insofar as its income was concerned; but it still would reap the benefits of this tax provision, based on its income in the previous year.

Mr. WILLIAMS of Delaware. That is correct.

The representative of one of the largest corporations in the United States testified when he was before our committee in opposition to such a provision.

He said it would be an unjustified subsidy and emphasized that his company is not asking for it. He pointed out that his company would benefit from it to the extent of approximately \$75 million, but he stated that his company would not spend one additional dime on construction even if it were allowed the \$75 million. I admire this company for its complete frankness, but if this Congress had no more sense than to pass that proposal, I am sure that their stockholders will insist that they take it.

Mr. MILLER. Mr. President, I note that the Senator from Illinois is on the floor. I wonder if the Senator from Delaware will yield to me so that I may ask a question of him which applies to the last question?

Mr. WILLIAMS of Delaware. I yield.

Mr. MILLER. I understood the Senator from Illinois to point out earlier today that a taxpayer might invest in equipment a certain sum of money and get the tax benefit under this provision notwithstanding the fact that the investment might be less than the combined depreciation deduction on his taxable income.

Mr. DOUGLAS. That is correct.

Mr. MILLER. Does the Senator from Illinois not recognize that if that happens we may have a situation where the taxpayer's taxable income has actually gone backward instead of grown, which is the purpose, as I understand, of this provision?

Mr. DOUGLAS. That is possible.

Mr. MILLER. If that is so, the Senator pointed out that the way the investment credit was originally proposed did not have that defect in it. Am I correct?

Mr. DOUGLAS. That is correct. The original proposal was for 15 percent investment credit on all sums invested in excess of depreciation and a 6 percent credit on the amounts invested between 50 percent of depreciation and 100 percent of depreciation, but nothing whatsoever if less than 50 percent of depreciation was provided.

This proposal provides 7 percent across the board for 10 percent of depreciation, 20 percent of depreciation, 50 percent of depreciation, or 80 percent of depreciation; and the bill has been transformed from one which aims to stimulate investment into one which rewards gross investment, not net investment, whether or not it meets depreciation charges.

Mr. MILLER. So the purpose of this provision, which is to stimulate growth, can well be frustrated into circumstances where the taxpayer has actually gone backward instead of grown?

Mr. DOUGLAS. That is correct. He will have grown with it.

Mr. WILLIAMS of Delaware. If the new machinery is merely to replace old machinery, he still gets credit, whether it is for expansion or not.

Much has been said about the fact that this provision would benefit the small businessman, a point to which I take exception. As I said before, not only is it too complicated, but under existing tax law there is a provision, not affected by this measure, whereby the small businessman can write off 20 percent up to \$10,000 for any 1 year, and

that 20 percent is in addition to the normal depreciation schedules. For example, if a piece of equipment has a 10-year life, he can write off 20 percent of it the first year and in addition claim another full 20 percent depreciation.

So we already have within the framework of existing law provisions which extend benefits to the small businessman, benefits which far exceed the benefits provided under the 7-percent investment credit proposal.

I ask unanimous consent that provisions of section 176 paragraphs (a) and (b) be printed at this point in the RECORD.

There being no objection, the section was ordered to be printed in the RECORD, as follows:

SEC. 179. ADDITIONAL FIRST-YEAR DEPRECIATION ALLOWANCE FOR SMALL BUSINESS.

(a) General rule: In the case of section 179 property, the term "reasonable allowance" as used in section 167(a) may, at the election of the taxpayer, include an allowance, for the first taxable year for which a deduction is allowable under section 167 to the taxpayer with respect to such property, of 20 percent of the cost of such property.

(b) Dollar limitation: If in any one taxable year the cost of section 179 property with respect to which the taxpayer may elect an allowance under subsection (a) for such taxable year exceeds \$10,000, then subsection (a) shall apply with respect to those items selected by the taxpayer, but only to the extent of an aggregate cost of \$10,000. In the case of a husband and wife who file a joint return under section 6013 for the taxable year, the limitation under the preceding sentence shall be \$20,000 in lieu of \$10,000.

Mr. WILLIAMS of Delaware. As I explained earlier, I have asked the staff of the committee to compile an explanation for the use of the taxpayer of the investment credit provision of H.R. 10650 as amended by the Senate Finance Committee.

If this is going to be the law, I think the taxpayers ought to be able to understand how it was intended to operate. It took the staff 5 pages to explain how a taxpayer can take advantage of this 7 percent credit if it is passed in the form now before the Senate.

I ask unanimous consent that the explanation be printed at this point in the RECORD.

There being no objection, the explanation was ordered to be printed in the RECORD, as follows:

EXPLANATION OF THE INVESTMENT CREDIT PROVISION OF H.R. 10650 AS AMENDED BY THE SENATE FINANCE COMMITTEE

The bill provides a credit which may be offset directly against income tax. Usually, this is 7 percent of "qualified investment." Investment which is eligible for the 7 percent investment credit is referred to in the bill as "qualified investment." Qualified investment includes both new property and up to \$50,000 used property. Property qualifies for the investment credit in the year it is placed in service by the taxpayer.

The percentage of investment which the taxpayer can take into account as qualified investment varies with the expected useful life of the property in his business. No part of the investment with a life of less than 4 years is taken into account, property with a life of 4 years up to 6 years is taken into account at one-third of the amount of invest-

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ment made, property with a life of 6 to 8 years is taken into account on the basis of two-thirds of the investment made, and property with a longer life is taken into account at the full amount of the investment.

Public utility property is taken into account as qualified investment at three-sevenths of the cost of the property. As a result, in the case of 4- or 5-year public utility property one-seventh of the investment is taken into account; in the case of 6- or 7-year property, two-thirds is taken into account; and in the case of property with a life of 8 years or more, three-sevenths is taken into account.

Qualified investment is reduced in the case of property which is a replacement for other property destroyed or damaged by fire, storm, shipwreck, or other casualty or storm, where this property was insured. The amount treated as qualified investment in the case of the replacement property is reduced by the amount of the insurance or by the cost of the replacement property, whichever is the lesser.

The property taken into account as qualified investment must be purchased or otherwise acquired after June 30, 1962.

Used property also is eligible for the credit if purchased after June 30, 1962, but the amount which may be taken into account is limited to a maximum of \$50,000 a year.

In the case of husband and wife filing separate returns, the used property with respect to each is limited to a maximum of \$25,000, unless one of the two has not purchased any qualifying used property in which case the other is entitled to the full \$50,000.

The tax credit may not exceed tax liability up to a level of \$25,000 and may not exceed 25 percent of tax liability above this amount. Any tax credit which may not be used in this fashion can be carried back 3 years and forwarded 5 years and used as if it were a credit for that year or years.

The bill provides a special recapture rule. If property is disposed of before the end of its estimated useful life in the hands of the taxpayer and this period is less than 8 years, then the amount of the credit which may be taken is reduced in such a manner as if the estimated useful life of the property had initially been correctly estimated. However, this adjustment is made in the current year rather than in the prior year.

The bill provides that the cost or other basis of the property is to be reduced by 7 percent of the qualified investment. This reduction is for purposes both of depreciation to be taken subsequently and also in case the property is subsequently sold. If because of limitations the full amount of the credit cannot be taken—this can arise either because the property is sold and the credit is reduced or because the carryover and carry-back do not permit the full use of the credit—then the taxpayer is allowed a special deduction from income equal to the amount by which the basis of his property was reduced but for which no credit was taken.

Only what is called section 38 property is treated as qualified investment under the bill. Most tangible personal property qualifies. Except for buildings and structural components, real property which is used in manufacturing, production or extraction or in furnishing transportation, communications, electrical energy, gas, water, or sewage disposal services also qualified. This is also true of real property other than buildings and structural components used for research or storage facilities in the case of any of the categories mentioned above.

There are, however, certain categories of property which are excluded from the definition of qualifying investment. These exclusions include:

(1) Most property used primarily for lodging.

(2) Most property used by tax-exempt organizations.

(3) Property used by governmental units.

(4) Most property used predominately outside of the United States.

(5) Livestock.

The bill also provides that a lessor may elect to treat investment as if made by the lessee rather than the lessor. If the lessor makes this election, the lessee is treated as if he had acquired the property himself. The useful life of the property in his hands, however, is the useful life in the hands of the lessor.

Special categories of taxpayers have their investment credit reduced on the grounds that they for one reason or another are not fully taxable. This includes mutual savings banks, savings and loan associations, regulated investment companies, cooperatives, and small business corporations treated in a manner similar to partnerships.

Mr. BUSH. Mr. President, I have a few comments to make about the bill. I am opposed to this amendment because I believe it is discriminatory. Take company A, for instance, which has gone ahead and improved its plant and modernized its equipment and completed this process, so that during the next 4 or 5 years it will not have to do further modernization. It would get no benefit whatsoever under this investment credit provision.

On the other hand, company B, which may be a less well managed company, a company which may be a larger or smaller company than company A, but has not been so farsighted, will get all of the benefit, for whatever it is worth, under the amendment.

I think, therefore, this is a discriminatory amendment. It discriminates against the efficient in favor of the inefficient. It discriminates against the forward looking, aggressive, adventurous business organization, and, conversely, it discriminates in favor of one that may be considerably less so. Therefore, on the ground of its discriminatory nature, I believe the investment tax credit should be deleted from the bill.

Secondly, I do not believe in selective tax treatment. I think, generally speaking, all taxpayers within groups, within industries, within any category, should be treated alike. Both large businesses and small businesses should be treated alike.

I also observe that there is no enthusiasm for this investment tax credit, so far as I have been able to find, among American businesses. This fact was admitted on the Senate floor this afternoon. My able and distinguished colleague from New York said that, although he finds little support for this tax credit, he thinks in due course it will be appreciated.

If I know anything about American businessmen, they are well able to determine for themselves what is likely to be beneficial to them, what is likely to induce them to go ahead and expand; and I do not think it needs interpretation from those who are not active in business management.

So I say if we are going to do something to stimulate activity in American business by way of expansion, extension of plant, and modernization, let us do it right. Let us do it in the way that the

established leaders of business, the students who have gained their knowledge from experience, feel is apt to provide the necessary stimulation.

What does the business community think will stimulate expansion? I would say, offhand, two things. As my able and distinguished colleague from Delaware said a few moments ago, an increased depreciation allowance would have an effect. What has already been offered by the Treasury will, no doubt have that effect to some extent; but I believe most American businessmen, if they had a chance, would vote, by a large majority, to increase depreciation allowances still further so as to take advantage, if you will, of the additional \$1,200 million that this tax credit provision will take out of the Treasury. By putting into effect further depreciation allowances, there would really be a stimulating effect, and there would also be the advantage of treating all alike.

This would give everybody an equal opportunity, the small businessman as well as the large businessman. I believe this is the way taxes should work. They should not be discriminatory.

Mr. WILLIAMS of Delaware. Mr. President, will the Senator yield?

Mr. BUSH. I yield to the Senator from Delaware.

Mr. WILLIAMS of Delaware. The Senator may be interested to know that I do not recall a single witness who appeared before the Senate Finance Committee during all of the lengthy hearings held who did not endorse the principle of a liberalization of the existing depreciation allowance as being far preferable to the investment credit.

Mr. BUSH. I thank the Senator for that observation. That being the case, I do not see why we should fly in the face of that kind of competent information merely because the administration has sent to the Congress this new idea to stimulate production or to stimulate business expansion of plant, and presumably to increase job opportunities.

I agree with the Senator from Delaware. My feeling is that this could be much more effectively done by a further liberalization of the depreciation allowances.

Secondly, what would be of equal value, or what would perhaps stimulate an even greater confidence in business, so that business might proceed to modernize and expand plant, would be a general revision of the income tax structure. I understand this problem is under consideration by the administration, by the House Committee on Ways and Means, and perhaps even by our own Committee on Finance. It is expected that in 1963 the Senate will consider a tax reform bill.

My fear is that, by passage of this kind of "gimmick" and this kind of tax bill, there will be an interference with and an inhibition against the possibilities of enacting the kind of tax reform bill we should enact, which is long overdue.

I fear that the hodgepodge bill, which probably will result from Senate action, will interfere with accomplishing real tax revision in 1963.

I also venture to express the fear now that when we have finished our consideration of this bill and of the amendments which may be attached to it, it will be the biggest hodgepodge bill passed in my memory.

Where does the Tax Foundation stand in connection with this? I have not been informed that they have taken a favorable view of it at all. I have tried to find a word of testimony in favor of it from the highly expert organization known as the Tax Foundation in New York.

Where does the Committee for Economic Development, which is regarded to be an authority in matters of this kind, stand?

What does the National Association of Manufacturers have to say? This is the great industrial organization representing the manufacturers of this country. I understand that they are opposed to the investment tax credit.

I understand the Chamber of Commerce of the United States is opposed to it.

I understand that the American Federation of Labor and the CIO likewise are opposed to it.

All of these people have an interest in the expansion of American business, of American plant. They are interested in American economic growth. No one of these people is in favor of this provision. In fact, it appears that all of them are opposed to the investment tax credit scheme.

Mr. WILLIAMS of Delaware. Mr. President, will the Senator yield?

Mr. BUSH. I yield to the Senator from Delaware.

Mr. WILLIAMS of Delaware. The Senator is correct. Not only are those organizations opposed to it, and vigorously opposed as the Senator has stated, but Mr. Charles B. Shuman, president of the American Farm Bureau Federation, likewise opposed it as being of no benefit to the American farmer or to the small businessman.

In fact, I have never seen a proposal on which there was such a unanimity of opinion in opposition. Several people said, "Surely; if Congress passes the bill we will take the money which is to be passed out, but it is an unwarranted subsidy." That phrase was repeated over and over again.

Mr. BUSH. I thank the Senator for his observation. I must say that over the years, I think, the American Farm Bureau Federation has taken very sound positions in respect to matters of this kind, affecting the economic life and the economic growth of the country.

If one talks to representatives of most companies privately, they say, "We are going ahead with our expansion program. We would be happy, perhaps, to get this windfall. If it is coming, we will take it. As a matter of fact, we will go ahead with our plans whether it is passed or not."

My final point is that I doubt very much whether it will offer any stimulation or create any new expansion of plant, which would not take place without an investment tax credit.

Mr. President, I have studied the hearings on the bill and the minority views,

as well as the majority report. I am convinced that we would be far better off if we knocked the tax credit provision out of the bill.

CRATER-LONG LAKES DIVISION OF SNETTISHAM PROJECT, ALASKA

Mr. HICKEY. Mr. President, I ask unanimous consent that the unfinished business be temporarily laid aside, and that the Senate proceed to the immediate consideration of Calendar No. 1744, S. 594.

The PRESIDING OFFICER. The bill will be stated by title for the information of the Senate.

The LEGISLATIVE CLERK. A bill (S. 594) to authorize the construction, operation, and maintenance of the Crater-Long Lakes Division of the Snettisham project, Alaska.

The PRESIDING OFFICER. Is there objection to the request by the Senator from Wyoming?

Without objection, the unfinished business will be temporarily laid aside and the Senate will proceed to consider the bill.

The Senate proceeded to consider the bill (S. 594) to authorize the construction, operation, and maintenance of the Crater-Long Lakes Division of the Snettisham project, Alaska.

Mr. HICKEY. Mr. President, this bill would authorize the construction, operation, and maintenance of the Crater-Long Lakes Division of the Snettisham project in Alaska. Favorable reports on this proposal have been received from the executive agencies involved. The Senate Interior and Insular Affairs Committee has reported the bill favorably. However, because of an agreement entered into between the Secretary of the Army and the Secretary of the Interior relating to the construction of projects in Alaska by the Corps of Engineers rather than the Bureau of Reclamation, the Senate Committee on Interior and Insular Affairs recommended that the bill be re-referred to the Senate Committee on Public Works.

Mr. President, I move that S. 594 be referred to the Senate Committee on Public Works.

Mr. DOUGLAS. Mr. President, will the Senator yield for a question?

Mr. HICKEY. I yield.

Mr. DOUGLAS. I notice the two Senators from Alaska [Mr. BARTLETT and Mr. GRUENING] are not in the Chamber. I should like to ask if this proposal is satisfactory to them.

Mr. HICKEY. It is my understanding, I reply to the Senator from Illinois, since the report was given to me, that it is satisfactory and the action is being requested at the request of the Senator from Alaska [Mr. GRUENING].

Mr. DOUGLAS. Can the leadership assure me on this point?

Mr. SMATHERS. Mr. President, will the Senator yield so that I might ask the Senator a question?

Mr. HICKEY. I yield.

Mr. SMATHERS. I am curious as to whether the able Senator from Wyoming has cleared this with our majority leader.

Mr. HICKEY. When I was in the chair as Presiding Officer, the clerk from the committee was talking to the Senator from Montana [Mr. MANSFIELD], and he brought this bill up, handed it to me, and asked me if I would make the request. I presume it has been cleared.

Mr. SMATHERS. I wonder if the able Senator would mind postponing his request for about 15 minutes, until we can check this out?

Mr. HICKEY. Very well.

REVENUE ACT OF 1962

The Senate resumed the consideration of the bill (H.R. 10650) to amend the Internal Revenue Code of 1954 to provide a credit for investment in certain depreciable property, to eliminate certain defects and inequities, and for other purposes.

Mr. DOUGLAS. Mr. President, the opponents of the investment credit windfall are ready to vote now. I hope very much that there will be no further delays, and that we can proceed to a vote.

Mr. KERR. Mr. President, I suggest the absence of a quorum.

The PRESIDING OFFICER. The clerk will call the roll.

Mr. MILLER. Mr. President, I wonder if the Senator from Oklahoma will withhold his suggestion of the absence of a quorum, so that the Senator from Iowa may say a few words.

Mr. KERR. Mr. President, I withdraw the suggestion for the time being.

Mr. MILLER. Mr. President, I have noted a lot of confusion about this investment tax credit. First, I wish to point out that it is not to be a tax reform, so far as depreciation is concerned. It has nothing whatsoever to do with depreciation. What it will be is a tax cut.

A person would figure up his tax bill, and then take a part of the tax bill off if he qualified under the provision. It would amount to a 7 percent portion of the total cost of new equipment or new assets for manufacturing purposes or farm purposes, with certain limitations.

In other words, if a person bought something new this year, after the effective date of the act, the language would apply, and it would apply to the extent of 7 percent. In the case of some small businesses, purchases could be made up to \$50,000 worth of used equipment. Many of the small businesses cannot afford new equipment, but have obsolete equipment and could upgrade their equipment by buying some good used equipment.

The equipment must have a useful life of at least 4 years. I ought to point out that the 7 percent credit is not a definite thing by any means. It is a graduated proposition. If a taxpayer buys something and hangs onto it for over 4 years, he would receive only one-third of the credit. If he should hang onto it for over 6 years, he would receive two-thirds of the credit. If he should keep it for over 8 years, he would then—and only then—get the full credit, although actually he would get a tax cut in the year in which the asset was put into service. Then later on, if he disposes of it in less than 4 years, he would get no credit.

He would have to refund the entire credit to the Government. Or if he disposed of it in less than 8 years, he would have to refund a portion of the credit.

To be fair about the proposal, there is something to be said about the inducement that the measure offers to invest in permanent type investments. In other words, the one-third-two-thirds proposition is designed to avoid a tax credit for someone who is merely going to take a quick tax deal and stay in the equipment for about 2 or 3 years and then get out and possibly sell it at a profit. The proposal is designed to encourage people to invest in assets that will have at least a life of 4 years, and preferably an 8-year life.

What is the reason for the proposed investment tax credit? I quote from the statement of the Secretary of the Treasury before the Senate Finance Committee. He summed up the policy very well. He said—

It will stimulate investment in modernization and expansion of our industrial capacity, contribute to economic growths, and substantially increase the competitiveness of American products abroad. We must increase our efficiency and our productivity to meet the competition of other nations which are already providing tax incentives for their businesses. In recent years, we have devoted less than 6 percent of our gross national product in investing in this productive capital, only one-half of the amount that West Germany has been devoting, only 60 percent of the combined average of the European nations that form the Common Market. And we must have a more satisfactory rate of capital formation.

Mr. President, with the Secretary's statement of the existing situation and the need for improvement I agree 100 percent. But I certainly disagree 100 percent with his proposed solution. I think we ought to make clear, first, that this is one of the unusual times when we find normally opposite groups going hand in hand together to oppose a piece of legislation. As has already been pointed out, the National Association of Manufacturers, on the one hand, and the American Federation of Labor and the Congress of Industrial Organizations on the other, normally opposed on legislation, are very much together on the proposal.

But it seems to me, getting at the merits of the proposal, the worst feature of it is that it would be highly discriminatory. A businessman who in prior years had been keeping his plant up by putting in new equipment and modernizing his plant might have a competitor down the road who had not been doing so at all. All of the sudden the competitor would find that he could have a nice juicy tax credit. Who would pay for it? The one who would pay for it is the fellow who had been doing the job of modernizing down through the years.

I suggest another case. Assume a corporation has been making a good profit but has been putting some of its profit aside for investment in good plant and good machinery, instead of paying all of its profit out as dividends. Another competitive corporation has been literally milking all the profits out in the form of dividends and its plant has become

obsolete. The second corporation in effect would receive a tax windfall under the proposal.

In fact, the tax investment credit would almost put a premium on past inefficiency. I certainly hope that the pending motion will prevail.

Mr. CURTIS. Mr. President, will the Senator yield?

Mr. MILLER. I yield.

Mr. CURTIS. What about the situation in which the taxpayer some time prior to the effective date of the proposal had already expanded or improved his plant and was carrying a debt load for it. Would he receive any tax credit?

Mr. MILLER. He would receive nothing at all. No effort has been made by the proponents of the legislation to make it retroactive and give some tax benefit to a taxpayer in that position.

Mr. CURTIS. The proposal applies not only to plant renewal and improvement but also to plant expansion, so far as machinery is concerned.

Mr. MILLER. That is correct.

Mr. CURTIS. Suppose the taxpayer is engaged in business in an area in which the prudent thing to do would be not to expand. If he followed that prudent course, he would not receive any tax deduction.

Mr. MILLER. That is correct.

Mr. CURTIS. How about the taxpayer that would expand anyway? He might get a windfall out of the proposal. Is that true?

Mr. MILLER. That is correct.

Mr. CURTIS. In the payment of that windfall, would the economy be spurred to any more construction or any more jobs by reason of the passage of the proposal?

Mr. MILLER. The Senator has already anticipated my answer as "no," because he has pointed out the situation in which the expansion would take place regardless of the provision.

Mr. CURTIS. Will the distinguished Senator in a few words, in layman's language, tell us the difference between a depreciation allowance or deduction and a tax credit?

Mr. MILLER. The depreciation allowance is a deduction which is used in arriving at the amount of taxable income. To the taxable income tax rates are applied. On the other hand, the investment credit is a cut in the tax bill that has been arrived at after applying the tax rates to the net taxable income.

Mr. CURTIS. In other words, it would reduce the amount of the tax owed.

Mr. MILLER. That is correct.

Mr. CURTIS. On the net profit.

Mr. MILLER. That is correct. That is why I wish to reemphasize that there is absolutely no relationship whatsoever between the investment credit and depreciation.

Mr. CURTIS. One more question. I do not wish to delay the Senate. What is the practical difference between allowing a taxpayer a tax credit and having the taxpayer pay his full taxes and then receive a subsidy check back from the Treasury? There is no difference, is there?

Mr. MILLER. In the first place, one can have a check back from the Treas-

ury in this situation in which he has had a tax. But he may have depreciation which he must take even though he does not.

Mr. CURTIS. I am not speaking about depreciation. In the proposed incentive credit, mathematically it would amount to the situation of a taxpayer paying the full amount of his tax and then receiving back from the Treasury a check for the amount of the credit.

Mr. MILLER. Yes. The Senator is absolutely correct.

Mr. CURTIS. I thank the Senator.

Mr. WILLIAMS of Delaware. Mr. President, will the Senator yield for a question?

Mr. MILLER. I yield to the Senator from Delaware for a question.

Mr. WILLIAMS of Delaware. We have before our committee the so-called trade act. Under that proposal the President would be given authority to cut the tariffs of certain industries up to 50 percent and, in some instances, 100 percent. In return for that he is supposed to obtain concessions from the European Common Market and other countries with which we could increase our exports. It is recognized that the proposal would cause some industries to suffer. Some industries would greatly benefit. The industries which would suffer would naturally have no reason for expansion—in fact, they would be faced with all they could do to hold their own, and may even be on the way out.

Under the proposed tax investment credit as contained in the bill, the tax credit would go to those industries which would benefit most from the trade program, and those which would be penalized by it would be penalized even more under this provision of the bill, because they would have no way of taking advantage of the tax reduction.

Mr. MILLER. We would add insult to injury. The Senator has pointed out another very important area of discrimination which this provision would permit.

Mr. KERR. Mr. President, I suggest the absence of a quorum.

Mr. HICKEY. Mr. President, will the Senator withhold that suggestion for a moment?

Mr. KERR. I withhold it.

CRATER-LONG LAKES DIVISION OF SNETTISHAM PROJECT, ALASKA

Mr. HICKEY. Mr. President, I ask unanimous consent that the Senate temporarily lay aside the pending business and proceed to the consideration of Calendar No. 1744, S. 594.

The PRESIDING OFFICER. The clerk will state the bill by title.

The LEGISLATIVE CLERK. A bill (S. 594) to authorize the construction, operation, and maintenance of the Crater-Long Lakes division of the Snettisham project, Alaska.

The PRESIDING OFFICER. Is there objection to the request?

There being no objection, the Senate proceeded to consider the bill.

Mr. HICKEY. Mr. President, I move that the bill (S. 594) be referred to the Committee on Public Works. This is in line with the request of the Senators from Alaska and the Committee on Interior and Insular Affairs. It has been cleared on both sides.

The PRESIDING OFFICER. The question is on agreeing to the motion of the Senator from Wyoming.

The motion was agreed to.

AMENDMENT OF TITLE 38, UNITED STATES CODE, TO PROVIDE INCREASES IN RATES OF DISABILITY COMPENSATION

Mr. MANSFIELD. Mr. President, I ask that the Chair lay before the Senate the amendment of the House to the amendment of the Senate to H.R. 10743. This procedure is satisfactory to all concerned, and I ask that it be approved.

The PRESIDING OFFICER (Mr. LAUSCHE in the chair) laid before the Senate the amendment of the House of Representatives to the amendment of the Senate to the bill (H.R. 10743) to amend title 38, United States Code, to provide increases in rates of disability compensation, and for other purposes, which was, to strike out the language proposed to be inserted by the Senate amendment and insert in lieu thereof the following: "the first calendar month which begins after the date of enactment of this Act, but no payments shall be made by reason of this Act for any period before such effective date. The increased rate of compensation payable to any veteran entitled thereto on such first day shall be further increased, for such month only, in an amount equal to three times the monthly increase provided for such veteran by the amendments made by this Act."

Mr. JAVITS. Mr. President, is this the veterans' disability compensation bill?

Mr. MANSFIELD. It is.

Mr. DIRKSEN. Mr. President, the Senate approved an amendment I offered to make payment beginning July 1. The Veterans' Administration will do that; but under the House amendment, by using a different procedure, about \$500,000 in administrative expenses can be saved. In that action, we full concur, because the intent and purpose of the bill will be carried out.

Mr. JAVITS. Mr. President, will the Senator from Illinois yield?

Mr. DIRKSEN. I yield.

Mr. JAVITS. The Senator from Illinois, in his own quiet way, acting with celerity, deprives us of an opportunity to comment upon the importance of the amendment. We in New York have much experience with disabled veterans. I have an office in New York which deals almost primarily with that subject. I had the privilege of addressing the Disabled American Veterans at their convention about a week ago. I can testify to the Senator from Illinois personally that he will have earned, by this amendment, and with the concurrence of the distinguished majority leader, I know, the profound gratitude of the veterans concerned. It is a bipartisan effort, long

overdue, and most gratifying, but it should be said that the Senator from Illinois moved so quickly that no other Senator had an opportunity to say so.

Mr. DIRKSEN. I thank the Senator from New York.

Mr. LONG of Louisiana. Mr. President, I believe, as the Senator from Illinois has suggested, that the House amendment carries out what the Senator from Illinois had attempted to do. I had two amendments at the desk, one to make the effective date June 1, and one to make the effective date August 1. I hoped one would be agreed to, and the Senate agreed to the amendment offered by the Senator from Illinois, making the effective date July 1. The amendment which comes to us from the House carries out the same intent. It makes a technical change so that checks may be received by veterans at an earlier date. It will also save a large amount in administrative expense.

Mr. MANSFIELD. Mr. President, when the Senator from New York used the word "celerity," he was understating the case. I think "lightning" would be a better description of the action.

Not only do I compliment and commend the distinguished minority leader for his action; I also thank the distinguished Senator from Louisiana [Mr. LONG] for the cooperation and accommodation which he accorded the leadership on both sides of the aisle in helping to bring up the bill and in helping, in part, to bring about something in the way of a retroactive provision. Both the Senator from Louisiana and the Senator from Illinois have performed a great work.

The PRESIDING OFFICER. Without objection, the amendment of the House to the amendment of the Senate is concurred in.

ORDER FOR ADJOURNMENT UNTIL 10 A.M. TOMORROW

Mr. MANSFIELD. Mr. President, I ask unanimous consent that when the business for today has been concluded, the Senate adjourn until 10 o'clock tomorrow morning.

The PRESIDING OFFICER. Without objection, it is so ordered.

REVENUE ACT OF 1962

The Senate resumed the consideration of the bill (H.R. 10650) to amend the Internal Revenue Code of 1954 to provide a credit for investment in certain depreciable property, to eliminate certain defects and inequities, and for other purposes.

Mr. DOUGLAS. Mr. President, the opponents of the giveaway of the \$1,300 million annual giveaway, in the form of the investment credit, are ready to vote. Let us have no more delays. The yeas and nays have been ordered. Let us proceed to vote.

Mr. KERR. Mr. President, a parliamentary inquiry.

The PRESIDING OFFICER. The Senator will state it.

Mr. KERR. Does the Senate decide when it votes, or does the Senator from Illinois decide when it votes?

The PRESIDING OFFICER. The Senate decides the question.

Mr. MANSFIELD. I ask unanimous consent that the Senate vote in 2 minutes.

The PRESIDING OFFICER. Is there objection? The Chair hears none, and it is so ordered.

Mr. MANSFIELD. Mr. President, I should like to read a part of a letter which I have received from the Secretary of the Treasury.

Mr. SMATHERS. Mr. President, may I ask the majority leader whether he intends that we have a quorum call before we vote?

Mr. MANSFIELD. Not necessarily.

The letter from the Secretary of the Treasury is dated August 27, 1962, and it is addressed to me. In part, it reads as follows:

The central element of the President's recommendations was the need for an incentive for investment in machinery and equipment that would stimulate a higher rate of economic growth and better enable our industry to compete in markets at home and abroad. The investment credit contained in this bill will operate as a powerful stimulus to investment. In combination with the Treasury's recent administrative reform of depreciation, the credit will, at long last, give to American business tax treatment on new investment in machinery and equipment approaching that of its chief competitors in Western Europe, Canada, and Japan. Its adoption will constitute a major advance toward our national goals of greater economic growth and the increased productive efficiency and competitiveness necessary to a solution of our balance-of-payments problem.

I yield back the remainder of my time.

Mr. WILLIAMS of Delaware. Mr. President, I ask unanimous consent that there may be printed at this point in the RECORD the statements in opposition to this provision as made by the AFL-CIO, the National Association of Manufacturers, the American Farm Bureau Federation, and the Farmers Union as shown at pages 348 and 349 of the committee report.

There being no objection, the statements were ordered to be printed in the RECORD, as follows:

Stanley H. Ruttenberg, research director, AFL-CIO, urged the committee to "delete this provision from the bill," because those he represented thought:

"It is a multi-billion-dollar windfall that will not really contribute anything to our national goals and will not relieve our balance-of-payments problems as it is claimed."

Walter Slowinski, appearing in behalf of the U.S. Chamber of Commerce, with respect to the "investment credit" provisions, said:

"The chamber again recommends against the adoption of this novel and untried preferential tax credit subsidy for business. It is also unnecessarily complex, and it will be difficult to administer."

Harold H. Scaff, chairman, Tax Committee, National Association of Manufacturers, said "investment credit would simply provide reduction in effective tax rates for taxpayers who use their income and other funds as the Government thinks is best for the economy at a particular time."

"There has been a tendency to promote and discuss the investment tax credit apart from the price which it would exact in terms of other changes in the tax law. Even without the exaction of such a price, we would oppose the credit for the reasons set forth

in the appendix attached hereto. Very simply, we believe that tax reductions should be afforded by direct means. We would take this position even if, in our opinion, all of the other provisions of H.R. 10650 constituted sound tax policy."

Charles B. Shuman, president, American Farm Bureau Federation, took the position that "these provisions are both unsound and likely to have a number of undesirable effects. It would be far better to liberalize the treatment of depreciation and work toward a general reduction in income tax rates."

"The proposed investment credit is a selective form of tax relief—in reality a subsidy. . . . The result would be to give some taxpayers a competitive advantage at the expense of others."

Although the Farmers Union did not send a representative to testify directly before the Finance Committee, a communication signed by James G. Patton, president, National Farmers Union, published in the CONGRESSIONAL RECORD of March 29, 1962 (p. 4984), said:

"Urge your influence to delete provision giving huge private corporations operating at less than full capacity over \$1½ billion and private electrical power monopoly over \$100 million in tax subsidies which would result in the flight of capital overseas and further aggravate the dollar crisis."

Mr. COTTON. Mr. President, after careful consideration and a great deal of soul searching, I have decided to cast my vote in favor of the investment credit provisions of section 2 of the pending tax bill, H.R. 10650. This is the central item in the bill and it allows a 7-percent credit against tax for most taxpayers for their purchases of machinery, equipment, and certain other property.

The fundamental purposes of the provision, as the President and the Secretary of the Treasury have repeatedly emphasized, are to stimulate our economy, to help American industry compete more effectively for markets at home and abroad, and to help alleviate our serious balance-of-payments problem.

I cannot escape the feeling that the section is not the best or fairest approach to those problems. It is discriminatory and costly. But it is also the studied recommendation of the President at a time when the Nation is faced with a sluggish, listless economy. Furthermore, we are faced, in the closing weeks of this session, with only the choice of saying yes or no. It is too late to start anew with the long process of drafting new proposals in this complex field.

To reject the provision means doing nothing. It means ignoring the state of the economy, and turning down the remedy sought by the President. If we accept the provision we have at least made an effort to do something beneficial for the economy, and an effort to help get the country moving again.

Therefore, I shall vote for the provision of section 2 as recommended by a majority of the committee.

Mr. KERR. Mr. President, I suggest the absence of a quorum. I have suggested it three times, and three times I have yielded for other purposes. I now suggest the absence of a quorum.

The PRESIDING OFFICER. The clerk will call the roll.

The legislative clerk proceeded to call the roll.

Mr. GORE. Mr. President, in view of the agreement, I ask unanimous consent that further proceedings under the call be dispensed with.

The PRESIDING OFFICER. Without objection, it is so ordered.

The question is on agreeing to the amendment offered by the Senator from Virginia [Mr. BYRD] and other Senators, to strike all of section 2, as amended, beginning at line 8 page 8, down to and including line 16 of page 38. The yeas and nays have been ordered, the clerk will call the roll.

The legislative clerk called the roll.

Mr. MANSFIELD (after having voted in the negative). Mr. President, on this vote I have a live pair with the Senator from Ohio [Mr. LAUSCHE]. If he were present and voting, he would vote "yea." If I were at liberty to vote, I would vote "nay." I therefore withdraw my vote.

Mr. HUMPHREY. I announce that the Senator from Nevada [Mr. BIBLE], the Senator from Michigan [Mr. HART], the Senator from Ohio [Mr. LAUSCHE], the Senator from Wyoming [Mr. McGEE], and the Senator from Massachusetts [Mr. SMITH] are absent on official business.

I further announce that the Senator from New Mexico [Mr. ANDERSON], the Senator from Alaska [Mr. GRUENING], the Senator from Missouri [Mr. LONG], and the Senator from Missouri [Mr. SYMINGTON] are necessarily absent.

On this vote, the Senator from Alaska [Mr. GRUENING] is paired with the Senator from Missouri [Mr. SYMINGTON].

If present and voting, the Senator from Alaska would vote "yea," and the Senator from Missouri would vote "nay."

I further announce that, if present and voting, the Senator from Missouri [Mr. LONG], and the Senator from Massachusetts [Mr. SMITH] would each vote "nay."

On this vote, the Senator from Montana [Mr. MANSFIELD] is paired with the Senator from Ohio [Mr. LAUSCHE]. If present and voting, the Senator from Montana would vote "nay," and the Senator from Ohio would vote "yea."

Mr. KUCHEL. I announce that the Senator from South Dakota [Mr. BOTTUM], the Senator from Indiana [Mr. CAPEHART], the Senators from Kansas [Mr. CARLSON and Mr. PEARSON], the Senator from Idaho [Mr. JORDAN], the Senator from New Hampshire [Mr. MURPHY], and the Senator from Texas [Mr. TOWER] are necessarily absent.

The Senator from Wisconsin [Mr. WILEY] is detained on official business.

If present and voting, the Senator from Indiana [Mr. CAPEHART], the Senator from Idaho [Mr. JORDAN], the Senator from New Hampshire [Mr. MURPHY], and the Senator from Kansas [Mr. PEARSON] would each vote "nay."

On this vote, the Senator from Texas [Mr. TOWER] is paired with the Senator from Kansas [Mr. CARLSON]. If present and voting, the Senator from Texas would vote "yea," and the Senator from Kansas would vote "nay."

The result was announced—yeas 30, nays 52, as follows:

[No. 221 Leg.]

YEAS—30

Alken
Allott
Bartlett
Boggs
Burdick
Bush
Byrd, Va.
Cannon
Chavez
Curtis

Douglas
Goldwater
Gore
Hickenlooper
Hruska
Keating
Kefauver
McNamara
Miller
Morse

Neuberger
Prouty
Proxmire
Robertson
Russell
Saltonstall
Stennis
Thurmond
Williams, Del.
Yarborough

NAYS—52

Beall
Bennett
Butler
Byrd, W. Va.
Carroll
Case
Church
Clark
Cooper
Cotton
Dirksen
Dodd
Eastland
Ellender
Engle
Ervin
Fong
Fulbright

Hartke
Hayden
Hickey
Hill
Holland
Humphrey
Jackson
Javits
Johnston
Jordan, N.C.
Kerr
Kuchel
Long, Hawaii
Long, La.
Magnuson
McCarthy
McClellan
Metcalfe

Monroney
Morton
Moss
Mundt
Muskie
Pastore
Pell
Randolph
Scott
Smathers
Smith, Maine
Sparkman
Talmadge
Williams, N.J.
Young, N. Dak.
Young, Ohio

NOT VOTING—18

Anderson
Bible
Bottum
Capehart
Carlson
Gruening

Hart
Jordan, Idaho
Lausche
Long, Mo.
Mansfield
McGee

Murphy
Pearson
Smith, Mass.
Symington
Tower
Wiley

So the amendment offered by Mr. BYRD of Virginia, for himself and other Senators, was rejected.

Mr. KERR. Mr. President, I move that the vote by which the amendment was rejected be reconsidered.

Mr. HUMPHREY. Mr. President, I move that the motion to reconsider be laid on the table.

The motion to lay on the table was agreed to.

The PRESIDING OFFICER. Pursuant to the agreement, the clerk will state the first committee amendment passed over.

The CHIEF CLERK. On page 41, in line 18, and on page 42, in lines 4 and 7, after the words "related to" it is proposed to insert the words "or associated with."

Mr. GORE. Mr. President—

Mr. HUMPHREY. Mr. President, will the Senator from Tennessee yield to me, so that I may make an inquiry?

Mr. GORE. I yield.

Mr. HUMPHREY. I wish to inquire whether the Senator from Tennessee hopes the Senate will vote tonight on this amendment. I ask this question so that we may have some information for the guidance of Senators.

Mr. GORE. I do not anticipate that the vote on the amendment will be taken tonight.

Never before did so much money hang on so few words. That is what this amendment involves. I expect to discuss the amendment, not in a dilatory way, but at some length. The amendment goes to the very heart of the expense account abuse. If the Senate wishes to leave the abuses of expense accounts as they are and permit them to go even further, and permit them to become worse, the Senate will adopt the committee amendment. But this is such a serious question that I expect to discuss it at some length. This concerns one of the scandals of our country. One of the slo-

gans that has become a symbol of cheating is "it is deductible."

So I expect to speak at considerable length against the amendment. I do not mean to say that I shall speak for a day or two—

Mr. HUMPHREY. I understand.

Mr. GORE. I am not threatening; but I do not think we shall soon reach a vote on the amendment.

Mr. HUMPHREY. I wish to make clear that the Senator from Tennessee has not been dilatory. He has been most cooperative.

Mr. GORE. I thank the Senator from Minnesota.

Mr. HUMPHREY. But several Senators have asked the majority leader or me about the schedule.

I believe the amendment should be debated, and I have no intention of indicating to the contrary.

Mr. GORE. In my judgment in this case the Senator from Tennessee and the Senators associated with him are representing the administration; and that point should be made crystal clear before the debate on the amendment is concluded.

Mr. SMATHERS. Mr. President, will the Senator from Tennessee yield?

The PRESIDING OFFICER (Mr. PELL in the chair). Does the Senator from Tennessee yield to the Senator from Florida?

Mr. GORE. I yield.

Mr. SMATHERS. That is just the opposite from the position of the Senator from Tennessee and the Senators associated with him on the amendment which was voted on a few minutes ago.

Mr. GORE. That is debatable. The provision now in the bill with respect to investment credit bears but little resemblance to what the President requested.

Mr. SMATHERS. The President originally requested 15 percent. It was later, I believe, reduced to 11 percent, and then 7 percent. So I do not think the Senator can take the view that he was on the President's side when he opposed investment credit.

Mr. GORE. I am not sure the junior Senator from Florida misunderstands it as much as his statement might lead one to conclude.

Mr. KERR. Mr. President, will the Senator yield?

Mr. GORE. In just a moment.

I think the Senator from Florida understands that the provision recommended by the President was 15 percent of net investment, intended as a reward for concerns which invested in plant and facilities over and beyond their depreciation allowance. What we have now is a tax reduction for almost everybody who buys a depreciable item.

Mr. KERR. Mr. President, will the Senator yield?

Mr. GORE. I yield to the Senator from Oklahoma.

Mr. KERR. The Senator from Tennessee is aware of the fact that the last thing the majority leader read into the RECORD was a letter from the Secretary of the Treasury, Mr. Dillon, in which he specifically stated that, speaking for the administration, he favored the tax credit provision before the Senate and urged that it be approved; is he not?

Mr. GORE. I heard the letter read, and I challenge the Senator from Oklahoma to obtain a similar letter recommending approval of wide-open expense accounts.

Mr. KERR. The Senator from Oklahoma was not talking about that—

Mr. GORE. I challenge the Senator—

Mr. KERR. The Senator from Tennessee would like to run from the corner into which he has been maneuvered. If he wants to escape, I always believe in giving the Senator the opportunity to escape.

Mr. GORE. I am willing to have the Senator from Oklahoma call Secretary Dillon and see if he can get a letter approving this amendment.

Mr. KERR. If the Senator from Oklahoma does so, will the Senator from Tennessee vote for it?

Mr. GORE. No; I would not vote for it. There are many reasons which influence me otherwise. These three little words sound innocent enough, "in association with"—

Mr. KERR. I would like to correct the Senator.

Mr. GORE. "Or associated with."

Mr. KERR. "Or associated with."

Mr. GORE. My friend is correct. He can be correct in the little things and wrong in the big things more often than any other man I know.

Mr. KERR. I thank the Senator, because to that degree I am ahead of him.

Mr. GORE. This raises a question. Since he and I have been in disagreement so often of late, I do not know how the Senator could claim to be too far ahead if he uses contrary positions as a measure.

Mr. KERR. Mr. President, will the Senator yield?

Mr. GORE. I yield.

Mr. KERR. If we were in disagreement all the time, would not that have to prove that the Senator from Oklahoma thought he was correct in his statement?

Mr. GORE. It is not all the time. There is a measure left for the Senator from Oklahoma to have an edge in error on the junior Senator from Tennessee.

Mr. KERR. At the end.

Mr. GORE. I am willing to concede that the edge may get thin between friends.

Mr. President, I started to say that these three words sound innocent enough, but when I read the committee report, which gives the committee's legislative intent, and therefore the legal effect and meaning of the three little words, I am unable to determine any item of personal expense that is now deductible under the scandalous practices that prevail today which would not be deductible under this amendment as interpreted by the committee report. As the meaning of these three words is interpreted by the report, this is a formula for tax cheating.

Mr. LONG of Louisiana. Mr. President, will the Senator yield?

Mr. GORE. I yield.

Mr. LONG of Louisiana. Where does the Senator get the idea that a clearly deductible item is tax cheating? It seems to me that if the law says one owes something, he owes it; and if he

does not pay, he is cheating. But if something is deductible under law, and intended to be so, I cannot see where the Senator gets the idea that a person is cheating if he takes a deduction he is entitled to take in his income tax accounting.

Mr. GORE. The Senator would maintain then, I take it, that there is no cheating under practices which now, unfortunately, prevail?

Mr. LONG of Louisiana. The Senator from Tennessee may have a different point of view from that of the Senator from Louisiana, but it is my theory that if one takes a deduction which is permitted under law, he is not cheating. If he attempts to take one that is not permitted, if he falsifies, if he misrepresents a fact, if he does something the law never intended that he could do, he is cheating; but if he has the right to deduct something—and I am talking about this amendment—such as the expense of taking to lunch or dinner someone he is trying to do business with, if it is clearly intended that the cost of entertaining someone a person is trying to do business with, or hoping to do business with, is a deductible item, and the law intends that a person may be permitted to take such deduction, how does that become cheating?

So far as this Senator is concerned, I hope the Senator from Tennessee is not trying to contend that someone is cheating if he takes a deduction which the law intended to permit him to take.

Mr. GORE. I take it, then, that the junior Senator from Louisiana would maintain that no cheating is involved in the scandalous practices which now prevail, and which were cited by the President of the United States and the Secretary of the Treasury in messages to the Congress and in testimony before committees of both Houses of Congress? Do I correctly understand the Senator to maintain that there is no cheating involved in present practices?

Mr. LONG of Louisiana. May I answer in my own words?

Mr. GORE. Certainly.

Mr. LONG of Louisiana. My answer is that I have not even seen an example of what the Senator is referring to, though I can guess what it may be.

My answer is that if the person, for example, took a man and his wife to dinner, in the hope of doing some business, or entertained them at a theater, not being in the theater business himself—a practice which might be expected of one in his business or, as Secretary Dillon said, to be expected in a particular business, even though he did not recommend being able to deduct the expense—if the court said that the man could deduct the expense, and the legislative history in the Congress permitted that deduction, in my judgment that would not be cheating.

If a man wrote down on an expense account somewhere a claim that he had entertained somebody he had never entertained, I would regard that as cheating. But this Senator does not think that someone is cheating when he merely takes a deduction or engages in a course of conduct which the law permits.

If the Senator wants the conduct outlawed, Congress could outlaw it, but I do not proceed on the assumption that a man violates tax law if the Congress never passes a law to tax him.

Mr. GORE. I think the Senator makes himself clear. He splits a legal hair and says that if a man can get by with it under present law that is not cheating. He does not say that it is morally right. He does not say that it is not tax avoidance. As I understand the Senator, he says that under the law it is not cheating.

Let me read to the Senator what the President of the United States said about it:

In recent years widespread abuses have developed through the use of the expense account. Too many firms and individuals have devised means of deducting too many personal living expenses as business expenses, thereby charging a large part of their cost to the Federal Government. Indeed, expense account living has become a byword in the American scene.

This is a matter of national concern, affecting not only our public revenues, our sense of fairness, and our respect for the tax system, but our moral and business practices as well. This widespread distortion of our business and social structure is largely a creature of the tax system, and the time has come when our tax laws should cease their encouragement of luxury spending as a charge on the Federal Treasury. The slogan—"It's deductible"—should pass from our scene.

Tighter enforcement of present legislation will not suffice. Even though in some instances entertainment and related expenses have an association with the needs of business, they nevertheless confer substantial tax-free personal benefits to the recipients. In other cases, deductions are obtained by disguising personal expenses as business outlays.

Mr. President, I digress a moment from reading the President's message to point out that another form of the word "associated" which the committee proposes to insert into the bill is contained in the sentence I have read from the Presidential message. I read it again:

Even though in some instances entertainment and related expenses have an association with the needs of business, they nevertheless confer substantial tax-free personal benefits to the recipients. In other cases, deductions are obtained by disguising personal expenses as business outlays.

Mr. CLARK. Mr. President, will the Senator yield for a question?

Mr. GORE. I will yield in a moment. I digress again from reading the President's message.

As the President has said, when a citizen disguises personal expenses as business outlays, I say to my friend from Louisiana that that is cheating.

I yield to the Senator from Pennsylvania.

Mr. CLARK. Mr. President, I would dislike to see the debate involve a question of semantics. I should like to ask the Senator a question in that regard.

I see no particular need to let the argument depend upon whether under present practices tax cheating is going on at a great rate. Does not the Senator agree with me that the committee amendment would require no substantial change in current expense account procedures?

Mr. GORE. When one reads the committee report carefully—it must have been devised by a shrewd tax lawyer from Philadelphia—

Mr. CLARK. I thank my friend for the implied rebuke.

Mr. GORE. I did not mean it as a rebuke. I was referring to the traditional competence of a Philadelphia lawyer.

Mr. CLARK. I thank my friend for his explanation.

Mr. GORE. When one reads the majority report of the committee, the authorship of which to me is unknown, one can only conclude, it seems to me, that the adoption of the amendment, with the legislative intent given by the majority report, would make the situation worse instead of better, because it would place legislative approval upon a whole line of unfortunate decisions and practices which help to constitute the pattern of abuse which the President has so accurately described.

Mr. CLARK. Mr. President, will the Senator yield further?

Mr. GORE. I yield.

Mr. CLARK. The Senator has been a member of this body far longer than I have. This is my sixth session. I have followed the Senator's lead on the question of expense account deductions ever since I became a Senator. The Senator attacked certain practices even before I became a Member of this body.

I had the privilege of being the author of an amendment—we called it the "anti-swindle-sheet amendment"—which passed the Senate on one occasion. It was promptly "kicked out" in conference by conferees who had voted against it in the Senate.

I wonder if the Senator would agree with me that under present law, which I gather would be made even worse under the committee amendment, open, notorious, scandalous, unethical and morally wrong practices are rampant in America today in connection with expense account deductions from income taxes.

Mr. GORE. I adopt the words used by the Senator from Pennsylvania. I have read from the message of the President of the United States equally strong words. He said, "deductions are obtained by disguising personal expenses as business outlays."

Mr. CLARK. Mr. President, will the Senator yield further?

Mr. GORE. I yield.

Mr. CLARK. The Senator will recall the famous case of the Pennsylvania couple who operated a dairy business in Erie, Pa. They took a safari to Africa, by way of London, Paris, and Rome. They ran up bills of more than \$20,000. When they came back to America, they were allowed by the Tax Court of the United States to deduct those bills for a personal and private safari to Africa as a proper business expense deduction, and the deduction was held to be in accordance with the present law.

Mr. GORE. I remember that case. It is one of the many unfortunate decisions which have helped to create such a pattern of tax avoidance, tax abuse, and tax cheating under present law.

Mr. CLARK. Mr. President, will the Senator yield?

Mr. GORE. I yield.

Mr. CLARK. Does the Senator recall further the notorious case of a very lovely and able motion-picture actress who, some years ago, was held entitled to deduct as a business expense a gift of very expensive jewelry to her make-up assistant and to her director on the ground that she had to make the gift in order to keep up with the Joneses in Hollywood, and that was held to be a proper business expense. The name of the lovely lady was Olivia DeHaviland, in case my friend needs assistance to his memory.

Mr. GORE. My memory of the loveliness of the lady prevents my remembering anything bad about her.

Mr. CLARK. I thank my friend. Since I love her as much as he, we should not be permitted to refer to the subject further on the floor of the Senate.

Will the Senator yield further?

Mr. GORE. I yield.

Mr. CLARK. Would the Senator not agree with me that as a result of present interpretation by the courts that expense deductions of hundreds of millions of dollars of tax revenue, which in accordance with any elementary system of justice and equity should be paid into the Treasury of the United States, are being lost, with the result that other taxpayers who do not live the same kind of life, who do not go on safaris to Africa, who do not engage in making expensive gifts of jewelry to people associated with them in business, who do not have private yachts, who do not have private hunting lodges, who do not go to the Stork Club and New York theaters with Uncle Sam paying 52 cents of every dollar of the money that is spent there, must themselves pay far higher taxes than otherwise would be the case?

Mr. GORE. I fully agree. The President has made that point very clearly.

Mr. LONG of Louisiana. Mr. President, will the Senator yield while he is talking about the safari?

Mr. GORE. Not now.

Mr. LONG of Louisiana. The Senator is very wise.

Mr. GORE. I shall finish reading the President's message, and then I shall be glad to yield. Continuing to read the President's statement:

But under present law, it is extremely difficult to separate out and disallow such pseudobusiness expenditures. New legislation is needed to deal with the problem.

I therefore recommend that the cost of such business entertainment and the maintenance of entertainment facilities (such as yachts and hunting lodges) be disallowed in full as a tax deduction and that restrictions be imposed on the deductibility of business gifts, expenses of business trips combined with vacations, and excessive personal living expenses incurred on business travel away from home.

I feel confident that these measures will be welcomed by the American people.

I digress to say that I am sure the President was referring to the kind of people described by the senior Senator from Pennsylvania, the great bulk of our people who are not beneficiaries of unlimited expense accounts, who pay their taxes through withholding from their wages and their salaries, and who

must dip in their pockets and pinch their pennies to pay their tax.

Mr. CLARK. Mr. President, will the Senator yield for a final question?

Mr. GORE. I yield.

Mr. CLARK. I should like to make very clear to the Senate, through the RECORD, that the luxury spending which the Senator from Tennessee and I have been discussing, and which the President of the United States has condemned, has resulted in the Government of the United States paying 52 cents on every dollar of business expense deduction claimed by a corporation on its personal income tax, and even more on the expense account of a wealthy individual who is in an income tax bracket higher than 52 percent when he takes those deductions on his own income tax. Am I correct?

Mr. GORE. The Senator is correct. But I am not sure that the dollars and cents involved constitute the most serious danger from a perpetuation of that practice. The President refers to the moral values. I read again what he said:

This is a matter of national concern, affecting not only our public revenues, our sense of fairness, and our respect for the tax system, but our moral and business practices as well.

Mr. President, when a scandalous practice of expense account abuses of our tax laws threatens to undermine the moral fiber of our country and threatens to disrupt the tax system, which is based primarily upon voluntary compliance, I say that it is a serious matter indeed. In opposing the amendment, I am confident that I am representing the wishes of the "American people" to whom the President referred.

Mr. CLARK. And also the wishes of the President of the United States. Is that not correct?

Mr. GORE. I fully believe so.

Mr. MANSFIELD. Mr. President, will the Senator yield?

Mr. GORE. I yield.

Mr. MANSFIELD. The Senator indicated sometime earlier today that there would not be a vote on the amendment tonight.

Mr. GORE. I expressed an opinion.

Mr. MANSFIELD. The Senator expressed that opinion.

Mr. GORE. Yes.

Mr. MANSFIELD. Would the Senator be amenable to considering a vote sometime tomorrow, say, at 11 o'clock or thereabouts?

Mr. GORE. I must say to the distinguished majority leader that, as he knows, I have tried to cooperate. I wanted these issues to be brought fully before the Senate. I wanted the Senate Finance Committee, which is responsible for the amendment and for the majority report, to carry the burden of persuading the Senate to agree to the amendment, which would subvert the recommendation of the administration on curtailing abuses of expense accounts.

In order to cooperate with the Senator, we agreed earlier to adopt en bloc about 165 amendments, I believe.

Mr. MANSFIELD. That is correct.

Mr. GORE. One vote has already been taken. So far as I am personally

concerned, I see no reason why we could not have a vote sometime tomorrow. But in all fairness to a number of Senators who have indicated their interest in the question and their willingness to oppose the amendment, I do not wish, at this late hour, when so many Senators are absent, to enter into a unanimous-consent agreement. So I suggest that the Senator let the request go over until tomorrow. It may then be possible to reach some agreement. There is no intent on my part to be dilatory in reaching a vote on the question. I want the amendment to be fully discussed. I wish to be sure that every Senator understands the interpretation placed upon those three words by the majority report. That will require some time, not only for myself but for other Senators.

Mr. MANSFIELD. Does the Senator have in mind any particular hour at this time, or would he prefer to let it go over until tomorrow?

Mr. GORE. I would prefer to let it go until tomorrow, because I assume the junior Senator from Florida will wish to speak, and the junior Senator from Louisiana has already indicated his concern. I know of several Senators who wish to speak against the amendment.

Mr. SMATHERS. So far as the junior Senator from Florida is concerned, I can be relatively brief. I believe that nearly every Senator has already made up his mind as to how he will vote on this particular amendment. I know that the able Senator from Tennessee will make an excellent record in support of his position. I have no doubt that those of us who will speak for the Committee on Finance will be able to make a pretty good record also in a short time. I do not operate under any illusion that what we say, or even what the able Senator from Tennessee may say, will change a great many votes. So far as I am concerned, I am perfectly agreeable to enter into some reasonable unanimous-consent agreement.

Mr. GORE. I do not compliment myself by thinking that what I am about to say will change many votes. I do believe that what is said in the majority report is going to change a large number of votes.

Mr. SMATHERS. I am delighted that the Senator from Tennessee should think so. I am sure the Senator thought the same of the amendment that has just been rejected.

Mr. GORE. I did not expect to win that fight, but I do expect to win this one.

Mr. SMATHERS. The Senator has been in the Senate long enough to know that if we were to ask Senators who are now present, they could tell us how they expect to vote on the amendment.

Mr. GORE. I know how the Senator from Florida is going to vote. He happens to be from Miami.

Mr. SMATHERS. That is correct—Miami, Fla.

Mr. GORE. I know that there is great concern in Florida about yachts in the harbors and all the ocean-front hotel suites that are held in the name of great corporations. I know that expense ac-

count living is important to the junior Senator from Florida.

Mr. SMATHERS. If the Senator wanted to be fair, all that he has been talking about, the yachts, and all that, unless they are primarily used for business activity, they are eliminated and are not allowable deductions. That is what we intended to do.

Mr. GORE. Let me read the President's statement, and I will let the Senator tell me what this amendment does. Let me read what the President of the United States said.

Mr. SMATHERS. I heard what he said.

Mr. GORE. The President said:

Too many firms and individuals have devised means of deducting too many personal living expenses as business expenses.

I am talking about the taxpayer who disguises expenditures for his own personal benefit as business outlays, in order to obtain a deduction, and use his expense account to get a deduction on taxes of the company which he serves. That is what I am talking about.

Mr. SMATHERS. I am with the Senator on that. We want to stop it. The Senator is exactly right.

Mr. GORE. I am talking this kind of deduction.

Mr. SMATHERS. We want to get at that problem too.

Mr. GORE. The majority report does not indicate that.

Mr. KERR. Will the Senator yield for a question? Is there any possibility of agreeing in the next few minutes on a unanimous consent agreement on a time certain tomorrow around noon to vote on the amendment?

Mr. GORE. I have already indicated that I could not enter into such an agreement. I assure the Senator, as I have already assured the majority leader, that I have no dilatory tactics in mind. I expect to show unmistakably what the majority report intends these words to mean. Fortunately we do not have to listen to speeches about what these words mean. The majority report has told us what the words mean and what they are intended to mean. They mean that no substantial loophole on expense account abuses will be closed. They mean that, in many respects the situation will be made worse than it is now.

Mr. DIRKSEN. If the Senator will yield, and addressing myself to the majority leader, I wonder if we could concur in a unanimous-consent request to reach an understanding that there will be no vote on this amendment tonight.

Mr. MANSFIELD. I do not believe we need any unanimous-consent agreement for that. That appears to be the fact.

Mr. DIRKSEN. I think, however—

Mr. GORE. I am agreeable.

Mr. DIRKSEN. It would be safe for Senators to go to dinner or go home or to fill engagements, if there were such an understanding.

Mr. GORE. I have a dinner engagement at 7:30, which I should like to keep.

Mr. SMATHERS. If no attempt is made to deduct the expense.

Mr. DIRKSEN. I have no engagement. I should like to be able to assure Sen-

ators on this side of the aisle that it would be safe for them to go home.

Mr. GORE. So far as I am concerned, the Senator can give that assurance. I should like to leave around 8 o'clock.

Mr. DIRKSEN. So would I.

Mr. MANSFIELD. The Senator has given me his assurance that he would not engage in dilatory tactics or delaying tactics.

Mr. GORE. Unless H.R. 10 is offered as an amendment to the bill.

Mr. MANSFIELD. I know the Senator to be an honorable man. I hope that the unanimous consent request will be given serious consideration tomorrow when we convene.

Mr. GORE. I am sure it will be. So far as I am concerned, I hope a vote on this amendment can be reached tomorrow.

Mr. MANSFIELD. Tomorrow is a long day. I hope that at a reasonable hour we shall be able to reach such an agreement. There are other amendments to be considered in addition to the committee amendments which remain to be considered, which have been set apart from those that have been agreed to. Other amendments have been submitted.

Mr. GORE. If in some way all copies of the majority report could be burned, we could then let the Senators who support the amendment tell us what it means. Unfortunately what they say cannot be heard because what is written speaks so loud.

Mr. SMATHERS. After the Senator from Tennessee has disposed of the Senator from Illinois, I should like to ask the Senator, in all fairness to read one paragraph—

Mr. DIRKSEN. May I address myself to the majority leader, with the consent of the Senator from Florida and the Senator from Tennessee? May we assume that there will be no vote tonight?

Mr. MANSFIELD. We have no choice.

Mr. GORE. Let me first read to the Senator what the President said. I know the President is a warm friend of the junior Senator from Florida.

Mr. SMATHERS. He is that.

Mr. GORE. I know the Senator will want to hear what the President of the United States said about these practices, which the junior Senator from Florida is defending.

Mr. SMATHERS. I have read it. The Senator is unfair in saying that I am defending practices that are illegal or immoral. I know he does not mean to say that.

Mr. GORE. I mean—

Mr. SMATHERS. I do not believe it is fair for the Senator to make that kind of imputation.

Mr. GORE. I say without qualification that a Senator who supports this amendment, after having read the majority report, supports a continuation of the situation which the President has described.

Mr. SMATHERS. I do not worry about myself, but I highly resent the Senator from Tennessee saying it about the Senator from Virginia [Mr. BYRD], or about the Senator from Utah [Mr. BENNETT], one of the pillars of the Mormon Church.

I also highly resent his saying it about the Senator from Louisiana [Mr. LONG], whose character is above reproach.

Mr. GORE. Let us see what I have said.

Mr. SMATHERS. The reputations of these men are above reproach.

Mr. GORE. I do not yield further until I have stated my position.

I said this, and I say it again: In my considered opinion a Senator who supports the adoption of this amendment, with the interpretation of its meaning in the report, votes to continue practices which the President of the United States has described in the message which I have been reading.

Mr. SMATHERS. Mr. President, will the Senator yield for a question?

Mr. GORE. I yield.

Mr. SMATHERS. Does not the Senator really mean to say that no one except the Senator from Tennessee has interpreted the language of the report in that way. If all of us interpreted the report in that way we would not be for it, any more than the junior Senator from Tennessee is for it now. It is merely a question of the meaning of the English language.

Mr. GORE. Would the Senator from Florida like me to tell what I know about the report?

Mr. SMATHERS. Probably the Senator from Tennessee ought to do that. Perhaps he has a duty to tell everything.

Mr. GORE. Suppose the junior Senator from Florida proceeds to tell what he knows about it?

Mr. SMATHERS. All I know about it is what I read. I know where it came from.

Mr. GORE. Where did it come from?

Mr. SMATHERS. It came as a result of the joint efforts of the Treasury of the United States and the staff of our committee. That is precisely where it came from. We asked them to do what they could to resolve the matter so that abuses in this area could effectively be eliminated.

Mr. GORE. That covers a great deal.

Mr. SMATHERS. I do not know who was better able to prepare this kind of language than the staff. Such language does not presume that every businessman is a cheat and a crook.

Mr. GORE. Does the Senator from Florida wish to reveal his part in it?

Mr. SMATHERS. Yes; I shall be delighted to reveal my part. I asked the members of the staff if they would prepare language that would make some sense; and language that did not presume every businessman, no matter where he was or where he resided, to be a crook or a cheat. That is what I asked them to prepare. They did so. We had the assistance of a representative from the Treasury Department. The Treasury, of course, would like to tighten up the language much more than it is in the bill.

Mr. GORE. I thought the Senator told us a few moments ago that the Treasury drafted the language.

Mr. SMATHERS. At my request, to provide some language which would be reasonable with respect to the business community, and recognizing that some

members of the business community, at least, were decent, honorable, fine people, and that legitimate deductions for legitimate business purposes were not the great evil which the Senator from Tennessee says they are.

I agree that the inclusion of personal expenses as business deductions ought to be stopped.

Mr. GORE. Mr. President, I do not yield further just now. The Senator from Florida has made his position reasonably plain, and I concede that he has every right and duty to fulfill his duty to represent his State as he sees fit. I fully accord to him the right to select his position and to exercise what influence he feels it proper to exercise upon a draft of a report or any other action of a committee on which he serves, or upon any other action of the U.S. Senate.

The Senator from Florida has said that the junior Senator from Tennessee is the only one who places this kind of interpretation upon the report.

Mr. SMATHERS. I am in error. I retract that statement. I know there are others, but they are not a majority of the Committee on Finance.

Mr. GORE. I thank the Senator from Florida for that concession. I am sure there are many more Senators who agree with me.

Mr. President, I shall finish reading the President's message on this subject:

I feel confident that these measures will be welcomed by the American people. I am also confident that business firms, now forced to emulate the expense account favors of their competitors, however unsound or uneconomical such practices may be, will welcome the removal of this pressure. These measures will strengthen both our tax structure and the moral fiber of our society. These provisions should be effective as of January 1, 1962, and are estimated to increase Treasury receipts by at least \$250 million per year.

I ask unanimous consent to have printed at this point in the RECORD a statement by Mr. Clarence Randall, which is contained in the committee report on page 408.

There being no objection, the statement was ordered to be printed in the RECORD, as follows:

Gone are the days when a salesman occasionally wined and dined his favorite customer, or perhaps gave a small theater party. Nowadays, when the deal gets big enough, the company yacht weighs anchor and moves into position, the company plane takes off for a duckblind in Arkansas, or the best hotel in Miami throws open its doors to expectant dealers for a week of continuous circus.

The distaff side is cut in, too, on both sides of the deal. How the ladies love it. With jet travel what it is, those who were getting a little tired of White Sulphur may now hope to look in on Capri or the Riviera.

The unseen partner in all this largesse, of course, the man who rides the afterdeck of the company yacht, copilots the duck hunters' plane, sits by while the caviar is spooned out and the crepes suzette are sizzling, the man who splits the check at the nightspot and hands the big bill to the headwaiter, is none other than Uncle Sam.

Mr. GORE. Mr. President, the House of Representatives substantially agreed with the President's recommendation, although the House bill does not contain

provisions as strong as the President recommended. But the House language plus the report of the House Ways and Means Committee will result in a great improvement in this situation, which the President says threatens the moral fiber of our country.

After long and careful consideration, the House voted for a provision, which, although falling short of the President's recommendations, would go a long way toward establishing a fairer set of rules. It would permit deductions for entertainment more closely related to the conduct of business, but would cut out deductions for many of the highly personal expenditures permitted under present law when the taxpayer can make a showing of some connection between the entertainment and the taxpayer's trade or business.

The allowance of deductions for such essentially personal entertainment has brought the integrity of the entire revenue system into disrepute. The expense account deduction has been a breeding ground for fraud and misrepresentation. It has encouraged disrespect for honest self-compliance with the tax laws among those not in a position to claim such deductions, but who have watched others satisfy their personal taste for amusement at the taxpayers' expense.

What has the Senate Finance Committee done with the House version of the bill? It has simply pulled the teeth from the proposal, leaving it merely with a dangling tongue—a tongue which is certain to confuse taxpayer and government official alike as to what it is trying to say. Certainly the vague and almost meaningless standard adopted by the committee will do very little, if anything, to change the style of operation of those who have been living high on their expense accounts at the cost of their fellow citizens.

THE PROBLEM

The basic problem is whether this country can continue to afford to permit a small group of taxpayers to take tax deductions for highly personal items such as nightclub hopping, fancy yachts and swanky country clubs, while the great majority of their fellow taxpayers cannot take such deductions. From a practical point of view the concern of the Nation is not only the basic unfairness of this situation—in itself a vital consideration—but also the effect that this legally created unfairness has upon those who are discriminated against. It makes them resentful of the law which permits such a situation to exist, and encourages them toward laxness in discharging their full tax obligations. It is quite natural to feel: "Why should I help keep that fellow on the gravy train—paying for his fancy yacht and swanky country club?" An expansion of this type of thinking could eventually destroy our tax system, the keystone of which is its voluntary character. We rely on each taxpayer to be his own tax assessor. The essential honesty of our citizens and, most important in this context, their respect for our tax laws have enabled this system of voluntary self-assessment to function most effectively. However, like all good things, the system must be nurtured and protected.

Expense-account abuses have become a real threat to the continued effectiveness of our self-assessing system. Much taxpayer distaste has already been voiced against this unwarranted privilege. The danger signals are loud and clear. In his testimony before the House Ways and Means Committee and the Senate Finance Committee, the Secretary of the Treasury documented the situation in great detail, with numerous case studies and many samples of editorial comment from all over the country.

Here are a few of them: A corporation engaged in manufacturing was allowed to deduct \$991,665 in 1959 for yachts, club dues, shipboard conventions, hunting and fishing trips, and parties. A taxpayer engaged in the insurance business was allowed to deduct \$97,500 for meals, lodging, transportation, entertainment, books, gifts, and so forth. The amount deducted covered \$6,000 for an apartment and more than \$30,000 for food, beverages, and other entertainment.

Mr. DOUGLAS. Mr. President, will the Senator from Tennessee yield?

The PRESIDING OFFICER (Mr. LAUSCHE in the chair). Does the Senator from Tennessee yield to the Senator from Illinois?

Mr. GORE. I yield.

Mr. DOUGLAS. And Uncle Sam picked up 52 percent of the check in those cases; is not that true?

Mr. GORE. I take it that was true. Certainly it would be true if the expenses were paid by a corporation which had a tax rate of 52 percent.

But that is not the worst thing. That citizen had all of it paid by the corporation whose expense account he was abusing, or by the Federal Government which was permitting the deduction under a faulty tax law.

Mr. DOUGLAS. In other words, due to the fact that great corporations are controlled by their management—who generally own only a small proportion of the stock, but nevertheless, through the use of proxies, control the corporations—the management can charge these bills to the corporation, but are able to get back 52 percent, by means of the tax deduction.

Mr. GORE. And the small stockholders have very little voice in the operation of the corporation.

The combination of a corporate insider and the use of expense accounts has erected in our midst a small coterie of a privileged few who, because of their abuses, threaten—according to the President—the very moral fiber of our society.

Mr. LONG of Louisiana. Mr. President, will the Senator from Tennessee yield?

Mr. GORE. I yield.

Mr. LONG of Louisiana. The Senator from Tennessee has undertaken to give examples. The first example given today by the Senator from Pennsylvania had to do with a safari in Africa.

Mr. GORE. Yes, it was cited by the Senator from Pennsylvania.

Mr. LONG of Louisiana. Does the Senator from Tennessee know that that safari in Africa involved that person's successful attempt to claim the cost of

the safari as an advertising expense, and thus he was able to obtain a deduction? It had nothing to do with entertainment expense.

Mr. GORE. It had to do with personal pleasure—a safari in Africa, and also a trip in Europe. The man was drawing an expense account for his personal pleasure, and the bills were paid for him, and a deduction was given on the tax return of the concern by which he was employed.

Mr. LONG of Louisiana. Is the Senator from Tennessee familiar with the fact—

Mr. GORE. I am not very familiar with that case.

Mr. LONG of Louisiana. Is the Senator familiar with the fact that it had nothing to do with the case the Senator from Tennessee is making, because that claim was made for a deduction as an advertising expense. He claimed that the safari helped his advertising. He brought back from Africa numerous animal heads and animal hides, and all that was good advertising for his business; and he successfully claimed that deduction as an advertising expense.

Mr. GORE. But I respectfully suggest that that is covered by the description given by the President—in other words, a practice by which a personal expense is disguised as a business expense. I am not attempting to state the details of that case, and I do not wish to make a particular point of it, the senior Senator from Pennsylvania cited it. I recall having read about it. I heard about it. I think it involved the abuse of an expense account. I think it clothed personal expenses, as the President has said, with a business function.

Mr. LONG of Louisiana. It has nothing to do with improper entertainment allowance, as the Senator knows.

Mr. GORE. I did not say it was entertainment. There is something more involved than entertainment.

Mr. DOUGLAS. Mr. President, will the Senator yield?

The PRESIDING OFFICER (Mr. METCALF in the chair). Does the Senator from Tennessee yield?

Mr. GORE. I yield.

Mr. DOUGLAS. If my good friend from Louisiana quarrels with illustration No. 1, the safari to Africa submitted by the Secretary of the Treasury, what would he say to some 59 other cases which the Secretary of the Treasury submitted in volume 1 of the Senate hearings, some of which are being quoted by the Senator from Tennessee?

Mr. LONG of Louisiana. I shall be glad to discuss them if they are brought up, but the first one has nothing to do with the case. The Senator from Illinois loves to play on it and suggest it is an improper use of entertainment expense. That case involved an advertising expense. So far as I am concerned, I would be glad to outlaw advertising expenses as deductible items.

Mr. GORE. There is much more involved in this issue than merely entertainment. There is much more involved than taking someone to a restaurant in New Orleans, or Nashville, Tenn., or the 21 Club in New York. There is much

more involved than entertainment. I think many other abuses are involved.

Mr. LONG of Louisiana. I hope before the Senator gets through he recognizes that this particular language in the bill has nothing to do with the safari in Africa. It is not involved.

Mr. GORE. I will come to that.

Mr. DOUGLAS. Mr. President, will the Senator yield?

Mr. GORE. I yield to the Senator from Illinois.

Mr. DOUGLAS. May I take case No. 48?

Mr. GORE. I will cite something more than entertainment. A manufacturer was allowed to deduct \$34,000 for football and theater parties, a speedboat, and so forth.

Mr. DOUGLAS. Let me take case No. 48, on page 318, of part 1 of the hearings of the Senate committee, the case of a physician who claimed and was allowed an expense item of \$1,182 for travel to Europe, where he spent 6 of the 22 days in Europe attending a medical congress at which he delivered a paper and presided at one of the meetings. The taxpayer was accompanied by his wife and two children.

Mr. GORE. This is not entertainment.

Mr. DOUGLAS. No; this is expense.

Mr. GORE. Personal expense.

Mr. DOUGLAS. That is right. They were allowed as a deduction because he was improving his specialized professional skills.

Mr. SMATHERS. Mr. President, will the Senator yield? I am sure the Senator wants to be completely fair. In the report of the majority of the Finance Committee we specifically mentioned the kind of things that should be eliminated. We talk about the safari case on page 28 of the report. We want to overrule that decision. We agree that it is bad. We also say, so far as taking one's wife on a trip is concerned, that the expense for that is to be disallowed. These are obviously abuses and should have been done away with a long time ago.

Mr. GORE. If the Senator will let me discuss the majority report—

Mr. SMATHERS. This is a part of it.

Mr. GORE. I know. The Senator has also cited the majority report as saying that it is not desired to permit the allowance of expense for call girls.

Mr. SMATHERS. I hope the Senator does not object if the majority wants to eliminate that.

Mr. GORE. I do not make the point or make the objection. The point really is, Why is it cited? That item is not deductible under present law.

Mr. LONG of Louisiana. Mr. President, will the Senator show me where under present law he has that nailed down? I said I made one mistake in offering my "prudent man" expense account amendment. Instead of saying "a prudent man," I should have said "a prudish man."

Mr. GORE. A prudish man?

Mr. LONG of Louisiana. A prude; deduct what a prudish man would under the circumstances. Perhaps that would be more agreeable.

Mr. GORE. I heard the Senator make a somewhat similar statement a day or two ago. He said he made a mistake by not providing what "a pious man" would do.

Mr. LONG of Louisiana. It is the same idea.

Mr. GORE. I think there is a little difference between pious and prudish.

The Senator will recall that he offered that "prudent man" amendment, and when the committee took a hard look at the meaning of the amendment, it voted it out and then adopted the words "or associated with," which seemed reasonably harmless. But by the time the committee's report was written, it took on a meaning that is just as bad as the "prudent man" amendment was.

Mr. DOUGLAS. Mr. President, will the Senator yield?

Mr. GORE. I yield.

Mr. DOUGLAS. In other words, after the abominable "prudent man" provision was thrown out the front door, it was brought in through the back door?

Mr. GORE. Through the committee report.

Mr. DOUGLAS. Yes.

Mr. GORE. The Senator has raised a question about the majority report. I do not wish to be understood as charging that any member of the committee wrote this report. The report, however, must speak for itself. Fortunately, the Senate can know what the report says.

It is printed. Senators can examine it. A copy of it is on every Senator's desk. The report is adroitly drafted. It is drafted as if it followed a mathematical formula. A strawman, or in one case a strawwoman, is set up in order that the report can knock it down; and then we get the real meat and meaning of what is intended. I shall demonstrate it. This is a cleverly done report, and it subverts the whole effort to close the loophole of expense account abuses. I shall prove that even to the junior Senator from Florida.

Mr. SMATHERS. I will wait in great anticipation.

Mr. DOUGLAS. I hold in my hand something like 10 pounds of hearings. I believe that the Senator from Tennessee and I were present at almost every session of the hearings. The first volume consists of evidence produced by the Treasury. Here is the report. We have been debating the bill for 3 days. The attendance in the Chamber has not been so good. Has the Senator seen any Senator pick up a copy of volume I and go through it? Or has the Senator seen any Senator pick up a copy of the report and go through it?

Mr. GORE. How many pages is it?

Mr. DOUGLAS. Four hundred and twenty-five pages.

Mr. GORE. No; I have not. It is very difficult reading. But with respect to the pending amendment, I discovered enough to show to the Senate that the adoption of these simple, innocent little words "or associated with," as an amendment, with the interpretation given as the legislative intent of that amendment, will mean continuing the abuses which the President has complained of.

Mr. SMATHERS. Mr. President, will the Senator yield for a question?

Mr. GORE. I yield. The Senator is very generous. I know of his keen interest in this subject. I yield to the Senator from Florida.

Mr. SMATHERS. I have no more keen interest in this subject than in any other part of the tax bill. I recognize, however, that a great many legitimate businessmen and legitimate businesses have followed the practice of taking legitimate business deductions. I do not wish to imply that they are cheats or crooks, or that they are acting improperly.

Mr. GORE. I agree absolutely.

Mr. SMATHERS. I further recognize that many musicians, restaurants, and hotels make conventions their business and thereby contribute to the welfare of the economy of the States in which they are located. I do not wish to see them put out of business when they are conducting legitimate businesses.

I rose to ask the Senator a question. I think it would be very helpful in the discussion of this particular amendment if the Senators who are opposed to the amendment which was adopted by the Finance Committee would stop ranting and raving about the safari, about taking wives on trips, and all that sort of thing.

Mr. GORE. Now—

Mr. SMATHERS. Let me finish.

Mr. GORE. I do not wish to be described as ranting and raving.

Mr. SMATHERS. Under the committee report those evils would be eliminated.

Mr. GORE. Mr. President, I decline to yield further.

Mr. SMATHERS. The committee attempted to eliminate them.

Mr. DOUGLAS. What about the mortician in Florida who invited prospective customers to go out on a yacht, and charged off \$23,000, claiming an expense in order to get business?

Mr. SMATHERS. He ought to be ashamed of himself.

Mr. DOUGLAS. He got his \$23,000.

Mr. SMATHERS. We hope that what is happening to him is what happened to his customers.

Mr. GORE. Mr. President, I decline to yield further.

Mr. SMATHERS. Mr. President, will the Senator yield further?

Mr. GORE. I yield for the very eloquent remarks which I know my friend from Florida is about to make.

Mr. SMATHERS. Does not the Senator agree that it is not quite cricket, if I may borrow that word, to make a big argument, talking about a straw man and about alleged abuses and evils, and to connote thereby that the Finance Committee is in favor of these things, when the Finance Committee has already sought to eliminate them? We have provided language in the report specifically about those things.

Mr. DOUGLAS. What about the yachts at Fort Lauderdale?

Mr. SMATHERS. And the yachts at Fort Lauderdale, too, unless the costs can be proved to be primarily business expenses. All of that will have to stop.

Mr. GORE. Mr. President, who has the floor?

The PRESIDING OFFICER. The Senator from Tennessee has the floor.

Mr. GORE. I should like to use it to ask the junior Senator from Florida a question. I know it would be a violation of the rules for a Senator who has the floor to interrogate another Senator.

Mr. SMATHERS. I am happy to answer.

The PRESIDING OFFICER. Without objection, the Senator from Tennessee may ask the Senator from Florida a question.

Mr. GORE. I should like to ask the junior Senator from Florida a question as to the meaning of the pending amendment, as interpreted by the majority report.

If a businessman took his customers to the Kentucky Derby, could he deduct the cost of entertaining them under the terms of the amendment and the committee report?

Mr. SMATHERS. I do not believe he could, and I do not think that was the intention.

Mr. GORE. The committee report so provides.

Mr. SMATHERS. I would be interested in knowing where it so states.

Mr. GORE. If the Senator will let me proceed, I will come to that.

Mr. SMATHERS. If the trip was a part of a vacation, the deduction would not be permitted.

I have been told that if a man goes to the Kentucky Derby, if that is a part of a vacation he may not deduct that expense. At no time could a person deduct the expense of taking his wife.

If a man went to the Kentucky Derby as a part of a particular business, that would be different. The Senator from Tennessee is in the cattle business. There may be someone who may be in the race horse business.

Mr. GORE. Do not use me as an example.

Mr. SMATHERS. I thought that was a pretty good illustration, because we are talking about horses. The Senator is very knowledgeable about the cattle business.

In any event, if a person who goes to the Kentucky Derby could prove the trip was in connection with his business, the expense would be deductible if directly related to the business. The taxpayer would have the burden of proving it. His own self-serving statement would not be sufficient to prove it.

Mr. GORE. All he would have to prove would be that it was "associated with" his business.

Mr. SMATHERS. What I want to know is what the language really means.

Mr. GORE. Mr. President, I ask unanimous consent that I may propound another question to the junior Senator from Florida.

Mr. SMATHERS. I agree to the unanimous consent request. I am sure there is no objection.

Mr. GORE. Very well.

If a businessman used his 100-foot yacht to entertain potential clients, would a single penny be nondeductible under the Finance Committee report?

Mr. SMATHERS. Would it be non-deductible?

Mr. GORE. I hope the Senator will give an answer.

Mr. SMATHERS. With respect to yachts, the yachts, the hunting lodges, and all such things are called "facilities."

If the facility is primarily used in connection with the man's business—and he would have to establish that—he could deduct the portion of the expense which he could show as being directly related to his business.

Mr. GORE. "Or associated with."

Mr. SMATHERS. "Or associated with."

Mr. GORE. "Or associated with."

Mr. SMATHERS. The "or associated with" actually comes in the entertainment area.

Mr. LONG of Louisiana. Mr. President, will the Senator permit me to comment on the question of the yacht? I think I understand it.

Mr. GORE. I will permit the Senator to do so.

Mr. LONG of Louisiana. I will state my understanding of the provision.

The proposal would tighten up very severely on yachts, swimming pools, hunting lodges, and anything like that. It would work in the following manner:

First, a person could not deduct 5 cents of expense unless he could meet the primary test. The test would be the proof that the yacht, the swimming pool, or the hunting lodge was used primarily to entertain business guests. If it were used 51 percent for personal use, a person could not deduct 5 cents. That is point No. 1.

Point No. 2: I hope the Senator will hear this—

Mr. GORE. I am listening.

Mr. LONG of Louisiana. Point No. 1 is that a person must meet the primary test, which is proof that the facility is primarily for business entertainment. That is point 1.

Mr. GORE. Wait just a minute.

There is some conflict. The junior Senator from Florida [Mr. SMATHERS] said that the provision did not apply to facilities. Now the Senator from Louisiana says that it would.

Mr. LONG of Louisiana. I believe the RECORD will show that there is no conflict between the two answers.

Mr. GORE. The RECORD will show that there is a conflict. Perhaps we should resolve it now. Does the Senator from Florida say that the provision would or would not apply to facilities?

Mr. SMATHERS. It would apply. I was mistaken.

Mr. GORE. The Senator told us a few minutes ago that it would not.

Mr. SMATHERS. I was mistaken.

Mr. GORE. Again my friend from Florida is getting incorrect information about the report.

Mr. LONG of Louisiana. I believe I understand the point. In my judgment the provision is too strict. In the committee I voted that it was too strict. Let me show the Senator how it would operate. First, to deduct the first 5 cents for a swimming pool, yacht, hunting lodge, or some other facility, a taxpayer must prove that it is used primarily for

business purposes. In other words, if he entertains business interests 40 percent of the time in the yacht or hunting lodge, he cannot deduct any part of the expense. Before he can deduct any part of the expense, he must first meet the primary test. Only after he meets the primary test does he get the opportunity to prove what percentage of the time the facility was used to entertain business guests.

If he could prove he entertained business guests, let us say, 52 percent of the time, he could deduct 52 percent of the cost of the facility. To do so he must have records to prove who the business guests were and prove the percentage of time that the facility was used to entertain those particular business guests. I objected to that provision because I feel that a person who has a boat and can prove that he had business guests on it 25 percent of the time, should be able to deduct 25 percent of the cost of the boat. He cannot do so. He could not deduct a nickel of the expense under the bill as it is drawn.

Mr. GORE. I am aware that the junior Senator from Louisiana, my dear friend and colleague whom I admire and respect, was the author of the "prudent man" amendment. I do not know how far my friend would go in that regard. I would not venture to say. But he has just told us that the provision does not go far enough.

Mr. LONG of Louisiana. I guarantee one thing I would do that the Senator from Tennessee would not do, and something that the bill would not provide. I would certainly let a businessman who asks a customer to go to dinner with him, hoping to get his business, but who would not go unless his wife were invited, deduct the expense of the meal for the taxpayer and his wife and the customer and his wife, if it was a legitimate entertainment effort to try to obtain the business of that particular customer. The bill provides that a taxpayer may only deduct the cost of a businessman's meal and that of his wife. I think that is too strict.

Mr. DOUGLAS. Mr. President, will the Senator yield?

Mr. GORE. I yield to the Senator from Illinois.

Mr. DOUGLAS. The Senator from Louisiana has touched on an interesting point which demonstrates the principle involved. To demonstrate further the principle involved, a businessman invited a customer to go with him to Alaska so that in the fjords of Alaska they could discuss technical questions—although they could have discussed them as well at home. The customer invited said, "I cannot go without my wife." So the customer's wife was invited, but she said, "I cannot go unless there is another woman in the party; namely, the wife of the host."

So they took the wife of the host. The expenses of all four people were charged to the Government, being deducted from the businessman's income tax.

Mr. GORE. I wish to ask the Senators from Louisiana and Florida—

Mr. LONG of Louisiana. I would like to respond to that statement.

Mr. GORE. No; I wish to ask the question myself. I wish to ask either the junior Senator from Florida [Mr. SMATHERS] or the junior Senator from Louisiana [Mr. LONG] what language in the bill or the committee report would disallow deductions for hunting lodges.

Mr. LONG of Louisiana. I do not have the information at my fingertips, but the language about facilities establishes the test I have described.

Mr. GORE. What language would disallow a deduction for yachts, country clubs, theater tickets, prizefights and nightclubs?

Mr. LONG of Louisiana. Does the Senator mean in the bill?

Mr. GORE. I am asking the Senator from Louisiana what language in the bill or in the report would disallow such a deduction.

Mr. LONG of Louisiana. First, I should like to answer the question the Senator would not permit me to answer about the trip to Alaska.

Mr. GORE. I should like some answers to my present question.

Mr. LONG of Louisiana. I shall be glad to answer the Senator's questions, but I should like to reply to that example stated by the Senator from Illinois.

Mr. GORE. I have six questions. I shall give the Senator time to speak on that subject.

Mr. LONG of Louisiana. Will the Senator let me answer the first proposition before I answer his question?

Mr. GORE. I yield.

Mr. LONG of Louisiana. With reference to the trip to Alaska, I ask the Senator to look at page 30 of the report. Under the same circumstances under which a deduction had previously been allowed, it would be ruled that the wife is not essential. The wife is not directly related to the business and the transportation of the taxpayer, so the expense of the taxpayer's wife and the wife of the other man would both be disallowed.

Mr. SMATHERS. Mr. President, will the Senator yield?

Mr. GORE. I yield.

Mr. SMATHERS. Specific reference is made on page 29 of the report to the very trip about which the Senator from Illinois spoke. I said that that was the kind of thing which should never be permitted again. That is illustration B, I believe.

Mr. LONG of Louisiana. There was previously a reference to Olivia De Haviland buying expensive jewelry for her domestic help. Under the bill she would be permitted to buy \$25 of jewelry for one maid and \$25 for the other maid, and that would be all she could buy and all for which she could claim a deduction.

Mr. GORE. Let us consider the hunting lodge. Show me language bearing on such expense.

Mr. LONG of Louisiana. I direct the Senator's attention to the section on facilities in the committee report.

Mr. GORE. The Senator intends to say that the expense would be only partly allowed?

Mr. LONG of Louisiana. No.

Mr. SMATHERS. The Senator is mistaken.

Mr. GORE. The primary use tests must be met, and then the use of facilities is deductible. When the phrase is added "or associated with," it is broadened to a very great extent. That is the answer, I am sure.

Mr. LONG of Louisiana. If the Senator is satisfied that he has answered the question the way I would, there is no point in my answering further. Frankly, I do not think he has. On page 30 of the report the Senator will find in the last paragraph, "Disallowance of expenses for entertainment facilities." The whole burden of the section that follows is that the cost of a yacht, a hunting lodge, or a swimming pool is not deductible, unless one can prove that it was used primarily for business entertainment.

Mr. GORE. Mr. President, that is what I said. I said that my friend would give me the answer that it was deductible only in part. But he has now supplied that answer. If it is primarily used as he has described it, the answer is "Yes."

Mr. LONG of Louisiana. I do not think the Senator understood what I said. I should like to try to explain it again. What that language means is that if one had a swimming pool at his home and his family, his children, and the neighborhood children used it more than 50 percent of the time, he could not deduct 5 cents for the swimming pool.

Mr. GORE. We left the swimming pool.

Mr. LONG of Louisiana. The same thing would apply with respect to a yacht or hunting lodge.

Mr. GORE. I read from the report at the top of page 31:

Under the bill, no deduction is to be allowed with respect to expenses relating to facilities unless the taxpayer establishes (1) that the facility was used primarily for the furtherance of his trade or business and (2) that the expenditure was directly related to the active conduct of his trade or business, or that it was associated with the active conduct of his trade or business.

Mr. President, I submit that when we read this report we read first the most favorable interpretation, and that the best face is put upon the interpretation in the first paragraph. When we read the second and third paragraphs we find the real meaning. I say advisedly, as a lawyer of limited training, as a student of tax law and tax legislation, that I have serious doubt that anyone can cite one personal expense that would be deductible under present law that would not be deductible under the interpretation which the majority report gives to this amendment. There is one little improvement in the bill, and that is the first stipulation on page 31, which states that the "facility was used primarily for the furtherance of his trade or business." The word "primarily" leaves a good deal of room for interpretation. Just how long would a man have to use a yacht, and how much would he have to use it for the entertainment of his prospective customers in order to say that it was primarily used in connection with his business? Would it be 50 percent, or less than 50 percent, or more than 50 percent?

Then we take up items Nos. 1 and 2. When we include in "primary use," uses which are merely "associated with," the business, we ask what that means. What is the legal meaning of "associated with"?

Then we have an interpretation that becomes quite loose, indeed. Nevertheless, in my opinion, the small improvement which I have cited—I think fairly—is more than offset by the adoption of the amendment, with the majority report, which gives legislative affirmation and condonement to many of the abuses and practices which constitute the unfortunate pattern of tax avoidance and expense account abuse.

Mr. LONG of Louisiana. Mr. President, will the Senator yield?

Mr. GORE. I yield.

Mr. LONG of Louisiana. I hope before the debate is over the Senator will realize that those of us who are on the committee felt that we should eliminate the abuses, but leave what we felt were legitimate deductions. On page 35 the Senator will note the requirement that the "taxpayer's statements be corroborated," and that this requirement "will insure that no deduction is allowed solely on the basis of his own unsupported, self-serving testimony."

As it stands now, a man who has a yacht can contend that he uses it for business purposes, without listing the names of people and dates and places and hours those people were on his yacht. He can settle with the income tax people on the basis that he states the yacht was used 60 percent for business and 40 percent for his family. Under the bill that we have written we make it clear that he must have actual proof that certain people were entertained, show the times when the people were aboard his yacht, and that he was either doing business with them or had a reason or basis for thinking that he would be able to do business with them.

Mr. GORE. That is true under present law.

Mr. LONG of Louisiana. Oh, no. That is not true under present law. The Senator is mistaken.

Mr. GORE. I believe I stand corrected on the Cohan rule relating to keeping records.

Mr. LONG of Louisiana. Furthermore, if he wants to deduct for a yacht he must establish by records that it was used more than 50 percent of the time for business entertainment or business purposes.

Mr. GORE. But what is meant by "associated with"? Can the Senator give a definition of that term?

Mr. LONG of Louisiana. It relates to situations in which a man hopes to do business with someone or has a reasonable basis for believing that he will do business with someone.

Mr. GORE. Will the senior Senator from Illinois give us the quotation about hope?

Mr. DOUGLAS. It is faith. According to the Bible, faith is the substance of things hoped for, the evidence of things not seen.

Mr. GORE. I thank the Senator.

Mr. LONG of Louisiana. I hope that the Senator will see this point.

Mr. GORE. I will not argue with the Bible.

Mr. SMATHERS. I have a little evidence which can be seen.

Mr. GORE. I am not sure that we can see all the "associations" that are going to be deductible.

Mr. SMATHERS. I would like to read certain language to the Senator, because I know he wants to understand this particular section, as all of us do. I refer to page 28 with reference to these expenses not being vague. The report states:

It will not be sufficient that the entertainment expense is vaguely or remotely connected with a business motive; it must be demonstrated that the predominant purpose of the expense is to further the trade or business of the taxpayer.

That language is in the report.

Mr. GORE. One may have a wonderful purpose. But then there come the theater tickets and prize fight tickets and nightclub entertainment and hunting lodges and yachts and liquor and parties and all those things that become deductible under this committee report.

Mr. DOUGLAS. Mr. President, will the Senator yield?

Mr. GORE. I yield.

Mr. DOUGLAS. It can be claimed that at rare intervals and in lucid moments there will be attempts to sell products and attempts at mentioning the products. In other words, a little business can be scattered over a great amount of costly entertainment, and the citizens will pick up 52 percent of the check.

Mr. GORE. The man who is riding the expense account is a privileged character whom the President of the United States has described as one who disguises personal expense with business associations.

Mr. DOUGLAS. Is it not true that there has been a great deal of interest in suburban living, with many executives living in the suburbs. I am sure the Senator has seen reports on domestic discord which has arisen when the husband rides the expense account and the wife sits at home and eats hamburgers.

Mr. GORE. I have heard neighborhood rumors. I do not know how much substance there is to these rumors.

Mr. DOUGLAS. Is it not to be expected that if the husband is living at the Ritz Carlton or in Miami and is cruising in a yacht and paying \$10 for lunches, or is eating expensive dinners at Antoinettes in New Orleans, and the poor wife is at home eating a humble sandwich, she becomes discontented and domestic discord increases—

Mr. GORE. And she feels neglected.

Mr. DOUGLAS. She feels neglected; therefore, in order that the business executive may function more efficiently he must take his wife along and dish out the gravy to her, also.

Mr. GORE. I wish to give a few more examples.

A family-held ship repair corporation was allowed to deduct \$23,758 for a Christmas dinner and party.

An enterprising banker effectively combined sentiment with business when he deducted, as present law permits, a

substantial part of the cost of his debutante daughter's coming-out party on the ground that some of the guests had business connections with him.

The committee amendment would add: "or associated with."

In another case, the taxpayer was allowed \$115,000 for entertainment and gifts.

His expenses included \$7,500 spent at a resort hotel; \$5,400 for food, liquor, and cigars for his office and farm; and \$8,700 in cash to officers of his closely held corporation for entertainment.

A beverage manufacturer claimed and was allowed \$10,903 for entertaining customers at the Kentucky Derby.

Huge sums are allowed to business taxpayers in connection with maintenance and operation of yachts and other fancy boats. One manufacturer was allowed to deduct \$253,000 for the expense of his yacht. Another was permitted to deduct \$112,000 for such expenses—as well as an additional amount of \$362,000 for a ranch-hunting lodge, a nightclub, and other similar expenses. A company in the business of selling fuel was allowed \$93,000 as deductions for a yacht, a fuel products company was allowed \$23,000 and an auto dealer was allowed yacht expenses of \$22,000.

A cake and cookie bakery was allowed \$66,000 for a yacht on which to entertain supermarket and chainstore buyers and branch managers. Despite its rather sad undercurrents, both from the viewpoint of the tax system as well as otherwise, one of the most interesting cases is that in which a mortuary business was allowed \$26,495 for yacht expenses to entertain visiting morticians, clergymen, and for meetings of employees.

These cases could be multiplied by the thousands. Similar large expenditures are constantly being made on hunting and fishing lodges, on elaborate beach resort homes, on exotic island retreats, on extended hunting trips, including plush safaris to far off Africa and India. Indeed, just about every kind of human activity in the nature of fun and frolic is being well subsidized on behalf of a privileged few by the average taxpayer who does not happen to be engaged in a trade or business so as to enable him to join in this Government-supported high life. Is it any wonder, then, that such strong taxpayer resentment has developed against the expense account privilege.

The important point to be derived is that all of the expenditures described were deductible under the broad standard of present law which permits the deductions of "all the ordinary and necessary business expenses" of the taxpayer. The fact that there is a business relationship, actual or even only hoped for, between the parties does not prevent them from enjoying the fancy resort living, the cruise on the expensive yacht, or the fancy nightclub.

Suppose company A sells its product to company B. If a sales executive of company A invites his close friend, an executive of company B, to join him for a cruise on his yacht, who can say that the executive of A did not intend to pro-

mote the business relationship between the two companies. The fact is that in the usual case the businessman's friends are his business customers or prospects. Under the text of present law, so long as this business connection exists between entertainer and entertained, the parties can enjoy tax deductible vacations in Bermuda, cruises on yachts and evenings in luxury nightclubs on a tax deductible basis. This can be done on a reciprocal arrangement of "you entertain me and I'll entertain you," with the Treasurer paying half the bill for each, and the individuals paying none of each. Business does not have to be discussed nor need the entertainment follow or precede business discussion. The taxpayer need not even be present at the entertainment. Because of absence of restrictions, taxpayers are encouraged to ask "Why should not I deduct my personal pleasures and entertainment, if everyone else can?" Because of this the expense account problem has grown to its present unmanageable proportions.

Mr. DOUGLAS. Mr. President, would the Senator develop that point a little further? It is sometimes said that legislation is based on the proposition: "You scratch my back, and I will scratch yours." But is not this a practice of: "You entertain me, and I will entertain you"? Is it not a situation of one executive saying, "You take me to lunch, you take me to dinner, you take me to the club, we will talk a little bit about business in between the acts or in between the courses, then next week I will take you"?

Is this not an illustration of a group of executives who got together and formed a club with the proviso that each would entertain the rest once a year; and it was all done in the name of business? In other words, "You scratch my back, and I will scratch yours. I will feed your stomach; you feed my stomach."

Mr. GORE. Once a year, and we will pass it around.

Mr. DOUGLAS. Pass it around.

Mr. GORE. Thereby, they become members of this privileged social group in our society which—

Mr. DOUGLAS. Which share the luxuries.

Mr. GORE. That, Mr. President, disguises their personal expenses by cloaking them in a business association.

Mr. SMATHERS. Mr. President, will the Senator from Tennessee yield?

Mr. GORE. I wish to be certain that my scintillating friend from Illinois has finished.

Mr. DOUGLAS. I have finished.

Mr. SMATHERS. I thought that what the Senator from Illinois said was scintillating, and I agree with him.

Mr. GORE. Does the Senator wish to keep it up?

Mr. SMATHERS. On the contrary. All the Senator has to do is start reading the report.

Mr. GORE. I shall do that.

Mr. SMATHERS. Because on page 36 we discuss that subject:

However, under this exception, it will not be possible to deduct luncheon expenses of a so-called reciprocity luncheon group under which a group of businessmen frequently lunch together and alternate in paying the

check (and claiming it as a business expense deduction). This practice is not connected with a trade or business, but is a personal or social expenditure which is not deductible under existing law.

Mr. GORE. On what page is that?

Mr. SMATHERS. Page 36 of the report.

Mr. GORE. Just a little further—

Mr. SMATHERS. It is not right to continue to talk about an old bag of bones. I do not believe it is quite fair for the Senator to continue to talk about going to Bermuda. We have eliminated the part about reciprocity lunches. We do not approve of these things any more than does the Senator from Tennessee. What must be remembered is that the bill we are now seeking to pass will tighten up the law immeasurably. That is what we hope to do.

Mr. GORE. I wish to speak a little about page 36, which the Senator from Florida has cited. I ask the Senator to read it carefully again. I hope the senior Senator from Illinois [Mr. DOUGLAS] and the junior Senator from Louisiana [Mr. LONG] will follow this. What I am about to read is under the heading, "Exceptions Where Disallowance Provisions Will Not Apply."

Mr. DOUGLAS. That is correct.

Mr. SMATHERS. Read the language: However, under this exception—

Mr. GORE. The Senator from Florida does not have the floor.

Mr. SMATHERS. The Senator ought to read all the language.

Mr. GORE. The Senator from Florida is giving his interpretation. I wish to read what the report actually states. On page 36, paragraph 6, the heading is as follows: "Exceptions Where Disallowance Provisions Will Not Apply." I emphasize the word "Not." I read:

(b) expenses for food and beverages (and facilities used in connection with them) furnished on the business premises of the taxpayer primarily for his employees. This is intended to exclude from the disallowance provision such facilities as a company cafeteria or an executives' dining room. This exception would continue to apply even though guests are occasionally served in the cafeteria or dining room.

The club which the Senator from Illinois was talking about might meet a few times a year in the executives' dining room; and this language specifically provides that the disallowance will not apply. So the Senator from Florida has selected an unfortunate provision of the report from his own point of view.

Mr. SMATHERS. The particular language that the Senator has just read is a part of the amendment which I understand the Senator actually favors. In other words, it is in the House language. This is the same as the House language; so what the Senator is now using is his own amendment.

Mr. GORE. No, Mr. President. The report from which I have read is the Senate committee report.

Mr. SMATHERS. But on that point it is the same as the House version of the bill.

Mr. GORE. Oh, no; I beg the Senator's pardon. The words are "associated with"; and the amendment before the

Senate, to which this report applies, uses the words "or associated with."

HOUSE SOLUTION TO THE PROBLEM

The test adopted by the House of Representatives is that the expense of an entertainment activity will not be deductible unless "directly related to the active conduct of the taxpayer's trade or business." Where an expense connected with a facility such as a yacht or a hunting lodge is involved, the taxpayer must also show that the facility "was used primarily for the furtherance of the taxpayer's trade or business." On its face, this standard seems almost as broad as present law and would appear to present many of the same problems.

However, in its report the House Ways and Means Committee has explained its test in a way which provides a number of tangible, practical, and meaningful guidelines: The report states:

The taxpayer will have to show more than a general expectation of deriving some income at some indefinite future time from the making of the entertainment-type expenditure; however, he will not be required to show that income actually resulted from each and every expenditure for which a deduction is claimed.

If the expenditure is for entertainment which occurs under circumstances where there is little or no possibility of conducting business affairs or carrying on negotiations or discussions relating thereto, the expenditure will generally be considered not to have been directly related to the active conduct of business. Thus, the absence of the taxpayer or his representative from the entertainment was not directly related to the conduct of the taxpayer's trade or business. Similarly, if the group of persons entertained is large or the distractions substantial, the cost of the entertainment will not be deductible, in the absence of a clear showing of a direct relationship to the active conduct of the trade or business.

This clear statement of legislative intent by the Ways and Means Committee of the House of Representatives, coupled with the statutory language, provides a partial solution to the difficult expense-account problem, and should go a long way toward reducing the abuses outlined above. However, critics of the House proposal attacked this crucial committee report statement on the ground that it had no support in the statute.

In view of the broad language of the statute, requiring explanatory implementation to make it useful, this contention is baseless. The true reason for the complaint is the fact that the bill as interpreted by the Ways and Means Committee report would have some real teeth in it.

It seems to me, however, that it would be the better part of wisdom to enact the original proposal of the President. I have prepared an amendment which would do this. Its language is clear, simple, and plain.

FINANCE COMMITTEE SOLUTION—FORMULA FOR CONFUSION

Mr. President, at this time I should like to address myself to the Finance Committee's solution—the pending amendment and the majority report, which I call a formula for confusion.

The only change in the pertinent House statutory language made by the Senate Finance Committee is the addi-

tion of the words "or associated with." Thus, a taxpayer could deduct an entertainment expenditure which was only "associated" with the active conduct of his trade or business, as well as one which was directly related thereto. Since this statutory language is quite similar to that of the House version of the bill, one would reasonably expect again to find a helpful explanation as to what the committee intended to accomplish by its additional phrase "or associated with."

Unfortunately, such is not the case. Unlike the clear, concise, and workable guidelines set forth in the House Ways and Means Committee report, the Senate Finance Committee report is a mass of vague, disconnected statements and examples which are destined to spawn controversies more numerous and intense than those which occur with such disturbing frequency under present law.

Mr. LONG of Louisiana. Mr. President, will the Senator from Tennessee yield?

Mr. GORE. Not just now, Mr. President. I am discussing in a very carefully prepared manner the majority committee report which both the junior Senator from Florida and the junior Senator from Louisiana have asked me to discuss. So if the Senator from Louisiana will defer for a few moments, then I shall be happy to yield.

Mr. President, although the Senate committee report attempts to paint a picture of virtue and righteousness, even a casual glance beneath the surface reveals that the virtuous exterior is more illusion than reality. For example, the report states:

Nothing in your committee's bill is to be construed as allowing a deduction for any expense which is against public policy or which violates the public conscience. Deducting an expense incurred for such purpose under the guise of generating "business goodwill" will not be condoned and under your committee's amendment is not deductible. Thus, the cost of liquor purchased for the entertainment of customers and the promotion of goodwill (which under existing law has been held deductible) will be disallowed if the serving of liquor violates the public morals of the community as expressed in local law.

Mr. President, I should like to read that again, for additional emphasis. The Senate committee report states:

Thus, the cost of liquor purchased for the entertainment of customers and the promotion of goodwill (which under existing law has been held deductible) will be disallowed if the serving of liquor violates the public morals of the community as expressed in local law.

Mr. DOUGLAS. Mr. President, will the Senator from Tennessee yield?

Mr. GORE. If the Senator from Illinois will permit me to continue, I shall appreciate it. A moment ago I declined to yield to the Senator from Louisiana. But I shall be glad to yield in just a moment.

Mr. DOUGLAS. Very well.

Mr. GORE. Mr. President, I continue to read from the Senate committee report:

Another example of expenses for immoral purposes which have been claimed on tax returns under existing law involves expenditures to provide call girls for the purpose of

entertaining clients. Under your committee's amendment no deduction whatsoever is to be allowed for expenditures of this nature. In no legitimate sense are they "directly related to or associated with the active conduct" of a trade or business.

The foregoing suggests that the committee's action will serve as a moral broom to disallow expenditures where liquor is illegal under local law, and where call girls are utilized as business entertainment. However, expenditures such as these, which violate clearly defined lines of public policy, are not deductible under present law. See *Smith*, 33 T.C. 861 (1960); *R. E. L. Finley*, 27 T.C. 406 (1956); *U.S. v. Winters*, 261 F. 2d 675 (1958). What, then, will be accomplished under the committee's language? Is it not clear that this is simply a smokescreen thrown up to suggest that abuses are being remedied, whereas in actuality little, if anything, is being accomplished beyond present law?

Mr. LONG of Louisiana. Mr. President, at this point will the Senator from Tennessee yield?

Mr. GORE. Not just now. I am dealing in a careful way with the Senate committee report, and also am showing that it claims to do something which it does not do.

Mr. President, the Senate Finance Committee report stresses the desirability and wholesomeness of goodwill entertainment. It states:

Goodwill has long been recognized as a legitimate objective of business entertaining and where the purpose of the expense and its clear relation to a business is firmly established, the expense ordinarily will continue to be deductible.

Mr. President, I wish to read that again. The Senate Finance Committee report states:

Goodwill has long been recognized as a legitimate objective of business entertaining and where the purpose of the expense and its clear relation to a business is firmly established, the expense ordinarily will continue to be deductible.

The report further states:

To eliminate the harshness resulting from the House report—

I digress to say that I recognize nothing harsh about the House report. In fact, I thought the House of Representatives dealt rather gingerly with the subject. I would have much preferred to see the House and the Senate adopt the recommendation of the President and the Secretary of the Treasury to stop this expense account tax abuse. I think the House bill, and particularly the committee report, does a fairly good job, but I recognize nothing harsh about it. I did not think, as I said, that it was strong enough.

I return to the quotation:

To eliminate the harshness resulting from the House report, amendment of the language of the House bill is necessary.

I digress. The advocates of this amendment may claim that the purpose of it is to stop certain abuses. I have just read the report. Why is it said that it is necessary to amend the House language?

To eliminate the harshness resulting from the House report, amendment of the language of the House bill is necessary.

What language did the committee adopt? Three innocent little words, "or associated with." And what do these words mean? I read now from the report:

This new language will permit deductions of expenses for entertainment, amusement, or recreation incurred for the creation or maintenance of business goodwill with regard to whether a particular exception applies.

However, this new language will apply only if the taxpayer demonstrates a clear business purpose and shows a reasonable expectation of deriving some income or other benefit to his business as a result of the expenditure. If he meets this test, the expenditure will be considered to be associated with—

Let me repeat, "associated with."

Let me repeat, "associated with."

Let it sink in, "associated with."

If he meets this test, the expenditure will be considered to be associated with the active conduct of his trade or business; otherwise, the expense would be disallowed under your committee's amendment.

Mr. DOUGLAS. Mr. President, will the Senator yield?

Mr. GORE. I yield to the Senator from Illinois.

Mr. DOUGLAS. In other words, under the name of good will, one could invite customers to the Kentucky Derby, pay their expenses, and entertain them, and that would be a deductible expense?

Mr. GORE. Let us read from the report:

This new language will permit deduction of expenses for entertainment—

Mr. DOUGLAS. The Kentucky Derby is entertainment.

Mr. GORE (continuing):
or amusement—

Mr. DOUGLAS. It is amusement, too.

Mr. GORE (continuing):

or recreation.

Mr. DOUGLAS. It is said to be recreation.

Mr. GORE (continuing):

incurred for the creation or maintenance of business good will.

Mr. DOUGLAS. That is the alleged purpose.

Mr. GORE (continuing):

Without regard to whether a particular exception applies—

That includes everything, does it not?

Mr. DOUGLAS. It is very broad. It could apply to tickets to prize fights, to build up good will.

Mr. GORE. If that is amusement.

Mr. DOUGLAS. Sixty-five-dollar tickets to see "My Fair Lady."

Mr. GORE. Yes.

Mr. DOUGLAS. Expenses at the 21 Club.

Mr. GORE. If that is amusement.

Mr. DOUGLAS. It is amusement.

Mr. GORE. Or entertainment.

Mr. DOUGLAS. Or for the purpose of building up good will.

Mr. GORE. Is that not wonderful?

Mr. MILLER. Mr. President, if the Senator will yield for a moment, I do not wish to interrupt, but having sat on the other side of the table from some rather sharp-penciled, long-nosed revenue agents, in trying to obtain for my clients a fair share of deductions, I must say that if the Senator from Tennessee were a revenue agent, he would be the most popular revenue agent in the world if he would allow all these deductions willy-nilly.

Mr. GORE. This is not the speech of the junior Senator from Tennessee that I am reading now. I am reading from the majority report. I am reading the legislative intent of the Senate Finance Committee.

Mr. DOUGLAS. And it will be cited by other able attorneys for the corporations that make such charges. If the Senator from Iowa were ever to return to his practice, he would be greatly strengthened by the legislative history which is now being made.

Mr. SMATHERS. Mr. President, I hope the Senator will cease using an example which is not justified, by any stretch of the imagination, in the majority report. We eliminated the trip to Bermuda, but we continue to hear about it. The Senator keeps talking about tickets to "My Fair Lady," dinner at Antoine's, and so forth.

Mr. GORE. I said in the beginning, Mr. President, that such language was not in the speech of the Senator; it is in the majority report. I am reading to the Senate what the committee says is the legislative intent of the three innocent little words, "or associated with." What do I read here?

If the taxpayer meets any of this test—if he meets the test to which I just referred—what will be the result?

The expenditure will be considered to be "associated with his business."

Mr. DOUGLAS. The luncheons at Antoine's would still be a business expense.

Mr. GORE. Or the suites on the waterfront at Miami, or the yachts in the harbor, or the prize fights. That is what it says.

Mr. DOUGLAS. And the caviar, dipped out at the "21" Club, the champagne cocktails before dinner, and the champagne after dinner.

Mr. GORE. If it is amusement.

Mr. DOUGLAS. Or recreation.

Mr. GORE. Or entertainment.

Mr. DOUGLAS. For good will.

Mr. GORE. A close analysis of these statements makes it eminently clear that expenditures for good will have been given preferred status.

In these references to good will the committee has presented our sophisticated expense account society with a blueprint for continued high living at Government expense and at corporate expense.

Mr. LONG of Louisiana. Who says that? Is that the Senator, or someone else?

Mr. GORE. I say that.

Mr. LONG of Louisiana. I thank the Senator.

Mr. GORE. I say that. If the Senator would like to have me read what he said when he signed the majority report, I shall be glad to read it again.

Mr. LONG of Louisiana. The Senator may suit himself.

Mr. SMATHERS. If the Senator would read it all, and in context, it would be better.

Mr. GORE. Mr. President, I read to the Senator the reference to "call girls."

Mr. SMATHERS. I said to read it all.

Mr. GORE. I read to the Senator about the "call girls." I read about the local laws against drinking liquor.

Mr. DOUGLAS. Are there any local laws against drinking liquor? I do not know of any.

Mr. GORE. There are in Carthage, Tenn.

Mr. SMATHERS. I asked the Senator to read it all, and the Senator said he had read about the "call girls." I would like to have him read all of the report, and in context.

Mr. GORE. Why did the Senator set up this straw girl?

Mr. SMATHERS. The committee wanted to get rid of the problem once and for all. We think we did. The Senator can read into the language all kinds of twists, paragraph by paragraph, out of context.

Mr. GORE. If my friend thinks he is going to get rid of that kind of recreation permanently, I fear he has another thought coming.

Mr. MILLER. Mr. President—

Mr. GORE. What I should like to do is to prevent such things from being tax deductible.

Mr. MILLER. Mr. President—

Mr. SMATHERS. So would we.

Mr. MILLER. Mr. President, may we have order?

The PRESIDING OFFICER. Men of good will, will be in order.

Mr. GORE. In a spirit of good will, Mr. President, I shall continue.

These statements in the majority report constitute a formula which would leave the Internal Revenue Service with an impossible enforcement task, for, in effect, almost all entertainment expenditures, both for the creation and maintenance of business good will, are declared to be hencefores deductible.

In stating that the taxpayer must demonstrate a clear business purpose and show a reasonable expectation of deriving some income—it does not say how much, but only some income or other benefit—and it does not say what kind—to his business from the making of the entertainment expenditure, the committee report would add nothing to the requirement of present law.

The taxpayer must meet precisely the same tests today, and it is under those tests that widespread abuses have arisen. As hundreds of cases illustrate, such vague and generalized requirements at present are so easy to meet as to be practically meaningless.

Mr. CURTIS. Mr. President, will the distinguished Senator yield for a question.

Mr. GORE. I yield.

Mr. CURTIS. I think the distinguished Senator from Tennessee realizes

that I did not support the bill in the committee. I voted against it.

Mr. GORE. So did I.

Mr. CURTIS. I need some information. The estimate of the Treasury Department as to the effect on revenue, found on pages 9 and 10 of the report, is that the section on expense accounts would pick up \$60 million in added revenue in a full year, and \$40 million net.

Mr. GORE. Compared to the President's estimate, and the estimate by the Secretary of the Treasury, that we ought to pick up a minimum of \$250 million.

Mr. CURTIS. What is the position of the distinguished Senator from Tennessee? Does the Senator favor the existing law, or something in lieu of the committee language?

Mr. GORE. First, I oppose the committee amendment which is now pending, which would add to the House-approved bill the words "or associated with."

I particularly oppose the addition of the amendment because the committee report states that the language of the House bill must be changed in order to eliminate the harshness resulting from the House report. As I said earlier, I did not think that the House action or the House report contained any harshness. It dealt a good deal less vigorously with this gnawing and cancerous problem than the President and the Secretary of the Treasury recommended.

The House did a fairly good job.

The Senate committee report, which neither the Senator nor I signed, states that to relieve the alleged harshness the "amendment of the language of the House bill is necessary."

When the committee added that language, it then proceeded to say what it would permit. I am against permitting the kinds of deductions which the report says the amendment would permit.

Mr. CURTIS. Is it not true that the bill as reported by the majority of the committee would represent a tightening of existing law?

Mr. GORE. By the Senate committee?

Mr. CURTIS. According to the decision by the Treasury Department it would be, because it is said that it would increase the revenues by \$60 million a year gross or \$40 million a year net. If the present law were to be changed in such a manner as to collect more revenue there would have to be a tightening of the present law.

Mr. GORE. I have readily accepted that, with respect to facilities, the primary use test constitutes some improvement. I do not believe, overall, that the amendment and the interpretation of it would constitute an improvement.

Mr. CURTIS. Then the Treasury Department must be incorrect in its estimate, because we could not liberalize the language and also collect more revenue.

Mr. GORE. I think one must consider the problem as involving something more than revenue. There are moral, political, and ethical values involved, some of which are not measureable by a dollars and cents figure.

To answer the Senator further as to my position, I would much prefer to have the request by the President and the Secretary of the Treasury written into law. I think the President and the Secretary of the Treasury did a magnificent job in analyzing and dramatizing this cancerous problem. I think they proposed measures for its solution which would have been effective and would have eliminated the abuses.

Mr. CURTIS. Why is the present law not effective?

Mr. GORE. I would prefer to see that recommendation adopted. However, that is not what is before the Senate. There is before the Senate the House-passed bill, which would do a fair job.

But the Senate committee has found it necessary to adopt an amendment. Why? "To eliminate the harshness resulting from the House report."

Let me say to my distinguished friend, the Senator from Nebraska [Mr. CURTIS] that the committee proposes to delineate—to spell out specifically—what the language would permit. What language is the committee talking about? Those three innocent words—"or associated with." What would be permitted? I hope the Senator is following me.

Mr. CURTIS. I am.

Mr. GORE. Deduction of expenses for entertainment, amusement or recreation incurred for the creation or maintenance of business and good will, without regard to whether a particular situation applies. However, this new language would apply only if the taxpayer demonstrated a clear business purpose and showed a reasonable expectation of deriving some income or other benefit to his business as a result of the expenditure. If he meets that test, the expenditure would be considered to be associated with the active conduct of his trade or business. Otherwise, the expense would be disallowed under the committee's amendment.

Mr. DOUGLAS. On page 26 of the committee report the following language appears:

The new language will permit deduction of expenses for entertainment, amusement or recreation incurred for the creation or maintenance of business goodwill without regard to whether a particular exception applies.

It is that which I am opposing. I fully believe that the administration, with all of its vigor, is opposed to the pending committee amendment. I hope that will be made clear by tomorrow.

Mr. President, on page 27 the committee went on to say:

Entertaining guests at night clubs, country clubs, theaters, football games, and prize fights, and on hunting, fishing, vacation, and similar trips are examples of activities that constitute "entertainment, amusement, and recreation."

Mr. GORE. I had not reached that point. I appreciate the Senator's calling that to my attention. It has been said that certain things would not be allowed. For example, we were told that vacation trips would not be allowed. I will not

say what we were told. The record will speak for itself.

I read again:

Entertaining guests at night clubs, country clubs, theaters, football games and prize fights, and on hunting, fishing, vacation, and similar trips are examples of activities that constitute—

What?

Mr. DOUGLAS. Entertainment.

Mr. GORE. Amusement.

Mr. DOUGLAS. And recreation.

Mr. GORE. To create goodwill.

Mr. CURTIS. Mr. President, will the Senator yield?

Mr. GORE. I yield.

Mr. CURTIS. Why are unreasonable deductions allowed at the present time? The code provides—

Shall be allowed as deduction all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business.

Why is it that the Treasury allows unjustifiable expense items?

Mr. GORE. I would not like to be diverted in that manner. It is a known fact that under present law widespread abuses occur. The President of the United States has told the Congress that the abuse cannot be corrected without amendment of the law. So I would not wish to discuss with my distinguished friend why, under present law, the abuses have occurred and cannot be stopped under present law.

I wish to discuss the committee amendment which would perpetuate many of the abuses.

I say to my friend from Nebraska that what I am about to read is what the committee report says the three little words "or associated with" mean:

In addition, "entertaining" includes any business expense incurred in the furnishing of food and beverages, a hotel suite, a vacation cottage, or an automobile, either to a customer (present or potential) or to any member of such a customer's family—

We have been told that it would not include the wives.

A wife is a member of a family. It would include the wife of a present customer or the wife of a potential customer.

Mr. CURTIS. Is the Senator reading from the House report or the Senate report?

Mr. GORE. I am reading the majority report of the Senate Finance Committee.

Mr. CURTIS. Is that not the same as the House bill, which the Senator supports?

Mr. GORE. No; it is not. I shall tell the Senator why. I shall go back. The Senator will notice that I started reading an interpretation of the word "entertaining." This is the legislative intent.

Mr. CURTIS. The Senator has said that he is reading from the Senate report. The same language is contained in the House report, which the Senator supports.

Mr. GORE. I am reading the interpretation contained in the Senate committee report of the language of the bill as amended by the pending amendment.

Mr. CURTIS. The points the Senator has enumerated are taken from the House report.

Mr. GORE. If the Senator will let me give him some information, I shall try to do so. I am reading now from the majority committee report.

Perhaps I should read the whole paragraph. Before I do so, I should like to say that it relates to the interpretation which I have previously read of the language contained in the committee amendment—"or associated with," which would permit deductions for entertainment, amusement, or recreation. Now I am reading the paragraph which gives the interpretation of the meaning of the word "entertain."

Entertaining guests at night clubs, country clubs, theaters, football games, and prize fights, and on hunting, fishing, vacation, and similar trips are examples of activities that constitute "entertainment, amusement, and recreation." In addition, "entertainment" includes any business expense incurred in the furnishing of food and beverages, a hotel suite, a vacation cottage, or an automobile either to a customer (present or potential) or to any member of such a customer's family. If deduction is claimed for any expense for "entertainment, amusement, or recreation" the facts and circumstances of each particular case will determine the extent to which the expenses will be disallowed.

How much more explicit could a committee report be?

After that good, sound beginning, we have the real meat and meaning of the words "or associated with."

Furthermore, though the committee report makes numerous references to good will, it gives no indication as to what is encompassed by this term. Nowhere is good will defined. How does a businessman go about creating good will?

Mr. DOUGLAS. Mr. President, will the Senator yield?

Mr. GORE. I yield.

Mr. DOUGLAS. The Senator must remember that in the French Revolution, when one of the Girondists was led to the guillotine, she exclaimed, "O liberty, liberty, what crimes have been committed in thy name."

Can we not now say, "Good will, good will, what crimes the Senate Finance Committee has committed in thy name"?

Mr. GORE. What is good will? It seems clear that the sky is the limit. If a businessman thinks a big yacht may be helpful in developing some customers, does not this committee report language put the official congressional stamp of approval on his deduction of these substantial costs of maintaining such a "business" asset?

Mr. DOUGLAS. Mr. President, will the Senator yield?

Mr. GORE. I yield.

Mr. DOUGLAS. Because it will create recreation.

Mr. GORE. And entertainment.

Mr. DOUGLAS. And amusement.

Mr. GORE. And maintain good will.

Mr. DOUGLAS. Or create good will.

Mr. GORE. Is not a revenue agent foreclosed from effectively examining into the matter?

In the light of all the foregoing statements respecting good will, very little is salvaged from the following comment—particularly in view of the illustration given as to what is meant by "vague good will."

Where good will generated by the expense is vague or where the possibility of the expenditure resulting in the production of income is remote, no deduction will be permitted. For instance, under present law a taxpayer may deduct expenses of entertaining buyers and others associated with his trade or business even though at the time he does the entertaining he already has more business than he can handle. Under your committee's amendment, however, no deduction will be allowed because, with a large backlog of unfilled orders, such entertainment ordinarily cannot be regarded as being associated with efforts to produce income.

This narrow exception to the basic theme of the Finance Committee report that all good will entertainment is deductible is scant evidence of tightening up present law. Rare indeed is the case where the taxpayer has such a backlog of unfilled orders that his entertainment activities cannot be regarded as being associated with efforts to produce income. It is interesting to note that even in such an extreme case the report hedges the consequences by providing that "ordinarily" the deduction will not be allowed. Moreover, there is a good possibility that entertainment expenditures in such a unique case are not deductible under present law because they are in the nature of capital expenditures—Cf. James Schulz, 16 T.C. 401.

Here again the committee has done nothing more than set up a strawman—to give the illusion that a cutback on existing law is being effected. In reality nothing has been accomplished—except that perhaps another arena for conflict has been created.

The "harshness" of which the report speaks is that the House provision, as explained by the Ways and Means Committee's report, has some effect and will disallow some entertainment expenditures which are deductible under present law. Presumably that is the purpose of this legislation. However, one must struggle hard to tell which of the above-described cases would be denied deduction under the Finance Committee report. How much, if anything, would be disallowed to the corporation which spent and deducted almost \$1 million in 1 year for yachts, club dues, shipboard conventions, hunting and fishing trips, and parties? Does not a corporation make such expenditures to develop good will? We have already seen that goodwill expenditures are clearly deductible under the Finance Committee report. How about the banker who deducted a substantial part of the cost of his daughter's coming-out party as a business expense? Wasn't he also developing customer good will? Certainly the Government is not, under the Finance Committee report, free to disallow expenses regardless of the form of entertainment the taxpayer may adopt to develop good will. Similarly, in all the other cases set forth above, the taxpayer would appear to be able to continue to deduct all entertainment expenditures.

Under the Finance Committee report, do yachting expenses continue to be deductible? If not, then the report should clearly so state. Does the cost of

maintaining hunting lodges for entertainment continue to be deductible? If not, then the committee report should so state. Is the cost of wining and dining at nightclubs deductible? If not, the committee report should clarify the situation. Do tickets at \$30 apiece for musical comedies continue to be deductible? If not, the committee report should so indicate or provide some standard or guideline by which the answers to these questions can be determined by the taxpayers and revenue agents who will be left floundering in their attempts to know what the rules are.

One further "red herring" in the Finance Committee report should be mentioned. The report states that no deduction will be allowed for entertainment expenses "which under the circumstances in which they are incurred are lavish or extravagant." Here again no standards or guidelines are furnished. What is lavish or extravagant under the circumstances? If the circumstances involve a taxpayer accustomed to entertaining in an elaborate and expensive style, can they be held to be "lavish" under the circumstances? When does a yacht become an extravagant expenditure? When is it 60 feet in length? One hundred feet in length? Would these criteria vary with the income—or expected income—of the taxpayer? Would a resident of Miami Beach, Fla., be entitled to a bigger and more expensive yacht than a resident of Providence, R.I.? Would a beach home with eight rooms be a lavish facility? What about one with 30 rooms? Would a corporate president be entitled to drink champagne whereas a vice president could have only a whisky highball and a proprietor of a country grocery store only ordinary corn liquor?

Is it not abundantly clear that the so-called test produced by the Finance Committee, superimposed upon the unsatisfactory test of present law, will simply compound existing difficulties? The litigation and controversy which would follow adoption of such meaningless language would even make the present situation seem a happy one. The result would be a real mess. And to what avail?

It seems clear that a change in existing law is necessary. Court decisions and administrative actions over the years have punched so many holes in the feeble wall of resistance to abuse which the statute now constitutes that a completely new structure is warranted.

It seems to me that the President's original proposal is a sound one. It ought to be enacted.

The Senate in 1960 did take a significant step in this regard. I hope it will do so again now.

Mr. DOUGLAS. Mr. President, will the Senator yield?

Mr. GORE. I yield.

Mr. DOUGLAS. I congratulate the Senator from Tennessee on his very able speech, particularly on the way he has leveled in on pages 26 and 27 of the committee report, which clearly indicates that everything in the field of

amusement, recreation and entertainment has been opened up, if it can be claimed that it creates good will. Has the Senator ever heard of a firm that has had too much business?

Mr. GORE. No. I thank the Senator from Illinois.

I believe that if those who read the CONGRESSIONAL RECORD will carefully peruse the detailed analysis which I have given of the majority report they will see why I felt justified in saying earlier, and why I feel justified now in saying, in conclusion, that if a Senator who reads and understands the report and the amendment votes to approve it he will vote to continue the widespread abuses of which the President and so many citizens have complained.

Mr. DOUGLAS. The country owes a great debt of gratitude to the Senator from Tennessee. I hope his words will have effect in the vote which is expected to come tomorrow. I am sure they will furnish material for students of this subject and for the general public in years to come. Even if we should be beaten by the bipartisan alliance tomorrow, we hope we will win in the future.

Mr. LONG of Louisiana. Mr. President, only a few days ago the junior Senator from Louisiana was engaged in a hard fight to the bitter end side by side with the junior Senator from Tennessee, on the subject of the space satellite. In that instance, both of us were opposed to the administration's position.

I now find that we must choose sides and to start all over again, because of our difference of opinion with respect to the pending measure. This difference of opinion does not diminish my admiration or high regard for the Senator from Tennessee. We just see things differently this time.

I find myself somewhat at a disadvantage to explain what I am about to say, because in some respects one would think that the background of the junior Senator from Louisiana would mean that he would choose the opposite position to the one he has chosen. One might think that in view of the politics that was occasioned by my family tradition. I was inspired by the example of my father, who was the author of the share the wealth plan. He had a theme song that went:

Every man a king.
Every man a King.
For you can be a millionaire.
But there is something belonging to others;
There's enough for each one to share.

As one who strongly admires and adores his father, I always want to go the extra mile and generally I try to agree with him on his share-the-wealth plan. However, nothing he ever suggested, so far as a person who hoped to earn money is concerned, was ever so extreme as the present income tax law of the United States. For example, my father, the late Huey Long, who was once a Member of this body, never conceived of a tax of 84 percent or 90 percent on personal income, the tax which a person pays today on the present tax base. Yet, in his day, he was the fore-

most advocate of a very high graduated income tax.

When a person is taxed at a rate of 90 percent—and for persons who are successful and are earning a substantial income, it does not require too much income to get into that bracket nowadays—he ought to be permitted every legitimate deduction which his business requires. That is my attitude.

When Secretary Dillon appeared before the Committee on Finance, he was testifying for a position which seemed to be totally impractical. The Secretary had previously testified for the position that a businessman, even one who had very great responsibilities, should not be permitted to spend more than \$4 or, at most, \$7 a day for business meals or for entertainment expenses.

He was testifying for a position that a person should not be permitted to spend more than \$30 a day for meals and lodging. That was the position he had recommended before the House committee, which he was not successful in bringing to the Senate. But that was basically the administration's starting point.

In my judgment, this is a completely impractical proposal. It will not work. It amounts to taxing people for necessary expenses in their business. It seems to me that necessary business expenses should be permitted. A person should not be denied the ordinary deduction which would be expected of a person in his position.

When the Secretary discussed some of these instances, I asked him if he did not understand that there would be a difference between what would be expected of a lawyer in my home town of Baton Rouge and a lawyer practicing in New York City. If a prominent businessman called on a lawyer practicing in Baton Rouge, the entertainment expected might be a dinner at a nice restaurant or at a country club. On the other hand, if he were to appear in New York City, and the client were a substantial person, under the existing rule that client would expect the lawyer, if he were doing business in a major degree, to get tickets to a Broadway show for himself and perhaps his wife, also.

Secretary Dillon said quite frankly before the committee that in his firm, which was not a law firm, but a brokerage or investment firm, it was standard procedure—they did it as their everyday way of doing business—to obtain theater tickets for some of their better customers. It appeared to me that he had been testifying more for the position of some of his assistants, who had perhaps never known what it was to entertain graciously in their lives, rather than for the position of one who understands what the needs of a businessman, particularly those in substantial positions, might be.

There is nothing in the bill which would give the businessman any deduction to which he is not already entitled. The bill is strictly a one-way street, so far as the entertainment sections are concerned. Compared with existing law,

the businessman does not gain in any respect; he loses in every respect.

It is very well for one Member of this body to talk about how completely wide open the loophole for the entertainment expense allowance might be. If you talk to some of the businessmen whom you respect in your community, let them tell how rough the revenue agents can be under existing law in denying them the right to take deductions which they feel would be fairly and properly deductible.

As an example, a business friend in my hometown had a small yacht. He took the president of the State University for a trip on his yacht. My friend was the chairman of the board of the State university. He was told by the revenue agents that he could not deduct that expense because he could not show them what business he expected to get at the university merely because he took the president of the university and his family for a ride on the yacht. My friend thought that position was an outrage, and he did the best he could to defend his position.

I know of many cases, as the Senator from Iowa [Mr. MILLER] has suggested, in which businessmen, in good conscience and good judgment, felt they were entitled to such deductions because they thought it was expected of them to entertain, and they considered the entertainment to be a necessary expense of doing business. Yet such expenses have been disallowed many times.

In my judgment, the committee report goes too far. The item in which I have been most interested involves merely permitting a man to entertain a business associate at dinner without having to twist his arm for the business the whole time. I do not know how it appeals to others, but as one who has been entertained by someone who has hoped to do business with me, and as one who entertained himself, it does not seem gracious to me only to entertain a person in such a situation that he can be badgered for a contract the whole time the person is trying to eat his meal.

It would often be better to entertain graciously without talking about business at dinner or lunch, and then, on a subsequent occasion, to talk about business. That would seem logical in many cases.

I have fought to try to preserve that right. If a substantial businessman comes to town, seeking to sell to somebody or seeking to do business with him, or if a lawyer entertains the head of a large corporation, hoping that that might lead to his firm being retained to represent that corporation, it seems to me that the expense of entertaining that man and his wife should be deductible, not only for the business client and his wife, but for the lawyer and his wife. Yet the committee report undertakes to say that the only expense that can be deducted is the expense of two dinners, one for the man and one for the client, but nothing for their wives. The Senator from Tennessee would make the amount totally nondeductible if the person did not take the client to a place which was conducive to talking business.

If those people went to a country club or a nightclub, it would be held that

that was not conducive to doing business. It would be necessary to show that it was a good place to get a hammer-hold on the person to make him sign a contract; otherwise, the expense would not be deductible. To me, that does not appear to make much sense. Yet the committee report tightens up to the extent that one-half the deduction would be allowed for entertaining the client and his wife.

The matter of good will has been discussed, and discussed elaborately. The Senator from Tennessee [Mr. GORE] and the Senator from Illinois [Mr. DOUGLAS] discussed the definition of "entertainment." They did not go on to say what else was necessary in order to get an entertainment allowance. But entertainment includes good will and various and sundry other things.

Mr. DOUGLAS. We were not giving our own interpretations; we were quoting from page 27 of the committee report, which reads:

Entertaining guests at nightclubs, country clubs, theaters, football games, and prize fights, and on hunting, fishing, vacation, and similar trips are examples of activities that constitute "entertainment, amusement, and recreation."

Mr. LONG of Louisiana. Yes; and the exact language is in the House report. So far as defining "entertainment" is concerned, there is no real difference whatever between the House and Senate language. We are talking about what must be proved in order to get a deduction under the amendment. The difference is what must be proved in order to obtain a deduction for entertainment. Under the Senate language, it would be necessary to show that there was more than a general expectation of doing business.

In other words, one could entertain for purposes of good will, but he would have to show more than just a general, vague notion of getting good will. He would have to show that there was more than a remote possibility of getting business. In fact, the Senate committee report states on page 28, in the third paragraph

It will not be sufficient that the entertainment expense is vaguely or remotely connected with a business motive; it must be demonstrated that the predominant purpose of the expense is to further the trade or business of the taxpayer.

So in order to obtain a deduction as an entertainment expense for any of these, it would have to be proved that there was more than a general expectation of obtaining business, and that the entertainment had as its predominant purpose the obtaining of business.

Mr. CURTIS. Mr. President, will the Senator from Louisiana yield?

Mr. LONG of Louisiana. I yield.

Mr. CURTIS. After the attack which has been made on the committee, I think it well to bring out, in this regard, all these references. The committee report also states, on page 30:

No deduction will be allowed under this provision for any "entertainment, amusement, or recreation" expenses which under the circumstances in which they are incurred are lavish or extravagant. This will be

so even where a direct business purpose is firmly established.

And at another point the committee corrects the rule, and requires that everyone substantiate his expenses with bookkeeping. The committee has tightened the present law to the tune of some \$40 or \$60 million.

Mr. LONG of Louisiana. This is more than a matter of tightening existing law to the tune of \$40 or \$60 million a year. The estimate made by our committee staff—and many times the estimates of our committee staff have been proved to be more accurate than those of the Treasury—is that this involves tightening the existing law by \$85 million, and it will knock out many allowances heretofore made. As I have said, in my judgment we are being too tough on the taxpayers.

When the Senator says no lavish entertainment will be permitted, he realizes that this would leave the Treasury's agents the right to adopt their own standards and definition of "lavish", and the taxpayer would have to reveal to the Treasury agent the information on which the Treasury agent would make the determination as to whether the expense was lavish. I certainly hope someone has talked about taking people to dinner at Antoine's—which is not as expensive as some people think—or taking people to dinner at Club 21, which I have heard is just about as expensive. Someone might determine that that was lavish, but I hope it will not be determined as being lavish. I think that a person who makes one or two trips a year to New York could very well entertain at Club 21.

Mr. DOUGLAS. Or at the Four Seasons?

Mr. LONG of Louisiana. I have never paid a bill there, so I do not know whether it would be considered lavish.

Mr. DOUGLAS. In the stratosphere.

Mr. CURTIS. Mr. President, I wish to concur in the commendation of the estimate made by the Joint Committee. It has demonstrated by its estimates that they are carefully made. However, I shall not go into that now.

I was addressing myself to what the Senator from Tennessee contended was the position taken by the committee. My concern is not as to what restaurant some person may choose to go to. I rise to defend the integrity of the majority of the committee. They have brought in a proposal which limits the deductions and increases the revenue. However, I believe that many of the utterances made on this floor would not give that impression to the listening public or the reading public.

I thank the distinguished Senator from Louisiana for permitting me to add that much of what I hope will be a clarification of the RECORD.

Mr. LONG of Louisiana. I thank the Senator from Nebraska.

From the statements made here, one would gain the impression that the taxpayer would be gaining something which he does not now have. But this is purely a one-way street, and the taxpayer will lose.

Frankly, it seems to me that one of these days the taxpayer should win once in a while, rather than lose all the time. Losing all the time seems to be the way this part of the bill would work.

Many references have been made to so-called horrible examples of what the bill would allow. For example, a safari to Africa was referred to. However, the cost of the safari was deducted as an advertising expense. But on page 28 the language spells out that that could not even be taken as an advertising expense.

Mr. President, I ask unanimous consent to have printed at this point in the RECORD an excerpt from page 28 of the committee report and also an excerpt from page 30, dealing with claimed deductions for activities of this type which would not be permitted.

There being no objection, the excerpts from the report were ordered to be printed in the RECORD, as follows:

An objective standard also will overrule arguments such as the one which prevailed in *Sanitary Farms Dairy, Inc.* (25 TC 463 (1955)) that a particular item was incurred, not for entertainment, but for advertising purposes. That case involved a big-game safari to Africa. The taxpayer argued successfully before the Tax Court that the expense of the hunt (including costs of making motion pictures which were later shown to customers and potential customers) were incurred solely for advertising purposes. Under the bill, if the activity typically is considered to be entertainment, amusement, or recreation, it will be so treated under this provision regardless of whether the activity can also be described in some other category of deductible items. This will be so even where the expense relates to the taxpayer alone.

Expenses for entertainment, amusement, and recreation should be identified by the taxpayer on his return and treated under the new rules of this bill. It will not be appropriate to include these expense items in other categories of business deductions, where their character will not be apparent, such as advertising, public relations, cost of goods sold, reimbursed expenses, etc. Failure to substantiate the claimed entertainment expenses by adequate records or other sufficient evidence may result in complete disallowance of the deduction.

Mr. LONG of Louisiana. Mr. President, much has been said about yachts, vacation cabins, hunting lodges, and so forth. Once again I say that in my judgment the bill is too strong, if anything. In order to be able to take any of these deductions, a person will have to maintain records as to when and where and who were present and for what purpose. That has not been necessary in the past. Records are one of the chief things the Treasury wishes to have in connection with claims for such allowances.

The language is:

The requirement that the taxpayer's statement be corroborated will insure that no deduction is allowed solely on the basis of his own unsupported, self-serving testimony.

But one who listened to what was said earlier this evening about this matter would have gained the impression that just the opposite was the case. However, of course, that is not true.

One of the examples which was given was that of a movie star—Olivia de Havilland—who deducted the expense of jewelry given to her servants. Under this bill she would be allowed to deduct a gift of \$25 to one and a gift of \$25 to the other, but no more.

Let us return to my statement about yachts, hunting lodges, and swimming pools, about which much has been said. As the situation is today, the taxpayer is able to negotiate with the Treasury—without proof, without records to prove it—a deduction of a certain percentage of his expenses for any one of those items. If the Treasury will not allow the taxpayer the entire expense of operating his boat, the Treasury will allow him perhaps 50 percent of it, without requiring him to produce records to prove it.

But under the Treasury's language here, the taxpayer would have to show that this facility—whether a yacht or a hunting lodge or a swimming pool, or whatever it was—was used primarily—which means more than 50 percent—for business entertainment; and he would have to have records to prove it; and the records would be subject to attack on the basis that he would have to show that there was more than just a general expectation of creating some goodwill.

In addition, when the taxpayer had met the primary test—when he had shown that the facility was not used primarily by his family or his friends for social entertainment, then he would have to allocate as between the business use and the personal and family uses; he would have to establish the percentage of the facility which was used for business purposes and business entertainment. In doing that, I suppose he would not be able to deduct for the entertainment of the wives, because the committee report is so tough on the wives that it seems that the tax would have to be paid if the man's wife were invited there.

So this is a very great strengthening—in my judgment, too much of a tightening—of the existing situation.

It seems to this Senator that if a man had a yacht and used it 30 percent of the time for entertaining business guests, and he could show it was used in pursuit of sales and business activities when these people were on the boat, he ought to be able to deduct 30 percent of the cost; but, under the bill, he would not be able to deduct 5 cents. That is the extent to which it has been tightened.

I do not think we should go beyond that point and be as severe as the House report—and I do not think the House committee intended to be that severe, when the Treasury Department wrote the report. That is why I insisted that the Treasury should not write the Finance Committee report, but that the staff should.

Let me read what our reaction to the House report was. I read from page 26 of the Senate committee report:

The report of the Committee on Ways and Means made it clear that the House bill was not designed to disallow completely deductions for entertainment, amusement, or recreation expenses, but rather it was in-

tended to eliminate abuses. Under the general rule, no deduction would be allowed for any such expenses except to the extent that such expenses are directly related to the active conduct of a trade or business. Despite the clear language of the House bill and the stated intent of the provision, considerable uncertainty and confusion as to the actual effect of the House draft has been created by the interpretation given this language in the House committee report.

It in effect interprets the proposed statutory language to disallow a deduction for any expense for entertainment, amusement, or recreation unless the expense is described in one of a series of specific exceptions to the general rule. Where the expense is covered by an exception, the rules of existing law would continue to govern the deductibility of the expense.

In other words, under the interpretation which the House committee report gave to the language, the bill provided a complete disallowance of any entertainment expense unless one could come under a specific exception.

The fact is that the exceptions were unreasonable and far too strict, and the committee felt that one should be permitted a certain amount of reasonable deductions where he could make a very clear showing that he had a purpose of generating business by the entertainment he gave.

I shall discuss this matter in greater detail tomorrow. I did not want to let the CONGRESSIONAL RECORD close for today without responding to some of the statements which I thought were extreme with regard to the action taken by the committee. Again, I say, in my judgment, the committee was too severe, and I feel other deductions should have been permitted.

Mr. SMATHERS. Mr. President, I shall be very brief. The hour is growing late. However, in the few remarks I shall make, I shall show that we have seen demonstrated a good deal of the difficulty in drafting legislation, when a group of Senators on one side do not think we are tough enough, and a group of Senators on the other side are of the opinion that we are too tough. So it falls, as it usually does, on the majority—in this case the majority of the Finance Committee—to finally arrive at some position which they feel answers in some measure the criticisms of those who wanted to be tougher and those who wanted us to be not quite so tough.

I cannot help but agree with the basic views which have been expressed by the Senator from Louisiana. I believe, under our system as we see it operating today in the business community, legitimate business expenses are an integral and necessary part of doing business.

The other day I had a visit from a very successful businessman who claimed that it took him 5 years to get the best client he had, a client that, as he said, his wife and children live upon, so to speak, whose children were educated by him, because he got his main business from him. He tried entertaining him at lunch. That did not do any good. He tried entertaining him at golf. That did not do any good.

Finally, he found that the man had a weakness for reading books, so he bought

some books and gave them to him. That made an impression on the client, and this businessman got his business.

This is a part of our business life. There are those who would like to eliminate it. If the day ever comes when taxes can be reduced from 91 percent to 35 or 40 percent, we can reduce corporate taxes, the day may arrive when we can do away with the so-called business expense deductions; but with the high taxes that we have now, and the manner in which our business community has grown up, we must permit honest businessmen to make business deductions.

Regrettably, there are some Senators who, in their zeal to close loopholes, have apparently been willing to go so far that they want, in effect, to burn down the barn in order to get a few rats. There is no question that there have been some abuses of the expense account provisions. I have not found anybody on the committee, I have not found anybody in the Senate, who approves of taking people to Bermuda, putting them in some cottage down there, and charging off the expense of sending them down and keeping them there as a business expense. I have not found any member of the Finance Committee, or any other Senator, who approves of hunting trips to Alaska, safaris to Africa, or the use of yachts as that practice has been abused. Yet these are the examples which are pointed to, with respect to the bill as it came from the Finance Committee, and it is made to look as though the Senator from Louisiana, the Senator from Nebraska, and the Senator from Virginia, as well as other Members, are in favor of this sort of thing. Of course we are not. What we are trying to do is arrive at some balanced program which will eliminate abuses and still recognize the legitimate expenses of legitimate businessmen.

This is what we have done. This is the best way we could do it. Necessarily, we do not have all the brains. We do not have the judgment of a Solomon. But we have done the best we can in the only way we can arrive at legislation. That is by taking something from one side and something from the other side and trying to arrive at something that is reasonable and fair.

There is no question that what we have arrived at is a tightening up of the measure, and the proof of it is that the Treasury says it will bring in \$60 million more than is being brought in at the present time. If it were, as was indicated earlier this evening by the Senator from Tennessee and his very able colleague the Senator from Illinois, in fact, a loosening provision, or if our amendment were a loosening provision, obviously the Treasury would not gain an additional \$60 million. So it must be a tightening provision.

I cannot help but believe that if Senators will read the report in its entirety they will arrive at the same conclusion which the majority of the Senate Finance Committee arrived at—that this is a tightening provision, that it will eliminate abuses, but at the same time permit legitimate businessmen to continue to

enjoy legitimate business expense deductions.

I do not believe it is possible for the Senate Finance Committee or any legislative committee to write provisions for all conditions which might arise, which some Senators on the other side would like to do. That cannot be done. The best we can do is give our impressions, and this is what we have endeavored to do in the committee report.

Mr. President, I ask unanimous consent that an excerpt from the committee report dealing with section IV, "Disallowance of Certain Entertainment, Etc., Expenses," explaining the particular section and the legislation pertaining to it may be printed in the RECORD at this point.

There being no objection, the excerpt was ordered to be printed in the RECORD, as follows:

IV. DISALLOWANCE OF CERTAIN ENTERTAINMENT, ETC., EXPENSES

(Sec. 4 of the bill and sec. 274 of the code)

A. Reasons for provision

The Treasury brought to the attention of Congress that widespread abuses have developed through the use of the expense account. In his tax message to the Congress last year, the President stated his conviction that entertainment and related expenses, even though having a connection with the needs of business, confer substantial tax-free personal benefits on the recipients, and that in many instances deductions are obtained by disguising personal expenses as business expenses. He recommended that the cost of such business entertainment and the maintenance of entertainment facilities be disallowed in full as a tax deduction and that restrictions be imposed on the deductibility of business gifts and travel expenses.

Much of the abuse described by the President can be traced to the broad judicial and administrative interpretation given to the term "ordinary and necessary" which has resulted in many entertainment expenses being allowed as deductions where their connection with a trade or business is quite remote. Under present law, where a business purpose, however slight, exists, then the entertainment expenses generally are fully deductible if they are "ordinary and necessary" business expenses.

After careful consideration of the proposal, your committee has concluded that deductions for entertainment and traveling expenses and business gifts should be restricted to prevent abuses. The committee agrees that this abuse of the tax law should not be condoned, but on the other hand it does not believe that complete disallowance as recommended by the President is the proper solution to the problem. Rather, your committee is convinced that expenses incurred for valid business purposes should not be discouraged since such expenses serve to increase business income, which in turn produces additional tax revenues for the Treasury. If valid business expenses were to be disallowed as a deduction (particularly expenses associated with selling functions), there might be a substantial loss of revenue where business transactions are discouraged, or where they fail to be consummated. Moreover, the entertainment industry employs large numbers of service personnel, most of whom are unskilled workers who would find it difficult to obtain new employment in other fields if the disallowance of entertainment expenses created considerable unemployment in the entertainment industry. In such cases, taxes now paid by these workers would be lost to the Treasury.

B. Comparison of committee amendment with House provision

The House bill provides rules which in general would: (1) Disallow a deduction with respect to entertainment activities, except to the extent that the expense is directly related to the active conduct of a trade or business; (2) disallow a deduction with respect to entertainment facilities, unless the facility is used primarily for the furtherance of the taxpayer's trade or business and the expense is directly related to the active conduct of the trade or business; (3) abolish the Cohan rule by requiring the taxpayer to substantiate, by adequate records or by sufficient evidence corroborating his own statement, all expenditures for entertainment and related facilities, and for travel and gifts; and (4) limit the deduction for gifts to \$25 per year per recipient.

Your committee's bill to a considerable degree retains the basic structure of the House bill. However, the effect of the principal provision (the disallowing of a deduction for certain entertainment expenses) has been modified to permit the deduction of expenses for goodwill where a close association is established between the expense and the active conduct of a trade or business.

The report of the Committee on Ways and Means made it clear that the House bill was not designed to disallow completely deductions for entertainment, amusement or recreation expenses, but rather it was intended to eliminate abuses. Under the general rule, no deduction would be allowed for any such expenses except to the extent that such expenses are directly related to the active conduct of a trade or business. Despite the clear language of the House bill and the stated intent of the provision, considerable uncertainty and confusion as to the actual effect of the House draft has been created by the interpretation given this language in the House committee report. It in effect interprets the proposed statutory language to disallow a deduction for any expense for entertainment, amusement, or recreation unless the expense is described in one of a series of specific exceptions to the general rule. Where the expense is covered by an exception, the rules of existing law would continue to govern the deductibility of the expense.

To eliminate the harshness resulting from the House report, amendment of the language of the House bill is necessary. Despite amendment of the House bill your committee has made certain that entertainment expense abuses are eliminated. By your committee's amendment an alternative rule is added to the House bill under which expenses for entertainment, amusement, or recreation (with respect to both activities and facilities) also will be deductible to the extent that such expenses are associated with the active conduct of a trade or business. This new language will permit deduction of expenses for entertainment, amusement, or recreation incurred for the creation or maintenance of business goodwill without regard to whether a particular exception applies. However, this new language will apply only if the taxpayer demonstrates a clear business purpose and shows a reasonable expectation of deriving some income or other benefit to his business as a result of the expenditure. If he meets this test, the expenditure will be considered to be associated with the active conduct of his trade or business; otherwise, the expense will be disallowed under your committee's amendment.

With respect to disallowance of a deduction for gifts in excess of \$25, your committee has adopted the rule of the House bill but has modified the definition of "gift" for purposes of applying the limitation. Under the modified definition: (a) certain specialty advertising gifts, (b) advertising material for use in connection with the recipient's busi-

ness, and (c) certain awards to employees costing not more than \$100, will not be taken into account in determining whether the \$25 limitation has been exceeded.

The requirements of the House bill regarding substantiation of claimed deductions for entertainment, amusement, or recreation expenses, gifts, and traveling expenses, have been approved without change.

The provision of the House bill which provided that expenses for meals and lodging included in the term "traveling expenses" were to be deductible only if "reasonable" has been clarified to assure that "traveling expenses" are not to include expenses for meals and lodging which are lavish or extravagant. In addition, your committee has added to the House-passed bill a new rule for the allocation of traveling expenses where the trip involves both business and pleasure. Under this rule, which would eliminate abuses involving tax deduction for vacation trips, if the trip is for more than 1 week and the personal portion of the travel time is in excess of 25 percent of the total time away from home, the traveling expenses (including meals and lodging) must be allocated between business and pleasure and only the portion allocated to business will be deductible.

As amended by your committee, the provisions of this section of the bill are to apply to taxable years ending after December 31, 1962, but only with respect to expenditures incurred after that date.

C. General explanation of provision

Your committee's bill adds a new provision to the code (sec. 274), which disallows, in whole, or in part, certain expenses which would be fully deductible under present law. The requirements imposed by this bill are in addition to the requirements for deductibility imposed by other provisions of existing law, which must be met by the taxpayer before this new provision becomes operative. Hence, if an expenditure is claimed as a business expense deduction under section 162, the taxpayer must first establish that it constitutes an ordinary and necessary expense incurred in carrying on a trade or business, before the new provisions of this bill become applicable.

Since the only purpose of this section is to disallow deductions, it will not make deductible any expense which is disallowed under the "ordinary and necessary" test of present law. Moreover, this section does not affect the question of the includibility or excludibility of an item in income of any individual. The rules presently applicable under present law will continue to govern in this respect.

1. Disallowance of expenses for entertainment activities: The first part of the provision provides that no deduction is to be allowed for any expense with respect to an activity which is of a type generally considered to constitute entertainment, amusement, or recreation, except to the extent that the taxpayer establishes that the expense was directly related to the active conduct of his trade or business or that the expense was associated with the active conduct of his trade or business. Certain exceptions to this rule are provided, however, for expenses not required to meet the new tests. They are discussed in No. 6 below.

Entertaining guests at nightclubs, country clubs, theaters, football games, and prize-fights, and on hunting, fishing, vacation, and similar trips are examples of activities that constitute "entertainment, amusement, and recreation." In addition, "entertainment" includes any business expense incurred in the furnishing of food and beverages, a hotel suite, a vacation cottage, or an automobile either to a customer (present or potential) or to any member of such a customer's family. If deduction is claimed for any expense for "entertainment, amusement, or recreation" the facts and circumstances of each

particular case will determine the extent to which the expenses will be disallowed.

The trade or business of the taxpayer will determine whether an activity is of a type generally considered to constitute entertainment, amusement, or recreation. For example, with respect to a taxpayer who is a professional hunter, a hunting trip would not generally be considered a recreation-type activity. On the other hand, with respect to a taxpayer whose trade or business consists of selling machine tools or manufacturing clothing, a hunting trip generally would be considered a recreation-type activity. Similarly, attending a theatrical performance would generally be considered an entertainment-type activity, but in the case of a professional theater critic, attending a theatrical performance would not constitute an entertainment activity.

An objective standard also will overrule arguments such as the one which prevailed in *Sanitary Farms Dairy, Inc.* (25 TC 463 (1955)) that a particular item was incurred, not for entertainment, but for advertising purposes. That case involved a big-game safari to Africa. The taxpayer argued successfully before the Tax Court that the expense of the hunt (including costs of making motion pictures which were later shown to customers and potential customers) were incurred solely for advertising purposes. Under the bill, if the activity typically is considered to be entertainment, amusement, or recreation, it will be so treated under this provision regardless of whether the activity can also be described in some other category of deductible items. This will be so even where the expense relates to the taxpayer alone.

Many entertainment expenses which have a business connection nevertheless will not be deductible. To justify their deduction, a taxpayer must establish that the incurring of the expenses relating to the entertainment activities was directly related to or associated with his effort to obtain new business or to encourage the continuation of an existing business relationship. This means that he must show a greater degree of proximate relation between the expenditure and his trade or business than is required under present law. To illustrate this principle, assume a taxpayer entertains a buyer and the buyer's family at lunch and the theater. Under existing law, he claims a deduction for the entire expense; under your committee's bill no deduction would be allowed for any portion of the expense attributable to the buyer's family since as to them he is unable to show a sufficiently close relationship between the expense and his trade or business.

It will not be sufficient that the entertainment expense is vaguely or remotely connected with a business motive; it must be demonstrated that the predominant purpose of the expense is to further the trade or business of the taxpayer. Where goodwill generated by the expense is vague or where the possibility of the expenditure resulting in the production of income is remote, no deduction will be permitted. For instance, under present law a taxpayer may deduct expenses of entertaining buyers and others associated with his trade or business even though at the time he does the entertaining he already has more business than he can handle. Under your committee's amendment, however, no deduction will be allowed because, with a large backlog of unfilled orders, such entertainment ordinarily cannot be regarded as being associated with efforts to produce income.

Under the bill, although deduction for entertainment expenses is restricted, such expenses will not be disallowed merely because they are incurred for the purpose of generating business goodwill. Goodwill has long been recognized as a legitimate objective of business entertaining and where the purpose of the expense and its clear relationship to

a business is firmly established, the expense ordinarily will continue to be deductible. However, nothing in your committee's bill is to be construed as allowing a deduction for any expense which is against public policy or which violates the public conscience. Deducting an expense incurred for such purpose under the guise of generating "business goodwill" will not be condoned and under your committee's amendment is not deductible.

Thus, the cost of liquor purchased for the entertainment of customers and the promotion of goodwill (which under existing law has been held deductible) will be disallowed if the serving of liquor violates the public morals of the community as expressed in local law. Another example of expenses for immoral purposes which have been claimed on tax returns under existing law involves expenditures to provide "call girls" for the purpose of entertaining clients. Under your committee's amendment no deduction whatsoever is to be allowed for expenditures of this nature. In no legitimate sense are they "directly related to or associated with the active conduct" of a trade or business.

On the other hand, the following examples are indicative of circumstances under which entertainment expenses ordinarily will not be disallowed. Where the taxpayer conducts lengthy negotiations with a group of business associates and that evening the group goes to a night club, theater, or sporting event for relaxation, such entertainment expenses are regarded as directly related to the active conduct of business. Moreover, if a group of business associates with whom the taxpayer is conducting business meetings comes from out of town to the taxpayer's place of business to hold substantial business discussions, the entertainment of such business guests prior to the business discussions also is directly related to the conduct of the business. Similarly, if in between business meetings at a convention the taxpayer entertains his business associates attending such meetings, such expenses will be allowable.

Although your committee's bill permits entertainment expenses to continue to be deducted where a business purpose is shown, deduction will be limited to the portion of the expense which is directly related to or associated with business.

Objective standards will be employed to determine the apportionment between the part of the expense which meets either of these tests and the part which does not. Expenses not so related may not be deducted. Under this rule, if a taxpayer entertains a group of 10 individuals, 3 of whom are business prospects and 7 of whom are social guests, deduction will be allowed under the bill only for three-tenths of expenses incurred. Since the taxpayer's motive is not relevant to this determination, it would make no difference that the taxpayer in the above example would not have done the entertaining but for the attendance of the three business-related guests. This rule would disallow deductions for expenses in the following cases which, under existing law, are fully deductible:

A. Officer-shareholder and wife accompanied customer and wife to Las Vegas for 12-day vacation. Taxpayer paid the expenses for the four individuals. Officer-shareholder asserted that he would not have made the trip except for business purposes and that his wife's presence was required by the customer and his wife.

B. Officer-shareholder and his wife traveled to Alaska with customer and wife. Expense of wife was allowed based on representation that customer would not go without his wife and his wife would not go without such shareholder's wife.

C. Expenses for tractor demonstration attended by corporate taxpayer's principal officer-shareholder and his wife. A purported

business reason for the wife's travel was established based on allowance of expenses for similar travel in the past.

In example A, no deduction would be allowed under your committee's bill because a vacation trip for a customer and his wife is not "directly related to the active conduct of the taxpayer's trade or business." In example B, deduction would be disallowed for expenses attributable to the taxpayer's wife and the customer's wife. In example C, no deduction would be allowed for expenses attributable to the taxpayer's wife.

D. Customers and their wives are entertained by taxpayer at derby parties such as breakfasts and luncheons, etc.; by furnishing box seats and tickets for the Kentucky Derby; and entertainment at the derby.

Under existing law, the entire amount expended was claimed as a deduction and was allowed. Under your committee's amendment, no deduction is permitted for expenses attributable to customers' wives because their connection with the taxpayer's trade or business is remote.

No deduction will be allowable under this provision for any "entertainment, amusement, or recreation" expenses which under the circumstances in which they are incurred are lavish or extravagant. This will be so even where a direct business purpose is firmly established. The application of this rule can be demonstrated by the following example:

E. The taxpayer, which is located in the midwest, asserted that lavish entertainment is essential in obtaining business and it established a Miami Beach residence for this purpose. The two principal officers and their wives are usually present at the residence when entertaining customers. Deductions allowed included depreciation on residence, food, liquor, boat expense and salaries of service employees and entertainment. Disallowance was made for amounts deemed to be personal expense.

Under the bill, no deduction would be allowed for any expenses attributable to the wives of either the principal officers or their customers (present or potential), or for any portion of the expenses incurred in example E which are lavish or extravagant. (The expenses of maintaining the residence are treated as expenses with respect to a facility discussed in No. 2 below.)

Expenses for entertainment, amusement, and recreation should be identified by the taxpayer on his return and treated under the new rules of this bill. It will not be appropriate to include these expense items in other categories of business deductions, where their character will not be apparent, such as advertising, public relations, cost of goods sold, reimbursed expenses, etc. Failure to substantiate the claimed entertainment expenses by adequate records or other sufficient evidence may result in complete disallowance of the deduction.

2. Disallowance of expenses for entertainment facilities: Your committee's bill (sec. 274(a)) also limits the deduction for expenditures incurred with respect to facilities used for entertaining. As in the case of expenses with respect to activities the new rules of this provision apply only if the expenses with respect to facilities qualify under existing law for deduction of business expenses. Moreover, these new rules establish additional tests which must be satisfied (in addition to the "ordinary and necessary" test of present law) in determining whether any deduction is to be allowed for expenses with respect to facilities. Under the bill, no deduction is to be allowed with respect to expenses relating to facilities unless the taxpayer establishes (1) that the facility was used primarily for the furtherance of his trade or business and (2) that the expenditure was directly related to the active conduct of his trade or business, or that it was associated with the active conduct of his

trade or business. In no event can the deduction exceed the portion of the expense which is directly related to (or associated with) the active conduct of the taxpayer's trade or business. Certain exceptions to this rule are provided, however, for expenses not required to meet the new tests. They are discussed in No. 6 below.

The term "facility" includes any item of personal or real property owned or rented by the taxpayer, such as a yacht, hunting lodge, fishing camp, swimming pool, tennis court, bowling alley, automobile, airplane, apartment, hotel suite, home in vacation resort, dining room, and cafeteria. In addition to items commonly regarded as expenses "with respect to a facility," such as expenditures for the maintenance, preservation, or protection of the facility, this provision also relates to depreciation and losses realized on certain sales of entertainment facilities.

Under the bill, if a facility is used more than one-half for business entertaining, so that more than one-half of the entertainment expense with respect to such facility would be deductible as a business expense under present law, that portion would continue to be deductible to the extent it meets the test of being directly related to (or associated with) the active conduct of the taxpayer's trade or business. If less than one-half of such entertainment expense would be deductible under present law, no deduction would be allowed. For example, if the taxpayer acquires a fishing camp which he uses almost exclusively for entertaining business guests, deduction of the expenses of the camp will be disallowed only to the extent that it was used for personal or other non-business purposes. On the other hand, if he uses it almost exclusively for personal purposes, but occasionally takes business guests to the camp, no deduction is to be allowed. A further illustration of this rule is as follows:

A. The taxpayer corporation claims the purpose of maintaining a resort residence is to have a place available for business conferences. The resort residence has facilities for boating, fishing, and entertainment. It was established that the personal convenience, pleasure, and health of the chairman of the board of the taxpayer corporation was the principal reason for maintaining the residence. However, the evidence did indicate that there was some entertainment expense incurred for business purposes and a portion of the expense was therefore allowed.

Under the bill no deduction would be allowed in the foregoing example because the facts established that the primary use of the resort residence was not in furtherance of the taxpayer's trade or business.

Under this provision the facility must actually be used in furtherance of the taxpayer's trade or business; it is not sufficient that the facility is merely available for business use. And where the facility is one which is likely to serve the personal purposes of the taxpayer, it will be presumed that the facility was primarily used by the taxpayer for his personal purposes. To justify a deduction under such circumstances the taxpayer will have to clearly establish that the primary use of the facility was not for his personal purposes but was directly related to or associated with the active conduct of his trade or business. The following example illustrates the operation of this rule:

B. Closely held corporate taxpayer located in Midwest maintains a summer home in Maine. Principal stockholder and wife spend 2½ months each summer at the Maine home and entertained high officials (and wives) of customers.

Under existing law the taxpayer in this case established that the summer home was used partly for business entertaining and was permitted to deduct a portion of the expenses attributable to the summer home. Under the bill, however, because the per-

sonal purposes of the principal stockholder are served by use of the corporation's summer home, it will be presumed that his personal purposes were primarily served by such use.

These rules will prevent tax abuses involving the use of luxury facilities for entertainment, amusement, or recreational purposes. Under these rules a taxpayer who lives in a luxurious apartment and who presently deducts a portion of its rent on the ground that the apartment is used for occasional entertaining of business guests (and thus has a business purpose), no longer will be able to deduct any portion of the rent because the principal purpose of the apartment is personal, rather than business. Moreover, a swimming pool constructed at the taxpayer's residence may not be charged off for tax purposes as an ordinary and necessary business expense because such a facility is presumed to be used primarily for personal, family, or living purposes unless the taxpayer can establish by a preponderance of the evidence that it was used principally in connection with his trade or business.

As in the case of activities described above, no deduction will be permitted for lavish or extravagant expenses incurred with respect to facilities. This means that luxurious resort facilities maintained for the purpose of entertaining will no longer be fully deductible. This rule is illustrated as follows:

C. Taxpayer, a domestic manufacturing corporation, owns luxurious facilities on a subtropical island. The principal use of the property is for entertainment of executives and key personnel of customer firms. Fishing cruises are maintained and air transportation furnished guests. The chairman of the board, who is the controlling stockholder, and other officers and key employees accompanied by their families spent considerable time at the island.

Under existing law the entire amount expended for maintenance of the resort and the airplanes (other than adjustments for amounts considered personal expenses of officers and employees) is deductible. Under the bill no deduction would be allowed for any expense which under the circumstances is either lavish or extravagant. Moreover, no deduction will be allowed with respect to expenses attributable to a member of the customer's (present or potential) family but the family's use of the facility will be considered in determining whether the use of the facility is primarily for personal purposes. In addition, as indicated in the portion of this report describing the deductibility of expenses for entertainment activities, expenses for vacations for customers may not be deducted. Where the expenses with respect to the facility are for "vacations," they will be disallowed under your committee's bill.

Club dues and fees paid to any social, athletic or sporting club or organization are treated by the bill as an expense with respect to a facility used for entertainment and therefore will not be deductible where the primary use of the club facilities is personal. If membership entitles the member's entire family to use the facilities of the club, their use as well as his will be considered in determining whether business use of the club exceeds personal use. Where the primary use of the club facilities is in furtherance of a trade or business the cost of the club dues or fees will be deductible to the extent of the use directly related to (or associated with) the active conduct of business.

Thus, if membership in a club costs \$100 per year and the club is used for such clear business purposes three-fourths of the time, \$75 will be deductible. As in the case of other facilities, it is the actual use of the club which establishes the deductibility of the club dues, not its availability for use, and not the taxpayer's principal purpose for joining the club. However, this does not mean that out-of-pocket business entertainment

expenses incurred at a club will not be deductible where the required relationship between the entertainment and the taxpayer's trade or business is shown to exist. Such expenses will be deductible under the rules applicable to entertainment activities without regard to the tax treatment of club dues.

Club dues for this purpose do not include dues or fees paid for membership in such civic organizations as Kiwanis, Lions Club, Rotary, Civitan, and similar groups because these organizations are not social, athletic or sporting clubs. Similarly, professional associations such as bar associations and medical associations are not considered social, athletic, or sporting clubs. Deductibility of these dues will not be affected by the new rules of this bill, but will continue to be governed by the rules of existing law.

3. Business gifts: Under the bill, deduction for business gifts will be disallowed to the extent that the total gifts during the year exceed \$25 with respect to any person. Where gifts are made to the wife of a man who has a business contact with the donor, these gifts are considered as made indirectly to the husband (for purposes of the limitation).

However, your committee has modified the definition of "gift" contained in the House provision so that items of a clear advertising nature which cost \$4 or less will not be required to be taken into account in applying the \$25 limitation. The purpose of this modification is to assure that businessmen who advertise their products or services by means of gifts of small value, commonly described as specialty advertising, may continue to do so without being burdened with the maintenance of detailed records of the amount of specialty advertising used with respect to each business prospect. This exception which includes such items as pens, desk sets, and plastic bags and cases, will apply only if the donor's name is clearly and permanently imprinted on the article.

Another modification of the definition of "gift" involves items such as signs, display racks, or other promotional material donated to a retailer by a producer or wholesaler for use on the business premises of the retailer. This material, generally referred to as point-of-purchase advertising, is not a gift; it is simply a form of advertising used right in the store to aid in the marketing process. As in the case of specialty advertising referred to in the preceding paragraph, this exception for point-of-purchase promotional devices used in normal business operations will eliminate the necessity of manufacturers or wholesalers (who donate the promotional material to retailers) maintaining detailed records and accumulating costs of promotional material with respect to each donee.

The third modification of the definition of "gift" excludes items of tangible personal property which have a cost to the taxpayer of \$100 or less if the item is awarded to employees by reason of length of service or for safety achievement. It is a common practice of many employers to give such items as pins or watches to employees upon their completion of a specified number of years of satisfactory employment or in recognition of some safety achievement. Your committee felt that gifts for these purposes which serve to strengthen the relationship between business and its employees should not be discouraged by the tax law. This exception will permit the practice to continue under the rules of existing law.

There is the possibility of overlapping application of the entertainment expense and gift provisions in this new section. An item which might be held to be a gift might also be held to be an entertainment expense. For example, tickets to a theater might fall in either category. Since different rules will apply depending upon the category in which the expense item falls, specific regulatory authority is given to the Secretary of the Treasury or his delegate to prescribe, in cases where both provisions would otherwise ap-

ply, which provision is to govern. Thus, a "gift" of theater tickets probably would be classified as coming under the entertainment provision, while a book probably would be classified as coming under the gift provision.

4. Allocation of traveling expenses: Your committee has added to the House bill a provision which will require taxpayers to allocate traveling expenses (including meals and lodging) between the portion of a trip which is for a business purpose and the portion which is for pleasure. This new rule will eliminate, in many cases, the "but for" rule of existing law under which a taxpayer is permitted to deduct his entire traveling expenses (even where a substantial portion of the time away from home is for purely personal purposes) if he is able to establish that the primary purpose of the trip was connected with a trade or business. This amendment will eliminate abuses whereby taxpayers often arrange vacations to coincide with a business trip so that they thereby, in effect, obtain a deduction for the vacation travel. However, to insure that this new rule will not impose unreasonable burdens on taxpayers to allocate trips between business and personal purposes where the duration of travel is only for a short period, your committee has provided that the allocation rule is not to apply where the period the taxpayer is away from home does not exceed 1 week, or where the time spent on the personal portion of the trip is less than 25 percent of the entire period the taxpayer is away from home on the trip. Where no allocation is required to be made, deduction of traveling expenses will continue to be governed by the primary purpose test of existing law.

5. Disallowance of expenditures not substantiated: Under the bill, taxpayers will be required to substantiate their entertainment and related expenses, their traveling expenses and gift expenses. The bill provides that the taxpayer must substantiate by adequate records or by other sufficient evidence corroborating his own statement: the amount of such expense or other item; the time and place of the travel, entertainment, amusement, recreation, or use of the facility, or the date and description of the gift; the business purpose of the expense; and the business relationship to the taxpayer of the person entertained, using the facility, or receiving the gift.

This provision is intended to overrule, with respect to such expenses the so-called Cohan rule. In the case of *Cohan v. Commissioner*, 39 F. 2d 540 (C.A. 2d, 1930), it was held that where the evidence indicated that a taxpayer had incurred deductible expenses but their exact amount could not be determined, the court must make "as close an approximation as it can" rather than disallow the deduction entirely. Under your committee's bill, the entertainment, etc., expenses in such a case would be disallowed entirely.

The requirement that the taxpayer's statements be corroborated will insure that no deduction is allowed solely on the basis of his own unsupported, self-serving testimony. However, the degree of corroboration required to support a claimed deduction will vary as respects the business relationship and purpose, the time and place, and the amount of the expense. Thus, oral testimony of the taxpayer together with circumstantial evidence available, may be considered "sufficient evidence" for the purpose of establishing the business purpose required under the new provision. However, oral testimony of the taxpayer plus more specific evidence would be required to be "sufficient evidence" as to the amount of an expense.

Generally, the substantiation requirements of the bill contemplate more detailed record-keeping than is common today in business expenses diaries. However, a clear, contemporaneously kept diary or account book containing information with respect to the date, amount, nature and business purpose of the

expense may constitute an adequate record under this provision. Moreover, expenditures merely incidental to entertainment, travel, etc. (such as taxicab fares, tips, and similar payments) will be deductible if they are substantiated by such a diary, account book, or similar record.

The following example illustrates the operation of the requirements of this provision: Taxpayer establishes that he traveled from California to New York on business. He should retain receipts for his transportation and hotel expenses while in New York. However, expenses incidental to that trip such as taxicab fare, tips, business luncheons, etc. could be substantiated by entries in a diary.

Your committee does not intend by this substantiation requirement to deny a taxpayer deductions for entertainment, etc., expenses where he has no records, if it can be shown that the failure to produce substantiating records was due to circumstances beyond his control, such as destruction of his records by fire or flood. In such a case, the taxpayer will be permitted to reconstruct the business entertainment, travel, or gift expenses incurred by him in the taxable year.

Under the bill, the Secretary or his delegate may, by regulation, prescribe certain situations in which the substantiation requirements will not be applied. For example, it may be provided that substantiation will not be required for traveling expenses, where such expenses (including the cost of meals and lodging) do not exceed prescribed minimum amounts. This will be of special benefit to employees whose per diem allowance while traveling is within limits established by the Secretary under this provision. Thus, if regulations are issued under which substantiation will not be required for traveling or entertainment expenses where per diem allowances do not exceed 125 percent of per diem allowed a Government employee in the same locality, it would be sufficient evidence for purposes of the substantiation rule to establish only the amount of the allowance and the fact that the business travel occurred.

6. Exceptions where disallowance provisions will not apply: The bill contains nine exceptions to the general disallowance provision described above under heading 1 or 2. Where an expense falls within one of the enumerated exceptions, the item will continue to be deductible to the same extent as allowed by existing law. However, the new substantiation requirements (discussed under heading 5) will have to be satisfied with respect to any such expense. The exceptions are as follows:

(a) Expenses for food and beverages furnished under circumstances which are of a type generally considered to be conducive to a business discussion. The question as to whether the circumstances are conducive to a business discussion are to be tested by such standards as: First, the surroundings in which the meal or beverage was furnished; second, the taxpayer's trade or business or income-producing activity; and third, the relationship to such trade, business, or activity of the persons to whom the food and beverages were furnished. Under this exception, the general custom of entertaining business guests at meals in restaurants and hotels would not be disallowed if they meet the ordinary and necessary test of existing law. This should leave undisturbed the most significant portion of goodwill entertainment conducted in this country. However, under this exception, it will not be possible to deduct luncheon expenses of a so-called reciprocity luncheon group under which a group of businessmen frequently lunch together and alternate in paying the check (and claiming it as a business expense deduction). This practice is not connected with a trade or business but is a personal or social expenditure which is not deductible under existing law.

(b) Expenses for food and beverages (and facilities used in connection with them) furnished on the business premises of the taxpayer primarily for his employees. This is intended to exclude from the disallowance provision such facilities as a company cafeteria or an executives' dining room. This exception would continue to apply even though guests are occasionally served in the cafeteria or dining room.

(c) Goods, services, and facilities to the extent that the entertainment, amusement, or recreation (or use of the facility) is treated on the taxpayer's return with respect to the recipient of the entertainment as compensation paid to an employee and from which income tax is withheld. For example, if the taxpayer permitted an employee to use a yacht for a vacation and treated the expenses for its use as compensation paid to the employee for purposes of the withholding tax and for purposes of the taxpayer's tax return, maintenance and crew costs attributable to such use would be deductible in full because of this exception. On the other hand, where a yacht was used exclusively for business entertaining the salaries paid to the captain and crew, even though they were treated as compensation and withheld on, would not come within this exception because they are not the recipients of the entertainment. Rather, the deductibility of the salaries would be determined under the general rule of the provision as an expense with respect to an entertainment-type facility.

(d) Expenses paid or incurred by the taxpayer where he pays or incurs the expenses for his employer or a client, customer, etc., and where he is reimbursed by the employer or client, etc. This is designed to prevent the double disallowance of a single expenditure, once to the employee or practitioner, etc., and a second time to the employer or client, etc. This provision will not apply, however, in the case of an employee where the employer treats the amount paid to him as compensation. It also will not apply in the case of a practitioner, etc., unless he accounts to the client, etc., for the expenses incurred. The accounting must represent sufficient substantiation to meet the tests set out under heading No. 5. Thus, if a lawyer enters into a fee arrangement under which his client agrees to reimburse him for expenses (including entertainment expenses) the exception will not apply unless he accounts to his client sufficiently to enable the client to substantiate the expenses as required by the bill.

(e) Expenses incurred for recreation, social, or similar activities (including facilities) primarily for the benefit of employees. The employees referred to in this case are those, other than officers, shareholders, or highly compensated employees. An individual would be considered a shareholder only if he (taking into account holdings of members of his family) holds an interest in the corporation of 10 percent or more. This category is intended to pertain to the usual employee fringe benefit programs, such as expenses of operating a company swimming pool or baseball diamond, as well as the expenses of the annual company picnic or Christmas office party.

(f) Expenses directly related to business meetings of the taxpayer's employees, stockholders, agents, or directors. While this category will apply to business meetings where some social activities are provided, it is not intended to apply to gatherings which are primarily for social purposes rather than for the transaction of the employer's or company's business.

(g) Expenses directly related and necessary to attendance at a business meeting of an organization, such as a trade association, chamber of commerce, real-estate board, etc., described in section 501(c)(6) of the code.

(h) Expenses for goods, services, and facilities made available to the general public by the taxpayer. This pertains to expenses

for the entertainment of the general public by means of television, radio, newspapers, and the like. It also permits deductions for expenses for parks, etc., maintained by companies where the general public may attend. Expenses of distributing samples to the general public would also come within this exception.

(i) Expenses for goods or services (including the use of facilities) which are sold by the taxpayer in a bona fide transaction for an adequate and full consideration in money or money's worth. This exception is designed to insure that a taxpayer who sells entertainment to others will be allowed to deduct expenses of producing that entertainment. Thus salaries paid to employees of nightclubs and amounts paid to performers other than employees will continue to be deductible by the operator. Moreover, since this type of expense is not considered to be "entertainment" the detailed substantiation requirements prescribed in this bill will not apply.

7. Interest, taxes, casualty losses: The restrictions provided by the bill are not to apply with respect to items which are deductible under specific provisions of law which apply both to business and nonbusiness taxpayers. Thus, deduction for interest paid on a loan to acquire an entertainment facility or property taxes paid with respect to it would continue to be allowed as a deduction, whether or not the entertainment facilities meet the tests of the new provision.

8. Treatment of entertainment-type facilities: Under the bill, if deductions with respect to entertainment-type facilities are disallowed, the disallowed portion is to be treated as an asset which is used for personal, living, and family purposes, rather than as an asset used in the trade or business. Under this provision the basis of such an entertainment-type facility will be adjusted for purposes of computing depreciation deductions and determining gain or loss on the sale of such facility in the same manner as other property (for example, a residence) which is regarded as used partly for business and partly for personal purposes. Thus, if a taxpayer has a yacht which is used three-fourths for direct business entertainment purposes, and he ordinarily would be entitled to \$1,000 for depreciation with respect to the yacht (if it were used entirely for business), \$250 of this amount would be disallowed as a depreciation deduction and would be included as a part of the basis of an asset not used in the taxpayer's business.

9. Meals and lodging while in travel status: The bill, as amended by your committee makes clear that the deduction provided for traveling expenses by section 162(a)(2) of present law is not to include expenses for meals and lodging which are lavish or extravagant under the circumstances.

10. Effective date: The amendments made by this provision are to apply with respect to taxable years ending after December 31, 1962, but only in respect of periods after that date.

COMMITTEE MEETING DURING SENATE SESSION TOMORROW

Mr. SMATHERS. Mr. President, I ask unanimous consent that the Housing Subcommittee of the Committee on Banking and Currency may be authorized to meet during the session of the Senate tomorrow.

The PRESIDING OFFICER. Without objection, it is so ordered.

ENROLLED BILLS PRESENTED

The Secretary of the Senate reported that on today, August 28, 1962, he presented to the President of the United States the following enrolled bills:

S. 538. An act to amend section 205 of the Federal Property and Administrative Services Act of 1949 to empower certain officers and employees of the General Services Administration to administer oaths to any person;

S. 981. An act to extend certain authority of the Secretary of the Interior exercised through the Geological Survey of the Department of the Interior, to areas outside the national domain;

S. 1208. An act to amend Public Law 86-506, 86th Congress (74 Stat. 199), approved June 1, 1960;

S. 2008. An act to amend the act of September 16, 1959 (73 Stat. 561, 43 U.S.C. 615a), relating to the construction, operation, and maintenance of the Spokane Valley project;

S. 2399. An act to provide for the establishment of the Frederick Douglas home as a part of the park system in the National Capital, and for other purposes;

S. 2916. An act to change the names of the Edison Home National Historic Site and the Edison Laboratory National Monument, to authorize the acceptance of donations, and for other purposes;

S. 2978. An act to revise the boundaries of Capulin Mountain National Monument, New Mexico, to authorize acquisition of lands therein, and for other purposes;

S. 3112. An act to add certain lands to the Pike National Forest in Colorado and the Carson National Forest and the Santa Fe National Forest in New Mexico, and for other purposes; and

S. 3174. An act to provide for the division of the tribal assets of the Ponca Tribe of Native Americans of Nebraska among the members of the tribe, and for other purposes.

ADJOURNMENT UNTIL 10 A.M. TOMORROW

Mr. SMATHERS. Mr. President, under the order previously entered, I move that the Senate adjourn until tomorrow morning at 10 o'clock.

The motion was agreed to; and (at 8 o'clock and 20 minutes p.m.) the Senate adjourned, pursuant to the previous order, until tomorrow, Wednesday, August 29, 1962, at 10 o'clock a.m.

NOMINATIONS

Executive nominations received by the Senate August 28, 1962:

UNITED NATIONS

The following-named persons to be representatives of the United States of America to the 17th session of the General Assembly of the United Nations:

Adlai E. Stevenson, of Illinois.

Francis T. P. Plimpton, of New York.

The following-named persons to be representatives of the United States of America to the 17th session of the General Assembly of the United Nations, to serve no longer than December 31, 1962:

Albert A. Gore, U.S. Senator from the State of Tennessee.

Gordon Allott, U.S. Senator from the State of Colorado.

Arthur H. Dean, of New York.

The following-named persons to be alternate representatives of the United States of America to the 17th session of the General Assembly of the United Nations:

Charles W. Yost, of New York.

Philip M. Klutznick, of Illinois.

Jonathan B. Bingham, of New York.

The following-named persons to be alternate representatives of the United States of America to the 17th session of the General Assembly of the United Nations, to serve no longer than December 31, 1962:

Carl T. Rowan, of Minnesota.

Mrs. Marietta P. Tree, of New York.

Digest of CONGRESSIONAL PROCEEDINGS

OFFICE OF
BUDGET AND FINANCE

(For information only;
should not be quoted
or cited)

OF INTEREST TO THE DEPARTMENT OF AGRICULTURE

Issued August 30, 1962
For actions of August 29, 1962
87th-2d, No. 155

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HIGHLIGHTS: Senate passed appropriations continuation measure. Sen. Yarborough commended REA program. House committee reported bill for retirement credit for Federal-State cooperative service. House passed public works acceleration bill.

HOUSE

- 1. PUBLIC WORKS.** Passed with an amendment (inserting the language of H. R. 10113) S. 2965, the proposed Public Works Acceleration Act. A similar bill, H. R. 10113, was laid on the table. pp. 16923-52

Agreed to the following amendments to H. R. 10113:

By Rep. Wright to delete the provision creating an Office of Public Works Coordination and Acceleration. pp. 16939-40

By Rep. Blatnik to provide that "No part of any allocation made by the President under this Act shall be made available for any planning of construction, directly or indirectly, of any school or other educational facility." pp. 16940-2

By Rep. Scranton, 122 to 70, to allow the Federal Government to contribute up to 75% of the cost of public works projects. pp. 16943-7

Rejected the following amendments to H. R. 10113:

By Rep. Dent, 10 to 121, to allow the Federal Government to finance the entire cost of public works projects in certain cases. pp. 16945-7

By Rep. Flynt to add to the definition of "eligible area" any "area which the governing body thereof certifies to the Secretary of Commerce is an area of substantial unemployment." pp. 16947-8

2. FARM LABOR. Rep. Derwinski inserted an article, "Priest Wages War on Migrants' Poverty." pp. 16970-1
3. PERSONNEL. The Post Office and Civil Service Committee reported without amendment H. R. 10539, to amend the Federal Employees Health Benefits Act of 1959 to provide additional choice of health benefits plans (H. Rept. 2294), and with amendment H. R. 3258, to allow credit under the Civil Service Retirement Act to certain Federal employees for service in Federal-State cooperative programs in a State (H. Rept. 2295). p. 16973
A subcommittee of the Post Office and Civil Service Committee voted to report to the full committee S. 1070, to amend the Federal Employees Life Insurance Act of 1954, so as to provide for an additional unit of life insurance. p. D787
4. LEGISLATIVE PROGRAM. Rep. Albert announced that on Thurs., Aug. 30, the rule to send the farm bill to conference will be considered, followed by H. R. 12712, to assist the States to provide additional facilities for research at the State agricultural experiment stations. pp. 16959-60

SENATE

5. APPROPRIATIONS. Passed without amendment H. J. Res. 864, the appropriations continuation measure to make temporary appropriations until September 30, 1962 for those departments and agencies whose annual appropriation bills have not yet been enacted. This measure will now be sent to the President. pp. 16977-8, 17010
A subcommittee of the Appropriations Committee approved for full committee consideration H. R. 12870, the military construction appropriation bill for 1963. p. D784
6. ELECTRIFICATION. Sen. Yarborough commended the REA program and inserted a letter to the editor by REA Administrator Clapp defending his agency against a report of "Edison Electric Institute Vice President Edwin Vennard as charging that the Rural Electrification Administration has overstepped its legislative mandate by 'promoting Government ownership of the electric power business'" pp. 16984-5
7. TAXATION. Continued debate on H. R. 10650, the proposed Revenue Act of 1962 (pp. 16987-17005, 17011-51). By a vote of 62 to 17, tabled an amendment by Sen. Douglas to repeal the provision of law providing for the withholding of income tax on wages and salaries (pp. 17045-6). Pending at adjournment was the committee amendment to permit income tax deductions for farmers for land-clearing expenses (pp. 17049-51).
8. OCEANOGRAPHY. Conferees were appointed on S. 901, to provide for a long-range national program in oceanography. House conferees have not yet been appointed. pp. 17010-11
9. SAFETY. The Judiciary Committee reported without amendment S. J. Res. 222, to provide for the designation of Oct. 1962 through Oct. 1963 as "National Safety Council 50th Anniversary Year" (S. Rept. 1981). p. 16974
10. FOREIGN TRADE. Sen. Smathers submitted amendments intended to be proposed to H. R. 11970, the proposed Trade Expansion Act of 1962. p. 16975

cargo and nobody knows what else are on the way to Cuba.

This, Madam President, is not rumor. It is an official announcement from Tass, the official Russian news agency.

The official Russian announcement was published by the New York Herald-Tribune today in an article from Moscow by Mr. David Miller.

So heavy have become the Russian shipments to Cuban ports that foreign ships are being chartered under the hammer and sickle to carry the load.

Tass says this has been going on since 1957, 2 years before the Communist Dictator Castro took over, which may explain what a lot of people wondered about where Castro got his support for the Castro revolution.

How long, Madam President, do we continue to "examine", as President Kennedy has promised, the Soviet intervention in Cuba—the establishment, in fact, of a Communist beachhead 90 miles from American shores?

How long are we going to stand for the flagrant violation of the Monroe Doctrine?

So that the facts may be made a matter of record, I ask unanimous consent to include in my remarks the article by Mr. Miller from Moscow.

There being no objection, the article was ordered to be printed in the RECORD, as follows:

RED FLOW TO CUBA
(By David Miller)

Soviet exports to Cuba have increased so much that foreign ships are now being pressed into service to handle the cargoes. Tass news agency reported last night.

Ships from West Germany, Norway, and Greece are loading in Leningrad. An Italian ship is being loaded at Novorossiysk on the Black Sea. A Lebanese ship and a Liberian ship are in Odessa. A West German ship is ready to leave Riga.

The ships, all of 7,000 to 13,000 tons displacement, are under Soviet charter to carry industrial equipment, flour, paper, and fertilizer to Cuba, according to a Tass report from Odessa. The ships will bring back raw Cuban sugar.

In reporting the departure for Cuba yesterday of 5,000 tons of grain and a floating 100-ton dock crane, Tass noted:

"This 6,000-mile-long shipping line is known to Soviet vessels since 1957.

"Hundreds of thousands of tons of Soviet export cargo have been transported to Cuba by sea—metal and grain, automobiles and tractors, building materials, oil and mining equipment.

"A marine ministry official told Tass the volume of Soviet-Cuban maritime shipment this year will be double over last year's."

Tass added:

"In any big port of the U.S.S.R., one will see today ships which are to sail for the Cuban shores . . . some 100 Soviet ships are converging on the ports of Havana, Santiago, and Cienfuegos."

The steamship *Ivan Polzunov* is about to sail from Leningrad with cars, canned food, and geological prospecting equipment.

The diesel vessel *Usolye* will leave Odessa with 6,000 tons of agricultural fertilizer for Cuban agricultural cooperatives.

The 10,000-ton diesel ship *Okhotsk* will leave the Far Eastern port of Nakhodka early next month with timber and rice-harvesting and grain-harvesting combines.

CIVIL RIGHTS LEGISLATION

Mr. CAPEHART. Madam President, today marks the fifth anniversary of the Civil Rights Act of 1957, the first civil rights law enacted by the Congress in more than 80 years previous to that date.

That law, designed to protect the voting rights of American citizens regardless of color, race, religion, or national origin was approved under the Eisenhower Republican administration. Specifically, this act directed the Commission on Civil Rights to investigate allegations in writing under oath or affirmation that certain citizens of the United States are being deprived of their right to vote and to have that vote counted by reason of their color, race, religion, or national origin; to study and collect information concerning legal developments constituting a denial of equal protection of the law under the Constitution; and to appraise the laws and policies of the Federal Government with respect to equal protection of the laws under the Constitution.

This law was followed, under the same administration, by the Civil Rights Act of 1960 which further strengthened the 1957 act by giving power to the courts to name special voting referees when it finds evidence that discrimination against Negroes exists, with the referees, under courts jurisdiction, being able to take appropriate steps to insure that qualified Negroes are able to register and vote. We are witnessing today the results of this law enabling qualified Negro voters to register and vote.

This 1960 strengthening law also provides schooling for children of servicemen whenever desegregation disputes lead to the closing of local schools in addition to providing criminal penalties for interference with court desegregation orders. It further made possible for the Federal Bureau of Investigation to enter cases involving bombings of schools, churches, and synagogues. And finally, it provided that voting records must be preserved for 22 months for possible Federal inspection.

Madam President, we Republicans who took every major action in Civil Rights from the Emancipation Proclamation from the 1860's to the 1960's are happy to welcome the action taken by this administration on the poll tax, the first such civil rights action taken by a Democrat administration.

Madam President, I think it is most fitting for us to commemorate this fifth anniversary of the Civil Rights Act of 1957, for it was the first major step in implementing the inalienable right of all American citizens to vote and take an active part in American political life.

REVENUE ACT OF 1962

The PRESIDING OFFICER. The Chair lays before the Senate the unfinished business.

Without objection, the Senate resumed the consideration of the bill (H.R. 10650) to amend the Internal Revenue Code of 1954 to provide a credit for in-

vestment in certain depreciable property, to eliminate certain defects and inequities, and for other purposes.

The PRESIDING OFFICER. The question is on agreeing, en bloc, to the committee amendments on page 41, line 18, and page 42, lines 4 to 10.

Mr. CLARK. Madam President, a parliamentary inquiry.

The PRESIDING OFFICER. The Senator from Pennsylvania will state it.

Mr. CLARK. Is this merely a routine request, one which will not make it impossible for me later to oppose the committee amendment to insert the words "or associated with"?

The PRESIDING OFFICER. The Senator is correct.

Mr. CLARK. May I be recognized and then yield for the purpose of having the request repeated?

The PRESIDING OFFICER. The Chair has laid before the Senate the unfinished business and has stated the question. The Senator from Pennsylvania may proceed with his remarks.

Mr. CLARK. I thank the Chair.

My position is consistent with the position I took on June 20, 1960, when my amendment to impose rigorous restrictions on expense account deductions was adopted by the Senate by a vote of 45 to 39.

In opposing the committee amendment now pending, I am taking a less drastic position than the one taken by a majority of the Senate only 2 years ago.

At the outset I should state that my opposition to the pending amendment does not mean that I do not earnestly believe that what we did in 1960, with the help of my good friend, the junior Senator from Louisiana [Mr. LONG], we should do again. It merely means that for present purposes I share the views of the Senator from Tennessee [Mr. GORE] and the Senator from Illinois [Mr. DOUGLAS] that the House language is infinitely preferable to the language of the Finance Committee amendment.

Mr. LONG of Louisiana. Madam President, will the Senator from Pennsylvania yield?

Mr. CLARK. I yield.

Mr. LONG of Louisiana. As one who defended the Senator's position in the conference, and voted with him, and actually opposed the conference report, let me say that in my judgment what the Senate has here is far more severe than what we had in conference. This provision would say that if a businessman and his wife entertain a client and his wife at dinner—a client who might be a very major client, and one whose business might be most important to the businessman—he could deduct only the cost of the meal of the client, but not the cost of the meal of the wives.

Our position a year ago was that he could deduct the cost of the meals of all four of them. So our position then was far more generous in this area.

Furthermore, according to the staff estimate, this amendment would bring in an additional \$85 million, which is a great deal of money.

Mr. CLARK. The Senator from Louisiana is certainly entitled to his opinion. In the next few minutes I shall endeavor to persuade him—open-minded as he always is—that he is incorrect both in his recollection of what we did in 1960 and in his interpretation of the effect of this committee amendment—although I fear that at the end of my effort, we still may have to disagree.

Mr. LONG of Louisiana. I am no better expert on the amendment than is the Senator from Pennsylvania. He is the best expert of what he had in mind when he offered his amendment. But I think I know more about what the committee meant when we put the amendment in this bill.

Mr. CLARK. Since the Senator from Louisiana has raised the point, let me state, in brief and general terms, what the Senate did in June of 1960, in connection with the business-expense deduction. At that time, by a vote of 45 to 39, we provided that no deduction shall be allowed for any expense paid or incurred for entertainment, except that expenses paid or incurred for food or beverages for the primary purposes of providing an opportunity to advance the trade or business of the taxpayer may be deducted. We also prohibited all gifts exceeding in value \$10; and we also prohibited the payment of dues or initiation fees in social or athletic or sporting clubs or organizations. So I submit that the amendment we adopted in 1960 was really more drastic than the House language, which those of us who oppose the committee amendment are presently advocating.

Madam President, I turn now to the three little words in the committee amendment—"or associated with"—just three little words. They are all that the Finance Committee added to the basic expense-account provision contained in the House version of the bill. But what a whale of a difference those three little words make. By using them as a vehicle by means of which to write into its report more lax standards for entertainment deductions from those in the House version of the bill, the Senate Finance Committee would continue to permit, in my opinion, the great bulk of the abuses in the entertainment area which presently exist to continue unabated. By inserting these three little words, the majority of the Senate Finance Committee have very effectively, in my opinion, robbed the House version of the bill of most of its effectiveness. By using this slight statutory modification as an opening wedge, the committee in its report has, in my opinion, destroyed the simple, but effective, rule which the House developed after 18 months of strenuous effort in this very difficult, technical, and troublesome area.

The House version poses as a test for the deduction of entertainment expenses the requirement that the expenses, in addition to meeting the requirements of the present law and with certain stated exceptions, be "directly related to the active conduct of the trade or business."

The report of the House Ways and

Means Committee explains that under this test the taxpayer is required to show more than a general expectation of deriving some income at some indefinite future time from the making of the entertainment-type expenditure. The House Committee report states that the bill would not allow a deduction for entertainment expense when there is little or no possibility of conducting business affairs or carrying on discussions relating thereto—such as when the taxpayer is absent from the activity or when the group entertained is large or when substantial distractions exist—for example, at the Kentucky Derby.

These basic guidelines, as laid down by the House, are clear and understandable for the taxpayers and for the revenue agents, alike. In my opinion, they will go a long way toward eliminating the abuses in connection with expense accounts.

I would go further; I would go as far as the Senate went in 1960—as far as the administration originally requested last year. But certainly we can improve the bill immeasurably by rejecting the committee amendment and returning to the House language. Enactment of the House provision would end many unwarranted tax benefits enjoyed by our long-standing and ever-expanding expense-account aristocracy.

Madam President, I have often deplored the fact that it is impossible to reproduce cartoons in the CONGRESSIONAL RECORD. I have presently pending before the Committee on Rules and Administration a resolution which would lift the face of the CONGRESSIONAL RECORD, and perhaps would make it more readable, so that, therefore, perhaps it would be of greater influence in the formulation of public opinion across the country. Would it not be a wonderful thing, Madam President, if we could have Herblock's cartoons reproduced in the CONGRESSIONAL RECORD?

This digression comes to my mind because of a wonderful cartoon I remember seeing in the New Yorker magazine 4 or 5 months ago. It showed two bald-headed, rather portly businessmen sitting in a cocktail bar, sipping martinis; and one said to the other, "Why, the expense-account deduction is just as American as blueberry pie." This is what I fear would be the position to which we would be giving our blessing if we were to accept the committee amendment.

I hold in my hand a cartoon published in June, 1960, in the Washington Post. It shows a rather portly businessman, smoking a rather long cigar, at a cocktail table, and accompanied by a young lady of uncertain appearance. Two empty martini glasses stand on the table. In the background is a palm tree and a beautiful new moon. The gentleman in question is saying to the waiter—whose expression I can only describe as a leer—"Two more glasses of food."

Again, Madam President, I do wish it were possible to have cartoons reproduced in the CONGRESSIONAL RECORD.

Mr. LONG of Louisiana. Madam President, will the Senator from Pennsylvania yield for a question?

Mr. CLARK. I am happy to yield to my friend, the Senator from Louisiana. I have enjoyed many a good meal in New Orleans, but at my own expense.

Mr. LONG of Louisiana. Will the Senator show me where in this bill that cartoon would be applicable? In other words, will he show me where the committee amendment would permit the man to entertain that lady and deduct that expense?

Mr. CLARK. I shall be happy to do so, but first I would prefer to complete my speech. If the Senator wants to reiterate the question at the conclusion of my speech, I shall be glad to meet him head-on, but I would like to get on with my speech.

Mr. LONG of Louisiana. While he is at it, I would like to have him support his statement that a safari to Africa can be allowed by the committee report, because it cannot be. It is expressly prohibited. I would like to have him show how there can be a business deduction for Olivia DeHaviland's gifts to her household servants. The Senator should not give misleading examples. I know better than that, but the Senator should not use such examples, because this type of thing is forbidden by the law, and the committee amendment expressly prohibits it.

If the Senator will use examples showing that this is allowed, I will debate it with him, but he should not use illustrations on which we have gone along with him in excluding from the bill such deductions.

Mr. CLARK. The Senator is coming perilously close to violating rule XIX, section 4, of the Senate Rules, but I shall not call him on it. If he will do me the courtesy of remaining for the remainder of my speech, I shall be glad to debate it with him.

Madam President, these three little words "or associated with" have injected a new breath of life into this expense account society of specially privileged taxpayers by allowing deductions for entertainment expenditures, such as trips to horseraces and entertainment at nightclubs. Through its committee report language interpreting what expenses are associated with the active conduct of a taxpayer's trade or business, the Finance Committee, in my opinion, has reopened the Pandora's box of expense account living which the House clamped shut by the "directly related" test.

Under the Finance Committee test as explained in the committee's report, it is abundantly clear that the good life, at Government expense, continues virtually unaffected. To illustrate—and now I ask for the attention of my friend from Louisiana—I ask him which of these actual cases described in the detailed and revealing study of entertainment abuses submitted to the Congress by the Secretary of the Treasury, and some of which are discussed in the supplemental views of the Senator from Illinois [Mr. DOUGLAS], would be affected one iota if the Finance Committee amendment is approved.

First, I call to the attention of the Senators from Louisiana and Florida the

case of a corporation engaged in manufacturing which was allowed to deduct \$991,665 in 1959 for yachts, club dues, shipboard conventions, hunting and fishing trips and parties. Do my friends seriously think that, under the "or associated with" amendment of the Finance Committee, these expenditures, which have already been allowed, would, if repeated, be rejected?

Mr. LONG of Louisiana. Every one of them would be affected.

Mr. CLARK. Every one of them would be affected?

Mr. LONG of Louisiana. By the committee amendment. They would also be affected to the disadvantage of the taxpayer.

Mr. CLARK. The Senator says "affected." That is a big word. Does the Senator mean they would be disallowed?

Mr. LONG of Louisiana. In part. Some in whole; some in part.

Mr. CLARK. The Treasury, of course, disagrees.

Mr. LONG of Louisiana. It does not disagree entirely. It disagrees in part.

Mr. CLARK. Will the Senator explain?

Mr. LONG of Louisiana. Every one of these examples has to meet the primary purpose test and has to be documented by proof on the part of the taxpayer, not his unsupported statement.

Mr. CLARK. The Senator is getting into accounting. I am talking about substantive law.

Mr. LONG of Louisiana. The Senator himself offered an amendment a couple of years ago that put the primary purpose test in there. One has to establish that the primary purpose of the entertainment was to get business. Everyone of those deductions must meet the primary purpose test.

Mr. CLARK. But the primary purpose test applies only to entertainment facilities, and it is, in turn, modified by the "or associated with" test.

Mr. LONG of Louisiana. The words "or associated with" are the cause of the difference between the House and the Senate committee reports; but one must look at the Senate committee report to see what we mean by the words "or associated with." The words "or associated with" carry out the primary purpose test.

Mr. CLARK. Then what is the purpose of the words? Why not strike them out if they are meaningless?

Mr. LONG of Louisiana. The words are here for this reason: The House committee wrote the language "unless the items are directly related to the active conduct of the trade or business."

Mr. CLARK. What is wrong with that?

Mr. LONG of Louisiana. That language would have been satisfactory from the point of view of most of those concerned about this matter if the committee report had included in its meaning the general rule that an item is deductible if it is directly related to the active conduct of the trade or business. Then there follow certain specific exceptions of what are allowed in any event. Those are very limited and restricted exceptions.

It was intended, I believe, by the House when it adopted the language "directly related to"—which, incidentally, has the same meaning as the words "or associated with"—that certain entertainment would be permitted which met the primary purpose test. That is what the language was intended to mean, but when the committee report was reached on the House side, the best we could arrive at was that the taxpayer was not permitted to deduct anything under the general rule. The general rule was so restricted by the House committee report that there was nothing allowed under the general rule but the specific exceptions.

Mr. CLARK. The Senator is entitled to his opinion, but I do not read the House committee report the way he does. If the House committee report does not say what the Senator thinks it says, then it seems to me it more than strengthens our view that we do not need the words "or associated with" and that they should be eliminated.

Mr. LONG of Louisiana. The primary difference in what we are talking about is the manner in which the two committee reports were drafted. One cannot find much to argue about in the difference between the words "directly related to" and "or associated with."

Mr. CLARK. Why is the Senator arguing about them? Why do we not take the House version?

Mr. LONG of Louisiana. Because we prefer the Senate version. We require everybody to meet the primary purpose test. If a taxpayer can show, for example, that he entertained and that the primary purpose of it was to get business, and he can document it and prove it, we prefer that he be able to deduct the expense, even though it might be entertainment at a night club or a country club. We feel that if he can show that the principal purpose was to establish a business relationship, and he has documentation more than his unsupported statement to back it up, and the entertainment was not lavish or extravagant, it should be allowed.

Mr. CLARK. Under the circumstances.

Mr. LONG of Louisiana. Surely, under the circumstances.

Mr. CLARK. That is the joker there—under the circumstances.

Mr. LONG of Louisiana. If I were a New York lawyer and a client who was giving my firm a lot of business, let us say \$200,000 a year in fees, showed up in New York with his wife, I would expect to take him to a show, if he and his wife cared to go. Unfortunately, the committee report would not allow me to deduct for the cost of the meal or a ticket for his wife—

Mr. CLARK. Why should it?

Mr. LONG of Louisiana. If one feels it helps him in his business to entertain the man, and that if he does not, his competitor is going to entertain him, that becomes necessary entertainment in my opinion. That may not be the opinion of the Senator from Pennsylvania.

Mr. CLARK. No, not at all. Under the standard for which I contend, the competitor would not be entitled to en-

ertain the customer, either. No one would be provided entertainment, except at his own expense.

I have always paid for my own entertainment. I am sure my friend from Louisiana pays for his own entertainment. Why should anybody else get away with something we do not permit ourselves to get away with?

Mr. LONG of Louisiana. If I entertain someone, directly related to business, I think I am entitled to deduct the expense, and I will deduct it.

Mr. CLARK. Does the Senator undertake to deduct business expenses for liquor and food, in connection with his own salary? I do not.

Mr. GORE. Madam President, will the Senator yield?

Mr. CLARK. I do not wish to take the privilege away from my friend from Louisiana, if he wishes to continue the colloquy.

Mr. LONG of Louisiana. I think I am entitled to a deduction, if I provide a meal for a graduating class from a school in Louisiana which is passing through town.

Mr. CLARK. Surely, but not for champagne, which, under the circumstances, might be considered appropriate.

Mr. LONG of Louisiana. Frankly, I cannot afford champagne for them, so that does not come into the picture.

With regard to facilities, the committee report is drafted to provide that if a yacht is used less than 50 percent for business purposes the person involved cannot deduct 5 cents of the expense. However, if a man has a boat and he uses it more than 50 percent for business purposes, and if he can support that by more than his own assertion, if he can prove it by records and evidence, and can satisfy the people from the Internal Revenue Service—who are hard people to satisfy, as the Senator knows—that it was used more than 50 percent for business purposes, then he should be able to deduct that portion of the expense of the yacht which was used for business purposes. He still would have to pay for the part used for social purposes. That is far more strict than existing law.

Mr. CLARK. I take it, at the end of this colloquy, my friend's answer to my question—which I will restate, "Does the Senator believe that under the committee amendment a corporation engaged in manufacturing would no longer be allowed to deduct \$991,665 for yachts, club dues, shipboard conventions, hunting and fishing trips and parties?"—is, "Perhaps so; perhaps not; perhaps in part but certainly not in whole."

Mr. LONG of Louisiana. It might be permitted to deduct some of that cost.

Mr. CLARK. I thank the Senator.

Mr. GORE. Madam President, will the Senator yield?

Mr. CLARK. I am happy to yield to my good friend from Tennessee.

Mr. GORE. Like the senior Senator from Pennsylvania, the junior Senator from Tennessee is perfectly content to have the distinguished junior Senator from Louisiana entertain whatever views he desires with respect to the propriety of expense accounts, their use and the

tax deduction therefor. I am sure the Senator from Pennsylvania is not in any way arguing with the right of our friend from Louisiana to entertain the views he holds.

Mr. CLARK. Certainly not, including the right to entertainment. But, of course, the Senator realizes that the net result is that Uncle Sam picks up 52 percent of the check.

Mr. GORE. I think there are two wrongs involved in the expense account abuse, at least. Perhaps there are more than two, but there are two very specific wrongs. One is the fact that the taxpayer is discriminated against. Another is the fact that the stockholders of many of the corporations are being bilked by the abuse of expense accounts by corporate "insiders."

Mr. CLARK. The Senator is quite correct.

Mr. GORE. So two groups of people are suffering severely, the stockholders and the taxpayers.

There is another element to which the President devoted a good deal of attention in his message to the Congress. That relates to the moral fiber of our country, to a sense of fairness in our tax laws and its importance to our society and to the system of taxation we have, which essentially depends upon voluntary compliance.

Mr. CLARK. I share the Senator's view that this is a great moral issue which we are debating today.

Mr. GORE. I am not sure that the third element is not more important than the first two, in the long run.

Mr. CLARK. The Senator may well be correct.

Mr. GORE. Is not the parliamentary situation as follows: The President and the Secretary of the Treasury recommended that the Congress deal vigorously with this abuse and do so in a manner to eliminate it, and the Treasury Department testified at great length in this regard?

Mr. CLARK. Let me interrupt the Senator to say that I am perfectly willing to admit on the floor, for the record, that I have had the assistance of Treasury Department officials in preparing the speech I am now making. They did not write it, but I had their help in its preparation.

Mr. GORE. There are very competent men serving in the Treasury Department.

The House passed a bill, did it not, which was not as stringent, which was not as effective, which was not as rigid, as the President and the Secretary of the Treasury had recommended?

Mr. CLARK. The Senator is correct.

Mr. GORE. Is it not also true that the House Committee on Ways and Means submitted a report on the bill which it reported to the House, and which the House subsequently passed, which states the clear, concise, effective and understandable legislative intent of the language of the bill?

Mr. CLARK. That is my own strong view. I gather the Senator from Louisiana feels the House Ways and Means Committee did not intend the language in its own report.

Mr. GORE. Is it not true that the Senate Committee on Finance has recommended that an amendment be attached to the bill passed by the House which would weaken the bill and in some respects make it even worse than present law?

Mr. CLARK. The Senator is an able and valuable member of the Senate Committee on Finance and has made a far greater study of this question than I have been able to make, but my own investigation confirms what the Senator has stated.

Mr. LONG of Louisiana. Madam President, will the Senator yield?

Mr. CLARK. I am happy to yield.

Mr. LONG of Louisiana. Will the Senator show me where in the report—which, after all, interprets the language—there is anything which would make the law more favorable to the taxpayer than existing law?

Mr. CLARK. I am not talking about the report. I am talking about the words "or associated with." I am making my whole speech in the endeavor to try to convince the Senator from Louisiana and other Senators that these three little words would destroy a large part of the House bill and its intent, as well as the President's intent.

Mr. LONG of Louisiana. It seems to me in a way ungracious for the President to give the most lavish parties in the history of America and then to come out with the statement that a man should not be able to deduct the cost of the entertainment of a man and his wife for business. The President and the First Lady give parties Cleopatra would have been honored to be invited to attend.

Mr. CLARK. I refuse to yield further in that regard. If the Senator wishes to criticize the President of the United States in extravagant terms on the floor of the Senate, that is his right, but I will be no party to that.

Mr. LONG of Louisiana. Let me say to the Senator that I am not criticizing the President. There is nothing immoral about the parties he is giving. I think they are a credit to America.

Mr. CLARK. What makes the Senator think the President does not pay for them out of his own pocket?

Mr. LONG of Louisiana. For one thing, we give him our own Federal money with which to pay for them. How much do we allow him? I believe it is about \$50,000 a year, for which he does not have to account. I voted that he would not have to account for it.

Mr. GORE. Madam President, will the Senator from Pennsylvania yield?

Mr. CLARK. I am happy to yield.

Mr. GORE. Official entertainment by the President of the United States of distinguished foreign visitors, or citizens and officials of our Government or of other governments, is one thing, while abuse of an expense account to disguise personal expenditures with business association, about which the President complained—and those were his words—is an entirely different thing. It is the latter subject with which the pending amendment deals.

Mr. CLARK. In my opinion, the junior Senator from Tennessee has placed his finger on the clear fallacy in the argument of the junior Senator from Louisiana.

Mr. LONG of Louisiana. Madam President, will the Senator yield?

Mr. CLARK. I yield to the Senator from Louisiana.

Mr. LONG of Louisiana. The point I am getting to is that businessmen find it necessary to entertain in their businesses.

Mr. CLARK. Only because of the customs built up under present law.

Mr. LONG of Louisiana. I do not agree with that statement.

Mr. CLARK. Let us agree to disagree and let me get on with my speech.

Mr. LONG of Louisiana. I should like to again ask the Senator the question he has not yet answered. Wherein does the bill before the Senate fail to tighten up on present law? The statement has been made that in some respects it would give the taxpayer a break that he is not getting under present law. Wherein does that statement occur in the bill?

Mr. CLARK. My entire speech is intended to show instance after instance in which improper deductions would be permitted under the committee amendment. I have just given the Senator one instance, and he has refused to give me a categorical answer. He has said, "Maybe yes, maybe no; perhaps; who knows?"

I have about six additional instances in which the expenses would be claimed as a deduction under the committee amendment.

Mr. LONG of Louisiana. Compared to present law?

Mr. CLARK. Yes. All the references in the Finance Committee report to the deductibility of goodwill expenditures may make it easier as a matter of fact for a taxpayer to prove his case under the bill than under present law.

Mr. LONG of Louisiana. I told the Senator that in no instance would a taxpayer get any better break than he gets under present law. I believe if the Senator will look at every one of those cases, he will find that in every instance the taxpayer would be worse off than he would be under present law. What we have sought to do is to eliminate abuses, but we have also sought to leave legitimate and necessary entertainment expenses incurred in the course of business as a deduction for businessmen. I think we should do that.

Mr. GORE. Madam President, will the Senator yield?

Mr. CLARK. In just a moment. The Senator from Louisiana is entitled to his opinion, but the RECORD will show that I completely disagree with his position, and so does the Treasury Department of the United States. The loophole opened by the committee language is far broader than he has indicated.

Mr. GORE. I know the Senator wishes to proceed with his speech—

Mr. CLARK. I am happy to yield.

Mr. GORE. Does not the Senator think that a legislative endorsement, acceptance, and condonement of many of the expense account abuses which would

be made possible by the Senate amendment, and particularly with the majority committee report interpretation of the amendment, would do serious and lasting damage to the sense of fairness that the American people have or ought to have and hope to have with respect to our tax system? Does not the Senator think that that would constitute a serious attack upon the moral fiber of our tax law?

Mr. CLARK. I do indeed. I will say to my friend from Tennessee what I have had occasion to say on the floor several times during the last 9 months.

The Senate is losing its hold on the American people. The Senate, by many of the actions which it has taken since January, has tended to bring itself into disrepute with the American people. The Senate is living in a past which is gone. Our rules, procedures, practices, and customs are entirely out of touch with the modern world. I would dislike to think that our morals and ethics are also out of touch with the high standards which a Christian nation should maintain. I very much fear that if we should take the action which is contemplated, we would be subjected justly to criticism for having lowered moral standards.

Madam President, I return to my task of endeavoring to persuade my good friends from Louisiana and Florida that the amendments which they are supporting would indeed open up or perpetuate, as the case may be, glaring loopholes through which wealthy taxpayers and large corporations could obtain business expense deductions which, under normal ethical standards, should not be permitted, and which in effect would deprive the U.S. Treasury of scores of millions of dollars annually which, in my opinion, the Treasury should be permitted to collect.

I turn to my next example, which is that of a taxpayer engaged in the insurance business, who is allowed to deduct \$97,500 for meals, lodging, transportation, entertainment, tickets, books, and gifts; the amount covered \$6,000 for rental of an apartment, and more than \$30,000 for food, beverages, and other entertainment. I ask my friends whether those deductions would not again be approved under the committee amendment, in part at least, perhaps in major part—if those three little words were inserted in the pending measure.

I note no reply, so I go on to the third example, which is that of a manufacturer who was allowed to deduct more than \$34,000 spent on liquor, football tickets, parties, and a speedboat. The expense for liquor alone totaled \$13,750. I ask again whether that expenditure could not be justified on the ground that it was associated with a legitimate business enterprise.

Again I hear no reply.

Mr. LONG of Louisiana. Madam President, will the Senator yield?

Mr. CLARK. I am happy to yield to my friend from Louisiana. I had hoped that we would make a little legislative history—and that he would remain in the Chamber to do so—to show that all these business deductions would be rejected under the tough bill which he says

the committee wrote. I note so far that he has been unwilling to do so.

Mr. LONG of Louisiana. Can the Senator tell me whether that very item would be directly related to the conduct of a trade or business?

Mr. CLARK. I think it would be highly unlikely that an expenditure of \$13,750 for liquor alone, unless the man was in the whisky business and was giving out samples of Old Crow, or something, would be directly related.

Mr. LONG of Louisiana. Do I correctly understand the Senator to say that under those circumstances he believes the expenditure would be directly related to the conduct of business?

Mr. CLARK. It would be allowed under present law but disallowed under the House bill. The committee language, if anything, as my friend from Tennessee has said a while ago, would weaken present law.

Mr. LONG of Louisiana. The Senator has made that statement. I am waiting for him to produce the first shred of evidence that would indicate that the present law would be weakened in any respect so far as expense allowances are concerned. The estimate of the Treasury Department is that we would tighten on the present law by \$60 million a year. Our estimate and our staff's estimate is that we would tighten the present law by \$85 million a year.

But I have yet to see the Department of the Treasury or one of our staff arrive at the conclusion which the Senator from Tennessee and the Senator from Pennsylvania seem willing to accept—that there is a single case in which a taxpayer would get a better break than he does under present law.

Mr. CLARK. The Senator is taking a position which is quite peripheral to my main argument. The Senator from Tennessee is quite competent to defend his own position, with which I tend to agree. What I am trying to persuade my friend from Louisiana and what I am trying to persuade the Senate is that under the proposed committee amendment, the three little words "or associated with," would permit grave expense account abuses which would not be permitted if we went back to the language of the House bill.

The Senator wanted to discuss the \$13,000 that some corporation deducted for expenses for liquor. It would be necessary to look at the specific situation involved in every one of these expenditures to determine what portion of the expenditure a corporation would have a right to deduct. The primary burden would be on the taxpayer to fill out that return.

I believe we have pretty well narrowed down the difference of opinion between us. However, let me restate the case. A manufacturer was allowed to deduct more than \$34,000 spent for liquor, football tickets, parties, and a speedboat. In the opinion of the Senator from Pennsylvania he should not be entitled to deduct 1 cent for liquor, not 1 cent for football tickets, not 1 cent for parties, and certainly not 1 cent for a speedboat. I believe this narrows the issue between us.

Mr. LONG of Louisiana. I believe we understand what we are talking about. There are some of us—that is, the majority of the committee—who feel that under certain circumstances a businessman should be able to deduct some of these expenses.

Mr. CLARK. I shall now turn to my next example.

Mr. BUSH. Madam President, will the Senator yield?

Mr. CLARK. I yield.

Mr. BUSH. Why would the Treasury permit the deduction of that kind of thing under present law?

Mr. CLARK. It is my understanding that present law permits the deduction of "ordinary and necessary" business expenses, and that court interpretations have stretched that test so far that examples of the type that I have given have been allowed under those court decisions. I do not think they should be allowed; neither does the President of the United States. In each instance the President of the United States has stated that if we accept the language which I recommend it would be impossible to take these deductions in the future. That is my whole point.

Mr. BUSH. I fully agree with the Senator that that type of deduction is absolutely beyond the pale. I cannot understand why existing law would permit such deductions to be taken.

Mr. CLARK. I am not a great tax lawyer, although I did practice a little tax law before I came to the Senate. I do not agree with these court interpretations, but they stand, and the Treasury is bound by them.

Mr. BUSH. Does the Senator say that the examples he is giving are the result of court interpretation?

Mr. CLARK. I must be a little more sophisticated. Many result from Treasury rulings based on court interpretations. Each one did not necessarily represent a court ruling itself. I believe that the most outrageous case of all is the African safari case, with which I am sure my friend from Connecticut is familiar.

Mr. BUSH. I thank the Senator.

Mr. LONG of Louisiana. Madam President, will the Senator yield?

Mr. CLARK. I yield.

Mr. LONG of Louisiana. Does not the Senator know that we have expressly said that African safari type of thing is over with and would no longer be permitted as a deduction?

Mr. CLARK. I hope the Senator is correct.

Mr. LONG of Louisiana. We cited it as an example of the kind of thing we wanted to have prohibited from the standpoint of a deduction being taken for it.

Mr. CLARK. Fine.

Mr. LONG of Louisiana. The Senator admits that at least in that respect the committee is right and the committee did what he wants it to do.

Mr. CLARK. No. The committee report does not prohibit a deduction for a safari. It merely says the safari is not "advertisement"—it is entertainment. If the taxpayer shows it was "associated with" a business purpose, I assume it would still be deductible. The new

words "associated with" may open a loophole from which other abuses may spring in the future.

Mr. LONG of Louisiana. The Senator has yet to produce his first shred of evidence that that would be the case, other than the unsupported statement of the Senator from Tennessee.

Mr. CLARK. The Senator's interpretation of the word "evidence" is different from mine. My whole speech is competent and relevant evidence in opposition to the amendment.

Mr. LONG of Louisiana. The Senator has yet to produce his first example in which a person would be paying more taxes under the amendment than he was paying before.

Mr. CLARK. I will not argue further with my friend from Louisiana. I have produced 3 examples. My friend does not agree with me on those examples. I believe we should let the Senate decide whether he is right or I am right.

Mr. SMATHERS. Madam President, will the Senator yield?

Mr. CLARK. I yield.

Mr. SMATHERS. The example which the Senator from Pennsylvania has cited, and which he apparently obtained from the examples which the Secretary of the Treasury brought to us and put in the record, are examples on which we agree with him.

Mr. CLARK. Some were related there, and some were brought to my attention later.

Mr. SMATHERS. They are pretty bad examples. The unfortunate fact is that under present law the Secretary of the Treasury settled 60 of those 69 examples. He agreed to do that under present law. The Senator from Connecticut [Mr. Bush] asked how it was possible that this could be done under present law. In the years 1958, 1959, 1960, and 1961, the Treasury Department agreed to these settlements. Then representatives of the Treasury Department came to us and said this ought to be stopped. We agreed. That is what we have attempted to do in the bill. We have tried to see to it that only legitimate business expenses will be allowed.

Mr. CLARK. If the Senator will permit me to continue now, I shall be glad to yield to him later.

I believe that for the benefit of our friend from Connecticut we ought to point out that most of these rulings of the Treasury Department were made in large part during the Eisenhower administration, which took a somewhat different view of the expense account situation than does the Kennedy administration.

Moreover, I believe that in justice to the Treasury Department I should make the statement, to which I suspect my friend from Florida and my friend from Connecticut will agree, that the Treasury Department has in its employ very able, competent, and honest tax lawyers, and that the Department would be highly unlikely to settle such cases out of court, unless the legal opinion from its attorneys was to the effect that the case should not be taken to court, because the Government would lose it.

Mr. SMATHERS. Madam President, I agree with the latter part of the Sen-

ator's statement. With respect to the policy that was followed under previous administrations, I believe that most members of the committee believe that the Internal Revenue Service is rather bipartisan in its actions. I have not noticed—and I hope it never occurs—that whether a man is a Democrat or a Republican determines whether he will prosecute a case with vigor; or how he will prosecute an individual case.

The second point the Senator makes is exactly right.

Mr. CLARK. I agree that until one reaches the top of the department the administration of the department is clearly bipartisan, and it clearly attempts honestly to interpret the present law. However, I suggest that it does make some difference who the Secretary of the Treasury is and who the Under Secretary of the Treasury is, and what their background in business or otherwise may have been; and it makes a difference as to how competent and able civil servants at a lower level interpret the law.

Mr. SMATHERS. I would like to leave that point for just a moment and ask the Senator a question. I refer to page 27 of the report:

Your committee's bill adds a new provision to the code (sec. 274), which disallows, in whole, or in part, certain expenses which would be fully deductible under present law. The requirements imposed by this bill are in addition to the requirements for deductibility imposed by other provisions of existing law, which must be met by the taxpayer before this new provision becomes operative.

In other words, what the committee tried to do—and I believe the Senator will agree—was to provide that, as tough as existing law is, by reason of various court decisions, loopholes have opened up. There is no question about that in the minds of the majority members of the committee. We have tried to close them. Whether we have entirely succeeded is a debatable matter. That is what the Senator is debating now.

We are placing additional requirements in the law, to make it more difficult for people to abuse the tax law. We would like the Senator to understand that we are just as much opposed to sin as he is.

Mr. CLARK. The Senator may be even more opposed to sin than I am.

Mr. SMATHERS. Perhaps so. If that were true, it would be a great compliment to me. In any event, I would like the Senator to know that the purposes and intentions of the majority of the committee were good and pure. We did not want to go to the extent of saying that the legitimate businessman, in providing legitimate entertainment which is directly related to his business—as is the case in the House bill, on which we eased up—should not be permitted to deduct such legitimate expenses, if those expenses were directly related to or associated with his business.

Under those circumstances, we think a deduction would be permitted. The Treasury would agree that the proposal is a tightening up measure, because it is said it would bring in \$60 million additional; whereas the committee staff, which is usually a better estimator than

the Treasury, believes it would bring in \$85 million in additional revenue.

Mr. CLARK. I believe the difference of opinion between the Senator from Florida and myself has narrowed down to the fact that he considers legitimate certain things that I think are illegitimate.

Mr. KERR. Madam President, will the Senator yield?

Mr. CLARK. I am happy to yield.

Mr. KERR. The Senator is referring to legislation?

Mr. CLARK. I believe the rule is that we should face the Chair.

Mr. KERR. I did not make an affirmative inquiry of the Senator. I thank him for assuming the responsibility of the Chair.

Mr. CLARK. Madam President, I turn to my next example, which is a case in which a taxpayer was allowed a deduction of \$115,000 for entertainment and gifts.

Let me digress to say to the Senator from Louisiana [Mr. Long] that I am in accord with him that gifts having a value in excess of \$25 are eliminated by the House bill as well as by the Senate bill; but that is not what we are arguing about. Olivia de Havilland would no longer be permitted to deduct the value of her gift above \$25, as she was under the previous law. But what we are concerned with are the three little words, "or associated with."

Among the \$115,000 expenses which were permitted to be deducted by the particular taxpayer to whom I have referred were \$7,500 spent at a resort hotel; \$5,400 for food, liquor, and cigars for his office and farm; and \$8,700 cash to officers of his closely held corporation for entertainment.

Another case is one of a beverage manufacturer who claimed and was allowed a deduction of \$10,963 for entertaining at the Kentucky Derby.

I ask the Senator from Louisiana and the Senator from Florida whether, in their opinion, expenses incurred in entertaining at the Kentucky Derby, or the Army-Navy football game, or the Orange Bowl or Cotton Bowl football games would still be permitted to be deducted under the committee bill. I do not ask them to answer me if they do not believe they should.

Mr. LONG of Louisiana. Yes, if the expenses are directly related to or are associated with the conduct of one's business. I assume that a taxpayer could take one of his better business clients, or a client with whom he had a good reason or a supportable reason to expect he had a reasonable chance of doing business to a football game, or even to the Kentucky Derby, but not on a vacation; that would be out. The Treasury would have to decide whether such a trip was a vacation trip or was a trip for the purpose of entertaining a client, for the primary purpose of obtaining business. If the latter, the taxpayer would be able to deduct the expense of entertaining his friend at the Kentucky Derby.

The committee report spells out the kind of entertainment of clients and their wives for which deductions would not be allowable, so far as the expense

of entertaining wives was concerned, because it was felt that the entertainment was not sufficiently related to or associated with the conduct of the business to permit the deduction of the expense for entertaining the wife. Based on the present practice, I should say that the taxpayer would be permitted to deduct about half of what he had been deducting.

Mr. CLARK. I thank the Senator from Louisiana for his candid answer.

Mr. GORE. Madam President, will the Senator from Pennsylvania yield?

Mr. CLARK. I am happy to yield.

Mr. GORE. The distinguished junior Senator from Louisiana has just answered as the RECORD will show. I should like to point out that the committee report gives a very lucid interpretation of the words "or associated with." I invite the Senator's attention to page 26 of the report. I shall begin to read from about the 19th line from the top of the page. What I shall read is the part of the committee's report which describes the meaning of this language:

By your committee's amendment an alternative rule is added to the House bill under which expenses for entertainment, amusement, or recreation (with respect to both activities and facilities) also will be deductible to the extent that such expenses are associated with the active conduct of a trade or business.

I digress to say that we shall now see a new interpretation in the following sentence:

This new language will permit deduction of expenses for entertainment, amusement, or recreation incurred for the creation or maintenance of business goodwill—

I digress again to say that later, at another part of the report, we find very amusing and interesting language with respect to "goodwill." But to continue to read:

This new language will permit deduction of expenses for entertainment, amusement, or recreation incurred for the creation or maintenance of business goodwill without regard to whether a particular exception applies. However, this new language will apply only if the taxpayer demonstrates a clear business purpose and shows a reasonable expectation—

Mr. CLARK. I ask the Senator to continue from there, because I think the next words are really quite critical.

Mr. GORE. I should like to stop, first, and inquire of the Senator from Pennsylvania, who is a learned lawyer, what is a "reasonable expectation"?

Mr. CLARK. As the Senator from Tennessee, who is a learned lawyer himself, knows, we have, in many a jury case, tried to persuade a jury that an individual had or had not exercised a reasonable degree of care when crossing a street. I do not believe we have ever come to any positive legal definition of that word. I should say that the phrase "reasonable expectation" is as wide as all outdoors.

Mr. GORE. It would leave the Internal Revenue Service almost helpless in enforcing the law and eliminating expense account abuses.

Mr. CLARK. Certainly there is no clearly defined standard.

Mr. GORE. But the remainder of the sentence makes it worse.

Mr. CLARK. Much worse.

Mr. GORE. It reads: "and shows a reasonable expectation of deriving some income"—

Mr. CLARK. "Or other benefit."

What does that mean?

Mr. GORE. I raise the question: How much is "some"?

Mr. CLARK. And what is the meaning of "other"?

Mr. GORE. What are "other benefits"? What kind of benefit? A social benefit? A political benefit? Physical recreation?

Mr. CLARK. Perhaps an invitation to attend the Kentucky Derby next year on the expense account of the man whom he took to the Kentucky Derby this year.

Mr. GORE. Perhaps that would be a reasonable expectation of "benefit."

Mr. CLARK. It would certainly be another benefit.

Mr. GORE. Perhaps one could reasonably expect such reciprocity.

Mr. CLARK. It would be courteous to do so.

Mr. GORE. Now I shall read to the Senator the next sentence:

If he meets this test—

I digress to say that I do not believe it is much of a test.

I really think that is stretching the word "test" beyond anything I have even seen it applied to—

If he meets this test, the expenditure will be considered to be associated with the active conduct of his trade or business.

I ask the distinguished Senator from Pennsylvania to utilize his imagination, and see whether he can conjure up and can suggest to me some personal recreation, entertainment, enjoyment, or amusement from which I could have a reasonable expectation of getting some income or some other kind of business that would not be deductible under this so-called test.

Mr. CLARK. My imagination fails me utterly, and I am completely incapable of conjuring up such an example.

Mr. GORE. Yet in the face of messages from the President of the United States and in the face of the abuses and scandalous conduct that we know are widespread, the Senate is asked to adopt this amendment with this interpretation of it printed and on the desk of every Senator. Fortunately for the Senate, the legislative intent is spelled out.

I thank the Senator from Pennsylvania for yielding to me.

Mr. CLARK. Madam President, I thank my friend, the Senator from Tennessee, for his helpful interjection.

Mr. LONG of Louisiana. Madam President, will the Senator from Pennsylvania yield?

Mr. CLARK. I am glad to yield to my friend, the Senator from Louisiana.

Mr. LONG of Louisiana. I thank the Senator from Pennsylvania.

I would suggest that the Senator from Pennsylvania and the Senator from Tennessee turn to page 28, paragraph 3, of the committee report, where the following language will be found:

It will not be sufficient that the entertainment expense is vaguely or remotely connected with a business motive; it must be demonstrated that the predominant purpose of the expense is to further the trade or business of the taxpayer. Where goodwill generated by the expense is vague or where the possibility of the expenditure resulting in the production of income is remote, no deduction will be permitted. For instance, under present law a taxpayer may deduct expenses of entertaining buyers and others associated with his trade or business even though at the time he does the entertaining he already has more business than he can handle. Under your committee's amendment, however, no deduction will be allowed because, with a large backlog of unfilled orders, such entertainment ordinarily cannot be regarded as being associated with efforts to produce income.

Mr. CLARK. "Ordinarily."

Mr. LONG of Louisiana. And elsewhere in the report there is also language which shows that the committee is aware of situations in which people reciprocally entertain one another, and that also is disallowed.

Mr. GORE. Madam President, will the Senator from Pennsylvania yield again to me?

Mr. CLARK. I am glad to yield.

Mr. GORE. Now we have an example—one as to which the authors of the majority report exercise their imagination almost beyond belief; the distinguished junior Senator from Louisiana has just read it. The one example given—the one he has cited—of a situation in which this amendment would not permit a deduction is the fanciful situation in which a businessman has such a large backlog of unfilled orders that "such entertainment cannot ordinarily be regarded as being associated with efforts to produce income."

Incidentally, I do not think such entertainment expenses are deductible even under present law.

I am sure that the distinguished Senator from Pennsylvania, who is a distinguished lawyer, is acquainted with the case of *James Schultz*, 16 Tax Court 401.

Mr. CLARK. I regret to state that I am not as erudite in this subject as is the Senator from Tennessee. The Schultz case has escaped my observation.

Mr. LONG of Louisiana. Will the Senator inform us who won the Schultz case?

Mr. GORE. Since we have this wonderful example of the exercise of a fertile imagination, one example of a deduction which would not be allowed—that of a businessman with such a large backlog of unfilled orders that by no stretch of the imagination could he increase his business or enlarge his plant or produce more income or receive any other benefit to his business from such an expense—and since that is cited as an example of a deduction which would not be permitted, I point out that it would not be permitted under existing law—if such a fanciful situation has any semblance of reality.

Mr. LONG of Louisiana. It was cited as just an example of the purpose here.

Mr. GORE. Can the Senator from Louisiana cite another?

Mr. LONG of Louisiana. The Senator from Tennessee can think of any number of examples.

Mr. GORE. No, I cannot.

Mr. LONG of Louisiana. I believe it covers the case to which the Senator from Tennessee referred—one in regard to which he believes the entertainment would be of benefit to the taxpayer next year.

Incidentally, Mr. Schultz, the little watchmaker, won his case against the Government. But next time he could not win it—not under this committee report. Next time, he will be just another little redskin who has hit the dust.

The Treasury has estimated that by means of this amendment it will collect \$60 million that it is not obtaining now from the taxpayers; but our estimate is that it will collect \$85 million.

Mr. CLARK. I suggest that not many redskins would hit the dust under the provisions of this committee amendment.

Mr. LONG of Louisiana. \$85 million worth of redskins will hit the dust.

Mr. CLARK. Of course the Senator from Louisiana is entitled to place his own interpretation in regard to the redskins—whether they represent Washington in the football arena or elsewhere.

Madam President, to return to my presentation, let me state that each year deductions in the amount of huge sums of money are allowed to taxpayers in connection with the operation and maintenance of yachts and boats.

One manufacturer was allowed to deduct \$253,000 for the expenses of a yacht. Another was allowed to deduct \$112,000 for such expenses, as well as an additional amount of \$362,000 for a ranch, a hunting lodge, a night club, and other similar expenses. A company in the business of selling fuel was allowed \$93,000 as a deduction for a yacht. A fuel production company was allowed a deduction of \$23,000. An automobile dealer was allowed a deduction for the expenditure of \$22,000. A cake and cookie bakery was allowed to deduct \$66,000 for a yacht on which to entertain supermarket and chainstore buyers and branch managers.

In one really fascinating case—and, Madam President, I think this is the best one of all; this is really something!—a mortician was allowed a deduction of \$26,495 for yacht expenses, to entertain visiting undertakers, clergymen, and for meetings of employees.

These are only a few of the thousands of cases in which every form of luxurious living is indulged in by the few, at the expense of the many—the many non-business and small business taxpayers who are not privileged or who on ethical grounds do not choose to deduct the cost of their personal enjoyment, in computing their tax liability.

I ask whether the results of any of the cases I have described would be different under the provisions recommended by the Senate Finance Committee. I have struggled in vain to find in the bill or in the committee's report anything which would assure me that the picture would be changed.

Practically all business expenditures have been blessed by the committee. It would indeed be an unimaginative businessman who could not justify a deduction of such expenses by him, either on the ground that they were for the creation of goodwill or on the ground that they were for the maintenance of goodwill. Neither can I find a specific guideline with teeth in it which tells the taxpayer with clarity that he cannot deduct an item, or tells a revenue agent with directness that he can disallow it.

A mass of generalities is thrown on the world. Everybody is left to flounder in them as best he can.

As the junior Senator from Louisiana said on the floor a few moments ago, this is really stretching the word "test" far beyond the bounds of reasonableness.

Perhaps the supporters of the Finance Committee will point to the language of the committee report that no deduction will be allowed for entertainment expenses "which under the circumstances in which they are incurred are lavish or extravagant."

My friend, the Senator from Louisiana, an able member of the Finance Committee, has already done it.

At first glance, this might appear to be of some help. However, when one tries to apply such a test, he soon finds he is wrestling with a mirage—an unproductive exercise, I add parenthetically; for what is lavish or extravagant under the circumstances? Does the circumstance that one taxpayer is wealthy entitle him to throw a bigger cocktail party than one who is less wealthy? If he lives in New York, can he run up a bigger bill than if he lived in Altoona, or Bethlehem, or Allentown, or any one of the urban communities in my Commonwealth, where businessmen are trying, just as hard, to get and to keep business as are those in New York, or Miami, or New Orleans?

Do we look to the volume of sales of a corporation in making this determination? Can a General Motors dealer take more than a Chevrolet dealer in a middle-sized town? If a business is operating at a loss, does the expense become lavish and extravagant? Must a business in a small town entertain on a more conservative scale than a similar business in a big city? Is this fair? If entertainment, as many in the business community would have us believe, is the highroad to business success, does not the "lavish and extravagant" test freeze the competitive position of the large taxpayer as against the small one, keeping the little fellow down?

Equally as important as these basic considerations of fairness and equity are the practical ones of application by Government officials of the new so-called rules of the taxpayers and their administration.

What standards are to be followed? Is it not apparent from the vagueness of these so-called tests that each revenue agent will, depending upon his personal background of frugality or extravagance, apply his own ethical and moral personal standards, leading quickly to a hopeless lack of uniformity, which no

doubt will have to be resolved many years later by the courts?

If these rather gloomy consequences which I have just outlined are not to follow, then is it not incumbent upon the proponents of the Finance Committee measure to state affirmatively, in support of their amendment, more precisely what they mean? Is it not apparent that any rule in this area, to be workable, must utilize some form of dollar limits? For example, if tickets to a musical comedy at \$30 apiece are lavish, is it not incumbent upon the committee to indicate at what point they lose their lavish character? Would it be at \$20 a ticket, \$10 a ticket, or \$2 a ticket? Or are \$2 tickets only those limited to pari-mutuel systems at racetracks?

What about football games? Are speculators' tickets on the 50-yard line at the Army-Navy game at Philadelphia out of the question?

The Senator from Illinois [Mr. Douglas], in his dissenting report, raises a number of pertinent questions along this line. I ask unanimous consent that an excerpt from the views of the Senator from Illinois be printed in the RECORD at this point in my remarks.

There being no objection, the excerpt was ordered to be printed in the RECORD, as follows:

If the circumstances involve a taxpayer accustomed to entertaining in an elaborate and expensive style, can they be held to be "lavish" under the circumstances? When does a yacht become an extravagant expenditure? When is it 60 feet in length? 100 feet in length? Would these criteria vary with the income (or expected income) of the taxpayer? Would a resident of Miami Beach, Fla., be entitled to a bigger and more expensive yacht than a resident of Providence, R.I.? Would a beach home with eight rooms be a lavish facility? What about one with 30 rooms? Would a corporate president be entitled to drink champagne whereas a vice president could have only a whisky highball and a proprietor of a country grocery store only ordinary corn liquor?

Mr. CLARK. What I have said so far might give one the impression that adoption of the House provision would mean that all tax deductions for the pleasant things of life had been taken away. This is very far from the truth, indeed. In seeking to restore the House version, I do not ask that all businessmen should lead a Spartan existence. The House bill still permits continuation of business entertainment in the most important areas where it is the normal, everyday business custom.

First of all, the usual type of entertaining business associates through meals at restaurants and hotels is not disturbed. This would include expenditures for the consumption of alcoholic beverages. I am no prohibitionist, but I think everyone should pay for his own liquor. This expenditure, even though it is used purely to build goodwill, and even though no business is actually discussed, is still deductible. This covers the most significant portion of goodwill entertainment conducted in this try.

This means also, for example, that the costs involved in attending or

inviting guests at banquets of business or professional groups are also left undisturbed.

Personally, I would disturb them.

Next, the deductibility of costs associated with business conventions is also largely unaffected. Thus, travel expenses for the purpose of the convention continue to be deductible. Of course, the cost of meals and liquor and lodging at the convention is also deductible. The deductibility of expenses of hospitality rooms—in other words, cocktail suites—to entertain at conventions to build good will is specifically continued by the House report, as under present law.

Personally, I would discontinue them.

Is it not clear, when the liberal treatment of wining and dining business associates and the generous rules with respect to conventions are taken into account, that, as the Senator from Illinois [Mr. DOUGLAS] points out, the House provision "strikes only at the high, wide, and fancy living and indulgences in personal pleasures which all taxpayers ought to pay for themselves without Government subsidy"?

I agree with the Senator from Illinois [Mr. DOUGLAS].

Let me point out to many of my business friends in Pennsylvania that the House bill does not affect the restaurant business, but it does curb deductions for items like trips to the Kentucky Derby and after-hours nightclub life.

I am proud to say that the Senate, recognizing the seriousness of the expense account problem and its destructive effect upon the morale of most taxpayers, passed in 1960 a measure I sponsored which was in some respects even more stringent than the one contained in the House bill. The provision which we approved in 1960 would have denied a deduction for all entertainment expenses with one exception—the cost of business meals. In addition, expenses for gifts would have been disallowed, subject to a \$10 annual limitation for each recipient and social club dues would have been completely disallowed. However, the conferees quickly kicked this amendment out of the compromise reported back to both bodies. They said they wanted to give the Internal Revenue Service another opportunity to improve the expense account picture by administrative measures.

Therefore, nothing was done.

Now comes the President of the United States to ask us to legislate, because administrative action is inadequate. This is what he said:

In recent years widespread abuses have developed through the use of the expense account. Too many firms and individuals have devised means of deducting too many personal living expenses as business expenses, thereby charging a large part of their cost to the Federal Government. Indeed, expense account living has become a byword in the American scene.

Then the President sent to Congress language far more stringent than that adopted by the House of Representatives, which in turn was substantially more stringent than what the committee

would have us accept in the Senate today.

As evidenced by the provision which it adopted this year, the House has now changed its views and has moved closer to the views of the Senate in 1960. I suggest, Madam President, that it would be sad, indeed, now that the House has come around to our view, if the Senate now were to jettison this major accomplishment and be the body responsible for a great step backward in the development of our tax laws. I urge restoration of the House provisions and accordingly the defeat of the committee amendment.

Madam President, I yield the floor.

The PRESIDING OFFICER. What is the pleasure of the Senate?

Mr. LONG of Louisiana. Madam President, the committee amendment dealing with the deduction of entertainment expenses would relieve somewhat the unreasonably extreme interpretation of the House provision. At the same time the committee amendment drastically would tighten the rules of existing law which, in some cases, may have been abused.

I supported the amendment of the Senator from Pennsylvania several years ago. I supported his amendment on the principle that there were abuses in regard to entertainment allowances and that the laws in respect to such abuses should be tightened. I fought in conference to try to bring back something in that regard.

As one who supported the amendment, it was my feeling that we could not tell exactly how far the amendment would go. I knew there were some abuses, and I felt that the subject deserved some consideration. I was sorry at the time that we could not bring back from conference something to correct the abuses. I was not wedded to any particular version or tightening-up method. I thought some way should be devised to tighten the law with respect to abuses, but I was one of those who, in an effort to tighten the law with respect to abuses, also wished to allow legitimate business expenditures for necessary entertainment expenses in connection with a person's business.

The committee amendment would tighten the rules relating to deductions for entertainment expenses to the tune of \$85 million a year. Let me make that point clear. \$85 million, or more, in new taxes would be collected each year as a direct result of the committee bill.

I have challenged anyone to show—though I have not heard a response—that there is any instance in which a taxpayer would get any break he is not already getting, insofar as anything which is in existing law is concerned. The taxpayer would have to pay more. Every example cited has been one in which the taxpayer would gain no advantage from the bill. This should quiet the fears of those who state that the committee amendment would do nothing.

The committee amendment would do quite a bit.

It would deny deduction for entertainment, amusement, or recreation expenses which are not "directly related to or associated with the active conduct of a trade or business." Now, let me tell Senators what a taxpayer would have to show to convince a revenue agent that his claimed deduction meets this test. He must show that he had a clear business purpose for making the expenditure. He must show that the "predominant purpose" of the expense was to further his trade or business. But even this would not entitle the taxpayer to a deduction. No, he must show more. He must prove—I repeat, prove—by evidence corroborating his own testimony the business purpose of the expense, the business relationship to the taxpayer of the person entertained, the time and place, and the precise amount expended. Failure to prove any one of these points will cost him not a part of his claimed deduction, but all of it.

This is a marked strengthening of the existing law. But the committee amendment would not stop there.

It would point out in clear, unambiguous terms the types of expenses which may not be deducted under any circumstances. Under the committee amendment, no deductions would be allowed for entertaining a customer's family. That would tighten the existing law.

Under the committee amendment, no deductions would be allowed when the entertainment cannot increase business. That would tighten the existing law.

Under the committee amendment, no deductions would be allowed for expenses for entertainment which is against public policy or which violates public morals. That would add new teeth to the existing law.

Under the committee amendment, no deduction would be allowed for partly social—partly business expenditures. No, only the purely business expenses which are "directly related to or associated with the active conduct of a trade or business" could ever be deducted. That would add new rules to existing law.

Under the committee amendment, no deduction would be allowed for vacations of any sort. That would strengthen existing law.

Under the committee amendment, no deduction would be allowed for expenditures which are either lavish or extravagant under the circumstances. That is to be made clear.

Under the committee amendment, no deduction would be allowed for facilities which are not used primarily for business purposes. Again, new teeth would be added to existing law.

Under the committee amendment, no deduction would be allowed for facilities which are used primarily for business purposes when the taxpayer fails to establish that the expense with respect to the facility is "directly related to or associated with" his trade or business. I have already shown what the taxpayer must go through to establish this fact. This would tighten the existing law.

Under the committee amendment, no deduction would be allowed for hunting used for vacation purposes. This would be an improvement over the existing law.

Under the committee amendment, no deduction would be allowed for "call when family use exceeds business use. This would tighten existing law.

Under the committee amendment, no deduction would be allowed for hunting safaris to Africa. These are deductible under existing law.

The safari to Africa is one of the six examples I have heard cited over and over again on the Senate floor. No deduction would be allowed for that.

Another of the horrible examples cited was the giving by a movie actress of jewels to one of her servants; \$25 could be deducted.

Under the committee amendment, no deduction would be allowed for Bermuda or Las Vegas or Miami Beach vacations. They are deductible under existing law.

Under the committee amendment, no deductions would be allowed for "call girls." They are claimed as deductions under existing law.

We wish to make clear that nothing of that sort is permitted.

Under the committee amendment, no deduction would be allowed for wives who accompany husbands on business trips. Under existing law expenses for wives have been allowed.

Under the committee amendment, no deduction would be allowed for wedding parties, honeymoons, or fancy debuts. Expenses for such purposes were claimed on tax returns under existing law.

Under the committee bill, no deduction for gifts to any person of more than \$25 would be allowed. Under existing law, there is no limit. This would tighten existing law.

Madam President, these are merely examples of what the committee amendment does. I submit that what the committee amendment would do is what the House committee sought to do. I quote from the House report:

The committee agrees that abuses in this or any other area of the tax law should not be tolerated, but it does not believe that complete disallowance of such expenses, as recommended by the President, is the proper solution to the problem.

Yet, the House committee report then proceeded to weave a virtually complete disallowance rule. I quote again from the House report:

If the expenditure is for entertainment which occurs under circumstances where there is little or no possibility of conducting business affairs or carrying on negotiations or discussions relating thereto, the expenditure will generally be considered not to have been directly related to the active conduct of business. Thus, the absence of the taxpayer or his representative from the entertainment activity ordinarily indicates that the entertainment was not directly related to the conduct of the taxpayer's trade or business.

Madam President, I ask, What entertainment expenses would be allowable under this language?

It was to get away from the harsh, unyielding rule of the House provision that the committee added three words to the House bill. Those three words are, "or associated with".

The addition of those three words, together with the interpretation given them by our committee report, would permit legitimate business entertainment expenses incurred for legitimate business purposes to be deducted if the taxpayer could satisfy the requirements I have already explained.

The addition of these three words together with the interpretation given them by our committee report permits legitimate business entertainment expenses incurred for legitimate business purposes to be deducted if the taxpayer satisfies the requirements I have already explained. At the same time these three words enable us to prevent and eliminate abuses where they occur.

The President has said that business entertainment expenses "confer substantial tax-free personal benefits to the recipients. In other cases," he says "deductions are obtained by disguising personal expenses as business outlays."

Let me read a provision of the Internal Revenue Code which makes it clear that personal expenses are never deductible.

Section 262 of the Internal Revenue Code of 1954 provides as follows:

Except as otherwise expressly provided in this chapter, no deduction shall be allowed for personal living or family expenses.

Personal expenses which may have been "disguised as business outlays" under existing law, will be disallowed under the committee amendment. This will be so for several reasons.

First, the expense must be shown to be directly related to or associated with the active conduct of a trade or business.

Second, the taxpayer must establish and prove by evidence other than his own testimony the business relationship of the person entertained, the time and place of the entertainment, and the amount expended. In other words he must disclose to the tax collector all the facts and circumstances surrounding the claimed deduction. If it is a disguised personal expense, it will be detected and disallowed. If there is fraud, there may also be criminal penalties. I am convinced the committee amendment stops the types of abuse described by the President.

Now let me say more about "disguised expenses." Under existing law many expenses for entertainment are deducted as "advertising," "cost of goods sold," "selling expenses," "miscellaneous." Under the committee amendment entertainment expenses, if they are to be deductible at all, are to be deductible only as an "entertainment expense" to which the committee bill will apply.

Moreover, as I have demonstrated, no longer can a taxpayer "contend"—as the Senator from Tennessee stated last night—that his yacht was used for business purposes and get a deduction. No. He must show a great deal more. I have already described these other features. In addition, no taxpayer will ever be able to "settle" with the income tax people for any claimed entertainment expense deduction. The "settling rule" is overruled by the committee bill, and no deduction will be allowed for any expense which the taxpayer proves and establishes his right to deduct.

It may be that under the existing law there may be cases of "you entertain me and I will entertain you." That will not be possible under the committee bill.

Reading from page 36 of the report—

However, under this exception, it will not be possible to deduct luncheon expenses of a so-called reciprocity luncheon group under which a group of businessmen frequently lunch together and alternate in paying the check (and claiming it as a business expense deduction). This practice is not connected with a trade or business but is a personal or social expenditure which is not deductible under existing law.

It has been said a taxpayer must meet precisely the same tests today as would be provided by the committee bill. This is erroneous; this is wrong. The tests of this bill are in addition to the "ordinary and necessary" rules of existing law. In no case are they in lieu of the present rules. In every case they would add to the current law new tests which also must be met by the taxpayer if his claimed deduction is to be allowed.

Now let me point out the circumstances which would be taken into account in determining whether expenditures are lavish or extravagant. The circumstances are specified in the statute—reading from page 44 of the Senate bill—

The taxpayer [must] substantiate by adequate records or by sufficient evidence corroborating his own statement (A) the amount of such expense or other item, (B) the time and place of the travel, entertainment, amusement, recreation, or use of the facility, or the date and description of the gift, (C) the business purpose of the expense or other item, and (D) the business relationship to the taxpayer of persons entertained, using the facility, or receiving the gift.

Add to these the possibility or probability that the entertaining will produce new business and we have the circumstances.

Note that these circumstances have no relation to whether the taxpayer is wealthy; or to where he lives.

Madam President, that would depend upon the circumstances of the particular case. Those who have opposed the provisions of the committee bill have in some cases stated quite explicitly that they would permit no entertainment expenses. As one Member of this body, I know that businessmen do have entertainment expenses. They must be claimed. Otherwise a person would pay an income tax at a higher rate than he should. In some instances the Government already takes 80 to 90 percent of a taxpayer's income. The taxpayer must therefore be permitted to deduct for expenditures which he must make in order to remain in business.

I know of cases in which businessmen have felt that if they could not entertain, they could not compete. Some of them are going to find it necessary to entertain in order to obtain business and attract business away from their competitors, even though they do have to pay taxes on the money spent for entertainment, and regardless of whether it is deductible or not deductible.

The point was made on the floor of the Senate by the Senator from Tennessee that a corporation might be victimized

because entertainment might be done at corporate expense. The corporation would be victimized if the corporation's executives did not entertain. The business of that corporation would go to its competitors, so that over a period of time the corporation would lose a great deal of its business.

I have made a statement about the President. I do not reflect on him or his wife. The President of the United States and the First Lady are two of the best entertainers in the entire United States of America. They give the best parties in America. If anyone gives any better parties, I would be curious to know who it is. The President happens to be a very wealthy man. However, I hope that we shall see to it now and forever that even if the President of the United States should happen to be a poor man, he could entertain as his guests visitors to our country, outstanding citizens, foreign diplomats or government officials, on the same general standard that is expected of other nations on this earth.

We provide many millions of dollars for our ambassadors to entertain all over the world. The President tells us that the amount is not adequate. We must try to spread our influence and generate good will in competition with the Soviet bloc and other nations throughout the world, in order to carry out the purposes of our Nation's foreign policy.

If the President recognizes the necessity of such expense and asks for more money for entertaining at our French Embassy and other embassies, and if the President and the First Lady can be among the most gracious entertainers in the world, I believe we should recognize some of the business people in our Nation and allow them a deduction for the expense of entertainment.

Some of the expenses are necessary. Businessmen either entertain and keep their business or competitors entertain over a period of time and take the business away. The expense will remain whether or not we allow it as a tax deduction. But in a nation in which the income tax rate is as high as 90 percent, it seems only fair that a businessman should be entitled to deduct his required and necessary expenditures in order to stay in business or to get business. To allow him less than that, in view of a 90-percent income tax rate for the highest bracket of income, would, in the judgment of this Senator, be extremely unfair.

For that reason I urge that the Senate go along with the committee report. In my judgment the committee went too far. To me it seemed an outrage in some respects. To cite one example: If a taxpayer is trying to do business with a client who is his main source of business, and that man comes to town, he invites the man to dinner. If the taxpayer did not entertain the client over a long period of time, he might lose the business to a competitor who otherwise would seek to entertain the man. If the client should say, "I am sorry, my wife is with me. I cannot go because I do not want to leave my wife in a hotel room," it seems to me that it would be rather unreasonable to refuse the tax-

payer the right to deduct the expense of a meal for his principal customer's wife.

Yet the committee would deny him that. It seems to me that is going too far. To go further and to seek to completely disallow necessary entertainment expenses under the restrictive rules the committee would impose seems to me to be most unreasonable and unfair. I hope the Senate will not go beyond what the committee has recommended.

Madam President, I suggest the absence of a quorum.

The PRESIDING OFFICER. The clerk will call the roll.

The legislative clerk proceeded to call the roll.

Mr. LONG of Louisiana. Madam President, I ask unanimous consent that the order for the quorum call be rescinded.

The PRESIDING OFFICER. Without objection, it is so ordered.

Mr. SMATHERS. Madam President, I feel that the committee amendment which was reported by a substantial majority of the Committee on Finance is essential unless we are to adopt the unreasonable philosophy that legitimate business expenses for legitimate business purposes are to be arbitrarily disallowed as a deduction.

I do not believe, and I do not think most members of the Committee on Finance believe, that businessmen as a whole are crooks. They do not believe that all businessmen are out to beat the Government willfully and deliberately. They do not believe that all businessmen are willful and determined chislers. They do not believe that all businessmen are endeavoring to evade the responsibility of carrying their fair share of the burden or obligation of paying for the operation of the Government.

On the other hand, most members of the Committee on Finance realize that there are and have been some abuses with respect to expense account deductions in the business community and elsewhere. These are the kinds of abuses which the Committee on Finance has endeavored to stop. While we want to stop the abuses, at the same time we desire, if at all possible, to continue the practice of permitting legitimate businessmen to deduct legitimate business expenses.

Under the House bill as interpreted by the House committee report, virtually no entertainment expense would have been deductible unless it were an expense described in a specific exception to the general rule. In other words, under the House bill, the general rule was a disallowance rule, pure and simple. It provided that all expenses were to be disallowed, but permitted the taxpayer to make a few minor exceptions. It was the feeling of the Committee on Finance that this practice would be too harsh. In an effort to catch the violators of the law, the committee felt that the report which was written by the Treasury in support of the House bill went too far in its purpose to catch the rats and instead burned down the barn. We did not believe the barn should be burned down.

So, unlike the House bill, the committee amendment permits the taxpayer to

continue to deduct certain entertainment expenses if he clearly demonstrates a close association between the expenditure and a trade or business or profession.

The majority of the Committee on Finance believe that a closer relationship should be required than that which is required under present law. We believe that is necessary if we are to eliminate the abuses which the Secretary of the Treasury and others have called to our attention.

I am not aware that any member of the Committee on Finance or, for that matter, any other Member of the Senate, condones the type of abuses which Senators who will oppose our amendment will continue to talk about—Bermuda vacations, Alaskan hunts, and safaris to Africa. No one desires or expects that practice to continue.

We do not believe that Senators who oppose our amendment have a first mortgage on virtue. We do not believe that they are the only ones who are against sin. We believe we are just as much against sin and just as much against abuses of the tax law as they are; but we do not go to the length to which they go in contending that the law should not permit legitimate businessmen to take legitimate business deductions.

I do not believe that the only way to prevent abuse is to condemn each and every American taxpayer who finds it appropriate or necessary to resort to business entertainment in order to market his product or service.

We know that various businessmen react differently to competitive pressures. Some cut prices; others provide fringe benefits to buyers, such as more attractive packaging or better servicing; still others advertise more extensively.

Business entertaining is nothing more or less than a form of advertising. However, it is a form of advertising which is particularly suitable to small, new, and struggling businesses, in which personal contact with potential customers or clients may be far more fruitful than a hundred newspaper or magazine advertisements. No one has yet suggested that deductions be allowed for expenses of other forms of advertising.

Last night, and again this morning, the able Senator from Louisiana [Mr. Long] stated that a legitimate business deduction made it possible for a small businessman to compete with a very rich businessman. If no legitimate business deductions are to be allowed, then, of course, the man who has a big business which earns a great sum of money can entertain and pay for the entertainment himself because he has the money to do so. But the small businessman, who is trying to increase his business and put it into the category of a business can compete only if he has a legitimate expense account.

Legitimate deductions for business entertainment have become an integral part of our way of life. The committee amendment is designed to outlaw the abuse of the entertainment expense deduction.

Let me describe some of the respects in which the committee amendment

makes provision for legitimate business entertainment deductions.

Mr. LONG of Louisiana. Madam President, will the Senator from Florida yield?

Mr. SMATHERS. I yield.

Mr. LONG of Louisiana. Before the Senator discusses that point, does he not see some inconsistency in the administration asking us, on the one hand, to provide more money so that our ambassadors to foreign countries may entertain in foreign lands, but, on the other hand, to provide for a complete disallowance of entertainment expense incurred by American businessmen in an effort to improve their business? We are asked to provide more money for ambassadors to entertain, so as to protect and further the interests of the United States in foreign affairs; but we are also asked to withdraw any allowance whatsoever for legitimate business entertainment by American businessmen.

Mr. SMATHERS. I agree with the able Senator from Louisiana. The distinguished Senator from Tennessee [Mr. GORE], a leading opponent of the amendment proposed by the Committee on Finance, believes that further restrictions should be imposed upon deductions of expenses for business entertainment. Still, the administration is asking for more money for ambassadors for entertainment purposes overseas. Evidently it is felt that such entertainment has some benefit, because the taxpayers are asked to pay for it.

If that is true with respect to our overseas operations, I am sure that we should not deny a legitimate businessman in the United States the right to make legitimate business-expense deductions. So I completely agree with the able Senator from Louisiana.

I return to the point in regard to what the amendments and report of the Senate Finance Committee do. We are tightening up—I wish to repeat that again and again—the law, as compared to what it is at the present time. The committee's bill will not permit a deduction for any entertainment expense which is not directly related to or associated with the active conduct of a trade or business.

The Senator from Tennessee makes much of the words "or associated with," and asks where they come from. I am not certain just where they come from, except that I may say that when we said to the staff of the Treasury Department that we did not like the language included by the House, and that we wanted a provision a little less severe than the one in the House version of the bill, and when we asked them what they would suggest, they suggested the words "or associated with." I have a sneaking suspicion that it would be found that the same individual in the Treasury who helped prepare the expense-account message for the President is responsible for those words. I noted last night that the words "or associated with" were used in the President's speech; and the Treasury has supplied us with the same words. So perhaps the same one who helped prepare the President's speech

also helped prepare this part of the report; and he is an employee of the Treasury Department of the United States.

Mr. LONG of Louisiana. I believe the President said he recommended a complete disallowance of all these expenses, although some of them were related to or associated with the conduct of the taxpayer's business.

Mr. SMATHERS. Yes; that is correct.

Mr. LONG of Louisiana. The House said it would allow the expenses if they were directly related to the conduct of the business. But after the House passed the bill and it came over to the Senate, we said we did not object to that language, but we thought the report was too tough.

Mr. SMATHERS. The Senator is correct.

Mr. LONG of Louisiana. So we wrote our own report, and included a few words to explain our meaning. We took the rest of the President's language; in addition to the words "directly related to," we took the words "or associated with"—so as to read, "directly related to or associated with the conduct of the trade or business."

Mr. SMATHERS. The Senator's statement is correct.

Mr. LONG of Louisiana. So, in effect, the President implied that it is difficult to justify disallowing entertainment expenses directly related to or associated with the conduct of a trade or business.

Mr. SMATHERS. Yes.

Mr. LONG of Louisiana. In other words, the House adopted half of the President's language, and we took the rest of it.

Mr. SMATHERS. Yes; and I am certain that is where the words came from. They are an effort on our part to stop the gross abuses which have been described in the RECORD and were described by the Secretary of the Treasury when he was before the committee, and yet not to go so far as to prevent legitimate businessmen from taking legitimate business-expense deductions. That is our purpose.

Under this amendment, no deduction will be allowed if the facts in the case indicate that no business could result from the entertainment; and under this amendment no deduction will be allowed for entertainment expenses of a nature which are against the public policy. We read some rather colorful language about things which would not be allowed. The able Senator from Tennessee asked, last night, "Where did the language about these illustrations come from?" We included them because we knew that if we did not, the able Senator from Tennessee and his cohorts would point out such examples, and would do so in such a way that it would seem to appear that we were advocating sin or illegality; and we did not wish to be put in such a position.

Furthermore, when an expense is for entertainment of both business and social guests, there will be no deduction for expenses attributable to the social guests.

Today that is a great area of abuse—situations in which a businessman en-

tertains some of his business friends and also entertains some of his social friends. Under the bill as reported by the committee, the only deduction which such a businessman would be eligible to take would be the costs of entertaining his business friends. He would not be eligible to take a deduction for the costs of entertaining his social guests.

Furthermore, no deduction whatever for any sort of vacation would be allowed. However, under existing law, deductions can be taken for vacations to Bermuda or to Miami Beach, even though during the vacation business was transacted on only 1 or 2 days. Nevertheless, under present law the expenses of the entire vacation can be claimed as a deduction. The Finance Committee says that is going too far; and the bill, as reported to the Senate, would stop that practice.

There will be no deduction for any entertainment expenses which the circumstances indicate are either lavish or extravagant. It will be for those in the Bureau of Internal Revenue to decide what expenses come in that category. But when someone says those in the Bureau of Internal Revenue will suddenly become generous, all I can say, in reply, is that one who takes that position must not have had much experience in recent years with the Bureau of Internal Revenue.

No deduction will be allowed for entertainment expenses relating to facilities, such as yachts—Senators should bear this point in mind, for I am sure that in a minute or so they will hear about the facts, all over again—and no deduction will be allowed for entertainment expenses relating to other facilities, such as hunting lodges or fishing camps, unless it is clearly established that the facility was used primarily for direct business purposes.

Mr. GORE. Mr. President, will the Senator from Florida yield?

The PRESIDING OFFICER (Mr. METCALF in the chair). Does the Senator from Florida yield to the Senator from Tennessee?

Mr. SMATHERS. I am happy to yield to my able friend from Tennessee.

Mr. GORE. Several references have been made—particularly by the junior Senator from Louisiana [Mr. LONG], and also, I think, by the junior Senator from Florida [Mr. SMATHERS]—or several statements have been made that the report specifically provides that a deduction for the expenses of a safari to Africa, such as the one indulged in by the Sanitary Farms Dairy, Inc., would not be allowed.

But now I find, according to the report, that, in fact, that is not the case. If the Senator from Florida will turn to page 28 of the committee report, and will read the paragraph carefully, he will see that an incorrect interpretation has been given.

I should like to know whether the junior Senator from Florida still insists that the committee report would prevent the deduction of the expenses of a safari to Africa.

Mr. SMATHERS. I do not know of any businessman who could do it; I do

not know of any businessman who is in the business of catching lions or alligators or buffaloes. But if there were one who was in the business of catching lions or alligators or buffaloes, and if he were on a safari for that purpose, and if that was his business, I suppose he could deduct those expenses. But I think the total implication is crystal clear—that they cannot be deducted unless the safari is directly related to his business.

Mr. GORE. The Senator is dodging the question.

Mr. SMATHERS. No; I am not. I say that I do not know of any businessman who could do that. Does the Senator from Tennessee know of any businessman in Tennessee who could justify, as a business expense, the expense of going to Africa? I do not know of any who could.

Mr. GORE. Mr. President, the Senator from Florida is a very good lawyer; and he knows that one way to avoid a question is to ask another one. But it has been repeatedly stated that, among the other things that the report would rule out as not deductible, would be the expenses of a safari to Africa, such as was indulged in by one taxpayer. However, I find that the committee report does not say that.

Mr. SMATHERS. The Senator from Tennessee well knows we are making legislative history here.

Mr. GORE. Well, the Senator is trying to make it with this report.

Mr. SMATHERS. Certainly it was the intention of the Finance Committee, and it is the intention of every Senator I know of here on the floor—certainly it is the intention of the Senator from Louisiana, the Senator from Virginia, the Senator from Oklahoma, and the other Senators who are supporting this amendment—to be certain that no businessman can have a vacation on a safari in Africa, when there is no reason that any reasonable man could possibly see to deduct it. We do not want him to be able to, and we think that is what the report says.

Mr. GORE. I will not press the Senator except this one more time. The statement was made on the floor of the Senate last night and today at least six or eight times that the committee report would deny deductibility of the cost of a safari to Africa. Now I ask the Senator, Does his report say that or does it not?

Mr. SMATHERS. It does that in every instance where a man would try to claim that that safari had a relationship to his business, and he could not deduct it otherwise. We do not go so far as the Senator would like to have us go—that, whatever a man's business is, he cannot have any business deductions. That is what the Senator from Tennessee really wants. We do not subscribe to that. We do not believe there are many people who can take a safari or trip to hunt lions, tigers, rhinoceroses, and alligators in Africa, and claim, and show it is a business deduction. We do not think they should have been permitted to claim it before, and we certainly do not think it can be done under the present language.

Mr. GORE. After conferences with the staff, I am sure that neither of my two distinguished friends will no longer insist that the statements they have been making with respect to the celebrated case are factual.

Mr. SMATHERS. On the contrary, we could not accept that statement.

Mr. GORE. Very well.

Mr. SMATHERS. The Senator from Tennessee is entitled to his conclusion.

Mr. GORE. The Senator from Florida does not have to accept it, but I carefully note that he is not still saying it.

Mr. SMATHERS. We are saying what I hope we have been saying, and that is, one cannot take a deduction for a vacation; vacations are totally and completely eliminated as bases for tax deduction.

Mr. GORE. I will challenge the Senator on that a little later.

Mr. SMATHERS. Very well, challenge me a little later. What we are saying is that, unless a man can demonstrate that a safari is directly related to or associated with his business, he obviously cannot take that deduction. We do not believe there are very many business men who can do it.

Mr. GORE. Will the Senator yield further?

Mr. SMATHERS. I yield.

Mr. GORE. The Senator has got to the point. He says "if associated with" the business, it would be deductible. Now I ask him to turn to page 26 of the report. Then we see what the test of "associated with is. If the Senator will read with me beginning in the middle of the second paragraph:

This new language will permit deduction of expenses for entertainment, amusement, or recreation incurred for the creation or maintenance of business goodwill without regard to whether a particular exception applies. However, this new language will apply only if the taxpayer demonstrates a clear business purpose and shows a reasonable expectation—

Whatever that is—
of deriving some income—

However much that is—
or other benefit—

Whatever that is—

Mr. SMATHERS. Finish the sentence—"to his business."

Mr. GORE (continuing):
benefit to his business as a result of the expenditure.

Mr. SMATHERS. That is right.

Mr. GORE. So the Senator has said that if a safari to Africa met this test, it would be deductible. Yet the Senate has been told at least six times in previous debate that under no conditions will it be deductible.

Mr. SMATHERS. If the Senator will turn to page 28 of the report, he will see this language:

It will not be sufficient that the entertainment expense is vaguely or remotely connected with a business motive; it must be demonstrated that the predominant purpose of the expense is to further the trade or business of the taxpayer.

The Senator always tries to prove his case by reading half of the language.

Mr. GORE. I have read the definition of "associated with" and I have read the test prescribed by the majority report. The Senator cannot dodge his own report, bearing his own name, by saying I read a part of it. I read it all.

Mr. SMATHERS. But the Senator did not read what is on the next page:

It will not be sufficient that the entertainment expense is vaguely or remotely connected with a business motive; it must be demonstrated that the predominant purpose of the expense is to further the trade or business of the taxpayer.

Mr. GORE. Will the Senator go on and read the one highly imaginary example that his report gives? It is laughable.

Mr. SMATHERS. That is a matter of opinion of the Senator from Tennessee. I have not been able to convince the Senator from Tennessee for a long time, and apparently I have no hopes this time.

Mr. LONG of Louisiana. Mr. President, will the Senator yield?

Mr. SMATHERS. I yield.

Mr. LONG of Louisiana. In the Sanitary Farms Dairy case, where a man took a safari to Africa, he did not claim it as an entertainment expense. Even under existing law the man could not deduct the expense as entertainment.

Mr. SMATHERS. That is correct.

Mr. LONG of Louisiana. As the law stands now, if a man takes a vacation and brings a client with him, we have fixed it so he cannot deduct that vacation expense. We say he cannot take it as an advertising expense. He has to claim it as an entertainment deduction, and as an entertainment deduction it was not allowed under existing law and will not be allowed under the proposed law. We say no deduction can be made for anything extravagant.

On page 30 of the report we say:

In example A, no deduction would be allowed under your committee's bill because a vacation trip for a customer and his wife is not "directly related to the active conduct of the taxpayer's trade or business."

So the point is that the man probably could not have claimed the expense of a safari to begin with as an entertainment expense. He might have claimed it as a vacation. But we outlaw that, knowing that he must claim it as an entertainment expense, which we say cannot be allowed as an advertising expense, where it would have been allowed.

I would have said that, under the facts of the Sanitary Farms Dairy case, the man could not have claimed the expense of the safari to Africa. As the Senator from Florida has said, if his profession had been that of a big game hunter, he might have claimed it, but under the facts of the Sanitary Farms Dairy case, he could not have claimed it.

Mr. SMATHERS. I thank the Senator.

When we write these provisions, we expect that reasonable men will give the language a reasonable interpretation. We do not expect the language to be quartered and stretched to unreasonable conclusions. We expect the Internal Revenue Service to be permitted to col-

lect all the taxes they can, with our help, and we do not expect them to permit a man to go to Africa, at lavish expense, and charge it as a business expense. We do not want them to. That is why we put this language in the report.

There will be no deduction for any expense relating to facilities which are used for vacation purposes.

There will be no deduction for any expenses relating to facilities which are lavish or extravagant.

There will be no deduction for any club dues unless the club is used primarily for business purposes.

In determining whether a facility or a club is used primarily for business purposes, use of the facility by the taxpayer's family, if any, will be counted as nonbusiness use.

Under the bill, although deduction for entertainment expenses is restricted, such expenses will not be disallowed merely because they are incurred for the purpose of generating business good will.

Good will has long been recognized as a legitimate business practice. Thus where the purpose of the expenditure for good will shows a clear relationship to the business, it will and should continue to be deductible.

However, on the other hand, when good will generated by the expense is vague or when the possibility of the expenditure resulting in the production of income is remote, no deduction for this purpose would be permitted under the committee's bill.

Mr. GORE. Mr. President, will the Senator yield?

Mr. SMATHERS. I would prefer to wait until I conclude my remarks, and then I shall be happy to yield.

Mr. GORE. I was very generous in yielding to the Senator last night.

Mr. SMATHERS. The Senator was. He is always generous. I am sorry I even hesitated for a moment. I am delighted to yield to my friend.

Mr. GORE. The Senator has told us again, flatfootedly, that no vacation expense could be deductible. Does the Senator still say that?

Mr. SMATHERS. Yes. We say that certainly the language, as we wrote it, as we intend it, and as we think it would be enforced, provides that there will be no vacation deductible as a business expense.

Mr. GORE. Would that apply to travel expense?

Mr. SMATHERS. It would not apply to travel expense. People may come to Washington, D.C., to see the Senator from Tennessee. They may go to a cattle show or something. If those people are in the cattle business and they take that travel for business purposes they can take the expense as a business deduction, and they should. We are not talking about that.

Mr. GORE. Suppose a taxpayer travels to Miami for a 5-day safari on the beach.

Mr. SMATHERS. I would think he would be pretty intelligent, to start with. I wish it were possible that he could take a deduction. Of course, being objective about it, since I represent not only

Miami Beach and Florida but also indirectly the other States, I know we could not permit people to go there solely for a vacation and to deduct the expense as a business expense. If a person goes there for some business reason and can establish that, he could deduct the expense.

Under the bill which was reported and the amendment the committee approved, the person would have to prove it. No longer would the situation be the same as it has been, when the taxpayer could say, "I was there on business." He would have to prove it. If he went there on business, obviously, he would be entitled to take the travel expense as a business expense.

Mr. GORE. If the Senator will turn to page 43 of the bill, I am sure he will see what I mean. I wish to read subsection (c):

TRAVELING.—In the case of any individual who is traveling away from home in pursuit of a trade or business or in pursuit of an activity described in section 212, no deduction shall be allowed under section 162 or section 212 for that portion of the expenses of such travel otherwise allowable under such section which, under regulations prescribed by the Secretary or his delegate, is not allocable to such trade or business or to such activity.

I ask the Senator to take note of the next sentence. I am sure the Senator can perceive it:

This subsection shall not apply to the expenses of any travel away from home which does not exceed one week or where the portion of the time away from home which is not attributable to the pursuit of the taxpayer's trade or business or an activity described in section 212 is less than 25 percent of the total time away from home on such travel.

I have pointed out to the Senator another loophole, which he said was not in the bill.

Mr. SMATHERS. I say first to the able Senator from Tennessee that this particular provision, to which he has now made reference, is not one of the provisions to which he has previously objected, or to which he has objected until this very moment. This is one of the provisions now in the law, as I understand, and also in the House bill. It is one of the provision which the Senator is supporting, because he is supporting the House bill. That is the first point I wish to make.

Mr. GORE. I point out to the Senator that I have not said I am supporting the House bill. I am trying to forestall Senators from making that bill worse. What I wish to offer later are the recommendations by the President and the Secretary of the Treasury to stop the expense account cheating.

Mr. SMATHERS. We are all for that.

Mr. GORE. The amendment pending would make the House bill worse.

Mr. SMATHERS. We want to stop any cheating, too. I will ask the Senator a question. Is the Senator against all deductions for business expense?

Mr. GORE. Of course not.

Mr. SMATHERS. I am glad to hear the Senator say that.

Mr. GORE. Why does the Senator ask such a question?

Mr. SMATHERS. Because it has been my impression, after listening to the Senator for the last couple of days, that he finally had arrived at the position of wishing to allow no expenses as business deductions, legitimate as well as illegitimate. The Senator says that is not the case.

Mr. GORE. It is not.

Mr. SMATHERS. I am happy to hear him say that.

Mr. LONG of Louisiana. Mr. President, will the Senator yield?

Mr. SMATHERS. I am happy to yield.

Mr. LONG of Louisiana. Was not the Senator on the floor when the Senator from Pennsylvania, who is associated with the Senator from Tennessee in this effort, made clear that he wants to cut out all allowances for any entertainment expense whatever.

Mr. GORE. I want to support the President's recommendations, to eliminate the tax deductions for entertainment. That is one way to stop the abuse. The House did not go that far, but the House did a fairly good job, and the Senate committee amendment would wreck the House bill and permit many of the abuses which now exist.

Mr. SMATHERS. I think the Senator now is making clear what we have suspected all along. The Senator from Tennessee does not think that even the House bill is strong enough.

Mr. GORE. Of course not.

Mr. SMATHERS. Neither does the Senator from Pennsylvania.

Mr. GORE. Neither does President Kennedy.

Mr. SMATHERS. The Senator's colleague from Pennsylvania apparently would go so far as to eliminate all business expense deductions. I do not say that with reference to the Senator from Tennessee.

Mr. GORE. If the Senator means he thinks he would like to eliminate tax deductions for entertainment, he is correct. If the Senator means he thinks I would like to eliminate all business deductions, for attending business conventions, for making business trips, for expenses in the pursuit of business, then he is utterly wrong. I cannot conceive by what reason he could have arrived at such a conclusion.

Mr. SMATHERS. Only by what the Senator says. That was the only reason.

Mr. GORE. I have said nothing which would justify such a conclusion.

Mr. LONG of Louisiana. Mr. President, will the Senator yield?

Mr. SMATHERS. I am happy to yield.

Mr. LONG of Louisiana. Does not the Senator recognize that the President has said just about what the Senator from Tennessee is saying; that he understands there is some need for business entertainment, but there have been abuses, so one way to be sure that there is no abuse is to eliminate it all, to cut it all out?

Mr. SMATHERS. It would be much easier that way.

Mr. GORE. But the Senator from Louisiana does not want to cut any of it out.

Mr. LONG of Louisiana. The Senator yielded to me.

Once again what we see is that the program of those who oppose the committee amendment is the program of burning the whole barn down. They are not satisfied with what the House did. They feel that the only way to be sure the rats are out of the barn is to burn down the barn, and then they will know there are no rats in the barn.

Mr. SMATHERS. The Senator is correct.

Mr. LONG of Louisiana. The President recognized that there was a legitimate basis for entertainment expenses, directly related to or associated with the taxpayer's business. But the President recommends that we ought to tell a businessman he cannot entertain, even though the President recognizes, more than anybody else, that our ambassadors have to entertain, and wants the Congress to provide money for it—millions and millions of dollars. Our friend from Tennessee has been voting for that kind of expense, with the money provided by the taxpayers. It is not merely a deduction, but it is an appropriation of money so that our ambassadors can entertain at our expense.

Mr. SMATHERS. Overseas.

Mr. LONG of Louisiana. Yes, overseas. This is entertainment of foreigners at our expense, though some do not wish to permit businessmen to entertain Americans at their own expense and to deduct it as a legitimate expense of doing business.

Mr. SMATHERS. I thank the Senator from Louisiana. I agree with him completely.

Mr. President, these new rules will strengthen existing law and will prevent abuses of the deduction privilege.

No longer will a taxpayer be able to claim deduction for such unrelated expenses as costs of his daughter's social debut or of her wedding reception, about which we have heard a great deal and no doubt will hear a great deal more. We have tried to eliminate all that sort of thing.

No longer will he be able to purchase a yacht, fishing camp or hunting lodge and simply charge its cost off as a deductible expense on the flimsy excuse, "It's for business."

No longer will lush facilities on tropical island paradises to which favored customers and their families may be sent for long winter vacations be deductible.

These are all improvements over the existing law. I cannot emphasize too strongly that existing law is to be modified by this bill only in one direction, and that is that it is to be made tighter.

If an expense is not deductible under existing law, it will never become deductible under this bill. On the other hand, if it is deductible under existing law, this bill will come into operation and may disallow all or a part of the claimed amount.

Mr. President, I repeat that statement. If an expense is not deductible under existing law it will never become deductible under this bill. On the other hand, if it is deductible under existing law, this bill will come into operation and may disallow all or a part of the amount which has been claimed as a business deduction.

The bill not only provides tighter rules for determining what business entertainment expenses may be deductible but also eases substantially the administrative difficulties of making the determination.

The bill requires the taxpayer who claims a deduction for entertainment expenses—or for travel or gift expenses—to clearly establish his right to the deduction by proof other than his own statements which may largely be self-serving. He must claim and prove the amount of the deduction. He must show the circumstances under which the entertainment occurred. He must identify the person entertained and must show the business relationship between that person and a trade or business.

By these requirements, the taxpayer must reveal to the tax collector all the information he needs to make a determination with respect to any claimed entertainment expense.

If the taxpayer fails to establish his proof, then there will be no deduction allowed.

Existing law which permits a partial deduction, even in the absence of substantiating evidence, is overruled by this bill. This eliminates one of the most flagrant abuses of existing law; that is, the fraudulent practice of claiming deduction for more expenses than were actually incurred and maintaining no records. In these cases the taxpayer knows that he will be allowed some deduction and the more he claims the more he will be allowed. The committee bill says that in such cases there will be no deduction whatsoever.

Now let me illustrate the type of entertainment expenses which will be allowed as a deduction under the committee amendment, but which were considered to be "high living" under the House bill. I quote from the committee report:

Where the taxpayer conducts lengthy negotiations with a group of business associates and that evening the group goes to a nightclub, theater, or sporting event for relaxation, such entertainment expenses are regarded as directly related to the active conduct of business. Moreover, if a group of business associates with whom the taxpayer is conducting business meetings comes from out of town to the taxpayer's place of business to hold substantial business discussions, the entertainment of such business guests prior to the business discussions also is directly related to the conduct of the business. Similarly, if in between business meetings at a convention the taxpayer entertains his business associates attending such meetings, such expenses will be allowable.

Mr. President, I stress and emphasize that the committee bill is designed to prevent abuse. It is not designed as was the House bill, to disallow all deductions.

The committee bill would compel taxpayers to weigh carefully the advantages entertainment may bring to their business when only a portion of the entertainment expense may be deductible.

If the expense is reasonable, the purpose legitimate and the business relationship clearly established and proven, the expense, or a part of it, may be deductible.

On the other hand, those who have been "living high" on expense accounts will find that the costs of their high living have gone up and that the Ameri-

can taxpayers no longer will participate with him in paying the bill.

It is estimated that the full year revenue effect of the committee amendment will bring into the Treasury some \$85 million.

The tighter rules in this bill, while preventing abuse, should not discourage business transactions which create the profits upon which our Treasury must rely for income tax receipts.

I believe the committee amendment represents a fair, logical approach to a problem we all feel should be solved.

Mr. GORE. Mr. President, will the Senator yield?

Mr. SMATHERS. I am happy to yield to the Senator from Tennessee.

Mr. GORE. The Senator has made another statement which I challenge. He has said that the businessman must prove something. What was it the Senator said?

Mr. SMATHERS. If the Senator does not remember what I said, I do not know how he can ask me a question about it.

Mr. GORE. I remember the purport of the Senator's statement. The Senator informed the Senate a moment ago that the expense would not be deductible unless a businessman could show a clear business connection. Have I accurately quoted the Senator?

Mr. SMATHERS. The language of the bill is that the businessman must show that the expense actually has some direct relationship to or association with his business.

Mr. GORE. The Senator did not use that word a moment ago.

Mr. SMATHERS. That is the word. I have said over and over—and I repeat it to the Senator now—that that is what we are talking about.

Mr. GORE. Mr. President, will the Senator yield?

Mr. SMATHERS. I am happy to yield, but I wish to point out to the Senator that in Tennessee there is an expression among cattlemen with respect to insects called "nits." Nits get on the cows, and one must go around among the animals and pick the nits off. It is called "nit-picking."

I would appreciate if the Senator would not pick up one or two phrases or sentences in the report out of context and would instead listen to what we are saying we are trying to do. What we intend to do—and what we want to do—is to eliminate the same abuses that the Senator is talking about. He has said he does not wish to destroy the right of a businessman to take legitimate business deductions—even entertainment—in cases in which the businessman can show that the expenses have a direct relationship to or are associated with his business. That is exactly what we are trying to do.

Mr. GORE. Mr. President, will the Senator yield?

Mr. SMATHERS. I yield.

Mr. GORE. Has the Senator ever heard of the parable of the man who thought he saw a mountain but instead saw a gnat in his eyebrow?

Mr. SMATHERS. I have heard the parable.

Mr. GORE. We are talking about three seemingly innocent words. They

are not nits. Those words are, "or associated with." That is what the Senator seeks to add to the bill. He has given an interpretation of what those words mean in his report. I should like to read to the Senator how definite it is.

Mr. SMATHERS. How many times has the Senator read that statement and put it into the RECORD in the past 24 hours?

Mr. GORE. I wish to read it to the Senator.

Mr. SMATHERS. Then I must come back and read the second paragraph below it and knock all that out. So we will be back where we started from. The Senator will make a speech in a minute. He can read it then, and we will read the succeeding paragraph.

Mr. GORE. The succeeding paragraph does not eliminate the paragraph to which I referred.

Mr. SMATHERS. Language appearing on the following page does.

Mr. GORE. Oh, no.

Mr. SMATHERS. The Senator has said that he wishes to eliminate abuses. We do eliminate the abuses. We do not presume that every businessman is a crook. We do not presume that every businessman is seeking willfully and intentionally to beat the Federal Government. We believe that there are legitimate purposes on the part of legitimate businessmen. As the Senator from Louisiana has said, we have as sincere a desire to eliminate abuses as he does. But we do not want to burn down the barn, because we think the barn is valuable.

Mr. GORE. How many strawmen must the Senator set up? How many times must he burn the barn down? Let us talk about the meaning of the three words—"or associated with." That is the loophole that the committee amendment would write into the law—a loophole that would permit continued expense account abuse and provide a tax deduction for it.

Mr. SMATHERS. That is the Senator's opinion. We shall have an opportunity to vote on the question. He did not obtain support for his position in the Finance Committee. I doubt if he will obtain support for it on the floor of the Senate.

Mr. GOLDWATER. Mr. President, I compliment the Committee on Finance for the excellent work they have done on this section. There is no question that there are abuses in this field. I know that there have been abuses over the past, and no doubt they have increased over the past few years. The bill that came from the House of Representatives is very unrealistic, in that it strikes out all deductions. The distinguished Senator from Tennessee [Mr. GORE], in his enthusiasm, would amend the bill with the result that we would have the same language in the Senate bill.

Let us face the fact that it is the graduated income tax, more than anything else, which has caused these abuses. I can remember when I was in business—and these problems no doubt have multiplied since then—in order to get a man to take a higher position than he then held, it was often necessary to meet his

demands, which might take the form of an automobile, expense-free, or might include membership in a country club, or a carte blanche expense account in restaurants around the country. Such a man would not be interested in stepping out of a \$20,000 a year job into a \$30,000 a year job, in light of the increased income tax that he would have to pay, resulting in very little substantial increase in actual income.

So, much as businessmen disliked doing these things, they had to resort to deductions in order to get the people they wanted and needed.

I would suggest to the Committee on Finance, when they meet next year on the President's proposal to change the income tax laws, that the graduated income tax might be one item they could examine. However, in the meantime, in order that business might continue and not be hamstrung by the restrictive legislation which the House has suggested and by the restrictive tax laws which are now on the books, the Senate would be very wise to adopt the provision which the Senator from Florida has so ably outlined on the floor of the Senate, and allow business to proceed, even though it must operate under present tax laws.

I again compliment the committee on the fine work it has done. I recognize what the Senator from Tennessee says, that there are excessive abuses in this field. I have decried them continuously. I do not like the situation. However, that is what we are confronted with. I do not like these abuses, but there they are.

No matter how the language is written, some businessmen are going to take advantage of loopholes in the law. It does not make much difference how the law reads, as long as we have on the books the graduated income tax, these loopholes will be taken advantage of—loopholes through which people will be able to crawl.

I again compliment the Senator from Florida.

Mr. GORE. Mr. President, will the Senator from Florida yield so that I may ask a question of the Senator from Arizona?

Mr. SMATHERS. I yield.

Mr. GORE. The Senator from Arizona has said that the House bill would eliminate all deductions for entertainment and business expenses.

Mr. GOLDWATER. I said it was highly restrictive.

Mr. GORE. The Senator used the word "all." However, to clarify the RECORD, if the Senator will refer to page 45 of the bill and turn to page 36 of the report, he will find that nine specific exceptions are made to the general rule on disallowances. He will find that in both the House bill and in the Senate bill deductions are possible for business meetings, food and beverages for employees, expenses treated as compensation. We turn now to page 46, where we find reimbursed expenses, recreational, et cetera; expenses for employees, and so forth. I shall not read all of them. There are nine exceptions which are contained in both the House bill and in the Senate bill.

It is not about those legitimate deductions for legitimate business purposes that I complain. I complain about the addition of these three little words "or associated with" in the Senate bill, and the interpretation and the legislative intent given them by the committee report, which opens the door so wide as to invite abuse.

Mr. GOLDWATER. I do not agree with the Senator's interpretation of those three words. I do agree with his intent. I wish that he had a better way of getting at it. I do not agree that these three words are a door opening, as he holds them to be.

Mr. GORE. Has the Senator read and studied the majority report?

Mr. GOLDWATER. I have read it. I cannot say that I have studied it. I have had other things to do.

Mr. GORE. I suggest that the Senator, before he reaches a conclusion, study the report. It is the report which provides the legislative intent and thus the legal effect and meaning of these three little words.

Mr. GOLDWATER. I have read the report. I do not agree with the Senator from Tennessee. That is a matter of debate. I am in perfect agreement with what he is trying to do. I have said so repeatedly in the years gone by. I do not believe that the elimination of these three words will do what he hopes will be done. I am in sympathy with what the Senator is trying to do.

Mr. GORE. The Senator is not in sympathy with what I am trying to do if he holds that view.

Mr. GOLDWATER. The Senator can interpret my words in any way he wishes. I disagree with his interpretation. I repeat that I am in sympathy with what he is trying to do.

Mr. SMATHERS. Mr. President, I am grateful to the Senator from Arizona for his comment. Rather than that these three little words are opening the door, we must remember that according to the staff estimate these three little words, in addition to what else we have done, will bring \$85 million additional into the Treasury. I do not see how we can say it is a bigger loophole, when we are collecting more money.

I yield the floor.

Mr. GORE. Mr. President, will the Senator yield?

Mr. SMATHERS. I have yielded the floor.

The PRESIDING OFFICER. The question is on agreeing, en bloc, to the amendments on page 41, line 18, on page 42, line 4 and line 7.

Mr. GORE. Mr. President, I ask for the yeas and nays.

The yeas and nays were ordered.

The PRESIDING OFFICER. The yeas and nays have been ordered, and the clerk will call the roll.

Mr. GORE. Mr. President, the Senate is about to vote upon an extremely important issue.

The PRESIDING OFFICER. The Senator from Tennessee will suspend until the Senate is in order.

The Senator from Tennessee may proceed.

Mr. GORE. The Senate is about to vote upon an extremely important issue. Let no one mistake the clarity of the issue. The situation presented is one which has an interesting history. The widespread abuse of expense accounts has developed over a period of years. Many of these abuses have been contested in the courts.

The PRESIDING OFFICER. The Senate will be in order.

Mr. BUSH. Mr. President, a parliamentary inquiry.

The PRESIDING OFFICER. The Senator will state it.

Mr. BUSH. What is the question before the Senate?

The PRESIDING OFFICER. The question is on agreeing, en bloc, to the committee amendments on page 41, line 18, and on page 42, lines 4 and 7.

Mr. GORE. Many of the expense account abuses have been contested by the Government in the courts, but in many of these instances the Government has lost the cases under present law. The abuses have become so widespread that in a state of the Union message, the President of the United States called attention to the abuses in dramatic language.

The President:

The slogan "It's deductible," should pass from our scene.

The President further said:

Deductions are obtained by disguising personal expenses as business outlays.

I shall not quote the President's message further. I quote it to this extent only to illustrate that this pattern of abuse, this pattern of tax avoidance, this pattern of disguising personal expenses as business outlays, reached such proportions as to be treated in a state of the Union message by the President of the United States.

Then the Secretary of the Treasury testified before committees of the Congress and submitted scores of examples of unconscionable abuses. He recommended measures to stop such abuses, which the President said affected the country's sense of fairness. I quote one more sentence from the President's message:

This is a matter of national concern, affecting not only our public revenues, our sense of fairness, and our respect for the tax system, but our moral and business practices, as well.

What has been the response of Congress, the legislative branch of the Government, which is supposed to speak the voice of the people? The action has been slow. But finally the House of Representatives passed a bill, not dealing with this problem as vigorously and effectively as the President and the Treasury Department had requested and recommended; but the bill of the House and the House report on the bill are fairly good. The House bill does not end all the abuses I have cited. The House bill specifically provides nine exceptions to the general rule, and expenditures in accordance with those exceptions, which can be found on page 45 of the bill, are

deductible under either the House bill or the Senate committee bill.

The House report undertook to spell out its legislative intent clearly and specifically to prevent loopholes for avoidance. As I have said, I do not think—and it is not only my opinion—that the House bill dealt with this subject with sufficient vigor and effectiveness. That is my opinion not only of the terms of the bill, but of the terms of the report, as well. But that question is not now before us. Later it may be that an amendment will be offered to substitute for the House action the recommendation of the President and the Secretary of the Treasury. But that is not before the Senate now.

What is before the Senate? It is an amendment offered by the Committee on Finance, accompanied by a report of the committee specifying the interpretation and the legislative intent of that amendment. It is that amendment and that report which are the subject at issue at the moment. What is the amendment? It is to add the words "or associated with." What is the legal effect of those words, and why did the committee approve the amendment? Why is it suggested and offered to the Senate? Fortunately, we need not rely upon anyone's imagination, anyone either for or against the amendment, because the committee has submitted a report which tells us the meaning of these innocent-sounding little words.

If Senators will read briefly with me, I shall set forth the meaning. I turn to page 24 of the committee report, under the heading:

IV. Disallowance of Certain Entertainment, Etc., Expenses.

I shall not read the prefatory paragraphs but come instead to the last paragraph on page 25, where we really begin to find in the committee report the interpretation of this language:

Your committee's bill to a considerable degree retains the basic structure of the House bill.

I call the attention of the distinguished chairman of the committee to the language on the bottom of page 25 of the committee report, which is:

Your committee's bill to a considerable degree retains the basic structure of the House bill.

I shall not interrogate the chairman; I appreciate his attention. But notice that the language does not say that the committee's bill retains the meaning and effect of the House bill; it "retains the basic structure of the House bill."

What is the structure of a bill? I read further:

However, the effect of the principal provision (the disallowing of a deduction for certain entertainment expenses) has been modified.

Why did the committee modify it? We are told in the report. Senators can read why. A copy of the report is on every Senator's desk. There can be no misunderstanding of the issue upon which we are about to vote. What is the purpose of the three words? I read:

To permit the deduction of expenses for goodwill where a close association is established between the expense and the active conduct of a trade or business.

Mr. President, a little later I shall illustrate how the definition of those terms reflects an interesting meaning and an untoward meaning and effect.

Now I read—and I ask Senators to follow my reading—from page 26, beginning at the top of the page:

The report of the Committee on Ways and Means made it clear that the House bill was not designed to disallow completely deductions for entertainment, amusement, or recreation expenses, but rather it was intended to eliminate abuses.

That is correct, and I think that is what the Senate should try to do.

I read further:

Under the general rule, no deduction would be allowed for any such expenses except to the extent that such expenses are directly related to the active conduct of a trade or business.

Why should they be deductible unless they are in fact directly related to the active conduct of a trade or business?

I read further:

Despite the clear language of the House bill and the stated intent of the provision, considerable uncertainty and confusion as to the actual effect of the House draft has been created by the interpretation given this language in the House committee report. It in effect interprets the proposed statutory language to disallow a deduction for any expense for entertainment, amusement, or recreation unless the expense is described in one of a series of specific exceptions to the general rule.

Those specific exceptions are liberal and generous. Senators will find them on page 26 of the report or on page 45 of the bill—9 of them. But apparently those who prepared this majority report were not satisfied with that.

I read further:

Where the expense is covered by an exception, the rules of existing law would continue to govern the deductibility of the expense.

Mr. President, what is wrong with that? Nothing that has been set forth in the paragraph I have read about the House report describes anything harsh. Indeed, it describes a situation which I think permits liberal deductibility—more liberal than I think is justified. Nine specific exceptions are set out, and then there is the general rule.

But listen to the next paragraph of the majority report:

To eliminate the harshness—

Mr. President, what harshness? What harshness has been described in the House committee report?

Mr. BUSH. Mr. President, will the Senator from Tennessee state the page from which he is reading?

Mr. GORE. I am reading from page 26 of the report. I had completed reading the first paragraph, which describes the report of the House Ways and Means Committee; and I had just begun to read the second paragraph, which I shall now read:

To eliminate the harshness resulting from the House report, amendment of the language of the House bill is necessary. Despite amendment of the House bill your committee has made certain that entertainment expense abuses are eliminated.

But it does not state how that would be done; it does not give a definition of an abuse.

I continue to read:

By your committee's amendment an alternative rule is added to the House bill—

Now, Mr. President, we begin to get to the point. Not being satisfied with the generosity of the report of the House Ways and Means Committee, this amendment is offered in an attempt to alleviate what is alleged to be harshness; therefore an alternative is provided:

By your committee's amendment an alternative rule is added to the House bill under which expenses for entertainment, amusement, or recreation (with respect to both activities and facilities) also will be deductible to the extent that such expenses are associated with the active conduct of a trade or business.

Mr. President, here are the words "associated with," and these words are not difficult for the American people to understand. This is a simple issue. It is an issue between right and wrong. This is an issue about which much will be heard in the future.

What is the meaning of the words "associated with"? The report states that—

Expenses for entertainment, amusement, or recreation (with respect to both activities and facilities) also will be deductible to the extent that such expenses are associated with the active conduct of a trade or business. This new language will permit deduction of expenses for entertainment, amusement, or recreation incurred for the creation or maintenance of business goodwill without regard to whether a particular exception applies.

What is good will, Mr. President? How definite is that? What kind of good will? With whom? Where? How? Of what nature? But, the committee report states:

This new language—

What new language is referred to? The three little words "or associated with." What does the new language mean? We are told here:

This new language will permit deduction of expenses for entertainment, amusement, or recreation—

What kind of recreation? Athletic? Intellectual? Travel? Therapeutics? No definition is given.

What kind of amusement? What kind of entertainment? But if there is an expense for any of this purpose, however indefinite, it is deductible, if you please, Mr. President, if it is for the purpose of maintaining good will—whatever that is.

I continue to quote:

without regard to whether a particular exception applies. However, this new language will apply only if the taxpayer demonstrates a clear business purpose and shows a reasonable expectation—

What is expectation? What is a reasonable expectation? A reasonable expectation of what? of deriving some income—

How much? Where? In what manner? Under what conditions? When? Some income.

I continue to quote:
or other benefit—

What kind? Social? Financial? Political? Healthful? Cultural? Matrimonial? What benefit? Other benefit. to his business as a result of the expenditure.

Mr. President, listen to the following sentence, which refers to this rigid requirement, this language that is offered to relieve the alleged harshness.

What is the next sentence?

If he meets this test—

Test? Test.

the expenditure will be considered to be—

What?

associated with—

"Associated with"—that is the amendment. That is what is pending.

And if a taxpayer, according to this report, makes an expenditure for entertainment, recreation, or amusement, with respect to either activities or facilities, to maintain good will, from which he has some reasonable expectation, at some time, somewhere, somehow, of receiving some income, in some amount, in some manner, of some quality, or some other benefit—whatever that is—then it is considered to be "associated with" his trade or business.

Yet the Senate of the United States is asked to vote to approve this amendment with this interpretation on every Senator's desk. Ah, Mr. President, I may be endowed with more than an ordinary share of self-confidence. However that may be, I am confident that if 99 of my colleagues would give me their attention for 20 minutes, this amendment would not be adopted by the Senate.

Unfortunately, it is not my privilege to reach very many of my colleagues by speech, but the issue is joined. I have stated it clearly. The Senate is not required to rely upon my interpretation of the words "associated with." I have just read what the committee report says they mean.

The amendment would open the gate wide. It would provide for a continuation of the pattern of abuse of expense accounts and tax avoidance.

Adoption of this amendment would subvert the effort for tax reform to eliminate this pattern of abuse, avoidance, evasion, and concealment which the President of the United States thought of such proportions as to ask, in a state of the Union message, that the Congress take forthright action to eliminate it.

Mr. President, I do not wish to detain the Senate further. I have stated the issue.

Mr. KEFAUVER. Mr. President, will the Senator yield?

Mr. GORE. Before yielding, I wish to correct one statement that my distinguished colleague, the junior Senator from Florida [Mr. SMATHERS], made. He said that this amendment would increase revenue. As a matter of fact, these three little words are estimated by the Treasury to reduce revenue to the Government, as compared with the House bill, by at least \$40 million a year. Mind you, Mr. President, the Secretary

of the Treasury estimated that if those abuses were completely eliminated, the revenue to the Government would be increased by \$250 million.

I yield to my senior colleague from Tennessee.

Mr. KEFAUVER. I wish to ask my colleague, who has given this problem much study, a question about it. I know the consideration he has given to it.

I had understood that in the state of the Union message and in other messages the President expressed his feeling that the expense account loophole was one of the big gaps which ought to be closed, at least to a considerable extent, and that it was being abused. Does the Senator feel that the three words involved, instead of closing the loophole, would open the gap wider so that there would be more abuse than before, or at least so that there might be more?

Mr. GORE. I cannot say that the three words would open the gap wider than the present law. Even with the words in the bill, the bill would provide one test with respect to facilities which would be of some help. Overall, I believe that the writing of the amendment into law, along with the interpretation which accompanies it, would make the situation worse than present law, because it would give legislative endorsement to and would constitute legislative condonement of widespread abuse, the scandalous avoidance of taxes.

Mr. KEFAUVER. Did I correctly understand that the President, through the Secretary of the Treasury, has opposed the inclusion of these three words, generally on the grounds the Senator has so forcefully set forth in the Senate today?

Mr. GORE. I have read into the RECORD the message of President Kennedy. There is on the desk of each Senator a statement by the Secretary of the Treasury.

I do not have a statement by either with respect to the three words "or associated with," because those have recently been reported and recommended as an amendment by the Senate Finance Committee. Certainly the adoption of the amendment would be 180 degrees contrary to the recommendation by the President and the Secretary of the Treasury.

Mr. KEFAUVER. I think my colleague is to be commended for pointing out the further loophole the three words would make in the tax bill, which has a purpose of closing gaps and also increasing revenue to our Nation. I commend the Senator. I shall certainly vote against the inclusion of the words.

Mr. GORE. I thank my colleague.

Mr. CARROLL. Mr. President, will the Senator yield?

Mr. GORE. I yield.

Mr. CARROLL. I commend the able Senator. I have listened to his speech today. I have read his remarks on this subject. I should like to ask a question or two, if he will permit me to do so.

Mr. GORE. I yield for a question.

Mr. CARROLL. The purpose of the President's message, as I understand it, and of the action taken by the other body, is to strengthen existing law with reference to the subject matter of the Senator's remarks.

Mr. GORE. Without which, the President advised the Congress, the abuses could not be eliminated.

Mr. CARROLL. I further understand that the abuses in a sense arose out of court interpretations. It is not that the court is in favor of the abuses, but the abuses occur because of the looseness of existing law.

I read to the Senator a portion of section 162 of the 1954 Code.

There shall be allowed as a deduction all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business.

That is the wording of the law. The court decisions interpreting that wording have made it nearly impossible for the Treasury Department to draft appropriate legislation to tighten up on what some of us believe to be loopholes, inequitable and unconscionable and not satisfactory to the American public.

The President has spoken. The House of Representatives has spoken in the endeavor to change the basic law. As I understand the remarks by the able Senator from Tennessee, what he seeks to do is do no less than the House of Representatives did when it passed the tax bill some time ago.

Mr. GORE. I seek to defeat an amendment which would wreck the House bill.

Mr. CARROLL. That was my understanding. The House bill really would tighten up the law?

Mr. GORE. To a commendable degree. Not as much as I would prefer, but to a commendable degree.

Mr. CARROLL. Do I correctly understand that if we accept the committee amendment, in a sense it would pull the rug out from under that which the House has done?

Mr. GORE. It would wreck the bill so far as correcting expense account abuses is concerned.

Mr. CARROLL. I intend to support the position taken by the able Senator from Tennessee. I am confident other Members of this body who understand the issue will do the same. I join the Senator in saying that if all Senators have a clear comprehension of this issue, they will want to go on record as trying to stop what I consider to be abuses as a result of enormous loopholes in the tax law, which give great benefit and, as I was going to say, comfort to people who would have no right to these sorts of deductions under a fair and equitable tax code.

Mr. GORE. I thank the Senator.

Mr. CARROLL. I thank the able Senator from Tennessee.

Mr. PROXMIRE. Mr. President, will the Senator yield?

Mr. GORE. I yield.

Mr. PROXMIRE. Is it not true that the position taken by the President of the United States in the state of the Union message was for the elimination of the deduction for entertainment expenses and club dues?

Mr. GORE. Completely. That is not the question now before the Senate, though I would like to see it done.

Mr. PROXMIRE. I understand that. Is it not true, therefore, that it is perfectly obvious the administration posi-

tion, as described by the President in his state of the Union message, is in support of the position of the Senator from Tennessee in opposition to the committee amendment, in view of the fact that the committee amendment would open up this abuse which the President so clearly described in his message?

Mr. GORE. That is correct.

Mr. PROXMIRE. So it is very hard for anyone by any logic to conclude anything other than that the position of the administration is in support of the position so ably, eloquently, and brilliantly taken by the Senator from Tennessee.

Mr. GORE. Well, I concur in the Senator's reference to the administration's position. I must demur from concurring in the Senator's generous remarks with respect to me.

I thank the Senator.

Mr. MORTON. Mr. President, I submit an amendment to the pending bill and ask that it may be printed and lie on the table. I shall speak with respect to it tomorrow.

The PRESIDING OFFICER. The amendment will be received and printed, and will lie on the table.

JAILING OF MINISTERS IN ALBANY, GA.

Mr. JAVITS. Mr. President, I am anxious to allow the Senate to vote, and I shall not detain the Senate, but I have something on my mind which concerns me and which I think ought to concern the country very much. It is the report which appears in this morning's press, which is of course verified, that 75 ministers of religion have been jailed in Albany, Ga. Fourteen pastors, Mr. President, are religious leaders from my own State of New York.

Mr. President, where are we living? I think that is the question which all Americans must answer. Where are we living?

This is not a matter of building a street or a road, or of putting in a sewer, which are local matters. We all understand that.

This is a matter of the Constitution of the United States and the freedom of any American citizen to go into any town or city in the United States and to get the benefit of protection there as a citizen of the United States. That is what this "United States" is all about.

If we are outsiders in Albany, Ga., then everyone in Albany, Ga., is an outsider in New York City, Chicago, and Los Angeles. That may be very uncomfortable. We could dismember our country upon that theory. Yet that is the theory on which the United States apparently, without enough of a vocal protest to make itself heard in Albany, Ga., is allowed to operate.

The situation has become intolerable and beyond anyone's endurance when 75 ministers of religion are arrested on a new theory of defeating the effort to break segregation in Albany, Ga., through mass arrests, which is yet to be passed upon by the courts. I do not think there is any question that it ought to be enjoined as running counter to the Constitution of the United States; nonetheless, it is one thing to be in court and

another thing to have the Nation express its conscience. That is what is needed now.

There could be no more eloquent speech of protest against this un-American and inhuman performance than a news report of the bare facts. I beg the Senate's indulgence while I read from the New York Times, a very reliable newspaper, merely the bare facts, nothing else, not embellished in any way:

Chief of Police Laurie Pritchett charged the demonstrators with congregating on the sidewalk, disorderly conduct, and failing to obey his commands to disperse. They were held in lieu of \$200 cash bonds each and jailed here and in nearby Leesburg.

The story continues:

This afternoon—

Which was yesterday, the 28th—they—

Meaning these clergymen and lay religious leaders—

marched by twos to the city hall, where Chief Pritchett and 20 patrolmen were waiting.

The demonstrators stood for a while in silence. One policeman remarked to another, "Is everybody bashful? Ain't nobody gonna say nothing?"

Then the Reverend Norman C. Eddy of East Harlem Protestant Parish in New York asked the Reverend John W. P. Collier of Israel Memorial A.M.E. Church in Newark, N.J., to read from the Scriptures.

"WHATSOEVER A MAN SOWETH"

Mr. Collier chose from the Sixth Chapter of Galatians: "For whatsoever a man soweth, that he shall also reap."

As he finished, Chief Pritchett stepped forward and said, "All right, Reverends, what's your purpose?"

After he had repeated the question several times, Mr. Eddy replied, "our purpose is to offer our prayers to God."

The chief then urged them to return home "in the name of decency."

Mr. President, is that ironic—in the name of decency, to stop appearing.

The article continues:

Rabbi Richard Israel of the Hillel Foundation at Yale University then stepped forward and read the 114th Psalm from "Prayers for Special Occasions."

He completed the psalm. Chief Pritchett moved forward and said, "Again, I'm asking you to disperse. This is the last and only time that this command will be given."

The group stood fast.

"All right," said the chief, "put them in jail."

The demonstrators were herded into a side door of the building in twos and threes and relieved of their Bibles and other possessions.

The story goes on—

After most of those arrested had been booked, a policeman emerged from the jail wearing a false beard and a skullcap that belonged to Rabbi Israel, and paraded through the first floor offices of the city hall.

Mr. President, consider such a shameful performance in any city or town in the United States of America as the one I have read. I ask all Senators who expressed such high indignation against the Supreme Court's decision on prayer in the public schools to consult their conscience on that one. Where are their voices now? Are they aroused over the fact that ministers of religion are treated like common criminals? Why?

Because they dared to stand upon a street, pray, and invoke the blessing of the Deity so that, in their view, even if they are wrong, American citizens may have their fundamental rights.

As a Senator of the United States and a representative of 17 million people, I say that such a situation is absolutely outrageous and disgusting. If our Government does not assert its majesty to put a stop to things like that, very serious doubt will be raised as to the effectiveness and power of the National Government to protect the rights of citizens under the Constitution of the United States anywhere in our country.

Mr. President, the description sounds to me like that of a whisky rebellion. That is how serious I think it is. As the story points out, it is becoming so shameful as to be intolerable in the eyes of all the people of our country. Indeed, I can hardly understand how the Governor of Georgia and the local authorities can themselves endure that kind of performance.

Mr. President, endemic in it, and at the bottom of it, is the fact that the Congress has never given the necessary power to the Attorney General of the United States to start suit in any of those cases. He is sitting around in court waiting to file briefs *amicus curiae*, not knowing whether the court will or will not allow him to do so, since he has no authority and no power, apparently, to go into court himself and even start a suit in a Federal court in order to deal with a situation which, in my opinion, is making the United States not only look ridiculous in the eyes of the world but look unjust and apparently unable to protect the very basic and fundamental rights of its own citizens—in this case ministers of religion—who are doing what? Seeking to pray upon a public street.

Mr. President, it seems to me that in most cities of our country prayer would be encouraged. There are prayer meetings in many cities. An effort is made to use the streets exactly for that purpose—to encourage the practice of religion among the population. In Albany, Ga., people are being jailed because they have the temerity to do it, though they are ministers of religion.

It seems to me that we do not have to embellish the situation. We only need to read the report. That is more than adequate to demonstrate a situation which, in my view, is becoming intolerable in the eyes of the country and under our Constitution.

Mr. RUSSELL. Mr. President, I just entered the Chamber. I did not hear all the remarks of the Senator from New York. However, I did hear his concluding remarks. I assume that he was engaged in one of his typical political forays into the State of Georgia from the floor of the Senate.

Someone told me that in this morning's issue of the New York Times there was an announcement that some Negro assemblywoman in New York who had been a Democrat, abandoned that party and organized headquarters for the Senator from New York in his bid for reelection. I am sure there is no connec-

tion whatever between that announcement and the position of the Senator on the floor of the Senate. I notice that he becomes more and more vehement as we approach November in his denunciation of a situation about which he knows nothing and cares only for the political mileage that might be involved.

It is very easy to denounce people in another section of our country. No one more deeply regrets or has suffered more anguish from the unfortunate events that are occurring in Albany, Ga., than have the people of that community. There is not a better city or a higher class of citizenry to be found anywhere in the United States than in the little city of Albany, Ga. It is one town in which there was never the slightest restriction on the right of colored citizens to go to the polls to vote. It is one town in which colored citizens have operated businesses and accumulated money. Considering some of the other cities in which such a campaign might have been launched to force the policemen of the city to take action, I cannot understand why Albany, Ga., was selected. I have never been able to understand that. But it was. The people there are confronted with this fact and with a very serious condition.

When the President of the United States made his remarks concerning Albany at his press conference, I said that it was unfortunate that he had undertaken to intervene in the situation there, because such intervention would cause many publicity seekers and sensationalists all over the United States to move into Albany.

I do not say that every one of the latest adventurers, or even most of them, are from New York. I do not know whether they are members of the club that has been organized by the Negro assemblywoman for the political benefit of the Senator from New York or not. I assume that perhaps most of them are. But I do not say that every one of them, without exception, would fall into that category. Most all of them are the type of people who have experienced frustrations of one kind or another, who have never seen their names in the press except to read that the Reverend Joe Doaks married this couple or the Reverend Joe Doaks conducted the last exercise at the cemetery.

They went to Albany, Ga., and violated the ordinances of that city. If they had done it, under the same circumstances, in New York City, they would have been arrested. The chief of police asked them four times to move and stop blocking traffic. They did not do so.

The amazing thing to me, Mr. President, is that when we approach election time, those who have shouted from the housetops that these disputes should be settled in the courts and left to the courts for decision, now take a different attitude, and now say that any means justifies the end, and that they will violate any and all laws with which they do not agree.

These people were asked four times to stop blocking traffic and to move on. They refused to do so. They came there

to be arrested, and they were arrested. From what I know of the incident I say they should have been arrested. According to press reports, the Senator from New York has sent a telegram to Albany saying that he would be very glad to go down there.

I can understand his position. I can tell the Senator, that if he does go to Albany, Ga., he will be safe. He will be able to walk on the streets of that city, in any section of it, in the daytime or at night, without any fear of violence being committed upon his person.

I dare say the distinguished Senator from New York would not dare to venture into Central Park in New York City after midnight unless he had a large police escort with him. He would not dare go on West 94th Street in New York City after nightfall unless he had a large police escort to protect him.

I feel that I owe some obligation to say a word in behalf of the honest, God-fearing people who have been generous to me in times past, and who are the peers of any people represented by the Senator from New York or by any other Member of the Senate.

About a week ago I saw a picture in a New York newspaper showing five or six policemen, wearing steel helmets, crouching and trying to get behind an automobile to avoid the crockery, bricks, and other materials that were being showered upon them from the upstairs floors of a building. Nothing like that occurs in Albany, Ga. When people come down there, even if they happen to be sent there by a New York Senator or anyone else, to try to create a situation of lawless chaos, the police department of that city does its duty and arrests them. But it protects them from any violence.

Therefore, I say the Senator would be much safer in carrying on his campaign by going to Albany, Ga. I again assure him that he could walk the streets of that town day or night, and he would be protected; no one would harm him. On the other hand, there are areas in New York City where he would not dare to go out after dark, because he knows he would be mugged and his life placed in peril.

I realize, of course, it is regrettable that three influential metropolitan newspapers are able to call the tune for the other media of communications in this land. I realize that they distort headlines, to influence fairminded men who do not live in the areas where these incidents take place. The press has tried to use the incidents at Albany, Ga., to heap calumny on a people who deserve better treatment.

I notice that the distinguished Senator from New York does not comment on any of the serious racial incidents that have taken place in New York City. It may be that the white people there have been completely cowed.

I have not heard him raise his voice against incidents which have very recently occurred at Cairo, Ill., where a number of members of the Negro race apparently tried to go to a public place, to which objection was made. I believe they tried to go into a skating rink, or

oceanographic and related environmental data, including, but not limited to, physical, geological, biological, fisheries, hydrographic and coastal survey, meteorological, climatological, and geophysical data.

And to amend the title so as to read: "An Act to provide for a comprehensive, long-range, and coordinated national program in oceanography, and for other purposes."

Mr. MAGNUSON. Mr. President, I move that the Senate disagree to the amendments of the House of Representatives, request a conference thereon with the House of Representatives, and that the Chair appoint the conferees on the part of the Senate.

The motion was agreed to; and the Presiding Officer appointed Mr. SMATHERS, Mr. ENGLE, Mr. BARTLETT, Mr. BUTLER, and Mr. KEATING conferees on the part of the Senate.

MESSAGE FROM THE HOUSE

A message from the House of Representatives, by Mr. Bartlett, one of its reading clerks, announced that the House had agreed to the amendments of the Senate to the bill (H.R. 7278) to amend the act of June 5, 1952, so as to remove certain restrictions on the real property conveyed to the territory of Hawaii by the United States under authority of such act.

ENROLLED BILLS SIGNED

The message also announced that the Speaker had affixed his signature to the following enrolled bills, and they were signed by the President pro tempore:

S. 3327. An act to make eligible for assistance under the public facility loan program certain areas where research or development installations of the National Aeronautics and Space Administration are located;

H.R. 1388. An act for the relief of Tai Ja Lim;

H.R. 5532. An act to amend chapter 137, of title 10, United States Code, relating to procurement; and

H.R. 10743. An act to amend title 38, United States Code, to provide increases in rates of disability compensation, and for other purposes.

REVENUE ACT OF 1962

The Senate resumed the consideration of the bill (H.R. 10650) to amend the Internal Revenue Code of 1954 to provide a credit for investment in certain depreciable property, to eliminate certain defects and inequities, and for other purposes.

Mr. MANSFIELD. Mr. President, what is the pending business?

The PRESIDING OFFICER (Mr. HICKEY in the chair). The question is on agreeing to the committee amendment in section 4, on page 41, line 18, after the word "to", to insert "or associated with"; on page 42, line 4, after the word "to", to insert "or associated with"; in line 7, after the word "to", to insert "or associated with".

The yeas and nays have been ordered on the amendment.

Mr. KERR. Mr. President, I ask unanimous consent that the rollcall, under the yeas and nays ordered on the amendment, start in 7 minutes.

The PRESIDING OFFICER. Is there objection?

Mr. GORE. Mr. President, reserving the right to object—

The PRESIDING OFFICER. Objection is heard by the Senator from Tennessee.

Mr. GORE. Mr. President, reserving the right to object, will the Senator reserve to me, in case I desire to use them, 2 minutes?

Mr. KERR. Mr. President, I make a unanimous-consent request that the vote on the amendment start in 9 minutes, the last 2 of which will be assigned to the Senator from Tennessee [Mr. GORE].

The PRESIDING OFFICER. Is there objection? Without objection, it is so ordered.

Mr. KERR. Mr. President, the motion before the Senate is to insert on pages 41 and 42 the words "or associated with" in three places. Those words were inserted in the House bill by the Senate Finance Committee for a very specific purpose. On page 41 of the bill, beginning in the statement concerning section 274, "Disallowance of Certain Entertainment, Etc., Expenses" are these words:

No deduction otherwise allowable under this chapter shall be allowed for any item * * *

With respect to an activity which is of a type generally considered to constitute entertainment, amusement, or recreation, unless the taxpayer establishes that the item was directly related to the active conduct of the taxpayer's trade or business.

A little further over in the section, beginning on page 45, is a list of specific exceptions to the application of subsection (a), which I have just read, and those specific exceptions cover most of page 45, page 46, page 47, and down to and through line 6 on page 48.

The House report makes an absolute nullity of the language on page 41, which is a general statement of the activities generally considered to constitute entertainment, amusement, or recreation directly related to the active conduct of the taxpayer's trade or business.

The House report is so strict that it makes a nullity of that part of the bill.

As the Secretary of the Treasury told our committee, he could not think of anything that could be deductible under these conditions other than those things listed in the bill on the pages I have referred to as specific exceptions to the application of the subsection.

The Senator from Tennessee told us a little while ago that the Senate is asked to approve this amendment, which is the insertion of the words "or associated with," and that by so doing we would approve the language in the report.

The choice actually is between the language of the two reports.

The Senator from Oklahoma asked the Treasury Department to provide some words which could be inserted in the bill without changing the meaning

of it, so that the strict report on the House bill would be in conference. These were the three words which were provided.

In the writing of the report by the staff of the Senate Finance Committee, it is the opinion of the Senator from Oklahoma that they went too far, but it is also the opinion of the Senator from Oklahoma that the language in the House report does not go far enough.

Therefore, Mr. President, if the language is approved, the subject will be in conference. If the language proposed by the Senate committee is disapproved, then, according to the statement of the Senator from Tennessee [Mr. GORE], we would thereby approve the language of the House bill, in accord with a House committee's very strict report.

I am sure that if Senators would read that report, they would not wish to approve it. Therefore, I urge the Senate not to disagree to the committee amendments, for the very simple reason that the only way we can take to conference a provision which will permit us to agree on a middle ground, between the report of the House committee and the report of the Senate committee, is to keep these three words in the bill and to arrive at an adjustment in conference.

In reality there is no difference, when we note that the item either was directly related to the active conduct of the taxpayer's trade or business or was associated with the active conduct of the taxpayer's trade or business. The meaning of the language is almost identical. The difference is in the two reports.

I assure the Senate that the difference can be adjusted in conference, provided the amendment of the committee is agreed to; and I urge that that be done.

I ask unanimous consent to have printed in the RECORD at this point a statement in respect to this question.

There being no objection, the statement was ordered to be printed in the RECORD, as follows:

The original recommendations of the Treasury included the following:

1. Disallowance in full of expenses for business entertainment, such as expenditures for entertaining guests at nightclubs, theaters, country clubs, prizefights, and on hunting and fishing trips.

2. Disallowance of expenditures attributable to a yacht, hunting lodge, fishing camp, resort property, or other facility of a type generally used for pleasure, recreation, entertainment, etc., if primarily used for such purposes. Deduction for company cafeterias and dining rooms on the business premises would not be disallowed. Expenditures for automobiles, airplanes, apartments, and hotel suites would be disallowed to the extent used for pleasure, recreation, entertainment, etc.

3. Disallowance of cost of gifts except where annual cost per recipient does not exceed \$10.

4. Disallowance in full of dues or fees of social, athletic, and sporting clubs.

5. Disallowance of expenditures for food and beverages except expenditures for food and beverages furnished to employees on the business premises, expenditures for food and beverages furnished as part of business meetings (but limited to \$4 to \$7 per day per individual), and expenditures for food and beverages included in travel.

6. Disallowance of expenditures for transportation, meals, and lodging attributable to traveling away from home except for cost of transportation allocable to the business and except for cost of meals and lodging not in excess of \$32 per day.

The Treasury estimated that these recommendations would increase revenues by at least \$250 million per year.

This reflects the disallowance of some \$625 million of expenditures.

On this basis, the Senate Finance Committee provision, which would increase revenues by \$85 million, involves the disallowance of some \$210 million of expenditures on business travel, gifts, and entertainment.

Mr. JAVITS. Mr. President, will the Senator yield?

Mr. KERR. Mr. President, how much time remains?

The PRESIDING OFFICER. One and one-half minutes.

Mr. KERR. They belong to the Senator from Tennessee.

The PRESIDING OFFICER. That is the share remaining to the Senator from Oklahoma.

Mr. KERR. Then I yield to the Senator from New York.

Mr. JAVITS. I merely wish to tell the Senator that I have inventoried this question with the Committee on Federal Taxation of the New York State Society of Certified Public Accountants. Their analysis of existing law would, in my view, sustain the Senator's position. I intend to vote that way. If the Senator will allow me, I should like to ask unanimous consent to include my exchange of correspondence in the RECORD.

Mr. KERR. Mr. President, I thank the Senator from New York for his observations, and I make that request.

There being no objection, the correspondence was ordered to be printed in the RECORD, as follows:

JULY 25, 1960.

GENTLEMEN: During the Senate consideration of the Public Debt and Tax Rate Extension Act of 1960, an amendment was adopted which would have prohibited the deduction for tax purposes of most business entertainment expenses. This amendment was stricken out in the conference between the two Houses and there was substituted for it a new section calling for studies by the Joint Committee on Internal Revenue Taxation and the Internal Revenue Service relating to this problem.

During the debate on this provision, I stated to Senator JOSEPH CLARK of Pennsylvania, the sponsor of the original amendment, that I would ask a number of leading public accounting firms in New York about this question, which has become a matter of major concern—it is claimed to be a multimillion-dollar tax loophole. My particular interest lies in the determination of a fair and equitable way of dealing legislatively and administratively with the ordinary deduction as necessary business expense of entertainment, gifts, dues, or initiation fees in nonprofessional organizations and similar items in order to avoid excesses and abuse.

In view of the respected position of your committee in the public accounting field, I would very much appreciate having your views and suggestions on this important economic issue.

Best wishes.

Sincerely,

JACOB K. JAVITS,
U.S. Senator.

OCTOBER 11, 1960.

DEAR SENATOR JAVITS: This is in answer to your letter of July 25, 1960, addressed to the Committee on Federal Taxation of the New York State Society of Certified Public Accountants, dealing with the deduction for tax purposes of business expenses for entertainment, gifts, dues, or initiation fees in nonprofessional organizations and similar items (all of which are, for purposes of brevity, hereinafter referred to as entertainment expenses). We regret very much our delay in answering, which was attributable to the time required to coordinate the views of our committee on this important question.

In considering the problem of entertainment expenses, one basic concept must be kept clearly in mind. There is no specific provision in the Internal Revenue Code dealing with entertainment expenses beyond that applicable to other business expenses. Such expenses are presently deductible under section 162 of the Code which allows "as a deduction all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business." Therefore, under the statute as it exists, only those entertainment expenses which are ordinary and necessary in a taxpayer's business may be deducted. It should also be noted that, in litigated cases, the courts have, generally speaking, applied this principal stringently. They have required the taxpayer to prove that the expenses were incurred, and that such expenses were necessary in the business and had a proximate relationship to the production of income. The portion of particular entertainment expenses applicable to the taxpayer personally has been disallowed.

Where deductions have been based on estimates of expenses, even though of a type which is difficult or impossible to prove exactly, only small portions have been allowed. A case such as the famous African safari deduction which has received so much publicity simply does not represent the treatment generally given by the courts in this area. Incidentally, in fairness to the Tax Court judge who decided that case, an objective scrutiny of the facts indicates that it was a borderline situation. The Internal Revenue Service has acquiesced in the decision but narrowly limited its application.

It is clear, then, that entertainment expenses are deductible only if they meet the same ordinary and necessary tests which apply to all business deductions. If any such expenses are deducted which do not meet the tests, but are nevertheless not detected by the Internal Revenue Service, we do not believe it is proper to state that a "tax loophole" exists. The problem in such a case is not to be found in the law, but in its enforcement. The same comment can be applied to many other provisions of the Code which are difficult to enforce, such as the deduction for dependents and the taxability of dividends and interest on bank accounts and other sources.

Since the same legislative and judicial tests apply to entertainment expenses as to other business deductions, any legislative limit on the deductibility of such expenses should have some justification. It is not enough to say that a loophole exists. If tax avoidance exists in this area, it is because of the difficulty of enforcement and not because of the statute itself, and such enforcement difficulties are equally applicable to many other tax provisions. It is true that expenses which are contrary to law are not deductible. But other expenses, such as kickbacks by opticians to doctors and administrative expenses of illegal businesses have been held to be deductible by the courts. If an entertainment expense is contrary to law, such as the purchase of liquor in a dry State, it is not deductible under the so-called public policy rule.

It is probable that some elements of what, for want of a better term, we will call public morality has influenced thinking in this area. It is not difficult to be incensed at the thought of a group of businessmen being entertained at a nightclub or taken to the Kentucky Derby on tax-deductible expense accounts. But once again, we submit that the matter is one of enforcement and not a "loophole" in the law itself.

It has been our experience that the large majority of entertainment expense situations which are properly looked on as abuses do not meet the ordinary and necessary tests and should be, and very often are, disallowed on examination.

On the other hand, a great many taxpayers incur perfectly legitimate entertainment expenses which are completely in keeping with ethical standards and are both required by business needs and are modest in proportion to the business involved. We sincerely believe that it would be unfair and unjustified to change the law to the detriment of these taxpayers because of the publicity given to abuses in claiming deductions which are improper under current law. You should be interested in knowing that excessive deductions in this regard by closely held corporations are not only disallowed to the corporation but also taxed to the individual accountable for the expenditures. This double impost, frequently as much and more than 100 percent in total, acts as a substantial deterrent.

In summary, we believe that the present law does not require change. As already interpreted by the courts, it gives the Internal Revenue Service adequate weapons with which to combat excesses and abuses. Any additional statutory limitation would operate unfairly against entertainment expenses which meet the statutory requirements. It would apply tests different from those applicable to all other types of business expenses.

It would be helpful for us to comment briefly on the administrative problems and practices affecting entertainment expenses. There is no doubt that the proper enforcement of the law as we have outlined it creates a great deal of work for the Internal Revenue Service. In addition to the detection of abuses, there are many honest differences of opinion between revenue agents and taxpayers or their representatives as to whether an expense is "ordinary and necessary." The Service's job would, therefore, be made much simpler if the deductibility of entertainment expenses was limited or eliminated completely. Of course, the same statement can be made of all of the other deductions permitted by the Internal Revenue Code. Thus, the necessity of checking on dependent and charitable contribution deductions also imposes a burden on the Service. Nevertheless, if the present statute is proper, as we think it is, the administrative burdens flowing from it are another inevitable function of government in this complicated society of ours. Similar illustrations abound in the tax field. The excess profits tax, for example, was certainly as complicated and burdensome on administrative officials as any other revenue statute we can imagine, yet it was used in both World War II and the Korean war.

As a second example, the entire concept of long-term capital gains is probably responsible for more serious tax litigation than any other problem area, yet it is not contemplated that capital gain taxation be eliminated.

As a matter of actual practice, we know that the Internal Revenue Service is well aware of the abuses in the entertainment expense area, and is constantly striving to make its audit procedures as effective and as far reaching as possible. For the past

couple of years, questions about reimbursed expenses have appeared on individual income tax returns, and 1960 tax returns will solicit additional information from employers. On the audit level, revenue agents are constantly being pressed to analyze and seek substantiation of entertainment expense deductions, even to the point where taxpayers with legitimate deductions may consider themselves as being overly harassed. As accountants dealing with this problem continuously, we assure you that the steps being taken by the Service are getting and will continue to get results. Furthermore, by words and action, the Service has indicated that it will continue to improve its practices and procedures until it has eliminated abuses in the deduction of entertainment expenses.

For all of the above reasons, we are of the opinion that the present statute is satisfactory and need not be changed to deal specifically with entertainment expenses, and that the administration of the statute by the Internal Revenue Service is good and getting better all the time.

We appreciate your inviting our views and hope they are of some help to you. If we can be of any further assistance to you in this matter, please do not hesitate to call on us.

Very sincerely,

COMMITTEE ON FEDERAL
TAXATION.
ARTHUR DIXON.

OCTOBER 28, 1960.

DEAR MR. DIXON: Thank you for your letter of October 11, 1960, expressing the views of the Committee on Federal Taxation of the New York State Society of Certified Public Accountants with respect to entertainment and gift deductions.

I have read your comments most carefully, and you may be sure that I appreciate the careful study and consideration that went into them. I believe that the accounting profession is performing an important public service in its continued concern with problems such as these, and I assure you that I too shall continue to follow most carefully the progress of the Internal Revenue Service's enforcement policy.

Best wishes.

Sincerely,

JACOB K. JAVITS,
U.S. Senator.

Mr. KERR. Mr. President, I yield the floor.

Mr. GORE. Mr. President, this is a remarkable situation. Neither the chairman of the Finance Committee, the distinguished senior Senator from Virginia [Mr. BYRD], nor the Senator in charge of consideration of the bill, the ranking majority member of the committee, the distinguished senior Senator from Oklahoma [Mr. KERR] has defended the committee report, which gives the legislative intent—the committee's intent—and, therefore, legal effect to the pending amendment. Indeed, the senior Senator from Oklahoma has told the Senate that the Senate committee report goes too far.

That does not resolve the issue. The report is on the desk of each Senator. It gives the meaning of the words "or associated with". This is what we shall vote upon. We are asked to vote to approve the language, and to leave it to the tender mercies of the conference committee to do something, of which we are not sure.

That does not resolve the issue. Senators must vote, when the roll is called, upon the pending amendment with the

meaning given to it by the report which is on the desk of each Senator.

Mr. President, the issue is serious. It goes to the heart of the question of whether we wish to move toward the correction of widespread abuses of expense accounts or whether we wish to permit them to continue.

Mr. MILLER. Mr. President, I rise in support of the committee amendment, which adds the phrase "or associated with" to the phrase "directly related to" in describing the kind of entertainment, amusement, or recreation expenses that are deductible. To delete this phrase, as the opponent would do, leaving the deductibility of such expenses governed solely by the test of whether or not they are "directly related to" the trade or business would be far too harsh and would be unnecessary in light of the present state of the tax law.

It is readily apparent to anyone who has had experience in business that there are types of expenses for entertainment, for example, which have no direct relationship to making a sale or obtaining a contract or effecting a transaction, but which have a powerful effect on promotion of good will and obtaining of business out of which additional income will be derived on which taxes will be paid. For example, I know of one small businessman who annually gives a Christmas party for the children of poor families in his community. The good will that this has generated among the people of the community has had a beneficial effect on this taxpayer's business down through the years. In fact, the party has become such an annual event that if he were to discontinue it now, it is possible that his business would fall off.

The standard of "ordinary and necessary" is still applicable to the deductibility of these expenses. Their disallowance by a careful revenue agent means that the taxpayer then has the burden of proving that they are ordinary and necessary. This is a heavy burden. Between it and the legislative history of this amendment as set forth in the report of the Committee on Finance, I do not foresee abuses such as those which we have occasionally read about in the newspapers. Sound enforcement of the tax laws by the Internal Revenue Service, aided by the very strong language contained in the committee's report, is all that is needed. I therefore hope that the Senate will accept this amendment by the committee.

Mr. BUSH. Mr. President, a parliamentary inquiry.

The PRESIDING OFFICER. The Senator will state it.

Mr. BUSH. Will the Presiding Officer clarify the vote which is about to be taken?

The PRESIDING OFFICER. The question is on agreeing en bloc to the committee amendments on page 41, line 18, and page 42, lines 4 and 7. The language is italicized on those pages.

Mr. BUSH. A "yea" vote is a vote for the committee amendments?

The PRESIDING OFFICER. A "yea" vote is a vote for the committee amend-

ments. A "nay" vote is a vote against the committee amendments.

On this question the yeas and nays have been ordered, and the clerk will call the roll.

The Chief Clerk called the roll.

Mr. HUMPHREY. I announce that the Senator from Nevada [Mr. BIBLE] is absent on official business.

I further announce that the Senator from New Mexico [Mr. ANDERSON], the Senator from Alaska [Mr. GRUENING], and the Senator from Missouri [Mr. SYMINGTON] are necessarily absent.

On this vote, the Senator from Alaska [Mr. GRUENING] is paired with the Senator from Missouri [Mr. SYMINGTON]. If present and voting, the Senator from Alaska would vote "nay," and the Senator from Missouri would vote "yea."

Mr. KUCHEL. I announce that the Senator from Maryland [Mr. BUTLER], the Senator from New Hampshire [Mr. MURPHY] and the Senator from Wisconsin [Mr. WILEY] are necessarily absent.

If present and voting, the Senator from New Hampshire [Mr. MURPHY] would vote "yea."

The result was announced—yeas 54, nays, 39, as follows:

[No. 223 Leg.]

YEAS—54

Alken	Goldwater	McCarthy
Allott	Hartke	McClellan
Beall	Hayden	Metcalfe
Bennett	Hickenlooper	Miller
Bottum	Hickey	Mundt
Byrd, Va.	Holland	Pearson
Cannon	Hruska	Proudy
Capehart	Javits	Randolph
Carlson	Jordan, N.C.	Robertson
Cotton	Jordan, Idaho	Saltonstall
Curtis	Keating	Scott
Dirksen	Kerr	Smathers
Dodd	Kuchel	Smith, Mass.
Eastland	Lausche	Stennis
Ellender	Long, Mo.	Thurmond
Ervin	Long, La.	Tower
Fong	Magnuson	Williams, N.J.
Fulbright	Mansfield	Young, N. Dak.

NAYS—39

Bartlett	Gore	Moss
Boggs	Hart	Muskie
Burdick	Hill	Neuberger
Bush	Humphrey	Pastore
Byrd, W. Va.	Jackson	Pell
Carroll	Johnston	Proxmire
Case	Kefauver	Russell
Chavez	Long, Hawaii	Smith, Maine
Church	McGee	Sparkman
Clark	McNamara	Talmadge
Cooper	Monroney	Williams, Del.
Douglas	Morse	Warborough
Engle	Morton	Young, Ohio

NOT VOTING—7

Anderson	Gruening	Wiley
Bible	Murphy	
Butler	Symington	

So the committee amendments on pages 41 and 42 were agreed to, as follows:

In section 4, on page 41, line 18, after the word "to", to insert "or associated with"; on page 42, line 4, after the word "to", to insert "or associated with"; in line 7, after the word "to", to insert "or associated with".

Mr. KERR. Mr. President, I move that the Senate reconsider the vote by which the amendments were agreed to.

Mr. SMATHERS. Mr. President, I move to lay that motion on the table.

The motion to lay on the table was agreed to.

Mr. KERR. Mr. President, I now ask unanimous consent that the Senate con-

sider the amendment designated as the sixth amendment, to be followed by the fourth amendment. The sixth amendment is found on page 385, line 1, through line 6 on page 386, and has to do with the treatment of certain charitable contributions for the purposes of part 1.

The amendment designated as the fourth amendment is the withholding amendment. I ask this unanimous consent after having consulted both sides.

Mr. ROBERTSON. Mr. President, reserving the right to object, I could not follow the statement of the numbers of the amendments. I shall speak briefly in support of the committee's action in eliminating the withholding section. Would the unanimous-consent agreement preclude my recognition for a few minutes to discuss that part of the bill?

Mr. KERR. Not at all.

The PRESIDING OFFICER. Is there objection? The Chair hears none, and it is so ordered.

Mr. MANSFIELD. Mr. President, I understand that the unanimous-consent request of the Senator from Oklahoma has been agreed to and that the Senate will consider, first the so-called sixth amendment, and that then the amendment designated "fourth" will be considered. The fourth amendment is the withholding amendment.

The PRESIDING OFFICER. The Senator is correct.

Mr. KERR. Mr. President, I yield to the Senator from Illinois.

LEGISLATIVE PROGRAM

Mr. DIRKSEN. Mr. President, I am not sure how much debate there will be on the withholding amendment. Is it anticipated that there will be a vote on that amendment tonight?

Mr. MANSFIELD. So long as the question has been raised, it is my hope that there will be a vote on the two amendments to which the Senator in charge of the bill has called the attention of the Senate, and other amendments as well. However, that is something which is within the discretion of the Senate as a whole.

ORDER FOR ADJOURNMENT

It is the intention to have the Senate meet at 10 o'clock tomorrow morning.

At this time I ask unanimous consent that when the Senate adjourns tonight—which may be late—it adjourn to meet at 10 o'clock tomorrow morning.

The PRESIDING OFFICER. Is there objection? The Chair hears none, and it is so ordered.

Mr. MANSFIELD. I should like to state further that it is anticipated that the Senate may well be in session on Saturday, because it does not appear at the moment that action on the tax bill will be completed at that time. If the Senate meets on Saturday, it will be to consider the tax bill and the independent offices appropriation bill.

Mr. SMATHERS. Mr. President, if consideration of the tax bill is concluded by Friday night, will it then be the majority leader's intention to bring the Senate back on Saturday to take up the

appropriation bill, or may we have Saturday off?

Mr. MANSFIELD. If any carrot is to be held before Members of the Senate, I am not the one who will hold it. If the Senate completes consideration of the bill on Saturday, it will go over until Tuesday. If it does not finish on Friday, it will meet on Saturday. If the Senate meets on Saturday it will go over until Tuesday.

Mr. DIRKSEN. Is that the stick, instead of the carrot?

Mr. MANSFIELD. It is neither a stick nor a carrot.

Mr. MAGNUSON. Mr. President, I wonder if it would be possible to take up the independent offices appropriation bill on Friday night after consideration of the tax bill is concluded?

Mr. MANSFIELD. If it is concluded; otherwise it will be taken up on Saturday.

Mr. MAGNUSON. Does the Senator mean after midnight?

Mr. MANSFIELD. After midnight or before, depending on the circumstances.

Mr. MAGNUSON. The Senator from Washington has a very important engagement in the State of Washington on Saturday, and intended to leave here Saturday morning, whether it be 1 or 3 or 5 or 6 o'clock in the morning. If the Senate could conclude consideration of the tax bill, could the independent offices bill be taken up at that time?

Mr. MANSFIELD. Yes; but again I remind the Senator that his skilled leadership and profound generalship are needed here on the floor of the Senate at this time to put through this very important legislation.

Mr. MAGNUSON. That is what I would call a gold carrot.

REVENUE ACT OF 1962

The Senate resumed the consideration of the bill (H.R. 10650) to amend the Internal Revenue Code of 1954 to provide a credit for investment in certain depreciable property, to eliminate certain defects and inequities, and for other purposes.

Mr. DIRKSEN. Mr. President, will the Senator from Oklahoma yield?

Mr. KERR. I yield to the Senator from Illinois.

Mr. DIRKSEN. Would it be in order to ask for the yeas and nays on both of the amendments to which reference has been made?

Mr. KERR. Before the Senator makes that request, let me say that I am of the opinion that there is grave doubt as to whether the yeas and nays will be asked for on the amendment of the Senator from Utah, which would merely give the donor of a charitable contribution the right to spread the effective period of it for deduction purposes over more than 1 year. I should like to inquire if Senators will ask for the yeas and nays on that amendment.

Mr. DIRKSEN. I withdraw my request at this time. I can ask for the yeas and nays when the withholding amendment is reached.

Mr. KERR. I do not believe the yeas and nays will be asked for. However,

my opinion is not binding upon the Senate.

The PRESIDING OFFICER. The committee amendment will be stated.

The CHIEF CLERK. At the top of page 385, it is proposed to insert a new section, as follows:

SEC. 22. CHARITABLE CONTRIBUTIONS MADE FROM INCOME ATTRIBUTABLE TO SEVERAL TAXABLE YEARS.

(a) TREATMENT FOR PURPOSES OF PART I OF SUBCHAPTER Q.—Section 1307 (relating to rules applicable to part I of subchapter Q) is amended by adding at the end thereof the following new subsection:

"(e) ELECTION WITH RESPECT TO CHARITABLE CONTRIBUTIONS.—In the case of an individual who elects (in such manner and at such time as the Secretary or his delegate prescribes by regulations) to have the provisions of this subsection apply, an amount received or accrued to which this part applies shall be reduced, for purposes of computing the tax liability of the taxpayer under this part with respect to the amount so received or accrued, by an amount equal to that portion of (1) the amount of charitable contributions made by the taxpayer during the taxable year in which the amount is so received or accrued which are allowable as a deduction for such year under section 170 (determined without regard to this part), as (2) the amount received or accrued to which this part applies is of the adjusted gross income for the taxable year (determined without regard to this part). In any case in which the taxpayer elects to have the provisions of this subsection apply, no portion of the amount to which this part applies shall, for purposes of computing the limitation on tax under this part, be taken into account for purposes of computing the limitation under section 170(b)(1) for the taxable year in which the amount to which this part applies is received or accrued."

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply with respect to amounts received or accrued in taxable years beginning after December 31, 1961.

Mr. BENNETT obtained the floor.

Mr. KERR. Mr. President, as I understand, the Senate is ready to adopt the committee amendment.

Mr. BENNETT. Mr. President, so far as I am concerned, I do not desire to make a speech. If the Senate is willing to adopt the amendment, I shall be happy to yield the floor.

Mr. GORE. Mr. President, will the Senator from Utah yield?

Mr. BENNETT. I am happy to yield.

Mr. GORE. The reason why I asked that this amendment, together with four others, which are really riders on the bill, be reserved for separate action was that I did not feel that these particular amendments, which do not relate to the subject matter of the bill, should properly be adopted en bloc as committee amendments. But I have no objection to the committee amendment.

Mr. BENNETT. Mr. President, so far as I know, there is no objection. Under those circumstances, I am perfectly willing to ask for action on the amendment.

The PRESIDING OFFICER. Is the Senator from Utah speaking of the committee amendment?

Mr. BENNETT. I refer to the committee amendment which has been reported, or which has been stated by the clerk, to insert a new section at the top of page 385 and continuing on page 386.

The PRESIDING OFFICER. The question is on agreeing to the committee amendment on page 385.

The amendment was agreed to.

Mr. KERR. Mr. President, I move that the action by which the committee amendment was agreed to be reconsidered.

Mr. BENNETT. I move to lay that motion on the table.

The motion to lay on the table was agreed to.

Mr. MANSFIELD. Mr. President, what is the pending business?

The PRESIDING OFFICER. Amendment No. 4 will be stated.

Mr. KERR. That is the withholding tax amendment.

Mr. WILLIAMS of Delaware. Mr. President, on this amendment I ask for the yeas and nays.

The PRESIDING OFFICER. First, the amendment will be stated.

The CHIEF CLERK. On page 307, after line 8, it is proposed to strike out:

SEC. 19. WITHHOLDING OF INCOME TAX AT SOURCE ON INTEREST, DIVIDENDS, AND PATRONAGE DIVIDENDS.

(a) IN GENERAL.—

(1) AMENDMENT OF SUBTITLE C.—Subtitle C (relating to employment taxes and collection of income tax at source) is amended by redesignating chapter 25 as chapter 26 and by inserting after chapter 24 the following new chapter:

"CHAPTER 25—COLLECTION OF INCOME TAX AT SOURCE ON INTEREST, DIVIDENDS, AND PATRONAGE DIVIDENDS

"Subchapter A. Interest.

"Subchapter B. Dividends.

"Subchapter C. Patronage dividends.

"Subchapter D. General provisions.

"Subchapter A—Interest

"Sec. 3454. Income tax collected at source on interest.

"Sec. 3452. Interest defined.

"SEC. 3451. INCOME TAX COLLECTED AT SOURCE ON INTEREST.

"(a) REQUIREMENT OF WITHHOLDING.—Except as otherwise provided in this chapter, every person who pays interest shall deduct and withhold on such interest a tax equal to 20 percent of the amount thereof.

"(b) PAYEE UNKNOWN.—If the withholding agent is unable to determine the person to whom the interest is payable, the tax under this section shall be deducted and withheld at the time payment of the interest would be made if such person were known.

"(c) CROSS REFERENCES.—

"(1) For credit, against income tax of the recipient of the income, of amounts deducted and withheld under this section, see section 39.

"(2) For special rules as to credit or refund of such amounts, see sections 3484, 3485, 3486, 3487, and 3505.

"(3) For exemption from requirement of deducting and withholding on certain interest paid to certain persons, see section 3483.

"SEC. 3452. INTEREST DEFINED.

"(a) GENERAL RULE.—For purposes of this chapter, the term 'interest' means—

"(1) interest on evidences of indebtedness (including bonds, debentures, notes, and certificates) issued by a corporation with interest coupons or in registered form, and, to the extent provided in regulations prescribed by the Secretary or his delegate, interest on other evidences of indebtedness issued by a corporation of a type offered by corporations to the public;

"(2) interest on deposits with persons carrying on the banking business;

"(3) amounts (whether or not designated as interest) paid by a mutual savings bank, savings and loan association, building and loan association, cooperative bank, home-stead association, credit union, or similar organization, in respect of deposits, investment certificates, or withdrawable or repurchasable shares;

"(4) interest on amounts held by an insurance company under an agreement to pay interest thereon;

"(5) interest on deposits with stock-brokers;

"(6) interest on obligations of the United States; and

"(7) in the case of a non-interest-bearing obligation of the United States—

"(A) issued on a discount basis, and

"(B) having a maturity date more than one year from the date of issue,

the amount by which the amount paid on surrender or redemption exceeds the issue price.

"(b) EXCEPTIONS.—For purposes of this chapter, the term 'interest' does not include—

"(1) interest on obligations described in section 103(a) (1) or (3) (relating to interest on certain governmental obligations);

"(2) any amount paid by—

"(A) a foreign government or international organization,

"(B) a foreign corporation not engaged in trade or business within the United States,

"(C) a nonresident alien individual not engaged in trade or business within the United States, or

"(D) a partnership not engaged in trade or business within the United States and composed in whole or in part of nonresident aliens;

"(3) interest on deposits with persons carrying on the banking business paid to a person described in paragraph (2) (B), (C), or (D);

"(4) any amount paid by one corporation to another corporation, if both corporations are members of the same affiliated group which filed a consolidated return for the preceding taxable year of the affiliated group;

"(5) interest subject to withholding under subchapter A of chapter 3 (sec. 1441 and following, relating withholding of tax on nonresident aliens and foreign corporations) by the person paying such interest, or which would be so subject to withholding by such person, but for the fact that it is not treated as income from sources within the United States;

"(6) any amount on which the withholding agent is required to deduct and withhold a tax under section 1451 (relating to tax free covenant bonds), or would be so required but for section 1451(d) (relating to benefit of personal exemptions);

"(7) to the extent provided in regulations prescribed by the Secretary or his delegate, any amount payable with respect to deposits in school savings accounts; and

"(8) any amount described in subsection (a) (2), (3), or (7) paid to a State or a foreign government or international organization (other than any amount described in subsection (a) (3) paid in respect of a transferable certificate or share).

"(c) EXEMPTION FOR UNITED STATES.—The Secretary may authorize exemption from the tax imposed by section 3451 for any amount paid by the United States or any wholly owned agency or instrumentality thereof to the United States or any wholly owned agency or instrumentality thereof if the Secretary determines that the imposition of the tax with respect to such amount will cause a burden or expense which can be avoided by granting the tax exemption.

"Subchapter B—Dividends

"Sec. 3461. Income tax collected at source on dividends.

"Sec. 3462. Dividend defined.

"SEC. 3461. INCOME TAX COLLECTED AT SOURCE ON DIVIDENDS.

"(a) REQUIREMENT OF WITHHOLDING.—Except as otherwise provided in this chapter, every person who pays a dividend shall deduct and withhold on such dividend a tax equal to 20 percent of the amount thereof.

"(b) PAYEE UNKNOWN.—If the withholding agent is unable to determine the person to whom the dividend is payable, the tax under this section shall be deducted and withheld at the time payment of the dividend would be made if such person were known.

"(c) AMOUNT OF DIVIDEND UNKNOWN.—If the withholding agent is unable to determine the portion of a distribution which is a dividend, the tax under this section shall be computed on the entire amount of the distribution.

"(d) CROSS REFERENCES.—

"(1) For credit, against income tax of the recipient of the income, of amounts deducted and withheld under this section, see section 39.

"(2) For special rules as to credit or refund of such amounts, see sections 3484, 3485, 3486, 3487, and 3505.

"(3) For exemption from requirement of deducting and withholding on dividends paid to certain individuals, see section 3483.

"SEC. 3462. DIVIDEND DEFINED.

"(a) GENERAL RULE.—For purposes of this chapter, the term 'dividend' means—

"(1) any distribution by a corporation which is a dividend (as defined in section 316); and

"(2) any payment made by a stockbroker to any person as a substitute for a dividend (as so defined).

"(b) EXCEPTIONS.—For purposes of this chapter, the term 'dividend' does not include—

"(1) any amount paid in the stock, or rights to acquire the stock, of the distributing corporation if the distribution is not includible in gross income of the recipient under the provisions of section 305 (relating to distributions of stock and stock rights);

"(2) any distribution to the extent that, under chapter 1—

"(A) the amount thereof is treated by the recipient as an amount received on the sale or exchange of property, or

"(B) gain or loss to the recipient is not recognized;

"(3) any amount which is includible in gross income as a taxable dividend by reason of the provisions of section 302 (relating to redemptions of stock), 306 (relating to dispositions of certain stock), 356 (relating to receipt of additional consideration in connection with certain reorganizations), or 1081(e) (2) (relating to certain distributions pursuant to order of the Securities and Exchange Commission);

"(4) any amount paid by one corporation to another corporation, if both corporations are members of the same affiliated group which filed a consolidated return for the preceding taxable year of the affiliated group;

"(5) an amount which—

"(A) is subject to withholding under subchapter A of chapter 3 (sec. 1441 and following, relating to withholding of tax on nonresident aliens and foreign corporations) by the person paying such amount, or

"(B) would be subject to withholding under such subchapter A by the person paying such amount but for—

"(1) the fact that it is attributable to income from sources outside the United States, or

"(2) the fact that the payor thereof is excepted from the application of section 1441(a) by the provisions of section 1441(c);

"(6) any amount paid by a foreign corporation not engaged in trade or business within the United States;

"(7) any amount described in section 1373 (relating to undistributed taxable income of electing small business corporations); and

"(8) amounts paid pursuant to the terms of a lease entered into before January 1, 1954, if under such lease the shareholders of the lessor corporation are entitled to such amounts without deduction for any tax which any law of the United States might require to be deducted and withheld on the payment of dividends.

"Subchapter C—Patronage dividends

"Sec. 3471. Income tax collected at source on patronage dividends.

"Sec. 3472. Amounts subject to withholding.

"SEC. 3471. INCOME TAX COLLECTED AT SOURCE ON PATRONAGE DIVIDENDS.

"(a) REQUIREMENT OF WITHHOLDING.—Except as otherwise provided in this chapter, every cooperative to which part I of subchapter T of chapter 1 applies which pays an amount described in section 3472 shall deduct and withhold on such amount a tax equal to 20 percent of such amount.

"(b) PAYEE UNKNOWN.—If the withholding agent is unable to determine the person to whom the amount is payable, the tax under this section shall be deducted and withheld at the time payment of the amount would be made if such person were known.

"(c) CROSS REFERENCES.—

"(1) For credit, against income tax of the recipient of the income, of amounts deducted and withheld under this section, see section 39.

"(2) For special rules as to credit or refund of such amounts, see sections 3484, 3485, 3486, 3487, and 3505.

"(3) For exemption from requirement of deducting and withholding on amounts paid to certain individuals, see section 3483.

"SEC. 3472. AMOUNTS SUBJECT TO WITHHOLDING.

"(a) GENERAL RULE.—Except as otherwise provided in this section or section 3483, the amounts subject to deduction and withholding under section 3471 are—

"(1) the amount of any patronage dividend (as defined in section 1388(a)) which is paid in money, qualified written notices of allocation (as defined in section 1388(c)), or other property (except nonqualified written notices of allocation as defined in section 1388(d)), and

"(2) any amount, described in section 1382 (c) (2) (A) (relating to certain nonpatronage distributions), which is paid in money, qualified written notices of allocation, or other property (except nonqualified written notices of allocation) by an organization exempt from tax under section 521 (relating to exemption of farmers' cooperatives from tax).

"(b) EXCEPTIONS.—The provisions of section 3471 shall not apply to—

"(1) any amount paid by one corporation to another corporation, if both corporations are members of the same affiliated group which filed a consolidated return for the preceding taxable year of the affiliated group;

"(2) an amount which—

"(A) is subject to withholding under subchapter A of chapter 3 (sec. 1441 and following, relating to withholding of tax on nonresident aliens and foreign corporations) by the person paying such amount, or

"(B) would be subject to withholding under such subchapter A by the person paying such amount but for the fact that it is attributable to income from sources outside the United States; and

"(3) any amount paid by a foreign corporation not engaged in trade or business within the United States.

"(c) EXEMPTION FOR CERTAIN CONSUMER COOPERATIVES.—A cooperative which the Secretary or his delegate determines is primarily

engaged in selling at retail goods or services of a type that are generally for personal, living, or family use shall, upon application to the Secretary or his delegate, be granted exemption from the tax imposed by section 3471. Application for exemption under this subsection shall be made in accordance with regulations prescribed by the Secretary or his delegate.

"(d) DETERMINATION OF AMOUNT PAID.—For purposes of this subchapter, in determining amounts paid—

"(1) property (other than a written notice of allocation) shall be taken into account at its fair market value, and

"(2) a qualified written notice of allocation shall be taken into account at its stated dollar amount.

"Subchapter D—General provisions

"Sec. 3481. Liability for return and payment of withheld tax.

"Sec. 3482. Return and payment by United States.

"Sec. 3483. Exemption certificates.

"Sec. 3484. Refund of tax to individuals.

"Sec. 3485. Refund of tax to States, tax exempt organizations, etc.

"Sec. 3486. Refund of tax to corporation.

"Sec. 3487. Credit for tax withheld on corporation.

"Sec. 3488. Obligation sold between interest payment dates.

"Sec. 3489. Presumption.

"Sec. 3490. Definitions.

"SEC. 3481. LIABILITY FOR RETURN AND PAYMENT OF WITHHELD TAX.

"(a) GENERAL RULE.—Every person required to deduct and withhold any tax under this chapter shall, on or before the last day of the first month following the close of each quarter of his taxable year, make a return of the tax required to be deducted and withheld during such quarter and pay the tax to the officer designated in section 6151. The withholding agent shall be liable for the payment of the taxes required to be deducted and withheld under this chapter, and shall not otherwise be liable to any person for the amount of any such payment.

"(b) TAX PAID BY RECIPIENT.—If the withholding agent, in violation of the provisions of this chapter, fails to deduct and withhold any tax under this chapter, and thereafter the tax against which such tax may be credited is paid, the tax so required to be deducted and withheld shall not be collected from the withholding agent; but this subsection shall in no case relieve the withholding agent from liability for any penalties or additions to the tax otherwise applicable in respect of such failure to deduct and withhold.

"(c) CROSS REFERENCE.—

"For limitation on the use of Government depositaries in the collection of taxes deducted and withheld under this chapter, see the last sentence of section 6302(c).

"SEC. 3482. RETURN AND PAYMENT BY UNITED STATES.

"If the withholding agent is the United States the return of the tax deducted and withheld under this chapter may be made by an officer or employee of the United States having control of the payment of the amount subject to withholding, or appropriately designated for that purpose.

"SEC. 3483. EXEMPTION CERTIFICATES.

"(a) GENERAL RULES.—

"(1) INDIVIDUALS UNDER 18.—Any individual may file with any withholding agent an exemption certificate on which he certifies the date of his birth. If such a certificate is filed, all amounts payable by such withholding agent to such individual, on and after the effective date for such certificate and before the beginning of the calendar year during which the certificate indicates that he will attain age 18, shall be exempt from the requirement of deducting and withholding under this chapter.

"(2) INDIVIDUALS OVER AGE 17.—Any individual may file with any withholding agent an exemption certificate in which he certifies—

"(A) that he will have attained age 18 before the close of the calendar year for which such certificate is filed, and

"(B) that he reasonably believes that he will not (after the application of the credits against tax provided by part IV of subchapter A of chapter 1, other than the credits under sections 31 and 39) be liable for the payment of any tax under chapter 1 for each of his taxable years any portion of which is included in the period for which such certificate will be in effect.

If such a certificate is filed, all amounts payable by such withholding agent to such individual during the period such certificate is in effect shall be exempt from the requirement of deducting and withholding under this chapter. Except as may otherwise be provided in regulations prescribed by the Secretary or his delegate, an exemption certificate filed by an individual described in this paragraph shall remain in effect only for the period beginning on the effective date of such certificate and ending at the close of the calendar year in which such period begins.

"(3) TAX EXEMPT ORGANIZATIONS.—

"(A) Any organization (other than a cooperative described in section 521) which is exempt from the tax imposed by chapter 1 may file with any withholding agent who pays amounts described in section 3452(a) (2), (3), or (7) an exemption certificate on which it certifies that it is such an organization. If such a certificate is filed, all amounts described in section 3452(a) (2), (3), and (7) payable by such withholding agent to such organization on and after the effective date for such certificate shall (except as provided in subparagraph (B)) be exempt from the requirement of deducting and withholding under this chapter.

"(B) An exemption certificate filed by an organization under subparagraph (A) shall cease to be effective on the thirtieth day after the day on which the withholding agent, with whom such certificate was filed, is notified by either the organization or the Secretary or his delegate that the organization is no longer exempt from the tax imposed by chapter 1. If an organization ceases to be exempt from such tax, it shall, within the time specified in regulations prescribed by the Secretary or his delegate, so notify each withholding agent with whom it has an exemption certificate in effect.

"(b) EXCEPTIONS AND SPECIAL RULES.—

"(1) CERTAIN EXCEPTIONS.—This section shall not apply to any amount—

"(A) described in section 3452(a) (1) (relating to interest on evidences of indebtedness),

"(B) described in section 3452(a) (3) paid in respect of a transferable certificate or share, or

"(C) described in section 3452(a) (6) (relating to interest on obligations of the United States).

"(2) SERIES E BONDS, ETC.—In the case of transactions involving the redemption of one or more obligations described in section 3452(a) (7) (relating to certain obligations of the United States issued on a discount basis), a separate certificate shall be filed with respect to each such transaction.

"(3) NOMINEES, CUSTODIANS, AND JOINT OWNERSHIPS.—Under regulations prescribed by the Secretary or his delegate, the exemption provided by subsection (a) may be extended, in a manner consistent with the other provisions of this section, to—

"(A) amounts (other than amounts described in section 3462(a), relating to dividends) paid through nominees;

"(B) amounts paid to custodians; and

"(C) amounts paid jointly to 2 or more individuals.

"(4) **EFFECTIVE DATE OF CERTIFICATE.**—Any exemption certificate under this section shall take effect on such day as is specified in accordance with regulations prescribed by the Secretary or his delegate.

"(5) **FORM AND CONTENTS OF CERTIFICATE AND NOTICE.**—Any exemption certificate under this section, and any notice under subsection (a) (3) (B), shall be in such form and contain such information as the Secretary or his delegate may by regulations prescribe.

"(c) **CROSS REFERENCE.**—

"For penalty for filing fraudulent certificate, or for failing to provide notice, under this section, see section 7205.

"SEC. 3484. **REFUND OF TAX TO INDIVIDUALS.**

"(a) **GENERAL RULE.**—Except as provided in subsection (e), the tax deducted and withheld under this chapter with respect to amounts received by an individual during any quarter (other than the fourth quarter) of his taxable year (together with any tax so deducted and withheld on amounts which were received by him during any prior quarter of such year and with respect to which no allowable claim for refund has been filed under this section) shall, to the extent such tax does not exceed his refund allowance as of the time the claim for refund is filed, be promptly refunded to him as an overpayment of tax. A refund of tax shall be made under this section only if the amount claimed and allowable equals or exceeds \$10.

"(b) **REFUND ALLOWANCE.**—For purposes of this section, the refund allowance of an individual as of the time the claim for refund is filed is an amount equal to the excess, if any, of—

"(1) an amount equal to 22 percent of—

"(A) the total of the deductions which, on the basis of facts existing at the time the claim for refund is filed, such individual would be allowed for the taxable year under section 151 (relating to deductions for personal exemptions), plus

"(B) in the case of an individual who, at the time the claim for refund is filed, reasonably expects that he will be allowed a credit under section 37 (relating to retirement income) for the taxable year, the amount which, at such time, such individual reasonably expects to be the amount of his retirement income (as defined in section 37(c) and as limited by section 37(d)) for the taxable year, less

"(C) the amounts (other than amounts on which tax is required to be deducted and withheld under this chapter) which, at the time the claim for refund is filed, such individual reasonably expects to be includible in his gross income for the taxable year; over

"(2) the amounts of tax with respect to which an allowable claim for refund has been previously filed under this section during taxable year.

For purposes of paragraph (1)(C), an individual who files more than one claim for refund under this section for any taxable year may use the estimate for the preceding claim for such year unless, at the time he files the claim, he reasonably expects the amounts referred to in paragraph (1)(C) to exceed such prior estimate by more than \$100.

"(c) **MARRIED INDIVIDUALS.**—For purposes of subsections (a), (b), and (d), married individuals shall be treated as an individual if, at the time the claim for refund is filed, they reasonably expect that they will file a joint return for the taxable year in which such claim is filed.

"(d) **TIME FOR FILING CLAIM.**—Not more than one claim may be filed under this section by any individual during any quarter of his taxable year. A refund of tax deducted and withheld on amounts received during a taxable year shall be made under this section only if claim therefor is filed on or before the last day of such taxable year.

"(e) **INDIVIDUALS NOT ELIGIBLE FOR REFUND.**—No claim for refund may be filed under this section by—

"(1) any individual (other than an individual referred to in paragraph (2) or (3)) unless, at the time the claim for refund is filed, he reasonably expects that his gross income for the taxable year will not exceed \$5,000;

"(2) any married individual unless, at the time the claim for refund is filed, he reasonably expects that the aggregate gross income of such individual and his spouse for the taxable year will not exceed \$10,000;

"(3) a head of a household (as defined in section 1(b)(2)) or a surviving spouse (as defined in section 2(b)) unless, at the time the claim for refund is filed, he reasonably expects that his gross income for the taxable year will not exceed \$10,000; or

"(4) any child, unless, at the time the claim for refund is filed, he reasonably expects that no deduction would be allowed for him under section 151(e)(1)(B) for the taxable year of his parent (or parents) beginning with or within the calendar year in which the claim for refund is filed.

"(f) **CROSS REFERENCE.**—

"For credit or refund of amounts not refunded under this section, see section 39.

"SEC. 3485. **REFUND OF TAX TO STATES, TAX-EXEMPT ORGANIZATIONS, ETC.**

"(a) **GENERAL RULE.**—In the case of a person which is—

"(1) the United States or a State,

"(2) an organization (other than a cooperative described in section 521) which is exempt from the tax imposed by chapter 1,

"(3) a foreign government or international organization, or

"(4) a foreign central bank of issue, if the tax deducted and withheld under this chapter with respect to amounts received by such person during any calendar quarter exceeds the credit, if any, claimed by and allowable to such person under section 3505 (relating to credit against employment taxes) for such quarter, the excess (together with any such excess for any prior quarter of the same calendar year with respect to which no refund has been claimed and allowed under this section) shall be promptly refunded or credited to such person as an overpayment of tax. In the case of a person to which paragraph (4) applies, the amount which may be refunded or credited under this section shall not exceed the amount of tax deducted and withheld under section 3451 on interest paid on obligations of the United States which are not held for, or used in connection with, the conduct of commercial banking functions or other commercial activities.

"(b) **CROSS REFERENCES.**—

"(1) For period of limitation for filing claim under this section, see section 6511.

"(2) For presumed date of payment for purposes of (A) period of limitation, see section 6513(b), and (B) allowance of interest on overpayments, see section 6611(d).

"SEC. 3486. **REFUND OF TAX TO CORPORATION.**

"(a) **GENERAL RULE.**—If the tax deducted and withheld under this chapter with respect to amounts received by a corporation (other than a corporation described in section 3485(a)) during any quarter (other than the fourth quarter) of its taxable year exceeds the amount claimed by and allowable to such corporation under section 3487 as a credit against its liability for tax under this chapter for such quarter, the excess (together with any such excess for any prior quarter of the same year with respect to which no refund has been claimed and allowed under this section) shall be promptly refunded or credited to such corporation as an overpayment of tax. A refund of tax shall be made under this section only if claim therefor is filed after the close of the

period covered by the claim and on or before the last day of the taxable year.

"(b) **CROSS REFERENCE.**—

"For credit or refund of amounts not refunded under this section, see section 39.

"SEC. 3487. **CREDIT FOR TAX WITHHELD ON CORPORATION**

"(a) **GENERAL RULE.**—Any tax deducted and withheld under this chapter with respect to amounts received by a corporation (other than a corporation described in section 3485(a)) during a taxable year shall, to the extent not claimed and allowable as a credit or refund to the corporation under section 3486, be allowed, under regulations prescribed by the Secretary or his delegate, as a credit against (but not in excess of) the tax for which such corporation is liable under this chapter in respect of amounts paid by it during such year.

"(b) **DIVIDENDS AND PATRONAGE DIVIDENDS PAID DURING TAXABLE YEAR.**—For purposes of determining the credit allowable to any corporation under subsection (a), a dividend, or amount subject to withholding under section 3471, paid by it may be considered as having been paid during the taxable year—

"(1) in the case of a personal holding company, if treated as paid during such taxable year under section 563(b),

"(2) in the case of a regulated investment company, if treated as paid during such taxable year under section 855(a),

"(3) in the case of a real estate investment trust, if treated as paid during such taxable year under section 858(a), or

"(4) in the case of a cooperative described in section 1381(a), if paid during the payment period (as defined in section 1382(d)) for such taxable year.

"(c) **SPECIAL RULE FOR CORPORATIONS WHICH ARE MEMBERS OF AN AFFILIATED GROUP.**—To the extent and subject to such conditions as may be provided in regulations prescribed by the Secretary or his delegate, the tax deducted and withheld under this chapter with respect to amounts received by a corporation which is a member of an affiliated group which filed a consolidated return for the preceding taxable year of the affiliated group may, for purposes of this section, be treated as tax deducted and withheld under this chapter from any corporation which is a member of the same affiliated group.

"SEC. 3488. **OBLIGATION SOLD BETWEEN INTEREST-PAYMENT DATES**

"For purposes of any credit or refund provided in section 3484, 3485, 3486, or 3487, in the case of an obligation which is sold or exchanged between interest-payment dates the amount required to be deducted and withheld on the interest at the end of the interest-payment period shall be treated in the manner provided in section 39(c).

"SEC. 3489. **PRESUMPTION.**

"For purposes of establishing that any person is entitled to a credit or refund of any tax required to be deducted and withheld under this chapter with respect to amounts received by such person, the correct amount of such tax shall, in the absence of evidence to the contrary, be presumed to have been so deducted and withheld.

"SEC. 3490. **DEFINITIONS.**

"For purposes of this chapter—

"(1) **PERSON.**—The term 'person' includes the United States, a State, a foreign government, and an international organization.

"(2) **STATE.**—The term 'State' includes a State, the District of Columbia, a possession of the United States, any political subdivision of any of the foregoing, and any wholly owned agency or instrumentality of any one or more of the foregoing.

"(3) **FOREIGN GOVERNMENT.**—The term 'foreign government' includes a foreign government, a political subdivision of a foreign government, and any wholly owned agency

or instrumentality of any one or more of the foregoing.

"(4) **NONRESIDENT ALIEN.**—The term 'non-resident alien individual' includes an alien resident of Puerto Rico."

(2) **CLERICAL AMENDMENTS, ETC.**—

(A) The heading for subtitle C is amended to read as follows:

"**SUBTITLE C—EMPLOYMENT TAXES AND COLLECTION OF INCOME TAX AT SOURCE**"

(B) The table of chapters for subtitle C is amended by striking out the last line and inserting in lieu thereof the following:

"**CHAPTER 25.** Collection of income tax at source on interest, dividends, and patronage dividends.

"**CHAPTER 26.** General provisions relating to employment taxes and collection of income taxes at source."

(C) The table of subtitles under the heading "Internal Revenue Title" at the beginning of the Internal Revenue Code of 1954 is amended by striking out the third line and inserting in lieu thereof the following:

"Subtitle C. Employment taxes and collection of income tax at source."

(D) The heading for chapter 26 (as redesignated by paragraph (1) of this subsection) is amended to read as follows:

"**CHAPTER 26—GENERAL PROVISIONS RELATING TO EMPLOYMENT TAXES AND COLLECTION OF INCOME TAXES AT SOURCE**"

(b) **CREDITS AGAINST INCOME TAX FOR TAX WITHHELD.**—

(1) **ALLOWANCE OF CREDIT.**—Part IV of subchapter A of chapter 1 (relating to credits against tax) is amended by inserting after section 38 (added by section 2 of this Act) the following new section:

"**SEC. 39. TAX WITHHELD ON INTEREST, DIVIDENDS, AND PATRONAGE DIVIDENDS.**

"(a) **GENERAL RULE.**—Under regulations prescribed by the Secretary or his delegate, the tax deducted and withheld under chapter 25 (relating to withholding at source on interest, dividends, and patronage dividends) shall be allowed, to the recipient of the amount with respect to which such tax was deducted and withheld, as a credit against the tax imposed by this subtitle for the taxable year in which such amount is received.

"(b) **SPECIAL RULE FOR DEPENDENT CHILDREN.**—If—

"(1) the taxpayer for his taxable year is entitled to a deduction under section 151(e) (1) (B) with respect to a child, and

"(2) such child had, for the calendar year ending with or within the taxpayer's taxable year—

"(A) gross income of less than \$600, and

"(B) no wages (as defined in section 3401 (a)) with respect to which withholding was required under chapter 24,

then, under regulations prescribed by the Secretary or his delegate, the taxpayer shall be entitled to the credit provided by subsection (a) with respect to amounts received by such child during such calendar year, but only if such child has not filed any claim for credit or refund of any portion of the tax deducted and withheld with respect to such amounts.

"(c) **APPORTIONMENT OF CREDIT.**—For purposes of subsection (a), if an obligation is sold or exchanged between interest payments dates—

(1) so much of the amount required to be deducted and withheld on the interest at the end of the interest-payment period as is properly allocable to that part of such period which ends on the date of the sale or exchange shall be treated as an amount deducted and withheld from the transferor on the date of the sale or exchange, and

"(2) so much of such amount as is properly allocable to that part of such period which begins on the day after the date of the sale or exchange shall be treated as an amount deducted and withheld from the transferee.

"(d) **LIMITATIONS.**—The credit provided by subsection (a) shall not be allowed—

"(1) **REFUND TO INDIVIDUALS.**—To any individual with respect to any amount of tax allowed him as a refund under section 3484.

"(2) **CREDIT OR REFUND TO STATES, ETC.**—To any person with respect to any amount of tax allowable to such person as a credit or refund under section 3485 or as a credit under section 3505.

"(3) **CREDIT OR REFUND TO CORPORATIONS.**—To any person with respect to any amount of tax allowed such person as a credit or refund under section 3486 or as a credit under section 3487.

"(4) **CERTAIN DEPENDENT CHILDREN.**—To any person with respect to any amount of tax which has been claimed and is allowable as a credit to such person's parent by reason of the provisions of subsection (b).

"(5) **NOMINEES, ETC.**—To any person with respect to any amount of tax allowed such person as a credit under section 1444(b)."

(2) **COMMON TRUST FUNDS.**—Section 584(c) (relating to the income of participants in the fund) is amended by adding at the end thereof the following new paragraph:

"(3) **TAX WITHHELD AT SOURCE ON INTEREST, DIVIDENDS, AND PATRONAGE DIVIDENDS.**—In any case where tax under chapter 25 is deducted and withheld on any amounts received by a common trust fund, for purposes of any credit or refund provided in section 39 or 3505, or chapter 25, such tax shall, in accordance with regulations prescribed by the Secretary or his delegate, be considered as having been deducted and withheld proportionately from each participant."

(3) **ESTATES AND TRUSTS.**—Section 642(a) (relating to special rules for credits and deductions in the case of estates and trusts) is amended by adding at the end thereof the following new paragraph:

"(4) **TAX WITHHELD AT SOURCE ON INTEREST, DIVIDENDS, AND PATRONAGE DIVIDENDS.**—In any case where tax under chapter 25 is deducted and withheld on any amounts received by an estate or trust, for purposes of any credit or refund provided in section 39 or 3505, or chapter 25, such tax shall, in accordance with regulations prescribed by the Secretary or his delegate, be considered as having been deducted and withheld from each beneficiary in an amount which, when added to the amounts paid, credited, or required to be distributed to him, equals the amounts which would have been paid, credited, or required to be distributed to him in the absence of chapter 25. Any tax under chapter 25 which is deducted and withheld on amounts received by the estate or trust shall be considered as withheld from such estate or trust to the extent it is not considered as withheld from a beneficiary under the provisions of the preceding sentence."

(4) **TECHNICAL AMENDMENTS.**—

(A) Section 164(b) (1) (relating to deduction denied in the case of certain taxes) is amended by—

(i) striking out the word "and" at the end of subparagraph (B);

(ii) striking out the comma at the end of subparagraph (C) and inserting "; and"; and

(iii) adding after subparagraph (C) the following new subparagraph:

"(D) the tax withheld at source under chapter 25 (relating to collection of income tax at source on interest, dividends, and patronage dividends)."

(B) Section 874(a) (relating to allowance of deductions and credits to nonresident alien individuals) is amended by striking

"31 and 32" and inserting in lieu thereof "31, 32, and 39".

(C) Section 1314(c) (relating to inapplicability of part II of subchapter Q of chapter 1 of subtitle A to taxes imposed by subtitle C) is amended by striking "employment taxes" and inserting in lieu thereof "employment taxes and collection of income tax at source".

(D) Section 6211(b) (1) (relating to rules applicable in determination of deficiency) is amended by striking "31" and inserting in lieu thereof "31 or 39".

(E) The table of sections for part IV of subchapter A of chapter 1 is amended by striking out "Sec. 38. Overpayments of tax." and inserting in lieu thereof:

"Sec. 38. Investment in certain depreciable property.

"Sec. 39. Tax withheld on interest, dividends, and patronage dividends.

"Sec. 40. Overpayments of tax."

(c) **INTEREST AND DIVIDENDS PAID TO NON-RESIDENT ALIENS, ETC.**—

(1) **WITHHOLDING RATE.**—

(A) Section 1441 (relating to withholding of tax on nonresident aliens) is amended by adding at the end thereof the following new subsection:

"(e) **TREATIES.**—In the case of amounts described in section 3452(a) (relating to interest) section 3462(a) (relating to dividends), and section 3472(a) (relating to patronage dividends), the tax required to be deducted and withheld under subsection (a) shall not by reason of the provisions of any treaty be less than 20 percent of such amounts."

(B) Section 1442 (relating to withholding of tax on foreign corporations) is amended by adding at the end thereof the following new sentence: "In the case of amounts described in section 3452(a) (relating to interest), section 3462(a) (relating to dividends), and section 3472(a) (relating to patronage dividends), the tax required to be deducted and withheld under the preceding sentence shall not by reason of the provisions of any treaty be less than 20 percent of such amounts."

(2) **NOMINEES, ETC.**—Subchapter A of chapter 3 (relating to withholding of tax on nonresident aliens and foreign corporations) is amended by adding at the end thereof the following new section:

"**SEC. 1444. INTEREST AND DIVIDENDS PAID TO NOMINEES; CREDITS TO WITHHOLDING AGENTS.**

"(a) **WITHHOLDING OF TAX BY PAYOR.**—Under regulations prescribed by the Secretary or his delegate, every person who pays amounts subject to withholding under chapter 25 and who has been notified by a payee thereof that the payee is a nominee required to deduct and withhold on such amounts under section 1441 or 1442 shall, in lieu of the nominee, deduct and withhold from such amounts paid to the nominee the tax required to be deducted and withheld under section 1441 or 1442, in the same manner as if such amounts were paid by such person directly to the beneficial owner thereof.

"(b) **CREDITS TO WITHHOLDING AGENTS.**—In the case of any person who is required to deduct and withhold tax under section 1441 or 1442 in respect of amounts received by him during any calendar year on which tax was deducted and withheld (or, in the case of amounts described in section 39(c) (1), was treated as deducted and withheld) under chapter 25, the taxes so deducted and withheld (or treated as deducted and withheld) under chapter 25 shall, under regulations prescribed by the Secretary or his delegate, be allowed as a credit against (but not in excess of) his liability for the year in respect of the taxes imposed by sections 1441 and 1442."

(3) **CLERICAL AMENDMENT.**—The table of sections for subchapter A of chapter 3 is amended by adding at the end thereof the following:

"Sec. 1444. Interest and dividends paid to nominees; credits to withholding agents."

(d) **CREDIT FOR STATES AND TAX EXEMPT ORGANIZATIONS.**—

(1) **ALLOWANCE OF CREDIT.**—Chapter 26 (general provisions relating to employment taxes and income tax withheld at source) is amended by adding at the end thereof the following new section:

"Sec. 3505. SPECIAL CREDIT IN CASE OF STATES OR TAX-EXEMPT ORGANIZATIONS."

"(a) **GENERAL RULE.**—In the case of a person which is a State (as defined in section 3490(2)) or which is an organization (other than a cooperative described in section 521) which is exempt from the tax imposed by chapter 1, the tax deducted and withheld under chapter 25 with respect to amounts received by it during any calendar quarter shall be allowed, under regulations prescribed by the Secretary or his delegate, as a credit against (but not in excess of) such person's liability (after the adjustments, if any, provided for in sections 6205(a) and 6413(a)) for such quarter in respect of the taxes imposed by chapter 21 (Federal Insurance Contributions Act) and by chapter 24 (collection of income tax at source on wages). Such credit shall be allowed only if claim therefor is made, in accordance with such regulations, at the time of the filing of the return with respect to the taxes under chapter 21 and chapter 24 for such quarter."

"(b) **OBLIGATIONS SOLD BETWEEN INTEREST-PAYMENT DATES.**—For purposes of this section, in the case of an obligation which is sold or exchanged between interest-payment dates, the amount required to be deducted and withheld on the interest at the end of the interest-payment period shall be treated in the manner provided in section 39(c)."

"(c) **CROSS REFERENCE.**—

"For refund under chapter 25, see section 3485."

(2) **TECHNICAL AMENDMENTS.**—

(A) Section 3502 (relating to nondeductibility of taxes in computing taxable income) is amended by adding at the end thereof the following new subsection:

"(c) The tax deducted and withheld under chapter 25 shall not be allowed as a deduction in computing taxable income under subtitle A either to the person deducting and withholding the tax or to the recipient of the amounts subject to withholding."

(B) The table of sections for chapter 26 is amended by adding at the end thereof the following:

"Sec. 3505. Special credit in case of States or tax exempt organizations."

(c) **OTHER TECHNICAL AMENDMENTS.**—

(1) **DECLARATION OF ESTIMATED INCOME TAX BY INDIVIDUALS.**—Section 6015(a) (relating to declaration of estimated income tax by individuals) is amended by striking out the period at the end of paragraph (2) and inserting in lieu thereof "and amounts on which tax is required to be deducted and withheld under chapter 25."

(2) **ADJUSTMENT OF TAX; UNDERPAYMENT.**—

(A) Subsection (a)(1) of section 6205 (relating to special rules relating to assessment of employment taxes) is amended by striking out "or 3402 is paid with respect to any payment of wages or compensation," and inserting in lieu thereof "3402, 3451, 3461, or 3471 is paid with respect to any payment of remuneration, interest, dividends, or other amounts."

(B) Subsection (b) of such section is amended by striking out "or 3402 is paid or deducted with respect to any payment of

wages or compensation" and inserting in lieu thereof "3402, 3451, 3461, or 3471 is paid or deducted with respect to any payment of remuneration, interest, dividends, or other amounts".

(C) The heading for such section is amended to read as follows:

"Sec. 6205. SPECIAL RULES APPLICABLE TO CERTAIN TAXES UNDER SUBTITLE C."

(D) The table of sections for subchapter A of chapter 63 is amended by striking out "Sec. 6205. Special rules applicable to certain employment taxes."

and inserting in lieu thereof

"Sec. 6205. Special rules applicable to certain taxes under subtitle C."

(3) **USE OF GOVERNMENT DEPOSITARIES.**—Section 6302(c) (relating to use of Government depositaries) is amended by adding at the end thereof the following new sentence: "The Secretary or his delegate shall not require the deposit under this subsection of any tax deducted and withheld under chapter 25 (relating to collection of income tax at source on interest, dividends, and patronage dividends) in a Government depository before the last day prescribed in section 3481 for payment of the tax."

(4) **EXCESSIVE WITHHOLDING.**—Section 6401 (b) (relating to excessive withholding) is amended to read as follows:

"(b) **EXCESSIVE WITHHOLDING.**—If the amounts allowable as credits under section 31 (relating to credit for tax withheld at source under chapter 24) and section 39 (relating to credit for tax withheld on interest, dividends, and patronage dividends under chapter 25) exceed the taxes imposed by chapter 1 against which such credits are allowable, the amount of such excess shall be considered an overpayment."

(5) **ADJUSTMENT OF TAX; OVERPAYMENT.**—

(A) Subsection (a)(1) of section 6413 (relating to special credit and refund rules applicable to certain employment taxes) is amended by striking out "or 3402 is paid with respect to any payment of remuneration," and inserting in lieu thereof "3402, 3451, 3461, or 3471 is paid with respect to any payment of remuneration, interest, dividends, or other amounts."

(B) Subsection (b) of such section is amended—

(i) By striking from the heading of such subsection the words "OF CERTAIN EMPLOYMENT TAXES"; and

(ii) By striking out "or 3402 is paid or deducted with respect to any payment of remuneration" and inserting in lieu thereof "3402, 3451, 3461, or 3471 is paid or deducted with respect to any payment of remuneration, interest, dividends, or other amounts".

(C) The following new subsection is added at the end of such section:

"(c) **CROSS REFERENCES.**—

"For special refunds or credits of tax withheld on interest, dividends, or patronage dividends under chapter 25, see sections 3484, 3485, 3486, 3487, and 3505."

(D) The heading for such section is amended to read as follows:

"Sec. 6413. SPECIAL RULES APPLICABLE TO CERTAIN TAXES UNDER SUBTITLE C."

(E) The table of sections for subchapter B of chapter 65 is amended by striking out "Sec. 6413. Special rules applicable to certain employment taxes."

and inserting in lieu thereof

"Sec. 6413. Special rules applicable to certain taxes under subtitle C."

(6) **OVERPAYMENT NOT DEDUCTED AND WITHHELD.** Section 6414 (relating to income tax withheld) is amended by striking "chapter 3" and inserting in lieu thereof "chapter 3 or 25".

(7) **TIME TAX CONSIDERED PAID.**—Section 6513(b) (relating to time tax considered paid) is amended by adding at the end thereof the following new sentences: "For purposes of section 6511 or 6512, any tax deducted and withheld under chapter 25 which is allowable under section 39, 3484, 3485, or 3486 as a credit against tax or as a refund of an overpayment (or an amount treated as an overpayment) of the tax imposed by chapter 1 shall, in respect of the person entitled to such credit or refund, be deemed to have been paid by him on the last day prescribed for filing the return (determined without regard to any extension of time for filing such return) of tax under chapter 1 for his taxable year in which the amount subject to withholding under chapter 25 is received by him or, if such person has no taxable year, on the fifteenth day of the fifth calendar month following the close of such person's annual accounting period within which such amount is received by him. In the case of an amount allowable as a credit under section 39(b) to the parent of a child, such amount shall, if claimed by the parent, be deemed to have been paid on the last day for filing his return (determined without regard to any extension of time for filing such return) for his taxable year which begins with or within the calendar year in which amounts subject to withholding under chapter 25 were received by the child."

(8) **FAILURE TO PAY ESTIMATED INCOME TAX.**—

(A) **INDIVIDUALS.**—Subsections (c) and (f) of section 6654 (relating to failure by individual to pay estimated income tax) are amended to read as follows:

"(c) **APPLICATION OF SECTION IN CASE OF WITHHELD TAXES.**—For purpose of applying this section—

"(1) the estimated tax shall be computed without any reduction for amounts which the individual estimates as his credits under section 31 (relating to tax withheld at source on wages) and section 39 (relating to tax withheld on interest, dividends, and patronage dividends); and

"(2) the amount of the credits allowed under section 31 and 39 for the taxable year shall be deemed a payment of estimated tax, and an equal part of such amount shall be deemed paid on each installment date (determined under section 6153) for such taxable year unless the taxpayer establishes the dates on which all amounts were actually withheld (or in the case of amounts described in section 39(c)(1), were treated as withheld), in which case the amounts so withheld shall be deemed payments of estimated tax on such dates."

"(f) **TAX COMPUTED AFTER APPLICATION OF CREDITS AGAINST TAX.**—For purposes of subsections (b) and (d), the term "tax" means the tax imposed by chapter 1 reduced by the credits against tax allowed by part IV of subchapter A of chapter 1, other than the credits against tax provided by section 31 (relating to tax withheld on wages) and section 39 (relating to tax withheld on interest, dividends, and patronage dividends)."

(B) **CORPORATIONS.**—Section 6655 (relating to failure by corporation to pay estimated income tax) is amended—

(i) by striking out the period at the end of subsection (e)(2)(B) and inserting in lieu thereof "other than the credit against tax provided by section 39 (relating to tax withheld on interest, dividends, and patronage dividends)"; and

(ii) by redesignating subsection (f) as subsection (g) and inserting after subsection (e) the following new subsection:

"(f) **APPLICATION OF SECTION IN CASE OF TAX WITHHELD ON INTEREST, DIVIDENDS, AND PATRONAGE.**—For purposes of applying this section—

"(1) the estimated tax shall be computed without any reduction for the amount which

the corporation estimates as its credit under section 39 (relating to tax withheld on interest, dividends, and patronage dividends); and

"(2) the amount of the credit allowed under section 39 for the taxable year shall be deemed a payment of estimated tax, and an equal part of such amount shall be deemed paid on each installment date (determined under section 6154) for such taxable year, unless the corporation establishes the dates on which all amounts were actually withheld (or in the case of amount described in section 39(c)(1), were treated as withheld), in which case the amounts so withheld shall be deemed payments of estimated tax on such dates."

(9) **PENALTY FOR FILING FRAUDULENT EXEMPTION CERTIFICATE.**—Section 7205 (relating to fraudulent withholding exemption certificate or failure to supply information) is amended by adding the following new sentence at the end thereof: "Any person who willfully files an exemption certificate with any withholding agent under section 3483, on which the certification is known by him to be fraudulent or to be false as to any material matter, or who is required to file a notice under subsection (a)(3)(B) of section 3483 and who willfully fails to provide such notice in the manner, at the time, and showing the information required under such subsection (a)(3)(B), or the regulations prescribed thereunder, shall, in lieu of any penalty otherwise provided, upon conviction thereof, be fined not more than \$500, or imprisoned not more than 1 year, or both."

(10) **OFFENSES WITH RESPECT TO COLLECTED TAXES.**—The last sentence of section 7215(b) (relating to offenses with respect to collected taxes) is amended to read as follows: "For purposes of paragraph (2), a lack of funds existing immediately after the payment of wages or amounts subject to withholding under chapter 25 (whether or not created by the payment of such wages or amounts) shall not be considered to be circumstances beyond the control of a person."

(11) **DEFINITION OF WITHHOLDING AGENT.**—Section 7701(a)(16) (defining the term "withholding agent") is amended by striking out "or 1461" and inserting in lieu thereof "1461, 3451, 3461, or 3471".

(f) **EFFECTIVE DATES.**—

(1) **GENERAL RULE.**—Except as provided in paragraph (2), the provisions of this section shall apply in the case of interest and dividends paid on or after January 1, 1963.

(2) **SPECIAL RULES.**—

(A) In the case of transferable obligations described in paragraph (1) or (6) of section 3452(a) of the Internal Revenue Code of 1954, the provisions of this section shall apply only to interest paid with respect to interest payment periods commencing on or after January 1, 1963.

(B) The provisions of this section shall apply to amounts described in section 3472 of such Code paid on or after January 1, 1963, with respect to patronage occurring on or after the first day of the first taxable year of the cooperative beginning on or after January 1, 1963.

And, in lieu thereof, to insert:

SEC. 19. REPORTING OF INTEREST, DIVIDEND, AND PATRONAGE DIVIDEND PAYMENTS OF \$10 OR MORE DURING A YEAR.

(a) **RETURNS REGARDING PAYMENT OF DIVIDENDS.**—Section 6042 (relating to returns regarding corporate dividends, earnings, and profits) is amended to read as follows:

"**SEC. 6042. RETURNS REGARDING PAYMENTS OF DIVIDENDS AND CORPORATE EARNINGS AND PROFITS.**

"(a) **REQUIREMENT OF REPORTING.**—

"(1) **IN GENERAL.**—Every person—

"(A) who makes payments of dividends aggregating \$10 or more to any other person during any calendar year, or

"(B) who receives payments of dividends as a nominee and who makes payments aggregating \$10 or more during any calendar year to any other person with respect to the dividends so received,

shall make a return according to the forms or regulations prescribed by the Secretary or his delegate, setting forth the aggregate amount of such payments and the name and address of the person to whom paid.

"(2) **RETURNS REQUIRED BY THE SECRETARY.**—Every person who makes payments of dividends aggregating less than \$10 to any other person during any calendar year shall, when required by the Secretary or his delegate, make a return setting forth the aggregate amount of such payments, and the name and address of the person to whom paid.

"(b) **DIVIDEND DEFINED.**—

"(1) **GENERAL RULE.**—For purposes of this section, the term 'dividend' means—

"(A) any distribution by a corporation which is a dividend (as defined in section 316); and

"(B) any payment made by a stockbroker to any person as a substitute for a dividend (as so defined).

"(2) **EXCEPTIONS.**—For purposes of this section, the term 'dividend' does not include—

"(A) to the extent provided in regulations prescribed by the Secretary or his delegate, any distribution or payment—

"(i) by a foreign corporation, or

"(ii) to a foreign corporation, a nonresident alien, or a partnership not engaged in trade or business in the United States and composed in whole or in part of nonresident aliens; and

"(B) any amount described in section 1373 (relating to undistributed taxable income of electing small business corporations).

"(3) **SPECIAL RULE.**—If the person making any payment described in subsection (a)(1) (A) or (B) is unable to determine the portion of such payment which is a dividend or is paid with respect to a dividend, he shall, for purposes of subsection (a)(1), treat the entire amount of such payment as a dividend or as an amount paid with respect to a dividend.

"(c) **STATEMENTS TO BE FURNISHED TO PERSONS WITH RESPECT TO WHOM INFORMATION IS FURNISHED.**—Every person making a return under subsection (a)(1) shall furnish to each person whose name is set forth in such return a written statement showing—

"(1) the name and address of the person making such return, and

"(2) the aggregate amount of payments to the person as shown on such return. The written statement required under the preceding sentence shall be furnished to the person on or before January 31 of the year following the calendar year for which the return under subsection (a)(1) was made. No statement shall be required to be furnished to any person under this subsection if the aggregate amount of payments to such person as shown on the return made under subsection (a)(1) is less than \$10.

"(d) **STATEMENTS TO BE FURNISHED BY CORPORATIONS TO SECRETARY.**—Every corporation shall, when required by the Secretary or his delegate—

"(1) furnish to the Secretary or his delegate a statement stating the name and address of each shareholder, and the number of shares owned by each shareholder;

"(2) furnish to the Secretary or his delegate a statement of such facts as will enable him to determine the portion of the earnings and profits of the corporation (including gains, profits, and income not taxed) accumulated during such periods as the Secretary or his delegate may specify, which have been distributed or ordered to be distributed, respectively, to its shareholders

during such taxable years as the Secretary or his delegate may specify; and

"(3) furnish to the Secretary or his delegate a statement of its accumulated earnings and profits and the names and addresses of the individuals or shareholders who would be entitled to such accumulated earnings and profits if divided or distributed, and of the amounts that would be payable to each."

(b) **RETURNS REGARDING PAYMENT OF PATRONAGE DIVIDENDS.**—Section 6044 (relating to returns regarding patronage dividends) is amended to read as follows:

"**SEC. 6044. RETURNS REGARDING PAYMENTS OF PATRONAGE DIVIDENDS.**

"(a) **REQUIREMENT OF REPORTING.**—

"(1) **IN GENERAL.**—Except as otherwise provided in this section, every cooperative to which part I of subchapter T of chapter 1 applies, which makes payments of amounts described in subsection (b) aggregating \$10 or more to any person during any calendar year, shall make a return according to the forms or regulations prescribed by the Secretary or his delegate, setting forth the aggregate amount of such payments and the name and address of the person to whom paid.

"(2) **RETURNS REQUIRED BY THE SECRETARY.**—Every such cooperative which makes payments of amounts described in subsection (b) aggregating less than \$10 to any person during any calendar year shall, when required by the Secretary or his delegate, make a return setting forth the aggregate amount of such payments and the name and address of the person to whom paid.

"(b) **AMOUNTS SUBJECT TO REPORTING.**—

"(1) **GENERAL RULE.**—Except as otherwise provided in this section, the amounts subject to reporting under subsection (a) are—

"(A) the amount of any patronage dividend (as defined in section 138(a)) which is paid in money, qualified written notices of allocation (as defined in section 1388(c)), or other property (except nonqualified written notices of allocation as defined in section 1388(d)),

"(B) any amount described in section 1382(c)(2)(A) (relating to certain nonpatronage distributions) which is paid in money, qualified written notices of allocation, or other property (except nonqualified written notices of allocation) by an organization exempt from tax under section 521 (relating to exemption of farmers cooperatives from tax), and

"(C) any amount described in section 1382(b)(2) (relating to redemption of nonqualified written notices of allocation) and, in the case of an organization described in section 1381(a)(1), any amount described in section 1382(c)(2)(B) (relating to redemption of nonqualified written notices of allocation paid with respect to earnings derived from sources other than patronage).

"(2) **EXCEPTIONS.**—The provisions of subsection (a) shall not apply, to the extent provided in regulations prescribed by the Secretary or his delegate, to any payment—

"(A) by a foreign corporation, or

"(B) to a foreign corporation, a nonresident alien, or a partnership not engaged in trade or business in the United States and composed in whole or in part of nonresident aliens.

"(c) **EXEMPTION FOR CERTAIN CONSUMER COOPERATIVES.**—A cooperative which the Secretary or his delegate determines is primarily engaged in selling at retail goods or services of a type that are generally for personal, living, or family use shall, upon application to the Secretary or his delegate, be granted exemption from the reporting requirements imposed by subsection (a). Application for exemption under this subsection shall be made in accordance with regulations prescribed by the Secretary or his delegate.

"(d) DETERMINATION OF AMOUNT PAID.—For purposes of this section, in determining the amount of any payment—

"(1) property (other than a qualified written notice of allocation) shall be taken into account at its fair market value, and

"(2) a qualified written notice of allocation shall be taken into account at its stated dollar amount.

"(e) STATEMENTS TO BE FURNISHED TO PERSONS WITH RESPECT TO WHOM INFORMATION IS FURNISHED.—Every cooperative making a return under subsection (a)(1) shall furnish to each person whose name is set forth in such return a written statement showing—

"(1) the name and address of the cooperative making such return, and

"(2) the aggregate amount of payments to the person as shown on such return.

The written statement required under the preceding sentence shall be furnished to the person on or before January 31 of the year following the calendar year for which the return under subsection (a)(1) was made. No statement shall be required to be furnished to any person under this subsection if the aggregate amount of payments to such person as shown on the return made under subsection (a)(1) is less than \$10."

(c) RETURNS REGARDING PAYMENT OF INTEREST.—Subpart B of part III of subchapter A of chapter 61 (relating to information returns) is amended by adding after section 6047 (as added by section 7(f) of this Act) the following new section:

"SEC. 6048. RETURNS REGARDING PAYMENTS OF INTEREST.

"(a) REQUIREMENT OF REPORTING.—

"(1) IN GENERAL.—Every person—

"(A) who makes payments of interest (as defined in subsection (b)) aggregating \$10 or more to any other person during any calendar year, or

"(B) who receives payments of interest as a nominee and who makes payments aggregating \$10 or more during any calendar year to any other person with respect to the interest so received.

shall make a return according to the forms or regulations prescribed by the Secretary or his delegate, setting forth the aggregate amount of such payments and the name and address of the person to whom paid.

"(2) RETURNS REQUIRED BY THE SECRETARY.—Every person who makes payments of interest (as defined in subsection (b)) aggregating less than \$10 to any other person during any calendar year shall, when required by the Secretary or his delegate, make a return setting forth the aggregate amount of such payments and the name and address of the person to whom paid.

"(3) OTHER RETURNS REQUIRED BY SECRETARY.—Every corporation making payments, regardless of amounts, of interest other than interest as defined in subsection (b) shall, when required by regulations prescribed by the Secretary or his delegate, make a return according to the forms or regulations prescribed by the Secretary or his delegate, setting forth the amount paid and the name and address of the recipient of each such payment.

"(b) INTEREST DEFINED.—

"(1) GENERAL RULE.—For purposes of subsections (a) (1) and (2), the term 'interest' means—

"(A) interest on evidences of indebtedness (including bonds, debentures, notes, and certificates) issued by a corporation in registered form, and, to the extent provided in regulations prescribed by the Secretary or his delegate, interest on other evidences of indebtedness issued by a corporation of a type offered by corporations to the public;

"(B) interest on deposits with persons carrying on the banking business;

"(C) amounts (whether or not designated as interest) paid by a mutual savings bank, savings and loan association, building and

loan association, cooperative bank, home-stead association, credit union, or similar organization, in respect of deposits, investment certificates, or withdrawable or repurchasable shares;

"(D) interest on amounts held by an insurance company under an agreement to pay interest thereon; and

"(E) interest on deposits with stock-brokers and dealers in securities.

"(2) EXCEPTIONS.—For purposes of subsections (a) (1) and (2), the term 'interest' does not include—

"(A) interest on obligations described in section 103(a) (1) or (3) (relating to interest on certain governmental obligations);

"(B) to the extent provided in regulations prescribed by the Secretary or his delegate, any amount paid by or to a foreign corporation, a nonresident alien, or a partnership not engaged in trade or business in the United States and composed in whole or in part of nonresident aliens; and

"(C) any amount on which the person making payment is required to deduct and withhold a tax under section 1451 (relating to tax-free covenant bonds), or would be so required but for section 1451(d) (relating to benefit of personal exemptions).

"(c) STATEMENTS TO BE FURNISHED TO PERSONS WITH RESPECT TO WHOM INFORMATION IS FURNISHED.—Every person making a return under subsection (a)(1) shall furnish to each person whose name is set forth in such return a written statement showing—

"(1) the name and address of the person making such return, and

"(2) the aggregate amount of payments to the person as shown on such return.

The written statement required under the preceding sentence shall be furnished to the person on or before January 31 of the year following the calendar year for which the return under subsection (a)(1) was made. No statement shall be required to be furnished to any person under this subsection if the aggregate amount of payments to such person as shown on the return made under subsection (a)(1) is less than \$10."

(d) PENALTIES FOR FAILURE TO FILE INFORMATION RETURNS.—Section 6652 (relating to failure to file certain information returns) is amended to read as follows:

"SEC. 6652. FAILURE TO FILE CERTAIN INFORMATION RETURNS.

"(a) RETURNS RELATING TO PAYMENTS OF DIVIDENDS, INTEREST, AND PATRONAGE DIVIDENDS.—In the case of each failure to file a statement of the aggregate amount of payments to another person required by section 6042(a)(1) (relating to payments of dividends aggregating \$10 or more), section 6044(a)(1) (relating to payments of patronage dividends aggregating \$10 or more), or section 6048(a)(1) (relating to payments of interest aggregating \$10 or more), on the date prescribed therefor (determined with regard to any extension of time for filing), unless it is shown that such failure is due to reasonable cause and not to willful neglect, there shall be paid (upon notice and demand by the Secretary or his delegate and in the same manner as tax), by the person failing to so file the statement, \$10 for each such statement not so filed, but the total amount imposed on the delinquent person for all such failures during any calendar year shall not exceed \$25,000.

"(b) OTHER RETURNS.—In the case of each failure to file a statement of a payment to another person required under authority of section 6041 (relating to certain information at source), section 6042(a)(2) (relating to payments of dividends aggregating less than \$10), section 6044(a)(2) (relating to payments of patronage dividends aggregating less than \$10), section 6048(a)(2) (relating to payments of interest aggregating less than \$10), section 6048(a)(3) (relating to other payments of interest by corporations), or section 6051 (d) (relating to infor-

mation returns with respect to income tax withheld), on the date prescribed therefor (determined with regard to any extension of time for filing), unless it is shown that such failure is due to reasonable cause and not to willful neglect, there shall be paid (upon notice and demand by the Secretary or his delegate and in the same manner as tax) by the person failing to so file the statement, \$1 for each such statement not so filed, but the total amount imposed on the delinquent person for all such failures during the calendar year shall not exceed \$1,000.

"(c) ALCOHOL AND TOBACCO TAXES.—

"For penalties for failure to file certain information returns with respect to alcohol and tobacco taxes, see generally, subtitle E."

(e) PENALTIES FOR FAILURE TO FURNISH STATEMENTS TO PERSONS WITH RESPECT TO WHOM RETURNS ARE FILED.—Subchapter B of chapter 68 (relating to assessable penalties) is amended by adding after section 6677 (as added by section 7(g) of this Act) the following new section:

"SEC. 6678. FAILURE TO FURNISH CERTAIN STATEMENTS.

"In the case of each failure to furnish a statement under section 6042(c), 6044(e), or section 6048(c) on the date prescribed therefor to a person with respect to whom a return has been made under section 6042(a)(1), 6044(a)(1), or 6048(a)(1), respectively, unless it is shown that such failure is due to reasonable cause and not to willful neglect, there shall be paid (upon notice and demand by the Secretary or his delegate and in the same manner as tax), by the person failing to so furnish the statement, \$10 for each such statement not so furnished, but the total amount imposed on the delinquent person for all such failures during any calendar year shall not exceed \$25,000."

(f) TECHNICAL AMENDMENTS.—Section 6041 (relating to information at source) is amended—

(1) by striking out, in subsection (a) thereof, "(other than payments described in section 6042(1) or section 6045)" and inserting in lieu thereof "(other than payments to which section 6042(a)(1), 6044(a)(1), or 6048(a)(1) applies, and other than payments with respect to which a statement is required under the authority of section 6042(a)(2), 6044(a)(2), 6045, 6048(a)(2), or 6048(a)(3))"; and

(2) by striking out subsection (c) thereof.

(g) CLERICAL AMENDMENTS.—

(1) The table of sections for subpart B of part III of subchapter A of chapter 61 is amended—

(A) by striking out

"Sec. 6042. Returns regarding corporate dividends, earnings, and profits."

and inserting in lieu thereof

"Sec. 6042. Returns regarding payments of dividends and corporate earnings and profits.";

(B) by striking out:

"Sec. 6044. Returns regarding patronage dividends."

and inserting in lieu thereof

"Sec. 6044. Returns regarding payments of patronage dividends.";

and

(C) by adding at the end of such table the following:

"Sec. 6048. Returns regarding payments of interest."

(2) The table of sections for subchapter B of chapter 68 is amended by adding at the end thereof the following:

"Sec. 6678. Failure to furnish certain statements."

(h) EFFECTIVE DATES.—

(1) DIVIDENDS AND INTEREST.—The amendments made by this section shall apply to

payments of dividends and interest made on or after January 1, 1963.

(2) **PATRONAGE DIVIDENDS.**—The amendments made by this section shall apply to payments of amounts described in section 6044(b) of the Internal Revenue Code of 1954 made on or after January 1, 1963, with respect to patronage occurring on or after the first day of the first taxable year of the cooperative beginning on or after January 1, 1963.

Mr. WILLIAMS of Delaware. Mr. President, on this amendment I ask for the yeas and nays.

The yeas and nays were ordered.

Mr. DOUGLAS. Mr. President, a parliamentary inquiry.

The PRESIDING OFFICER. The Senator from Illinois will state it.

Mr. DOUGLAS. Am I correct in understanding that the yeas and nays have been ordered on the committee action in striking out the provision for the withholding of tax on dividends and interest?

The PRESIDING OFFICER. The yeas and nays have been ordered on the committee amendment which strikes out the withholding tax portion of the bill.

Mr. DOUGLAS. I thank the Chair.

Mr. ROBERTSON. Mr. President, I support the action of the committee in striking out the provision to withhold taxes on income from dividends and interest. I am pleased that the Committee on Finance has stricken this provision from the proposed Revenue Act of 1962. As I indicated to the Senate on May 16 of this year, I oppose the dividend and interest withholding provisions of the original legislation. Accordingly, I support the committee action to delete this feature of the bill.

There is no doubt in my mind, as I remarked last May, that the "extension of withholding to cover interest and dividends would not be advisable at this time." Today, I continue to favor the principle of withholding of income taxes on wages and salaries, just as I did with respect to the tax bill of 1943, of which I was a joint author. That legislation inaugurated the 20-percent withholding plan on wages and salaries that I had previously endorsed. Yet, as I said several months ago, I believe that withholding on interest and dividends at this time is impractical, unnecessary, and unwise.

In my earlier remarks I pointed out:

The question now at issue is not whether income from dividends and interest is taxable. This income has been taxable for many years. Nor is there any question about the authority of the Internal Revenue Service to collect taxes, whether on income from dividends, interest, salaries, wages, or other sources. Everyone should pay his fair tax share.

The question now before us relates solely to methods of preventing avoidance of tax on income from dividends and interest. In that respect I see no need at this time for withholding as a solution to the problem.

The net effect of the withholding provision, as I indicated before, would "apply across the board to dividend and interest recipients, without regard to their past record for conscientious and accurate income reporting. Admittedly, the proposal is designed solely to catch

tax evaders. But its sweeping rules apply with equal force to the most conscientious and meticulously careful taxpayers—and, even much worse, to hit persons of small incomes, those who are not taxpayers."

As a matter of principle, withholding on wages and salaries represents a much different matter from withholding on dividends and interest. I remarked earlier:

Withholding on wages and salaries consists of deductions from current income derived from gainful employment. Withholding on dividends and interest potentially covers a much wider spectrum of the population, by including recipients who may or may not be gainfully employed. It is one thing to withhold from income derived from rendering current services. It is another thing to withhold income derived as a return on capital saved from the rendering of past services.

In another respect, the proposal to withhold on dividends and interest is not identical to our present withholding system on wages and salaries. I stated previously:

Wage withholding was a collection technique and a necessary step in placing income tax collections on a current basis. This dividend and interest withholding proposal appears to be designed simply as a weapon to catch nonreporters of taxes, and it would operate by treating every dividend and interest recipient as though he were a tax evader. This is repugnant to the traditions of our income tax as a self-assessing system.

The isolated cases of under-reporting or nonreporting, I believe, do not of themselves justify the need for withholding. Instances of fraud and mistake, as I said before, are unfortunately like to occur no matter what the method of revenue collection may be.

Generally, under-reporting or non-reporting of taxable interest and dividend income suggest, as I declared earlier, "the need for more intensive public efforts to inform responsible taxpayers who are not yet completely aware that interest and dividends should be fully reported."

In that respect, I am pleased that the Senate Finance Committee adopted an amendment which I endorsed in my remarks of May 16. This amendment would require payers of dividends, interest, and patronage dividends to report to the Treasury all payments of \$10 or more a year.

As I indicated before in recommending such a requirement:

Another step which I believe worthy of consideration would require designated payers of interest to report to the Treasury all interest payments as low as some minimum amount such as \$50 or \$10.

That is what I said last May; and now the committee has put that provision into the bill.

I also said:

This would extend reporting coverage to include substantially all recipients of income from dividends and interest. Dividend payments of \$10 or more and interest payments of \$600 or more are reported currently to the Treasury. With the computers and office machines now available, I am confident that when the taxpayer account number system goes into effect, all these re-

ports can be assembled and classified readily and simply, and at relatively little expense.

I support, therefore, the committee's amendment as set forth in section 19 of the bill. It would make mandatory all reporting to the Treasury of cash or credited dividend, interest, or patronage dividend payments of \$10 or more a year made on or after January 1, 1963; under present law, reporting in some cases is required only at the discretion of the Treasury. The amendment would require a uniform statutory reporting minimum of \$10; now, the statutory or administratively determined minimum varies from \$10 in the case of most dividend payments to \$600 in the case of interest payments. The amendment would also require by statute that annual statements must be submitted to all recipients of such payments of \$10 or more a year; under present regulations, reports only of dividends must be made to recipients as well as to the Treasury.

Stepped up reporting of dividends, interest, and patronage dividends should greatly increase the ability of the Treasury to collect all taxes payable on income from these sources. During the first full year that this requirement is operative, the staff of the Joint Committee on Internal Revenue Taxation has estimated that it would result in a \$275 million increase in revenue. More conservative estimates, made by the Treasury, are somewhat lower. I believe, however, that once the reporting requirement has been put fully into effect, and once automatic data processing enables information returns and tax returns to be matched readily, the revenue effect of this reporting requirement could be considerably larger.

Steps such as these toward publicizing dividend and interest payments and toward informing the public about its tax liabilities on such payments seem to me to be the proper approach. Withholding, on the contrary, would do just the opposite. As I pointed out several months ago, it would involve "virtually no reporting requirements imposed upon the withholding agents." The impracticality of the proposed withholding plan seems clear. I stated last May:

Under the plan, persons withholding 20 percent from interest and dividend payments would not be required to give to the recipients of these payments any receipts or notices whatsoever of the amounts withheld from them. Furthermore, the withholding agents would not even be required to report to the Revenue Service the amounts withheld from each individual. Instead, they would merely report to the Government the gross amount withheld from everyone in the aggregate, leaving both the payees and the Revenue Service without a record of the amount withheld from each person.

Since the withholding proposal would not require detailed reports and records, it would tend to encourage fraudulent claims against the Treasury for over-withholding and for improper refund claims. I said last May:

I do not see anything in the withholding mechanism which would permit a dividend or interest recipient to meet the burden of proof of establishing the amount withheld, if he has a tax dispute in court. Such a sys-

tem would have no relationship to the wage withholding system, in which the withholding agent is required to furnish both the employee and the Government with a copy of the form W-2 showing the amount of the compensation and the amount of the tax withheld from it.

A further objection to the proposed withholding plan is that not all types of interest payments would be subject to withholding tax. Payments of interest on personal loans and on home mortgages, for example, would be excluded. The confusion arising about what dividends and interest payments had been withheld on, and about what payments had not been withheld on, would undoubtedly be considerable. In many cases, persons entitled to refunds might have a hard time finding out how much they paid or what was due them. The Internal Revenue Service, lacking any detailed information for each withholding transaction, might have equal difficulty in verifying claims for refunds.

In conclusion, Mr. President, I reiterate my opposition to withholding on dividends and interest at this time. I declared on May 16, in summarizing my remarks:

I am convinced that we need a more comprehensive effort to inform taxpayers of their liabilities under the present tax laws. Such an effort would, I think, result in greatly increased tax collections. The widespread conviction among taxpayers that withholding on interest and dividends would represent a new tax imposed for the first time is, to my way of thinking, clear evidence of the need for giving more information to taxpayers.

It seems to me quite clear that we will collect virtually all of the taxes due on interest and dividends if we can give clear and complete information to the taxpayers. I believe we should make every effort to do this before we engage in a new withholding program on interest and dividends with all the redtape, all the expense, all the refunds, all the trouble, and all the economic disadvantages which this withholding program would involve.

There is no doubt in my mind that everyone should pay his fair tax share. I am in favor of collecting taxes on dividends and interest, as well as on every other sort of income.

But, Mr. President, a provision to impose withholding on dividends and interest at this time seems unworkable, unneeded, and unsound.

Mr. DOUGLAS. Mr. President, I suggest the absence of a quorum.

The PRESIDING OFFICER. The clerk will call the roll.

The legislative clerk proceeded to call the roll.

Mr. SMATHERS. Mr. President, I ask unanimous consent that the order for the quorum call be rescinded.

The PRESIDING OFFICER. Without objection, it is so ordered.

RESIGNATION OF ASSOCIATE JUSTICE FRANKFURTER AND APPOINTMENT OF ARTHUR J. GOLDBERG TO SUPREME COURT OF THE UNITED STATES

Mr. DOUGLAS. Mr. President, a few moments ago the President of the United States announced that Mr. Justice Frankfurter had resigned from the U.S.

Supreme Court, and that he was appointing the Secretary of Labor, Hon. Arthur J. Goldberg, to fill the vacancy.

I think this is a magnificent appointment. I have known Mr. Goldberg for 30 years.

He is held in high esteem by all groups in Illinois. He has made a magnificent record as Secretary of Labor. He has shown that not only is he an able and competent lawyer, but that he is impartial in his judgments. I think the Supreme Court has had a most worthy replacement for Mr. Justice Frankfurter.

As the senior Senator from Illinois, as a long time personal friend of Secretary Goldberg, and as an admirer of President Kennedy, I say that this appointment does the administration great credit. I hope and believe that the nomination will be ratified by the Senate, and I predict for Mr. Goldberg a great career on the Supreme Court of the United States.

Mr. PASTORE. Mr. President, will the Senator yield?

Mr. DOUGLAS. I yield.

Mr. PASTORE. I associate myself with the glowing remarks of the Senator from Illinois. They are well deserved. It has been my privilege and honor to have had frequent contacts with Mr. Goldberg. I have always viewed him to be a man of sterling character, integrity, and wisdom. He will be a fine addition to the Court.

I wish for him and his family many years of success and happiness.

Mr. SMATHERS. Mr. President, will the Senator yield?

Mr. DOUGLAS. I yield.

Mr. SMATHERS. I associate myself with the remarks of the Senator from Illinois with respect to the new appointment. It has been my happy privilege to know Secretary Goldberg very well during the past year and a half. I have been greatly impressed with his ability, objectivity, energy, and fairness. I cannot help believing that he will be a fine addition to the Supreme Court, and I congratulate him and his family.

Mr. DOUGLAS. Mr. President, I ask unanimous consent that the Senator from Vermont [Mr. AIKEN] may be recognized for 2 minutes with the understanding that his remarks will appear at the end of my statement.

The PRESIDING OFFICER. Is there objection to the request of the Senator from Illinois? The Chair hears none, and it is so ordered.

Mr. AIKEN. Mr. President, once in a while our country enjoys a real bit of good fortune. In reading the ticker this afternoon I think today is one of our lucky days. I read that President Kennedy has announced his intention to appoint Arthur Goldberg to the Supreme Court to succeed the illustrious Justice Frankfurter, who is retiring.

In my opinion, Arthur Goldberg is one of the most conscientious public servants that our country has had. He is an able lawyer, devoted to his country, and a squareshooter all around. He will make a worthy successor to the great Justice Felix Frankfurter, who has had such a long and meritorious career on our Supreme Court. I know that Arthur Goldberg as a Justice of the Supreme Court

will make a record of which we will all be proud.

I wish to take this occasion to extend to Arthur and to his wife Dorothy all the good things of life that they both so richly deserve.

Mr. CARROLL. Mr. President, will the Senator yield?

Mr. HART. Mr. President, will the Senator yield?

Mr. DOUGLAS. Mr. President, I yield to the Senator from Michigan, with the understanding that the remarks of the Senator will follow those of the Senator from Vermont and will be subsequent to my comments.

Mr. AIKEN. I was going to have my remarks segregated somewhat from the discussion on the pending bill.

Mr. CARROLL. Mr. President, will the Senator yield?

Mr. AIKEN. I apologize for using the word "segregated," but I could not think of another one.

Mr. CARROLL. Mr. President, will the Senator yield?

Mr. AIKEN. If I have the floor, I shall yield.

The PRESIDING OFFICER. The Senator from Illinois had yielded to the Senator from Vermont. Has the Senator from Vermont completed his discussion?

Mr. AIKEN. I have completed my statement.

Mr. HART. Mr. President, will the Senator from Illinois yield?

The PRESIDING OFFICER. To whom does the Senator from Illinois yield?

Mr. DOUGLAS. I do not believe the Senator from Vermont has finished his statement.

Mr. AIKEN. I had finished the statement. I had not taken my seat. If I am permitted to yield to the Senator from Colorado [Mr. CARROLL] or the Senator from Michigan [Mr. HART], I shall be glad to do so. Without objection, I will yield to the Senator from Colorado.

The PRESIDING OFFICER. Without objection, the Senator from Vermont yields to the Senator from Colorado.

Mr. CARROLL. Mr. President, I commend the able Senator from Vermont for a very fine statement. I desire to associate myself with his remarks. As a member of the Senate Committee on the Judiciary I listened very carefully to the President's press conference today. Of course, I have the highest regard for Justice Frankfurter, who has served his country long and well in a most distinguished and learned career. I thought the President's selection of Arthur Goldberg was outstanding. I know him personally. I have observed him as a lawyer, as an administrator, as a public servant. He has appeared before the Senate Committee on the Judiciary on several important occasions. I have followed his work as Secretary of Labor. His character, his public service, his ability, his integrity, his knowledge of the Constitution and the history of America commands the respect of the American people. He is a distinguished lawyer. I know he will do the excellent work that we all expect of him on the Supreme Court.

I thank the Senator from Vermont for his very fine remarks.

Mr. HART. Mr. President, whoever has the floor, I wish he would yield to me.

Mr. AIKEN. Without objection, I yield to the Senator from Michigan.

Mr. HART. Mr. President, the Senator from Vermont and the Senator from Colorado quite properly have responded to the announcement made by the President with respect to the appointment of Arthur Goldberg to the Supreme Court. I share the sentiments expressed by both Senators. I have a very deep conviction that as the record of that Court is written in the generations ahead, a very brilliant chapter will analyze the service on that Court by Arthur Goldberg.

Very little can be added to what I thought was the moving expression by the Senator from Vermont. Yet I believe that the resignation of Justice Frankfurter and the appointment of Arthur Goldberg should remind us that controversy is not foreign to the life of the Supreme Court. In recent years we have been inclined to think that for the first time it has become the center of controversy, and that if that is wrong, someone is at fault.

I am not quite old enough to remember vividly when Justice Frankfurter was nominated to the Supreme Court. However, I have read some of the comments that then were made. I remember some of the predictions on the course he would take on the bench. We know now that those predictions were wrong. Labels were applied to him then which are the reverse of the labels that have been applied now.

In making the appointment, the President has been properly guided by the ultimate assumption that the courts shall be available to each and all, and that in filling a vacancy on the Court, the President is not looking for a man who will consider it the duty of the Court to stamp automatically with approval every prior and earlier decision. Certainly that helps to insure justice, but it does not insure justice. Sometimes, with the passage of time, what appeared to be just and right in one generation later proved to be wrong in another generation.

I believe that Arthur Goldberg will be sensitive to both of these aspects of his Court role. As one member of the Judiciary Committee I shall be glad to give the Senator from Colorado [Mr. CARROLL] an opportunity to affirmatively vote for the confirmation of the nomination.

Mr. AIKEN. I wish not only to thank the Senator from Illinois [Mr. DOUGLAS] for yielding the time, and to say that the yielding has been worth while, but also to congratulate him on having such an able and distinguished constituent that the President has seen fit to choose Arthur Goldberg of Illinois to sit on the Supreme Court of the United States.

Mr. DOUGLAS. I thank the Senator from Vermont and the Senator from Michigan. This is one of those rare occasions when it is delightful to be interrupted in one's speech. Earlier this

afternoon I had the pleasure of making the announcement that the President had appointed Mr. Goldberg, and expressing to the Senate my great pride in him as an individual, and my great pride in the President of the United States.

Since I am in a yielding and forgiving mood, I will be glad to yield to the Senator from Ohio, who, I believe, wishes to present an amendment. I do so with the understanding that all of these interruptions will be printed at the conclusion of my remarks.

The PRESIDING OFFICER. Without objection it is so ordered.

SUBSIDIZATION OF MASS TRANSPORTATION SYSTEMS

Mr. LAUSCHE. Mr. President, pending on the calendar is a bill which contemplates the authorization of \$500 million in grants over a period of 3 years as a subsidization to local governmentally operated mass transportation systems. That bill, while it deals substantially with commerce, was referred to the Banking and Currency Committee for consideration, and not to the Commerce Committee, where it properly belonged.

About a half-hour ago I had a talk with the chairman of the Commerce Committee, the Senator from Washington [Mr. MAGNUSON], telling him that I contemplated, if and when the bill is called up for consideration, moving that the bill be sent to the Commerce Committee for its attention and consideration.

The Senator from Washington—not only today, but also when the bill was sent to the Banking and Currency Committee—agreed with the Senator from Ohio that the bill deals primarily with subjects which are within the jurisdiction of the Commerce Committee.

The bill, as is known by Members of the Senate, contemplates making available \$500 million as a subsidy to local governmentally operated transportation systems. The \$500 million is a mere drop in the bucket of what the final cost will be if there is to be a subsidization to practically 1,300 privately and governmentally owned systems.

If that whole gamut of operations is to be covered—and in my opinion the ultimate result of the provisions will mean that all of them will have to be subsidized—in my judgment the amount needed will be not \$500 million, but probably \$12 to \$15 billion.

Mr. President, the subject of which I speak is pertinent in connection with the general subject of discussion that has been taking place on the tax bill. It will be more pertinent when the tax bill of next year comes before the Senate. It will be pertinent because it foretells the complications that are to come when we decrease taxes but increase spending. Probably a dozen bills that are contemplated for consideration and that are pending entail expenditures in a sum, when placed face to face with the purpose of reducing taxes, which in the end will be calamitous to our whole system.

I make this statement so that the Senate will know in advance that when the new subsidy bill comes before this body,

I shall ask that we abide by the rules and send the bill to the committee which, under the rules, legitimately has jurisdiction of it.

I yield the floor.

REVENUE ACT OF 1962

The Senate resumed the consideration of the bill (H.R. 10650) to amend the Internal Revenue Code of 1954 to provide a credit for investment in certain depreciable property, to eliminate certain defects and inequities, and for other purposes.

Mr. SMATHERS. Mr. President, I suggest the absence of a quorum.

The PRESIDING OFFICER (Mr. BURDICK in the chair). The clerk will call the roll.

The legislative clerk proceeded to call the roll.

Mr. SMATHERS. Mr. President, I ask unanimous consent that the order for the quorum call be rescinded.

The PRESIDING OFFICER. Without objection, it is so ordered.

Mr. SMATHERS. Mr. President, I rise in support of the committee amendment to substitute for withholding on dividends and interest a requirement for the reporting of dividend and interest payments.

As a member of the Senate Finance Committee which considered this proposal, and as one who has listened to thousands of words of testimony and received thousands of letters from constituents, I have found few individuals or organizations expressing any sentiment in favor of it.

I recognize, of course, that we must find a way which will enable the Treasury Department to collect all of the tax revenue due from these taxpayers.

Certainly, I would not favor the continuation of the existing situation in which the Treasury Department tells us that there is some \$850 million to a billion dollars of tax due in the case of dividends and interest which presently is not being paid.

I agree that we must find a way to insure the payment of tax due on these dividends and interest. I do not believe it has been demonstrated, however, that withholding is the best procedure for assuring the collection of this tax.

Withholding has been presented to us as a simple and effective procedure for collecting the tax due on dividends and interest. The facts, however, do not bear this out. The statutory language included in the House bill which deals with withholding itself covers nearly 50 pages. But this is not the major consideration. The major consideration is the effect of a withholding tax law on the taxpaying public, on the businesses and banks paying dividends and interest to their savers and shareholders, and the administrative burdens imposed on the Internal Revenue Service.

First, let us look at it from the standpoint of the individuals receiving dividend and interest payments. A 20-percent withholding rate, as provided by the House bill, would be very burdensome to many taxpayers. This is indicated by the fact, which is substantiated by the

Internal Revenue Service, that the average effective tax rate on adjusted gross income of those paying tax is 13.3 percent. This means, right to begin with, that a withholding rate of 20 percent for the average taxpayers means "over-withholding" to the extent of 6.7 percentage points. This is inevitable in a withholding system which does not take into account personal exemptions, itemized deductions, nor even the standard deduction, the retirement income credit, or the special exemption for the aged.

The House bill itself recognized that a flat 20-percent withholding would be too burdensome, and, therefore, provided an exemption certificate system.

This exemption certificate system, however, was much more limited in its application than is generally understood. It would be available for all individuals under age 18, but for those 18 or over the exemption certificates could be used only by those who are willing to certify before the beginning of the year that they do not expect to have any tax liability—I emphasize the words "any tax liability."

Those who expected to have \$1 of tax liability, even though withholding exceeds by many times the amount of that tax liability, nevertheless would not be eligible to file exemption certificates.

Moreover, even those who are eligible to file exemption certificates under the House bill would have to file a separate certificate each year for each separate bank account or shareholding or patronage dividend even though the amount of income involved was only \$5 or, for that matter, only 5 cents.

In many cases the Government would be unjustly enriched in these situations because the taxpayers, when the amounts were small, would be likely to neglect to file either the exemption certificates or to claim a refund at the end of the year.

For taxpayers with any tax liability, the quarterly refund was the only procedure provided by the House bill to restore overwithheld amounts before the end of the year.

This still would deprive the taxpayer of the use of his own funds for at least a portion of the year. It also would present him with the nuisance and worry of having to file a quarterly refund claim.

Only one refund claim could be filed by the taxpayer during any quarter. As a result, if he received dividend or interest income from more than one source and this income was paid to him at different times during the quarter, he would have to wait until after the receipt of the last income during the quarter before filing the refund claim—if he hoped to receive a refund with respect to this amount at that time.

As a result, if a taxpayer received income both early and late in the quarter, he would be deprived of the use of 20 percent of at least part of this income received for the entire 3-month period.

In addition, a period of time would elapse after the refund claim was filed before the Government returned the money to the taxpayer.

The Treasury Department has said that this could be done in 3 or 4 weeks.

Personally, I would be inclined to doubt whether in practice it would actually be quite this soon. In any case, this can mean that the taxpayer would be deprived of the use of his own funds for a period of up to approximately 4 months. This, of course, could reoccur each quarter with respect to the income received in that quarter. As a result of this, the proposed withholding system would deprive taxpayers of the use of their own funds for living expenses for an average period of up to 4 months, or deprive them of the investment return on the average for up to the same 4-month period.

I should also point out that since for the fourth quarter of the year the regular refund provision would not be available, the taxpayer would have to claim the refund for this quarter on his regular tax return. The delay in this case might be still longer than I have indicated. This would be likely, because it probably would require additional time for the taxpayer to prepare his regular tax return since he would have to wait for his W-2 withholding slip from his employer—which probably would be well along in January—before filing his return.

The worry and concern involved in filing this quarterly refund claim for the small taxpayer can hardly be imagined. Filing an annual tax return is something he has gradually become accustomed to over a long period of time. In any case, the quarterly refund claim would be quite new to him.

On this he would have to list his exemptions and any retirement income credit he expects. Next, he would have to subtract any nondividend or non-interest income he received. Then, for what would certainly appear to be an unknown reason to him, he would have to multiply what was left after this subtraction by 22 percent. Next he would have to list any dividend and interest income he received during the quarter, and determine 20 percent of this amount. The result then would be subtracted from the previous computation. While this would be all of the computing the taxpayer would have to do in the first quarter, if there were changes in the subsequent quarters he would have to go through the computations again and take into account, in addition to all that I have already mentioned, the amounts which had been refunded in prior quarters.

Another area of complexity for the taxpayer would be in filing his regular tax return. The complexity here involves the so-called gross-up procedure. This is the procedure whereby the taxpayer would be required to enter on his tax return the net interest or dividends received and then to increase this amount by one-fourth. Taxpayers would have difficulty in understanding why they should report more dividend or interest income than they received.

In addition, the instructions with the tax return would have to have detailed information indicating that some dividends and interest should be grossed-up while others should not be.

This would make it necessary to have separate boxes on the tax return for dividends to be grossed up and dividends not to be grossed up, and for interest to be grossed up and for interest not to be grossed up.

Next, the taxpayer would have to figure out into which of the particular boxes he should place the type of interest or dividend income which he received. Interest income received from other individuals, for example, he would enter in the box where no gross-up was to be provided. Similarly, dividend income received from foreign corporations would go in the box where no gross-up was to apply. Moreover, if he erred and got such dividends or interest in the wrong box on his return, there would be a windfall gain for the Government.

I believe it is abundantly clear that the exemption certificate and refund procedure that I have outlined above would be complicated.

These procedures would be sufficiently complicated to the point that those with small accounts would be unlikely to go to the bother of obtaining the necessary information to get their money back when no tax was owed.

It has been estimated that there are 79 million savings accounts in the Nation on which less than \$5 would be withheld each year. This is wholly apart from the school savings accounts which would be specifically exempted from the House withholding provision.

It is quite likely that in a large proportion of these cases no tax would be due, but because of the complexity in obtaining an exemption certificate or quarterly refund the taxpayer would fail to get back the withheld amount due him. As a result, the Treasury would obtain a windfall gain and the taxpayers would suffer a windfall loss.

Still another problem presented for the taxpayer by the withholding provisions is the fact that the withholding system would interfere with the taxpayer's choice as to which funds he would accumulate and as to which funds he would use to pay his taxes.

Many individuals have embarked on planned savings programs whereby they intend to accumulate a certain fund of capital for a particular purpose such as retirement, a college education for their children, or for some other special purpose.

To accomplish this purpose they plan to set aside a given amount of money periodically so that at a given time this accumulation will reach a predetermined amount. Included in their calculation is a compounding of the dividend and interest income.

Moreover, some specialized funds are set up in such a manner as to make such an accumulation a permanent feature of their plan.

By withholding on dividends and interest, we would prevent the taxpayer from using his discretion in paying taxes due out of other funds such as current income. In this way, the withholding provision would penalize the saver with a planned saving program.

The scope of the problem for the payors of dividends and interest is indicated

by the number of the various types of accounts or stock on which there would be withholding.

Savings and loan associations in 1961 had over 32 million savings accounts. Mutual savings banks had nearly 23 million such accounts. Credit unions have 12 million more. Commercial banks account for 62 million more savings accounts, and postal savings slightly over a million additional. In all, it has been estimated that there are some 130 million savings accounts in the Nation.

In addition, the House provision calls for withholding on policyholder dividends which are left to accumulate with the insurance companies. The House provision also applies to dividends of various corporations. There are 118 million policyholders in insurance companies, a large proportion of which undoubtedly will accumulate policyholder dividends. In the case of corporations generally, there are some 17 million shareholders in the country.

At the present time the relationship between these savers and stockholders and the payors frequently is an impersonal one, and the contact of the payors with these recipients of dividends and interest frequently is handled solely or primarily by the mails.

A withholding tax and the accompanying exemption certificates would force these payors into a much more extensive and elaborate correspondence, or contact with their savers and shareholders to inform them of the withholding tax, to answer their particular questions as to how it works in individual cases, and then to find out whether they wish to file an exemption certificate and to explain to them how this works.

The initial burden for the payors is an exceedingly heavy one, because in reality the payors, in order to keep their customers, must explain to them how the system works, and educate them as to how to claim quarterly refunds or file exemption certificates. This is not solely a one-shot proposition, however, as the exemption certificates, under the House bill, are annual, which will require a renewal of these contacts or correspondence each year.

In addition to this educational problem with interest and dividend recipients, the payors must also classify their savers or stockholders according to the circumstances surrounding their exemption or absence of exemption from withholding.

Since most payors of dividends and interest classify their accounts or stockholders on an alphabetical or numerical basis, this new classification will change almost completely the procedure they use. It will not be limited merely to two categories, those exempt and those not exempt.

The types of accounts will have to be segregated and placed under separate controls and at least include the following categories:

First. Accounts of individuals under 17 for which exemption certificates have been filed. A separate classification is needed in this case since these certificates expire automatically in the calen-

dar year in which the individual reaches the age of 18.

Second. Individuals over 17 for whom temporary exemption certificates have been filed.

Third. Accounts for tax-exempt organizations.

Fourth. School savings accounts, since these are nonsubject to withholding.

Fifth. Accounts of States, municipalities, their agencies and instrumentalities.

Sixth. Accounts of nonresident aliens. As under existing law these accounts may have to be subdivided according to treaty rate in each case.

Seventh. All other accounts.

Additional problems will arise for the payors in their handling of trust accounts. The House withholding provision is silent as to the manner in which these accounts are to be handled thereby, apparently precluding the filing of exemption certificates in their case. Yet the beneficiary in any of these accounts might be a person who would otherwise qualify for the filing of an exemption certificate.

The administration of the proposed system of withholding on dividends and interest would be far from simple for the Internal Revenue Service.

The educational program which will have to be carried on by the payors must also be shared with the employees of the Internal Revenue Service. They, too, will be called upon in thousands of cases to explain why an individual is receiving 20 percent less than the amount expected, should the withholding provision be adopted.

The Internal Revenue Service would also be faced with the necessity of developing a new program for handling the quarterly refunds. It would undoubtedly require an entirely new and distinct unit in the Internal Revenue Service to handle these special refunds.

The Internal Revenue Service would also find its auditing problem considerably increased or else put up with numerous opportunities for tax avoidance. It would be required to follow through on the exemption certificates, in a large number of cases to make sure that the individuals involved really had no tax liability. Not to do so would be an invitation to file these exemption certificates even though tax was due. It would have to carefully check the returns of those who claimed quarterly refunds to make sure that the interest and dividend refunds were actually attributable to dividends or interest received.

Another check would be necessary to make sure that these refunds are properly reported on the final tax returns. A still further check would be necessary to be sure that there is no overlapping of the filing of exemption certificates with the claiming of quarterly refunds.

Frequently the statement is made "We have withholding on salaries and wages, why are dividends and interest recipients so much better that there should not be withholding on them?" There are, however, many differences which make a withholding system much less practical in the case of dividends and interest.

In the case of wage and salary withholding, it is possible to calculate quite closely the actual amount of tax owed by the individual involved. Here it is possible to take into account the number of his exemptions, as well as the 10-percent standard deduction.

On the other hand, the 20-percent withholding for interest and dividends provided by the House bill makes no allowance for exemptions and no allowance for the standard deduction. In the case of dividends received it makes no allowance for the 4-percent credit or the \$50 exclusion. In addition, the 20-percent rate itself is substantially over the average effective rate applying to individuals generally.

In the case of wage and salary withholding, the taxpayer normally deals with only one employer, with whom he comes in frequent contact, either directly or with the employer's agent.

In the case of dividends and interest, the recipient may deal with numerous corporations with which he never comes in contact, except through the mails.

Though the wage and salary withholding requires a large and complex collection system, the revenue yield of some \$20 billion makes it more practical compared to setting up a similar but more complicated method where the aggregate amount involved would be less than one-twentieth of this amount.

The Finance Committee, for reasons such as those that I have outlined—and there are many others which I presume will be gone into later on in the debate—abandoned the idea of the withholding system and substituted procedures for improved dividend and interest reporting.

The committee amendment requires payors of dividends and interest to report both to the Internal Revenue Service and to the taxpayers receiving dividends and interest from any payor of \$10 or more.

At the present time, payors of dividends report this information to the Treasury but most of them do not do so on an annual basis and no copies of this information are required to be sent to the taxpayer although it is understood that some do so on a voluntary basis.

In the case of interest no report is made to the Treasury unless the amount involved exceeds \$600 per year per payor.

I am convinced that requiring reporting to the Internal Revenue Service of all dividend and interest payments of \$10 or more, coupled with the requirement that this information also be presented to the taxpayer on an annual basis, will result in an immediate substantial increase in collecting the tax due on dividends and interest. In the long run, as the Internal Revenue Service automatic data processing system becomes effective, it should result in the collection of substantially as much as a withholding system.

On that point I should like to add that this morning's issue of the Wall Street Journal contained a story, apparently issued by the Internal Revenue Service, that the Service is rapidly installing and

putting into effect the system of numbering accounts. Once the numbered account system is in operation, under the law the Internal Revenue Service would require the information to go out to the recipients of dividends and interest. When that program has been finally completed, which we believe will be within a year or 18 months, we believe the money due and owing to the Government will be paid.

One point should be made abundantly clear, and that is that the average taxpayer is honest and wants to report all income received for tax purposes.

I am not one of those who believe that all the savers and interest receivers and all dividend receivers in my State or for that matter any other State, are crooks. I believe that in most instances those people would be willing to pay their taxes, but that the truth of the matter is they have not realized that they are supposed to pay a tax on some of their accumulations, particularly in savings accounts, when only \$5 or \$6 in interest is added in their passbook possibly on a yearly basis. I do not believe those people are willful tax dodgers. I believe that if they knew that they were supposed to pay a tax on their accumulations in most instances they would pay the tax.

I believe that the notification system would bring about this information on the part of the recipients of dividends and interest payments and that they in turn will then make the payments which are due and owing. Certainly with the system of notification and the processing of the numbering system, the IBM machines would be able to pick out very quickly the few persons who have received payments of dividends and interest and who have not reported them on their tax returns. It would be very easy to ascertain who has not paid his tax when we get this system working, and we expect that it will be working within the next year or 18 months.

The main reason why interest and dividends are not reported as income in the majority of cases is because of the fact that the taxpayer did not know this should be done. These individuals

are not tax dodgers or tax evaders. If they had known that under our complex tax system they should have reported all interest and dividends received as income they would have done so. With the reporting system, as recommended by the Finance Committee, placed in effect this, in my opinion, will provide an effective means of making sure that all taxpayers report taxable income from whatever source received.

Let me list a few of the reasons why the reporting system will accomplish this objective:

First. In many instances the taxpayer does not know the actual amount of interest paid or credited to his account. Obviously, if the taxpayer does not know how much interest he has received, he cannot be at all accurate in reporting this income on his tax return. In the case of most savers, the dividends or interest which they earn on their account is not paid to them in cash, but rather is credited to their account balance. The only way a saver knows the exact amount of his interest or dividend income is to have this amount credited to his passbook. In the case of a substantial number of savers, passbooks are not presented to the financial institution for such crediting early enough in the year to provide them with this information. By sending form 1099 to these savers, this problem will be overcome and savers will be fully and properly informed as to the amount of dividends and interest credited to their accounts.

Second. Many savers and investors who do receive dividends and interest by check are not accustomed to maintaining accurate records regarding this type of income. Consequently, they may have forgotten the amount they received by the time they file their tax returns. By sending taxpayers form 1099, this problem will be eliminated.

Third. Treasury officials admit that ignorance on the part of the taxpayer that dividend and interest income is subject to Federal income tax has been a major contributing factor to the under-reporting. When corporations send this taxpayer an official income tax form stating the amount which he has received

during the previous year and emphasizing the fact that this income is subject to tax and should be included as such in his tax return, this problem will be overcome.

Fourth. The saver or investor who in the past has deliberately failed to report his dividend and interest income no longer will be inclined to do so now that he knows that the Treasury has been notified as to the amount of this type of income that he has received.

The fact that there is a considerably higher percentage of corporate dividends reported on individual income tax returns than interest payments—92 percent versus 73 percent of the payments attributable to taxable individuals—undoubtedly is due to the fact that these individuals know the amount of their corporate dividends and know that the Treasury has been informed. By reducing the level of interest reporting from \$600 to \$10, it is only logical to assume that reporting of interest income will increase considerably.

It is clear that the installation of automatic data processing equipment, the tax numbering system, and an improved system for dividend and interest reporting can result in the virtual elimination of the loss of revenue resulting from the nonpayment of tax on dividend and interest income.

Let us not abandon these tools which are available and in their place hang the millstone of withholding around the neck of the American taxpayer. On four previous occasions the Senate has defeated this withholding proposal.

In my judgment and the judgment of the majority of the members of the Committee on Finance, and I believe it will be the judgment of the Senate again, this so-called withholding of interest and dividends proposal should be defeated.

Mr. President, I ask unanimous consent to have printed in the RECORD at this point copies of the various complex forms, prepared by the Treasury Department, which would be used if the withholding provision were adopted.

There being no objection, the forms were ordered to be printed in the RECORD, as follows:

Exemption certificate, form No. 1

PROPOSED FORM	U.S. Treasury Department—Internal Revenue Service EXEMPTION CERTIFICATE FROM WITHHOLDING ON DIVIDENDS AND INTEREST File with payor named below. (See instructions on reverse side)	1. Identification Number (See instructions) 514-91-2078
2. TO: Name of Dividend or Interest Payor Anytown Bank Address (number and street) 1412 Main Street city, town, or post office zone State Anytown 12 Md.	3. FROM: Name of person claiming exemption John F. and Mary L. Smith Address (number and street) 1000 Oak Street city, town, or post office zone State Anytown 6 Md.	
4. I certify that I am exempt from the withholding of tax on any interest or dividends that you may pay me on or after 1/1/62 for the reason checked below: (a) ☐ I will be under 18 years of age as of the close of the first calendar year for which this certificate is effective. Date of birth (date) (b) ☒ I will be 18 or over as of the close of the first calendar year for which this certificate is effective and reasonably believe that no tax liability will be due for my taxable year in which this certificate goes into effect. Date of birth (month day year) (c) ☐ Tax exempt organization. Sign here JOHN F. SMITH 11-26-62 (Signature and date) (If for husband and wife both must sign) MARY L. SMITH 11-26-62 (Wife's signature & date)		

WITHHOLDING ON DIVIDENDS AND INTEREST

The attached forms illustrate how the quarterly refund system would operate for Mr. and Mrs. Jones, a retired couple both over age 65:

The Jones family receives the following income during 1963:

Mr. Jones:

Dividends from General Motors (paid quarterly)	\$800
Social security benefits	1,200
Pension (all taxable)	1,200

Mrs. Jones:

Dividends from General Electric (paid quarterly)	400
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Joint income:

Interest on savings account (paid quarterly)	2,000
Total	5,600

The Jones expect to itemize deductions for the year and believe that they will have \$1,000 of deductions.

As shown on the forms, the Jones have a refund ceiling for the year of \$440 and will receive quarterly refunds of \$160, \$160, and \$120 respectively. They will claim a refund of \$56 on their tax return for the year computed as follows:

Dividends and interest (less \$100 exclusion)	\$3,100
Pensions	1,200
Total	4,300

Less:

Personal exemptions	2,400
Itemized deductions	1,000
Total	3,400
Taxable income	900
Tax at 20 percent	180
Less 4 percent dividend credit	36
Balance	144
Credit for tax withheld	200
Refund	56

¹ Gross amount including tax withheld.

First quarter refund claim, form No. 2

PROPOSED FORM

INITIAL CLAIM FOR REFUND OF TAX WITHHELD FROM DIVIDENDS AND INTEREST OF INDIVIDUAL TAXPAYERS

File only one claim in each quarter. (See separate instructions.)

PLEASE PRINT	1. Name John F. and Mary L. Jones	2. Your Identification Number 514-91-2078
	Address (number and street) 964 Oak Street	3. Wife's Identification Number 141-16-9940
	(city, town, or post office) Anytown	(zone) 6
	State () Md.	4. Claim covers period: from Jan. 1, 1963 to March 31, 1963

DIVIDENDS AND INTEREST RECEIVED FROM WHICH FEDERAL INCOME TAX WAS WITHHELD DURING PERIOD SHOWN IN ITEM 4

Name of Payor	Amount received after withholding
5. General Motors	\$160.00
General Electric	80.00
First National Bank	400.00
6. Total	640.00
7. 25% of line 6 above. (Enter here and on line 8, page 2)	160.00

U.S. Treasury Department—Internal Revenue Service

—FRONT—

COMPLETE AND SIGN OTHER SIDE

Tab Card 7³/₈ x 3¹/₄
REFUND COMPUTATION

8. Enter amount shown on line 7, page 1		\$ 160.00
9a. Number of exemptions 4, multiplied by \$600	2,400.00	
b. Estimated deductions: Standard or itemized	1,000.00	
c. Enter your estimated retirement income. (see instructions)		
10. Total of lines 9a, b, and c	3,400.00	
11. Estimated income (except dividends and interest subject to withholding)	1,200.00	
12. Line 10 less line 11	2,200.00	
13. 20 per cent of the amount on line 12		440.00
14. Refund claimed. Amount on line 8 or 13, whichever is smaller. (Refund will be made for this quarter only if claim amounts to \$10. or more)		\$ 160.00

I declare under the penalties of perjury that this claim has been examined by me and to the best of my knowledge and belief is true and correct.

JOHN F. JONES 4-1-63
(Signature and date)

MARY L. JONES 4-1-63
(If joint claim, BOTH HUSBAND AND WIFE must sign) (Wife's signature & date)

Second quarter refund claim, to be mailed to taxpayer by Internal Revenue Service, Form No. 3

Proposed Form

CLAIM FOR REFUND OF TAX WITHHELD FROM DIVIDENDS AND INTEREST
FOR USE IN CLAIMING ADDITIONAL REFUND FOR 3-MONTH PERIOD BEGINNING APR. 1, 1963

PLEASE PRINT	Name • John F. and Mary L. Jones	Claim No. 514-91-2078	A. Estimated refund ceiling for year • 440.00
	Address (number and street) • 964 Oak Street		B. Refunds previously made • 160.00
	City, town, or post office • Anytown	Zone 6	State Md.

To claim your additional refund, please answer the following question and furnish the information required: Has there been any change in your income tax exemptions, estimated deductions, retirement income credit, or an increase of more than \$100 in the other income amounts as reported in your original claim?

☐ Yes ☒ No

D. If "No", complete Schedule A on reverse and enter amount from line 3, Schedule A. \$160.00
Your refund will be the smaller of Item C or D. Refund will be made for this quarter only if claim amounts to \$10 or more.

E. If "Yes", complete Schedules A and B on reverse.

I declare under the penalties of perjury that this claim has been examined by me and to the best of my knowledge and belief is true and correct.

Sign here JOHN F. JONES 7-1-63 MARY L. JONES 7-1-63
(Signature and date) (If joint claim, BOTH HUSBAND AND WIFE must sign) (Wife's signature and date)
• Filled out by Internal Revenue Service.

SCHEDULE A.—DIVIDENDS AND INTEREST RECEIVED FROM WHICH FEDERAL INCOME TAX WAS WITHHELD DURING PERIOD COVERED BY THIS CLAIM

Name of Payor	Amount received after withholding
1. General Motors \$160; General Electric \$80. First National Bank	\$240.00 400.00
2. Total	640.00
3. 25 percent of line 2	160.00

SCHEDULE B.—REFUND COMPUTATION (Complete only if the question on the face of this form is answered "Yes.")

4a. Number of exemptions _____, multiplied by \$600	
b. Estimated deductions: Standard or itemized	
c. Enter your estimated retirement income (see instruction)	
5. Total of items 4a, b, and c	
6. Estimated income (except div. and int. subject to withholding)	
7. Line 5 less than 6	
8. 20 percent of amount on line 7	
9. Less: Amounts withheld on dividends and interest previously claimed	
10. Balance of refund ceiling (Line 8 less line 9)	
11. Refund claimed. Amount on line 3 or 10, whichever is smaller (Refund will be made for this quarter only if claim amounts to \$10 or more)	\$

Third quarter refund claim, to be mailed to taxpayer by Internal Revenue Service, Form No. 3A

Proposed Form

CLAIM FOR REFUND OF TAX WITHHELD FROM DIVIDENDS AND INTEREST
FOR USE IN CLAIMING ADDITIONAL REFUND FOR 3-MONTH PERIOD BEGINNING JULY 1, 1963

PLEASE PRINT	Name • John F. and Mary L. Jones	Claim No. 514-91-2078	A. Estimated refund ceiling for year • \$440.00
	Address (number and street) • 964 Oak Street		B. Refunds previously made • \$320.00
	City, town, or post office • Anytown	Zone 6	State Md.

To claim your additional refund, please answer the following question and furnish the information required:
Has there been any change in your income tax exemptions, estimated deductions, retirement income credit, or an increase of more than \$100 in the other income amounts as reported in your original claim? ☐ Yes ☒ No

D. If "No", complete Schedule A on reverse and enter amount from line 3, Schedule A. \$160.00
Your refund will be the smaller of Item C or D. Refund will be made for this quarter only if claim amounts to \$10 or more.

E. If "Yes", complete Schedules A and B on reverse.

I declare under the penalties of perjury that this claim has been examined by me and to the best of my knowledge and belief is true and correct.

Sign here JOHN F. JONES 10-1-63 MARY L. JONES 10-1-63
(Signature and date) (If joint claim, BOTH HUSBAND AND WIFE must sign) (Wife's signature & date)

• Filled out by Internal Revenue Service.

SCHEDULE A.—DIVIDENDS AND INTEREST RECEIVED FROM WHICH FEDERAL INCOME TAX WAS WITHHELD DURING PERIOD COVERED BY THIS CLAIM

Name of Payor	Amount received after withholding
1. General Motors \$160; General Electric \$80 First National Bank	\$240.00 400.00
2. Total	\$640.00
3. 25 percent of line 2.....	\$160.00

SCHEDULE B.—REFUND COMPUTATION (Complete only if the question on the face of this form is answered "Yes.")

4a. Number of exemptions _____, multiplied by \$600.....	
b. Estimated deductions: Standard or itemized.....	
c. Enter your estimated retirement income (see instructions).....	
5. Total of items 4 a, b, and c.....	
6. Estimated income (except dividends and interest subject to withholding).....	
7. Line 5 less line 6.....	
8. 20 percent of amount on line 7.....	
9. Less: Amounts withheld on dividends and interest previously claimed.....	
10. Balance of refund ceiling (Line 8 less line 9).....	
11. Refund claimed. Amount on line 3 or 10, whichever is smaller (Refund will be made for this quarter only if claim amounts to \$10 or more).....	\$

Annual statement of refunds to be furnished by Internal Revenue Service, Form No. 4

Form (Aug. 1961)
U.S. Treasury Department
Internal Revenue Service
Address any inquiry to—
[Internal Revenue Service,
Baltimore 2, Maryland.]

Claim Account No. 514-91-2078
Refunds made this year \$440.00

DETACH AND KEEP THIS
STUB WITH THE RETAINED
COPY OF YOUR INCOME
TAX RETURN

Form (Aug. 1961)
STATEMENT OF REFUNDS MADE ON DIVIDENDS AND INTEREST
REFUND CLAIM ACCOUNT
Refund(s) of income taxes withheld from your dividend and interest in the amount indicated below were made to you during calendar year 1963.
Please attach this statement to your Income Tax Return, Form 1040, and file it with your District Director.
Your claim Account No. 514-91-2078
Refund made this year \$440.00

Name John F. & Mary L. Jones
Address (Number and street) 964 Oak Street
City or town Anytown Zone 6 State Md.

DO NOT FOLD, STAPLE OR MUTILATE

Mr. SMATHERS. Mr. President, I suggest the absence of a quorum.

The PRESIDING OFFICER. The clerk will call the roll.

The legislative clerk proceeded to call the roll.

Mr. SMATHERS. Mr. President, I ask unanimous consent that the order for the quorum call be rescinded.

The PRESIDING OFFICER. Without objection, it is so ordered.

Mr. LAUSCHE. Mr. President, I send to the desk an amendment which would delete section 18 from the pending bill, if and when it finally is included in it.

This amendment would delete section 18 of the bill, relating to inclusion of foreign real property in gross estate and substitutes for it a new provision which requires foreign real property acquired in contemplation of death to be included in the gross estate of a U.S. citizen or resident. The amendment will prevent the avoidance of the U.S. estate tax through the ownership of foreign real property and will do so in a manner which will not raise any constitutional issue. Under the amendment, any acquisition of foreign real property is prima facie deemed to have been made in contemplation of death and this places the burden on the estate to show that it was

not so acquired if the U.S. estate tax is to be avoided.

I ask unanimous consent that the amendment may be printed.

The PRESIDING OFFICER. The amendment will be received and printed, and will lie on the table.

SUPPORT WITHHOLDING DIVIDENDS AND INTEREST AT SOURCE

Mr. DOUGLAS. Mr. President, we now move to one of the most important features of the bill—namely, the proposal of the Senate Finance Committee to eliminate the provisions for withholding at the source the tax already owed on dividends and interest, as a basic provision in connection with the income tax. On this question a vote "yea" will be to eliminate the withholding feature for dividends and interest; a vote "nay" will be to uphold the withholding feature for dividends and interest.

Mr. President, last year, when the President submitted his tax program to Congress, he included as one of its integral and most important parts—indeed, as the chief reform proposed—the provision for withholding on dividends and interest. That was embodied in the tax bill submitted by the President to the House of Representatives; and it was approved by the Ways and Means

Committee, earlier this year, and was passed by the House.

It was eliminated from the House version of the bill by the Senate Finance Committee, by a vote of 12 to 5. The Senate is now being asked to uphold the committee's amendment, which is directly contrary to the President's recommendation.

A PRESIDENTIAL PROPOSAL

Only last week the President again declared himself on this subject; and the one feature of the tax measure which he singled out for comment was this one. He expressed the hope that Congress might retain the withholding provision. So there is no doubt that the President wants to have withholding of the tax already owed on dividends and interest, just as there now is withholding on wages and salaries.

I had hoped that voices more influential and more eloquent than mine would be raised in support of this proposal of the President. I had hoped that the Senatorial leaders of my party might take the floor to defend the President's program. I admit that I have a certain feeling of sickness of heart when I look around this vast Chamber and find only three other Senators present, and find that many Senators who, in my judg-

ment, should be speaking and working for the President are either absent from the floor or are working and speaking against this program.

As I have said, I personally feel somewhat unworthy to take on this burden; and I admit that one has moments of discouragement, particularly after the two defeats which we of the liberal bloc suffered, yesterday and today. Yesterday by a vote of 52 to 30, when the mangled version of the investment-credit provision was inserted in the bill; and only a few minutes ago, by the extraordinary vote of 54 to 39, when in opposition to the President the Senate opened wide the door for the continuation of the abuses in the field of expense accounts.

So the fact that many Members of the Senate have not answered the quorum call and the attitude of the leaders of my party on the floor of the Senate all make me realize that in all probability I am speaking in vain.

The question is whether one should stand up—in opposition to this powerful steamroller—to speak from a back bench in behalf of the President's program, when those who sit in the front benches and the seats of the mighty do not take the field to defend it.

PRESENT WAGE WITHHOLDING 20 YEARS OLD

Mr. President, 20 years ago, almost to the day, the Congress, while in the midst of World War II, imposed a withholding tax on wages and salaries. At that time, great objection was voiced in Congress to that proposal. It was said to be unjust. It was said that it would deprive wage earners and salaried workers of income which they should keep until the end of the year. It was said to be unworkable administratively. It was said to place too great a burden upon employers, who would have to make the deductions. But it was passed; and it has now been the law for 20 years, and it is an integral part of our revenue system. From it are collected many billions of dollars, with comparative success.

WITHHOLDING A CENTURY OLD

Mr. President, the principle of withholding at the source is not a recent one. In 1862, in the midst of the Civil War, Congress passed an income tax, and it remained on the statute books for approximately 10 years. That income tax had as a feature the withholding of the tax on governmental salaries, both civil and military, and also the withholding of the tax on interest and dividends paid by railroads, banks, trust companies, and insurance companies—which were about the only types of corporations in the United States at that time. Thus, for 10 years, withholding at the source was an integral part of that first Federal income tax.

In 1871, under the corruption of the Grant administration, that income tax was repealed. An income tax was later passed in the 1890's, but was declared unconstitutional by the Supreme Court. But a constitutional amendment was ratified by the States in 1912 or 1913, and it permitted the Federal Government to levy an income tax. In 1913 the Federal Government again levied an income tax; and it is upon the foundation

of that tax that we have now continued for 49 years.

WITHHOLDING PART OF 1913 INCOME TAX LAW

The basic administrative method in that first pre-World War I income tax was withholding at the source; and it was applied to wages, salaries, dividends, and interest. It was an across-the-board withholding system.

It was built not only on the experience which we had during the Civil War and the post-Civil War years, but it was also built upon the basic principle which had been embodied in the British income tax laws, of withholding at the source. This system has been in effect decade after decade in Great Britain, and it has worked very well.

In 1916, when the income tax law was revised, the withholding feature was eliminated. Then for 26 years wages and salaries and dividends and interest were reported by the recipients and taxes were paid on them by the recipients with no withholding at the source.

WITHHOLDING ON WAGES APPLIED AGAIN IN 1942

But in 1942, as I have said, the Congress of the United States applied withholding to wages and salaries, but did not apply withholding to dividends and interest.

The result has been that for 20 years we have operated under a system of withholding on wages and salaries, but not on dividends and interest.

I do not think it is necessary for me to point out that those who receive wages and salaries have, on the average, lower incomes than those who receive dividends and interest. The average salary of employed workers in manufacturing is a little under \$100 a week. There is, however, some unemployment in the country. Therefore, I suppose the average salary received in manufacturing tends to be somewhat less than \$5,000 a year. More than half the wage earners receive less than this amount.

So, in the main, it is the lower income groups which have their basic income tax withheld against them, and they can get a refund of the amount withheld in excess of the taxes they owed, but only at the end of the year. For a year they are deprived of the use of the money. I am informed that approximately 60 million wage and salary workers have their income tax withheld in this fashion. This is very interesting, for 37 million of them, or about 60 percent, file claims for funds at the end of a year. The records show that these refunds are made within 3 to 4 weeks, and that the average amount of the refunds is \$142.

There has been very little complaint against this type of withholding during the last 20 years.

Mr. HARTKE. Mr. President, will the Senator yield?

Mr. DOUGLAS. I yield.

Mr. HARTKE. What happens to a wage earner who has had his taxes withheld, and has overpaid his taxes, if he does not make an application for a refund?

Mr. DOUGLAS. As I understand it, he is out of luck.

Mr. HARTKE. This is the story that is being told by people who would have

their taxes on interest withheld. They say, "Suppose I do not make an application for refund?" Would they be in any worse position than wage earners who did not make applications?

Mr. DOUGLAS. Not at all. In fact, they would be better off, because as a group their incomes are higher.

In connection with dividends and interest, an automatic refund is provided after the first application.

Mr. HARTKE. So, if the withholding provision were retained, as was provided by the House, is it not a fact that persons who receive their income from dividends and interests would be in a better position than wage earners who worked for a living?

QUARTERLY REFUND

Mr. DOUGLAS. Yes, I am glad the Senator has pointed that out. The House provided for a quarterly refund in the case of dividends and interest, but there is only an annual refund in the case of wages and salaries. The recipients of dividends and interest would get their refunds quarterly, and not yearly. So the period of retention would be less for recipients of dividends and interest than it would be for salaried workers.

Mr. HARTKE. Is it not true that the person who works for a living would be denied the right to use money which was rightfully his during the entire period the Government had the money?

Mr. DOUGLAS. That is correct. That is what now happens.

Mr. HARTKE. That is the same type of approach and argument made against withholding of taxes on dividends and interest.

Mr. DOUGLAS. Yes. It is more severe in the case of wage and salary workers, not only because of the fact that they can only get refunds at the end of the tax year, whereas the recipients of dividends and interest would be able to get them quarterly, but also because, generally, the dividends and interest will be paid quarterly, and the quarterly due periods, under the Internal Revenue Service, would be closely coincident with the periods in which the dividends and interest would be paid to the recipients, so that, in all probability, there would be a loss, not for months, but for probably 3 or 4 weeks at the most.

Mr. HARTKE. And probably, at most, about 30 days.

Mr. DOUGLAS. That is correct. The Internal Revenue Service processes 37 million applications for refunds on wages and salaries, and pays them within 3 to 4 weeks; and there would be only about two million applications for refunds on dividends and interest, at the most.

ALMOST NO WAGE EVASION OR AVOIDANCE

Mr. President, let us notice what is the effect upon collections. There is virtually no evasion of income taxes in the case of the recipients of wages and salaries. Ninety-seven percent of the taxes on wages and salaries is collected. Only 3 percent is evaded or avoided.

But see what the difference is in the case of dividends and interest. In the case of dividends and interest approxi-

mately 11 percent of the dividends are not reported by the recipients and hence escape payment. In the case of interest, approximately 34 percent of all interest is not declared, and hence payment is avoided. As a result, the Treasury has estimated that for the fiscal year 1960 approximately \$4,400 million of dividends and interest which was paid out was not reported. It is estimated that in the next fiscal year of 1963 this will amount to between \$4.9 billion and \$5.2 billion. In other words, on the combined figures, somewhere between 20 and 25 percent of the dividends and interest is not reported and at present no taxes are paid on it.

Of course, the amount of taxes which is thus evaded is very large. For the current year it is estimated to be \$1,100 million. The failure to pay taxes on this amount means either that the rest of us must pay more to make up for those who do not pay at all or the deficit must be increased thus increasing the burden of society.

Mr. CARROLL. Mr. President, will the Senator yield further?

Mr. DOUGLAS. I yield.

Mr. CARROLL. I wish to ask the Senator from Illinois a question. It is an important question, and one that has bothered me a great deal. Will the Senator inform me as to whether the people who evade taxes on interest payments have been broken down into groups? Are they small holders or large holders? As to those who evade taxes on dividends, are they large or small holders? What brackets do they fall into?

Mr. DOUGLAS. Of course, we cannot get those figures from the ordinary statistical reports of income because these statistical reports relate to those who pay their taxes.

The Internal Revenue Service, however, made two special studies on a total of approximately 6,000 to 8,000 cases of unreported income and found that 70 percent of the amount of dividends and interest not reported was received by individuals who had more than \$10,000 a year of income.

In other words, on the basis of the samples of from 6,000 to 8,000 cases, 70 percent of the taxes which were not paid on dividends was from people having incomes of over \$10,000 a year.

So in terms of amounts of evasion and avoidance, it is, in the main, the upper income group, and not the lower income group, which evades and avoids on dividends.

Mr. CARROLL. Mr. President, will the Senator yield further?

Mr. DOUGLAS. I am glad to yield.

Mr. CARROLL. Is there a difference between interest payments and dividends, with reference to the groups, on the breakdown?

Mr. DOUGLAS. We shall try to obtain the information. The Senator is asking a very important question.

Mr. CARROLL. I suggest to the able Senator from Illinois that this is one of the key issues which bothers many Senators.

When I was last home in Colorado I talked with many people who had savings in building and loan associations or

in savings banks. Often they were not aware that the payments they received on their accounts were taxable income. They were holders of small accounts. They were not aware of the interest rates. The payments were included in their bank accounts. Often the interest amounted to only a very few dollars a year.

Mr. DOUGLAS. I understand.

Mr. CARROLL. I am very serious about this question. The answer to it will help me determine how I shall vote on this issue.

Would the Senator's proposal reach every little account? Would there be a breakoff point anywhere? Even school-children have a little money in savings accounts. Would the income from their accounts be taxable?

Mr. DOUGLAS. The House bill would exempt juveniles under 18 years of age, and those of any age who are not taxable.

Mr. CARROLL. What was the last group?

Mr. DOUGLAS. Those who are not taxable. That means those whose incomes are less than the amounts which would be exempted.

In this connection I point out that the standard personal exemption is \$600 per person for those under the age of 65, which would mean an exemption of \$1,200 for a couple under the age of 65. However, there is a double exemption for those who are over the age of 65, so after a couple is over the age of 65 they have a \$2,400 exemption.

Then there is a little known but very important retired income tax credit which roughly—and I put it roughly—amounts to the equivalent of a deduction of about \$1,200 for each recipient over the age of 65 for income received from dividends, interest, rents, royalties, and pensions. So if there were a husband and wife each receiving \$1,200 in these five categories this could be further deducted, and there would be another \$2,400 deduction added on top of the first \$2,400, making a total deduction of \$4,800.

Then the couple could also take the 10-percent standard deduction. All of this means that if a couple received less than \$5,300 in interest they would pay no income taxes whatsoever and they would be entirely exempt from withholding.

In addition, as we well know, in 1954 the Congress—I think inadvisedly but nevertheless actually—passed the 4-percent dividend credit and \$50 exclusion. So if the holdings of the aged couple were in stocks, they could have an income of \$6,100 before they would pay any income tax whatsoever, and everything under that amount would be exempt.

If that couple received, let us say, the full amount of social security, and \$3,000 in interest, let us say at 4 percent, that would mean they would have capital holdings of \$75,000. That would be exempt. In the case of dividends, at 4 percent to obtain \$4,000 they would require capital holdings of approximately \$100,000.

The idea that this would pinch the young and the old is wrong. The young would be completely exempt. Very few

of those over the age of 65 would have any withholding applied against them.

Mr. CARROLL. I thank the able Senator for his explanation. This is very important, and it has not been as fully presented as it might have been.

Mr. DOUGLAS. I have tried to present this issue time after time on the floor of the Senate. But the country will not listen. The newspapers will not listen. The building and loan associations will not listen.

Mr. CARROLL. The explanation has also been presented on the floor of the other body, as I remember.

Mr. DOUGLAS. The Senator is correct.

Mr. CARROLL. I wish to ask the Senator from Illinois a question in this regard. Does the Senator from Illinois, in his proposal, seek to restore the measure to the State in which it was passed by the House of Representatives?

Mr. DOUGLAS. What I am trying to do is to retain the House provisions. The Finance Committee is trying to knock them out. I am defending the House provisions.

Mr. CARROLL. Mr. President, will the Senator yield further?

Mr. DOUGLAS. I point out that three-fourths of those who are over the age of 65 are now tax exempt.

Mr. CARROLL. Three-fourths of those who are over the age of 65 are now tax exempt?

Mr. DOUGLAS. Yes. Therefore, there would be absolutely no withholding applied to them, because they would not owe any income taxes.

Mr. CARROLL. Does the Senator know what percentage of those under 18 years of age would be subject to withholding?

Mr. DOUGLAS. All of those would be exempt. That is one of the provisions the House put in the bill. The House changed the original proposal of the President. Those under 18 would be exempted from withholding completely.

Mr. CARROLL. If I correctly understand the Senator's explanation, those over 18 years of age would be treated like anyone else, and would have a \$600 exemption?

Mr. DOUGLAS. That is correct. It would be \$1,200 for a couple, and \$600 for each dependent. A man with a wife and three children would get an exemption of \$3,000.

Mr. CARROLL. Does that refer to gross income or net income?

Mr. DOUGLAS. That would be a deduction from gross income.

Mr. CARROLL. Do we know what percentage of the people who earn less than \$10,000 of gross income a year would be affected by the withholding provision?

Mr. DOUGLAS. We can obtain that information. Eighty percent of all the dividends are received by those whose incomes are more than \$10,000 a year. This was shown in a table which I inserted in the *Record*, at page 16712, on Monday in the general speech I made.

Mr. CARROLL. Is that based upon testimony in the committee hearing record on the bill?

Mr. DOUGLAS. It is based on figures computed by the Office of Tax Analysis of the Treasury Department. It is derived, I suppose, from the statistics of income which are published regularly.

Mr. CARROLL. Is the statement the Senator has made supported by the hearings?

Mr. DOUGLAS. There was testimony in the hearings in that regard, and it was not challenged.

Mr. CARROLL. In the hearings before the Senate Finance Committee?

Mr. DOUGLAS. That is correct.

Mr. CARROLL. Will the Senator repeat that? It is a very significant fact.

Mr. DOUGLAS. Those having incomes of under \$10,000 a year received only 20 percent of all the dividends. Those having incomes of over \$10,000 a year received 80 percent of all the dividends.

Mr. CARROLL. Let us forget about the dividends for a moment and let us direct our attention to interest. What is the story relating to interest?

Mr. DOUGLAS. That can be seen in the table No. 2 which I submitted, on page 16712 of the RECORD. I have not figured that out in any close precision.

Mr. CARROLL. The Senator will not have to do so at this time.

Mr. DOUGLAS. The total amount of interest reported was roughly \$4.4 billion. Of that amount, approximately \$1.9 billion was received by those whose incomes were under \$10,000. That amount would be roughly 40 percent of the interest. That figure means that those whose incomes were over \$10,000 received 60 percent of the interest and 80 percent of the dividends.

Mr. CARROLL. That is the point I wish to make. The Senator has given us the breakdown on interest. What was the gross total on dividends?

Mr. DOUGLAS. I have given the figures on dividends.

Mr. CARROLL. I am not speaking about percentages. I have asked for the gross total. The Senator said that the figure on interest was \$4.4 billion.

Mr. DOUGLAS. The total of dividends received was \$9.7 billion. Of that amount, approximately \$1.9 billion went to those receiving less than \$10,000 a year, or 20 percent. Therefore, those receiving over \$10,000 a year received \$7.8 billion in dividends, or approximately 80 percent of all dividends. In other words, those receiving over \$10,000 got 80 percent of the dividends and 60 percent of the interest.

Mr. CARROLL. I think this is a very important point. I ask the Senator to give us again the total gross in dividends.

Mr. DOUGLAS. The total amount paid in dividends was \$9,714 million, which I treated in round numbers at \$9,700 million.

Mr. CARROLL. What was the total gross on interest?

Mr. DOUGLAS. The total gross on interest received was \$4,395 million, or in round numbers, \$4,400 million. Those whose incomes were under \$5,000 received \$732 million; those whose incomes were from \$5,000 to \$10,000, received \$1,145 million. The two groups together re-

ceived \$1,877 million, or roughly \$1,900 million out of the \$4,400 million, or roughly around 40 percent. Those with incomes of more than \$10,000 received 60 percent.

Mr. CARROLL. As I understand it, those in the category of taxpayers receiving over \$10,000 in income receive—

Mr. DOUGLAS. Eighty percent of the dividends went to those in the category of taxpayers receiving over \$10,000.

Mr. CARROLL. In relation to interest, those in the category of taxpayers receiving an income of \$10,000 and over received about 60 percent of the interest.

Mr. DOUGLAS. Again I point out that those are not people or returns, but the figures are in terms of dollars.

Mr. CARROLL. I understand.

Mr. DOUGLAS. Sixty percent of the dollar amount of interest goes to those with incomes of over \$10,000, and 80 percent of the dividends goes to those with incomes over \$10,000.

Mr. CARROLL. That analysis was prepared by whom?

Mr. DOUGLAS. By the Office of Tax Analysis of the Secretary of the Treasury.

Mr. CARROLL. And that analysis is contained within these reports?

Mr. DOUGLAS. I think the one on dividends is. The table on interest was prepared for me personally. I think it appeared in yesterday's RECORD for the first time, but it was supplied by the Treasury.

Mr. CARROLL. With reference to interest, is there any evidence contrary to that which the able Senator has presented?

Mr. DOUGLAS. No. I have great confidence in the Office of Tax Analysis, which has been operated under both the Republican and Democratic administrations. I have never known them to misrepresent facts.

Mr. CARROLL. I thank the able Senator. He has been very helpful to the junior Senator from Colorado.

DOUBLE STANDARD APPLIED

Mr. DOUGLAS. In the main, the major portions of dividends and interest are received by those with incomes of over \$10,000 a year. They do not have withholding applied to them. The major portion of wages is received by those who have wages of less than \$5,000 a year.

Therefore, there is a system applied to those in the lower income brackets which is not applied to those in the upper income brackets.

It is interesting that those with incomes of over a million dollars get 48 percent of their entire income from dividends. The percentage received from dividends rises as the income rises.

ETHICAL QUESTION AT STAKE

A fundamental and ethical question is involved. A certain system has been applied for 20 years to the lower income groups in the community. During those 20 years the upper income groups in the community have been exempt from this provision. The result has been gross evasion and avoidance of taxation, which in the current year will amount to nearly \$5 billion of income not reported, and a

loss on taxes of nearly a billion dollars a year.

Mr. HARTKE. Mr. President, will the Senator yield?

Mr. DOUGLAS. I yield.

Mr. HARTKE. The Senator was discussing with the Senator from Colorado the question of the difference in the grades for the amount of income received from dividends and interest. Lest the colloquy be misinterpreted, and it could possibly be misinterpreted—is it true that those people have any special forgiveness of tax if they earn less than \$10,000? Does the fact that it is \$10,000 make any difference on their tax liability?

Mr. DOUGLAS. It is diminished by the degree of their exemption.

Mr. HARTKE. The point is, if they owe a tax, they owe it, whether it is above or below \$10,000.

Mr. DOUGLAS. That is correct. Those with an income of over \$10,000 have no more legal exemption from taxes than those who have income of under \$10,000.

Mr. HARTKE. The people the Senator is talking about, if they owe taxes, owe them; and the matter we are talking about in connection with this legislation is how to collect taxes that are owed.

Mr. DOUGLAS. The Senator from Indiana is completely correct. I have mentioned on the floor that I have received 75,000 letters from constituents in my own State protesting against the withholding method of collecting taxes on dividends and interest. We analyzed a large sample of those letters, and we found that in one-third to one-half of the cases the writers spoke of withholding as though it were a new tax, as though dividends and interest were not now taxable. Of course, this is a gross misconception.

Dividends and interest are income, just as wages and salaries are income. They are subject to taxation. The extraordinary thing is that from one-third to one-half of the persons who corresponded with me thought that dividends and interest were exempt from taxation. The fact that they thought so was, to me, presumptive evidence that they were not now paying taxes on dividends and interest.

Mr. CARROLL. Mr. President, will the Senator from Illinois yield?

Mr. DOUGLAS. I yield.

Mr. CARROLL. May I ask the Senator from Illinois to repeat the figure that he has mentioned regarding the distribution of dividend payments?

Mr. DOUGLAS. It is that 80 percent of the dollar amount of dividends that are received by those having incomes over \$10,000.

Mr. CARROLL. We have been talking about the amount of money that is lost to the Government.

Mr. DOUGLAS. That is correct.

Mr. CARROLL. I voted yesterday for the 7-percent tax credit incentive to industry for capital expenditures. I noted that the Senator from Illinois did not join with me in that vote. This credit will increase industrial profits and dividends; I should like to know how the benefits will be apportioned.

Mr. DOUGLAS. I have tried to state that information. I will break it down a little further.

Mr. CARROLL. I do not mean my question to reflect upon any group.

Mr. DOUGLAS. I understand. In terms of dividends, about 7 percent of the dividends are received by those having incomes of less than \$5,000; about 13 percent are received by those having incomes of from \$5,000 to \$10,000; about 80 percent, as I have said, of the dividends are received by those having incomes of more than \$10,000.

Mr. CARROLL. Before the Senator leaves dividends and discusses interest, I should like to know whether there is willful evasion.

Mr. DOUGLAS. I shall discuss that subject later.

Mr. CARROLL. There is a tax loss from dividends, is there not?

Mr. DOUGLAS. Yes; 11 percent of the dividends paid out by corporations is not reported by the recipients. There is a gap of that proportion between the amounts which we can trace which are paid out by corporations and the amounts declared by individuals on their income tax returns.

Mr. CARROLL. Is there any estimate as to how much is lost in taxation? In what categories do the individuals fall?

Mr. DOUGLAS. It is the high income groups, with respect to dividends; so it is hard to tell. But the amount is a very considerable percentage.

Mr. CARROLL. I want to support the principle of paying taxes, because I think an ethical question is involved. I am not for tax evasion. But I wish to ascertain at this time whether it is intended to reach down into the low income groups in order to make up for the money which will be lost due to the 7-percent tax credit?

Mr. DOUGLAS. The difficult point is that since nonpayers do not make returns, there are no returns upon which an estimate can be made with complete accuracy of the precise amounts of taxes, which are avoided or evaded by various income classes. The totals can be estimated.

Mr. CARROLL. Dollars and receipts can be estimated, but not groups. I think the Senator from Illinois understands what I am getting at.

Mr. DOUGLAS. I understand.

Let me discuss the question of who are the evaders and the avoiders, and whether such action is conscious or unconscious. No one quite knows, by income classes, who the evaders and avoiders are in the case of dividends. There is probably a more conscious avoidance in the case of dividends, and it is the more conscious the larger is the amount of interest and dividends received by the individual. However, I do not claim that all such avoidance or evasion is conscious. A very large proportion is not conscious. This largely comes about in the case of people who have only a small amount of money on deposit in savings and loan institutions or savings banks. They have credited to them quarterly an amount of interest. Unless that amount is transferred into a

checking account or a separate savings account, it is automatically added to the capital. Therefore, many persons do not think of this as income at all, because they never spend it. But it is income, even if it is added to the capital. But not spending it, and not having it entered into individual checking accounts or separate savings accounts, they tend to disregard it.

Mr. CARROLL. Mr. President, will the Senator further yield?

Mr. DOUGLAS. I yield.

Mr. CARROLL. The Senator from Illinois has explained clearly the situation which I have found in Colorado. Many small taxpayers say they do not consider reporting their interest income. It is not reported; it is not included in their earnings. But legally it is income. Frankly, I do not know what the answer is.

Mr. DOUGLAS. The answer is that unconsciously they have not declared as income amounts which they have received and which have been automatically added to the capital which they already have.

I do not in the slightest accuse such people of bad faith; I simply say they received the income. Such income is taxable, provided it is not exempt under the exemption limits.

Mr. CARROLL. Of course, that is true. The Senator has said that such people do not consider those earnings as income, and thus have never reported it. They are not conscious violators or evaders. Most of the nonreporting is in the field of interest; some of it is in the field of dividends. Some persons have said, "I get only \$10 in dividends; I have never paid any attention to reporting it."

My question is: How many such persons exist? We are willing to take the money from those people; but, as the Senator from Illinois says, we do not know, percentagewise, the number of such individuals from whom it is desired to recapture this money. Let us concentrate upon the big evaders if we can.

Mr. DOUGLAS. The two sample studies by the Treasury show that in the case of 6,000 to 8,000 returns, about 70 percent of the nonreported dividends were received by individuals having incomes of more than \$10,000. In the nonreported interest group, approximately 30 percent of the interest was received by persons having incomes of less than \$5,000; 40 percent by those having incomes between \$5,000 and \$10,000; 30 percent by those having incomes of more than \$10,000. Therefore, in the case of nonreported interest 70 percent was received by persons having incomes above \$5,000; in the case of nonreported dividends, 70 percent of the dividends were received by persons having incomes of above \$10,000.

Mr. CARROLL. I thank the able Senator from Illinois for his patience in answering this series of questions. These are matters that bother every Member of the Senate who has received letters expressing concern over this withholding proposal from the people at home. Interest has been credited to

their accounts and has been compounded year after year, and until now they have not thought of it as income.

Mr. DOUGLAS. That is correct. Let me make another point: Lower income groups, who have bought series E savings bonds, have paid let us say \$75 for the bond, which after a period of time may be cashed for \$100. When a person sells one of those bonds, he makes \$25 in interest. But large numbers of people do not regard that interest as income; they regard it simply as a return of capital and therefore do not declare as income the difference between the price they paid for the bond and the price they received. This has also been a source of avoidance.

Yet I am certain that as to the large proportion of these people, too, the nonpayment of tax is unintentional and unconscious. But I emphasize that whether it is unintentional or unconscious, if the income is taxable, the tax should be paid.

I am not any more in favor of tax evasion by lower income groups than I am in favor of tax evasion by high income groups—although I think we shall see that the major portion of the evasion—as shown by these studies—seems to be in the groups with incomes above \$10,000 a year.

Mr. CARROLL. Mr. President, will the Senator from Illinois yield further to me?

Mr. DOUGLAS. I yield.

Mr. CARROLL. I was hopeful that we could establish a breakoff point above the really small amounts, and could get at the large evaders.

Mr. DOUGLAS. That would complicate the matter too much. The Senator from Oklahoma [Mr. KERR] once proposed, I believe, that those with incomes of less than \$5,000 should not have anything withheld. But the mechanics of that would be difficult. As a matter of fact, the refunds would be quarterly, and generally would fall at times only a few weeks after the times when interest is paid, because the quarterly payments of the income tax are almost synchronous with the normal quarterly payments of dividends and interest—in other words, April 1, July 1, October 1, and January 1.

Mr. CARROLL. Mr. President, I thank the Senator from Illinois for his statement and for yielding to me, and for his patience.

IMMEDIATE REFUNDS

Mr. DOUGLAS. I thank the Senator from Colorado. He has been patient with me, rather than the other way around.

The Treasury has also declared its willingness to have any person go to a bank, claim a refund, and have the bank make the refund, and then pay the refund to the bank. As a matter of fact, Mr. Roth, of the Franklin National Bank, on Long Island, has offered to do just that.

I have in my hand an advertisement published in the New York Times, the Washington Post, and other newspapers. It reads as follows:

NOTICE

Additional expanded refund services when withholding of income tax on interest and dividends becomes law.

May 28 Franklin National announced refunds of withholding will be paid direct to its eligible savings depositors: At the bank's teller's windows, in cash, immediately, and without charge.

Now, Franklin National will also make the same refunds of withholding to its eligible depositors on their accounts with other banks, mutual savings banks, and savings and loan associations, and on dividends and interest on their securities as well.

No need to send refund claims to Washington and wait for checks from the Treasury.

If you are not subject to Federal income tax, Franklin National will also arrange for exemption from withholding.

We have 47 branches on Long Island; 2 branches in New York City in 1963; resources over \$900 million; member FDIC.

THE FRANKLIN NATIONAL BANK.

Mr. Roth is a most public-spirited banker. Incidentally, I believe his bank is the 24th largest in the country, with assets of close to \$1 billion. He is a highly successful banker. He had the courage to come before the committee and defend the proposed withholding. He and Mr. Shirley Tark, of Chicago, and a representative of a Michigan chain of banks, are about the only ones who have had the courage to take that position, and I think they deserve great credit. I honor them.

Mr. CARROLL. Mr. President, if the Senator from Illinois will yield further to me, let me say that a banker in Colorado—he lives in a very small town, and his is a very small bank, with very small accounts—came to me and said, "If you institute withholding, it will cost us about \$250 a month to keep the records, and our profits could not stand that."

I am not asking the Senator for an answer—

Mr. DOUGLAS. I can give the Senator an answer to that. All that the bank will have to do will be to deduct one-fifth of the amounts it pays out in dividends and interest to those who do not file exemption certificates. This can be done easily. They do not have to file with the Treasury the list of names, addresses, and amounts from which the 20 percent is deducted. They will not have to inform the individual depositors or shareholders that these amounts have been deducted. The institution will have to carry on only a minimum of reporting.

The Senator from Virginia [Mr. BYRD] will get them into much more trouble by means of his amendment, I can assure the Senator from Colorado.

Mr. CARROLL. Mr. President, if the Senator from Illinois will yield further, he knows that soon it will be September. So probably we shall be here for 2 or 3 weeks longer, and it may be October 1 before the session ends.

Mr. DOUGLAS. I hope not.

Mr. CARROLL. Judging from what I have heard today, that may be the case. I understand that the House of Representatives may not take up the foreign aid bill until September 19.

The Senator from Illinois is my great friend, and I consider him my mentor in most things.

Mr. DOUGLAS. Be careful.

Mr. CARROLL. Will we be able to return home and educate the people of our

States in 30 days in regard to a program of this scope?

Mr. DOUGLAS. I doubt it.

Mr. CARROLL. Can we expect the people to understand easily the merits of this proposal?

Mr. DOUGLAS. I doubt it.

Mr. CARROLL. I am glad to have the Senator's comment.

Mr. DOUGLAS. I doubt whether we can do this, because of the publicity which has been issued by the building and loan associations, by the savings banks, and by the banking community in general.

Mr. CARROLL. Mr. President, I think the Senator from Illinois is morally and ethically and legally correct. I wonder that the administration did not give this proposal greater support. Why have we not heard more from the President?

Mr. DOUGLAS. The President made a statement last week.

Mr. CARROLL. I know; and I am for it. But there was no great effort made at the grassroots level. About the only voice I hear is that of the Senator from Illinois.

Mr. DOUGLAS. Telstar does not carry on the earth.

Mr. CARROLL. Certainly these taxation problems are most difficult of solution.

Mr. DOUGLAS. I think it might be well for those who run for election this year to realize that they may seal their death warrants if they voted for withholding. I think that is quite possible.

I do not deserve any special commendation for bravery, because I will not have to run for reelection until 1966. So it cannot be said that I am heroic in what I am doing. The voters will have 4 years either to forget what I did or to become educated about what I did. So I am not going to pin any roses on myself, and I am sure no one else will. I disclaim any heroism.

Mr. CARROLL. Mr. President, will the Senator from Illinois yield again?

Mr. DOUGLAS. I am glad to yield.

Mr. CARROLL. I thank the Senator from Illinois for his patience. He has helped me develop in my mind a course of action. I say that withholding is bound to come—it is just and equitable.

The House provision impressed me and so did the President's position. In the words of a great historian, we are no longer confronted with a theory; we are confronted with a condition.

The able Senator from Illinois has helped me understand that condition, and I thank him for his courtesy and his great patience.

Mr. President, I intend to vote with the able Senator from Illinois in favor of collecting taxes, already existent, on dividends and interest payments by means of a withholding system.

Such a system is not new. It has been in use for 20 years collecting taxes on wages and salaries. It works well. It works fairly. It allows families to budget their tax payments throughout the year.

The extension of this withholding system to dividends and interest payments is natural and is needed. We have heard

today of the hundreds of millions of dollars that are lost to the Government through unpaid taxes on dividends and interest payments. It is unjust to the majority of the American people who pay their taxes without complaint to allow this loss to continue.

I will vote, Mr. President, for this withholding proposal because I believe it is just.

We shall be defeated today, I know. This vote will be symbolic; for withholding will come.

The House of Representatives have endorsed the proposal; the President endorses it. The people, when they understand the issue, will support us.

I urge the President, as the only elected official who can speak for all the people, to take this matter to the country.

The people will support us as they always support a proposal that is fair, just, and necessary.

Mr. DOUGLAS. Mr. President, I wish to pose this simple ethical question: Is it not improper to withhold taxes on persons in the lower income groups who receive wages and salaries, and who pay in withholding 97 percent of their taxes, but to refuse to impose withholding on the recipients of dividends and interest, who receive higher incomes, but do not pay taxes on close to 25 percent of the total amount of dividends and interest received? That, I think, is the basic question.

One can talk all he wants to about dividends and interest being received in multiple accounts by individuals or about other false issues, but the fundamental, ethical contradiction will remain.

If we refuse to put in the bill a provision for withholding the tax already owed on dividends and interest, to be consistent we should go the full way and then take off the withholding on wages and salaries. The Senator from Illinois, if he is defeated on this proposal, will introduce an amendment to that effect. Then we shall see whether those who are opposed to withholding on dividends and interest insist on having that same system in effect for wages and salaries.

Mr. President, there is a great deal of money at stake here, somewhere around \$1 billion a year. May I point out that the campaign of education which the Eisenhower administration promised in 1958, and which they tried to carry out, has not resulted up to date in any appreciable increase in collections. Thus far moral suasion and persuasion have failed to produce results.

It is true that, under the bill reported by the chairman of the Finance Committee last year, the automatic data processing system was begun, and the account number which one has under social security will be identical with the account number of his income tax return. So we shall now have a unified system. As the amounts of dividends and interest are reported, they will be recorded by the automatic computers under the account numbers of the individuals, and then they can be compared with the amounts the individuals declare as shown by his account number. Therefore, it is said by some per-

sons that it removes the necessity for withholding.

In the first place, I should like to point out that, fully carried out, this means an enormous amount of redtape. As a matter of fact, the automatic data processing system, with the coordination of social security and tax symbols, does not collect a dollar of taxes in itself. It merely gives to the Internal Revenue Service information with which it can go out and try to collect the taxes. The Internal Revenue Service has said that in order for it to collect every dollar in taxes that was due, it would have to double the number of Internal Revenue agents, and that would cost about \$200 million in extra money.

AUTOMATIC DATA PROCESSING NO SUBSTITUTE FOR WITHHOLDING

So automatic data processing is no substitute for withholding. As a supplement to withholding, it can be very valuable in getting at those in the upper income brackets whose taxes will be in excess of the basic 20 percent, and whose numbers, therefore, will be more limited, and who can then be followed up by the agents of the Internal Revenue Service.

Mr. President, I want to clarify some of the misconceptions that have been fostered.

Mr. COOPER. Mr. President, will the Senator yield?

Mr. DOUGLAS. I yield.

Mr. COOPER. Perhaps the matters about which I desire to question the Senator are those the Senator wants to clarify.

Mr. DOUGLAS. I could not have a more stimulating experience than to try to reply to the Senator from Kentucky.

Mr. COOPER. I have heard the Senator from Illinois speak on this subject at least twice before. I remember one evening session when he discussed the subject thoroughly and responded to the many arguments that were made against the withholding provision. I do not want to make such a long introduction to my questions, but I will cite my own experience. When this bill passed the House I studied it as best I could, in view of its great length, but I did direct my attention to the withholding provision—if not with the background in economic and fiscal affairs of the Senator from Illinois.

Mr. DOUGLAS. I may say that an expert was once defined as one who is a long way from home, and I do not pretend to be a real expert in this tangled field of fiscal policy and administration.

Mr. COOPER. I could understand the withholding provision clearly. For I knew withholding had been applied to wages and salaries, for years and today, against over 50 million taxpayers, I know this also from personal experience.

Mr. DOUGLAS. We all know about that.

Mr. COOPER. I know that \$1 billion in revenues are lost annually; that we have large annual deficits; and yet there is the hope in which I share, that taxes can be cut. Yet in this fiscal situation, some people, whether through inadvertence or purposely, are failing to pay \$1 billion annually in taxes, on dividends

and interest. It seems to me reasonable that in this situation Congress should provide this way to collect these unpaid taxes. Believing this, I took my position favoring withholding months ago on a television program. As a result, I received 6,000 or 7,000 letters, some of them angry but most of them expressing concern and making inquiries that people have the right to make of me and Members of the Congress. I found from these letters that some persons thought withholding was a new tax, although the tax on dividends and interest has been in effect, substantially, since 1913. Is that correct?

Mr. DOUGLAS. That is correct.

Mr. COOPER. Some of the writers thought it was a capital levy.

Mr. DOUGLAS. A large proportion of my correspondents thought that, too.

Mr. COOPER. They thought it was a capital levy on bank and savings accounts of 20 percent.

Mr. DOUGLAS. That is right, whereas it is only a 20 percent tax upon interest and dividends. If a person has a deposit of \$1,000, it is not a tax of 20 percent upon the \$1,000, but 20 percent upon the interest. Assuming the interest to be 4 percent, it would be a tax of 20 percent upon \$40, or \$8.

Mr. COOPER. I understood that. I answered the letters and assured the writers that it was not a new tax, and certainly not a capital levy, and asked them to direct any further questions they had to me. I received several thousand more letters. Nearly every objection to withholding was presented in these letters. The Senator has answered these questions in his speech. But one question came from older people, of small means, and it was troubling: Would the withholding of interest work a hardship upon them by depriving them of the money that they had been accustomed to have and which they needed for housing, rent, food?

The Senator from Illinois has pointed out in his report, along with the Senator from Tennessee, that any overwithholding beyond actual taxes due, on this account would be true only for the first quarter, for application for the refund of any overwithholding could be made then, and any such amount refunded.

Mr. DOUGLAS. The application for the refund would be made in the first quarter of the year, but it would carry over automatically to the other quarters.

Refunds would be made quarterly, probably within 3 or 4 weeks.

Again I wish to emphasize that the quarterly period in which the taxes would be due, under the Internal Revenue Service system, would be approximately the quarterly period in which dividends and interest would be paid out by the institutions.

Mr. COOPER. That is correct.

Mr. DOUGLAS. I think the wording is "approximate synchronization" of the two periods.

Mr. COOPER. The Senator has pointed out that those under the age of 18 would not be subject to withholding on interest or dividends.

Mr. DOUGLAS. That is correct.

Mr. COOPER. Also, persons who did not believe they would incur tax liability could file requests for exemption and would not be subject to withholding.

Mr. DOUGLAS. That is correct.

Mr. COOPER. These exemptions are reasonable and more favorable than to wages and salaries. Am I correct?

Mr. DOUGLAS. The Senator is correct.

Mr. COOPER. It seemed to me, with these exemptions, withholding would deal with people who owe taxes and some people who have not paid the taxes they owe.

Mr. DOUGLAS. That is correct.

Mr. COOPER. I repeat, I think a part of the failure to pay has been due to inadvertence.

Mr. DOUGLAS. That is correct.

Mr. COOPER. And some of it has been purposeful.

I stand where I did months ago. The more I have studied the problem, I have come more strongly to the conclusion that withholding would not work a hardship on small taxpayers, and that in all justice to those who do pay their taxes an effort should be made to collect the taxes not being paid.

There is another question I should like to ask the Senator.

Mr. DOUGLAS. I shall be glad to try to answer.

Mr. COOPER. I have received letters from certain institutions, such as savings banks and other, saying that if the withholding system should be adopted it would cost more than the amount which would be collected. I know that could not be true, but if the Senator has not already put into the RECORD the facts as to the probable cost, I wish he would do so.

Mr. DOUGLAS. The cost to the Government is estimated under withholding to be about \$19 million. The reports which the paying institutions would be required to make would be relatively simple. All they would have to do would be to forward to the Government one-fifth of the amount paid out in interest or dividends. That is all. They would not have to list the individuals who received those amounts, or the amounts given to individuals. They would not have to notify the individuals as to the amounts withheld.

The Senator from Virginia [Mr. BYRD] would require them to report to the Government the amounts paid to each individual and to notify the individual of this. I wish to give the Senator from Virginia credit for his proposal, because he offered it very honestly. Under his proposal there would be about 200 million pieces of paper that the institutions would have to send out, plus all the internal computing that would have to be done. This is what the banks and savings institutions asked for, and this is, very properly, what the Senator from Virginia [Mr. BYRD] would give them. His rugged honesty demanded that this be done. The institutions will rue the day when they proposed this method.

Mr. COOPER. In reading the Senator's report, I believe it estimated that the cost of withholding would be about

\$48 million annually—to collect the \$650 to \$850 million of unpaid taxes.

Mr. DOUGLAS. I do not think it would cost that much. To collect \$650 million of the \$850 million without a followup by agents would cost \$19 million. To follow up with agents, to get the difference between the \$650 million and the \$850 million, would cost about \$29 million more. These cost figures are based on the 1959 revenue gap figures of the Treasury.

Mr. COOPER. \$48 million.

Mr. DOUGLAS. That is correct. The latter group would involve a relatively small number of cases.

Mr. COOPER. I believe the Senator has made the statement that if the reporting system which the committee recommends is adopted it would be necessary to employ hundreds, if not thousands, of additional employees to follow up on the reports, and collect the unpaid taxes.

Mr. DOUGLAS. The collecting force would have to be doubled.

Mr. COOPER. I believe an estimate has been made that it could cost as much as \$400 million annually to collect \$850 million under the reporting system, as compared to \$48 million under withholding.

Mr. DOUGLAS. It would cost vast sums of money.

Mr. COOPER. I made my decision to support withholding, before the great campaign formed against it. I respect the opinion of those who oppose it. I respect those who have written me; for many of them have been quite concerned. I have been worried about letters I have received from older people—many 75, 80, or more. Many of them are people I know, who have been led to believe that this proposal would take from their savings money they need for bare existence. The letters have been difficult to answer, difficult to give assurance that their fears were unfounded. But they are unfounded.

I cannot escape the fact that over a billion dollars of taxes on dividends and interest are unpaid annually and should be collected. The taxes have been payable under the law since 1913. An effort ought to be made to collect them.

I have received letters from some businessmen who object very strongly to withholding. I respect them but I think their position is inconsistent with the position that the Congress should develop on sound fiscal position. They ask that Congress should cut expenditures and I agree. But there is another side to fiscal order. If we are to achieve fiscal balance there must be an honest and full payment of taxes.

Mr. DOUGLAS. I thank the Senator from Kentucky. His statement and his position are in thorough keeping with the nobility of purpose which we have observed in the Senator from Kentucky ever since he first came to the Senate many years ago. I believe he is absolutely correct. The same considerations have been largely those which have led me to the feeling that we should apply withholding across the board.

There is one factor which is sometimes ignored, and we might as well get it out on the table now. I refer to the fact that

under the present method there is an automatic snowballing of the interest paid out by savings banks and the amounts paid out by savings and loans institutions to the capital accounts of recipients, and these amounts are then used by the institutions. To the degree that taxes are not paid on those amounts, there is an increase in the capital sum by that amount. In other words, there is a snowballing of existing capital rolling up at the rate of nearly 4 percent a year. If the taxes which are owed upon this are not paid, that means that the size of the annual increment through the snowballing is greater than it would be if the taxes were paid.

Therefore a part of the gross of savings institutions has come from taxes owed to the Government but not paid. We might as well recognize that. Since this is a real world, we also might as well recognize that while it is not the only reason, it is one of the reasons why the savings institutions are opposed to the withholding system. If we had withholding, the money collected by the Government in taxes owed to them would not be available for the automatic addition to capital. To that extent, the growth rate of those institutions would be slowed down.

The heads of some savings institutions tell me that very frankly. The question is, Should those institutions grow at the expense of the Federal Government by reason of receiving money which is really owed to the Federal Government? Should those institutions grow to this degree because of tax evasion or tax avoidance? That is perhaps a better way to put the question. I think if that question is raised, there can be only one answer. No institution has the right to grow on taxes owed but not paid. That is a morally indefensible position to take. If the issue were really known to the American people, I think the conclusion would be very clear.

I prepared a series of questions and answers which was printed at the conclusion of my remarks on Monday, and which I do not wish to insert again in the RECORD. Many of them have been covered. I wish to emphasize again that those over the age of 65 could receive \$6,100 in dividends or \$5,333 in interest before they owed any tax whatsoever. Hence there would be no withholding for them. Those under 18 would be specifically exempted. All but a small proportion of those over the age of 65 would be exempted. The burden of the evasion or avoidance comes from those with incomes over \$10,000 a year.

I hope that Congress will have courage enough to stand behind the President in this matter. I hope I shall not be accused of self-righteousness by saying that I think that the issue is an ethical issue.

Last night before I went to sleep I turned, as I often do, to the Oxford Book of English Verse. I found there the poem of Matthew Arnold entitled "The Last Word." Since the Senator from Oklahoma set us a worthy precedent yesterday in quoting poetry, I hope he will not object, since he is not present, to my quoting better poetry than that which he quoted. It is a poem addressed

to the man who takes an unpopular stand. As I remember, the poem starts like this:

Creep into thy narrow bed,
Creep, and let no more be said!
Vain thy onset! all stands fast.
Thou thyself must break at last.

Let the long contention cease!
Geese are swans, and swans are geese,
Let them have it how they will!
Thou art tired; best be still.

They out-talked thee, hissed thee, tore thee?
Better men fared thus before thee;
Fired their ringing shot and passed,
Hotly charged—and sank at last.

In the late hours last night, being somewhat fatigued by standing beside the Senator from Tennessee all day yesterday, I asked myself, "What is the use of resisting the combined leadership of both parties and the bipartisan political machine which dominates the Senate?" Then I thought of the last verse of that poem. I hope I shall not be accused of mock heroism. I am not up for election until 1966. By that time most voters will have forgotten the issue. Matthew Arnold concluded the poem with the following verse:

Charge one more, then, and be dumb!
Let the victors, when they come,
When the forts of folly fall,
Find thy body by the wall!

There will probably be political casualties as a result of this vote. I tried to warn some of my friends what was coming and I urged them to get out of town, because there is a good deal of merit to the statement that, "He who fights and runs away will live to fight another day."

But, Mr. President, sometimes we move forward by having issues squarely presented, having the roll called, and getting the issues crystalized. Then even though the steamroller goes over one, and the bodies pile up at the wall, the very piling up of the bodies permits others to scale the wall later.

I am as confident as that I stand here that in the long run withholding will be applied to dividends and interest as it now is applied to wages and salaries. It will inevitably come. But it will come more rapidly if we make the fight now than if we do not make the fight.

Mr. President, I yield the floor.

Mr. HUMPHREY. Mr. President, will the Senator yield before he yields the floor?

Mr. DOUGLAS. I shall be glad to. I yield to the Senator from Minnesota.

Mr. HUMPHREY. I want the Senator to know that he has more allies than he thinks. I believe the issue of withholding on dividends and interest is basic to the integrity of our tax laws. There was an honest disagreement among some of us over a proposal which did not satisfy all of my desires on tax legislation, but which long ago I felt I would support. That was the investment tax credit. I do not think it is the best form of tax legislation. I do not think it is as good as the consumer type of tax relief. I believe it might be of some help.

But the tax bill that was sent here by the administration was supposed to have some balance in it.

Mr. DOUGLAS. That is correct.

Mr. HUMPHREY. It was well understood that the investment tax credit was to be a sort of special tax privilege to American business. There is no doubt about that. It was allegedly designed to promote investment, to improve plant, and to increase efficiency of output. But the dividend and interest withholding provision was the one feature in the tax law that was supposed to bring what I would call morality to the tax law, a sense of fairplay, and bring in revenue.

Mr. DOUGLAS. That is correct.

Mr. HUMPHREY. I watched the development of the proposal relating to withholding of the tax on dividends and interest. Many years ago, when the Senator from Illinois and other Senators were submitting amendments on tax laws, one of the first amendments that was submitted was intended to bring some equity into the tax structure by imposing withholding of the tax on dividends and interest, as it operates on wages and salaries.

Mr. DOUGLAS. That was in 1951, when the Senator from Minnesota and the Senator from Illinois, newly arrived in the Senate, fought for a week on the floor of the Senate to get those provisions into the law.

Mr. HUMPHREY. We were not successful then. There are those who say that the Senator from Illinois and other Senators will not be successful now. I do not believe that is important at this stage. The House of Representatives passed a tax bill including a provision for the withholding of taxes on dividends and interest. I am not an expert on taxation. One cannot be all over the lot, so to speak, and it is therefore necessary for a Senator to rely on certain experts and certain procedures. However, I have long been convinced that if we are to have tax legislation which will tighten certain loopholes, and at the same time give an incentive, which in the real sense are benefits and privileges to a limited group in this country, by way of an investment tax credit, it is necessary to raise revenue through an equitable and honest and honorable procedure called withholding of the tax on dividends and interest.

I have listened to what the Senator from Kentucky said when he engaged in colloquy with the Senator from Illinois, with respect to all the information which has been going out throughout the land, to the effect that certain Senators will be caused a great deal of trouble and heartache.

People write to me to say, "What do you mean by saying that you are going to assess us 20 percent of our income?"

As the Senator from Kentucky has said, some people interpreted the provision correctly. However, most of the letters that I received said, "So you are going to put a new tax on us."

The Senator from Illinois has pointed out that the tax on dividends and interest has been with us since 1913.

Mr. DOUGLAS. Since 1913. And reports have been made by the recipients since 1916.

Mr. HUMPHREY. Yes. Some improvements have been made in the tax law. We have required corporations and others to report dividends to the In-

ternal Revenue Service. I am not familiar with all the details of this particular provision in the bill. However, I have read the provisions very carefully during the days when we had caucuses on this subject. The Senator from Illinois remembers that there were several meetings of Senators in which this particular withholding provision was discussed. I shall support in this area what the President has asked for. I will try to support what the President has sent to us in the form of a tax program as best I can. I voted with the Senator from Illinois, the Senator from Pennsylvania, and other Senators on the expense account provision. The Senator from Tennessee sought to strike that provision from the committee bill, particularly the section that dealt with the "or associated with" language.

Soon we shall have before us the question of deciding upon the lobbying provision. I intend to vote with Senators who are supporting an amendment to strike that provision.

I assure the Senator from Illinois that we are doing the right thing in voting for the withholding of taxes on dividends and interest. I do not believe it would cost any Senator his seat in the Senate. Even if that were the case with respect to the Senator from Minnesota, I am sure the country could get along very well.

Mr. President, it is very difficult for me, when I go home, to face a worker in a factory or a department store and know that that person has income tax payments taken out of his pay check every week. How long does he have to wait if there is a refund?

Mr. DOUGLAS. A full year.

Mr. HUMPHREY. A full year. Then we are told that we cannot vote to have withheld a tax on dividends and interest. If there were refunds under the bill—

Mr. DOUGLAS. They would come to the payer quarterly.

Mr. HUMPHREY. Every 3 months.

Mr. DOUGLAS. Generally only 3 or 4 weeks after the amount has been paid out.

Mr. HUMPHREY. I commend the Senator from Illinois, and I am proud to be on his side.

Mr. DOUGLAS. The Senator from Minnesota belongs on this side, and generally he is on our side. We welcome him back.

Mr. HUMPHREY. I knew that the Senator would feel that way when I came back. There have been only a few moments in my life when I have strayed from him, and each time it has caused me heartache and sadness.

Mr. CLARK. Mr. President, I commend the Senator from Illinois for the brilliant speech he has made in opposition to the pending amendment. I am also glad to note the fine support he has been given by the junior Senator from Tennessee, and now by the senior Senator from Minnesota.

I am not one of those who believe that bleeding political corpses will be piled up at the wall, and that that will happen to Senators who are up for reelection, because we oppose the committee amendment. I am up for reelection.

In my opinion there is absolutely no justification for striking the withholding provision from the House bill. I have been saying that for the past 6 or 7 months. I have received nearly 60,000 letters from constituents in my State opposing the withholding of the tax on dividends and interest.

I believe I received between 45 and 60 letters supporting the withholding. At least 6 months ago I wrote to my constituents who wrote to me—all 60,000 of them—telling them that I thought they were wrong and that I thought that the withholding of the tax on interest and dividends was a sound tax, wholly justifiable, and not a new tax, but one which had been on the books for a long while.

There are those who say that this proposal would cost me my reelection this fall. I do not believe so. Like the Senator from Illinois, I am not engaged in any mock heroics. I am not particularly proud of the fact that I am swimming upstream. I do not believe that those of us who are fighting a just battle for a decent equalization of the tax will be defeated. There are many times when, as the Senator from Illinois has said, it is a good thing to be licked.

Mr. DOUGLAS. But it should not be a steady diet, such as has been meted out to the liberals in the Senate during this session. Once in a while we want to win.

Mr. CLARK. Perhaps we shall be able to remedy the situation by the votes that will be cast on the first Tuesday after the first Monday in November.

I see in the Chamber the junior Senator from Illinois.

Mr. HUMPHREY. If the Senator from Pennsylvania will yield briefly, we may be able to enter into a unanimous-consent agreement to vote on the pending amendment tonight. We have talked to all Senators who are particularly interested. I have spoken to the Senator from Wisconsin [Mr. PROXMIRE], who had written a letter opposing any unanimous-consent agreement. However, he was more than willing that we should enter into such an agreement on this vital amendment. Will the Senator from Pennsylvania yield for that purpose?

Mr. CLARK. In a moment I shall be happy to do so.

The Senator knows that in my view the rules of the Senate ought to be drastically changed.

Mr. HUMPHREY. Yes.

Mr. CLARK. So that it would not be necessary to legislate by unanimous consent. There have been occasions in the past when I would not have yielded by unanimous consent because it is a good idea to point out to my colleagues in the Senate occasionally that the rules under which we are operating are ridiculous, and that if any Senator wanted to enforce them, the Senate would not be able to transact any business. I say to my friend the Senator from Minnesota, with whom I am almost always in accord, and to my good friend the junior Senator from Illinois [Mr. DIRKSEN], with whom I occasionally find myself in accord, that I shall not be contumacious in this regard, and that if they will yield

me 10 minutes so that I can finish these relatively brief remarks, I shall be glad to agree to the unanimous-consent request.

I am glad to yield now so that the Senator may propose the unanimous-consent agreement, with the understanding that I will be yielded 10 minutes to say what I wish to say.

Mr. HUMPHREY. Mr. President, I ask unanimous consent that 20 minutes on a side be allowed on this amendment and that at the conclusion of that time the Senate proceed to vote on the pending committee amendment, the time to be equally divided.

Mr. CLARK. Provided that I have 10 minutes before the unanimous-consent agreement goes into effect.

Mr. DIRKSEN. I shall be glad to yield 10 minutes to the Senator from Pennsylvania now.

Mr. HUMPHREY. That will be made a part of the agreement.

Mr. CLARK. My friends are their usual gracious selves.

The PRESIDING OFFICER. Is there objection? The Chair hears none, and it is so ordered.

Mr. DIRKSEN. Mr. President, I now yield the 10 minutes to the Senator from Pennsylvania.

Mr. CLARK. I shall be everlastingly grateful to the Senator.

The President of the United States gave his reasons in support of his tax proposal at his press conference last May 9. Secretary of the Treasury Dillon amplified the President's views in extensive testimony before the appropriate legislative committees. Those views have not changed in substance with respect to the request for a withholding of the tax on dividends and interest.

The views of the Secretary of the Treasury and of the President can be summarized as follows:

First, the withholding of the tax on interest and dividends is necessary to prevent tax dodgers from cheating the Government out of \$800 million a year. There is no other feasible way of stopping this widespread tax evasion. The suggestion that by buying five more business machines and making out more forms and sending the forms, as they are now being sent, to a warehouse in Kansas City will collect this tax, falls. If we were to retain an adequate number of additional Internal Revenue agents and their subordinates to make this tax effective without withholding, I think we would come pretty close to adding from 10 to 15 percent to the total number of Government employees, whom some of those who oppose the withholding tax already think are far too many.

My second point is that according to the President and the Secretary of the Treasury—and this is very clear indeed—this would not be a new tax. Dividends and interest have been subject to income tax since 1913. The President's proposal merely provides for collecting this old tax in the same way the same income tax on wages and salaries has been collected for many years: by withholding by the paying corporation or financial institution.

I have never seen the slightest moral or ethical justification for saying to a

person who works for his living, either as a white-collar or blue-collar worker, "We do not trust you. We are going to take your tax out of your wages or your salary before you get it, because we do not think you would pay your tax if we left it to you to do so"; and then to say to someone who does not work for a living, who lives on inherited income or perhaps on savings accumulated during a lifetime of work, "Oh, we trust you. We do not have to withhold tax from you. You are an honest citizen, but the man who works for a living cannot be trusted."

That attitude seems to me to be completely unethical and not morally sustainable.

Mr. CARLSON. Mr. President, will the Senator from Pennsylvania yield?

Mr. CLARK. Does the Senator from Kansas understand that I have only 10 minutes? The Senate is operating under a unanimous-consent agreement. I suggest that the Senator from Kansas ask for time, so that my remarks will not be curtailed.

Mr. CARLSON. I am most pleased, in accordance with a suggestion by the minority leader, to yield further time to the Senator from Pennsylvania.

Mr. CLARK. I thank the Senator from Kansas.

Mr. CARLSON. Does not the distinguished Senator from Pennsylvania believe there is some difference in the case of withholding of the tax on interest and dividends, since there would be no provision for deductions as a result of marital status and no deductions for dependents? Does the Senator really believe there would be withholding of taxes on wages if the withholding was the full 20 percent of the wages?

Mr. CLARK. I am perfectly prepared to have the same withholding provisions applied for dividends and interest as are applied with respect to salaries.

I honor my friend from Kansas. He is a friend of long standing. But I suggest to him that this distinction is a distinction without a difference, and frankly is a bit specious.

Mr. CARLSON. Does not the Senator agree that this proposal has never been considered or brought out in any pending legislation? The proposal is for a 20-percent withholding tax regardless of the amount to be taxed, with no deductions allowed?

Mr. CLARK. I understand; but, again, I do not believe that is a very convincing argument. I am sorry not to agree with the Senator from Kansas.

There will be no appreciable hardship on those who do not legally owe taxes. The procedures for exemption and for refund are more generous to the taxpayer than those which have worked well for years in the case of wages and salaries.

At the time I sent to my constituents the letter from which I have been quoting, I also enclosed a memorandum from the Treasury Department entitled "Withholding on Dividends and Interest—A Necessary and Fair Proposal."

That memorandum points out that most taxpayers pay their income taxes, but that millions of them do not, and that the withholding of taxes on interest and dividend payments is essential as a

matter of simple fairness and is necessary to put a stop to widespread tax evasion.

Far from hurting the average taxpayer, withholding would help him by insuring that the Government would collect most of the \$800 million in taxes on interest and dividends which are now being evaded each year—lost taxes which must be made up by heavier taxes on honest and conscientious people.

The withholding proposal has been grossly misrepresented and distorted by those who have their own selfish reasons for wishing to see it defeated. They have fostered widespread misunderstanding of the plan and have aroused baseless fears.

In my opinion, at least half, if not at least two-thirds, of the letters I received from my constituents opposing the proposal were based on misinformation which had been furnished them by corporations in which they held securities.

Withholding has been erroneously represented as imposing a hardship on indigent elderly couples. Under the present law, which gives people over 65 a double exemption and also a tax credit on retirement income, an elderly couple could have as much as \$5,377 in income each year from social security and interest and be liable to no tax and no withholding at all. If a part of their income were from dividends, the total income could be even higher. To have this income completely free of taxes or withholding, the couple would be receiving the maximum social security benefit of \$2,178 and interest income of \$3,199. This couple, who would avoid withholding entirely, would need about \$80,000 in savings deposits, earning 4 percent, to receive \$3,199 in interest. So I suspect there have been many arguments made which simply do not stand the light of day in connection with the proposed legislation.

Mr. President, I ask unanimous consent to have printed at this point in the RECORD the text of my letter to my constituents together with the enclosure furnished to me by the Treasury Department.

There being no objection, the letter and statement were ordered to be printed in the RECORD, as follows:

DEAR FRIEND: Thank you for your communication telling me of your views on President Kennedy's tax reform bill. I regret that I have been so swamped with mail on this proposed legislation that I am forced to use this form reply.

The President gave his reasons in support of his tax proposals at his press conference on May 9. Secretary of the Treasury Dillon amplified the President's views in extensive testimony before the appropriate congressional committees. Their views can be summarized as follows:

1. Withholding of the tax on interest and dividends is necessary to prevent tax dodgers from cheating the Government out of \$800 million a year. There is no other feasible way of stopping this widespread tax evasion.

2. This is not a new tax. Dividends and interest have been subject to income tax since 1913. The President's proposal merely provides for collecting this old tax the same way the same income tax on wages and salaries has been collected for many years: by withholding by the paying corporation or financial institution.

3. There will be no appreciable hardship on those who do not legally owe tax. The procedures for exemption and for refund are more generous to the taxpayer than those which have worked well for years in the case of wages and salaries.

4. The burden on the paying institutions is not appreciably more onerous than in the case of wages and salaries. Banks and other financial institutions may well net a profit from the free use of the withheld funds for appreciable periods of time.

5. The other tax loopholes which the bill would close are all unfair favors to special classes of taxpayers who for years have been able to avoid legally their fair share of our national tax bill—thus imposing a heavier burden on those who are not in the special privilege category. Examples are: padded expense accounts, inadequate taxation of foreign income, foreign tax havens, unfair tax preferences to mutual savings banks, mutual insurance companies, and cooperatives.

6. The investment tax credit for new machinery and equipment is necessary to help American industry to retool and thus compete more successfully with the modern industrial plants of Western Europe, Japan and, to some extent, Soviet Russia.

7. It is important that the new revenue from closing tax loopholes should equal or exceed the tax loss from the investment credit. We must keep our fiscal policies sound if we are to avoid a run on the dollar and a disastrous deficit in our foreign trade accounts and balance of payments.

I am confident that if you give careful study to these seven points you will understand why President Kennedy's position is in the national interest. Of course the bill has not yet been reported from the Senate Finance Committee and may contain amendments which you may be sure I shall study carefully.

Sincerely yours,

JOSEPH S. CLARK,
U.S. Senator.

WITHHOLDING ON DIVIDENDS AND INTEREST—A NECESSARY AND FAIR PROPOSAL

Most taxpayers pay their income taxes but millions do not. Withholding of taxes on interest and dividend payments is essential as a matter of simple fairness and necessary to put a stop to this widespread tax evasion.

Far from hurting the average taxpayer, withholding will help him by insuring that the Government collects most of the \$800 million in taxes on interest and dividends which are now being evaded each year—lost taxes which have to be made up by heavier taxes on honest and conscientious people.

There is no reason why those who receive all or part of their income from interest and dividends should not have their taxes withheld—as wage and salary earners have been for 20 years.

The withholding proposal has been grossly misrepresented and distorted by those who have their own selfish reasons for wishing to see it defeated. They have fostered widespread misunderstanding of the plan and aroused baseless fears.

These misconceptions deserve to be cleared up.

This is not a new tax. Withholding is merely a method of collecting taxes which are owed the Government but—because of ignorance or intentional deceit—are not now being paid. Dividends and interest are income and, as such, have always been subject to income tax.

Withholding will impose no hardship and little inconvenience on taxpayers. People who have such low incomes that they do not owe any taxes can easily prevent withholding by signing a simple form certifying that fact. Those under 18 can be exempted from withholding whether or not they owe any tax.

Elderly couples, widows, and others who may owe a little tax but less than the amount withheld, can get quarterly refunds by filling out a simple refund slip which will be available at banks, post offices, and other places. These refund slips can be filed at any time during a quarter after withholding has taken place. It is not necessary to wait until the end of the quarter. Internal Revenue will mail out quarterly reminders to refund claimants. The refunds will, in most cases, be received within a month—as they are now by the 37 million taxpayers who are over-withheld each year on their wages and salaries. Those who don't wish to bother with quarterly refunds will get them annually by filing their regular tax returns.

Withholding has been erroneously represented as imposing a hardship on indigent elderly couples. Under present law, which gives people over 65 a double exemption and also a tax credit on retirement income, an elderly couple could have as much as \$5,377 in income each year from social security and interest and be liable to no tax—and no withholding—at all. If part of their income is from dividends, the total income could be even higher. To have this income, completely free of taxes or withholding, the couple would be receiving the maximum social security benefit of \$2,178 and interest income of \$3,199. This couple, which would avoid withholding entirely, would need about \$80,000 in savings deposits, earning 4 percent to receive \$3,199 in interest.

An elderly couple with full social security benefits and \$1,000 more than this in interest income—\$4,199 a year—would, however, fall into the much discussed over-withheld category. Their savings deposits would have to total about \$105,000. The withholding each quarter would be \$210—\$160 more than necessary. Under the quarterly refund procedure, the couple would never be out of pocket more than \$160, which is the first quarter's overwithholding. The quarterly refund from the first quarter would offset the overwithholding in the second and so on indefinitely. This \$160 would earn only about \$6 for an entire year if left in their savings account at 4 percent.

How can anyone say this is hardship? Such a couple is well-to-do by almost anyone's standards—and there are very few such couples. Most elderly people would not be subject to withholding at all.

The amounts overwithheld generally will not be large. For more than half the people entitled to refunds, the amount overwithheld will be less than \$10 per year. The average refund of overwithheld wages and salaries in contrast, is \$143—and wage and salary earners can collect their refunds only at the end of the year.

Withholding is necessary. A total of nearly \$4 billion in dividends and interest—nearly 20 percent of the total—goes unreported on tax returns each year. Publicity campaigns aimed at increasing voluntary reporting have simply not worked. Internal Revenue has no way of checking many evasions, especially on interest payments, because only the large ones—\$600 or more—have to be reported by the payors to the Government.

Withholding will pay for itself many times over. The estimated administrative cost of the withholding system is \$19 million per year but \$650 million in presently-evaded taxes will be collected. Use of withholding to eliminate the many small and frequently unintentional evasions will free Internal Revenue agents to pursue the upper income bracket evasions which account for the difference between the \$800 million in tax receipts now being lost and the \$650 million withholding will bring in. These well-to-do evaders will, of course, be withheld 20 percent like everyone else—but they owe more than that.

Use of ADP, the suggested alternative to withholding, would cost more to do one-third of the job. Automatic data processing does not collect one penny in taxes. All it does is identify suspected tax evaders, who then have to be located and audited. Following-up and auditing all evaders turned up by ADP would be literally impossible—there are 6 million taxpayers who have interest and dividend income and don't report any of it. At least an equal number—maybe more—report some, but not all, of their dividend and interest income. Just following-up the biggest evaders, to recover \$200 million in taxes, would cost the Government \$29 million—half again the price of a withholding system that would collect more than three times that amount. The maximum additional tax that the Internal Revenue Service could collect effectively with ADP and a reasonable enforcement effort is \$200 million. And even to accomplish only the \$200 million increase in tax receipts would require an increase of over 3,000 in Internal Revenue's enforcement staff—a 55 percent jump in the number of office auditors presently employed and a 10 percent rise in the number of agents. In addition, use of ADP and enforcement personnel followups would require that business organizations make much more detailed and numerous reports to Internal Revenue than they do now—or would have to do under withholding. In addition, there is no ADP system fully in operation as of now—and won't be until 1966.

The system will be simple and convenient for payers of interest and dividends. They will make their payments of withheld taxes to the Government in one lump sum quarterly. They will not be required to keep detailed records of individuals to whom they make dividend and interest payments. In addition, they will be permitted to retain use of the withheld taxes for certain specified periods before they are turned over to the Government—a provision which will help offset the cost of withholding.

Withholding may involve some inconveniences, it is true. But the alternative is clear—continued lawless evasion of \$800 million worth of taxes each year on nearly \$4 billion of unreported interest and dividend income.

Honest taxpayers will support this proposal in justice to themselves and all others who now pay their full share of taxes.

Mr. CLARK. Mr. President, before I close, I should like to point out what seems to me to be the most outrageous tax chiseling which can be easily done unless there is a withholding of the tax. It has to do with wealthy individuals who own Government coupon bonds in denominations of \$1,000 or more. Such an individual can, without fear of ever being caught, take from his safe deposit box once each 6 months his Government coupon bonds, clip the coupons, and take them to his bank, which will promptly cash them. The bondholder can then put the money in his pocket, never deposit it in his checking account, and never account for it in any way, and he will never be caught. In my opinion, tens, if not hundreds, of millions of dollars of taxes are going down the drain through this one cheating device, day after day, years after year. But we never hear a word about it. All we hear about is the alleged inequity to some poor little citizen and his wife, who are usually living on a pension, and who, it is said, would be deprived of their honorable, just savings by having their savings account interest taxed.

There is a large smokescreen about this particular amendment. I think every Senator should appreciate the fact that when he votes to support the committee amendment, he will be voting to cheat the Government of the United States out of a minimum of \$800 million a year.

I yield the floor.

Mr. BYRD of Virginia. Mr. President, the question of withholding the tax on dividends and interest engaged the attention of the committee for many months. Hundreds of pages of testimony were taken. The committee considered every phase of the proposal.

Two votes were taken in the committee. The result of the first vote was 10 to 5 in opposition to the withholding of tax on dividends and interest. The result of the second vote was 11 to 5 in opposition. So by a vote of more than 2 to 1, the members of the Committee on Finance voted in opposition to the withholding plan.

Mr. President, House bill 10650 as it passed the House required withholding of tax from recipients of dividends and interest. The Senate Finance Committee amended H.R. 10650 by substituting a requirement that information returns be furnished to the Government and to recipients. The substitution was made because of the superiority of this procedure over withholding.

It is superior because it is less onerous on the taxpayer, less burdensome to the payors, avoids much of the administrative difficulties involved in the withholding scheme, will make a greater contribution to voluntary compliance, applies to recipients in all tax brackets, and is a more precise way of doing the job.

On the last point—that the furnishing of information returns is a more precise way of doing the job—the Secretary of the Treasury is in agreement. In answer to a question, raised by a member of the Committee on Ways and Means, as to whether information returns of payors coupled with data processing would not be a more precise way of doing the job, the Secretary, after stating his preference for withholding and after noting that information returns would pose an extra burden on payors, conceded:

But you are certainly correct. It would be more precise if they did this.

The information return method is less onerous on the taxpayer. Under the withholding method, many individuals, both in the elderly category and among younger people, would have been faced with substantial hardship because of overwithholding. Even those who could have filed exemption certificates were required to state under penalty of perjury that they would expect to owe no tax for the coming year. Many conscientious persons who in fact turn out to owe no tax would feel that they could not sign such a statement before the year even commences; and, therefore, they would be effectively deprived of the use of the exemption certificate. Moreover, under the quarterly refund system of the withholding plan, there would be a delay of at least 3 or 4 weeks before the recipient could receive back the withheld amounts

and many recipients would have to wait 3 or 4 months. This would deprive them of the use of their own funds as living expenses or as sources of investment during the interval. Moreover, the quarterly refund system of the withholding plan does not make allowance for the \$50 dividend exclusion—\$100 on many joint returns—or for the 4 percent dividend credit or for deductions where the taxpayer itemizes. Not only is the information reporting requirement less onerous to the recipient, but it is also a fairer and more just way for him to be treated. Many individuals whose dividends and interest would have been diminished by withholding might fail, through ignorance or otherwise, to file refund claims for overwithheld amounts. In such a case, under the withholding plan, these individuals would have been permanently deprived of their income.

While the exemption certificates and quarterly refunds would not resolve the hardship problems for the shareholder or depositor, they nevertheless would present many compliance problems for the corporate and bank payors of the dividends and interest. Corporations and banks would have to maintain two files of stockholders or depositors. Corporations would also have to be prepared to shift stockholders back and forth between these two files as shares are purchased and sold or as exemption certificates are issued or withdrawn. Moreover, under the withholding plan, special problems would arise when stock is sold just before a dividend date by someone who has filed an exemption certificate to someone who has not, if the stock certificate has not actually been delivered to the corporation before the dividend date. Moreover, in order to use exemption certificates at all, taxpayers would have to forgo the convenience of leaving stock in their brokers' names.

Under the information reporting provisions, banks and corporations have only one simple duty to perform: That is, they must furnish to the Government and to the recipient information regarding the amount of interest or dividends paid to the recipient. Not only is this far less burdensome than the duplicate recordkeeping required by withholding, but it provides a system for which the payers themselves have expressed a decided preference.

There would also have been serious administrative problems for the Internal Revenue Service under withholding, as a result of the use of exemption certificates and quarterly refunds. These could have led to substantial tax evasion. There was no assurance, for example, that only those who "reasonably expect no tax liability" could file exemption certificates. Moreover, these certificates would not have been easy to check, because many of them represent persons not required to file tax returns; so frequently there would be no returns to match them against.

Similarly, since the individual who would file a quarterly refund claim was not then required to submit proof of the receipt of dividend or interest payments, there was ample opportunity for tax evasion and fraud, as well as unintentional mistakes.

These required checking in detail and comparison with the amount shown on final returns, if the purpose of the legislation was to be fully accomplished. In fact, it was entirely possible that some taxpayers might file exemption certificates, file quarterly refund claims, and still claim refunds on their final returns at the end of the year, all with respect to the same dividend or interest payment or with respect to no dividend or interest payment at all. While the Internal Revenue Service might have been able to control this form of tax evasion and unintentional errors, it would have required a very large enforcement effort.

Mr. President, the information reporting program approved by the Senate Finance Committee will make a greater contribution toward voluntary compliance than the withholding program would have made. Withholding would take too much money from the multitude of low income taxpayers and too little from the higher income taxpayers. The Treasury has estimated that 29 percent of the unreported interest income is being received by those with incomes under \$5,000, and that 42 percent of the unreported interest is being received by those with incomes between \$5,000 and \$10,000. Thus, 71 percent of the unreported interest goes to those with incomes under \$10,000. The Treasury also estimates that 29 percent of the unreported dividends is received by those with incomes under \$10,000.

The 20-percent-withholding plan would require the lower income recipients of interest and dividends to file tax-exemption certificates if they are not taxable, and to file for refunds if subject to overwithholding, while at the same time there would be underwithholding on the higher income recipients. Many of those who would be subject to this underwithholding would, by mistake or with malice, assume that having been withheld on, they should pay no more. In the absence of information to the Government and reminders to the taxpayers, how much of this underwithheld tax would be forthcoming? Much less, in my opinion, than under a program where the Government is informed and the taxpayers are reminded that the Government is informed of the amount of interest and dividends these taxpayers had received, and where the taxpayers are reminded that the Government has the means of comparing its information with the taxpayers' tax returns.

The Finance Committee report states that the Treasury estimates that the withholding proposal would produce \$780 million of revenue in a full year. It should be noted, however, that only \$580 million of this amount is due to application of the 20-percent withholding. The additional \$200 million would be realized only—to use the Treasury's words—

If in addition to withholding there is an improvement in tax compliance by persons subject to individual income tax rates above the 20-percent bracket.

On the other hand, the estimate of revenue to be derived from the information return system is placed at \$275 million by the staff of the Joint Committee

on Internal Revenue Taxation, and at \$240 million by the Treasury, with a negligible allowance in each case for the compliance improvement which would result from the Government's knowing how much dividends and interest the taxpayer had received and the taxpayer's knowing that the Government knew and had the means through automatic data processing and enforcement to do something about it—not only as regards the low-income taxpayer but for all taxpayers.

I believe that the information-return-data-processing-enforcement system will prove a stronger stimulation toward voluntary compliance than withholding of 20 percent of dividends and interest, and will increase the revenue from this source significantly above the estimated amounts.

Particularly is this true in view of the fact that, as the Secretary of the Treasury has stated:

Much of the nonreporting of interest and dividends is due to inadvertence, forgetfulness, and failure to keep records, particularly by taxpayers who receive a small portion of their incomes from such sources.

If the inadvertent and forgetful are reminded, they will pay; if the willful evader knows that the Government knows and intends to collect, he will be induced to pay.

Thus, the reporting of dividends and interest to the Government by the payors, along with statements to the taxpayers of amounts so reported, will greatly enhance the compliance program of the Internal Revenue Service. Even before the Senate Finance Committee approved this information return system, which will greatly strengthen the compliance program, the Commission of Internal Revenue stated during the appropriation hearings in January:

As a byproduct of the automatic data processing system * * * we have noted a trend of people just walking into our offices and making voluntary disclosures. * * * They said they have been reading about automatic data processing."

And in March he had this to say of automatic data processing:

Today we do not see any saving of personnel but we do see a big closing of the revenue gap which Senator BYRD referred to on the floor as a potential \$5 billion figure. We think we will collect more money through our increased capability for identifying the sources of error.

For reasons I have given today, and also because the withholding scheme is impracticable and unworkable, as I attempted to demonstrate in my statement to the Senate on May 21, I believe the reporting provision in the Finance Committee bill is the proper solution to the underreporting problem.

Mr. THURMOND. Mr. President, the Senate Finance Committee's action in striking the House-passed provision of H.R. 10650 which would have established a system of withholding 20 percent on interest and dividend payments gives me a great deal of satisfaction. Had this provision been enacted into law, many complications and hardships would have resulted. This particular provision was requested to offset the loss of revenue

which is estimated as a result of people who fail to adequately report and pay taxes on interest and dividends. I feel that the provision which the Committee adopted in lieu of the withholding system will adequately protect the interests of the Treasury without necessitating such a great administrative expense as the withholding proposal. This bill provides, in lieu of withholding, for the reporting of most interest, dividend, and patronage dividends of \$10 or more per year. These reports must be made to the Government and to the recipients of the payments on an annual basis, and additional civil and criminal provisions are added to those in existence for failure to report unless there is a reasonable cause for that failure.

A system of taxation should be characterized by equitable application and simplicity of administration. The provision which was passed by the House and stricken by the Finance Committee would have been inequitable in its application. In order to achieve equity the administration of necessity would have been overly complicated. Many individuals would have been deprived of a portion of either dividends or interest in the periods of time in which they were sorely needed. To overcome this problem many solutions were advanced, such as quarterly refunds, exemption certificates, credits, and offsets. However, these solutions merely complicated the administration of the provision and would have resulted in increased expenses for the Government.

There has been much controversy over this withholding provision and the volume of mail which I have received has been staggering. The charge has been made that there was a deliberate plan to brand this as a new tax so that opposition to it would be much greater than normal. The mail which I have received reveals that the people understand that they are liable to the Government for taxes on dividends and interest, but do not wish to be deprived of the benefit of these funds when they will incur no tax liability for the year.

In view of the numerous difficulties and hardships which would have been created by the withholding provision, I gladly support the Finance Committee's position in deleting this section of the bill and inserting in lieu thereof a strengthened reporting system.

Mr. KEATING. Mr. President, I shall support the dividend and interest reporting plan proposed by the Senate Finance Committee.

The more people have talked about the administration's withholding proposal, the faster has its support dwindled. It is a true orphan in the world of high finance. Even its parents, the Treasury Department, have apparently turned away from it. Nothing remains for us to do but carry this motion.

This bill and all of the debate on withholding have shown that the objective of greater compliance in paying taxes owed on dividend and interest income can be achieved by far easier and more efficient means than by a giant, burdensome withholding system.

Automated tax processing and the new efforts recommended by the Senate com-

mittee to inform taxpayers as to their tax liability make a withholding system unnecessary under present circumstances. The Treasury Department has already ordered new automated equipment to keep records on income received and on revenues owed to the Government. Soon this machinery will enable the Department to isolate interest and dividend payments. I favor using these machines in connection with the committee reporting plan, rather than loading our taxpayers with an impractical withholding system that may fail anyway.

In the case of fairly well-to-do individuals, the withholding of 20 percent of all income from dividends and interest would make little difference. They would undoubtedly owe more than 20 percent in taxes on their dividend and interest income. But, I am worried about people of modest circumstances who would not understand how to file for refunds, people who do not owe any taxes at all, pension funds, trust funds, and tax-exempt charitable foundations. No matter how many exceptions you make, there will always be problems with a bookkeeping system as massive and inexact as that proposed by the administration.

An elderly couple with a limited interest and dividend income and a double deduction would be completely befuddled by a giant withholding system. If they delayed in doing the necessary paperwork to apply for a refund, there is always the chance that the would die and never be able to enjoy income rightfully due to them.

We must take every practical step to catch tax chisellers, but this "shotgun" approach is unfortunate and may not even work. Furthermore, it would hurt many people, especially retired persons and those of modest means who need their income promptly. The administration and the Senator from Illinois in this instance are using a Polaris missile to hunt for rabbits. Their plan would involve mountains of paperwork and in all likelihood would fail.

There are better ways to accomplish the objective here envisioned. The Senate bill is a feasible and logical alternative. With the new devices and equipment available to the Treasury, I am strongly in favor of using these more practical and less burdensome methods to see to it that taxes are paid—to the full extent which they are owed—on all dividend and interest income.

Mr. MILLER subsequently said: Mr. President, I intend to vote for the committee's amendment, which would strike from the bill the Kennedy proposal to withhold tax from interest and dividends. My reasons for opposing the Kennedy proposal and supporting the committee amendment were well outlined in the course of a radio interview carried on various Midwest stations last May, and I ask unanimous consent that the transcript of this interview be printed at this point in the RECORD.

There being no objection, the transcript was ordered to be printed in the RECORD, as follows:

RADIO INTERVIEW WITH SENATOR MILLER OF IOWA

ANNOUNCER. From the Nation's Capital, we bring you an interview with U.S. Senator JACK MILLER, of Iowa. Senator MILLER is a tax lawyer by profession. At one time he served as an attorney in the Office of the Chief Counsel, Internal Revenue Service, here in Washington. He has taught tax law, written numerous articles on taxation, and given lectures on various tax subjects throughout the United States. He formerly served as chairman of the Committee on Tax Problems of Farmers of the American Bar Association. The subject of the interview will be the President's proposal to withhold income tax on interest and dividends. Now, let's join the discussion.

BOB COAR. Well, Senator MILLER, this is a rather dry subject to some, but I think it would be most interesting to most of our taxpayers, particularly those who depend on small incomes from stocks and bonds and things of that sort, yet don't make a very large profit. I'd like you to tell us, if you would, just what the President's proposal to withhold income tax on interest and dividends amounts to.

Senator MILLER. First, Bob, let me point out that this is just one of many proposals in this 224-page monstrosity known as the omnibus tax bill. The President's proposal on this withholding on interest and dividends is that the payor—whether it's a bank or a corporation which pays interest or dividends to a customer during the year—will withhold 20 percent of that as income tax, so that the recipient will receive only 80 percent of the interest and dividends. This is something like the withholding on wages, except that on withholding on wages there is no flat 20 percent of income tax withheld. There may be a very small amount, there may be a much larger amount, depending entirely upon the dependents and the exemption status of the taxpayer. But here it's a flat 20 percent of income tax that is withheld. I might point out that although the President of the United States has said that there have been letters coming into the White House complaining that this is a proposed new tax, I haven't received a single letter like that from the thousands of Iowans who have written to me. This is merely a withholding of the present tax in anticipation of what would be due at the end of the year.

Mr. COAR. Isn't the inference there, Senator MILLER, that some of our people aren't quite honest, and that includes a great many of them?

Senator MILLER. Well, the President has estimated that there's some \$3 billion of interest and dividends that isn't getting on the tax returns and having tax paid on it, and that as a result from \$600 to \$800 million a year of income tax is being lost to the Federal Treasury. I think, however, that it isn't quite this simple. As a matter of fact, the statements by the President of the United States and by the Secretary of the Treasury constitute an unwarranted indictment against the integrity of the hundreds of thousands and millions of people who receive income from interest and dividends. You see, these people—most of them—are ready, willing and able to pay their income tax that is due, although I'll say there has been increasing resentment lately of the burden of taxes, particularly the burden that has been increasing due to some of these domestic nondefense spending programs of this administration. But the trouble is that many people who receive interest and dividends really don't understand the income tax consequences. Let me give you a few examples. There are hundreds of thousands

of people who have savings accounts at banks and savings and loan associations. During the year there is a crediting of interest to those accounts, although the interest is not drawn out. A lot of these people think that until they draw out that interest, they don't have to report it on their income tax returns; whereas the tax law says that if you can pull that interest out of the account, that once it is credited, it's taxable income. Then some corporations pay out dividends, not out of accumulated profits or current earnings but out of capital or out of depreciation reserve, and there is no income tax owing on those dividends. And some dividends include some capital gain income on which only a portion of the income must have tax paid, and there is confusion on that. And then there is much dividend and interest income which is very small, maybe \$2 or \$3 or \$5 or \$10. Improper records are kept. This is not reported, not due to fraud but due to inadvertence. Then we have a \$50-dividend exclusion. If you as an individual receive \$45, you don't even have to pay any tax on that; you list it on your income tax return but then you subtract \$50 away from it and you don't have any tax to pay. If you are a married couple and the stock is held in the joint names of the husband and wife, you have a \$100 dividend exclusion. There are millions of people who receive only a few dollars in dividend income so there is no tax owing on that. And then, of course, you have millions of small savings accounts in the names of children and older and retired people, and while it's dividend income, many of these people don't even have to file an income tax return. So I don't think it is quite as simple as inferring—as the President and the Secretary of the Treasury have done—that we have millions of tax evaders running around here in the United States. That isn't true at all.

Mr. COAR. A certain amount of money is being missed, but it is most difficult to determine accurately what that amount is, isn't it?

Senator MILLER. There is no question but what there is some tax revenue being missed. The point is, I think that this \$600 to \$800 million of missed revenue is a gross overestimate, and I think that it has been overestimated in an effort to try to force this proposal through the Congress.

Mr. COAR. Well, now couldn't we correct that, Senator MILLER, by some change in the method of reporting these payments, or a reduction of our \$600 allowance or exemption we get, the things we file normally with Internal Revenue?

Senator MILLER. The mere fact that there is missed revenue doesn't automatically lead you to this withholding scheme. As a matter of fact, under the present tax law, information returns have to be filed by people who pay interest or dividends of \$600 or more. They have to make out a little information return slip at the end of the year and send in to the Internal Revenue Service. Ordinarily they send a copy to the taxpayer or to the recipient. Now it seems to me that we could expand this information return system and require that the payor of interest or dividends of say \$10 or more during the year—or perhaps of any amount—will at the end of the year file an information return with the Internal Revenue Service listing the taxpayer's account number—you know, last year we authorized the use of these account numbers—and send an information copy of that return to the taxpayer. Now I am quite well satisfied that if people receive at the end of the year a statement from the bank or from the corporation saying "Dear Mr. So and So, you receive so much interest or so much interest was credited to your account during the year, or you receive so much in

dividends and this amount of the dividends is taxable income"—with a copy of that going to the Internal Revenue Service, we are not going to have very much missed revenue.

Mr. COAR. Now that system that you recommend is a very simple one, considering that they are converting Internal Revenue almost to automation entirely, using computers and so forth, things that will automatically pull out the account number, and they can attach all of this information that you mention to it.

Senator MILLER. That's right. However, I want to make it clear that this is not going to happen overnight. Last year we authorized the Internal Revenue Service to equip itself with several of these very expensive and very complex computers which record this information on magnetic tapes and can store on one roll millions of items of information. It is going to take 2 or 3 years for all of these computers to become installed and ready to go. But when they are, the payor of interest or dividends by sending in the account number to the Internal Revenue Service will enable the Internal Revenue Service through these computers to match up all interest or dividends that are attributable to that account number so that they will know exactly how much interest and dividend income a particular taxpayer received.

Mr. COAR. Senator, is there a possibility, for example, of an elderly couple who jointly receive \$90 as a small dividend from a piece of stock that they have held for years, having this 20 percent automatically taken out? How are they going to get that back? Will they have to write a letter to Internal Revenue or do they get it back?

Senator MILLER. Well, I want to be fair about this. The proposed law provides that people who do not expect to owe any tax can file an exemption certificate with the payor saying that they don't expect to owe any tax and therefore, the payor does not withhold any tax on them. Also, in the case of individuals under 18 years of age, they can file an exemption certificate. But you can understand how you might estimate that you wouldn't owe any tax and I might estimate that I wouldn't owe any tax but you might be right and I might be wrong, I might owe some tax. And so it's going to be discriminatory between you and me. And then also, just visualize the millions of exemption certificates that are going to have to be filed. And they will have to be updated, and this will mean filing these millions of exemption certificates every year with the banks and the corporations, and having them processed. And when young people become over 18 then they have to file an exemption certificate or have to file a withdrawal of an exemption certificate. This is a horribly complex mechanism for giving people the benefit of not having to have this tax withheld. But I want to be fair about it and point out that there is a provision in here to cover that situation. But in my judgment is a highly unworkable, complex burden upon the businesses and also upon those people on whom this tax burden would otherwise fall. Now there is another thing that ought to be brought out. If you expect to owe even \$1 of income tax, then you can't file an exemption certificate and they are going to withhold 20 percent on your interest or dividend income. They say you can then file a claim for refund and you can do so every quarter during the year. And they say also that you will get your refund quite promptly. But I can also visualize a horrible administrative complexity here because there will be literally millions of these income tax refund claims being filed. It's going to cause a lot of these people who can't really understand how to make out these compli-

cated claims for refund—it is going to cause them to go to the trouble of making them out; it is going to require a lot more Federal employees to process these. So while they do cover it, I think they cover it in a most unsatisfactory, complex way.

Mr. COAR. Is there a possibility, Senator MILLER, that the amount of money that is returned might all be eaten up by the administration of this plan, because, as you say, they will have to add probably thousands of employees to handle this tremendous amount of paperwork that is being added?

Senator MILLER. Well, I think you can say this—that the amount of income tax that will be lost to the Internal Revenue Service because of the extra expense of businessmen to implement this will probably be substantial; but on the other hand, if there is a lot of revenue that is being missed, the Federal Government expects to have a net take from this. They will lose some tax from the extra expenses that the businessmen will be allowed to deduct. But they expect to catch more revenue by having this withholding. But my point is that I think it is overestimated—this amount of leaking income—and furthermore, they can get it if they will put in a sensible information return system.

Mr. MANSFIELD. Mr. President, I suggest the absence of a quorum.

The PRESIDING OFFICER (Mr. SMITH of Massachusetts in the chair). Does the Senator wish to take the time for the quorum call out of the time remaining on the amendment?

Mr. MANSFIELD. Yes.

The PRESIDING OFFICER. The clerk will call the roll.

The Chief Clerk proceeded to call the roll.

Mr. MANSFIELD. Mr. President, I ask unanimous consent that the order for the quorum call be rescinded.

The PRESIDING OFFICER. Without objection, it is so ordered.

Mr. MANSFIELD. Mr. President, I yield back all the time on this side.

Mr. DOUGLAS. I yield back all the time on our side.

The PRESIDING OFFICER. All time having been yielded back, the question is on the amendment to strike out section 19 and insert new language. The yeas and nays have been ordered, and the clerk will call the roll.

The Chief Clerk proceeded to call the roll.

Mr. DOUGLAS. Mr. President, a parliamentary inquiry.

The PRESIDING OFFICER. The Senator from Illinois will state it.

Mr. DOUGLAS. Is this a quorum call or a rollcall on a yea-and-nay vote?

The PRESIDING OFFICER. This is a yea-and-nay vote.

The Chief Clerk resumed the call of the roll.

Mr. DOUGLAS. Mr. President, a further parliamentary inquiry.

The PRESIDING OFFICER. The Senator from Illinois will state it.

Mr. DOUGLAS. Will the Chair state the question which is now before the Senate?

The PRESIDING OFFICER. The question is on the committee amendment beginning on page 307, after line 8, extending through page 369.

Mr. DOUGLAS. A further parliamentary inquiry.

The PRESIDING OFFICER. The Senator from Illinois will state it.

Mr. DOUGLAS. Am I correct in my understanding that the committee amendment would eliminate the withholding feature on dividends and interest embodied in the House bill?

The PRESIDING OFFICER. That is correct.

Mr. DOUGLAS. I thank the Presiding Officer.

The PRESIDING OFFICER. And insert new language.

Mr. MANSFIELD. Mr. President, a further parliamentary inquiry.

The PRESIDING OFFICER. The Senator from Montana will state it.

Mr. MANSFIELD. Mr. President, is this amendment carried on page 16768 of the CONGRESSIONAL RECORD for yesterday, in the first column, as follows: "Fourth. The withholding committee amendment, on page 307, line 9, through page 369, line 19"?

The PRESIDING OFFICER. That is correct.

Mr. MANSFIELD. In other words, this is the withholding amendment?

The PRESIDING OFFICER. Yes.

Mr. DIRKSEN. Mr. President, a parliamentary inquiry.

The PRESIDING OFFICER. The Senator from Illinois will state it.

Mr. DIRKSEN. As I understand the situation, the amendment that is pending is a committee amendment to strike the withholding provision and to insert instead the so-called reporting provision?

The PRESIDING OFFICER. The Senator is correct.

Mr. DIRKSEN. And Senators who are for the amendment to eliminate the withholding provision should vote "yea"?

The PRESIDING OFFICER. That is correct.

Mr. DOUGLAS. Mr. President—

The PRESIDING OFFICER. The Senator from Illinois.

Mr. DOUGLAS. This situation is becoming more complicated by the minute. I had understood that the motion was to strike the withholding provision on dividends and interest included in the House bill, and nothing more.

The PRESIDING OFFICER. No; and to insert new language to take its place, relating to reporting.

Mr. DOUGLAS. To insert new language on reporting?

The PRESIDING OFFICER. Yes.

The clerk will call the roll.

The Chief Clerk called the roll.

Mr. MANSFIELD (after having voted in the negative). Mr. President, on this vote I have a pair with the Senator from Washington [Mr. MAGNUSON]. If he were present and voting he would vote "yea." If I were at liberty to vote I would vote "nay." Therefore, I withhold my vote.

Mr. HUMPHREY (after having voted in the negative). Mr. President, on this vote I have a pair with the Senator from Missouri [Mr. SYMINGTON]. If he were present and voting he would vote "yea." If I were at liberty to vote I would vote "nay." I withhold my vote.

Mr. HUMPHREY. I announce that the Senator from Nevada [Mr. BIBLE], the Senator from New Mexico [Mr. CHAVEZ], the Senator from Arizona [Mr.

HAYDEN], the Senator from Washington [Mr. MAGNUSON], and the Senator from Oregon [Mrs. NEUBERGER] are absent on official business.

I further announce that the Senator from New Mexico [Mr. ANDERSON], the Senator from Alaska [Mr. GRUENING], the Senator from Oregon [Mr. MORSE], and the Senator from Missouri [Mr. SYMINGTON] are necessarily absent.

On this vote, the Senator from Oregon [Mr. MORSE] is paired with the Senator from Alaska [Mr. GRUENING]. If present and voting, the Senator from Oregon would vote "nay," and the Senator from Alaska would vote "yea."

On this vote, the Senator from Washington [Mr. MAGNUSON] is paired with the Senator from Montana [Mr. MANSFIELD]. If present and voting, the Senator from Washington would vote "yea," and the Senator from Montana would vote "nay."

On this vote, the Senator from Minnesota [Mr. HUMPHREY] is paired with the Senator from Missouri [Mr. SYMINGTON]. If present and voting, the Senator from Minnesota would vote "nay," and the Senator from Missouri would vote "yea."

Mr. KUCHEL. I announce that the Senator from New York [Mr. JAVITS], the Senator from New Hampshire [Mr. MURPHY], and the Senator from Wisconsin [Mr. WILEY] are necessarily absent.

If present and voting, the Senator from New York [Mr. JAVITS], and the Senator from New Hampshire [Mr. MURPHY] would each vote "yea."

The result was announced—yeas 66, nays 20, as follows:

[No. 224 Leg.]

YEAS—66

Aiken	Fong	Mundt
Allott	Fulbright	Muskie
Beall	Goldwater	Pastore
Bennett	Hickenlooper	Pearson
Boggs	Hickey	Prouty
Bottum	Hill	Randolph
Bush	Holland	Robertson
Butler	Hruska	Russell
Byrd, Va.	Jackson	Saltonstall
Byrd, W. Va.	Johnston	Scott
Cannon	Jordan, N.C.	Smathers
Capehart	Jordan, Idaho	Smith, Maine
Carlson	Keating	Sparkman
Case	Kuchel	Stennis
Church	Lausche	Talmadge
Cotton	Long, Mo.	Thurmond
Curtis	Long, La.	Tower
Dirksen	McCarthy	Williams, N.J.
Eastland	McClellan	Williams, Del.
Ellender	Miller	Yarborough
Engle	Monroney	Young, N. Dak.
Ervin	Morton	Young, Ohio

NAYS—20

Bartlett	Gore	McNamara
Burdick	Hart	Metcalf
Carroll	Hartke	Moss
Clark	Kefauver	Pell
Cooper	Kerr	Proxmire
Dodd	Long, Hawaii	Smith, Mass.
Douglas	McGee	

NOT VOTING—14

Anderson	Humphrey	Murphy
Bible	Javits	Neuberger
Chavez	Magnuson	Symington
Gruening	Mansfield	Wiley
Hayden	Morse	

So the committee amendment on page 307, after line 8, was agreed to.

Mr. BYRD of Virginia. Mr. President, I move to reconsider the vote by which the committee amendment was agreed to.

Mr. MANSFIELD. Mr. President, I move to lay that motion on the table.

The motion to lay on the table was agreed to.

Mr. MANSFIELD obtained the floor.

Mr. MANSFIELD. Mr. President, I yield to the Senator from Oklahoma.

Mr. KERR. Mr. President, I ask unanimous consent that I may have a colloquy with the Senator from Illinois [Mr. DOUGLAS] and the Senator from Tennessee [Mr. GORE] to obtain some information in which both I and other Senators will be interested in determining the course for the evening. I should like to have the attention of the Senator from Delaware [Mr. WILLIAMS] and the Senator from Virginia [Mr. BYRD].

Under our unanimous-consent agreement, the next amendment to be considered would be the second committee amendment, which would eliminate section 482 entirely from the bill. I should like to ask the Senator from Illinois [Mr. DOUGLAS] and the Senator from Tennessee [Mr. GORE] if they would be agreeable to skipping that amendment and the third amendment and going to the fifth amendment, discussing those in order to see whether or not yea and nay votes would be requested on those amendments.

Mr. DOUGLAS. Mr. President, I should like to oblige my good friend the Senator from Oklahoma, but I hope he will adhere to the sequence laid out. When he does so, I wish to propose an amendment to the committee amendment.

Mr. KERR. We have unanimous consent to proceed with the sequence as set out in the RECORD. Unless changed by unanimous consent, that will be the procedure.

Mr. DOUGLAS. I must reluctantly object.

Mr. KERR. Then, Mr. President, I ask that the second committee amendment be stated.

The PRESIDING OFFICER. The amendment will be stated.

The LEGISLATIVE CLERK. At the top of page 52 it is proposed to strike out all down to and including line 22 on page 57, the same being an amendment to section 482.

The committee amendment is, as follows:

At the top of page 52, to strike out:

"SEC. 6. AMENDMENT OF SECTION 482.

"(a) IN GENERAL.—Section 482 (relating to allocation of income and deductions among taxpayers) is amended by adding at the end thereof the following new subsection:

"(b) SALES AND PURCHASES WITHIN A RELATED GROUP WHICH INCLUDES A FOREIGN ORGANIZATION.—

"(1) IN GENERAL. In applying subsection (a) to sales of tangible property within a group of organizations—

"(A) owned or controlled directly or indirectly by the same interests, and

"(B) at least one of which is a domestic organization and at least one of which is a foreign organization,

the Secretary or his delegate may allocate the taxable income of the group arising from such sales in the manner set forth in paragraph (2). This subsection shall not apply with respect to any sale of tangible property for which the taxpayer can establish an arm's length price (within the meaning of paragraph (4)).

"(2) METHODS OF ALLOCATION.—

"(A) CONSIDERATION OF CERTAIN FACTORS.—Except as provided in subparagraph (B), the allocation referred to in paragraph (1) shall be made by the Secretary or his delegate by taking into consideration that portion of the following factors which is attributable to the United States and that portion thereof which is not attributable to the United States—

"(i) assets of the group, to the extent used in the production, distribution, and sale of the property,

"(ii) compensation of officers and employees, to the extent attributable to the production, distribution, and sale of the property, and

"(iii) advertising, selling, and sales promotion expenses (including technical and servicing expenses), to the extent attributable to the property.

Such method of allocation may also give consideration to other factors, including the special risks (if any) of the market in which the property is sold.

"(B) ALTERNATIVE METHODS.—If the taxpayer establishes to the satisfaction of the Secretary or his delegate that an alternative method of allocation clearly reflects the income of each member of the group with respect to the property referred to in paragraph (1), such alternative method shall be used (in lieu of the method provided in subparagraph (A)).

"(3) SPECIAL RULES.—In applying the method of allocation referred to in paragraph (2) (A), the following rules shall be applied:

"(A) ADJUSTED BASIS OF ASSETS.—The values to be assigned to the assets referred to in paragraph (2) (A) (1) is their adjusted basis in the hands of the taxpayer or, if such basis is not available in the case of a foreign organization, then their book values, adjusted to approximate their adjusted basis.

"(B) INCLUDIBLE ASSETS.—The assets referred to in paragraph (2) (A) (1) include real property and tangible personal property (whether owned or leased by a member of the group), but do not include inventory and stock in trade.

"(4) ARM'S LENGTH PRICE DEFINED.—For purposes of this subsection, the term "arm's length price" means—

"(A) the price at which tangible property similar or comparable to the property referred to in paragraph (1) generally is or can be sold in transactions in the same areas involving unrelated persons and made under similar conditions of sale; and

"(B) if subparagraph (A) does not apply, the price at which tangible property similar or comparable to the property referred to in paragraph (1) is sold in the same or other areas under similar circumstances and in transactions involving unrelated persons, with adjustment for material differences in quantity, marketing conditions (including customs duties and transportation costs), and other relevant factors.

Subparagraph (B) shall apply only if the adjustment referred to therein is properly determinable.

"(5) SALES COMMISSIONS.—The Secretary or his delegate shall by regulation prescribe rules for the allocation of commissions arising from sales of tangible property within a group of organizations described in paragraph (1). Such rules shall be consistent with the principles specified in the other paragraphs of this subsection.

"(6) GROSSLY INADEQUATE ASSETS, ETC., OUTSIDE UNITED STATES.—In allocating taxable income under this subsection, no amount shall be allocated to a foreign organization whose assets, personnel, and office and other facilities which are not attributable to the United States are grossly inadequate for its activities outside the United States.

"(7) INFORMATION NECESSARY FOR CONSIDERATION OF FACTORS.—In the case of any transaction to which paragraph (2) (A) applies, if—

"(A) the information submitted with respect to the group of organizations is insufficient for the proper application of the method of allocation set forth in the first sentence of such paragraph, and

"(B) upon request of the Secretary or his delegate, such group fails to furnish such additional information with respect to such transaction as may be reasonably supplied, the Secretary or his delegate may estimate the taxable income arising from such transaction and may allocate such taxable income among the members of the group or to any single member thereof.

"(8) TREATMENT OF FOREIGN TAXES.—

"(A) For purposes of this subsection, taxable income shall be determined without regard to any income, war profits, or excess profits taxes paid to any foreign country or to any possession of the United States.

"(B) Where the application of this subsection results in a decrease in the taxable income of any foreign organization and an increase in the taxable income of any domestic organization, then any of the taxes referred to in subparagraph (A) paid by such foreign organization and attributable to the taxable income so transferred shall be treated for purposes of this chapter—

"(i) as paid by such domestic organization, and

"(ii) as not paid by such foreign organization."

"(b) CLERICAL AMENDMENT.—Section 482 is amended by striking out 'In any case of two or more organizations' and inserting in lieu thereof the following:

"(a) GENERAL RULE.—In the case of two or more organizations'.

"(c) EFFECTIVE DATE.—The amendments made by this section shall apply with respect to taxable years beginning after December 31, 1962."

Mr. DOUGLAS. Mr. President, a parliamentary inquiry.

The PRESIDING OFFICER. The Senator will state it.

Mr. DOUGLAS. Is that the amendment now before the Senate?

The PRESIDING OFFICER. The Senator is correct.

Mr. DOUGLAS. Mr. President, I send to the desk an amendment to the committee amendment and ask that it be stated, and that I be privileged to explain the amendment.

The PRESIDING OFFICER. The amendment of the Senator from Illinois will be stated.

The LEGISLATIVE CLERK. The Senator from Illinois proposes on page 57, after line 22, to insert the following new section:

SEC. 20. REPEAL OF WITHHOLDING OF INCOME TAX AT SOURCE ON WAGES.

Effective with respect to wages paid on or after January 1, 1963, chapter 24 (relating to collection of income tax at source on wages) is hereby repealed.

Renumber succeeding sections of the bill.

Mr. DOUGLAS. Mr. President, the Senate has just voted by an overwhelming majority not to apply withholding to dividends and interest. That is obviously the considered judgment of the Senate. If we do so, how can we consistently withhold taxes on wages and salaries? Now that we have stricken the provision

for withholding of dividends and interest, in all logic we must strike out withholding on wages and salaries. I ask for the yeas and nays.

Mr. MANSFIELD. Mr. President, I move to lay that amendment on the table.

The PRESIDING OFFICER. The question is on agreeing to the motion of the Senator from Montana.

Mr. DOUGLAS. Mr. President, I ask for the yeas and nays on the motion to lay on the table.

The yeas and nays were ordered.

Mr. DOUGLAS. Mr. President, a parliamentary inquiry.

The PRESIDING OFFICER. The Senator will state it.

Mr. DOUGLAS. What is the motion which is now before the Senate?

The PRESIDING OFFICER. The question is on the motion of the Senator from Montana to table the amendment of the Senator from Illinois to the committee amendment.

Mr. DOUGLAS. Then do I correctly understand that Senators, who believe in retaining withholding on wages and salaries even though we do not have withholding on dividends and interest should vote "aye"——

The PRESIDING OFFICER. The Chair informs the Senator that his question is not a proper parliamentary inquiry.

Mr. HOLLAND. Mr. President, a parliamentary inquiry.

The PRESIDING OFFICER. The Senator will state it.

Mr. HOLLAND. Have the yeas and nays been ordered on the motion to lay on the table?

The PRESIDING OFFICER. The yeas and nays have been ordered.

Mr. DIRKSEN. Mr. President, a parliamentary inquiry.

The PRESIDING OFFICER. The Senator will state it.

Mr. DIRKSEN. Mr. President, if we can have absolute quiet for a moment, is it a proper parliamentary inquiry to say that the proposal now before the Senate, if agreed to, would put an end to withholding on all wages in the country?

Mr. DOUGLAS. Mr. President, is that a proper parliamentary inquiry?

The PRESIDING OFFICER. The Chair rules that it is not a proper parliamentary inquiry.

Mr. DIRKSEN. Mr. President, I ask that the amendment be stated for the information of the Senate.

Mr. HUMPHREY. Mr. President, a motion to lay on the table has been made.

Mr. DIRKSEN. I know; but Senators are entitled to know what they are asked to lay on the table.

The PRESIDING OFFICER. The Senator is correct.

Mr. DIRKSEN. I ask that the amendment be repeated to the Senate for the information of the Senate.

The PRESIDING OFFICER. The clerk will state the amendment.

Mr. DIRKSEN. May the clerk read slowly and distinctly?

The LEGISLATIVE CLERK. On page 57, after line 22, it is proposed to insert the following new section:

SEC. 20. REPEAL OF WITHHOLDING OF INCOME TAX AT SOURCE ON WAGES.

Effective with respect to wages paid on or after January 1, 1963, chapter 24 (relating to collection of income tax at source on wages) is hereby repealed.

Renumber succeeding sections of the bill.

Mr. DIRKSEN. Mr. President, I suggest the absence of a quorum.

Mr. HOLLAND. Mr. President, a parliamentary inquiry.

The PRESIDING OFFICER. Does the Senator from Illinois withhold his suggestion of the absence of a quorum?

Mr. DIRKSEN. I withhold my suggestion.

The PRESIDING OFFICER. The Senator from Florida will state his inquiry.

Mr. HOLLAND. Would it be appropriate to ask, by way of a parliamentary inquiry, whether or not the amendment, if adopted, would put an end to withholding of taxes from the salaries of Members of Congress and the withholding of taxes from the wages of all employees in the Government?

Mr. MANSFIELD. Mr. President, I make the point of order that that is not a proper parliamentary inquiry.

The PRESIDING OFFICER. It is not a parliamentary inquiry.

The yeas and nays have been ordered, and the clerk will call the roll.

The legislative clerk called the roll.

Mr. HUMPHREY. I announce that the Senator from Nevada [Mr. BIBLE], the Senator from New Mexico [Mr. CHAVEZ], the Senator from Connecticut [Mr. DODD], the Senator from Mississippi [Mr. EASTLAND], the Senator from California [Mr. ENGLE], the Senator from Arkansas [Mr. FULBRIGHT], the Senator from Alabama [Mr. HILL], the Senator from Tennessee [Mr. KEFAUVER], the Senator from Washington [Mr. MAGNUSON], the Senator from Hawaii [Mr. LONG], and the Senator from Oregon [Mrs. NEUBERGER] are absent on official business.

I further announce that the Senator from Oregon [Mr. MORSE], the Senator from New Mexico [Mr. ANDERSON], the Senator from Pennsylvania [Mr. CLARK], the Senator from Tennessee [Mr. GORE], the Senator from Alaska [Mr. GRUENING], and the Senator from Missouri [Mr. SYMINGTON] are necessarily absent.

I further announce that, if present and voting, the Senator from Mississippi [Mr. EASTLAND], the Senator from California [Mr. ENGLE], the Senator from Arkansas [Mr. FULBRIGHT], and the Senator from Alabama [Mr. HILL] would each vote "yea."

On this vote, the Senator from Oregon [Mr. MORSE] is paired with the Senator from Washington [Mr. MAGNUSON]. If present and voting, the Senator from Oregon would vote "nay," and the Senator from Washington would vote "yea."

On this vote, the Senator from Pennsylvania [Mr. CLARK] is paired with the Senator from Missouri [Mr. SYMINGTON]. If present and voting, the Senator from Pennsylvania would vote "nay," and the Senator from Missouri would vote "yea."

Mr. KUCHEL. I announce that the Senator from New York [Mr. JAVITS], the

Senator from New Hampshire [Mr. MURPHY], and the Senator from Wisconsin [Mr. WILEY] are necessarily absent.

The Senator from Massachusetts [Mr. SALTONSTALL] is detained on official business and if present and voting would vote "yea."

On this vote, the Senator from New York [Mr. JAVITS] is paired with the Senator from New Hampshire [Mr. MURPHY]. If present and voting, the Senator from New York would vote "yea," and the Senator from New Hampshire would vote "nay."

The result was announced—yeas 62, nays 17, as follows:

[No. 225 Leg.]

YEAS—62

Aiken	Hayden	Monroney
Allott	Hickenlooper	Morton
Beall	Hickey	Moss
Bennett	Holland	Mundt
Boggs	Hruska	Muskie
Bottum	Humphrey	Pastore
Bush	Jackson	Pearson
Butler	Johnston	Pell
Byrd, Va.	Jordan, N.C.	Prouty
Byrd, W. Va.	Keating	Proxmire
Cannon	Kerr	Randolph
Carlson	Kuchel	Robertson
Case	Long, Mo.	Smathers
Church	Long, La.	Smith, Mass.
Cooper	Mansfield	Sparkman
Curtis	McCarthy	Williams, N.J.
Dirksen	McClellan	Williams, Del.
Ellender	McGee	Yarborough
Ervin	McNamara	Young, N. Dak.
Fong	Metcalf	Young, Ohio
Hart	Miller	

NAYS—17

Bartlett	Goldwater	Smith, Maine
Burdick	Hartke	Stennis
Capehart	Jordan, Idaho	Talmadge
Carroll	Lausche	Thurmond
Cotton	Russell	Tower
Douglas	Scott	

NOT VOTING—21

Anderson	Fulbright	Magnuson
Bible	Gore	Morse
Chavez	Gruening	Murphy
Clark	Hill	Neuberger
Dodd	Javits	Saltonstall
Eastland	Kefauver	Symington
Engle	Long, Hawaii	Wiley

So the motion to lay on the table Mr. DOUGLAS' amendment to the committee amendment was agreed to.

Mr. KERR. Mr. President, I move that the action whereby the motion to lay on the table was agreed to be reconsidered.

Mr. HUMPHREY. I move to lay that motion on the table.

The motion to lay on the table was agreed to.

Mr. KERR. Mr. President, I now ask the distinguished Senator from Tennessee [Mr. GORE] and the distinguished Senator from Illinois [Mr. DOUGLAS] if they have objection to the adoption of the second or the amendments, together with the others, and to their becoming a part of the text, subject to further amendment.

Mr. GORE. Will not the Senator from Oklahoma pass over the second and third amendments, and leave them as they are?

Mr. KERR. We will pass over the second and third amendments.

I now make the same inquiry with reference to the fifth amendment. That is the clearing land committee amendment.

Mr. GORE. I have no objection to passing to the fourth and fifth remaining amendments which are riders to the bill.

Mr. KERR. This is one such amendment.

Mr. GORE. I have no objection.

Mr. KERR. To its becoming a part of the text of the bill?

Mr. GORE. I have no objection to its consideration.

Mr. KERR. Does the Senator believe there will be a request for the yeas and nays on that amendment?

Mr. GORE. I have no intention of making such a request. I cannot speak for other Senators.

Mr. KERR. Mr. President, if it be in order, I should like to ask if other Senators expect to make such a request.

I ask the Senator from Tennessee the same question with reference to the seventh amendment, which relates to the determination of the number of stockholders in small corporations.

Mr. GORE. I make the same response.

Mr. KERR. Mr. President, I ask if other Senators expect to ask for a yeas-and-nay vote on that amendment.

The eighth amendment is the amendment with reference to the Twin Cities Railway.

Mr. GORE. I should like to say to the Senator from Oklahoma that I have no intention of making a fight on any of these amendments. They are in the nature of bills for private relief. They have no place in this bill. One such bill was vetoed by President Eisenhower. As amendments, they are now riders on the bill. But there is a limit to the number of fights I feel I can afford to make on the bill, so I simply call this fact to the attention of the Senate and express no further objection to any of these amendments. I think there should be an explanation to the Senate of each amendment.

Mr. KERR. Yes.

Mr. DOUGLAS. Mr. President, I also believe there should be a full explanation of the Twin Cities Railway amendment. I hope the amendment will be explained in full. Like the Senator from Tennessee, I have no present intention of asking for a yeas-and-nay vote on that amendment, but I think it ought to be thoroughly explained and that the Senate as a whole should have a chance to pass upon it without giving automatic approval to it without discussion.

Mr. KERR. Mr. President, I ask that we may begin with the 7th amendment and proceed with an explanation discussion deliberation and action on the amendment. In the event it should develop that Senators wish to ask for a yeas-and-nay vote on any of them I ask that the one with reference to which the vote is requested go over until tomorrow and that the Senate proceed to consider the 7th, 8th, 9th, 10th, and 11th amendments listed, on the basis that if the Senate wishes to act on them after an explanation, it may be permitted to do so, but that if a controversy arises and a yeas-and-nay vote is sought, the particular amendment with reference to which the yeas-and-nay vote may be sought go over until tomorrow.

Mr. CARROLL. Mr. President, will the Senator from Oklahoma yield?

Mr. KERR. I yield. I assume the Senator reserves the right to object.

Mr. CARROLL. Yes. I ask unanimous consent that I may be permitted to speak on the Douglas amendment which related to the repeal of the withholding of tax on salaries and wages. It will take me only a minute or two to do so.

Mr. KERR. Could not the Senator do that after the present discussion has been completed?

Mr. CARROLL. I should like to make my statement now. It will take only a minute. I ask unanimous consent that I may do so.

Mr. KERR. Mr. President, I ask unanimous consent that the Senator from Colorado be granted 1 minute.

The PRESIDING OFFICER. Is there objection? The Chair hears none, and it is so ordered.

Mr. CARROLL. The reason why the Senator from Colorado registered his vote against the motion to table was this: When the able Senator from Illinois [Mr. DOUGLAS] offered his amendment, he asked for the yeas and nays. Before he had an opportunity to explain his amendment, a motion to table was made. I object to such a procedure because I believe the able Senator from Illinois had a right to explain to the Senate the purpose of his amendment. If I may draw upon my imagination, I believe the Senator from Illinois sought to demonstrate the difference between the votes of Senators who voted against the withholding of tax on dividends and interest and the votes of Senators who might vote for the withholding of the tax on wages and salaries. I think he had a right to explain his position. He was denied that right; therefore, I voted against the motion to table. I am not against the withholding of taxes on salaries and wages. This has been an important part of our tax statutes for many years.

I think the Senate has not acted in accordance with the democratic process. I do not think it is in the interest of the Senate to deny to any Senator the right to explain his amendment, even for only 2 or 3 minutes; even though it is known that the amendment will be defeated; and even though the Senator who offers the amendment knows it will be defeated, but merely wishes to create an issue to carry to the people of the country.

That is the statement I wished to make at this time. I am not wholly in opposition to the motion of the majority leader. I am not in opposition to the principle of withholding taxes on salaries and wages. That has been a part of the revenue system of the country for 20 years. But I believe the able senior Senator from Illinois had a right to present his amendment. I think the Senate should have had a right to debate this question for a reasonable length of time.

Mr. President, with that observation in the RECORD, I withdraw my objection.

Mr. GORE. Mr. President, reserving the right to object, do I correctly understand the Senator from Oklahoma to request consent that amendments 2 and 3 be passed over?

Mr. KERR. Yes; until tomorrow.

Mr. GORE. Until tomorrow?

Mr. KERR. That is correct.

Mr. GORE. I thank the Senator from Oklahoma. Having spoken for about 2 hours today, I am perfectly willing to have them passed over.

Mr. LAUSCHE. Mr. President, reserving the right to object, let me say that I voted for a definite reason against the motion to lay on the table. In my opinion, ultimately the country would be better off if we created a taxpaying situation in which every citizen would have brought to his mind the exact amount of taxes he was paying. A tax consciousness has been developing among the people of the Nation. I think it has been reflected by the President's recommendation that taxes on the Federal level be reduced, and also by the recommendation of the Governor of California that taxes in California be reduced. If each citizen knew the tremendous burden of taxes which he pays, we would not be spending their money as extravagantly as we are on the floor of the Senate.

Mr. DOUGLAS. Mr. President, reserving the right to object, I should like to make some comments on this question.

Mr. KERR. Does the Senator from Illinois wish to make his comments before the proposed unanimous-consent agreement is entered into?

Mr. DOUGLAS. Yes.

Mr. KERR. Then, Mr. President, I withdraw the request.

Mr. DOUGLAS. Mr. President, I believe the withholding method is an efficient way of collecting taxes, and I believe it should be universal. But it is not universal now. It now applies to wage earners and salary earners, but it does not apply to the recipients of dividends and interest. I and the 19 other Senators who voted with me tried to make it universal, but we were defeated by an overwhelming vote. Having been defeated by that overwhelming vote, it seems to me that it is not consistent to maintain withholding against anyone. A Senator cannot consistently maintain that withholding should be applied to low paid wage earners and salary earners but should not be applied to the higher income recipients of dividends and interest.

My position is that withholding should be applied either to everyone or else not to anyone. I believe that is a basically sound position.

Senators who voted against withholding on dividends and interest, but who voted in favor of withholding on wages and salaries are in a basically inconsistent position; and if they examine their consciences, I believe they will find it very hard to justify taking that position, and I believe they will also find it difficult to justify it to the voters.

Mr. CARROLL. Mr. President, will the Senator from Illinois yield?

Mr. DOUGLAS. I yield.

Mr. CARROLL. Did the Senator from Colorado ever confer with the Senator from Illinois about his amendment?

Mr. DOUGLAS. No.

Mr. CARROLL. The Senator from Illinois did not seriously declare in favor

of repealing the withholding taxes on wages and salaries, did he?

Mr. DOUGLAS. I knew I would be defeated on that amendment, just as we were defeated on the proposal to have withholding on dividends and interest. But I thought the amendment would point an interesting moral. I did not confide in a single person, and I am very glad I did not.

Mr. CARROLL. I had no idea that this amendment was coming up. But again I take the position that, whatever the reasons of the Senator from Illinois were, and whatever the motivation of the Senator from Illinois was, he had a right to be heard on his amendment, without being shut off by a motion to table.

Mr. SCOTT. Mr. President—

Mr. CARROLL. I have not finished. The Senator from Illinois has yielded to me.

I am in favor of a motion to table after debate has been exhausted, but I do not like to see a motion to table used as a means of shutting off reasonable, intelligent debate. I am opposed to filibusters and to the long-drawn-out debate procedures which seem to be prevalent in this body. My record shows that.

Whenever a Senator submits an amendment, I think he is entitled to be heard on it, no matter how facetious it might seem.

Mr. DOUGLAS. I assure the Senator that it was not facetious.

Mr. CARROLL. I ask the Senator from Illinois, what his purpose was in submitting the amendment.

Mr. DOUGLAS. The purpose was to inform the people of the United States where Senators stand in this connection.

Mr. MANSFIELD. Mr. President, will the Senator from Illinois yield?

Mr. CARROLL. Mr. President, has not the Senator from Illinois yielded to me? We have not finished our colloquy, have we?

Mr. DOUGLAS. No.

Mr. CARROLL. Let us not—

Mr. HOLLAND. Mr. President, I request the regular order.

Mr. CARROLL. What is the regular order?

Mr. DOUGLAS. Mr. President, who has the floor?

The PRESIDING OFFICER. The Senator from Illinois has the floor.

Mr. DOUGLAS. Mr. President, I shall be glad to yield to the Senator from Colorado for a question.

Mr. CARROLL. I understood the Senator from Illinois to say he had a serious purpose in submitting the amendment—

Mr. HOLLAND. Mr. President, I demand the regular order.

The PRESIDING OFFICER. The Senator from Illinois has the floor, and he can yield only for a question.

Mr. DOUGLAS. I yield to the Senator from Colorado for a question.

Mr. CARROLL. I am putting the question now, if Senators will be patient; I am laying the foundation for the question.

Mr. DOUGLAS. The Senator is laying the predicate of a question as the Senator from Florida often says.

Mr. CARROLL. The Senator from Illinois has had experience in laying the predicate.

Mr. HOLLAND. Mr. President, I demand the regular order.

The PRESIDING OFFICER. The Senator from Illinois has the floor, and he can yield only for a question.

Mr. DOUGLAS. I yield for a question.

Mr. CARROLL. What was the purpose of the Senator from Illinois in submitting the amendment?

Mr. DOUGLAS. My purpose was to find out whether Members of the Senate were consistent or were inconsistent.

Mr. CARROLL. Did the Senator from Illinois have an opportunity to debate his amendment?

Mr. DOUGLAS. I did not.

Mr. CARROLL. I think that answers the question.

Mr. HART. Mr. President, will the Senator from Illinois yield for a question?

Mr. DOUGLAS. I yield for a question.

Mr. HART. Is it not true that the Senator from Illinois said that Senators who voted against withholding on dividends and interest and then voted to lay his amendment on the table are in an inconsistent position?

Mr. DOUGLAS. That is correct.

Mr. HART. Let me ask this question: Having myself voted in favor of withholding on dividends and interest and having voted to lay on the table the amendment of the Senator from Illinois—

Mr. DOUGLAS. The Senator from Michigan is completely consistent; and the Senator from Illinois is also completely consistent, because he wants withholding either to be applied to everyone or, if it cannot be applied to everyone he thinks it should not be applied to anyone. But Senators who voted to put the screws on the working people, but to let the higher income dividend and interest recipients off the hook are inconsistent.

Mr. CARROLL. Mr. President, will the Senator from Illinois yield for a further question?

Mr. DOUGLAS. Yes; but I yield for a question only.

Mr. CARROLL. The question I put is this: Under the motion to lay on the table, did the Senator from Illinois have an opportunity to discuss his amendment?

Mr. DOUGLAS. I did not.

Mr. CARROLL. Therefore the making of the motion to lay on the table prevented the Senator from Illinois discussing his amendment, did it not?

Mr. DOUGLAS. That is correct.

Mr. CARROLL. And, therefore, Senators who voted in favor of the motion to lay on the table were not necessarily in favor of the Senator's amendment, were they?

Mr. DOUGLAS. I am sure of that. I am sure that neither the Senator from South Carolina nor the Senator from Mississippi favored it. But they do not believe in artificially shutting off debate by means of a premature motion to lay on the table. If we are going to give medals for consistency, I am ready to give them medals for consistency—but

they should be leather medals, not bronze stars.

Mr. SCOTT. Mr. President, will the Senator from Illinois yield?

Mr. DOUGLAS. I yield.

Mr. SCOTT. I should like to address a question to the Senator from Illinois, in view of the questions of the Senator from Colorado—namely, whether a position on both sides of the question is available to all Senators.

Mr. DOUGLAS. I do not understand the question.

Mr. KERR. Mr. President—

Mr. DOUGLAS. Mr. President, who has the floor?

Mr. KERR. I thought the Senator from Illinois had yielded.

Mr. MANSFIELD. Mr. President, does the Senator from Illinois withdraw his reservation of objection?

Mr. TOWER. Mr. President, will the Senator from Illinois yield for a question?

Mr. DOUGLAS. Certainly.

Mr. TOWER. Will the Senator from Illinois inform me whether the amendment he offered is a part of the program and platform of the John Birch Society?

Mr. DOUGLAS. I do not think so.

The Senator from Texas may be more cognizant of the platform of the John Birch Society than the Senator from Illinois. The Senator from Illinois does not know. I believe the constitution of the John Birch Society is secret. The Senator from Illinois is not an expert in it and does not know what is in it. But if the Senator from Texas says he knows what is in it, I will accept that answer. [Laughter.]

Mr. TOWER. Mr. President, will the Senator yield for a question?

Mr. DOUGLAS. I yield.

Mr. TOWER. The Senator from Texas is not a member of the John Birch Society.

Mr. DOUGLAS. I did not accuse him of being a member.

Mr. TOWER. Nor does he believe in what the John Birch Society believes in; but since the Senator from Illinois is making a good case of consistency, I think, in the interest of consistency, since he has expressed approval of one plank of that platform, he should support all of it.

Mr. DOUGLAS. I think the Senator from Texas should have voted for the withholding of the tax at the source on dividends and interest, when I presented my motion, so that along with the withholding on dividends and interest the withholding of taxes would have applied to all recipients universally.

Mr. President, so far as I am concerned, I am ready to yield the floor, unless there are other questions. But the Senator from Texas is still on his feet.

Mr. KERR. Mr. President, I now renew my unanimous-consent request as stated awhile ago.

The PRESIDING OFFICER. Without objection, the second amendment will be temporarily put aside and the request of the Senator from Oklahoma is agreed to. The clerk will read amendment No. 7—

Mr. DIRKSEN. Mr. President, will the Senator yield?

Mr. KERR. I yield.

Mr. DIRKSEN. If I understood the unanimous-consent request correctly, it now means the Senate will proceed to consider No. 7?

Mr. KERR. No. 5.

Mr. DIRKSEN. And then 6?

Mr. KERR. No. Nos. 5, 7, 8, 9, 10. We have already had 6.

Mr. DIRKSEN. There is one more.

Mr. KERR. And No. 11.

Mr. DIRKSEN. It was the intent of the unanimous-consent request that the Senate would proceed to this group of amendments with the understanding that there would be no yea-and-nay votes tonight, but that if a yea-and-nay vote were requested, the vote would go over until tomorrow?

Mr. KERR. It would not be before tomorrow.

The PRESIDING OFFICER. The clerk will read amendment No. 5.

The LEGISLATIVE CLERK. On page 381—

Mr. DIRKSEN. Mr. President—

The PRESIDING OFFICER. The Senator from Illinois.

Mr. DIRKSEN. I ask the Chair to make a decision with respect to the inquiry.

The PRESIDING OFFICER. The Chair said "without objection." Now the clerk is reading the first amendment.

Mr. DIRKSEN. I asked whether or not it was the understanding of the Senate, under the consent request, that the Senate proceed to this amendment, but in the event there is a request for a yea-and-nay vote, that vote shall go over at least until tomorrow?

The PRESIDING OFFICER. That is the understanding of the Chair.

Mr. HICKENLOOPER. Mr. President, what is the ruling of the Chair?

The PRESIDING OFFICER. That was the understanding of the Chair.

Mr. HICKENLOOPER. Has the unanimous-consent request been granted?

The PRESIDING OFFICER. That has already been granted. The clerk will read amendment No. 5.

The LEGISLATIVE CLERK. On page 381, in line 16, it is proposed to insert the language down to and including—

Mr. HUMPHREY. Mr. President, will the Chair restore order and permit no further business to be transacted until order is restored?

The PRESIDING OFFICER. Senators will please take their seats.

The LEGISLATIVE CLERK. On page 381, after line 15 it is proposed to insert a new section, as follows:

SEC. 21. EXPENDITURES BY FARMERS FOR CLEARING LAND.

(a) ALLOWANCE OF DEDUCTION.—Part VI of subchapter B of chapter 1 (relating to itemized deductions for individuals and corporations) is amended by adding after section 181 (as added by section 2(c) of this Act) the following new section:

"SEC. 182. EXPENDITURES BY FARMERS FOR CLEARING LAND.

"(a) IN GENERAL.—A taxpayer engaged in the business of farming may elect to treat expenditures which are paid or incurred by him during the taxable year in the clearing

of land for the purpose of making such land suitable for use in farming as expenses which are not chargeable to capital account. The expenditures so treated shall be allowed as a deduction.

"(b) LIMITATION.—The amount deductible under subsection (a) for any taxable year shall not exceed whichever of the following amounts is the lesser:

"(1) \$5,000, or

"(2) 25 percent of the taxable income derived from farming during the taxable year. For purposes of paragraph (2), the term 'taxable income derived from farming' means the gross income derived from farming reduced by the deductions allowed by this chapter (other than by this section) which are attributable to the business of farming.

"(c) DEFINITIONS.—For purposes of subsection (a)—

"(1) The term 'clearing of land' includes (but is not limited to) the eradication of trees, stumps, and brush, the treatment or moving of earth, and the diversion of streams and watercourses.

"(2) The term 'land suitable for use in farming' means land which as a result of the activities described in paragraph (1) is suitable for use by the taxpayer or his tenant for the production of crops, fruits, or other agricultural products or for the sustenance of livestock.

"(d) EXCEPTIONS, ETC.—

"(1) EXCEPTIONS.—The expenditures to which subsection (a) applies shall not include—

"(A) the purchase, construction, installation, or improvement of structures, appliances, or facilities which are of a character which is subject to the allowance for depreciation provided in section 167, or

"(B) any amount paid or incurred which is allowable as a deduction without regard to this section.

"(2) CERTAIN PROPERTY USED IN THE CLEARING OF LAND.—

"(A) ALLOWANCE FOR DEPRECIATION.—The expenditures to which subsection (a) applies shall include a reasonable allowance for depreciation with respect to property of the taxpayer which is used in the clearing of land for the purpose of making such land suitable for use in farming and which, if used in a trade or business, would be property subject to the allowance for depreciation provided by section 167.

"(B) TREATMENT AS DEPRECIATION DEDUCTION.—For purposes of this chapter, any expenditure described in subparagraph (A) shall, to the extent allowed as a deduction under subsection (a), be treated as an amount allowed under section 167 for exhaustion, wear and tear, or obsolescence of the property which is used in the clearing of land.

"(e) ELECTION.—The election under subsection (a) for any taxable year shall be made within the time prescribed by law (including extensions thereof) for filing the return for such taxable year. Such election shall be made in such manner as the Secretary or his delegate may by regulations prescribe. Such election may not be revoked except with the consent of the Secretary or his delegate."

(b) CLERICAL AMENDMENT.—The table of sections for such part VI is amended by adding at the end thereof the following:

"Sec. 182. Expenditures by farmers for clearing land."

(c) EFFECTIVE DATE.—The amendments made by this section shall apply with respect to taxable years beginning after December 31, 1962.

Mr. KERR. Mr. President, I ask unanimous consent that I may yield to the Senator from Delaware [Mr. WILLIAMS] without losing my right to the floor, to explain the amendment.

The PRESIDING OFFICER. Without objection, it is so ordered.

Mr. WILLIAMS of Delaware. Mr. President, under existing law, expenses incurred in carrying on a trade or business of farming are deductible in determining taxable income. In 1954, Congress amended the statute to include in the deductible category, expenses for soil and water conservation.

This new provision deals with a problem quite similar to that which resulted in the enactment of the soil and water conservation provision. At the present time, expenditures made during the preparatory period in extending a farm may not be deducted since they are not expenses incurred in the business of farming. Examples of expenditures of this nature which, under existing law, must be capitalized are expenditures—including material and labor—incurred in: clearing brush, trees, and stumps, leveling and conditioning land, and straightening creek beds. Because expenditures for these purposes, when incurred in order to make the land suitable for farming—like expenses for soil conservation—are also closely associated with the trade or business of farming, the committee believes that it would be proper to allow their deduction to a limited extent.

This provision permits taxpayers engaged in the business of farming to deduct, in computing their Federal income tax, expenditures incurred by them in clearing land to make it suitable for farming. Activities included in clearing and preparing land to make it suitable for farming include the clearing of brush, trees, stumps, and boulders, the leveling and conditioning of the land, and the diversion of streams.

Under the bill, deduction of expenditures in any taxable year for these purposes may not exceed \$5,000, or, if less, 25 percent of the taxpayer's taxable income from farming.

Mr. DOUGLAS. Mr. President, will the Senator yield for a question?

Mr. WILLIAMS of Delaware. Yes.

Mr. DOUGLAS. Has the Senator completed his statement?

Mr. WILLIAMS of Delaware. Yes.

Mr. DOUGLAS. Why should we encourage more acres of land to be put into production when we are attempting to take land out of production? The Senator from Delaware is proposing to bring into production additional acreage when the policy of the United States is to diminish the productive acres.

Mr. WILLIAMS of Delaware. The Senator from Illinois misunderstands the amendment. I have opposed reclamation projects which bring new land into production.

Mr. DOUGLAS. But the Senator is not opposed to bringing new land into production in Delaware.

Mr. WILLIAMS of Delaware. This has nothing to do with that question. It can be done now. Under existing law a taxpayer can buy equipment to use for clearing land and the law allows him to charge off the cost of the equipment. A small operator cannot afford to buy equipment. He is forced to contract for his work and then capitalize this cost in

the value of his farm, with the result that it costs him \$75 to \$100 an acre more than the larger operators to clear the land. This amendment gives to the smaller farmer some of the advantages the larger operator now has.

Mr. DOUGLAS. How is a small farmer defined?

Mr. WILLIAMS of Delaware. By the limitation in this amendment, it provides that it cannot exceed \$5,000, or 25 percent of his income from farming, whichever is the lesser.

Mr. DOUGLAS. A year?

Mr. WILLIAMS of Delaware. A year.

Mr. DOUGLAS. Five thousand dollars a year for clearing land? A great deal of land can be cleared for that. Moreover, I think it can be said that this provision will encourage bringing more land into cultivation at the very time when we are trying to decrease the amount of land in cultivation. I think it is completely inconsistent with the position the Senator from Delaware, along with the Senator from Illinois, has taken on reclamation projects, and also inconsistent with his general position on the farm problem.

Mr. KERR. Mr. President, if the Senator will yield for just a moment, I would like to say that the effect of this amendment does not change the right of the farmer to charge off the costs referred to in the amendment if certain events occur. The farmer who clears land and then sells it receives the benefit of this cost through a higher basis for his property. Therefore, the committee amendment in this case only changes the time in which he is permitted to charge these expenses off. If he goes ahead, under existing law, and does what the Senator has referred to, he in effect is permitted to charge it off if he sells the property but not otherwise. This provision would permit the chargeoff in 1 year which now takes longer than 1 year or may never occur.

Mr. WILLIAMS of Delaware. The large operators naturally buy the equipment. Under existing law this is subject to depreciation. They can charge this depreciation against their income other than farming, on any other type of income. This provision is limited to small farmers.

Mr. DOUGLAS. It is not the income to the farmer which is involved. It is the amount spent in the clearing of land.

Mr. WILLIAMS of Delaware. But limited to a percentage of income from farming.

Mr. DOUGLAS. For clearing land.

Mr. WILLIAMS of Delaware. The language would limit it to 25 percent of his farming income or \$5,000, whichever is smaller. A farmer with a small amount of farming income would not be able to spend it all on clearing land.

Mr. DOUGLAS. It is not \$5,000 of income, but it is a \$5,000 allowance for clearing land.

Mr. WILLIAMS of Delaware. Yes, if the farmer wished to spend all of his income that year, I suppose he could spend the full amount on clearing land.

Mr. DOUGLAS. The sum of \$5,000 a year would clear a great deal of land. It might clear 100 acres.

Mr. WILLIAMS of Delaware. Mr. President, it costs more than that to clear land; we approved a bill the other day for payments for farmland.

Mr. DOUGLAS. If a farmer cleared 100 acres a year, year after year, followed by year after year, he would not be a small farmer.

Mr. WILLIAMS of Delaware. If the Senator from Illinois has had any experience in this regard, he knows that \$5,000 would clear only about 25 acres.

Mr. DOUGLAS. It all depends on the land.

Mr. WILLIAMS of Delaware. No. This would be a fair average.

Mr. DOUGLAS. Yes. Wait just a minute. It all depends on the amount of timber on the land, the toughness of the timber, the amount of stones in the soil, and so on. In the fertile lands of Delaware, which are sandy and which do not have the boulders of Vermont, a bulldozer can operate very quickly. Five thousand dollars would do a lot in Delaware, to increase ultimately the chicken yield.

Mr. WILLIAMS of Delaware. It costs about \$175 or \$200 an acre to clear land, even in Delaware.

I am surprised that there should be objection to this particular proposal by anyone connected with the administration, especially since Congress passed a bill wherein it was provided that penitentiaries can draw as much as \$60,000 a year for not farming, and we have provided for payments to other large farmers for not farming.

This involves a benefit for the small farmers and I submit the amendment on its merits.

Mr. MILLER. Mr. President, will the Senator yield?

Mr. WILLIAMS of Delaware. I yield.

Mr. MILLER. I have two questions to ask the Senator. The first relates to the language used on page 383 of the bill, which refers to "land suitable for use in farming."

The definition is that this "means land which as a result of the activities described in paragraph (1) is suitable for use by the taxpayer or his tenant for the production of crops, fruits, or other agricultural products or for the sustenance of livestock."

The Senator knows that there is a problem in this regard for the Internal Revenue Service with respect to the so-called hobby farmer.

For the purposes of legislative history, I wonder if the Senator would agree that it is the intention of the Congress that when the definition says, "is suitable for use by the taxpayer or his tenant" for this type of production, it means that suitability implies profitability, that there must be a profitable type undertaking, rather than the hobby farming type of activity?

Mr. WILLIAMS of Delaware. Not only is that the intention, but also the amendment was drafted with the specific intention of prohibiting the benefits going to hobby farmers. Before the hobby loss provision applies in the case of a farming operation there must be a loss. Where there is a loss, 25 percent of income from farming is zero. Therefore

in such a case there would be no deduction under this provision.

I think both the report and the language properly protect us, as the language was drafted by the legislative counsel and the staff of our committee.

Mr. MILLER. I thank the Senator. My second question relates to the limitation about which the Senator from Illinois was inquiring.

On page 382 the language of the bill is:

The amount deductible under subsection (a) for any taxable year shall not exceed whichever of the following amounts is the lesser:

- (1) \$5,000, or
- (2) 25 percent of the taxable income derived from farming during the taxable year.

As I read the language, the \$5,000 would not necessarily have to come from farming. A doctor, for example, who was not otherwise engaged in the business of farming, except perhaps during a current year he might decide to become engaged in the business of farming, might have a marginal operation but, by reason of clearing land and otherwise preparing it, as I read the language, he could deduct the land preparation expenditures against his medical professional income, up to \$5,000.

Mr. WILLIAMS of Delaware. The language provides that the deduction for clearing land may not exceed \$5,000 or 25 percent of the income from farming, whichever is smaller.

I think that is adequate limitation on the provision because, no matter where the income which is spent comes from, it may not exceed 25 percent or less of his income from farming.

Mr. DOUGLAS. Mr. President, I suggest the absence of a quorum.

Mr. MILLER. Mr. President, will the Senator withhold his suggestion?

Mr. WILLIAMS of Delaware. Mr. President, I have the floor.

The PRESIDING OFFICER. The Senator from Delaware has the floor.

Mr. WILLIAMS of Delaware. I will yield the floor later. If the Senator wishes to suggest the absence of a quorum at that time.

Mr. MILLER. If the Senator will permit, I should like to pursue this point a moment.

Mr. WILLIAMS of Delaware. I yield to the Senator.

Mr. MILLER. Perhaps my difficulty arises over the way the bill is drafted. I think the Senator from Delaware and I have the same idea as to what we are trying to achieve. I should like to ask the Senator from Delaware whether we could achieve it if the language read as follows, starting with line 12, with the word "Limitation":

The amount deductible under subsection (a) for any taxable year shall not exceed 25 percent of the taxable income derived from farming during the taxable year, not to exceed \$5,000.

If that language were provided, it would confine the deduction to farming income and would avoid the problem which I previously posed.

Mr. WILLIAMS of Delaware. Mr. President, I have great respect for the

Senator from Iowa, but, as a layman, I learned long ago that one can never get two lawyers to agree on language. I am neither a lawyer nor a draftsman. We asked the legislative counsel and the committee staff to work out this language in the way to protect it against abuse. I would rather keep the language they have approved. In conference I think we can take care of any problem which might arise, because the language will be in conference. The intent is definitely clear.

Mr. MILLER. Mr. President, I have one more question in regard to intent. Do I correctly understand that the intention is that the \$5,000 is to be applied only against farming income?

Mr. WILLIAMS of Delaware. This deduction is limited to a percentage of the taxpayer's income from farming.

Mr. MILLER. As distinguished from income from a medical profession or otherwise?

Mr. WILLIAMS of Delaware. The income must be from farming. Hobby farmers get no benefit from this amendment nor will it help the large promoter.

Mr. AIKEN. Mr. President, will the Senator yield?

Mr. WILLIAMS of Delaware. I yield to the Senator from Vermont.

Mr. AIKEN. From reading the language, it appears to me that regardless of the amount of income the landowner might have from any source, or from all sources, he could not spend more than 25 percent of the taxable income derived from farming during that year.

Mr. WILLIAMS of Delaware. That is correct.

Mr. AIKEN. If the total income were \$5,000 from farming, he could not spend more than \$1,250.

Mr. WILLIAMS of Delaware. And it certainly would be limited to the point that it could benefit only a very small farmer.

This is not a subsidy program. It would not require expenditure of any public money. It would merely allow a small farmer to compete more favorably with the larger operator. We passed the investment credit for business. I do not see why the small farmers should not be entitled to at least this much consideration.

Mr. AIKEN. It is also true that if the farmer's taxable income were \$50,000 from farming, he still could not spend more than \$5,000 for clearing land and have it deductible?

Mr. WILLIAMS of Delaware. The Senator is correct.

The PRESIDING OFFICER. The question is on agreeing to the committee amendment on page 381, after line 15.

MESSAGE FROM THE HOUSE

A message from the House of Representatives, by Mr. Bartlett, one of its reading clerks, announced that the House had disagreed to the amendment of the Senate to the bill (H.R. 11974) to authorize appropriations for the Atomic Energy Commission in accordance with section 261 of the Atomic Energy Act of 1954, as amended, and for other pur-

poses; agreed to the conference asked by the Senate on the disagreeing votes of the two Houses thereon, and that Mr. HOLIFIELD, Mr. PRICE, Mr. ASPINALL, Mr. VAN ZANDT, and Mr. HOSMER were appointed managers on the part of the House at the conference.

ENROLLED BILL AND JOINT RESOLUTION SIGNED

The message also announced that the Speaker had affixed his signature to the following enrolled bill and joint resolution, and they were signed by the President pro tempore:

H.R. 10432. An act to amend title 39, United States Code, to codify certain recent public laws relating to the postal service and to improve the Code; and

H.J. Res. 677. Joint resolution relating to the admission of certain alien children.

AUTHORIZATION FOR JUDICIARY COMMITTEE TO MEET DURING SENATE SESSION TOMORROW MORNING

Mr. MANSFIELD. Mr. President, I ask unanimous consent that the Judiciary Committee be permitted to meet during the session of the Senate tomorrow morning.

The PRESIDING OFFICER. Is there objection? Without objection, it is so ordered.

BYRON B. GENTRY, PASADENA, CALIF., NEW COMMANDER IN CHIEF OF VFW

Mr. KUCHEL. Mr. President, on August 17, the Veterans of Foreign Wars of the United States elected a new commander in chief to lead that great organization of overseas combat veterans for the next year.

The new commander in chief of the Veterans of Foreign Wars is Mr. Byron B. Gentry. Commander Gentry is a distinguished attorney, a long time and nationally known leader in veterans affairs, one who has devoted unselfishly of his time to community activities, a noted author, and I take pride in mentioning also that he is a resident of California and a long-time friend of mine. Commander Gentry is currently the city prosecutor for the city of Pasadena, Calif., a position he has held for the past 10 years.

Mr. Gentry succeeds, as commander in chief of the VFW, Mr. Robert E. Hansen, of South St. Paul, Minn., who, during his tenure as head of the VFW, was well known to Members of the Senate for his helpful contributions in domestic matters, national security, and foreign affairs.

In addition to his professional and organizational achievements, the new head of the VFW has left a memorable record in the history U.S. sports. He was one of the great linemen at the University of Southern California. While playing for USC, he had the rare distinction of participating in two Rose Bowl games. In 1938, Mr. Gentry was selected as a member of the United Press All-Ameri-

can Professional Team with Pittsburgh. He was a member of the All-American All Stars who toured Japan in 1935.

As Members of the Senate are aware, the Veterans of Foreign Wars of the United States requires that its members have served overseas in combat. The wartime record of Byron Gentry abundantly qualifies him for membership in, and leadership of, such an organization. Commander Gentry enlisted as a private in 1942, and rose through the ranks to captain in 1944. He served as combat intelligence officer of the 161st Tactical Reconnaissance Squadron. He was assigned to Army Air Forces attached to both the 3d and 9th Armies. He served 2 years in the European theater where at various times he was staged in England, France, Luxembourg, Belgium, Holland, and Germany. He was awarded six Battle Stars, Presidential Citation, Belgian Fourragere, and three commendations. He remained in Military Intelligence Reserve until 1954. He is a graduate of Air Intelligence School, Harrisburg, Pa., and British Intelligence School, Highgate, England. As additional duty he defended 150 enlisted men in military courts and lost less than 10 cases. He was the first defense counsel appointed to the general court for black market cases in the Brussels area.

His VFW activities include judge advocate general, 1959-60; the three chair offices on the post level and two terms as post commander; two terms as district commander, and the three chair offices on the department level. He served as commander of the department of California, 1956-57. As a district commander he was a two-time winner of the Distinguished Service Award for district commander. As department commander he was selected as a member of the all-American team and named Department Commander of the Year 1957. He served on the national council of administration, 1957-59. He also served on numerous committees and was president of the 60th National VFW Convention Corp.

As previously mentioned, Commander Gentry has long been active in community service activities. The importance and extent of such contributions to his community is indicated by the following: Member of board of directors, American Gold Star Mothers Home Corp.; member, Los Angeles County Committee for the Aging; board of directors, Pasadena Committee for Employment of the Physically Handicapped; cofounder and two-time president, Pasadena Committee for Education on Alcoholism; cofounder and former president, Pasadena Committee for Narcotics Education.

It is remarkable that in addition to his many professional, veteran, and community activities he has also become a noted writer. Recently a book of his poetry, "Voices of the Airways," was published and has received many favorable reviews. His writing ability is not limited to poetry, as his excellent speech of acceptance of the position of commander in chief of the VFW well demonstrates. Some few years ago, when Mr. Gentry was becoming increasingly active

in the VFW, he wrote an essay entitled "The Spirit of the VFW." This has become a noted document among the members of the VFW, because it reflects so clearly, so eloquently, and so accurately the spirit of patriotism and service that motivates that great veteran organization. It was, therefore, highly appropriate that Commander Gentry used his "The Spirit of the VFW" as his remarks on the occasion of his election to the position of commander in chief of the Veterans of Foreign Wars of the United States.

Having had the privilege of enjoying the friendship of Byron Gentry since the days we were fellow students at the University of Southern California, and having observed through the intervening years those qualities which have distinguished him as a lawyer, a community leader, a public servant, an author, and now the national commander in chief of the largest overseas veterans organization in the world, I am confident that the VFW in particular, and our Nation in general, will benefit as a result of Byron Gentry's service as the head of the VFW.

I am confident that Members of the Senate will join with me in extending to Byron Gentry our sincere congratulations upon his election as commander in chief of the Veterans of Foreign Wars of the United States. Because of the simple beauty of its prose, as well as its meaningful content, I ask unanimous consent to include, at the conclusion of my remarks, "The Spirit of the VFW," by Byron Gentry, a distinguished American, who continues in peace, as in war, to serve his country.

There being no objection, the speech was ordered to be printed in the RECORD, as follows:

THE SPIRIT OF THE VFW

(By Byron B. Gentry, commander in chief, Veterans of Foreign Wars of the United States)

Ideals are like stars—we can see them but we can never touch them. Destroy man's idealism and you destroy his civilization. This Nation was conceived in the idealistic union of human rights; born midst the violent din of battle. Her sire was justice; her mother liberty; her cradle human dignity. She has given her sons and daughters a moral courage as yet unparalleled in the annals of mankind.

The Veterans of Foreign Wars of the United States is also founded upon an ideal. The cross of Malta is the symbol of that ideal—handed down to us through the dust of a thousand years from the knights of St. John. It is the symbol of faith and courage; of the eternal brotherhood of fighting men, serving a just and noble cause.

For nearly two centuries American men and women have gone marching down the long road to physical destruction in order to perpetuate those ideals. They have achieved immortality. Courageous and unflinching, with no single backward glance, they have stood for a brief moment in the shadow of time. They have defied the full fury of the storms which have threatened American idealism. They have cast life itself upon the flaming altar of American salvation.

Some of them traveled alone—in the still void of the night; some in the vast reaches of the ocean; some in the blazing emptiness of the sky; others in the crowded, violent din of the battlefield. But each in turn served but one cause and one people.

We are intensely human, and in humanity there is inevitable frailty, but no people and no nation has contributed more generously to the dignity of man.

We, as members of this great order, are irrevocably dedicated to the welfare and security of America as a free and independent nation; to the perpetuation of her sovereignty in an honorable association with other respectable nations of the world; to an honest and intelligent recognition of the legal and moral rights of our fellows, regardless of their affiliation; to the welfare of their widows and orphans; to an active participation in all worthy community service programs, directed toward the furtherance of true Americanism and the dignified alleviation of the undue burdens of man; to a long-range commitment to our youth, calculated to prepare them realistically for fearless and honest citizenship consistent with the unimpeachable ideals of our fathers, and to attain a man's full stature in an ever changing world; to work toward ultimate peace with honor and self respect for all peoples of the earth.

The ideal goal of our organization is the honorable realization of a world, a nation, and a day when no man shall ever again be eligible for membership. But in the interim we face reality.

Peace did not come to us in the generation of our fathers. Peace has not come to us in our own generation. Therefore, it is a matter appropriately left to posterity. You and I have been fighting men. We are still fighting men. Ours is a fighting organization.

How then shall we fight?

We shall fight with every weapon at our command to insure this Nation's free and independent future. We shall fight unholy alliances. We shall fight immoral capitulation. We shall fight the intellectual lethargy which has repeatedly brought us to the brink of disaster. We shall fight the unrealistic tendency to waste our economy in a vain attempt to win loyalty and appreciation from a fallen foe. We shall fight international bribery.

We shall fight the threatened destruction of our national obligation to our disabled brothers; to our fallen comrades; to their widows and orphans.

Compensation for service-connected disability is no gratuity. It is a just and equitable attempt to compensate for the loss of physical ability, just as workmen's compensation or accident insurance is such an attempt. It has no relation in fact or theory to one's ability to earn a livelihood. A lawyer may lose his legs and still practice law. A singer may lose his sight and continue to sing. They still are entitled to an equitable compensation for their loss.

In the wars which America has fought we have suffered many casualties. Casualties are a normal incident of war. We will admit that death is inevitably tragic. But the greatest tragedy of war is to the living.

Men die in battle with little time for reflection—with even less for personal regret. The real terror which haunts the soldier's sleepless nights is the return to civilian life, maimed and helpless and unwanted.

Prior to World War II these men were the objects of our doubtful generosity. We enacted legislation which permitted them to beg without a license. We made it possible for them to drag their mangled bodies to our public street corners to sell pencils. We broke their hearts and destroyed their human souls.

We ignored the fact that these objects of our dubious charity were Americans—brave men, independent men, heroic men. It is not enough to pay some intangible and symbolic tribute to their heroism for the purpose of easing our own conscience. They are not concerned with our hollow tributes. Heroism

is not unique to an American. It is a normal incident of his birth.

These men do not want tribute. They ask only an opportunity to walk with equal dignity among their fellows. And dignity comes from within.

How did they acquire their physical limitations? How did they lose their arms and legs and eyes? They lost them on the long and bitter roads to Tokyo and Berlin; and more recently to the Yalu River.

They lost them going forward—sometimes flying; sometimes running; sometimes walking; sometimes crawling; and sometimes just standing and stubbornly dying, but always putting behind them an ever-increasing margin of safety between this Nation and its mortal enemies.

They were the flower of American manhood. They were proud men; independent men; strong and courageous men. They were essentially young men. Theirs was no brief flight to glory. Theirs was a long and bitter journey into the unknown. It encompassed months and years of the type of living and dying which proved they could travel a great distance.

They still have a great distance to travel.

Do we now expect these proud and independent and courageous men to accept gracefully a life of uselessness and pity—of meaningless charity? Shall we bar them from a useful occupation; from successful readjustment, as the price of legitimate compensation? These men who were born to ambition—to an indomitable will to surmount all obstacles?

They have proven their absolute loyalty to principle. Their American ideals are untarnished. Their integrity is certain. We shall fight to keep their independence and ambition alive and bright.

We shall fight for their widows and orphans. An innocent child deprived of its father through war has burden enough without adding the insult of economic hardship; without further depriving it of the companionship of its mother; and without depriving the mother of reasonable security and hope.

There will always be those who involve us in wars—some of them perhaps wisely; some of them through sheer folly. We are Americans—proud of our American heritage. We will fight those wars.

But having fought them, we will not be relegated to the status of poor and unwanted relatives; to the darkened closet of shame. We have administered justice. We demand justice in return. We demand justice for our children. We demand justice for our widows. We demand eternal respect for our fallen.

We shall fight for the continued right to educate our children in the American tradition of our fathers; in the fundamentals of true Americanism. We will not tolerate foreign ideology in our schools or in our homes.

We shall fight all alien isms in this land we call our own. We shall search out and destroy any threat to our independent sovereignty—whether it be on some foreign field or at home in our own backyard.

This is our homeland; these are our people; our institutions; our freedoms; our religions; our own inalienable rights. We shall retain them.

We are not militaristic. We are not dictatorial. We are not selfish. But neither are we sloughful and craven cowards.

We shall be generous. We shall be tolerant. We shall be kind and even forgiving. But we refuse to be fools.

We shall respect every man's freedom, but we shall not forget that his freedom ends where ours and our country's begins.

This is the spirit of the VFW.

Digest of CONGRESSIONAL PROCEEDINGS

INTEREST TO THE DEPARTMENT OF AGRICULTURE

OFFICE OF
BUDGET AND FINANCE

(For information only;
should not be quoted
or cited)

Issued August 31, 1962
For actions of August 30, 1962
87th-2d, No. 156

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HIGHLIGHTS: House appointed conferees on farm bill. House committee voted to report wilderness bill. House passed bill to provide additional research facilities for experiment stations. House committee voted to report bill to facilitate work of Forest Service. Sen. Kerr inserted Treasury report supporting foreign trade bill. Sen. Muskie urged support for his amendment to foreign trade bill re imports from low-wage countries. Sen. Pastore defended President's textile program against recent attack.

SENATE

1. TAXATION. Continued debate on H. R. 10650, the proposed Revenue Act of 1962 (pp. 17070-120, 17124-55). Agreed to the committee amendment to permit farmers to deduct, in computing their Federal income tax, expenditures incurred by them in clearing land to make it suitable for farming, up to \$5,000 or 25 percent of the taxable income from farming for the year, whichever is the lesser (p. 17070). Sens. Carlson, Proxmire, Miller, Douglas, Curtis, Javits, and Sparkman submitted amendments intended to be proposed to this bill. pp. 17058-62, 17163-4
2. FOREIGN TRADE. Sen. Kerr inserted a letter and memorandum from Treasury Secretary Dillon supporting the proposed Trade Expansion Act of 1962. pp. 17123-4
- Sen. Muskie inserted his testimony before the Senate Finance Committee in support of his proposed amendment to the foreign trade bill to give the President authority to enter into marketing agreements with foreign countries to protect domestic industry from imports from countries with sub-standard wages and working conditions. pp. 17162-3

3. TEXTILES. Sen. Pastore defended the President's textile program against recent attack that it was "to appease the strongly protectionist elements in the cotton textile industry," and inserted several tables to support his position. Sens. Muskie, Thurmond, and Hickey commended Sen. Pastore's statement. pp. 17155-9
4. MINING. The Interior and Insular Affairs Committee reported with amendments S. 3451, to provide relief for residential occupants of unpatented mining claims upon which valuable improvements have been placed (S. Rept. 1984). p. 17058
5. LAW; COURTS. The Judiciary Committee voted to report (but did not actually report) H. R. 1960, to amend title 28 of the U. S. Code relating to the jurisdiction of the U. S. district courts. p. D790-1
6. WILDLIFE. The Commerce Committee reported with amendments H. J. Res. 489, to provide for the protection of the golden eagle (S. Rept. 1986). p. 17163
7. EXPORT CONTROL. Both Houses received from Commerce a report on Export Control for the second quarter of 1962. pp. 17163, 17210
8. VIRGIN ISLANDS. Both Houses received from GAO "a report on the review of certain activities of the government of the Virgin Islands." pp. 17163, 17210
9. PERSONNEL. Sen. Proxmire expressed concern over "the serious shortage of scientific and engineering manpower" and inserted several items on the subject. pp. 17120-3
10. LEGISLATIVE PROGRAM. Agreed to a unanimous-consent agreement to begin consideration of the independent offices appropriation bill on Fri., Aug. 31. p. 17119

HOUSE

11. FARM PROGRAM. Agreed to H. Res. 772, to send to conference H. R. 12391, the proposed Food and Agriculture Act of 1962. Conferees were appointed. Senate conferees had already been appointed. pp. 17183-6
12. WILDERNESS. The Interior and Insular Affairs Committee voted to report (but did not actually report) with amendment H. R. 776, the proposed National Wilderness Preservation Act. p. D793
13. RESEARCH. Passed without amendment H. R. 12712, to assist the States to provide additional facilities for research at the State agricultural experiment stations. pp. 17186-8
14. FORESTRY. The Subcommittee on Forests of the Agriculture Committee voted to report to the full committee with amendment H. R. 12434 consisting of miscellaneous administrative provisions to facilitate the work of the Forest Service. p. D793
15. TERRITORIES. Agreed to the conference report on H. R. 10062, to extend the application of certain laws to American Samoa. This bill will now be sent to the President. p. 17173
16. PERSONNEL. Passed with amendment S. 919, to amend the Hatch Political Activities Act to eliminate the requirement that the Civil Service Commission impose no penalty less than 90 days' suspension for any violation of Sec. 9 of the Act. A similar bill, H. R. 12661, was laid on the table. pp. 17165-6
The Post Office and Civil Service Committee reported without amendment H. R. 5698, to extend the apportionment requirement in the Civil Service Act to

to capture in words the spirit of his effervescent personality.

Garety and seriousness, stern intellectuality and the warmest emotion are likely to mix in the matter of a moment. The constant in his ever-changing moods is the human flame, burning more fiercely and closer to the surface in Justice Frankfurter than in almost any other human being.

"Wherever Frankfurter is there is no boredom," Matthew Josephson wrote in 1940. "As soon as he bounces in—he never walks, he bounces—the talk and the laughter begin, and they never let up."

Archibald MacLeish, who was his student at the Harvard Law School, spoke of "a voice which can crackle under a fool's complacency like dry wood under an empty kettle."

That was written of Mr. Frankfurter the law professor, but it remained true of Mr. Frankfurter the judge. From the bench he penetrated lawyers' foggy understanding of their own cases with sharp questions that sometimes approached the heckling level. Off the bench, he has never suffered cant in any conversation.

WIDE RANGE OF FRIENDS

Many who are close to Justice Frankfurter believe that his qualities as a human being are even greater than those of the judge. They speak of his warmth, his range of friends among the great and small, his phenomenal reading, his intimate acquaintance with the history of this country for the last 50 years.

Mr. Frankfurter played a part in much of that history. His public career began in 1906 as an assistant to Henry L. Stimson, President Theodore Roosevelt's U.S. Attorney in New York. He served other Presidents in many official and semiofficial capacities until Franklin D. Roosevelt named him to the Supreme Court.

In his more than 20 years on the Harvard law faculty he was an extraordinary gadfly to society. He helped many liberal causes, playing perhaps his most prominent part in the attempt to save Sacco and Vanzetti from execution in Massachusetts.

A CONSERVATIVE HERO

His libertarian record made him suspect to conservative interests when he was appointed to the Supreme Court. At his confirmation hearing witnesses denounced his religion (Jewish) and his birth (he emigrated from Austria at age 12.). A Senator asked whether he believed in the doctrines of Karl Marx.

"Senator," Mr. Frankfurter replied, "I do not believe you have ever taken an oath to support the Constitution of the United States with fewer reservations than I have or would now."

The great paradox of Justice Frankfurter's career is that in recent years he has become a conservative hero. This was because he became a dominant voice on the Supreme Court pleading for judicial restraint, caution, and deference to the wishes of Congress and the States.

Many liberals grew disenchanted with Justice Frankfurter and said that he decided too often against the liberal position. But his strong view was that a Justice must disregard his private beliefs in deciding a case.

Once recently on the bench he got the idea that a lawyer arguing a case was appealing to his own personal view of a harsh immigration law.

"Never mind what I think of it," he said sharply. "I think very ill of it."

HIS DISSENT RECALLED

His famous opinion in 1943 dissenting from a decision that children must be excused from saluting the flag if their religion forbids it put his view succinctly.

"One who belongs to the most villified and persecuted minority in history is not likely

to be insensible to the freedoms guaranteed by our Constitution," he wrote, continuing: "But as judges we are neither Jew nor gentile, neither Catholic nor agnostic. * * * As a member of this Court I am not justified in writing my private notions of policy into the Constitution, no matter how deeply I may cherish them or how mischievous I may deem their disregard."

Although as a judge he spoke of restraint and aloofness, in person Mr. Frankfurter is a man of emotion. He loves romantic music. In conversation, his thoughts and his passions rush out as he grips his listener's elbow to emphasize a point.

"A passionate person," one friend has called him, "who has given up the other passions of his life for this one."

Like his two greatest heroes, Justice Oliver Wendell Holmes and Justice Louis D. Brandeis, Mr. Frankfurter performed much of his service on the Supreme Court at an age when other men might have retired. He will be 80 years old November 15.

He is married to the former Marion Denman of Longmeadow, Mass.

Arthur Joseph Goldberg was working on a labor-management dispute in Chicago, a few miles from his West Side birthplace, when President Kennedy called today to tell him his next assignment was the Supreme Court.

"What are your plans now?" a friend asked the Secretary a short time later.

"My plans are to settle this strike," he replied, as though surprised by the question. "I've got unfinished business to perform as Secretary of Labor."

Mr. Goldberg went to Chicago to try to head off a threatened strike of telegraphers on the Chicago and Northwestern Railway. The odds were, in view of his 19-month record as Secretary of Labor, that a call from the President would find him trying to settle a dispute somewhere.

Mr. Goldberg had presumably alerted his wife Dorothy. She and their son Robert turned on the television set in their Washington home and watched the President make the announcement.

"What an opportunity for him to serve," she exclaimed. "You know he has a judicial temperament if anybody has."

The telephone jingled in the study off the big living room. It was the Secretary calling from Chicago. There was a few minutes of excited, affectionate conversation.

Then, turning to a friend, Mrs. Goldberg remarked that she was just beginning to feel the importance of the event.

"I'm not excited enough," she said. "Isn't that awful? I guess it's because I always believed it was going to happen."

Mr. Goldberg is a gray-haired, medium-sized man with extraordinary mental energy and physical stamina. He was born August 8, 1908, the last of 11 children, 2 of whom were born in Russia and died there before their parents, Joseph and Rebecca Goldberg left for the United States.

From San Francisco, his port of entry, Joseph Goldberg went to Texas where he worked as a peddler for a year and a half before moving on to Chicago. There he acquired a blind horse and a wagon and started a small business carting fruits and vegetables from the city's markets to hotels.

LAW GRADUATE OF 1929

Arthur remembers riding with his father occasionally and bringing home some half-spoiled fruit and sharing it with neighborhood boys. It was a poor, rough neighborhood where the Jews and the Irish were rock-throwing rivals.

"I used to fetch bricks for my brothers to throw," Mr. Goldberg recalls.

Mr. Goldberg observes the Jewish holidays and the Chicago rabbi who married him and Dorothy Kurgans is a guest at the Goldberg home whenever he comes to Washington.

Mr. Goldberg finished Northwestern University Law School in 1929 at the top of his class. He had already written dozens of briefs for a Chicago law firm. His pay was \$20 a week. Later, another law firm employed him to work on mortgage foreclosures—a busy practice in depression days—but Mr. Goldberg did not like the work and opened a law office of his own.

He had taken a course in labor law but had no plans to become a labor lawyer. However, one of his first clients was the Chicago Newspaper Guild. He practiced labor law from then until he was chosen for the Kennedy Cabinet.

On taking office he let it be known immediately that he was not going to follow any traditional pattern. Any big, threatened strike was a challenge and he moved into the middle of it.

"Operator" is a word that has been applied frequently to the Secretary, sometimes admiringly, sometimes not.

"He's never been just an ordinary operator," an admirer commented. "The fact that he isn't inhibited about it adds to his charm, and besides he always operates from an ideological base of genuine interest and concern."

As a lawyer, he was no ordinary practitioner. He used to recall the assertion of the man he is succeeding, Felix Frankfurter, that a good lawyer needs to be, above all, a cultivated man.

Another favorite quotation, from his law school dean, was:

"If you're going to practice law, do it in the grand manner."

As an Associate Justice of the Supreme Court, Mr. Goldberg will have occasion to recall another of his favorite quotations, this one from the Italian historian.

"We cannot be impartial. We can only be intellectually honest * * * aware of our passions and on guard against them. Impartiality is a dream, and honesty a duty."

Mr. Goldberg has two children. His son, Robert, is a senior at Amherst.

His daughter, Barbara, is the wife of Dr. David A. Cramer, a Chicago physician.

SOVIET OIL CHALLENGE

Mr. JAVITS. Mr. President, I have spoken on a number of occasions about the increasingly serious economic challenge presented to the West by the Soviet bloc trade, a challenge which has become increasingly a matter of public record. Typical of the growing awareness of this serious offensive, particularly in regard to oil, is an editorial which appeared in the Washington Post on August 27, 1962. I ask unanimous consent that the editorial be printed in the RECORD at this point in my remarks.

There being no objection, the editorial was ordered to be printed in the RECORD, as follows:

SOVIET OIL CHALLENGE

Premier Khrushchev has thrust a devilishly tempting oil pipeline offer before the oil-hungry Japanese. Seconding Mr. Mikoyan's motion of last August, he offered to extend a Soviet pipeline from Irkutsk to the Pacific if Japan would provide the materials to build it. Japan now takes about 3 percent of its oil from the Soviet Union. A pipeline could bring in 10 times as much at prices perhaps 30 percent lower than existing levels. Jogged by the United States and their own apprehensions, the Japanese have reacted warily toward Soviet oil in the past. Whether the country's growing economic restiveness will make it more hospitable to the pipeline proposal remains to be seen.

The proposal is merely the latest gambit in the increasingly aggressive and effective "So-

let oil offensive." With politics determining prices and repayment and marketing terms, Russian oil exports have climbed at the rate of 6 million or more metric tons a year since 1958. They now go to nine Western European countries; in Italy the Western oil position has been particularly undermined. The Soviet Government is also stimulating the oil ambitions of a number of key underdeveloped nations, which regard a national oil capability as a matter of independence and status as well as development. The twin goals of Soviet oil policy, to disrupt if not to displace non-Communist oil operations and to apply political leverage in the neutral world, have gained a measure of success which makes Western oil men and statesmen shudder at what may come.

The very real and well-documented prospect of economic and political hardship has so far led to much sounding of alarms in the West but to precious little action. Hobbled by Italian objections, the Common Market nations have sat on a proposal to apply voluntary restrictions to Soviet oil imports. Middle Eastern producers have been inclined to pass the brunt of the Soviet challenge to the West. Western producers have made no substantial changes in pricing and other policies to meet their Communist competition.

A forthcoming administration-requested report from the National Petroleum Council promises to spur official activity. But meanwhile, specific suggestions from congressional and industry quarters on how to arm the United States for imminent oil combat have not been treated with any urgency. Soviet oil indeed represents a stinging nettle to the free world. It must be firmly grasped.

Mr. JAVITS. Mr. President, the editorial notes that "specific suggestions from congressional and industry quarters on how to arm the United States for imminent oil combat have not been treated with any urgency." I have pressed for at least a congressional inquiry into one approach to the Soviet oil offensive through my amendment to section 708 of the Defense Production Act, which would restore to its pre-1955 status the authority of the Attorney General to exempt from the antitrust laws cooperative action in furtherance of the purposes of the Government under the act. The distinguished chairman of the Banking and Currency Committee has opened this question to hearings, which have begun but have not yet been completed. I would hope that the kind of urgency to which the editorial refers would be communicated to the committee by those in industry and Government who are aware of the problem. A concrete opportunity is now being presented for the Congress to consider techniques for dealing with the problem. The national interest cannot afford to let that opportunity pass as it is very likely to do unless greater interest is expressed in these hearings.

Mr. MANSFIELD. Mr. President, is there further morning business?

The PRESIDENT pro tempore. Is there further morning business? If not, morning business is closed.

REVENUE ACT OF 1962

Mr. MANSFIELD. Mr. President, I ask unanimous consent that the unfinished business be laid before the Senate and made the pending business.

The PRESIDENT pro tempore. Is there objection?

There being no objection, the Senate resumed the consideration of the bill (H.R. 10650) to amend the Internal Revenue Code of 1954 to provide a credit for investment in certain depreciable property, to eliminate certain defects and inequities, and for other purposes.

The PRESIDENT pro tempore. The question is on agreeing to the committee amendment No. 5, to insert certain language on page 381, after line 15, through line 24 on page 384, "SEC. 21. EXPENDITURES BY FARMERS FOR CLEARING LAND".

The amendment was agreed to.

Mr. KERR. Mr. President, I move to reconsider the action whereby amendment No. 5 was agreed to.

Mr. WILLIAMS of Delaware. Mr. President, I move to lay that motion on the table.

The PRESIDENT pro tempore. The question is on agreeing to the motion by the Senator from Delaware to lay on the table the motion by the Senator from Oklahoma.

The motion to lay on the table was agreed to.

Mr. KERR. Mr. President, I call up the seventh amendment and ask that it be stated.

The PRESIDENT pro tempore. The amendment will be identified.

The LEGISLATIVE CLERK. On page 386, after line 6, it is proposed to insert language through line 10, page 388.

Mr. KERR. Mr. President, under existing law certain small business corporations may elect to have income taxed directly to their shareholders, thereby eliminating tax at the corporate level. For such an election to be valid, however, the corporation must have no more than 10 shareholders and each shareholder must give his consent to the election.

Previously a problem existed as to the proper method of determining the number of shareholders of a corporation in community property States or where the stock of a corporation was held jointly by husband and wife. In 1959 Congress removed this problem by specifically providing how the number of shareholders was to be determined where husband and wife resided in community property States or where they held stock jointly. Congress provided in such cases that the spouses would be treated as one shareholder (Public Law 86-376, approved September 23, 1959). This provision was made effective with respect to taxable years of small business corporations beginning after December 31, 1959. However, cases have come to the attention of your committee in which small business corporations were prevented from making (or continuing) an election to have their income of 1958 and 1959 taxed to their shareholders because husbands and wives in community property States or who held stock jointly have each been counted as a separate shareholder for those years. The first year with respect to which such an election could be made was 1958.

The committee does not believe that the rule enacted by Public Law 86-376 for determining the number of shareholders of a small business corporation

should be limited to years after 1959, but should apply to all years for which such an election may be made. This will insure the application of the same rules in applying the 10-shareholder limitation for all years in qualifying a small business corporation for such an election. Accordingly, this provision of the bill makes that rule of Public Law 86-376 apply also to years 1958 and 1959.

Thus, this bill provides that with respect to the years 1958 and 1959, in determining the number of shareholders of a small business corporation for purposes of the election provided by subchapter S of the Internal Revenue Code (under which shareholders are taxed directly on the corporate earnings), spouses who hold stock of such a corporation jointly or under the community property laws of a State are to be treated as one shareholder; that is, section 1371(c) of the code will now be applicable to such years.

In order to insure that a small business corporation whose status may be affected by this provision will have an opportunity to qualify for treatment under subchapter S, the bill provides a special 1-year period within which a special election may be made to have the earlier effective date of section 1371(c) apply. For the special election to be valid, however, a corporation must have met the statutory requirements of subchapter S in 1958 and 1959, and must have filed a timely election to be subject to subchapter S for those years. Furthermore, each person who is a shareholder at the time of the special election must give his consent and each person who was a shareholder for any taxable year ending before the year in which the special election is made also must give his consent. Finally, where an election—and the requisite consents—has been made, the statute of limitations for assessing additional tax against the corporation or its shareholders is to remain open, or be opened, for 1 year following the date of the election. Tax assessed or credit or refunds granted within this special period of limitations must relate only to changes resulting directly from the election.

I ask that the amendment be agreed to.

The PRESIDENT pro tempore. The question is on agreeing to the committee amendment No. 7, which is, after line 6, on page 386, to insert "SEC. 23. EFFECTIVE DATE OF SECTION 1371(c) OF INTERNAL REVENUE CODE OF 1954".

The amendment was agreed to, as follows:

On page 386, after line 6, to insert a new section, as follows:

"SEC. 23. EFFECTIVE DATE OF SECTION 1371(c) OF THE INTERNAL REVENUE CODE OF 1954.

"(a) IN GENERAL.—Subject to the provisions of subsection (b), section 1371(c) of the Internal Revenue Code of 1954 (as added by section 2(a) of the Act entitled 'An Act to amend the Internal Revenue Code of 1954 to provide a personal exemption for children placed for adoption and to clarify certain provisions relating to the election of small business corporations as to taxable status', approved September 23, 1959 (Public Law 86-376)), shall (notwithstanding the provisions

of the first sentence of section 2(d) of such Act) also apply to taxable years beginning after December 31, 1957, and before January 1, 1960.

"(b) ELECTION AND CONSENT BY CORPORATIONS; CONSENTS BY SHAREHOLDERS.—Subsection (a) shall apply with respect to any corporation and its shareholders only if, within one year after the date of the enactment of this Act—

"(1) such corporation (in such manner as the Secretary of the Treasury or his delegate prescribes by regulations) elects to have the provisions of subsection (a) apply and consents to the application of subsection (c); and

"(2) each person who is a shareholder of such corporation on the date on which such corporation makes such election, and each person who was a shareholder of such corporation during any taxable year of such corporation beginning after December 31, 1957, and ending before the date of such election, consents (in such manner and at such time as the Secretary of the Treasury or his delegate prescribes by regulations) to such election and to the application of subsection (c).

"(c) TOLLING OF STATUTES OF LIMITATIONS.—In any case in which a corporation makes an election under subsection (b)—

"(1) if the assessment of any deficiency against the corporation making such election, or any shareholder of such corporation who consents to such election, for any taxable year is prevented, at any time on or before the expiration of one year after the date of such election, by the operation of any law or rule of law, assessment of such deficiency may, nevertheless, be made, to the extent such deficiency is attributable to the application of subsection (a), at any time on or before the expiration of such one-year period; and

"(2) if credit or refund of any overpayment of tax by the corporation making such election, or any shareholder of such corporation who consents to such election, for any taxable year is prevented, at any time on or before the expiration of one year after the date of such election, by the operation of any law or rule of law, credit or refund of such overpayment may, nevertheless, be allowed or made, to the extent such overpayment is attributable to the application of subsection (a), if claim therefor is filed on or before the expiration of such one-year period."

Mr. KERR. Mr. President, I move to reconsider the action by which the amendment was agreed to.

Mr. WILLIAMS of Delaware. Mr. President, I move to lay that motion on the table.

The PRESIDENT pro tempore. The question is on agreeing to the motion by the Senator from Delaware to lay on the table the motion by the Senator from Oklahoma.

The motion to lay on the table was agreed to.

Mr. KERR. Mr. President, the next amendment is No. 8.

The PRESIDENT pro tempore. The amendment will be identified for the information of the Senate.

The LEGISLATIVE CLERK. On page 388, after line 10, it is proposed to insert language through line 14 on page 389.

Mr. KERR. Mr. President, present law provides that business losses incurred in 1 year can be carried back to the 3 prior years and then, to the extent not absorbed by income in those years, carried forward to the 5 succeeding years after the year in which the losses occurred. For most companies which again earn income such a period is long enough

to absorb all of their losses against income.

Rapid transit companies in recent years have had a special problem in connection with the very large losses they have incurred in converting from streetcar to bus operations. Because of the size of these losses, most transit companies have spread their conversion to buses over many years—some over as many as 15 years—so that a sufficient period will be available to absorb the losses against income. However, a situation has come to the attention of the committee in which the conversion from streetcars to buses was completed in an 18-month period. It appears that the conversion was made in such a short period because of fraud on the part of the then existing management. Moreover, evidence is available that the then existing management made this conversion in the 18-month period despite the fact that it was pointed out to them by their financial experts that such losses could not be absorbed within the period of the 5-year carryforward.

After the mismanagement was discovered, the company was reorganized and new officers and a new board of directors elected. However, the conversion from streetcars to buses in the 18-month period could not be undone. As a result of this conversion the company sustained a loss of approximately \$10,200,000. At the end of the 5-year carry-forward period about \$5,200,000 of this loss remained unused. While the company has recently been making a small profit, it appears that rate increases may have to be requested if this remaining loss cannot be offset against the income of future years.

The committee believes that since ordinary prudent, honest management would have spread the conversion over a number of years, a longer carry forward of the unused loss should be permitted. This is a particularly serious problem because of the present inadequacy of our mass transportation system and the fact that a rapid transit system is involved here. Moreover, in this case it is likely that in the long run it will be the users of the transportation who will suffer if the company is not permitted to utilize the benefit of this loss.

The bill provides that in the case of net operating losses incurred in the calendar years 1953 and 1954, principally as a result of the conversion from streetcar to bus operations, an additional 5 years is to be allowed to offset such losses against income. The bill achieves this result by providing that such losses are to be known as "unused conversion losses" to the extent they still remain unused after the end of the normal 5-year carry-forward period. The bill provides that such an unused conversion loss from these 2 years is to be considered a net operating loss sustained in 1959 and therefore available as a net operating loss carry-forward to the calendar year 1960 and 4 subsequent taxable years.

The treatment described above is to apply only for years in which the taxpayer is engaged in the furnishing or sale of transportation on a local electric rail-

road, trackless trolley system, or bus system. The rates for the transportation in such cases must have been established or approved by a governmental unit, by a public service or public utility commission or similar body.

In the case brought to the committee's attention there is an unused loss of approximately \$5,200,000 from the years 1953 and 1954, and it is estimated, based upon anticipated revenues, that from \$2 to \$3 million of this loss can be offset against income in the additional 5-year period allowed by this bill.

Mr. President, I ask unanimous consent that we may temporarily lay aside committee amendment No. 8 and consider committee amendment No. 9.

The PRESIDENT pro tempore. Is there objection to the request by the Senator from Oklahoma? The Chair hears none, and it is so ordered.

The committee amendment No. 9 will be identified for the information of the Senate.

The LEGISLATIVE CLERK. On page 389, after line 14, it is proposed to insert the language through line 8 on page 390.

Mr. KERR. Mr. President, I believe the Senator from Delaware has an explanation.

Mr. WILLIAMS of Delaware. Mr. President, under present law, a pension trust is qualified for income tax exemption only if it meets certain requirements relating to coverage of employees and nondiscrimination of contributions or benefits. Where the pension trust is properly qualified, not only is it exempt from Federal taxation with respect to its income, but contributions paid to it by an employer on behalf of his employees are deductible for Federal income tax purposes. Thus, there is considerable incentive for a pension trust to meet the requirements of the Internal Revenue Code and thereby become a qualified trust.

Occasionally, however, it is difficult for a pension trust to achieve qualified status before employer contributions are received by it. This is particularly true in the case of pension plans negotiated under collective-bargaining agreements with many employers both large and small. Often, considerable time is required to obtain sufficient factual data upon which to insure the actuarial soundness of the plan. Sometimes a formality is not properly performed.

In such cases, where the pension plan operates for some period as a nonqualified plan prior to securing qualification under the Internal Revenue Code, any income it may earn during such period is subject to income tax, thereby reducing amounts which would otherwise serve to provide employee benefits under the plan. In addition, employer contributions are not allowed as deductions unless the employee is given immediate vested rights to the contribution.

The committee believes these are rather severe consequences, particularly where failure to meet the conditions of the statute for qualification is due to the fact that, because the plan involved many employers, the arrangements could not be worked quickly although it was the initial intention of both the em-

employers and the unions to meet those conditions. If the pension trust has never been operated in a manner which would jeopardize the interest of its beneficiaries, and if, when completed, the pension plan of which the trust is a part conforms with the Internal Revenue Code and has received the approval of the Internal Revenue Service, your committee believes it is just, under such circumstances, to provide that the pension plan be treated as a qualified trust during the intervening period between its inception and the time it actually qualified for tax exemption.

This section of the bill provides that the pension plan of Local Union No. 435, International Hod Carriers' Building & Common Laborers' Union of America, established pursuant to negotiations between the union and the Building Trades Employers' Association of Rochester, which is a qualified trust under section 401(a) of the Internal Revenue Code, is to be treated as having been a qualified trust and to have been exempt from taxation for the period beginning May 1, 1960, and ending April 20, 1961. For this provision to apply however, it must be shown to the satisfaction of the Secretary of the Treasury or his delegate that the trust has not in the period designated been operated in a manner which would jeopardize the interests of its beneficiaries.

Under the bill not only will the income of the pension plan during the specified period be exempt from tax but also contributions made under the plan within such period by employers generally will be deductible by them in determining their Federal income tax liability.

The amendment has been approved by the Treasury Department. It is the customary amendment similar to that which has been agreed to on previous occasions.

Mr. KEATING. Mr. President, will the Senator yield?

Mr. WILLIAMS of Delaware. I yield.

Mr. KEATING. I wish to express my gratitude to the distinguished Senator from Oklahoma [Mr. KERR] and the distinguished Senator from Delaware [Mr. WILLIAMS] for their assistance in support of this meritorious amendment. It is very much desired by both labor and management, and I am very appreciative of the action taken.

I am indeed grateful for this assistance for the pension plan of Local No. 435 of the International Hod Carriers' Building and Common Laborers' Union of America of Rochester, N.Y. This plan was negotiated between local 435 union and the Building Trades Employers' Association of Rochester to take effect May 1, 1960. However, Treasury approval for a tax deduction was not obtained until April 20, 1961. The purpose of this amendment is to extend the retroactive qualifications under the Internal Revenue Code of 1954 to include the year when there was no approved plan.

The amendment also grants the plan exemption from the tax on its investment income during this prequalification period. It has the endorsement of the Treasury Department.

Mr. President, this amendment is straightforward and there are, as the letter from the Assistant Secretary indicates, ample precedents for it. I am grateful that the Senate Finance Committee has included it in the present bill.

Mr. KERR. Mr. President, I ask for approval of the amendment.

The PRESIDENT pro tempore. The question is on agreeing to the amendment.

The amendment was agreed to, as follows:

On page 389, after line 14, to insert a new section, as follows:

"SEC. 25. PENSION PLAN OF LOCAL UNION NUMBERED 435, INTERNATIONAL HOD CARRIERS' BUILDING AND COMMON LABORERS' UNION OF AMERICA

"The pension plan of Local Union Numbered 435 of the International Hod Carriers' Building and Common Laborers' Union of America, which was negotiated to take effect May 1, 1960, pursuant to an agreement between such union and the Building Trades Employers Association of Rochester, New York, Incorporated, and which has been held by the Internal Revenue Service to constitute a qualified trust under section 401(a) of the Internal Revenue Code of 1954, and to be exempt from taxation under section 501(a) of such Code, shall be held and considered to have been a qualified trust under such section 401(a), and to have been exempt from taxation under such section 501(a), for the period beginning May 1, 1960, and ending April 20, 1961, but only if it is shown to the satisfaction of the Secretary of the Treasury or his delegate that the trust has not in this period been operated in a manner that would jeopardize the interests of its beneficiaries."

Mr. KERR. Mr. President, I move that the vote by which the amendment was agreed to be reconsidered.

Mr. KEATING. Mr. President, I move to lay that motion on the table.

The motion to lay on the table was agreed to.

Mr. KERR. Mr. President, I call up the 10th committee amendment and ask that it be identified.

The PRESIDENT pro tempore. The committee amendment will be identified.

The LEGISLATIVE CLERK. On page 390, after line 8, it is proposed to insert the proposed language on lines 9 through 21 on page 391.

The PRESIDENT pro tempore. The question is on agreeing to the amendment.

Mr. KERR. Mr. President, I ask unanimous consent to have printed at this point in the RECORD an explanation of the 10th amendment. So far as I know, there is no objection to the amendment, and I ask for its approval.

There being no objection, the explanation was ordered to be printed in the RECORD, as follows:

XXVI. CONTINUATION OF PARTNERSHIP YEAR FOR SURVIVING PARTNER IN A TWO-MAN PARTNERSHIP WHERE ONE DIES

(Sec. 26 of bill and sec. 188 of 1939 code)

The attention of your committee has been called to a case where the partnership provisions of the 1939 code worked a substantial hardship. The case brought to your committee's attention involves a two-man partnership with a partnership year ending on January 31. The 1939 code provides that income of partnerships is to be reported

by the partners for tax purposes in their year in which, or with which, the partnership year ends. Thus, income from the partnership year ending on January 31, 1946, for example, would be reported by partners on a calendar year basis in their calendar year 1946. However, where one of the partners dies, for example, before the end of December 1946, the partnership income in that year, which ordinarily would be reported for tax purposes by the partners in 1947, must then be reported by the partners, or their estate, in the calendar year 1946. This can result in a bunching of income, and therefore application of the higher surtax rates, since income of a partner for as long as 23 months may, in this manner, have to be reported in a single year.

At the time of the passage of the 1954 code, the law was changed to provide that the partnership year was not to close upon the death of a partner but instead was to run to its normal conclusion. In this regard the report of your committee on the 1954 code stated as follows:

"Under present law there has been the contention that the death of a partner closes the partnership year and [in] the bunching of more than a year's income in the decedent's last year. Where the partnership and the partners are on different taxable years, this would have the effect of concentrating as much as 23 months' income in the final return of the deceased partner, that is, the income for the partnership year ending within his taxable year and the income for the taxable year closed by the partner's death."

The problem presented in the case called to your committee's attention occurred before the 1954 code provision became applicable. Moreover, here the bunching occurs not only with respect to the deceased partner, but with respect to the surviving partner as well, since a partnership was held to no longer exist upon the death of one of two partners.

The bill adds a provision to the 1939 Internal Revenue Code to provide that the death of a partner in a two-man partnership is not to result in the termination of the partnership, or the closing of the taxable year of the partnership with respect to the surviving partner, prior to the time the partnership year would have closed if neither partner had died nor disposed of his interest. Thus, in the case of a partner dying in 1946 where the partnership year does not end until January 31, 1947, the partnership year would continue to that date and the income for such year would be reported by the surviving partner on his tax return for 1947. This provision is to apply only if the surviving partner so elects within 1 year after the date of enactment of this provision.

This amendment applies to taxable years of a partnership beginning after December 31, 1946, to which the Internal Revenue Code of 1939 applies. Generally the 1939 code applied to partnership taxable year beginning before January 1, 1955. The bill also provides that if refund or credit for an overpayment resulting from the application of this provision is prevented by the operation of any law or rule of law (other than those relating to closing agreements or compromises) the refund or credit of the overpayment may nevertheless be made if the claim is filed within 1 year after the date of enactment of this bill.

Mr. MILLER. Mr. President, before we vote on the amendment, I should like to say that while I recognize the equities the amendment seeks to accomplish, I believe it is not good policy to have special relief-type legislation enacted in the course of consideration of a general tax bill such as we have before us. But I shall not object to the amendment.

Mr. KERR. I thank the Senator from Iowa.

The PRESIDENT pro tempore. The question is on agreeing to the committee amendment.

The committee amendment was agreed to, as follows:

On page 390, after line 8, to insert a new section, as follows:

"SEC. 26. CONTINUATION OF A PARTNERSHIP YEAR FOR SURVIVING PARTNER IN A TWO-MAN PARTNERSHIP WHERE ONE DIES.

"(a) CLOSE OF TAXABLE YEAR OF TWO-MAN PARTNERSHIP WHEN ONE PARTNER DIES.—Section 188 of the Internal Revenue Code of 1939 (relating to different taxable years of partner and partnership) is amended—

"(1) by striking out 'If' and inserting in lieu thereof '(a) GENERAL RULE.—If'; and

"(2) by adding at the end of such section 188 the following new subsection:

"(b) TWO-MAN PARTNERSHIP.—For the purpose of this chapter, the death of one of the partners of a partnership consisting of two members shall not, if the surviving partner so elects within one year after the date of enactment of this subsection, result in the termination of the partnership or in the closing of the taxable year of the partnership with respect to the surviving partner prior to the time the partnership year would have closed if neither partner had died or disposed of his interest."

"(b) EFFECTIVE DATE, ETC.—The amendments made by subsection (a) shall apply with respect to taxable years of a partnership beginning after December 31, 1946, to which the Internal Revenue Code of 1939 applies. If refund or credit of any overpayment resulting from the application of the amendments made by subsection (a) of this section (including interest, additions to the tax, and additional amounts), is prevented on the date of enactment of this Act, or within one year from such date, by the operation of any law or rule of law (other than section 3760 of the Internal Revenue Code of 1939 or section 7121 of the Internal Revenue Code of 1954, relating to closing agreements, and other than section 3761 of the Internal Revenue Code of 1939 or section 7122 of the Internal Revenue Code of 1954, relating to compromises), such refund or credit of such overpayment may, nevertheless, be made or allowed if claim therefor is filed within one year after the date of the enactment of this Act. No interest shall be allowed or paid on any overpayment resulting from the enactment of this section."

Mr. KERR. Mr. President, I move that the action by which the committee amendment was agreed to be reconsidered.

Mr. WILLIAMS of Delaware. Mr. President, I move to lay that motion on the table.

The motion to lay on the table was agreed to.

Mr. KERR. Mr. President, I call up the 11th committee amendment and ask that it be stated.

The PRESIDENT pro tempore. The committee amendment will be stated.

The LEGISLATIVE CLERK. On page 305, line 23, after the word "before," it is proposed to strike out "July 1, 1964" and insert "January 1, 1963."

The PRESIDENT pro tempore. The question is on agreeing to the committee amendment.

Mr. KERR. Mr. President, with reference to the pending amendment, the Senator from Iowa was going to ask that the date in the bill be moved forward to

conform to the date that is in the House bill. I have discussed the question with him. In view of the fact that the House bill provides the date of July 1, 1964, it was suggested that we move it forward to January 1, 1964. However, I see no objection to amending the provision to conform to the date in the House bill, which would be July 1, 1964. Even after the amendment is agreed to by the Senate, it will become original text and be subject to amendment if any Senator wishes to seek to amend it. Therefore I ask unanimous consent that the provision be amended to that extent.

Mr. GORE. Mr. President, reserving the right to object, I do not think that we should permit the date to be moved forward by unanimous consent. The date on the bill should be the effective date of the amendment. The date contained in the provision should be the date of the enactment of the bill, rather than having it moved forward. That is an unjustified privilege that exists under present law. I see no reason for extending it until 1964. If the Senator wishes to move that the amendment be agreed to, he may be able to have the motion agreed to. But I would not wish to sit still and let it go by with unanimous consent, because I am opposed to it. Therefore, I object.

Mr. KERR. Mr. President, I move that the committee amendment be rejected.

The PRESIDING OFFICER (Mr. PEARSON in the chair). The question is on agreeing to the amendment.

The amendment was rejected.

Mr. KERR. Mr. President, I move that the vote by which the amendment was rejected be reconsidered.

Mr. HUMPHREY. Mr. President, I move to lay that motion on the table.

The motion to lay on the table was agreed to.

Mr. KERR. Mr. President, I ask unanimous consent that the Senate return to the consideration of amendment No. 8.

The PRESIDING OFFICER. The amendment will be identified for the information of the Senate.

The LEGISLATIVE CLERK. On page 388 it is proposed to insert the language commencing on line 11 down through line 14 on page 389.

Mr. KERR. Mr. President, I have explained the purposes of the amendment. As I understood, the Senator from Illinois was on his way to the Senate Chamber and desired to be present during the consideration of the amendment.

Mr. MANSFIELD. Mr. President, will the Senator yield briefly?

Mr. KERR. I yield.

Mr. MANSFIELD. Mr. President, I suggest the absence of a quorum.

The PRESIDENT pro tempore. The clerk will call the roll.

The legislative clerk proceeded to call the roll.

Mr. MANSFIELD. Mr. President, I ask unanimous consent that the order for the quorum call be rescinded.

The PRESIDING OFFICER (Mr. TADMAGE in the chair). Without objection, it is so ordered.

NATIONAL DRIVER REGISTER SERVICE

Mr. MANSFIELD. Mr. President, in 1960 Congress established a National Driver Register Service. This proposal established a clearinghouse through which new driver applications might be checked against revocation made for drunken driving or conviction for involvement in a fatal accident. This service is available to each of the 50 States and our territories.

The chief sponsor of this legislation here in the Senate was our distinguished colleague, chairman of the Senate Commerce Committee, the Senator from Washington [Mr. MAGNUSON]. The senior Senator from Washington recently prepared a progress report on this program for the Hearst Headline Service.

Mr. President, I ask unanimous consent that the article, which was published in the Seattle Post Intelligencer on July 22, be printed at the conclusion of my remarks in the RECORD.

There being no objection, the article was ordered to be printed in the RECORD, as follows:

DRIVER REGISTER KEEPS DANGEROUS ONES OFF ROADS

(By Senator WARREN G. MAGNUSON, Democrat, of Washington, chairman, Senate Commerce Committee)

Many are alive and drive today because Congress heeded the call of the States for a National Driver Register Service. For the same reason, some now walk or ride with others.

Effect of the driver register service is to provide a central clearinghouse available for each State and territory. They may check new driver applications against revocations made for drunken driving or conviction for involvement in a fatal accident, the only two offenses to bring national listing.

Congress established the new service in midsummer, 1960. Adopted was a measure I had introduced in the Senate, identical with one sponsored in the House. Our law enforcement officials had requested both, as had State and territorial officials concerned with licensing operators of motor vehicles.

The problem, they said, was a lack of interchange of information between States on license revocation for either drunken driving or conviction as an outgrowth of a fatality. Quite often, a person convicted in one State would step to another and obtain a license. Back on the highway he went with barely more than a short court stop.

Iowa provides an example of how our National Driver Register Service has short-circuited this maneuver. Recently an Iowa official advised Wendell Eames, Director, NDRS:

"We have had nine cases in which drivers we have revoked for drunken driving have been revoked by other States. We have subsequently written these States to obtain certified copies of the driving records of the drivers involved. We have received four of these certified copies at the present time and are in the process of taking action against them."

The same official added in his letter to Eames:

"We also use NDRS to check all applications for a new driver's license that have recently moved to Iowa from another State. This, too, has been beneficial. We have had 10 returned with an indication that these drivers have had or are presently under revocation. Seven of these ten were revoked in other States and three were revoked in Iowa. Of the three Iowa revocations, we

have filed charges of obtaining a fraudulent license against two of them."

The new service was effective in finding the Washington State driver who knew his Washington license would be revoked, so applied for one in Idaho. Idaho officials asked the national records be searched. They were. Not once, but several times, at different time intervals. The driver didn't get his Idaho license.

Or the South Carolinian who forgot to mention his previous violations when applying for a Texas operator permit. The complete file was in Washington, however.

Within 8 days he was out of the car in Texas, too.

One driver from Kentucky varied the procedure of his first name and omitted his middle initial when applying for a driver's license in Colorado. The national register filled in the blanks and supplied the Kentucky background of offenses to Colorado officials.

Probably the most optimistic, however, was the driver who, with revocations already received in two States—New York and New Jersey—both for drunken driving—applied again in Maryland only to be crossed up by the National Driver Register.

Recently, the Driver Register Service reported that it had in file two reports received from Texas which might refer to the same individual even though he had used considerably different names when convicted of each offense. Receiving this information, Texas officials replied:

"It was determined the two subjects mentioned in your memo were identical. We appreciate the information which you furnished * * * and take this opportunity to express appreciation for the splendid job which you are doing."

This type performance prompted members of the International Association of Chiefs of Police to adopt a resolution urging members to "actively support efforts by their State officials directed toward exploring the possibilities inherent in the operation of the National Driver Register Service."

It is true that many States interchanged information concerning potentially dangerous drivers before the new service was inaugurated within the Bureau of Public Roads, Department of Commerce. However, the interchange was on a regional basis, mainly. To do the job properly, it would have been necessary to send individual inquiries to each of the 50 States and 5 territories.

Now, the same end is achieved by dispatching one inquiry to the National Driver Register Service in Washington, D.C., and awaiting an answer.

The time saved in making an electronic check of the growing files may be just enough to save a life.

Mr. MANSFIELD. Mr. President, I suggest the absence of a quorum.

The PRESIDING OFFICER. The clerk will call the roll.

The Chief Clerk proceeded to call the roll.

Mr. MANSFIELD. Mr. President, I ask unanimous consent that further proceedings under the quorum call may be dispensed with.

The PRESIDING OFFICER (Mr. BURDICK in the chair). Without objection, it is so ordered.

REVENUE ACT OF 1962

The Senate resumed the consideration of the bill (H.R. 10650) to amend the Internal Revenue Code of 1954 to provide a credit for investment in certain depreciable property, to eliminate certain defects and inequities, and for other purposes.

Mr. KERR. Mr. President, is the committee amendment No. 8 the pending question?

The PRESIDING OFFICER. The Senator is correct.

Mr. KERR. I ask that the amendment may be agreed to.

The PRESIDING OFFICER. The question is on agreeing to the committee amendment No. 8.

Mr. DOUGLAS. Mr. President—

The PRESIDING OFFICER. The Senator from Illinois.

Mr. DOUGLAS. Do I correctly understand that the so-called Twin Cities Rapid Transit Co. amendment is now before the Senate?

The PRESIDING OFFICER. That is one characterization of it.

Mr. DOUGLAS. I did not hear the reply by the Presiding Officer.

The PRESIDING OFFICER. The amendment before the Senate is committee amendment No. 8.

Mr. DOUGLAS. I still cannot hear the Presiding Officer.

The PRESIDING OFFICER. The question before the Senate is on agreeing to committee amendment No. 8.

Mr. DOUGLAS. And what is that, may I ask?

The PRESIDING OFFICER. It relates to the subject to which the Senator referred.

Mr. KERR. Mr. President, if the Senator will turn to the page of the bill, I will show it to him.

Mr. DOUGLAS. Mr. President, I am asking a simple question, which I think can be answered simply.

Would the Presiding Officer kindly inform the Senate whether the amendment is the so-called Twin Cities Rapid Transit Co. amendment.

The PRESIDING OFFICER. That is correct.

Mr. DOUGLAS. I thank the Presiding Officer. We could have found that out much earlier.

Now may I address some questions either to the Senator from Oklahoma or to the Senator from Minnesota?

Mr. KERR. I should like to have the Senator from Minnesota answer the questions.

Mr. DOUGLAS. Mr. President, do I correctly understand that this amendment is designed for the relief of the Twin Cities Rapid Transit Co., of Minneapolis, Minn.?

Mr. McCARTHY. I do not know whether it could be properly described as designed for their relief. It is designed to take into account some rather questionable conduct by officers of the company. Because of mismanagement of the Twin Cities Rapid Transit Co. some years ago, the people who used that transit service, and the whole community, as well as the management, were deprived of the benefits which ordinarily would have gone through that company into the community.

Mr. DOUGLAS. Do I correctly understand that the amendment would permit the Twin Cities Rapid Transit Co. an additional 5-year carryover for the period commencing in 1960, in which to deduct losses as a result of converting from a streetcar to a bus system?

Mr. McCARTHY. That is correct.

Mr. DOUGLAS. Do I correctly understand that the losses were incurred in 1953 and 1954, when the company was managed by officers who were subsequently found guilty of conspiracy to defraud the company?

Mr. McCARTHY. That is correct. I am not sure that all of the officers were found guilty, but at least some people were involved.

Mr. DOUGLAS. As I understand the position of the company, it is that the management converted rapidly from a street railway system to a bus system in order to complete its fraudulent activities quickly, intentionally disregarding the income tax consequences.

Mr. McCARTHY. That is the way in which the action was interpreted. It was a unique operation compared to the record of other companies.

Mr. DOUGLAS. Do I correctly understand that the Internal Revenue Service turned down the claims of this company for relief?

Mr. McCARTHY. I do not know whether they made claims. If they did, I am sure they were turned down.

Mr. DOUGLAS. Was any attempt made to obtain relief from the courts?

Mr. McCARTHY. I do not know that they ever tried to obtain relief. There were actions in court against the officers, but whether the company used the laws relating to internal revenue for relief, I do not know.

Mr. DOUGLAS. Was the case taken before the Tax Court?

Mr. McCARTHY. So far as I know, it was not. I may be mistaken.

Mr. DOUGLAS. Do I correctly understand that a separate bill to this effect was passed in 1961, in the last session of Congress, in the concluding days?

Mr. McCARTHY. It was passed. That is correct. It was passed in the House and approved by the Senate Finance Committee, and then passed in the Senate in the concluding days of the session.

Mr. DOUGLAS. Do I correctly understand that the bill was vetoed by the President of the United States on October 4, 1961?

Mr. McCARTHY. That is correct, yes.

Mr. DOUGLAS. I hold in my hand a copy of the veto message.

Mr. McCARTHY. I have one on my desk.

Mr. DOUGLAS. Would the Senator from Minnesota permit me to read it?

Mr. McCARTHY. I should be glad to. I have read it, of course.

Mr. DOUGLAS. I think it might be of interest to make it a public record.

Mr. President, I ask unanimous consent that I may be permitted to read sections of this veto message.

The PRESIDING OFFICER. Without objection, it is so ordered.

Mr. DOUGLAS. Mr. President, I now read from the veto message by the President of October 4, 1961:

I can see no reason for making an exception to the policy of uniform treatment under the net operating loss carryover provisions of the taxing statutes under these circumstances. First, the extent to which tax considerations governed or would have governed the conversion from street railway to bus operations is necessarily uncertain. Secondly, assuming that the fraudulent conduct of the management of the com-

pany made it impossible to deduct all the losses sustained, it would be unfair to shift the consequences of that dereliction to the public through special tax relief. The stockholders of the company were certainly in a better position than the general public to guard against the misconduct of their officials. Thirdly, approval of this legislation is inconsistent with orderly tax administration. It discriminates in the treatment of taxpayers similarly situated and grants relief retroactively.

Although disapproval of this legislation may reduce the ability of the company to postpone or avoid a request for increases in its rates of fare, that fact should not be used to modify the tax system to shift the burden of losses from the taxpayer and the local community to the country as a whole.

Does the Senator from Minnesota agree that the Senator from Illinois has read the veto message accurately?

Mr. McCARTHY. I think the Senator has read it quite accurately; yes.

Mr. DOUGLAS. Now, however, the amendment is being offered as a rider on a general tax bill which the President cannot veto. Therefore, it is being sheltered from Presidential review.

Mr. McCARTHY. There are two things that took place when the veto message was written which have bearing on the discussion. One is the President's transportation message. I should like to read from the message of 1962 in which the President said:

(4) Income taxes: Another effort to improve equity in taxation is being taken by the Treasury Department, which is reviewing the administrative guidelines now governing depreciation rates in the transportation industry. The objective of this administration will be to give full recognition to current economic forces, including obsolescence, which in their impact upon the lives of depreciable assets may affect quite differently the different modes of transportation and, therefore, their competitive relationships. In addition, I recommend that the Internal Revenue Code be amended to increase from 5 to 7 years the period during which regulated public utilities, including those in transportation, can apply prior year losses to reduce current income for tax purposes.

That, of course, is a message and a recommendation. But it comes pretty much to the point that we are now proposing. The other and perhaps more significant point is that since the veto message was sent to the Congress, the Congress has acted upon the Du Pont bill. The Du Pont bill was approved by the President.

Mr. DOUGLAS. The Senator has referred to a highly iniquitous bill which the Senator from Illinois and the Senator from Tennessee fought on the floor of the Senate. I am not certain how the Senator from Minnesota voted on that issue.

Mr. McCARTHY. So as far as the President is concerned, the objections which might be made to this rather limited Twin City rapid transit bill might have been made also against the Du Pont bill, which he approved. I do not feel that the President's freedom to act on the bill would in any way be restricted by adding the provision to the pending tax bill.

Mr. DOUGLAS. Would not the Senator feel that the better way would be to withdraw the amendment from the

general tax bill and present the measure as a separate bill?

Mr. McCARTHY. I think not. The question of time is running against us. The bill was passed last year. It was approved by the Ways and Means Committee of the House.

Mr. DOUGLAS. I should be glad to help the Senator get the bill before the Senate. I do not promise to vote for it. From what I have seen, it is a bad bill. But I would not indulge in any delaying tactics. I believe the House has passed the bill, has it not?

Mr. McCARTHY. Not at the present session.

Mr. DOUGLAS. The House has not taken it up? Yet an effort is being made to blanket it into the general tax bill so that the House will have to take it and the President will have to sign it.

Mr. McCARTHY. The House has already acted on the measure at this session of the Congress in the Ways and Means Committee. It did so last year. It was not at the present session, but in the present Congress.

Mr. DOUGLAS. That action was wiped off the board by the presidential veto.

Mr. McCARTHY. We have the same membership in the House. We have not had an election since then.

Mr. DOUGLAS. The Senators from Minnesota are mighty men, and their persuasive influence extends to both the north and south wings of the Capitol.

Mr. McCARTHY. I hope that is true. I am glad to have the Senator make that statement.

Mr. DOUGLAS. Mr. President, I think we should be very careful about the measure. At present I am compelled to oppose the amendment. It grieves me very much to do so. The two Senators from Minnesota are personal friends of mine, but there is a saying that Caesar's sword in a righteous cause shall spare no one.

Mr. HUMPHREY. What about DOUGLAS' sword?

Mr. DOUGLAS. I must follow what I think is right whether it involves friend or foe.

Mr. HUMPHREY. Mr. President, will my colleague yield?

Mr. McCARTHY. I yield.

Mr. HUMPHREY. I am sure that our friend from Illinois knows that the industry is a regulated utility, and that the rate structure of the utility is determined by the operating profits or losses of that particular public transportation system. If the system operates at a loss, there is only one thing that happens. They go before the Minnesota Railroad and Warehouse Commission and get an increase in rates. So if the mismanagement of this particular transit company is to be left as a heritage upon the stock and capital structure of the transit company, there is only one thing that happens. The Commission raises the rates. The rates are not set by the company. The rates are set by a public body. There is in this particular transit system a continuing pattern of raising of rates, because of the operating difficulties the company had under bad management.

I wish to point out that there are a number of tax precedents in support of the measure. This is not unusual. In 1959 there was an amendment to the Life Insurance Income Tax Act which allowed an 8-year period to new life insurance companies for the carrying forward of operating losses, as distinguished from the normal 5-year period. There was a 1947 amendment, having a retroactive effect, providing specific relief for 7 railroads involved in receivership proceedings.

Mr. DOUGLAS. Mr. President, will the Senator yield?

Mr. McCARTHY. I yield.

Mr. DOUGLAS. I think what the Senator is saying is that since murder has been committed before, it should be permitted in the present case.

Mr. HUMPHREY. Not at all. What the Senator from Minnesota is saying is that since equity was granted before, it should be granted in the present case—not murder, but equity.

Mr. DOUGLAS. Why should the taxpayers of Illinois, Ohio, and Wisconsin pay for the derelictions—and I shall later come to what the derelictions were—of a transit company in Minnesota? It is a shifting of the tax burden.

Mr. HUMPHREY. There will be no refunds. The company has paid its taxes. What the measure amounts to is exactly what the President asked for in his transportation message. It would give a longer carryover period for losses; that is all. It just applies in this particular instance what the President has asked for in his general transportation message.

Mr. DOUGLAS. The President vetoed the proposal last year in a stinging veto.

Mr. HUMPHREY. The Senator is correct.

Mr. DOUGLAS. Why are not the Senators willing to submit the measure to the President as a special bill this year?

Mr. HUMPHREY. May I point out to the Senator that the Department of the Treasury has not registered any objection to the amendment.

Mr. DOUGLAS. The Treasury Department sometimes slips. They certainly slipped on the Du Pont bill.

Mr. HUMPHREY. If the Department slipped, the President slipped also, because the Treasury Department is his responsibility.

Mr. DOUGLAS. We must consider what is right, whether the measure is supported by the Senators from Minnesota and whether it is objected to by the Treasury Department. It is very clear that the President objected to the measure last year. Let it go to him as a separate bill this year and let him decide what he should do.

Mr. HUMPHREY. The Senator from Illinois judges that the bill is wrong, with all due respect—

Mr. DOUGLAS. Is it not true that the transit company of Minneapolis was controlled by elements that were supposed to be allied with the criminal underworld?

Mr. HUMPHREY. There were some elements in it that have been indicted and are serving sentences; that is true.

Mr. DOUGLAS. Were they not allied with what is supposed to be the criminal underworld?

Mr. HUMPHREY. That is the allegation that was made. I am not here to make that statement on the floor of the Senate. That is something for a judge or a court to determine.

Mr. DOUGLAS. Was not that question really decided in the case?

Mr. HUMPHREY. That was previous management; that is not current management.

Mr. DOUGLAS. I know, but the losses were incurred under the former management, and it is relief from those losses which the present company is seeking to obtain by special legislation sponsored by the Senators from Minnesota.

Mr. MCCARTHY. I point out to the Senator that losses were incurred by practically every metropolitan transit company that was operating.

Mr. DOUGLAS. Are these specific losses?

Mr. MCCARTHY. Not necessarily. They wanted to get in and out as fast as they could.

The Senator expressed concern over the fact that Minnesotans would receive advantages of the provision that people in Illinois, Ohio and Wisconsin would not receive. In the city of Chicago a similar loss was carried over.

Mr. DOUGLAS. I do not know about that. We bought the traction lines in the forties and paid a hundred million dollars for the lines. We converted to buses and paid for the buses out of our own money, and we floated bonds. We have not asked for tax relief. We have received no tax relief.

Mr. MCCARTHY. Is the Senator sure that there were no carryovers?

Mr. DOUGLAS. The Senator is asking for 5 additional years.

Mr. MCCARTHY. Only because—

Mr. HUMPHREY. I might say that the loss carryover was paid for in part by the people of Minnesota, for the benefit of those people in Chicago. I do not get to Chicago very often.

Mr. DOUGLAS. The Senator is asking for special legislation. I do not believe there was any loss carryover in the case of Chicago.

Mr. HUMPHREY. I do not know of any similar situation in the United States where there was not a carryover. If there is, I want to pin a medal on them.

Mr. LAUSCHE. Mr. President, will the Senator yield?

Mr. MCCARTHY. I yield.

Mr. LAUSCHE. We should not tie into a tax bill a measure that gives special relief. I do not believe it is sound for Congress to begin acting on an ad hoc basis in trying to deal with situations that might require a remedy. Two instances have been cited about the granting of some type of special relief. I recall the insurance company issue, and I opposed it. There are a number of weaknesses in this matter. The bill in the Senate was passed in the closing days of our last session. I did not even recall the matter having come up, because Senators will recall that we were grinding out bills, and no one could keep up with what we were doing. The

President said it was wrong to do it that way, and he vetoed it. Now it is sought to be wrapped into a package so that the President will not be able to reach this measure.

Mr. DOUGLAS. That is correct.

Mr. LAUSCHE. Perhaps he will want to approve it. If he does, let us submit it to him in a separate bill. If we are to start passing this type of legislation in this type of bill, where will it lead to? I venture to say that in Ohio, if I started combing around, I could find private companies which are confronted with the same type of problem. If this can be done for the Twin Cities Coach Co., of necessity, it has to be done for every individual and every corporation in the United States suffering from similar distress. I will oppose this measure. I believe it ought to come before the Senate in a separate bill.

Mr. DOUGLAS. I can imagine that every Senator could use not only the insurance precedent, which the Senator from Minnesota has used, but also this precedent that we are about to establish. We will then have a whole series of precedents. As a member of the Finance Committee I have looked askance at this practice. I have not always been able to stop it. At times it was because of a feeling of effection for my fellow Senators that I have allowed some of these matters to get on the floor. One man cannot stop many of them. However, in view of the fact that this bill was vetoed by the President, with what seemed to be a very cogent message, I join the Senator from Ohio in feeling that it is a great mistake to put it in a general bill which cannot be vetoed. I say it should be the subject of separate consideration.

Mr. LAUSCHE. The caution that has been exercised is manifested by the fact that there are only two instances in which this has been done.

Mr. MCCARTHY. No; we have a whole record of similar situations.

Mr. HUMPHREY. There are more than two. I had a chance to read only two. There are many instances.

Mr. DOUGLAS. Yes; I interrupted the Senator in his reading of the previous instances.

Mr. LAUSCHE. The fact is that in our Government we must have laws which are uniform in operation. When we start to depart from that rule we get into trouble. I would like to help the Senators from Minnesota.

Mr. HUMPHREY. Not help us. I have no interest in the street railway company. I have not even ridden their busline. The people in my city are of the opinion that this type of remedial legislation would be helpful to them. I wish to make it crystal clear that it is special legislation. We know it is. However, it is not unique. Special legislation has been passed here, changing effective dates, and changing certain tax laws, and other matters in which certain Senators are interested.

Mr. MCCARTHY. We passed a bill for the Senator from Illinois providing for retroactive relief for a pension fund.

Mr. DOUGLAS. Yes; for a union pension fund.

Mr. KERR. Mr. President, in view of the remarks of the Senator from Ohio, I refer to the 11th amendment. The Senator from Ohio has said that there should be uniform action. For years we had a provision in the law that an American citizen who owned real estate in a foreign country, or outside the United States in certain areas, would not have that property subject to our inheritance tax laws.

The House bill dealing with the subject now before the Senate had a provision in it repealing that special exemption from the general revenue law and from the general law applicable to everyone; and the effective date of the repeal in the House bill was July 1, 1964. The Committee on Finance changed that date and made the repeal of that special privilege under the law for real estate owned by American citizens, so as not to be subject to the inheritance tax laws, January 1, 1963. In other words, we changed the date from the date in the House bill, July 1, 1964, to January 1, 1963. That was objected to by the Senator from Ohio. He would not agree that that law be repealed, which granted special privilege to Americans owning real estate abroad not being subject to the inheritance tax, until we moved the effective date of the repeal of that special privilege back to July 1, 1964. It was done at the request of the Senator from Ohio, and it is now in the bill.

Mr. DOUGLAS. Yes; but—

Mr. KERR. I call attention to this fact to show that the Senator from Ohio is not always fighting for the application of uniform laws with reference to all.

Mr. DOUGLAS. Does the Senator contend that two wrongs make a right?

Mr. KERR. The Senator from Oklahoma does not contend that either is wrong; nor does the Senator impose his conscience upon other Senators who have as much conscience as the Senator from Oklahoma. I want to say to the Senator from Illinois that he is not the only man on the floor with a conscience. I wish to say further that the fact that he does not agree with something does not make it wrong.

Mr. DOUGLAS. Of course not.

Mr. KERR. The Senator from Oklahoma does not know why the Senator from Illinois should say that if on something someone does not agree with him, that that something is wrong.

Mr. DOUGLAS. I say in my judgment it is wrong.

Mr. KERR. I agree that the Senator's judgment is wrong. I have never agreed more with the Senator.

Mr. DOUGLAS. I said that in my judgment the proposal is wrong.

Mr. KERR. That is not what the Senator said.

Mr. DOUGLAS. Yes, I did.

Mr. KERR. I do not agree with the Senator's judgment.

Mr. LAUSCHE. With regard to the measures that was brought up by the Senator from Oklahoma, at the time the provision in the bill before the Senate came out of committee, citizens came to me and said, "We would be forced probably to sell at a depreciated value the

properties which we own in the Virgin Islands."

Mr. KERR. They needed time.

Mr. LAUSCHE. Just a moment. I have listened to the Senator from Oklahoma more than I like to listen to him. I am asking him to listen to me for a moment.

Mr. KERR. I have listened to the Senator from Ohio longer than I like to listen to him. However, he still listens to me.

Mr. LAUSCHE. Will the Senator from Oklahoma please listen to me?

Mr. KERR. The Senator still listens to me.

Mr. LAUSCHE. Mr. President, I am one of a hundred Senators. I have a right to speak, and I should not be burdened with listening to the Senator from Oklahoma talk down Senator after Senator who is expressing his view.

Mr. KERR. The Senator from Oklahoma always expresses his views, and so does the Senator from Ohio.

Mr. LAUSCHE. So does the Senator from Oklahoma. The Senator from Ohio will not be a slave to the Senator from Oklahoma. I have my own mind. I have my own conscience. I will not let the Senator from Oklahoma rule my mind. I need not let the Senator from Oklahoma rule my thoughts.

Mr. KERR. The RECORD shows that the Senator from Ohio asked for—

Mr. MANSFIELD. Mr. President, I ask for the regular order.

Mr. KERR (continuing). A special privilege law.

Mr. LAUSCHE. The Senator from Ohio never asked for special privilege. It is the Senator from Oklahoma who is—

Mr. MANSFIELD. Mr. President, I demand the regular order. Who has the floor?

The PRESIDING OFFICER. The Senator from Illinois has the floor.

Mr. McCARTHY. Mr. President, I think I have the floor.

The PRESIDING OFFICER. The Senator from Minnesota has the floor.

Mr. KERR. Mr. President, a parliamentary inquiry.

The PRESIDING OFFICER. The Senator from Oklahoma will state it.

Mr. KERR. Did the Senator from Minnesota yield to the Senator from Oklahoma?

Mr. McCARTHY. I yielded to the Senator from Oklahoma. I want to hear the Senator from Oklahoma.

Mr. KERR. Mr. President—

Mr. DOUGLAS. Mr. President, did the Senator from Minnesota yield to the Senator from Oklahoma for a speech or for a question?

Mr. McCARTHY. I will yield for a question or a speech.

Mr. KERR. I thank the Senator for yielding for a question. What I wish to say cannot be stated in the form of a question, so I will wait and speak on my own time.

Mr. McCARTHY. I said I would yield for a question or for a speech.

Mr. KERR. The Senator from Montana asked for the regular order.

Mr. DOUGLAS. I will not object.

Mr. KERR. The Senator from Illinois is not the Senator from Montana, either.

Mr. MANSFIELD. I do not object.

Mr. KERR. Mr. President, I ask unanimous consent that the Senator from Minnesota may yield to me for an observation, without losing his right to the floor.

The PRESIDING OFFICER. Is there objection? The Chair hears none, and it is so ordered.

Mr. KERR. The Senator from Oklahoma thinks the Senator from Ohio has as fine a mind and conscience as there is in the membership of this body. The Senator from Oklahoma is satisfied with his own mind and his own conscience. He asks for its approval by no other Senator. He merely called attention to the fact that there is on the statute books of this country a special law for the benefit of American citizens who own real estate abroad. It is a special law which provides that such real estate or its value is not subject to the inheritance tax when the owner dies. I think that is a special law. Everyone is entitled to his own opinion as to whether that is a special law. Either it is or it is not. The Senator from Oklahoma says it is.

In the bill, the House proposes to repeal that section effective July 1, 1964. The Senator from Oklahoma, believing it is a law to give special privilege to American citizens who own real estate abroad, felt that it should be repealed as quickly as possible rather than be repealed effective July 1, 1964. So the Senator from Oklahoma, in the Committee on Finance, sponsored an amendment which would make the repeal effective January 1, 1963. It was unanimously voted into the bill by the Committee on Finance.

That amendment has come to the floor of the Senate. It is 1 of 174 amendments which the committee made. The Senator from Oklahoma asked unanimous consent that all those amendments be agreed to en bloc, considered as a part of the original text, and then be subject to amendment offered by any Senator. That unanimous consent request was objected to by the Senator from Tennessee [Mr. GORE] and other Senators with respect to 10 amendments. The unanimous consent request was objected to by the Senator from Ohio [Mr. LAUSCHE] with reference to the amendment which would end on January 1, 1963, instead of July 1, 1964, what the Senator from Oklahoma regards as a special privilege.

The Senator from Ohio [Mr. LAUSCHE] said there were some citizens in his State who had some property abroad and that they needed additional time in which to dispose of it without being penalized by having to put the property on the market for a quick sale before January 1, 1963. The Senator from Oklahoma thought two things about that request: First, there was possibly some merit to it. The bill is coming to a vote in the Senate; and if enacted, it would be much later in 1962 than would have been the case had it been enacted some months earlier. Also, the Senator from Oklahoma, anxious to have the bill acted upon by the Senate, went to the extent

of asking the Senate not to agree to that amendment, which means that the bill will be left in such form that it will not repeal what the Senator from Oklahoma regards as a special privilege until July 1, 1964; and he did so at the request of the Senator from Ohio [Mr. LAUSCHE]. That is the cold record.

Mr. MANSFIELD. Mr. President, will the Senator from Minnesota yield?

Mr. KERR. Mr. President, Senators may make up their own minds as to whether the right to own real estate abroad and not have it subject to inheritance tax in the event the owner dies is a special privilege. Any real estate which a citizen owns in this country is reflected in his estate when he dies, and its value is taxed. Senators may make up their own minds whether the right to own real estate in a foreign land and have it escape the inheritance tax is a special privilege. If it is, and if the bill is enacted, that privilege will continue to exist by reason of the request of the Senator from Ohio, until July 1, 1964, instead of expiring January 1, 1963.

Mr. MANSFIELD. Mr. President, will the Senator from Minnesota yield?

Mr. McCARTHY. I yield.

Mr. MANSFIELD. I think there was great merit in the amendment proposed by the Senator from Ohio. Had I been in his shoes, I would have offered the same amendment. At the same time, it was the Senator from Oklahoma who called up the amendment today, and, over opposition orally expressed in the Chamber, was able to persuade a majority of the Senate to approve the amendment. I think that statement also should be in the RECORD.

Mr. KERR. But to comply with the request of the Senator from Ohio, who was not present, I thought I was doing him a special courtesy, a special favor, to take care of it even though he was not on the floor of the Senate, and even though his request was objected to by Senators who were in the Chamber.

Mr. LAUSCHE. The tone and words of the Senator from Oklahoma are completely different now from what they were when he jumped to his feet and started to point shafts at me. If he had spoken in his first presentation of this issue in the tone which he has now used, I would not have responded in the way I did. But he took the floor and made it appear as though I were trying to have something passed which was iniquitous.

Mr. KERR. Why—

Mr. LAUSCHE. Just one moment. In the House, it was determined that real estate owned in foreign countries should be included as a part of the estate of a deceased person immediately, which is not the situation as the law exists today.

The House provided that July 1, 1964, should be the date of the operation. In the Committee on Finance, the date was changed from July 1, 1964, to January 1, 1963; it was moved back 18 months. An Ohio citizen came to me and said, "If a death occurs after this law has gone into effect, we will be forced to divest ourselves of that holding with a speed which will work an injustice." So I spoke with the Senator from Oklahoma

and presented the problem of fixing the date as of July 1, 1964.

I came downtown this morning and contemplated taking the date January 1, 1964, as was suggested last night. But I did not ask for any special legislation or any special consideration.

If there is anything that I take pride in it is my purpose not to ask for my State or for anyone any special consideration from the U.S. Congress; and I shall continue to follow that course.

Mr. President, the pending proposal means nothing whatsoever to me. I have no interest in it, except in wanting to assure that justice will be done. If, in the effort to attain that objective, I must be made to appear, on the floor of the Senate, as a base individual, I will not stand for it. Others may subject themselves to that type of attack, but I will not stand for it. I have been in public life for 30 years. I have striven with all my might to protect my reputation. I have not become alined with any group—so I could come on the floor of the Senate or act in the office of mayor or act in the office of Governor as boss of myself.

So, Mr. President, to come here and have what I have striven to build up through the years sought to be destroyed by men with powerful words is more than a Senator should be subjected to; and when I say that, I say it in behalf of other Senators, who likewise have been subjected to treatment of that type.

Mr. MANSFIELD. Mr. President, will the Senator from Minnesota yield?

Mr. McCARTHY. I yield.

Mr. MANSFIELD. Mr. President, no one doubts the honesty or integrity of the Senator from Ohio or his lack of special pleading in the interest of anyone. He is an honorable and a conscientious man, who has proved that fact through the years. So, also, is the Senator from Oklahoma [Mr. KERR].

I point out also that today both the Senators from Minnesota—the senior Senator from Minnesota [Mr. HUMPHREY] and the junior Senator from Minnesota [Mr. McCARTHY]—have stated that they, likewise, have no personal interest in the issue which is before the Senate for consideration.

Mr. DOUGLAS. I am sure that is true.

Mr. MANSFIELD. Yes; and I, too, am sure of it.

So I hope that any apprehension which may have arisen today will be forgotten, because I am sure there is not the slightest intention to reflect on the honesty or integrity of the Senator from Ohio.

Mr. LAUSCHE. The whole thing is trivial, so far as dollars are concerned. The essential thing is the matter of integrity.

I ask Senators to pardon me for this outburst. But if I did not express my convictions, if when I returned home tonight I had to confess to myself that I had not stood up for the things in which I believe, but had allowed myself to be overrun by a juggernaut, and had not spoken up and protested, I would have to feel that I was a worm. And that I do not propose to do.

Mr. KERR. Mr. President, will the Senator from Minnesota yield?

Mr. McCARTHY. I yield.

Mr. KERR. Mr. President, I did not say there was anything iniquitous in what the Senator from Ohio did or asked. If I had thought there was, I would not have sought to do the favor that I thought I was doing for the Senator from Ohio when I acceded to the request.

Mr. LAUSCHE. It is not a favor to me. Strike it from the bill.

Mr. KERR. That may be done.

I was merely indicating for the RECORD my understanding and my purpose.

I do not think any Senator is a worm.

I have two further things to say, Mr. President: I have not impugned the motives or the character or the senatorial integrity of the Senator from Ohio, and I will not. Neither will I again seek, over opposition nor with others in union, to do a favor for the Senator from Ohio. From here on, he may seek his own.

Mr. DOUGLAS. Mr. President, will the Senator from Minnesota yield?

Mr. McCARTHY. I yield to the Senator from Illinois.

Mr. DOUGLAS. Mr. President, if we may return to the Twin Cities Rapid Transit Co. case, let me ask the Senator from Minnesota whether any Senate committee hearings have been held on this measure.

Mr. McCARTHY. They were held last year.

Mr. DOUGLAS. Were they hearings, or was it considered in executive session?

Mr. McCARTHY. I think it was considered in executive session.

Mr. DOUGLAS. I think that is correct. So there were no general hearings.

Mr. McCARTHY. I think the hearings were held in the House committee.

Mr. DOUGLAS. I think that is correct.

I find that the bill was reported last year from the Senate Finance Committee on September 23; and the Senate adjourned on September 26. So the bill was reported in the concluding days of the session. It came out last year as a special bill. As I remember the situation, I more or less accepted it on the word of the Senator from Minnesota, without question. Perhaps I was derelict in doing so; but the pressure of legislation was very great, and perhaps I was trying to be accommodating to the Senator from Minnesota.

I think that, in general, special legislation at the end of the session is dangerous. But we always have the President to fall back upon. In this case the President, in the exercise of his judgment, vetoed the bill.

This year, however, no attempt is being made to pass the bill over the President's veto; this proposal is not being submitted again as a separate bill. It is being blanketed in a general tax bill, which in all probability the President must sign in order to have enacted into law certain measures of which he approves. So this procedure really means circumventing independent action by the Executive.

I have great respect for the Senator from Minnesota. He is one of the finest Members of the Senate. He has a very fine philosophical attitude. He is a man of high personal integrity. He has a dry wit which is very penetrating and throws much light on issues which otherwise would not be understood. I hope he does not regard my attitude as in any sense personally hostile to him.

But we are legislators for the United States of America. Sometimes we assume the attitude of according accommodation for our friends. Perhaps at times I have not been as vigilant as I should have been. I am aware of the fact that frequently I am criticized—as I was criticized by the Senator from Oklahoma—for being too vigilant and I have been charged with pretending that I know it all—which I certainly do not.

But I think this proposal should be considered on its own merits, and should not be attached as a rider to the general tax bill.

I felt somewhat similarly about the amendment of the Senator from Delaware; and I regret that because I worked very late into the morning and had only a few hours sleep, I was not able to be on the floor when the amendment of the Senator from Delaware came up. I thought I had an agreement with him that there would be no voting until I came on the floor. But I find that the amendment was agreed to. However, I make no complaint about that.

But now I am in the Chamber, and I think I have a duty to raise questions about the amendment.

Why is not the Senator from Minnesota willing to have this proposal considered as a separate bill? I promise that I would not then object to its consideration. I doubt that I would vote for it, but I would not try to delay or impede its consideration in the slightest degree.

Mr. McCARTHY. Mr. President, I appreciate the position of the Senator from Illinois. It is no different from his policy in regard to general legislation.

However, this is not the kind of bill that one is happy to carry to the floor of the Senate. One carries it there by necessity and, I think, with justification.

We are not asking for any change in the basic laws regarding transit companies. We are merely requesting special consideration because under very unusual circumstances the transit company in our State and the people who use that service were deprived of the benefits made available to everyone else in the country under the general tax laws of the country. I would be glad to have this proposal presented separately. I am not sure, but I think the veto of the President last year was a mistake. Certainly it seems to me a mistake in light of his transportation message, and in light of the request which was made of the Congress last year when we appropriated something like \$50 million to give assistance to transit companies in the cities. There are two or three bills now pending in this general area.

A basic tax provision was laid down for the purpose of helping transit companies change over from streetcars to

buses. Because of very unusual circumstances in the Twin Cities, Rapid Transit Co. of Minnesota, they were not able to take advantage of the law, an advantage which was given to everyone else in the country, so far as I know. We are asking for this advantage as a retroactive request. I do not think it is unreasonable. I think it is reasonable in the name of equity and justice. Whereas there may not be an exact precedent for it, many precedents have been established in the same general area.

Mr. DOUGLAS. It seems to me there is a distinction between this case and others. First, there was fraudulent conduct on the part of the management of the company; second, the fraudulent conduct made it impossible to deduct all the losses sustained; third, it is proposed to shift the consequences of the fraudulent conduct to the public by tax relief. It was largely on that basis, according to the President's veto message, that the President vetoed the bill.

From what I know of the case, I should say the President was correct. From what I know of the case, I would vote against the amendment if it were brought up as a separate bill. But I think the Senate should consider it as a separate bill, and not blanket it into a general tax bill, which would immunize it from any possibility of Presidential veto.

Mr. McCARTHY. It was not my intention to do that so that the President could not veto it. I was not the first to make a move to offer what might be called legislation outside the bill, but when I saw the senior Members of the Senate offer proposals so that they could get action in this session of Congress, I decided that time was running out on us. Since time is important, and every year that passes the inequity increases and the difficulty of getting action on it increases, it seemed to me this was the time to act. I believe it would be impossible to obtain separate consideration and separate action on the measure in this session of Congress.

Mr. DOUGLAS. I understand the motives of the Senator from Minnesota. I think he makes a valid point. My own feeling is that too many bills are considered in executive session in the Finance Committee without prior hearings. The volume of work of the Finance Committee this year has been staggering. The tax bill, the trade bill, veterans' legislation, and the sugar bill were all poured in upon us. The major bills of the session have had to go through the Finance Committee, which does not have subcommittees, and which operates as a committee of the whole.

The Senator from Louisiana and I have felt for some time that there should be subcommittees of the Finance Committee, but this is not the occasion to go into the internal organization of the committee. I think this situation illustrates the disadvantage at which we are placed.

I can understand that once the rush starts, once the senior members of the committee bring up special interest bills, one can hardly be expected to fold his arms, take no action, and allow strategic

Members to get on board the gravy train, and not do anything for their own constituents back home. I understand that perfectly.

I want it understood that I am not blaming the Senator from Minnesota in the slightest. It seems an ungracious thing for me to do this. The friendship that exists between Senators would make it much easier to soft-pedal these matters. But this proposal involves approximately \$5,800,000. It is a very large sum. Without being self-righteous—and I think the Senator from Minnesota has perhaps at times regarded me as being self-righteous—I feel that we should not blanket this measure into the tax bill.

The special legislation with which we deal in the Senate never raises taxes, and never raises revenue. It is always to give a favor and to lessen taxes for some particular individual. We never remedy injustices in the tax structure that have to do with the general public. What we do is grant relief to pressure groups or certain individuals.

Mr. McCARTHY. There is an unused loss of approximately \$5 million, all of which probably could have been transferred to the taxpayers of Illinois, Minnesota, and other taxpayers. The situation developed because of mismanagement and corrupt management. The fact is that probably \$2 million to \$3 million of the loss can be offset, so whoever is involved in the transit company would have losses of \$2 or \$3 million anyway.

Mr. DOUGLAS. I do not know the circumstances attending the purchase of the transit system from the undesirable elements which formerly owned it, but when the purchase was made the purchasers should have gone into these matters with their eye open.

Mr. HUMPHREY. Mr. President, if the Senator will yield, it was not a matter of purchase. What happened was that the managerial body or group that was operating the transit company engaged in fraudulent activities. There are now new directors and new management, but there is not necessarily new ownership.

My interest in this situation was aroused by the fact that some of the most eminent and prominent citizens in our community asked that we consider this case and see if some relief could not be afforded. The present Internal Revenue Code provides that any transit company may convert from a street railway to buses over a period of years, and that losses that are sustained thereby are deductible against income.

Other transit companies have made this change and have taken advantage of the full-time factor under the present Revenue Code. This company did not do so. It did everything in 18 months instead of converting over a period of several years as prudent management would do in order to take full advantage of the present loss carry-forward provisions in the law. It was one of the most unhappy, unfortunate situations.

Mr. DOUGLAS. It was not only unhappy and unfortunate, but it was fraudulent and crooked.

Mr. HUMPHREY. It was fraudulent and criminal.

Mr. DOUGLAS. Now the question is, Should the taxpayers be asked to bail out the company? I was interested in hearing the Senator say that the owners are the same now. Having allowed the former management—

Mr. HUMPHREY. I do not know that they are all the same. The majority of the shares of stock of this company are owned by thousands of people. As a matter of fact, the stock is listed on the New York Stock Exchange.

Mr. DOUGLAS. The Senator from Minnesota has again and again criticized the use of widows and orphans—

Mr. HUMPHREY. I do not mean that they own the bulk of the stock, but it is widely held. It is an old company. It has been in existence from the 1890's. It is the same old company.

Mr. DOUGLAS. How much of that was fraudulent?

Mr. HUMPHREY. The fact is that because of the fraudulent management of the company there was a failure to take advantage of \$5 million of conversion expense in round figures.

Mr. DOUGLAS. Five million dollars was adjudged to be fraudulent?

Mr. HUMPHREY. I do not know that, Senator.

Mr. McCARTHY. It was not adjudged fraudulent. The fraudulent actions did not bear upon this. It was bad management to convert in 18 months, instead of spreading it over a longer period of time, so that the loss could be carried forward, as other companies carried forward their losses. My understanding is that the loss was not related to the fraudulent management at all. That was incidental and outside, I say to the Senator from Illinois.

Mr. DOUGLAS. I do not wish to delay the proceedings on the bill. I do not wish to carry on the discussion interminably. I merely ask whether the Senators from Minnesota would be willing to withdraw this amendment from the bill and to treat the matter separately.

Mr. McCARTHY. To do that, in effect, would be to say that there would be no action in this Congress, and I would have to refuse.

Mr. DOUGLAS. Then, Mr. President, I think we should have the discussion before the full Senate. Unless I hear a good reason to the contrary, I am going to suggest the absence of a quorum, which I am not quite doing at this moment.

Mr. HUMPHREY. Mr. President, before the Senator does that, I wish to say that there is legislation which is to come before the Senate very shortly, known as the mass transit legislation.

Mr. McCARTHY. The same argument which the Senator makes against this amendment would run against that proposal.

Mr. HUMPHREY. That mass transit legislation would provide grants and loans and financial assistance running into millions and millions of dollars.

Mr. DOUGLAS. It is not special legislation.

Mr. HUMPHREY. It is special legislation for cities which have mass transit systems.

Mr. DOUGLAS. Possibly Minneapolis could come in under that legislation.

Mr. HUMPHREY. That might be true.

Mr. DOUGLAS. I simply object to a \$5.8 million grant for operations which were certainly at least partially fraudulent.

Mr. HUMPHREY. I say to the Senator from Illinois that the point is that if this company had been under normal prudent management the tax situation would have been identical to that we propose.

Mr. DOUGLAS. That remains to be demonstrated.

Mr. HUMPHREY. The figures show that there was a \$10.2 million conversion loss.

Mr. DOUGLAS. And they allowed \$5.2 million.

Mr. HUMPHREY. That was because there was a conversion in only 18 months, instead of taking the full time permitted under the law. The company did not have an opportunity under the law to take care of all the conversion loss.

Mr. DOUGLAS. Was not the conversion period speeded up because the management of the company wanted to loot the company?

Mr. HUMPHREY. Exactly. Exactly. The management of the company is one thing, and the stockholders and the bus riders are another.

Mr. DOUGLAS. But the owners of a company must be responsible for the management of the company. The management does not float in a void. It is elected by the stockholders. If the stockholders neglect their duty and permit a fraudulent management to continue, they are responsible.

Mr. HUMPHREY. Very well. What happens when a president of a bank runs away with the funds of depositors, and is then put in jail?

Mr. DOUGLAS. The bank suffers a loss.

Mr. HUMPHREY. The depositors are insured under a program of the Federal Government. The people of the United States help to pay for that insurance.

When there are programs of public interest, such as those involving the bank structure, when somebody takes the deposits we do not merely say, "Well, it is too bad for the depositors." We provide a program which says, in effect, "Savings up to so much are protected by the Federal Deposit Insurance Corporation."

We would say in this instance that since there were fraudulent practices, a criminal element, which resulted in defrauding the people and defrauding the company, there should be protection. Had the company adopted the practices of other transportation companies and converted gradually the losses of the company could have been charged off against profits in ensuing years.

All we say is that we do not want to have the stockowners and the public penalized because of the fraudulent activities of those who are presently serving prison sentences, when the tax laws could be modified so that there would

be no loss either to the company or to the bus riders.

Mr. DOUGLAS. I will say to the Senators that in the absence of general legislation to protect the owners of street railway systems from fraudulent conduct by management, with the information which I now have available, I certainly do not wish to approve special legislation to bail out one company which suffered losses largely because of fraudulent conduct, which company now seeks relief.

Mr. MCCARTHY. If the Senator would permit me to make a point in this regard, the company suffered losses not because of the fraudulent actions of the management but because the management was in and out so quickly. If the company had had the most honest management, the conversion losses would have occurred even under the honest management, but the losses could have been carried forward, and advantage taken of the general law with respect to rapid transit systems.

Mr. DOUGLAS. The junior Senator from Minnesota lives in one of the Twin Cities. The senior Senator from Minnesota lives in the other of the Twin Cities, and has been mayor of that city. The Senators are much more acquainted with the local situation than I am. I wish to say, however, it seems to be apparent that part of the speed with which the conversion was accomplished was itself part of the fraud.

Mr. MCCARTHY. It was a different kind of fraud.

Mr. DOUGLAS. Now the general taxpayers of the country are being asked to bail out the owners who permitted these fraudulent officers to stay in office. They elected them to office and permitted them to continue for a period of time.

I do not wish to labor this point. I have great respect for the Senators from Minnesota, but I would like to suggest the absence of a quorum, and then we will get a vote on the amendment.

Mr. MILLER. Mr. President, will the Senator from Illinois yield for a question?

Mr. DOUGLAS. The Senator from Minnesota has the floor.

Mr. MCCARTHY. Mr. President, I yield the floor.

Mr. MILLER. Mr. President, I should like to ask the Senator from Illinois whether this is about the same as asking Congress to waive the statute of limitations with respect to the filing of a claim for a refund of taxes.

Mr. DOUGLAS. I think that is correct, but in this circumstance it is connected with fraud.

Mr. MILLER. I can visualize, and I am sure the Senator from Illinois can visualize, a situation in respect to which a claim for refund was not filed because of mismanagement. In that situation, it has been my observation, the Congress usually does not waive a statute of limitations by a special act.

Mr. DOUGLAS. Sometimes the Congress does, unfortunately, by special legislation.

Mr. MILLER. If Congress should do that, would it do it under circumstances similar to those of this case?

Mr. DOUGLAS. Congress does that under circumstances in which the Ways and Means Committee of the House and the Finance Committee of the Senate will approve it. Generally, it is without public hearings, as a result of discussion in executive session. Then the provision goes through on the floors of the Houses of Congress, because no one wants to make himself unpopular by standing up and opposing a proposal advanced by an individual Senator.

Mr. MILLER. What the Senator is really saying is that while this has been done in the case of claims for refunds, because of special circumstances, he does not favor the approach in this case.

Mr. DOUGLAS. I do not favor it as a general approach. I certainly do not favor having such a thing blanketed into a general tax bill.

Mr. MILLER. I thank the Senator from Illinois.

Mr. PROXMIRE. Mr. President, will the Senator yield for a question?

Mr. DOUGLAS. Do I have the floor, Mr. President?

The PRESIDING OFFICER. The Senator from Illinois has the floor.

Mr. DOUGLAS. I am glad to yield, though I must say that I am not an expert on this matter. I have been merely questioning the amendment.

Mr. PROXMIRE. Although the Senator may not be an expert on this particular matter, he is an expert on this bill and I should like to ask him a question.

Is the pending amendment a proposal to put into the tax bill a special carry-forward opportunity for a particular utility in Minnesota?

Mr. DOUGLAS. Yes; and a carry-back opportunity, too, for a prior period of loss.

Mr. PROXMIRE. Would this apply to a particular utility?

Mr. DOUGLAS. Yes.

Mr. PROXMIRE. And not to others?

Mr. DOUGLAS. Yes.

Mr. PROXMIRE. Is that because only a specific year is involved?

Mr. DOUGLAS. Yes.

Mr. PROXMIRE. Would it be special legislation, in the sense that it would involve one particular concern?

Mr. DOUGLAS. That is correct.

Mr. PROXMIRE. Is it also true that, while special legislation of this kind has been passed in previous years, this would be unprecedented, or virtually unprecedented, in that it would be passed as a part of a general taxation bill?

Mr. DOUGLAS. I wish I could reply to that in the affirmative.

Mr. PROXMIRE. I said "virtually unprecedented." It is very rare?

Mr. DOUGLAS. Yes; I think it is relatively rare, but I think it is a practice which is increasingly creeping into legislation.

Mr. PROXMIRE. One of the advantages, from the standpoint of those who propose this amendment, as I understand, is that if it should become a

part of the tax bill it would mean it would be impossible for the President of the United States to exercise his constitutional opposition to this particular provision by vetoing it, unless he vetoed the entire tax bill. Is that correct?

Mr. DOUGLAS. That has not been explicitly stated—

Mr. PROXMIRE. No; I do not say that is the intention. I say that would be one of the consequences.

Mr. DOUGLAS. That would be one of the effects, without question. The President could not exercise independent judgment with respect to the provision which he vetoed last year.

Mr. PROXMIRE. The Senator from Wisconsin is also deeply concerned about the implications of that kind of approach. Does it not seem that Senators who happen to have the advantage of being influential with powerful dominant members of the Finance Committee are in a position to obtain special consideration for their States, but those of us who have no such dominant representation or friends on that very important committee cannot obtain such recognition for our States?

Mr. DOUGLAS. There is a little verse that goes—

The good old rule,
The simple plan,
That they shall take
Who have the power
And they shall keep
Who can.

Those who have powerful friends on the Finance Committee, or are friends of powerful members of the Finance Committee, can frequently enjoy a better meal at the public table than those to whom the doors are barred.

Mr. SMATHERS. Mr. President, will the Senator yield?

Mr. DOUGLAS. I yield.

Mr. SMATHERS. I should like to have the Senator from Wisconsin know that any time that he has any problem involving anybody in Wisconsin, he will get just as sympathetic and prompt consideration from me as if the problem arose in my own State. So I do not want him to feel lonely or left out. He has a friend.

Mr. PROXMIRE. I thank the Senator. It is good to know that I have a friend.

Mr. KEFAUVER rose.

Mr. PROXMIRE. Before the Senator yields to the Senator from Tennessee, I should like to ask the Senator from Illinois finally if what I am about to state is a fair summation: First, the proposed provision is one which would favor one particular city or one particular State in the Union.

Mr. DOUGLAS. I would not say a city or a State.

Mr. PROXMIRE. One particular company.

Mr. DOUGLAS. One particular company.

Mr. PROXMIRE. That is correct; the stockholders and customers of that concern.

Mr. DOUGLAS. Not necessarily the customers.

Mr. PROXMIRE. Very well. The stockholders.

Second, it is a provision with respect to which the President has already indicated his position on the merits by vetoing it.

Mr. DOUGLAS. That is correct. He vetoed it last year.

Mr. PROXMIRE. If the measure were attached as a rider to a general tax bill the President would not have such independent opportunity in the future.

Mr. DOUGLAS. That is correct.

Mr. PROXMIRE. Third, the particular method attempted, while it may not be totally unprecedented, seems to be rare and, at least on the basis of the limited experience of the Senator from Wisconsin, who has been a Member of this body for 5 years, it is most unusual and does not seem to be available to Senators who represent other States.

Mr. DOUGLAS. I think it would create a most unfortunate precedent.

Mr. PROXMIRE. I thank the Senator.

Mr. KEFAUVER. Mr. President, will the Senator yield?

Mr. DOUGLAS. I yield.

Mr. KEFAUVER. Unfortunately, I did not hear all the colloquy. What is the difference, if any, between the proposed legislation and the measure that was previously vetoed by the President?

Mr. DOUGLAS. As I understand, they are identical.

Mr. KEFAUVER. I thank the Senator.

Mr. DOUGLAS. Mr. President, I suggest the absence of a quorum.

Mr. KERR. Mr. President, before the Senator does so, the Senator from Oklahoma would like the floor for a moment.

The PRESIDING OFFICER. Does the Senator withhold his request?

Mr. DOUGLAS. Yes. I withhold the request to oblige the Senator from Oklahoma.

The PRESIDING OFFICER. The Senator from Oklahoma is recognized.

Mr. KERR. Mr. President, for the record, I should like to make clear one or two things with reference to the amendment. In the first place, it is a general amendment which would be applicable to any company that might come under the specifications contained in the amendment.

Second, in view of the fact that the utility is regulated, its rates would ordinarily be set so as to enable the company to obtain a fair return on its investment and replace its investment.

It was an unfortunate set of circumstances that brought about the situation in which the streetcar company became involved. The company sustained severe losses due to the corruption of certain of its officers and managers. As I understand, some of those who were guilty were sent to the penitentiary.

The Senator from Oklahoma feels that the real people at interest are the consumers in Minneapolis and St. Paul, Minn. The rates of the street railway company will have to reflect its losses as well as be affected by its earnings. If it is not permitted to recoup its losses, its only alternative is to seek to increase its rates.

The Senator from Oklahoma feels, therefore, that the amendment has

equity. Had he not thought so, he would not have favored its adoption in the committee. He would not have favored adoption and passage of the bill last year.

It is true that a similar bill was vetoed by the President of the United States. The President has a right to veto any bill that comes before him. It is also true that the Congress of the United States passed the bill. The Congress passed it because the Congress believed it was equitable. It passed it as it has passed many other pieces of legislation calculated to provide a better environment for transportation companies, both municipal and railway, intrastate and interstate. Many of them are in serious economic difficulties.

The Congress of the United States has probably given more consideration to the enactment of legislation calculated to provide a more favorable economic opportunity or environment for transportation companies than to any other subject upon which we have acted, except agriculture.

We have not done too well, in either field. The Senator from Oklahoma is in favor of legislation that will provide a more favorable economic opportunity for both. He thinks the amendment would do that. While it is a general measure, its application would be limited. If I were to find fault with it, it would not be because it was too broad, but because it was too limited. The Senator from Oklahoma still thinks that the principal beneficiaries of it would be the consumers, those who pay street railway transportation costs in the Twin Cities of Minnesota. He feels that the Senate would be not only justified, but acting in a spirit of equity and justice, if it approved the amendment.

Mr. HUMPHREY. Mr. President, will the Senator yield?

Mr. KERR. I yield.

Mr. HUMPHREY. I wish to correct, if I can, an impression relating to the bill. Under present internal revenue law, had the company had responsible and prudent management, and had converted over a period of years—rather than in 18 months—it could have charged off its conversion losses against future years' profits.

Because of the fraudulent management, and because the management converted in 18 months instead of 5 or 6 or 7 years, as many transit companies have, it was impossible for the company to take advantage of the provisions of the Internal Revenue Code which provide for a deduction of this conversion loss from income.

This bill does not cost the Treasury one dime more than had the company been operating under normal prudent management. It does not add new costs. It merely places the company in the position it would have been in had it had prudent management and converted over a period of years.

I have studied the report of the House Ways and Means Committee on this measure of a year ago, as well as the report of our own Committee on Finance. Even if there had been no

fraudulent management, there would be the same problem relating to the conversion loss, because what really happened was a too rapid conversion to make the company eligible under the existing law. Therefore, we are merely asking that the law be modified so as to permit the company to take advantage of the provisions of the Internal Revenue Code, which provisions could have been and should have been applied under normal, prudent management back in the years 1953 and 1954 when the conversion losses were sustained.

This is no drain on the Treasury. As the Senator from Illinois has said, this is a regulated utility. I call to the attention of my colleagues in the Senate that under the constitution of the State of Minnesota, State statutes and judicial decisions, both State and Federal, it is mandatory that shareholder investments are entitled to a reasonable rate of return. Such reasonable rate of return is guaranteed, regardless of Federal income taxes incurred by the company in any amount. Shareholder's return is determined by law as administered by the Minnesota Railway and Warehouse Commission, and is not affected by the passage of this act.

I call attention to the fact that if this legislation is not provided, there is only one thing left for the company to do, and that is to raise its rates, which means that the bus rider, who is also a taxpayer, will pay more. This is the law. The State constitution itself provides that.

All we are asking for is what was indicated a moment ago in the discussion and colloquy. We are asking for an extension of time, as the President has suggested in his own mass transit message of this year; an extension of time for conversion loss privileges. That is all.

I remind Senators that before many months we will have mass transportation problems in city after city. We are trying to take care of one of these problems in our own community. It seems it is a matter of simple equity to support the amendment.

Mr. KERR. Mr. President, as I understand, if the bill is enacted, the loss that can be carried forward is less than \$2½ million. I would like to have the Senator from Minnesota correct me if I am not correct.

Mr. HUMPHREY. Yes; it is estimated that the losses the company could avail itself of based on projected future earnings is around \$2.5 million.

Mr. KERR. In other words, if it earned it under its present rates, it would have an opportunity to recover approximately \$2½ million in losses which it did not recover in the regular 5-year carry-forward period. Is that correct?

Mr. HUMPHREY. Yes; and had it converted gradually over a several-year period it could have recovered even more of its loss. In fact, it could have recovered the full \$5,200,000. Time is running out. If we lose this opportunity, to recover approximately \$2½ million, and wait another year, the recoverable loss will be lower. As my colleague, who is a member of the Committee on Finance has pointed out, when people ask,

why must this be done this year, the answer is that it must be done this year because if we wait another year, the recoverable loss will be even lower, perhaps a million or a million and a half dollars. We have already hurt the people who have made investments, and the people who ride the buses.

Mr. PASTORE. Mr. President, will the Senator yield?

Mr. DOUGLAS. Mr. President, who has the floor?

The PRESIDING OFFICER. The Senator from Oklahoma has the floor.

Mr. KERR. I yield to the Senator from Minnesota.

Mr. DOUGLAS. I thought the rules of the Senate provided that a Senator loses the floor when he sits down.

Mr. KERR. The Senator's point is well taken. The Senator from Oklahoma will remain on his feet.

I ask unanimous consent that I may yield so that the Senator from Rhode Island may ask a question of the Senator from Minnesota.

The PRESIDING OFFICER. Is there objection? The Chair hears none, and it is so ordered.

Mr. PASTORE. I understand that this concession applies to only one company, although it is general in terms.

Mr. HUMPHREY. That is correct.

Mr. PASTORE. I understand that this company has its affairs and charges and profits regulated by some State authority. Is that correct?

Mr. HUMPHREY. Yes; a State constitutional provision also applies, under which the shareholders are guaranteed a certain rate of return. If this conversion loss is not approved now, and the time is extended, the only answer is an increase in rates. We have already had an increase in rates.

Mr. KERR. Mr. President, I yield the floor.

Mr. DOUGLAS. Mr. President, this is a very important matter. It deserves to be discussed before a larger number of Senators than there is on the floor now. A hasty count indicates only 11 or 12 Senators on the floor. I am about to ask for a quorum. I do not intend to tie up the Senate on quorum calls, but I do think we should have a larger attendance. I therefore suggest the absence of a quorum.

The PRESIDING OFFICER. The clerk will call the roll.

The legislative clerk called the roll, and the following Senators answered to their names.

[No. 226 Leg.]

Aiken	Cooper	Holland
Allott	Cotton	Hruska
Bartlett	Curtis	Humphrey
Beall	Dirksen	Jackson
Bennett	Dodd	Javits
Boggs	Douglas	Johnston
Bottem	Eastland	Jordan, N.C.
Burdick	Ellender	Jordan, Idaho
Bush	Engle	Keating
Butler	Ervin	Kefauver
Byrd, Va.	Fong	Kerr
Byrd, W. Va.	Fulbright	Kuchel
Cannon	Goldwater	Lausche
Capehart	Gore	Long, Mo.
Carlson	Hart	Long, Hawaii
Carroll	Hartke	Long, La.
Case	Hayden	Magnuson
Chavez	Hickenlooper	Mansfield
Church	Hickey	McCarthy
Clark	Hill	McClellan

McGee
McNamara
Metcalf
Miller
Monroney
Morse
Morton
Moss
Mundt
Muskie
Neuberger

Pastore
Pearson
Pell
Prouty
Proxmire
Robertson
Russell
Saltonstall
Scott
Smathers
Smith, Mass.

Smith, Maine
Sparkman
Stennis
Talmadge
Thurmond
Tower
Williams, N.J.
Williams, Del.
Yarborough
Young, N. Dak.
Young, Ohio

Mr. HUMPHREY. I announce that the Senator from Nevada [Mr. BIBLE] is absent on official business.

I further announce that the Senator from New Mexico [Mr. ANDERSON], the Senator from Alaska [Mr. GRUENING], the Senator from Missouri [Mr. SYMINGTON], and the Senator from West Virginia [Mr. RANDOLPH] are necessarily absent.

Mr. KUCHEL. I announce that the Senator from New Hampshire [Mr. MURPHY] and the Senator from Wisconsin [Mr. WILEY] are necessarily absent.

The PRESIDING OFFICER. A quorum is present.

Mr. DOUGLAS. Mr. President, what is the pending question?

The PRESIDING OFFICER. The pending question is on agreeing to the committee amendment known as No. 8, beginning on page 388, in line 11.

Mr. DOUGLAS. Is it section 24 of the bill?

The PRESIDING OFFICER. Yes, section 24.

Mr. DOUGLAS. Is it the proposed legislation in regard to the Twin Cities Transit Co.?

The PRESIDING OFFICER. That is correct.

Mr. DOUGLAS. Mr. President, on the question of agreeing to this amendment, I ask for the yeas and nays.

The PRESIDING OFFICER. Is there a sufficient second?

The yeas and nays were ordered.

Mr. DOUGLAS. Mr. President, I am glad there is now a quorum present, or at least that a quorum answered to the rollcall.

I wonder whether we may have an explanation of this proposal. Are its sponsors on floor?

Mr. DIRKSEN. Mr. President, will the Senator from Illinois yield for a parliamentary inquiry?

Mr. DOUGLAS. I shall be glad to yield for a question.

Mr. DIRKSEN. I wish to direct a parliamentary inquiry to the Chair.

Mr. DOUGLAS. I yield for a parliamentary inquiry, with the understanding that I shall not thereby lose my right to the floor.

The PRESIDING OFFICER. Without objection, it is so ordered.

Mr. DIRKSEN. Mr. President, as I understand, the pending question, on which the yeas and nays have been ordered, is on agreeing to the committee amendment to make certain tax restitution to the street railway system of the Twin Cities of St. Paul and Minneapolis, as a result of the peccadillos or peculations of officers of that company, and because of the fact that in order for it to continue in operation, it would be necessary for it to have a sharp increase in its rates if this proposed tax relief were not afforded.

Mr. DOUGLAS. Mr. President, is that a proper parliamentary inquiry?

Mr. DIRKSEN. Well, Mr. President, it is not, as a matter of fact, as I understand.

Mr. DOUGLAS. Mr. President, is that a proper parliamentary inquiry?

The PRESIDING OFFICER. No, it is not.

Mr. DIRKSEN. It is a matter of general information.

Mr. DOUGLAS. Mr. President, is no sponsor of the amendment ready to rise to defend it?

Mr. DIRKSEN. Mr. President, I suggest the absence of a quorum.

The PRESIDING OFFICER. Does the Senator from Illinois yield for that purpose?

Mr. DOUGLAS. No, I do not yield for that purpose. I think the sponsors of the amendment should be allowed a decent period of time in which to come to the floor and explain the amendment.

Mr. KERR. Mr. President, a parliamentary inquiry: What is the pending question?

The PRESIDING OFFICER. The Senator from Illinois has the floor—

Mr. DOUGLAS. Mr. President, I had hoped that the sponsors of this amendment would—now that the yeas and nays have been ordered—explain the amendment. The previous discussion took place before a relatively small number of Senators.

Mr. KERR. Mr. President, if the Senator from Illinois is looking at me, I wish to say that I put an explanation of the amendment in the RECORD and in the report. The amendment has been explained on the floor of the Senate by the Senator from Oklahoma, by the Senator from Minnesota [Mr. McCARTHY], by the Senator from Minnesota [Mr. HUMPHREY], and by the Senator from Illinois [Mr. DOUGLAS]. Not only has the Senator from Illinois listened to a number of explanations of this amendment, but he has also made an explanation of the amendment, on the floor; and it is in the RECORD. If he cannot remember it any longer than this, then I see no reason why it should be explained again.

So far as I am concerned, I am willing to have the Senate vote.

Mr. DOUGLAS. Mr. President, who has the floor?

Mr. KERR. You do.

The PRESIDING OFFICER. The Senator from Illinois has the floor.

Mr. DOUGLAS. I thank both the Presiding Officer and the Senator from Oklahoma.

Mr. President, the previous explanation took place when only a few Senators were on the floor. I think at one time I counted six or seven. It was for that reason that I asked for a quorum call.

The Senator from Oklahoma has said there has already been sufficient explanation, because it is in the RECORD. But the RECORD will not be printed or read until tomorrow morning. So the Senator from Oklahoma is really suggesting that the Senate vote without an adequate oral presentation to the Senators now present.

I see a number of very important and very fine Senators on the floor—the great Senator from Texas [Mr. YARBOROUGH], the Senator from Georgia, the Senator from New Mexico, the Senator from South Carolina, the two Senators from Vermont, the Senator from Hawaii, the two Senators from Delaware, the Senator from South Dakota—who were not here when the original discussion took place. I therefore hope we can get an explanation. Then, I want to say, my comments will be brief, and we can proceed to a vote. But I do not think the Senate should be asked to proceed in the absence of an explanation.

Mr. President, I pause. I try to be fair to the proponents of the bill. I am ready to sit down.

Mr. KERR. Nobody is hindering the Senator.

Mr. DOUGLAS. I thank the Senator for his characteristic courtesy.

Mr. KERR. Does the Senator yield the floor?

Mr. DOUGLAS. Mr. President, I am ready to yield the floor, if the proponents of the amendment will take the floor and explain it and defend it.

The PRESIDING OFFICER. The question is on the amendment.

Mr. KERR. Mr. President, as I said a while ago, the proposal has been explained in committee and on the floor, this year and last year. The Senator from Minnesota [Mr. McCARTHY], author of the amendment, is present, and the Senator from Minnesota [Mr. HUMPHREY] is familiar with it. If Senators want to ask them any questions, I am sure they will be glad to answer them. I am sure the Senator from Illinois will want Senators to speak for themselves as to what information they want on the amendment.

The PRESIDING OFFICER. The question is on agreeing to the amendment—

Mr. DOUGLAS. Mr. President, are we to put the question without any real explanation of the amendment?

Mr. HUMPHREY. Mr. President, will the Senator yield?

Mr. DOUGLAS. I yield.

Mr. HUMPHREY. I want to do the best I can to accommodate the Senator, but I am not the expert in this field. I see present my distinguished colleague [Mr. McCARTHY], who is on the Finance Committee. We have attempted three or four times to explain the measure. Some Senators were not present at that time.

The simple explanation is that the present Internal Revenue Code provides that any transit company may convert from a street railway to buses over a period of years and losses thereby sustained are deductible against income. Other transit companies, when changing from streetcars to buses, took full advantage of the loss carryover provision in the law by converting over a period of many years. The company sustained a conversion loss of \$10.2 million. Due to a combination of fraudulent and poor management, the company did not take advantage of its full conversion offsets under the tax code. It took advantage

only of approximately \$5 million of such conversion loss.

Under present law, the carry forward time has expired. The pending amendment seeks to extend the time so that the company may take advantage of the remaining conversion losses under the Internal Revenue Code.

Mr. PASTORE. Mr. President, will the Senator yield?

Mr. HUMPHREY. I yield.

Mr. PASTORE. In other words, this is something to which the company would have been entitled if the officers of the company had not been corrupt and if they had not been in jail?

Mr. HUMPHREY. The Senator is correct. I want to make crystal clear that this is a stock company regulated under the laws of the State of Minnesota. The constitution of the State provides that shareholders are entitled to a reasonable return on stock. Therefore, if this type of remedial legislation is not passed, there is only one way in which the shareholders can receive what the State constitution provides; namely, a fair return, and that is by an increase in rates. This amendment does not provide for a single thing the company was not entitled to had there been a gradual conversion. It provides only that this particular company, which converted in 18 months, under, regrettably, most unfortunate and corrupt management, but which is now reorganized and has a new management, and which represents some of the finest citizenry of our State, will be permitted to take advantage of the tax loss to which it was entitled.

Mr. RUSSELL. Mr. President, will the Senator yield?

Mr. HUMPHREY. I yield.

Mr. RUSSELL. How many of the old managers were involved in the speculations?

Mr. HUMPHREY. I could not tell the Senator, but the manager of the company was indicted in the district court and sentenced. Others were involved and sentenced to the penitentiary.

Mr. RUSSELL. Will the Senator inform us as to the length of time?

Mr. HUMPHREY. Several years. I do not want to make it appear that those who defrauded the company ran away with the money involved in this situation.

Mr. RUSSELL. Was any restitution made?

Mr. HUMPHREY. Some restitution was made, yes.

This company is not particularly a profitmaking company, as is true of most transit companies. What we are trying to do is to provide an opportunity, in case this company does make enough money, to use its conversion losses as deductible items against income. It will be very fortunate if the company is able to claim \$2 million out of the \$5 million, because most transit companies are barely getting by today.

Not only was this measure thoroughly considered by the Ways and Means Committee of the House and the Finance Committee of the Senate, but the Treasury Department has not raised any objection to this particular proposal.

Equity is involved here. Of course, these are unusual circumstances, there is no doubt about it, and the unusual circumstances are so unusual that the case went to the district court, and jail sentences were fixed for those who managed the company.

Mr. RUSSELL. Does the Senator remember the amount lost as a result of the speculations, and the amount recovered?

Mr. HUMPHREY. No, I do not. Had there not been fraudulent conduct, had the management been honest, the fact of the matter is that by accomplishing conversion in an 18-month period the company could not possibly have taken advantage of the provisions of the Internal Revenue Code, which provide for 3 years back and 5 years forward. It was bad management. It was fraudulent management. The company would have been entitled to a \$10,200,000 conversion loss. We are seeking to extend the carryover provisions of the Internal Revenue Code for a few more years within the spirit of the terms of the President's transportation message so that if the company makes money—I repeat, if the company makes money—it can charge off some of these conversion losses which the Internal Revenue Service has said it can certify against the profit. There is no guarantee that it will be able to do it. It may not make money. It may break even, or lose money, and it may not be able to take advantage of the legislation at all.

This is no windfall. It permits the company, now that it has been reorganized—and it is a public utility regulated by the Railroad and Warehouse Commission of Minnesota—to be able to charge a conversion loss against its profit, as any other company has the right.

Mr. PROXMIRE. Mr. President, will the Senator yield?

Mr. HUMPHREY. I yield.

Mr. PROXMIRE. If this bill passes, will this provision apply to any other company in the country besides the Twin Cities Rapid Transit Co.?

Mr. HUMPHREY. Yes; under similar circumstances it will.

Mr. PROXMIRE. The similar circumstances would mean that the corporation would have had to suffer a net loss between December 31, 1953, and December 31, 1954. If it had it in the following year or the previous year, it would not apply?

Mr. HUMPHREY. That is correct. That is not unusual.

Mr. PROXMIRE. It seems unusual to this Senator that it would have to apply to that particular year, and not to the year before or the year after; it would have had to occur in the same year that it happened to the Twin Cities Rapid Transit Co., and would apply only under those circumstances.

Mr. HUMPHREY. That is correct.

Mr. PROXMIRE. Now I ask the Senator if we would not be establishing the precedent that, if at any time in the future, because of bad management or fraudulent management, a utility should lose money, or should be in a position similar to the one in which this com-

pany is, it would be appropriate to come to the Congress and to have a rider put on a general tax bill for the relief of that company, in the form of an additional carryforward provision? That is what is to be done under these circumstances, rather than to introduce the proposal as a bill, because, if introduced as a bill, the President would veto the bill. Is it the position of the Senator from Minnesota that it should be put and can be put on a general tax bill as a rider, so that the President cannot veto it? Is that correct?

Mr. HUMPHREY. I know my colleague wants me to be very frank with him.

Mr. PROXMIRE. Yes.

Mr. HUMPHREY. The truth is that it might be better if we could do this by regular special legislation.

I will say to the Senator, however, that each year we let this problem go by, this particular company and this particular public service loses an opportunity to regain its so-called conversion losses.

In addition, there is the fact that we know we are coming to the end of this session, and we shall have very little opportunity to pass any legislation such as this.

This is not an unusual proposal. I have in my hand a whole series of remedial tax precedents which have been used for railroads, street railways, steamship lines, banks, and insurance companies. This has happened repeatedly.

Mr. PROXMIRE. Not under circumstances of this kind.

Mr. HUMPHREY. Each time there is a separate set of circumstances. Each time remedial legislation is passed it relates to a special set of circumstances.

Mr. PROXMIRE. This is a situation in which the owners now are the same owners, roughly, the street railway had in 1953 and 1954, when the difficulties developed. Is not that correct?

Mr. HUMPHREY. In part, but not completely.

Mr. PROXMIRE. Generally, they are the same owners.

Mr. HUMPHREY. The stock is on the New York Stock Exchange.

Mr. PROXMIRE. Do not the owners of a company, basically and as a matter of principle, have the responsibility for the management of the company? They own the stock. They can vote one management out and vote another management in.

Mr. HUMPHREY. And they did.

Mr. PROXMIRE. Yes, indeed. The Senator is saying that when this happens the Government should step in and provide a "bail-out" operation.

Mr. HUMPHREY. What the Senator from Minnesota is saying is that the management of the company was entitled, according to the Internal Revenue Code, to a \$10.2 million conversion loss.

The management of the company was very poor management, working supposedly in the name of the stockholders, and was a fraudulent management, and converted in only 18 months instead of over a period of several years as prudent management would, and thus could take

advantage of only slightly more of \$5 million of the \$10.2 million conversion losses.

That management was fired. That management was prosecuted. That management was imprisoned.

All my colleague, the junior Senator from Minnesota [Mr. McCARTHY] did, by offering his proposal, was to say that since the company was entitled, according to the Internal Revenue Code, to \$10.2 million of conversion losses had there been proper management we should amend the law to permit an additional period of time for the company to qualify, if it can.

I am before the Senate saying the company cannot qualify for more than a fraction of that amount. They will be lucky to qualify for \$2 million.

Mr. PROXMIRE. Why not generalize?

Mr. HUMPHREY. So the Treasury Department has gained a windfall of \$3 million. We have helped the other States.

Mr. DOUGLAS. Mr. President, will the Senator yield?

Mr. PROXMIRE. If the Senator will yield for one more question before the Senator from Illinois interrogates him, why not generalize the provision to apply to all circumstances and to all utilities, in the event of such a loss, instead of limiting it to 1 year and in effect to Twin Cities Rapid Transit.

Mr. HUMPHREY. If the Senator will permit me, why does the Senator not offer such an amendment?

Mr. PROXMIRE. I think it would be unconscionable. I think it would be very bad. I think this is a bad proposal.

What we are asked to say, in effect, is, "if you have bad management and if because of this management the company loses money, then, if you have powerful friends in the U.S. Senate on the Finance Committee"

Mr. HUMPHREY. May I say to the Senator—

Mr. PROXMIRE. Surely this is the case. The Senator knows this is the case.

Mr. HUMPHREY. I say to the Senator—

Mr. PROXMIRE. It is obvious. The Senator from Wisconsin does not have this power. I am sure that I could not possibly persuade the "powers that be" on the Finance Committee to do this. I would not have a chance.

Mr. HUMPHREY. The Senator from Wisconsin has as much power as any Senator in this body. Some people think that he has more power than other Senators in this body.

Mr. PROXMIRE. I am sure that is not true. If a person happens to come from a State which has powerful Senators of this kind, he can then seek to tie riders onto bills, even if the President of the United States says that it is wrong and vetoes it, and says that it should not be done. It would still become law. I say that would be a bad precedent. I think it would be very bad public policy, unless generalized and applied to all equally, and then the proposal would not get enough votes to put in the Senator's hat, if we should generalize

this kind of provision, and the Senator knows it.

Mr. HUMPHREY. I say to the Senator that one of the duties of any public body—legislative, judicial, or executive—is to give equity. That is the first duty of government.

Mr. PROXMIRE. I agree. That is why I am opposing this amendment.

Mr. HUMPHREY. What we are attempting to do, stated simply, is to provide in the law an opportunity for the stockowners and for the bus riders to be treated equitably. They were defrauded. They were victims of poor management. They were victims of fraudulent management.

The Congress of the United States has written into the law that railway and street railway systems in converting into bus systems may apply losses thereby incurred against past and future earnings.

This company, because of its then corrupt management, could not take full advantage of this law. Who was hurt? The stockholders were hurt. Who else was hurt? The bus riders were hurt.

Make no mistake about it, the shareholders of this company, under the Constitution of the State and the statutes of the State, as well as the judicial decisions pertaining thereto, are entitled to a reasonable return on their investment. If they do not get that reasonable return under the present rates, and if they do not get some relief under tax laws passed for their benefit, the rates will go up.

It is that simple. That is all there is to it. I am not one who ordinarily rides the buses. I do not own a share of stock.

Mr. PROXMIRE. I have never said that. Nobody has challenged the integrity of the Senator from Minnesota.

Mr. HUMPHREY. I understand that. I fully understand that these matters ought to be debated.

The Senator from Illinois said that we ought to have an explanation. I agree with the Senator. This ought to be debated. This is not an easy matter to present, but thousands of people are involved. A community was victimized. Hundreds and thousands of stockholders were victimized. Thousands of bus riders can be victimized, and the Congress of the United States can give them equity.

That is all we are seeking to do. We simply say, "Help us out." We do not ask help for the Senators from Minnesota, but we ask help in regard to a set of circumstances which was unique and different.

If the Senator from Wisconsin presents such a set of circumstances pertaining to the welfare of the people whom he represents, I shall be the first to back him up, and that goes for any other Senator.

Mr. PROXMIRE. Let the bill stand on its own feet, rather than be proposed as a rider.

Mr. HUMPHREY. The bill before the Senate is a tax bill.

Mr. PROXMIRE. Under the present proposal, the constitutional process cannot work itself out.

Mr. HUMPHREY. The bill is a tax bill.

Mr. PROXMIRE. The President vetoed it once.

Mr. AIKEN. Mr. President, may I ask the Senator from Minnesota a question?

Mr. HUMPHREY. I yield.

Mr. AIKEN. When did this infamous skullduggery take place?

Mr. HUMPHREY. The court decision was a recent one. I am not familiar with all the details.

Mr. AIKEN. Has a bill been introduced?

Mr. HUMPHREY. Yes. An identical bill passed Congress last year.

Mr. AIKEN. It passed the House last year?

Mr. HUMPHREY. Yes. It was reported unanimously by the House Ways and Means Committee, after hearings and a report.

Mr. DOUGLAS. If the Senator will pardon me, will the Senator correct that statement? It is my understanding that there were no hearings in the House. The bill was passed after an executive session by the House Ways and Means Committee.

Mr. HUMPHREY. I am sorry.

Mr. DOUGLAS. It was passed after an executive session by the Senate Finance Committee.

Mr. McCARTHY. There was a report.

Mr. HUMPHREY. There was a published report.

Mr. DOUGLAS. But not hearings.

Mr. HUMPHREY. There were no public hearings, but the Treasury Department officials were called in. There was a discussion, and there was testimony taken in executive session. The Senator is correct.

(At this point Mr. YARBOROUGH assumed the chair as Presiding Officer.)

Mr. DOUGLAS. Mr. President, now that the Senator from Minnesota has taken his seat, I wish to say that this matter can be considered in two forms: First, from the standpoint of procedure; and, second, from the standpoint of substance.

So far as the procedure is concerned, the bill, as has been shown by the questioning, was passed by the House without debate last year and without prior hearings by the House Ways and Means Committee. The bill came to the Senate in the concluding days of the session last year. I well remember the pressure under which we were operating in those last hectic days.

The proposal was reported without public hearings as a separate bill by the Senate Finance Committee 5 days before the Congress adjourned. It was passed I believe in those midnight hours when we were trying to get legislation through and when legislation would pass with the speed of light, it being very difficult to trace each individual measure which was being considered.

The bill then went to the President of the United States, and he vetoed it on the 4th of October.

It was quite a detailed veto. He said that the measure was designed "for the relief of one taxpayer, the Twin City Rapid Transit Co., of Minneapolis, Minn." He explained:

The losses were incurred in 1953 and 1954, when the company was managed by officers

who were subsequently found guilty of conspiracy to defraud the company. The position of the company is, in essence, that the management converted rapidly from a street railway to a bus system in order to complete its fraudulent activities quickly, intentionally disregarding the income tax consequences.

In other words, the speed of the conversion was a part of the whole fraudulent process, not separate from the fraudulent process.

The President went on to say:

I can see no reason for making an exception to the policy of uniform treatment under the net operating loss carryover provisions of the taxing statutes under these circumstances.

The President then went on to give his reasons:

First, the extent to which tax considerations governed or would have governed the conversion from street railway to bus operations is necessarily uncertain.

The following is extremely important:

Secondly, assuming that the fraudulent conduct of the management of the company made it impossible to deduct all the losses sustained, it would be unfair to shift the consequences of that dereliction to the public through special tax relief.

Mr. President, I emphasize what the Senator from Minnesota, with his characteristic honesty, has said. They are substantially the same now as they were then.

Continuing to read from the President's veto message:

The stockholders of the company were certainly in a better position than the general public to guard against the misconduct of their officials. Thirdly, approval of this legislation is inconsistent with orderly tax administration. It discriminates in the treatment of taxpayers similarly situated and grants relief retroactively.

In the final paragraph the President said:

Although disapproval of this legislation may reduce the ability of the company to postpone or avoid a request for increases in its rates of fare, that fact should not be used to modify the tax system to shift the burden of losses from the taxpayer and the local community to the country as a whole.

The veto message is signed by John F. Kennedy.

The junior Senator from Minnesota, who followed the reading of the veto message, has stated that the reading is accurate and correct.

We find the same bill reemerging as section 24 of the general tax bill. I think it can be described as a rider to the bill. It is special legislation in the very thin disguise of general legislation.

If it were a separate bill, the President would have an opportunity to consider it again. The Senators from Minnesota have said that the administration has changed its position during this time, as evidenced by the President's message on mass transportation and his public sponsorship of the Du Pont bill, which the Senator from Illinois, the Senator from Tennessee, and others opposed, and which at least the junior Senator from Minnesota favored.

I do not know whether the President has changed his mind or not, but at least

he should be given an opportunity to pass upon the proposed legislation in a separate bill. If he has changed his mind, and if the Congress wishes to pass the measure and put it up to the President, that is all right with me, although on the basis of my present knowledge I shall vote against such a bill. But I submit that it should be submitted, if it is submitted at all, as a separate bill, and not as part of a general tax measure which the President could not reach. Section 24 would be immunized from a veto. I should like to see the proposal stand on its own merits.

Passing from the procedural features to the substantive features of the measure, I have listened to the argument. It seems to me the bill aims to give to shareholders a guaranteed return, even if the officers run off with the money.

It would make the general taxpayers responsible for the dereliction and fraud of the officers of the company. The Senator from Minnesota used the illustration of a bank president's embezzlement. I suggest that such a loss is made good through a guarantee of the bank deposits. Even in that case, there is no true analogy, because the assessment is upon banks as a whole, and not upon the general taxpayers. This proposal would be an assessment upon the general taxpayers. If the Senator from Minnesota wishes to propose the establishment of a separate fund to protect the officers of companies from the fraud and theft of officials, he can do so. I will not vote for such a measure. I doubt whether the Senator from Minnesota would ever propose it. But if he wishes to do so he can.

But what he is saying is that in cases in which officers have looted a company—and the testimony in the criminal trial indicated that the officers were closely connected with the so-called criminal syndicate—the stockholders should be bailed out.

Mr. PROXMIRE. Mr. President, will the Senator yield on that point?

Mr. DOUGLAS. I am glad to yield.

Mr. PROXMIRE. I understand that the Senator has pointed out that the FDIC analogy is invalid because the FDIC benefit is based upon charges against the benefiting bank's premiums which it pays for its own insurance.

Mr. DOUGLAS. That is correct.

Mr. PROXMIRE. The loss is not an imposition on the public.

Mr. DOUGLAS. The Senator is correct.

Mr. PROXMIRE. To argue that a bank failure is taken care of in that way provides no analogy. There is no comparison between that kind of situation and one in which there is fraud on the part of management.

Mr. DOUGLAS. There is no logical analogy.

Mr. PROXMIRE. There is no logical analogy.

Mr. DOUGLAS. Mr. President, that is the situation. The subject is not a pleasant one for me to discuss. The two Senators from Minnesota have been my long-time personal friends. I campaigned for both of them. I hope that my personal friendship will continue after today. It is not pleasant to rise

on the floor of the Senate and make objections, and subject oneself to the barbs of the powerful Senator from Oklahoma [Mr. KERR]. That is not a pleasant experience. But this is a subject of general importance; and although I am sure the Senators from Minnesota have the worthiest of motives and are merely trying to help an important corporation in their cities, the proposal is really against the public interest. So I very much hope that the provision will be stricken out.

Mr. HUMPHREY. Mr. President, will the Senator yield?

Mr. DOUGLAS. I yield.

Mr. HUMPHREY. The management of that company, by poor management—aside from their fraudulent activities, gave the Treasury of the United States a windfall of more than \$5 million, because had the management taken advantage of existing law, there would have been an additional \$5 million of conversion losses that could have been applied against the future earnings of the company if the company had earned that much money. All we are saying is that perhaps the Treasury ought not to have that windfall.

Secondly, we are saying that since the President, in his proposed new transit legislation, has recommended a 7-year carryover on losses for conversion purposes in connection with mass transit, we should extend the opportunity of this company. We are further saying that not a single dollar would be lost to the Treasury under the proposal that would not have been lost to the Treasury under the present Internal Revenue laws had the management of that company acted in a prudent manner. That is all. That is the simple case.

Mr. DOUGLAS. Mr. President, I wish to reply briefly to my good friend. I hope he is my good friend.

Mr. HUMPHREY. I assure my friend from Illinois that in moments like these, when we stand up and voice some honest disagreement, I love him even more.

There is no Senator who is closer to my heart and affection than the Senator from Illinois.

Mr. DOUGLAS. That is mutual and reciprocal. If all the things the Senator from Minnesota has said are true, I should like to ask why did the President veto the bill last year? The President does not operate in a void. He gets advice not only from the White House staff but also from the Treasury. I would presume that he did it with the advice of the Treasury. If there has been a change of heart on this matter, let the President have a chance to pass upon it in the form of a separate bill.

Mr. MCCARTHY. Mr. President, will the Senator yield?

Mr. DOUGLAS. I yield.

Mr. MCCARTHY. The Senator knows that the President vetoed the bill on October 4, after Congress had adjourned. I would therefore suggest that after the Congress adjourns the President operates in a partial vacuum.

Mr. DOUGLAS. The Senator knows that the bill was passed in the last hectic moments before we adjourned, when parliamentary dignity tends to be

thrown aside, and in the rush to get out all kinds of things go through. The Senator from Illinois for some years, acting in his role of gadfly, which has not made him popular, used to object to these last minute tax bills. I can remember doing that. However, one gets worn out by the strain, particularly when one is subject to the mighty verbal bludgeonings of the Senator from Oklahoma, who then says I pretend to be the only man of conscience in the Senate, which of course is not true.

Mr. AIKEN. Mr. President, will the Senator yield?

Mr. DOUGLAS. I yield.

Mr. AIKEN. I was intrigued by the statement of the senior Senator from Minnesota, when he said that as a result of this embezzlement by the management the Federal Treasury received \$5 million which it otherwise would not have received. My question is, how many embezzlements would it take throughout the 50 States of the Union in order to balance the budget?

Mr. DOUGLAS. That is very amusing, and I believe it shows up the faultiness of the claim. I am willing to yield the floor, and I suggest that we proceed to vote. First, may I make a parliamentary inquiry?

The PRESIDING OFFICER. The Senator will state it.

Mr. DOUGLAS. What will a "yea" vote on this measure be?

The PRESIDING OFFICER. A "yea" vote will be to sustain the committee amendment and keep the section in the bill.

Mr. DOUGLAS. And a "nay" vote will be to strike the section from the bill.

The PRESIDING OFFICER. A "nay" vote will strike that section from the bill.

Mr. GORE. Mr. President, a parliamentary inquiry.

The PRESIDING OFFICER. The Senator will state it.

Mr. GORE. Would not a "yea" vote, instead of being a vote to sustain the amendment, be one for the adoption of the amendment?

The PRESIDING OFFICER. It would be to sustain the position of the committee and be for the adoption of the amendment.

Mr. GORE. I thank the Chair.

Mr. DOUGLAS. I do not know whether that ruling is correct but at least it lays down the ground rules. A "yea" vote is a vote for the amendment and for the section, and a "nay" vote is a vote against the section. Is that correct?

The PRESIDING OFFICER. That is correct. The yeas and nays have been ordered, and the clerk will call the roll.

Mr. WILLIAMS of Delaware. Mr. President, our committee gave careful consideration to this proposition. As one member of the committee, I believe it has merit and I believe the amendment should be adopted.

I realize that we are dealing with a particular situation, but I do not know how else we can approach it. I and a majority of the committee believe there is merit to it and that the amendment should be approved. I say that as one who has not had the good fortune of visiting the great city of Minneapolis.

I do not know any of the stockholders; nor do I know any of the company officials. I merely say that the amendment has been approved by the committee on the basis of its merits, and I believe the Senate should consider it on the same basis.

The PRESIDING OFFICER. The question is on agreeing to the committee amendment. The yeas and nays have been ordered, and the clerk will call the roll.

The Chief Clerk called the roll.

Mr. HUMPHREY. I announce that the Senator from Nevada [Mr. BIBLE] and the Senator from Arizona [Mr. HAYDEN] are absent on official business.

I further announce that the Senator from New Mexico [Mr. ANDERSON], the Senator from Alaska [Mr. GRUENING], the Senator from Missouri [Mr. SYMINGTON], and the Senator from West Virginia [Mr. RANDOLPH] are necessarily absent.

I further announce that, if present and voting, the Senator from Missouri [Mr. SYMINGTON], the Senator from Nevada [Mr. BIBLE], the Senator from Arizona [Mr. HAYDEN], and the Senator from New Mexico [Mr. ANDERSON] would each vote "yea."

On this vote, the Senator from West Virginia [Mr. RANDOLPH] is paired with the Senator from Alaska [Mr. GRUENING]. If present and voting, the Senator from West Virginia would vote "yea," and the Senator from Alaska would vote "nay."

Mr. KUCHEL. I announce that the Senator from New Hampshire [Mr. MURPHY], the Senator from Massachusetts [Mr. SALTONSTALL], and the Senator from Wisconsin [Mr. WILEY] are necessarily absent.

If present and voting, the Senator from New Hampshire [Mr. MURPHY] and the Senator from Massachusetts [Mr. SALTONSTALL] would each vote "yea."

The result was announced—yeas 74, nays 17, as follows:

[No. 227 Leg.]

YEAS—74

Aiken	Fulbright	McNamara
Allott	Goldwater	Metcalf
Bartlett	Hart	Monroney
Beall	Hartke	Morton
Bennett	Hickenlooper	Moss
Boggs	Hickey	Mundt
Bottum	Hill	Muskie
Bush	Holland	Neuberger
Butler	Hruska	Pastore
Byrd, Va.	Humphrey	Pearson
Byrd, W. Va.	Jackson	Pell
Cannon	Javits	Robertson
Capehart	Johnston	Scott
Carlson	Jordan, N.C.	Smathers
Carroll	Jordan, Idaho	Smith, Mass.
Case	Keating	Smith, Maine
Church	Kerr	Sparkman
Clark	Kuchel	Stennis
Cooper	Long, Mo.	Talmadge
Cotton	Long, Hawaii	Thurmond
Curtis	Long, La.	Tower
Dirksen	Mansfield	Williams, N.J.
Eastland	McCarthy	Williams, Del.
Ellender	McClellan	Young, N. Dak.
Fong	McGee	

NAYS—17

Burdick	Gore	Prouty
Chavez	Kefauver	Proxmire
Dodd	Lausche	Russell
Douglas	Magnuson	Yarborough
Engle	Miller	Young, Ohio
Ervin	Morse	

NOT VOTING—9

Anderson	Hayden	Saltonstall
Bible	Murphy	Symington
Gruening	Randolph	Wiley

So the committee amendment on page 388, after line 10, was agreed to, as follows:

On page 388, after line 10, to insert a new section, as follows:

"SEC. 24. CERTAIN LOSSES SUSTAINED IN CONVERTING FROM STREET RAILWAY TO BUS OPERATIONS.

"(a) IN GENERAL.—If a corporation has a net operating loss for the taxable year ending December 31, 1953, or the taxable year ending December 31, 1954, principally as the result of conversion from street railways to bus operations with respect to part or all of the company's operations, then its unused conversion loss will be subject to the treatment provided in subsection (c).

"(b) UNUSED CONVERSION LOSS DEFINED.—The amount of the unused conversion loss shall be the aggregate of the net operating losses for years described in subsection (a) reduced to the extent that they have been used as net operating loss carryovers or carrybacks to reduce taxable income for any taxable year beginning before January 1, 1960.

"(c) TREATMENT OF UNUSED CONVERSION LOSS.—If a taxpayer has an unused conversion loss, then in determining the amount of the operating loss carryover from the taxable year ending December 31, 1959, to each of the 5 taxable years following such taxable year for purposes of section 172 of the Internal Revenue Code of 1954, such unused conversion loss shall be treated as a net operating loss for the taxable year ending December 31, 1959. This subsection shall apply only for years in which the taxpayer is engaged in the furnishing or sale of transportation (as defined in section 1503(c)(1) (A) of the Internal Revenue Code of 1954).

"(d) REGULATIONS.—The Secretary of the Treasury, or his delegate, may prescribe by regulation such rules as may be necessary to carry out the purposes of this section."

Mr. HUMPHREY. Mr. President, I move that the vote by which the amendment was agreed to be reconsidered.

Mr. SMATHERS. Mr. President, I move that the motion to reconsider be laid on the table.

The PRESIDING OFFICER (Mr. HICKEY in the chair). The question is on agreeing to the motion to lay on the table the motion to reconsider.

The motion to lay on the table was agreed to.

Mr. SMATHERS. Mr. President, under the agreement, I move that the Senate proceed to the consideration of committee amendment numbered two, the second amendment.

The PRESIDING OFFICER. The amendment will be stated.

The LEGISLATIVE CLERK. It is proposed to strike out all of section 6, beginning on page 52, in line 1, and ending on page 57, in line 22.

The PRESIDING OFFICER (Mr. METCALF in the chair). The question is on agreeing to the committee amendment.

AN INSTALLMENT AND A PROMISE ON TAXES

Mr. JAVITS. Mr. President, I shall not detain the Senate very long; but I feel it my duty, in terms of my representation of my State and also in terms of my duty to the country, to set forth

for the Senate the situation now existing as it relates to the question of an incentive tax cut or what the President calls a creative tax cut.

Obviously this will be the last tax bill before this Congress; and obviously, also, neither the President nor any appreciable number of Senators will seek this kind of tax cut. So at least we should understand what we are doing and why we are doing it.

I also use this occasion to urge the President to lay before us his creative tax cut, at least in principle, before the session ends, so that the people may know what to count on, in terms of creative tax reform.

I think the mere fact of informing the people of the principles on which the President intends to proceed, when added to what we are doing in this bill, especially as the bill relates to the investment credit amendment now included in the bill, will constitute a most helpful package and, in my opinion, will help to avoid the development of a situation which might deteriorate into a recession.

The Senate this Tuesday put down the second installment on a tax program to get our economy moving again, by voting to retain the investment credit provision of the Revenue Act of 1962. The first installment came from the Treasury Department at the beginning of July, when the revised depreciation schedules for business were finally released. And a promise for the future was made by the President on August 13, when he pledged to present a "creative" tax program to the Congress in 1963.

On the other hand, the President has permitted intra-Democratic dissension to cancel the possibility of an incentive tax cut this year—in spite of the dangers of such inaction.

This summarizes the precarious stand of the Kennedy administration as the unpredictable winds of economic change buffet the Nation. There are still nearly 1 million who have been unemployed for more than 15 weeks, and more than one-half a million who have been out of work for more than 6 months. In addition, 2.7 million are able to take only part-time jobs, because of lack of work. On the other hand, latest reports show that 10 out of 17 of the so-called leading economic indicators pointed upward last month. This was the first time since February—one-half a year—that more of these indicators were up than down. But not all of the 30 which are generally considered are yet available; and even if the rest do follow in the same proportion, we are almost becalmed on the sea which the President would have us sail. Our ship is not trimmed, and its sails are not ready to meet the next strong gust of wind—whatever quarter it may come from.

I believe that we must trim the ship now, lest we be roused suddenly during the next months by a Presidential alarm—a call for a special session of the Congress to act in haste on matters we should be considering now.

I shall not follow the battle cry on economics of this administration, which seemingly goes: "Act on impulse—the country can afford it."

I propose that the following be done: Before this Congress adjourns, the President should submit, at least in broad outline, his "creative" tax program to be enacted in 1963.

Such an act of good faith by the administration could help to restore the economic confidence of many people who find it hard to live on a presentation of a mediocre past economic performance, no matter how brightly dressed up by the President. A promise is not enough. The Nation deserves to know, at least in principle, what it can expect in terms of government action on taxes.

It should be made very clear that there is no hidden-ball trick about tax reform. This is not a game. Let the President give the people the facts on what he and his party plan to do, so that we can weigh his proposals and can decide on their implementation.

Furthermore, the "creative" tax program of which the President spoke cannot be based on short-term economic considerations. This must be the program of the decade; and it is fatuous to argue that plans presented now may have to be changed in the light of economic conditions in January of 1963.

Those who believe that the President is planning to present next year a program of short-term expediency and political compromise on taxes to the Nation do justice neither to the needs of the United States nor to the good faith of our administration.

I have repeatedly advocated an incentive tax program to meet the short-term economic needs. I believe that the President's deferral of an incentive tax cut has subjected our economy to unnecessary risks. There was no need for the ship of state to remain becalmed until next year or to be exposed to heavy damage. We could have gone into next year trim and ready for the basic reforms of our tax system.

The incentive tax program which I put forward would have cost about \$5.5 billion annually in revenue—including the \$1 billion estimated cost of the investment credit provision on which the Senate acted favorably this week. If one adds to this the estimated \$1.5 billion cost of the equipment depreciation schedules announced in July, the total program would represent a \$7 billion incentive. The rough outline of this program would call for:

First. Virtual elimination of income taxes for those earning less than \$2,000 a year.

Second. Reduction of the tax burden of other lower income and middle income groups, with emphasis on those earning less than \$6,000 a year.

Third. Reduction of the maximum tax on top personal income brackets from the present 91 percent to 65 percent.

Fourth. Reduction of the corporate income tax from the present 52 percent to 50 percent.

The first three points, all relating to personal income, would cost an estimated \$3,695 million in annual income. In the

specific legislative form, of which I have prepared a preliminary draft, this incentive cut of personal income would be accomplished through increasing the personal exemption from \$600 to \$650, reducing the tax on the first \$2,000 of taxable income from 20 percent to 18 percent, recouping a part of this loss on taxable income between \$2,000 and \$6,000, and eliminating all tax rates above 65 percent. No person's tax would be increased. Even the higher middle-income brackets would derive some benefits; for example, a married man with two children, earning \$14,000, with \$1,400 in deductions, and filing a joint return, would pay \$62 less in taxes than at present; and a married man, with no children, and earning \$7,000 a year with \$700 in deductions, and filing a joint return, would save \$87 in taxes.

The reduction in the corporate income tax from 52 percent to 50 percent would cost an estimated \$1 billion in revenues. By placing a statutory base under the \$1.5 billion new depreciation schedules—which would cost nothing, but would result in further strengthening of business confidence—and by adding the \$1 billion investment credit, an incentive tax cut of \$3.5 billion for business would be established.

Thus, in round figures, we would have a \$7 billion incentive program, equally shared by business and individuals.

If the President's decision already announced would not make it a futile gesture, I would offer this proposal now as an amendment to the Revenue Act of 1962. It is ready. Distinguished individuals and major organizations, such as the chamber of commerce and the AFL-CIO, have spoken of the need for an immediate tax cut. I do not claim that all of them favor going about it in the same way; but the considered opinion that there is a need for action is very clear.

It is most important to understand that in the hearings before the Joint Economic Committee, of which I am a member, a number of the most distinguished economists in the country, of all shades of opinion and position—liberal, conservative, academic, and business—urged that a tax cut would be extremely advantageous in order to enable the country to move forward in the way President Kennedy has been talking about. So I should like to cite the statements of nine economists who appeared at the recently concluded hearings on the state of the economy held by the Joint Economic Committee:

J. Fred Weston, professor of business economics at the University of California, Los Angeles, testified on August 7:

The repetition of an abortive business recovery calls for immediate action to alter the impact of the fiscal choke on the economy.

Professor Weston asked for personal and corporate tax cuts.

Otto Eckstein, associate professor of economics, Harvard University, testified on August 9:

A tax cut would not be a mistake even if the optimists were correct and things turned out just as well as one could reasonably hope

for. * * * The prudent action, therefore, is a tax cut.

Joseph A. Pechman, director of economic studies, Brookings Institute, testified on August 9:

Under the circumstances, tax reduction would be the best and most effective method of providing a strong and immediate stimulus to the economy.

Leon Keyserling, former chairman of the President's Council of Economic Advisors, testified on August 9:

Dawdling or delaying with respect to tax reduction has no justification in the face of the chronic economic ailment which is now being confirmed rather than alleviated.

Stanley H. Ruttenberg, director of research department, AFL-CIO, testified on August 13:

The economic situation is today sufficiently serious * * * to justify an immediate emergency short run tax cut.

Alan C. L. Day, professor of economics, London School of Economics, testified on August 13:

Deliberate policies designed to encourage an expansion of demand are justified now * * * the choice should be for tax cuts.

J. M. Culbertson, professor of economics and commerce, University of Wisconsin, testified on August 14:

I believe that a moderate tax reduction this year would be a wise policy.

Marriner S. Eccles, former Chairman of the Federal Reserve Board, testified on August 15:

Speaking of an immediate tax cut, he said, "Why not act now before there is an emergency and in this way prevent a recession from developing."

Daniel B. Suits, professor of economics, University of Michigan, testified on August 6. Professor Suits urged a gradual release of the "tax brake" through a tax reduction of \$5 to \$10 billion.

Mr. President, those who believe that the President is planning to present a program of short-term expediency and political compromise on taxes to the Nation next year do justice neither to the needs of the United States nor to the good faith of the administration. I believe the President can show that good faith by at least disclosing to us his tax plan now. I strongly urge that he do it.

It has been said in an editorial written on this subject that this should not be done, because perhaps the economy will materially improve, and therefore there will be no need for a creative or incentive tax cut. That is the very point, Mr. President—a creative or incentive tax cut is necessary to have the economy drive forward, which the President said in his campaign he wanted it to do, and not for the purpose of giving the benefit of more money in one's pocket or getting us out of a recession. All of us agree on the need to avoid one, but more important is the need to find a way to bring back into employment those who are unemployed in a number which is unacceptable to the country, and quite properly so, and bring back into utilization the equipment of the American industrial machine which is today under-used.

Therefore, I close as follows: It is evident that we will not get an immediate incentive tax cut. It is also evident that it would be fruitless, indeed unwise, to try to attach it to a tax bill which contains other vital provisions such as investment credit.

Therefore, I confine myself to calling on the President to put before us in principle his tax plan for next year. At least in this way the economy can obtain some view of what is ahead and the Congress will then be able to act with the deliberation essential to thoroughgoing reform of our tax system.

A GREAT JUSTICE FOR A GREAT COURT

Mr. YARBOROUGH. Mr. President, in the selection of Arthur Goldberg as an associate justice of the Supreme Court, President John F. Kennedy has called to that high bench one of the keenest craftsmen of the law of our times.

Arthur Goldberg is a lawyer's lawyer, a brilliant legal light who was moved over into the executive field last year in the difficult post of Secretary of Labor, where he has served with ability, distinction, and success.

Mr. President, while Arthur Goldberg has a fine legal mind, it is not attuned to ritualism or rigidity. Rather, he is a 20th century man, broad in his interests and his learning, schooled in the problems of the country and the world, humanitarian in his outlook and his instincts, just in his actions and orders, courteous always in all places to all persons, and esteemed by those who know him.

Mr. President, I commend the President of the United States for his wisdom in selecting Arthur Goldberg for appointment as Associate Justice of the Supreme Court of the United States.

I request unanimous consent that the editorial in the Washington Post of August 30, 1962, under the title "Mr. Justice Goldberg," and an article from the Washington Post of the same date, entitled "World of Goldberg Turns From Strikes to Supreme Court," from page A-26 of that paper, also be printed in the RECORD at this point in my remarks.

There being no objection, the editorial and article were ordered to be printed in the RECORD, as follows:

MR. JUSTICE GOLDBERG

The most surprising fact about the President's nomination of Secretary of Labor Arthur J. Goldberg to succeed Justice Felix Frankfurter on the Supreme Court of the United States is the willingness of the President to lose Mr. Goldberg as a member of the Cabinet. As head of the Department of Labor, Mr. Goldberg has been a dynamo of enormous usefulness to the President and to the country. Many of his efforts to settle labor-management disputes have been successful. While he has functioned as a champion of labor in the Cabinet, he has done his job with a keen sense of obligation to the country as a whole.

For many years Mr. Goldberg was counsel for the United Steelworkers and the CIO. He came to be recognized as one of the country's ablest lawyers. In 1959 he represented the Steelworkers in their fight against

the Taft-Hartley injunction which ended the 116-day steel strike. Though he lost the case, his oral argument before the Supreme Court earned him high respect from its members and a sincere compliment from the Justices for his efforts.

Mr. Goldberg has made a practice of knowing everything about any case with which he has associated himself, and he has an extraordinary capacity to convey his views to others in an impressive way. On the supreme bench it may be taken for granted that he will be one of its most energetic and conscientious members. Mr. Goldberg has also shown a remarkable capacity for adjustment to new situations. When he became Secretary of Labor, for example, he considered his career as a labor lawyer to be closed forever. He addressed himself to his new job with a measure of objectivity that was greatly to his credit. Instead of acting as a partisan of organized labor, he has functioned as a dedicated public servant with a keen interest in the success of industry and Government in general as well as in the welfare of labor.

Another index to his type of public service may be found in his renunciation of a \$25,000 steel union pension when he became Secretary of Labor. He did not want anyone to suppose that his judgment might be swayed by a pension in his favor. On the bench we surmise that he will perform in the traditional spirit of objectivity, without any relinquishment of his keen interest in human problems.

From the long-range viewpoint, therefore, the appointment of Mr. Goldberg will doubtless merit high praise. From the short-range view, the loss of his dynamism in the Department of Labor will be keenly regretted. But this is the way of Government. It is especially important that the successor to Justice Frankfurter be a man of great energy, capacity in the law and force of personality, for the retiring Justice has been for many years a powerful influence on American law. We shall devote a later editorial to his notable career on the bench. At the moment it is sufficient to say that if Mr. Goldberg succeeds in following the Frankfurter footsteps, his name will be written large in the future legal annals of the United States.

WORLD OF GOLDBERG TURNS FROM STRIKES TO SUPREME COURT

The world of Arthur Goldberg is about to change dramatically.

Tuesday night, he rushed to Chicago in an effort to head off a strike that would have tied up a major midwestern railroad.

A few weeks ago, he was engaged in a furious fight with the steel industry. At other times in recent months, he has settled a dispute at the Metropolitan Opera, looked for jobs for the unemployed, lobbied for bills before Congress, and operated in complete harmony with the Kennedy administration's conception of what an "operator" is.

Now, if the Senate confirms the President's choice for Justice Frankfurter's seat on the Supreme Court, the term "operator" will have to join others that once described the Secretary of Labor but no longer fits.

LOST LABOR'S LABEL

A man who made his reputation as a lawyer for labor, Goldberg quickly lost the label of labor spokesman when he joined the Kennedy Cabinet 19 months ago. His activities since have apparently won for him the respect of big businessmen, a respect growing more out of acknowledgment of his intellectual abilities and his integrity than from the causes he has espoused.

As a lawyer, Goldberg is proud of his ability, which brought him a summa cum laude when he graduated from Northwestern's Law School in 1930.

He soon developed a reputation as a "lawyer's lawyer," a technician who understands the ins and outs that the law often takes. But he does not like to think of himself as a technician and likes to quote from Justice Frankfurter that a good lawyer must, above all, be a cultivated man.

A BALANCE WHEEL

Not long ago, Goldberg spoke of the law as a "flexible, living instrument * * * a balance wheel, not a brake." Too many lawyers, he added, have become mere servants of their clients.

He frequently recalls that Dean John Henry Wigmore, one of his teachers and one of the well known men in the history of American law, once told him, "if you're going to practice law, do it in the grand manner."

That phrase "grand manner" perhaps best describes the seat on the Court Goldberg has been named to fill. It is a seat that has long been occupied by some of the Nation's deepest thinkers.

Before Justice Frankfurter, the seat was held by Benjamin Cardozo, Oliver Wendell Holmes, and John Chipman Gray, all men who saw the law as a set of principles that surpasses the immediate problems of the day.

Mr. JAVITS. Mr. President, will the Senator yield on the same subject?

Mr. YARBOROUGH. I yield to the Senator from New York.

Mr. JAVITS. I should like to join with the Senator and many other colleagues who have complimented the President on this appointment; and I compliment him, too. I have known Arthur Goldberg for 20 years or more as a distinguished labor lawyer, and I have known him in his work as Secretary of Labor. I worked with him in the settlement of the Metropolitan Opera labor dispute.

He has been a very effective Secretary of Labor, probably one of the best we have had in the history of the Department, in comparison with great Secretaries like our own Jim Mitchell, who I think was also a great Secretary.

I shall vote for the confirmation of Mr. Goldberg's appointment, and I feel certain that the Senate will confirm the nomination, and very promptly. What is more, Arthur Goldberg will be a judge on the U.S. Supreme Court of whom we shall have every reason to be proud. I know his character. He will lay aside any previous representation, any previous ideas he had in advocacy, and he will bring to the bench a pure, clear, and luminous legal mind, anxious only to dedicate itself for all the days of his years to justice under the Constitution of the United States. He will be, in my view, neither liberal nor conservative, any more than Cardozo or Brandeis were liberals or conservatives. He will be a great judge in the great constitutional tradition of our country, with courage, and complete dedication.

I think it is most important, in speaking of Arthur Goldberg, that these facts be emphasized to the country by persons like myself who have had the great privilege of knowing him so well for so long and meeting him, not only as Secretary of Labor and in political life, but as a practicing lawyer for trade unions and other clients. I am delighted to be able to pay this very well-deserved tribute to him.

Mr. YARBOROUGH. I thank the Senator from New York for the information he has offered about Justice Goldberg. I have not had the privilege of knowing Justice Goldberg for as long as the distinguished Senator from New York, but I think I met him 10 years ago in Texas. He has been really one of the most active and successful practitioners in this vast field. I knew him through my association with Mr. Leon Green, one of the most successful law teachers in the country, who was dean of Northwestern University at Chicago when Justice Goldberg was a student there. Mr. Leon Green now lives in Austin, Tex. He started as a young man at the University of Texas, and he has come back now to teach law there. He told me he regarded Justice Goldberg as the prize law student of his career. He is very proud of the record which Justice Goldberg made.

Justice Goldberg has been editor of the *Illinois Law Review*. It is important that Supreme Court Justices not only know the law, and not only that they know how to apply the law as legal craftsmen, but that they know how to write law, and that they know how to articulate with the pen. Justice Goldberg is articulate with his pen. He not only graduated from the postgraduate school of Northwestern University *summa cum laude*, but he has written many articles in addition to legal briefs and opinions, and is the author of a book, "AFL-CIO: Labor United."

I think we will see in the years ahead in Justice Goldberg a man who will grace that High Court with increasing confidence in the Court among lawyers and citizens of the United States.

THE MYSTIQUE OF GOLD

Mr. MILLER. Mr. President, in the Thursday, August 29, 1962, issue of the *Christian Science Monitor* is an excellent article by the distinguished writer, Richard L. Strout, entitled "The Mystique of Gold." The article is highly informative and will be most helpful to readers in understanding the problem of the drain on the gold reserve of the United States, its relationship to the gold reserve backing up our currency, and its relationship to the world monetary market.

I ask unanimous consent that the article be printed in the *RECORD*.

There being no objection, the article was ordered to be printed in the *RECORD*, as follows:

THE MYSTIQUE OF GOLD (By Richard L. Strout)

WASHINGTON.—Foreign rumors about U.S. dollar devaluation persist. Americans can't understand it. Gold outflow from New York declines, but nevertheless continues. The Federal Reserve Board is sensitive: it rejects easy money (low interest rates to stimulate halting recovery) because low interest rates here might cause foreigners to take out more funds to reinvest abroad at higher rates. It is a tangled problem.

Let's go back a bit. Originally gold was the basis of paper currency. But the world gold supply, in the opinion of many economists, isn't adequate. It is one of the world's ironies that gold, on which capitalism operates, comes—at a nice profit—largely

from Soviet Russia. The Soviet sells about \$200 million a year to the West. South Africa is another big producer.

The mystique of gold is a kind of fairy tale. A man from Mars wouldn't believe it. Gold is dug out of the ground in order that man can store it underground again, at Fort Knox, say. The rate of gold mining is inadequate under present usage to sustain the rate of world economic growth. Other commodities in short supply go up in value, but the price of gold is pegged to the dollar.

The West has got around the inadequacy of gold reserves. Instead of the gold standard there is now the "international gold exchange standard." This means that instead of holding gold as a reserve other countries hold dollars, or perhaps pounds, against their currencies. This has permitted the vast expansion of reserves needed to carry on international trade. The United States is the only Nation on earth committed to exchange its currency for gold at a fixed price—\$35 an ounce. The other countries can come to us and get gold for our dollars at any time; but if our Government holds francs, lira or pounds we can't get gold for them. The dollar carries enormous responsibility.

There are embarrassments in this situation. Britain knows about them. After World War I, Britain returned to convertibility (i.e., agreed to exchange pounds for gold) in 1925. World investors built up sterling balances. But this made the pound highly vulnerable. As long as London discount rates—interest payments—were high foreigners kept short-term funds there, but they moved out overnight if rates rose in other monetary centers. Short-term movements also embarrass the United States today. Rumors of sterling weakness constantly circulated. Dollar rumors circulate today.

When Britain's domestic economy declined economists urged the stimulus of lower interest rates, but Montagu Norman, Governor of the Bank of England, wanted high rates to keep short-term foreign funds in London. William McChesney Martin, head of the Federal Reserve Board, has somewhat the same feelings today.

Finally Britain, facing unemployment and raids on sterling devalued the pound, September 21, 1931. It knocked over a whole row of financial dominoes.

America has a vastly stronger gold reserve today, the largest in the world, \$16,200 million. We have had an adverse balance of payments but this is not due to profligacy or inflation but to calculated U.S. export of foreign aid and defenses. It could be halted overnight.

Nevertheless, the world can't quite believe this. Foreign central banks hold more than \$12 billion of short-term dollar obligations. What if they should all cash in at once? They won't, but this is a matter of confidence, not logic. Again, the world's liquidity requirements have been derived in recent years only partly from current gold production and Soviet sales; two-thirds have come from continuous depletion of U.S. net reserves. How long, it is asked, can this go on?

Leaders of the World Bank and the International Monetary Fund meet in Washington next month. Though press and public don't realize it yet another basic battle has begun over interest rates—Mr. Martin wanting them high (for international considerations); economists wanting them low (to stimulate flagging domestic business). Incidentally, Chairman Martin's term at the Reserve Board expires shortly.

The present system puts an unfair burden on the United States. International exchange should not be tied any longer to one or two national currencies. International liquidity demands a broader base with a new permanent mechanism. The United States isn't going to permit a dollar collapse. But

it conceivably might be forced into a slowdown of contributions to world liquidity and to international aid.

MESSAGE FROM THE HOUSE

A message from the House of Representatives, by Mr. Bartlett, one of its reading clerks, announced that the House had passed, without amendment, the bill (S. 2250) to provide for the incorporation of the National Woman's Relief Corps, Auxiliary to the Grand Army of the Republic, organized 1883, 78 years old.

The message also announced that the House had agreed to the following concurrent resolutions of the Senate:

S. Con. Res. 87. Concurrent resolution authorizing the printing of additional copies of the hearings entitled "Military Cold War Education and Speech Review Policies" and the report thereon; and

S. Con. Res. 88. Concurrent resolution authorizing a change in the enrollment of S. 2321, the District of Columbia Tissue Bank Act.

The message further announced that the House had agreed to the amendment of the Senate to the bill (H.R. 7782) to authorize the Secretary of the Interior to convey certain lands in the State of Maryland to the Prince Georges County Hospital, and for other purposes.

The message also announced that the House had agreed to the report of the committee of conference on the disagreeing votes of the two Houses on the amendment of the Senate to the bill (H.R. 10062) to extend the application of certain laws to American Samoa.

The message further announced that the House had disagreed to the amendment of the Senate to the bill (H.R. 12391) to improve and protect farm income, to reduce costs of farm programs to the Federal Government, to reduce the Federal Government's excessive stocks of agricultural commodities, to maintain reasonable and stable prices of agricultural commodities and products to consumers, to provide adequate supplies of agricultural commodities for domestic and foreign needs, to conserve natural resources, and for other purposes; agreed to the conference asked by the Senate on the disagreeing votes of the two Houses thereon, and that Mr. COOLEY, Mr. POAGE, Mr. GATHINGS, Mr. BREEDING, Mr. HOEVEN, Mr. BELCHER, and Mr. QUIE were appointed managers on the part of the House at the conference.

REVENUE ACT OF 1962

The Senate resumed the consideration of the bill (H.R. 10650) to amend the Internal Revenue Code of 1954 to provide a credit for investment in certain depreciable property, to eliminate certain defects and inequities, and for other purposes.

The PRESIDING OFFICER. The question is on agreeing to committee amendment No. 2, to strike the language beginning on line 1, page 52.

FOREIGN PROVISIONS

Mr. GORE. Mr. President, several sections in the pending bill deal with the taxation of income and profits earned abroad by American taxpayers through

technically foreign subsidiary corporations which they control. Several of the provisions in these sections are meritorious. On balance, however, the bill would not go nearly far enough to correct the situation which now exists and restore our tax system to a position of neutrality as between domestic and foreign operations.

We need to improve this bill and make it less favorable to foreign economic operations. We need to do this now, not next year or some year thereafter.

The problem created by the favorable tax treatment of income earned abroad adversely affects the national interest, particularly with respect to the balance-of-payments problem and the movement of U.S. industry and employment abroad.

My colleagues are well aware of the fact that it is difficult to obtain legislative momentum on any given subject. When any particular subject has been under consideration for both sessions of a Congress and has gotten through the House and finally to the floor of the Senate, it is most difficult to repeat the process until several years have passed.

In view of this well-known fact of legislative life, it behooves us to deal thoroughly and properly with the subject at hand right now. We may not have another opportunity for years to come. By that time, unless we take effective action now, more drastic measures may well be required.

Now, what is the problem in the foreign area, involving the taxation of profits earned by American interests abroad? The President has defined the problem and offered a solution.

In the words of the President, enunciated in his message to the Congress on April 20, 1961, the problem is this:

Changing economic conditions at home and abroad, the desire to achieve greater equity in taxation, and the strains which have developed in our balance-of-payments position in the last few years, compel us to examine critically certain features of our tax system which, in conjunction with the tax system of other countries, consistently favor U.S. private investment abroad compared with investment in our own economy.

And, what was the President's recommended solution?

I, therefore recommend that legislation be adopted which would, after a two-step transitional period, tax each year American corporations on their current share of the undistributed profits realized in that year by subsidiary corporations organized in economically advanced countries. This current taxation would also apply to individual shareholders of closely held corporations in those countries.

The President also recommended "elimination of the tax haven device anywhere in the world, even in the underdeveloped countries, through the elimination of tax deferral privileges for those forms of activities, such as trading, licensing, insurance, and others, that typically seek out tax haven methods of operation. There is no valid reason to permit their remaining untaxed regardless of the country in which they are located."

Secretary Dillon strongly endorsed the President's recommendations and gave them concrete backing in testimony be-

fore the Ways and Means Committee and the Finance Committee. Indeed, Secretary Dillon went so far as to agree, in testifying before the Finance Committee, that anything short of complete removal of the deferral privilege, whereby U.S. taxation of profits earned abroad may be indefinitely postponed, would be but "piddling" with the problem.

Despite this clear recognition of the problem, and these strong recommendations for its correction, the House went only a part of the way in correcting the situation. The Finance Committee, for no reasons which I can determine except the pressure of the business community—which, understandably, never wants to pay more taxes than absolutely necessary—refused to consider the President's principal recommendation and, instead, backed away from even the House provisions and reported to the Senate a weak, watered down and wavering tax haven approach. The committee then provided broad escape hatches in even this wholly inadequate approach to the problem.

One can see, then, Mr. President, why I find it necessary to disagree with the majority action of the committee on which it is my privilege to serve.

Just what is our problem insofar as operations abroad by American interests are concerned?

Briefly, the problem is this. Due to changing world conditions during the past several years, entirely too much American capital is moving abroad. This capital is moving into the wrong areas and the wrong activities.

This capital movement takes several forms—direct investment, long-term portfolio investment, and short-term or hot money flows. This capital outflow, particularly that represented by direct investment—that is, investment which goes into setting up separate corporations, or branch operations, in foreign countries owned and controlled by American interests, generally large U.S. corporations—is particularly hurtful to the domestic economy since much of it represents the direct shipment of jobs from the United States to the foreign country concerned.

The other forms of capital outflow, long-term portfolio and hot money, are not so directly harmful to the economy, although they are quite troublesome insofar as the balance of payments is concerned.

Not all foreign investment is harmful to the economy, of course. As I shall discuss later, about 10 percent of our foreign investment is related to our own export activities, and is of assistance to the domestic economy. Part of our foreign direct investment is in the form of petroleum and mining operations, and helps us to obtain a steady inflow of needed raw materials and semifinished goods.

It so happens that most of the petroleum and mining operations are conducted in branch form and are, therefore, little affected by proposed changes in U.S. tax law. It also happens that the 10 percent of direct foreign investment associated with the encouragement of our exports would be little affected

since, if the corporations involved are keeping their books legitimately, the larger part of the total profit obtained from exports will be earned by the manufacturing process in the United States, and the much smaller portion of the profit earned by the sales organization in Europe or elsewhere, even if taxed currently on its net profit, should not deter the overall export activity involved.

On the other hand, tax changes will not accomplish all that needs to be done in balancing our payments to and from foreigners. Other changes of a regulatory nature may well be necessary for this purpose.

TAXATION AND CAPITAL FLOWS

One of the most startling economic phenomena of the past 5 years is the large-scale movement of American capital abroad. Though some of the economic activity represented by this movement may be desirable and may serve to increase exports, much of it directly and materially weakens the base of our economy. Some of this capital is drawn abroad for legitimate economic reasons. Much of it, far too much, is stimulated to move abroad because of faulty U.S. tax provisions.

Several reasons exist, of course, for this unprecedented movement of capital abroad. International barriers of all sorts are being broken down. Convertibility of currency exists in large measure. Electronic communications insure effective control of economic activities anywhere in the world from one central office. The movement of persons and goods has been speeded up and cheapened to a point where distance makes very little difference. American economic style and business organization have made American know-how welcome in most countries. American free world leadership has lent prestige to all things American.

In view of these facts—facts which we may not want to alter, even if we could—it is most inappropriate to set up additional artificial stimuli to the movement of American capital abroad, particularly into activities and in amounts which are contrary to the national interest. Existing law relating to the taxation of economic activities carried out by American interests in foreign countries constitutes just such an artificial stimulus to the movement of capital abroad into areas and activities which pose dangers to the domestic economy and make more difficult a solution of the balance-of-payments problem.

As our tax laws now stand, they constitute a positive subsidy to the movement of American capital abroad. There are numerous ways in which the taxation of profits from foreign operations can be reduced to the extent that it may be more profitable to expend American capital and American know-how in building up the economy of West Germany rather than the economy of West Virginia, or south Italy rather than South Carolina.

The existence of this unhappy circumstance is given implicit verification by virtue of the fact that this bill, in 11 of its 27 sections, deals with the taxation of foreign operations of U.S. taxpayers,

both individual and corporate. Unfortunately, having recognized the existence of certain problems, the bill proceeds toward correction of these problems in a most timid and halfhearted manner.

Our tax laws regarding foreign operations are hopelessly out of date. For the most part they stem from rules laid down when the income tax was developed prior to the First World War. Developments in communications, transportation, and even in international politics and political organization have made some of these laws obsolete.

In theory, the United States taxes its citizens wherever they are and from whatever source their income is derived. Although this would seem to preclude the use of the tax laws as a subsidy to draw economic activity abroad, in practice we have nullified theory to a great extent by, first, allowing American interests to operate abroad in subsidiary form without the imposition of any U.S. taxation whatsoever on the profits from those operations until those profits are remitted—often in a form which can take a capital gains rate or no rate at all—and, second, by providing for a credit for foreign income taxes paid against ultimate U.S. taxes on income earned abroad.

There are several separate and distinct tax advantages to locating a factory in Europe, for example:

First. Deferral: Most foreign enterprises owned by U.S. corporations, except those connected with petroleum and mining operations, are organized as subsidiaries rather than branches. This means that no U.S. taxes are due until such time as dividends are paid to the parent organization in the United States. In many instances, income taxes in foreign countries are considerably lower than in the United States. Furthermore, even when the tax rate is substantially the same, as in the case of Germany, a sales office and a holding company in Switzerland can be used in such a way as to lower the effective German tax.

The value of tax deferral is real and measurable. It amounts to an interest-free loan of tax moneys which should have been, and were not, paid over to the United States. A study made about 2 years ago by the American Management Association showed that, because of this preferential tax on operations abroad, as compared with taxes here at home, reinvestment of foreign earnings could provide, over a 3-year period, "roughly double the rate of profit accumulation for reinvestment that is possible under domestic tax schedules."

The deferral privilege, then, both draws funds overseas and tends to keep them there.

Second. Foreign tax credit: A business enterprise located in a typical city in the United States must pay State taxes, county taxes, city taxes and often other special taxes in addition to its U.S. income tax. All these non-Federal taxes are, of course, business expenses and are properly deductible from gross income in determining income subject to tax by the Federal Government. But in the case of foreign income and similar taxes, these items of actual busi-

ness expense are not charged off as expenses. Instead, they are applied as a credit against the U.S. income tax if and when that tax is finally paid. This ability to use foreign income taxes as a credit against U.S. income taxes rather than a deduction from taxable income gives a decided edge to foreign investment.

Third. Gross-up: Due to imperfect language in the statute dealing with the crediting of foreign taxes against U.S. income taxes, there is allowed, in effect, both a deduction and a credit for foreign income and associated taxes paid. This has the effect, even without setting up a tax haven operation, of reducing the effective U.S. tax rate to close to 40 percent in some instances.

Fourth. Tax haven abuses: I do not wish to take the time today to detail all of the various types of tax haven abuses possible under our tax laws. Let me say just now that these abuses are legion and are used, not only to reduce foreign taxes and pull profits of legitimate foreign operations into tax havens almost tax free, but tax havens are also used to pull profits from American domestic operations into tax havens so as to escape U.S. taxes. This latter type of outflow, or lack of proper inflow, of dollars is doubly harmful.

It is also often possible to collect profits for several years in a tax haven dummy corporation, then collapse the corporation and bring home the accumulated profits in the form of capital gains which are subject to a maximum tax rate of 25 percent.

Many of these tax haven abuses are subject to correction administratively—if they can be detected, if the books are available, and if all taxpayers concerned are cooperative. These circumstances seldom prevail. Detection is difficult and requires the time of many more highly trained and skilled revenue agents than we have available, even if all of them were put on such cases. Furthermore, with the books in a foreign country, and often subject to strict so-called anti-espionage laws, it is impossible to get at the true facts.

I shall have more to say about tax haven operations and abuses. Suffice it to say right now that similar operations and opportunities for tax avoidance and evasion are not available to domestic operations. The bill before us would probably put a stop to many tax haven abuses.

Fifth. Income earned abroad by individuals: Foreign operations have a further tax advantage over domestic operations in that U.S. citizens are allowed, under our faulty tax laws, to go abroad and work for a number of years and avoid payment of U.S. income taxes. This makes working overseas relatively attractive and enables companies with foreign operations to hire capable U.S. personnel at a lower salary or wage than they would otherwise have to pay.

All of the above give an advantage, insofar as taxation is concerned, to operating abroad as against performing the same operation here at home. This tax advantage cannot help but act as a magnet to draw funds abroad—funds which could and should be allocated to

expanding and modernizing our domestic plant and equipment.

I do not think it necessary to penalize overseas operations, although the situation may get so bad that some positive, active steps must be taken to prevent or slow down the flow of capital into certain foreign countries. But it seems to me that we should now, during this session, take the necessary legislative steps to insure that taxation is at least neutral. We should at least tax foreign operations as heavily as operations here at home. This would not put an end to foreign investment—indeed, such would not be desirable. But it would slow down the currently rapid growth of foreign investment and insure the repatriation of sufficient foreign earnings in the years immediately ahead to be of material assistance in the balance of payments as well as to assist in the needed modernization of domestic plant and equipment.

TAX EQUITY

Equity in taxation is a subject to which lipservice is paid from time to time. Everyone claims to be in favor of equity, but many define equity in strange and tortured ways. Generally speaking, if a dollar earned by a particular type of taxpayer in any economic activity, in any geographical area, pays the same tax as another dollar earned under other circumstances by similar types of taxpayers, we can say that tax equity has been achieved.

Of course, from time to time preferences are given to certain types of operations, certain areas, and certain organizations, but when this is done it should be done consciously, and deliberately, in the full knowledge of what is being done, and with the accomplishment of definite objectives in mind. When a subsidy is voted—and a subsidy can be awarded a taxpayer by giving him a tax preference just as surely as it can be awarded by way of a cash payment—it should be voted to accomplish a proper national or social goal, not done accidentally, or as a private giveaway.

For example, there is no question that the average homeowner receives better tax treatment than the average renter of living quarters. But the Congress has deliberately provided this because it is considered socially desirable to foster homeownership.

In certain other instances tax advantages are given inadvertently, or because of reasons which are no longer valid. Certain of our laws dealing with the taxation of the profits and income earned abroad by American taxpayers, both corporate and individual, directly and through technically foreign subsidiaries, fall in each of these two categories.

Business decisions today are often made on the basis of tax consequences. Many decisions as to what operations should be moved abroad are made on the basis of tax consequences. Many foreign operations are set up in order to avoid taxes, in a virtual maze of interlocking and overlapping organizations, confusing to customers and operators alike. This is hardly in keeping with concepts of equity or even good business management.

The best way to achieve tax equity, particularly in this field, is to seek tax neutrality, this is, to seek to have tax laws such that economic decisions are made on the basis of economic criteria, not on tax consequences. Unfortunately, the bill reported by the Finance Committee, although it recognizes the existence of inequity, does little to deal with it effectively. Under terms of this bill, operations carried on abroad will still receive favored tax treatment as compared with the same type of operation carried on here at home.

DOMESTIC ECONOMY HEALTH

Many who are concerned, and who so often express that concern, about the so-called export of jobs because of the liberalization of trade restrictions and the lowering of tariff barriers will rarely stop to examine our faulty tax laws and the part they play in exporting entire factories to Europe.

When we break down artificial trade barriers we promote a two-way trade which ultimately benefits and strengthens the economy of all trading nations. This is not to say, of course, that some individuals or segments of industries will not be hurt temporarily, or even permanently. A glass manufacturer, for example, may curtail his activities and his employees may be thrown out of work. But at the same time, production for export may be increased in other lines such as chemicals, machinery, electronics, and farm products. President Kennedy has recognized the domestic problems associated with increased trade and has proposed ways to deal with those problems.

But what about the factory which is lured abroad by a tax loophole? Who benefits from that? Surely our economy as a whole does not. A few large stockholders may benefit. A few insiders may profit from speculation. But our national interest is injured. Payrolls are lost. People are left unemployed. The productive potential of the country is lessened. The gross national product is lessened, and our standard of living is just that much lower.

Of course, the host country benefits from our shipping industries to it. For this reason Congress may not want to discourage investment of a proper type in certain underdeveloped countries. Unfortunately most of the private investment in such countries is in the extractive industries and this may do the host country but little permanent good. Moreover, the use of tax favors in foreign policy, even in foreign aid, to underdeveloped countries may not be the best or most effective means of achieving our objectives.

I have found no better proof of the benefits to be derived by the host country from the establishment therein of American subsidiary corporations than an article published in the *Anglo American Trade News* in January 1962. This article is so interesting that I should like to read it in its entirety; it is not long. It reads as follows:

AMERICAN EXPORTS FROM BRITAIN—A NEW SURVEY OF 120 U.S. MANUFACTURING SUBSIDIARIES OPERATING IN THE UNITED KINGDOM

American manufacturing enterprises based in the United Kingdom are continuing

to make solid and constructive contribution to Britain's export effort and payments balance.

This is the story that emerges from export performance data gathered by the American Chamber of Commerce in London from chief management executives of the leading American manufacturing subsidiaries in the United Kingdom. Results of a recent survey which included hard figures from 120 chamber member companies of American parentage show that 26 percent of them exported from 41 to 100 percent of their entire production during the first half of 1961.

Thirty percent of these American owned companies shipped 21 to 40 percent of their output abroad during the first 6 months of last year. The remaining 44 percent of the group sampled by the chamber sold up to 20 percent of their production in overseas markets.

Additionally, 15 firms reported that they estimated their contributions in indirect exports were of much greater importance to the British economy than the direct export figures indicate. These makers of components and subassemblies supply British customers whose products in turn are prime sellers in world markets.

The majority of U.S. subsidiaries in this category estimated that inclusion of their indirect exports in their totals would be sufficient to more than double their direct export performance. Two companies which reported no direct imports noted that their entire production finds its way to export markets in this manner.

Proper evaluation of figures and percentages requires comparison to convey meaning, and it is by using a yardstick of past performance and by measuring against current available data on exports of British industry generally that the scope of American financed contribution becomes significant.

In his 1954-55 study, "American Investment in British Manufacturing Industry" (George Allen & Unwin, 1958), Prof. John H. Dunning, of the University of Southampton, revealed that 152 American manufacturing subsidiaries in the United Kingdom reported the following export performance: 26.2 percent of them exported 41 to 100 percent of their production; 41.3 percent sold 21 to 40 percent of output to foreign markets, and 32.5 percent recorded export sales up to 20 percent.

It can be assumed that many of the companies in the Dunning study are identical with those sampled in the chamber survey, although a number of firms in the current sample have been established during the past 8 years. This is worth noting because recently the United Kingdom Government has tended to relax its entry requirements for foreign direct investment in manufacturing enterprises. Formerly the dollar shortage in the United Kingdom made it mandatory that the prospective investor's product be a vital dollar saver on the domestic market and a prodigious seller overseas.

With easier entrance for the newcomer and with more affluent domestic consumers to be tapped by both the neophyte and the long established companies, it might be expected that the current export graph would drop precipitously below the 1954 mark. This has not been the case.

Measured against contemporary performance of British industry generally, the American manufacturers in the United Kingdom appear to run slightly ahead of the current. The Federation of British Industries export supplement to "Industrial Trends Enquiry No. 12," released for publication on October 13, 1961, shows that 492 United Kingdom manufacturers with annual exports amounting to more than £10,000 line up in this manner: 12 percent deliver more than 50 percent of their output overseas; 28 percent export 25 to 50 percent; 31 percent sell 10 to 25 percent abroad; 17 percent export 5

to 10 percent, and 12 percent record export sales of less than 5 percent.

Comparable figures for the 120 American firms in the United Kingdom are: Exports over 50 percent, 19 percent of the companies; 25 to 50 percent, 29 percent of the companies; 10 to 25 percent, 36 percent of the total, and in the 5 to 10 and less than 5 percent categories, 5 and 10 percent of the companies, respectively.

Again, in the FBI inquiry it can be expected that a majority of the U.S. companies are included, but it should be remembered that the FBI includes among its members this country's largest concerns and its most formidable exporters. On the other hand, with the exception of a small minority of the U.S. financed companies, the American firms supplying information for the chamber study class themselves in the small to medium sized brackets. Notwithstanding this, American industry in Britain has been credited by numerous British authorities with employing nearly 1 in every 20 workers employed in United Kingdom manufacturing industry today.

Enlarging on this, Sir Miles Thomas, chairman of Monsanto Chemicals, Ltd., in a talk he gave at a chamber luncheon meeting in mid 1959, said:

"I wonder if any of you read some relevant and extremely interesting figures in the *Times* recently? There are roughly 400 U.S. subsidiaries and Anglo-American companies in the United Kingdom and they employ about 375,000 people. Impressive figures, but—and it's a very considerable but—these people only represent about 4 percent of our total labor force. And the total value of the output of those 400 or so companies, at around £1,200 million, is about 5.5 percent of the gross output for all United Kingdom manufacturing industry for 1957.

"A further fact was that, at the present time, U.S. representation in United Kingdom industry is confined almost entirely to industries supplying products which were first developed on a significant scale in the United States, if not actually discovered there.

"Let me take three more points, all from the same source. Between 1950 and 1957 U.S. subsidiaries and Anglo-American firms accounted for something like 7.5 percent of the net capital expenditure of all British manufacturing industry. Secondly, such firms have access to the benefits of more research and development than all United Kingdom industry (on private account) combined. Finally, these firms currently supply between 10 and 12 percent of all United Kingdom manufacturing exports and one-third of the exported goods commercialized within the last two decades."

Further emphasis on the impact of the contribution of direct American investment on the British economy can be drawn from a statement made recently by Carl Gilbert, chairman of the Gillette Co., of Boston, at the convention of the National Foreign Trade Council in New York. He stated that of the 3 million overseas workers employed by U.S. industry only about one in every hundred is a U.S. citizen. Rough calculations in the United Kingdom show that this ratio is, for Britain, entirely unrealistic. The British labor participation, from the managing director's desk to the apprentice's bench, in American manufacturing industry in the United Kingdom comes much nearer complete saturation.

Returning to data compiled from answers to the chamber's questionnaire, two outstanding trends come to light.

(1) Additional manufacturing facilities established by the U.S. parent within the Common Market or in other areas where various conditions make local manufacture unavoidable have cut into exports from a number of the United Kingdom subsidiaries; and

(2) Domestic United Kingdom sales have in numerous cases increased sufficiently to

downgrade export percentage figures, although actual exports have remained static, or even improved.

Consolidation of answers to the questionnaire which asked respondents for a simple "percentage figure which your exports represented in relation to your total sales for the first half of 1961 compared with the corresponding period of 1960, together with two or three main areas of their destination, e.g., the Far East, Middle East, Western Hemisphere, and Western Europe," gave the following picture:

A total of 23 concerns directly exported between 50 and 100 percent of their total sales in each of the two periods (January to July 1960, 1961). These companies manufacture specialized lines of capital goods and consumer durables for which there is a relatively limited market in the United Kingdom. They possess either their own world marketing organizations or highly qualified distributors. The majority of them—15—registered increases in their export sales for the 1961 period; the increases varied from 13 to 0.4 percentage points.

The remaining companies in this group indicated decreases in their export business during the first half of 1961. One of the causes mentioned being the type of business involved (often consisting of large contracts) does not lend itself to meaningful comparisons between given periods. In some cases the total volume of exports was up in the 1961 period, although the percentage was less, compared with 1960.

The destinations of the exports of the companies in the 50 to 100 percent category were worldwide, the percentages by markets having varied considerably between the two periods. In the rough order of importance the destinations were Europe, Far East, and Australia, South America, Middle East, and Africa.

The group showing exports ranging between 25 and 50 percent in each of the two periods consisted of 35 companies. Of these, 19 indicated increases of a few points in most instances during 1961. The decreases shown by the balance of the group were also of minor magnitude, while the percentage of total sales was lower in some cases during the 1961 period, the actual amounts were greater. Again the marketing areas were more or less worldwide, that is, Europe, South America, the Far East, Middle East, Africa, and North America.

The largest group in the sample comprised the 43 companies which exported from 10 to 25 percent of their total sales in the 1961 period. Barring a few exceptions these concerns were also in the same category in 1960. The export sales of 22 of the companies increased in the 1961 period; the highest of an individual company having been from zero in 1960 to 17 percent of total sales in 1961. The smallest increase recorded was from 20.2 percent in 1960 to 20.4 percent in 1961.

The firms reporting reduced sales in 1961 numbered 19, the reductions in most cases being small. Reasons given for some of the reductions were the opening of other overseas plants by the parent companies concerned, due to the unavoidable need in many countries to set up local manufacturing operations. Here again several of the companies confided that in actual fact there were appreciable increases in the export sales during the 1961 period, though the percentages were slightly diminished owing to a proportionately slightly greater increase in the consolidated sales. The percentage of exports to the several areas of destination varied considerably in many cases, but in general the principal areas were Europe, Far East, Middle East, Africa, and the Americas.

There were only seven companies in the group exporting from 5 to 10 percent of their total sales, two of these enterprises having reported decreases in such sales during the 1961 period. One of the companies

showing a decrease explained that the relatively low percentage in the 1961 period under review was due to the fact that an associated firm in a Common Market country began to supply that area. The other company stated that while its export business has been growing, the lower percentage export figure in January-July 1961 was chiefly due to unusually high exports in the corresponding period of 1960. Destinations in general were Europe, the Middle East, and Far East.

The group having less than 5 percent of direct export sales consisted of 12 concerns, 4 of which reported decreases in the 1961 period. The differences in all cases were small, and the areas of destination were Middle East, Africa, Europe, and the Far East. A few of these companies have been established in the United Kingdom only a short while, and others reported the fact that sales in the United Kingdom materially affected the export figures.

Finally, an aggregate of 70 companies reported export sales running at 20 percent of total sales during both periods; 53 firms showed export business ranging from 25 to 100 percent in the first half of both 1960 and 1961, and no less than 39 U.S. subsidiaries stated that their export shipments were at the level of 40 percent or more of their output during both periods in question.

Export performance

[All figures in percentages]

120 U.S. MANUFACTURING SUBSIDIARIES IN BRITAIN, 1961

Exports.....	To 21	21 to 40	41 to 100
Companies.....	44	30	26

152 U.S. MANUFACTURING SUBSIDIARIES IN BRITAIN, 1964

Exports.....	To 20	21 to 40	41 to 100
Companies.....	32.5	41.3	26.2

492 UNITED KINGDOM MANUFACTURERS, 1961

Exports...	To 5	5 to 10	10 to 25	25 to 50	50 to 100
Companies....	12	17	31	28	12

120 U.S. MANUFACTURING SUBSIDIARIES, 1961

Exports...	To 5	5 to 10	10 to 25	25 to 50	50 to 100
Companies....	10	5	36	29	19

Mr. President, several points should be emphasized:

First. These companies had a very high export-to-production ratio which was of very material assistance to Great Britain in solving her own balance-of-payments problems.

Second. These companies manufactured and sold in Britain and elsewhere throughout the world, including the United States "almost entirely products which were first developed on a significant scale in the United States, if not actually discovered there." I shall have more to say on this point shortly.

Third. These companies employed about 375,000 people, about 4 percent of the total United Kingdoms labor force, and produced about 5.5 percent of the manufacturing output of the United Kingdom.

Fourth. About 3 million overseas workers are employed by American industry

altogether, and only about 1 in 100 is an American. In Britain there are almost no Americans employed by these subsidiaries located there and "British labor participation, from the managing director's desk to the apprentice's bench, in American manufacturing industry in the United Kingdom comes much nearer complete saturation."

Fifth. Manufacturing facilities "established by the U.S. parent within the Common Market or in other areas where various conditions make local manufacture unavoidable have cut into exports from a number of the United Kingdom subsidiaries," and at least one of these British companies reported that the "relatively low percentage" of exports from its plant in that 1961 period under review was due to the fact that an associated firm in a Common Market country began to supply that area.

I think these observations are most appropriate to the discussion at hand. Certainly we can see from the operation of these British corporations controlled by American interests and manufacturing American-type products that the employment and balance-of-payments benefits inure to the United Kingdom, not the United States.

Points 2 and 5 are particularly interesting to me. This is a clear recognition of the competition which is offered to domestic production when factories of the same type, producing the same type goods, are set up in areas where our own factories have been exporting.

I hope that Members of the Senate who have been misled by the testimony, entreaties, and letters of the very small minority of American concerns and interests which have moved their industries abroad, which actually show some benefit to the United States, will read the article which I have now read to the Senate. This article was not written for the purpose of influencing the U.S. Congress, but it is a factual article about how the establishment of American-owned industry in Great Britain has vastly benefited Great Britain, and has correspondingly been harmful to American domestic business engaged in export trade. Not only is this true of Great Britain, but of other major areas of the world.

There are many more instances which show the hurtful effect that flows from the subsidy of the movement of American business, capital, industry, and jobs abroad.

I think these observations are most appropriate to the discussion at hand. Certainly we can see from the operations of these British corporations, controlled by American interests and manufacturing American-type products, that the employment and balance-of-payments benefits inure to the United Kingdom and not to the United States. This results in the employment of citizens of the United Kingdom and reaches, as the article says, the point of saturation.

It is but natural that the establishment of an industry in Great Britain would benefit the economy of Great Britain. There is nothing strange about that, I say to my distinguished friend, the senior Senator from Connecticut,

who does me the honor of his attention. The same would be true with respect to the establishment of industry in Connecticut, even though it might be owned by Dutch interests, by British interests, or by German interests.

What I speak of now is the vast amount of American investment in Great Britain, constituting, as I have read, a large part of the manufacturing potential of the whole United Kingdom. Some of the factories in Great Britain have employment almost exclusively of citizens of the host country. This not only curtails the export of goods from U.S. factories to the United Kingdom, but also, as I have read from the article, it curtails American production in that the products of those factories, of American type—many of them originating in America in design, in labels, and in trade names—are then exported to Europe, to the Far East, to the Near East, and to South America, as well as to the United States.

Mr. BUSH. Mr. President, will the Senator yield?

The PRESIDING OFFICER (Mr. PELL in the chair). Does the Senator yield?

Mr. GORE. I yield to the senior Senator from Connecticut.

Mr. BUSH. I have been very much interested in the Senator's comments, and I have tried to follow them as closely as possible. The Senator is dealing with the tax bill. I take it from what the Senator has said so far, as I have heard him, that he believes it is the tax incentive rather than any other incentive—such as the cost of production—which entices American manufacturers to go abroad and to establish branches and subsidiaries to make their products abroad.

I have studied this problem pretty closely, too, especially in connection with the trade bill which will be before the Senate in 2 or 3 weeks, with which the Senator is also familiar, I know. It seems to me that the evidence is pretty strong that the other advantages, such as lower costs of production, including labor cost, have attracted American industries to establish branches and to manufacture goods in Common Market countries, and in the United Kingdom particularly, because this is where most of it has gone, I believe.

The question which I wish to ask the Senator is whether he agrees that these other influences, these other cost advantages, which result in very much reducing the ultimate cost of the products sold within those markets, and even the products brought back into our markets, as the Senator has said, are more influential and have been more influential in enticing American manufacturers to operate in foreign countries than the tax advantage which may have accrued as a result of the differential of taxation on earned income in those foreign countries.

I should like to have the Senator comment on that, if he would be kind enough to do so.

Mr. GORE. I can understand how, in listening to my address today, my colleague, the distinguished and able senior Senator from Connecticut, for whom I

have great affection and the highest of respect, and whose presence will be sorely missed in this Chamber when he departs at the end of his term, could arrive at the impression or the conclusion which he has stated, because I have been talking about the tax incentive for the movement of industry abroad.

I readily concede that there are other incentives. Whether the tax incentive is greater or whether the others are greater is a question I think one would have to determine by study of each individual case, though there may be a general situation.

Before speaking to that particular point, let me say that it is not within the power of the U.S. Government to establish a minimum wage in Great Britain, in Italy, in Germany or in Belgium.

Mr. BUSH. That is correct.

Mr. GORE. It is not within the power of the U.S. Government to prevent a province in southern Italy from offering to build a factory and to let an American concern have it rent free.

It is not possible for the U.S. Government to stop some country from lending money interest free to an American concern to buy machinery.

It is not possible for the U.S. Government to prevent other countries from giving such American-owned industries a direct subsidy for the exports they make to the United States.

These things are beyond the jurisdiction of the United States.

Mr. BUSH. Mr. President, will the Senator yield on that point?

Mr. GORE. Let me continue one moment.

What I am dealing with in my address and what is before the Senate is the question of American taxes. I think this is something with which we can properly deal. It is the removal of the tax subsidy for such export of American factories and jobs that I now advocate.

I do not contend that this would solve the problem. Indeed, I do not propose to stop the movement of American industry and capital abroad. I propose to remove the tax subsidy for such a movement.

Now I yield to the Senator.

Mr. BUSH. I say to the Senator that my recollection is—and I think we had this evidence before the Joint Economic Committee within the past 12 months—that the income from American investments abroad was measured last year in terms of about \$2.2 billion in this country, as against which we exported for investment some \$2 billion. So to that extent, if the figures are correct—and I believe they are—the balance of payments on the total question of investment was a benefit to the extent of \$200 million.

Mr. GORE. I believe the Senator has rushed to conclusions that are not justified. A vast amount of the inflow—perhaps half of it—comes from mineral and petroleum operations which are organized in branch form and therefore would be unaffected by the pending measure.

Mr. BUSH. But the funds come back to the country in taxes in the amount of \$2,200 million.

Mr. GORE. Insofar as branch operations are concerned, there is no tax favoritism. There is no tax incentive involved either with respect to the export of capital or the retention of earnings abroad.

The figures which the able Senator has cited have been frequently cited.

Mr. BUSH. They include the return of branch office income.

Mr. GORE. Yes. It represents approximately half of the amount.

Mr. BUSH. Yes. I am glad the Senator brought out that point. However, it would not change the fact that both the branch office and the foreign corporation are established for some other reason beside tax incentives. Does the Senator see my point?

Mr. GORE. I do. I concede the validity of it. I have never contended that American business has been moving abroad solely because of the tax incentives which our laws provide. But I suggest that it is a very important part and may often be the determining factor—the incentive added on top of the other inducements—in bringing about a decision for such migration of our industry.

Mr. BUSH. Mr. President, will the Senator yield?

Mr. GORE. I yield.

Mr. BUSH. As the Senator has pointed out, the fact is that approximately \$2,200 million comes back from branch office operations, which certainly is a strong indication that there is no great incentive to incorporate abroad in order to isolate such earnings or to defer tax liability on them.

If the Senator and I were going into business together, starting a corporation, and we planned to operate abroad, we would certainly want our earnings to come back to this country because, as stockholders, we could not get them until they were returned to this country. Is that not so?

Mr. GORE. I think the Senator has overlooked a fact of which I know he is aware, and will recall when I bring it to his attention. The mineral and petroleum operations have the advantage of percentage depletion in U.S. tax law. Therefore branch operation happens to be more favorable to them than foreign subsidiary operations. The Senator has made a point that certainly is worthy of consideration—the fact that some income is brought back to the United States from foreign investment.

There have been times when it has been in the interest of the United States to maximize U.S. private investment abroad. I believe that during the post-World War II period in Western Europe it was definitely in our national interest to help rebuild the war-torn economies. There come times, however, both with respect to regions of the world and countries in the world, when it is no longer in the interest of the United States to maximize our private investment in foreign countries. I call particular attention to the present situation in Western Europe, where the rate of economic growth is more than twice the rate of growth in the United States, and where unemployment is no problem.

In fact, countries in Western Europe are importing labor from other continents.

Mr. BUSH. That is correct.

Mr. GORE. So, irrespective of the inflow of income from branch establishments, and even though the income from our investment in foreign subsidiaries were equal to the capital outflow, it still would not lead me to conclude that under present circumstances it would be in our national interest to permit a tax subsidy for such investment to stand, particularly in Western Europe.

Mr. BUSH. I should like to ask a further question.

Mr. GORE. May I make one additional point?

Mr. BUSH. Do not let me forget the question.

Mr. GORE. I shall make a note.

Mr. BUSH. I will write it down.

Mr. GORE. I point out that there is one further question to consider with respect to the point of view which the Senator has suggested that has a great deal of validity. The inflow of income on an annual basis is from an accumulation of investment made throughout the history of our country.

Mr. BUSH. Which amounts to approximately \$50 billion.

Mr. GORE. Yes. So the annual income from an accumulated investment of 150 years is hardly comparable to the yearly investment or outflow of capital. It must be considered. But the fact that this inflow is from the accumulation of investment during all of our history is being suggested as a measurement against the outflow for 1 year. The outflow for 1 year, therefore, assumes far greater proportions when it is realized. I yield.

Mr. BUSH. I agree with that statement. I think the \$2,200 million of income returned from oversea investments relates itself to an investment of approximately \$50 billion over a long period. Perhaps it would not be 150 years, but maybe 50 years.

Mr. GORE. Throughout our history, whatever it is.

Mr. BUSH. My question of the Senator, which I have written down, is as follows: I ask the Senator to assume that the figure of \$2.2 billion is correct. It is approximately correct.

Mr. GORE. For the sake of our discussion, let us assume it is correct.

Mr. BUSH. Let us assume that it is. Let us assume further that the Senator is correct in his assumption that half of it comes from unincorporated sources in Western Europe, including branch organizations, and so forth.

Mr. GORE. The Senator—

Mr. BUSH. Let me complete my question. I almost forgot it previously.

Mr. GORE. Senators are noted for their assumptions.

Mr. BUSH. At any rate, we agree that those figures can be used for that purpose. I ask the Senator, What percentage would the \$1.1 billion, which we are assuming comes from corporate sources in Western Europe, but owned in this country, bear to the total corporate income of corporations owned by the United States in foreign countries? Does the return of \$1.1 billion relate to total

earnings abroad of \$2 billion or \$3 billion, or does the Senator have any figures on that?

Mr. GORE. I am advised by my staff that last year there was reinvestment by foreign subsidiaries of about a billion dollars of retained earnings, plus about a billion and a half dollars of new capital outflow, plus the depreciation allowances, which added up, last year, to the investment of capital abroad of approximately \$4 billion.

Mr. BUSH. Are the figures which were given to the Senator by his staff related to corporate earnings abroad, or are they the total earnings abroad?

Mr. GORE. That was the total.

Mr. BUSH. The Senator is addressing himself to the corporation's advantage that may be enjoyed. What I am wondering about—and I do not know—and if I did, I would tell the Senator—what I am wondering about is how much more corporate earnings by American-owned corporations were there than the \$1,100 million returned last year, if the Senator's figure is correct with respect to the \$1,100 million. Is that 50 percent or 25 percent or the corporation's earnings over there of the American-owned corporation? What I am trying to get at is how much of an influence is this supposed tax advantage that the Senator is talking about? How much of an influence is that in corporations keeping their earnings abroad? Is it 50 percent, or is it 25 percent?

I do not see any great advantage to American corporations building up earnings in Europe through efficient operation and through more profitable cost conditions than here, unless these earnings can be repatriated and paid out in dividends to American stockholders.

Mr. GORE. The Senator has asked a very good question, for which an accurate answer is very hard to provide, because of inability of even our Government to obtain complete information. From the manufacturing profits reported by American foreign subsidiaries, approximately 50 percent was returned to the United States. However, this is not a reliable figure. I say that because this is 50 percent of the book profits remaining to the subsidiary manufacturing corporations from operations within particular countries after a great deal of the income from the operations of such corporations have been bled off or funneled into tax havens subsidiaries in tax haven countries. Only 15 percent of the profits of American corporate subsidiaries in tax haven countries was repatriated to the United States.

Unless the U.S. Government has access to the books and to the records and the accounting procedures of the various foreign subsidiaries and the foreign subsidiaries of subsidiaries and the contracts between the two or more foreign subsidiaries operating in different countries, it is impossible to arrive at an accurate answer and to have a recapitulation of the total profits, and what part of those profits are repatriated.

As the Senator knows, some countries, such as Switzerland and Liechtenstein and other countries, have antieconomic espionage laws, and if a U.S. revenue

agent were to go there and try to obtain information about an American-owned foreign subsidiary, the agent might find himself thrown into jail very quickly.

Mr. BUSH. I would say to the Senator that I am not defending any tax-haven operations, and I know the Senator is not either.

Mr. GORE. I know that. I was pointing out to the Senator how interlocked and interwoven foreign manufacturing subsidiaries are with foreign tax-haven subsidiaries. Because of that fact I am unable to give accurate information; nor does our Government have an accurate answer to the Senator's question.

Mr. BUSH. The Senator did give me one statement that helps me somewhat. He said he thought about half of the earnings were repatriated.

Mr. GORE. About half of what is left after a substantial portion of the profits have been diverted into tax-haven subsidiaries.

Mr. BUSH. Then that does not help me.

Mr. GORE. I agree it does not. It disturbs me, because these tax-haven abuses are very great, and they have an economic meaning that is harmful to the United States.

Mr. BUSH. May I just make one more observation to the Senator? I do appreciate his patience and his attention to my questions.

Mr. GORE. I appreciate the opportunity, since I have been in the Senate, of visiting with the Senator personally and debating questions with him frequently. We have often been on opposite sides. I was highly pleased and honored that the Senator followed my rather laborious arguments on the question of the expense-account amendment.

Mr. BUSH. I did more than that. I voted with the Senator.

Mr. GORE. I was coming to that. After the Senator had followed my arguments, he voted with me. I am grateful to him. I speak in all sincerity when I say that the departure of the distinguished Senator and his lovely wife will be a great loss to the Senate and to the U.S. Capital.

Mr. BUSH. I certainly appreciate the Senator's very friendly comments, and I reciprocate thoroughly his feeling of friendship.

I have one final question I should like to ask, and then I will let the Senator proceed with his remarks, because I see that he has further text before him.

Mr. GORE. Oh, yes; I have.

Mr. BUSH. Going back to my earlier point, as to the relative attractiveness, that of taking so much of our industry to other countries, including Europe, particularly, my own State of Connecticut has suffered from that considerably. I do not like it, because it has resulted in considerable disemployment in our State. As I have gone into this matter with the manufacturers in my State, I have found that the controlling element for their going over and buying a plant or building a plant and going into the manufacturing business over there has been cost, particularly labor cost, where

the cost differential in labor alone is a difference of 60 cents an hour in the Common Market countries as compared with \$2.30 an hour, which is the national average, or was last year, in this country for manufacturing operations. That cost figure, plus other cost advantages, including local taxes and power and so forth, has attracted our industries overseas. I have never had one of these manufacturers say to me that it was the tax advantage or the tax deferral advantage that was a part of the reasoning in going over there.

They want to bring their earnings back to their stockholders. I cannot believe that the tax deferral has been as much of an incentive in attracting modern industry over there as these other cost factors have.

I thank the Senator for letting me discuss this matter. I know he does not agree with me fully. I hope he does see that these other cost advantages are very attractive to our people. Therein lies, in my judgment, the problem that we face. I do not like to see a continuing exporting of jobs, as the Senator calls it, quite correctly. I do not like to see it. However, I question whether the pending tax bill, no matter what we do, is going to have as much to do with that as I would like to have it do, because I would like to see this trend change. I thank the Senator very much.

Mr. GORE. I thank the Senator. He has brought up a point that certainly needs discussion. I have never contended and I do not now contend that there are not several other circumstances which operate as an incentive to the establishment of American industry abroad and the investment of American capital abroad and in some instances the actual movement of American factories abroad.

Before going further, I should like to observe that I doubt whether there is any other country which would for very long, against its own national interest, permit its individual or corporations to move whatever capital they desired or whatever factories they desired to whatever country they desired purely for their own benefit.

Mr. BUSH. The Senator is quite correct. Many of the countries he has mentioned this afternoon absolutely forbid such movement or limit it very severely.

Mr. GORE. At a dinner party one evening not long ago, I was quite struck by a conversation I had with my partner, who was the charming wife of a noted industrialist from another country. I inquired of her under what conditions her husband or her husband's company could invest in Brazil. I believe she spoke of some investment they had there. The information she gave me was that that decision could not be made by him or his company alone; that he must apply to his government; and that permission to export capital to Brazil or to any other country would not be given unless the government first determined that such an operation would serve the interests of their country.

Mr. BUSH. That is correct.

Mr. GORE. His own individual welfare would be secondary. I am glad the Senator from Connecticut agrees with me in that regard.

Coming to the broader point which the Senator raised, I should like to read a paragraph from a statement by a representative of the H. J. Heinz Co., which appears on page 2538 of part 6 of the hearings. Before doing so, and because I find it difficult otherwise to discuss in an intelligible way a table on that page, I ask unanimous consent that the table which appears on page 2538 be printed at this point in the RECORD.

There being no objection, the table was ordered to be printed in the RECORD, as follows:

	U.S. companies ¹	Foreign companies ¹
	Percent	Percent
Sales.....	100	100
Cost of sales.....	60	67
Gross profit.....	40	33
Selling, general and administrative expense.....	34	22
Operating profit.....	6	11

¹ These percentages have been rounded to the nearest full numbers and the dollar figures on which they are based are determined by converting foreign currencies at exchange rates at fiscal year end and are influenced by minor technical accounting consolidation eliminations. However, the percentages are essentially correct for the purpose under discussion.

Mr. GORE. As the Senator from Connecticut will note, the table shows that the cost of sales, which includes labor, of the U.S. companies owned by H. J. Heinz Co., is 60 percent of sales, while the cost of sales of foreign companies owned by H. J. Heinz Co. is 67 percent.

When we come to selling, general, and administrative expense, as the Senator will see, the cost in the United States is a much greater percentage of sales.

The operating profit abroad is almost double; and this, I point out, is not due to lower production cost, but to lower sales and administrative cost. Now I shall read the paragraph which follows the table:

These percentages indicate quite clearly that our foreign business is almost twice as profitable (at the operating profit level) as is our U.S. business. Foreign companies' cost of sales are higher than comparable U.S. company costs (by 7 percentage points), but selling, general, and administrative expenses of foreign companies are substantially below similar U.S. cost items (by 12 percentage points).

As the Senator will note, this belies the general statement, which we hear so often, that foreign labor costs are so much greater. The truth seems to be, certainly in the case of this company, that the productivity of foreign labor is so much less than the productivity in the United States that the per-unit cost of production is greater in the foreign plants. It is the overhead administrative costs which are higher in the United States.

Mr. BUSH. Will the Senator permit me to observe that I think the H. J. Heinz Co. is a very interesting illustration.

Mr. GORE. I am not sure it is generally applicable.

Mr. BUSH. My point is that I am sure it is not general, because manufacturing operations with which I am familiar in my own State of Connecticut have quite the opposite figures to show, so far as the cost of doing business is concerned. I do not know how H. J. Heinz does so poorly overseas on the cost of sales, but obviously they do. I think it is surprising also that other costs are very much lower than they are in Connecticut. That is a very interesting table, but I do not believe it is conclusive.

Mr. GORE. I do not cite it to the Senator as evidence of a general conclusion. As the Senator has said, other situations would produce different figures. However, there are many more which would show a similar pattern. But I cited this example to demonstrate that we cannot race unquestionably to the conclusion that foreign labor costs are always a big incentive for the movement of American industry abroad.

Mr. BUSH. No; but they are an incentive for industries whose labor cost is a high percentage of the total cost. That is not true of the Heinz Co., whose product is automatically placed in cans by machines. In that kind of operation labor is not a high percentage of the total cost. In that kind of operation, where there might be better technical equipment or more advanced machinery for the type of work that needs to be done, there would be a cost of operation preference.

But many American industries which establish plants abroad are protected by the cost differential, because in the manufacturing of their products in this country the labor cost is a high percentage of the total cost. I do not know how we can appraise exactly which companies experience such a high labor cost or what percentage that cost is of the total.

Mr. GORE. I agree.

Mr. BUSH. I think a point to be remembered is that it is not only a tax incentive or a tax deferral incentive which causes the establishment of plants abroad. I do not believe, really, that that is the big thing, or one of the big things, which influences American companies to establish plants abroad. I do not believe that was what influenced H. J. Heinz Co. I think they established their foreign plants in order to expand their markets and increase their business, and they decided they could make money by doing so, as their own figures show they are doing.

Did the Senator gather in talking with the Heinz representatives that the tax incentive was an important factor?

Mr. GORE. The Senator's question raises a point on which I have some feeling. Mr. H. J. Heinz appeared before the House Ways and Means Committee and testified on behalf of 19 selected companies. They were selected, I think, because of the relatively large amounts of their earnings which are returned annually to the United States. His statement was carried widely by the press,

and many persons seemed to rush to the conclusion that the experience of these 19 companies was typical of that of all American investments abroad.

After doing a great deal of work on this matter, I found some very large loopholes in his testimony. The Treasury Department found more. The Senate Finance Committee invited Mr. Heinz to testify before it; and I telegraphed to him and requested him to testify. But, for some reason, we never were able to get Mr. Heinz to testify before the Senate Finance Committee and defend the statement he had made.

In fact, his statement did not represent a typical cross section of repatriation of the earnings of American investments abroad.

Mr. BUSH. Did his testimony show that there was a reasonable repatriation of the earnings?

Mr. GORE. For the 19 companies, the showing was rather remarkable. But upon close examination it was found that theirs constituted mature investments which up to that date had not, in the case of the larger companies involved, gone very heavily toward the tax haven operation.

But I am sorry to report to the Senate that the H. J. Heinz Co. is now moving into a tax haven operation.

I should like to read a paragraph from a memorandum from Mr. Heinz. When I was unable to get him to testify, I submitted a memorandum to him, and he supplied an answer—not in person, but in writing. I read now from page 2539, volume 6 of the hearings, the second paragraph following the table:

Our Swiss subsidiary company was established in fiscal year 1961 and is in charge of a full-time executive domiciled in Switzerland.

I note he refers to only one employee. That is rather typical. But profits from manufacturing and from sales all over Europe or perhaps in other parts of the world may well find their way into the coffers of that subsidiary in Switzerland in future years. Let me say this is rather typical.

I should read the entire paragraph, I suppose, in fairness. It reads as follows:

Our Swiss subsidiary company was established in fiscal year 1961 and is in charge of a full-time executive domiciled in Switzerland. This company was organized for the purpose of investigating, organizing, and administering foreign business opportunities primarily in the Common Market area. To date this company does not have any earnings, but we hope that over the next 10 years it will become as profitable as have our other subsidiary companies and will be paying taxable dividends and fees to the parent company as do our other longer established subsidiaries.

Mr. BUSH. That does not sound bad, to me.

Mr. GORE. It shows that the company has established a subsidiary in a tax-haven country. What he will do with that tax-haven operation in the next 10 years, I do not know. Perhaps that will be affected by what we do with this tax bill. But I wanted to point out that although this company had been returning to the United States a sizable amount of earnings from matured invest-

ments, now it has established a subsidiary in a tax-haven country.

This creates some interest on my part, because we had testimony from a leading U.S. drug concern which showed a rather favorable return to the United States. The going rate of this company was about at the 50-percent mark. But then a witness for another concern testified; and his competitors listened to him. He showed an effective tax rate for his company—or, rather, I had the figures to show it; and when I asked him the questions, he certified that the statistics I had were correct. They showed a tax rate of only about 30 percent for some years.

When the testimony had been completed, one of the gentlemen—whom I should not like to identify—came up and talked to me privately. He said, "We are just catching on, and we are establishing subsidiaries in tax-haven countries."

I say to the Senator from Connecticut that this is happening in thousands of instances.

The Senator from Connecticut has referred to some of his constituents who have moved abroad, and he has referred to the reasons they gave him for doing so. He has not identified them, and I am sure he would not want to do that. I shall now refer to one of my own constituents who talked to me confidentially, and whose identity I would not like to reveal. His company is quite successful. It has a nationwide retail network in the United States, selling well-known American-brand products. He told me that he had made arrangements to manufacture and import from 23 countries products bearing the labels of American brands. We talked about the tax situation; we discussed it fully and frankly. He said, "You can't blame me for taking advantage of it as long as you fellows leave it in the law."

I said, "No, I cannot."

He said, "I am not breaking any law."

I replied, "No; and I am not saying that you are breaking any law."

But I say to the Senator from Connecticut that this tax incentive for the movement of our industry abroad is what I want to try to eliminate.

I should say, in all fairness, that my constituent did not say that the tax situation alone had caused that decision to be made. He also referred to other factors. He referred to labor costs; and he referred to the incentive of having a factory built for him by another country, as a subsidy. But the tax incentive was a part of the reason. As I have said to the Senator from Connecticut, I do not know what part it is, but it seems to be a significant part. I want to remove that part, because we simply cannot remove the others.

Mr. BUSH. I thank the Senator from Tennessee.

Mr. GORE. I wish to read to the Senate a portion of an article entitled "Jurisdiction to Tax and International Income," written by Martin Norr, who is a member of the Massachusetts and New York bars, Research Associate and Editor, World Tax Series, Harvard Law

School, International Program in Taxation. I am reading from page 458:

Winston Churchill pointed out that countries are judged by their national performance. In the tax field our national performance is not everywhere well regarded. The effect of anti-tax-haven legislation on the American image abroad may be salutary. We must recognize that there is an image abroad of the American as a tax avoider. Last summer the writer got out of a car at Sodom on the Dead Sea with two British tax lawyers and a Swedish national. Looking at the panorama of ancient desolation, one Englishman whispered to the other: "Good place for Americans to set up a base company."

In other words, a good place to set up a tax haven.

Not long ago I was invited to make a speech, which invitation I accepted. My host for the evening was an eminent businessman. We were discussing this subject, and I soon found he was not in full agreement with my point of view. So, to illustrate my concern, I said to him, "You know, there is a little place in Switzerland called Zug, about which I never heard until I learned a few days ago that within the last few months 45 American corporation subsidiaries had been established there." He said, "Well, now, Senator, if you are going to refer to that, it is called 'Zoog.' It is where one of my subsidiaries is located."

Mr. BUSH. Mr. President, if the Senator will yield, I do not know what the implication of that is, but presumably the implication is that they are going over there to avoid paying taxes.

Mr. GORE. He frankly admitted it.

Mr. BUSH. I assume that is the reason, because there is nothing else to attract them to those places.

Is it not also true that companies incorporating for business will go from Tennessee or Connecticut to Delaware in order to take advantage of the tax laws incident to incorporating in Delaware, as distinct from Illinois or Ohio or other States? So the establishment of a base of operations for corporate purposes, if it be established in some other place than where the company does business, does not necessarily connote guilt or an offense, but connotes only a desire to take full advantage of what the tax laws are. In other words, they do not go there to do something wrong. They go there to take advantage of what may be there in the way of escaping, if you will, the disadvantages which may exist by locating elsewhere. We see that done in our own country by reputable corporations. They do not incorporate in New Hampshire or Vermont; they go to Delaware. I do not know the attraction of Delaware. Perhaps I did at one time, but I have forgotten. I cite that as an example of the fact that it is not unusual for corporations to incorporate in another State than their own. Therefore, it should not be considered unusual if they are doing business abroad, if they find a place where it would be most advantageous to them to locate.

I want to say in conclusion, lest I leave the Senator in any doubt, I am not seeking in any way, any more than the Senator from Tennessee is, to protect

any company or any individual who is doing anything wrong in avoiding the payment of just taxes in the United States. I fully commend the Senator for his zeal in attempting to close any loophole that exists for that purpose.

I do not think that one can jump suddenly to the conclusion that there is something wrong with a company just because it will open up an office in Switzerland, as the Senator pointed out Mr. Heinz did. Mr. Heinz explained that they did it for certain purposes. I do not think it is fair to assume that the reason why he did it was for a tax avoidance purpose.

Mr. GORE. I readily agree that we are not dealing here with a matter of criminality. I have never endeavored to deal with it here in that light.

Mr. BUSH. I do not mean to bring that word into it, but I suppose anyone who avoids the payment of just taxes is a criminal.

Mr. GORE. Generally speaking, evasion is regarded as a crime. Avoidance may be a broader term. So long as the avoidance is within the law, it is not a crime, although I am not sure that all tax avoidance can be entirely excused, and that one can say it is not wrong to avoid taxes. Sometimes there are advantages taken, such as was illustrated in the subject matter we discussed yesterday, in the case of an expense account where a personal expenditure is clothed, deceptively, in a business function.

I cannot say that all tax avoidance, though it may be within the clear confines of the law, is not wrong. I think there is a moral question involved, and there is a question of degree; but at least in the case of taxation of foreign subsidiaries, I have never sought to deal with the problem from the standpoint of tax evasion. I have never sought to deal with taxation of income earned by American citizens in foreign countries as a matter of right or wrong. I have tried to deal with it as a matter of public policy.

It seems to me that if our national economy is being injured, as the Senator's State has been injured—

Mr. BUSH. The Senator is correct.

Mr. GORE. By the movement of factories to foreign countries, then, to the extent that we can do so, within our jurisdiction, we should eliminate those advantages which our own law provides for such migration of business and jobs and capital.

I do not propose that we stop it. I merely propose that American tax laws be placed in a position of neutrality. A survey has shown that reinvestment of foreign earnings over a 3-year period can provide "roughly double the rate of profit accumulation for reinvestment that is possible under domestic tax schedules."

Mr. BUSH. Because of lower taxes overseas?

Mr. GORE. Yes.

Mr. BUSH. But what good would that be for the American stockholder, to keep the money overseas?

Mr. GORE. His assets would be of much greater value. There are numerous instances in which foreign cor-

porations, after a period of years, with an accumulation of profits, have been collapsed or otherwise made liquid, and the money brought home at capital gains rates.

Mr. BUSH. They sell out overseas?

Mr. GORE. They are collapsed or otherwise become liquid.

Of course, there is another situation which I am glad to say the pending bill would correct. Under the present law foreign real estate is completely exempt from U.S. estate taxes.

Mr. BUSH. Yes. The bill would close that loophole.

Mr. GORE. Fortunately, the bill would close that. I am not one who is willing to say that the bill does not have some good features, for it does. I am pointing out that is one of several ways in which accumulated earnings may inure either to the original investor or to his heirs at a very low tax or, in some instances, at no tax at all.

Mr. BUSH. I should like to ask the Senator a final question. Has the Senator or the committee received testimony which supports his statement that they might collapse an oversea operation, or sell out, so as to bring the profits of years—10 or 20 years, or whatever amount is involved—to the United States in the form of capital gains?

Mr. GORE. Yes. The evidence is that is widespread.

Mr. BUSH. The committee does have that testimony?

Mr. GORE. The committee does have evidence on that.

Mr. BUSH. I thank the Senator.

Mr. GORE. I thank the Senator for his interest and attention.

Mr. President, in conjunction with considerations of competition, it is bad enough when foreign corporations set up by our own people begin to displace our export markets, but it is even worse when they begin to export back into our own country. The cruelest competition which an American producer can be forced to undergo is competition from American-type goods with well known American brand names, produced abroad by American-owned subsidiaries which have achieved rapid growth because of the ability to dodge U.S. taxes and plow back practically all earnings, with these products distributed throughout this country through a well-established chain of wholesale and retail outlets.

It is all very well to want to assist other countries, but the crying need right now is to build up our own economy. We do need to continue to render appropriate assistance to underdeveloped countries, but certainly the wholesale shipment of factories to Europe must be slowed down.

We still have a long way to go to reach full employment and production. We are not going to reach this goal by giving our domestic corporations a tax cut which the Senate voted on Tuesday to do—and the fact that this tax cut is computed on the basis of certain plant and equipment purchases does not at all mean that it will influence in one iota the amount or types of such purchases—

if at the same time we continue to encourage them to move overseas.

We need to stop this hole in the bottom of our economic bucket through which our economic potential is pouring to other countries. We must do this before or in conjunction with whatever other steps we may take which we hope will build up our domestic economy and improve our international economic position.

Sales by U.S.-controlled foreign factories in 1960 amounted to about \$24 billion, up about 29 percent from 1957.

Our Commerce Department has estimated that expenditures for plant and equipment abroad by U.S.-controlled foreign operations will amount to about \$4.5 billion this year, including new capital sent abroad from the United States plus earnings and depreciation allowances plowed back. How many new jobs would such expenditures, added to our normal expenditures for domestic plant and equipment, create here at home? I have no satisfactory yardstick with which to measure this, but we are surely shipping many thousands of jobs overseas every year.

When this subject comes up, many will invariably advance the argument that our foreign operations assist our domestic economy because of the increased sales of exports which our activities overseas generate. As in the case of most arguments, there is some truth in this one. One needs to know just how much truth there is in it. The answer is, it is just about 10-percent true.

There are four general types of oversea investment. Each must be viewed in a different light insofar as its effects on the domestic economy are concerned. These are:

First. Sales promotion: This is the first type of foreign activity to be discussed by most of those who would defend our present lax tax laws regarding foreign operations. Those who rush to the defense of the tax status quo argue, first and foremost, that to tax foreign operations equitably would destroy this type of activity overseas and thus ruin our export business and harm our domestic economy.

A strange and baseless argument.

In the first place, this type of activity accounts for only 10 percent of our foreign direct investment. In the second place, this type of activity exists, or should exist, because of the profits it can promote for the factory in the United States, not for the profits the sales activity itself can earn in a foreign country. The tightening up of taxes on this small sales activity would not disturb or lower the profits of the major activity which is, after all, located in the United States.

The type of tax reform I am talking about would not harm our foreign sales activities.

Second. Raw materials and supplies: This type of activity now accounts for about 42 percent of direct foreign investment. By and large, these operations do not harm the domestic economy. In fact, they are decidedly of assistance. This is where we get 54 percent of our minerals, metals, and semi-finished im-

ports. These operations ship very few jobs out of the country. These operations probably do us more good than they do the host countries.

But what is of importance vis-a-vis taxation is that these operations are not particularly encouraged by our faulty tax laws. Being in the extractive field, these enterprises are set up so as to take advantage of our very generous depletion allowances. They are, therefore, usually organized as branch, rather than subsidiary, operations and repatriate earnings annually on which they pay the regular U.S. rates, less the credit for foreign taxes paid. The changes in the taxation of foreign operations which I am now advocating would have little bearing on the taxes of branch operations and, therefore, little effect on this segment of our foreign private economic activity.

Third. Public utilities, transportation, and banking: This type of foreign activity might be curtailed somewhat by tightening up on foreign taxation, although I doubt it. At any rate, this accounts for only 15 percent of our direct foreign investment, and this percentage is declining. These are types of activities, also, it might be noted, which lend themselves readily to nationalization.

Fourth. Manufacturing: This is the activity which hurts. It is also the activity which would be most affected by tightening up our foreign tax laws.

Manufacturing already accounts for 33 percent of our direct foreign investment and is the fastest growing segment. In Western Europe 75 percent of our direct investment has gone into manufacturing—in the United Kingdom, 85 percent. It is this type of foreign investment which hurts our domestic economy and contributes to our balance-of-payments deficits.

Since this type of activity is usually organized as subsidiaries, and since it often is associated with tax havens, there is less current repatriation of earnings. This is where the deferral privilege, the credit, the gross-up and the tax haven sales hook-up really pay off. Changes in these areas of taxation would slow down—although this would not stop the movement of enterprises drawn abroad legitimately—the wholesale movement of manufacturing plants to Europe.

EFFECT ON BALANCE OF PAYMENTS

A great deal has been said about the balance-of-payments problem in the last 2 or 3 years. In fact, it is currently one of the most fashionable topics of conversation. I must say that it is somewhat misunderstood, even by many who are directly concerned with its solution.

As with so many other problems in this country, the balance of payments is not an absolute but a relative problem. There are several ways by which we might solve the problem, or at least greatly lessen it without serious damage to our domestic economy or our ability to compete in the markets of the world. Some solutions, however, are not compatible with broad national policy.

Many countries, on the other hand, have an absolute problem with their balance of payments. Many countries must import large quantities of important

items. These may be raw materials and fuels, or they may be manufactured products beyond the capability of the local economy. Furthermore, domestic consumption must often be curtailed in order to get together enough goods for necessary exports. In such cases there is generally a low level of gold, dollar, or sterling reserves to fall back on. The balance of payments, then, becomes a problem which must be resolved year by year on an absolute basis. If the solution is not forthcoming within a year or two, the economy will collapse and a political upheaval will be inevitable.

Our problem is not of this sort, as I have said. We could cut off the flow of private funds abroad through different types of controls, direct or indirect. We could reduce military expenditures overseas by bringing troops home, by bringing dependents home, or by reducing oversea purchases for their maintenance. We could reduce our foreign aid. We could refuse to allow tourists to carry dollars out of the country. We could refuse to make pension or social security payments to anyone who moved outside the country. We could reduce imports by instituting licensing controls such as those which are in force in many countries. We could increase exports immediately in several ways—by subsidies, for example.

But there are reasons, perhaps good ones, for not doing these things—at least not to an extreme degree. Steps we take along these lines must be taken with a view to the welfare of our friends and allies and to the overall strength of the West as well as to strengthen our domestic economy.

We have taken some reasonable steps in recent years to take up some of the slack in our balance of payments. We can do more in this regard and still not damage our domestic economy and our western allies. But certain steps are more productive of good and less productive of harm than others.

The great emphasis now is on increasing exports, and this is all to the good. There are limits to such increases, however, without also increasing imports. It would seem that we will have difficulty in maintaining a favorable balance of trade in excess of \$5 billion.

But we must find a way to reduce our balance-of-payments deficit by about \$2 billion per year. I doubt that increased exports can carry the burden alone. In my view, we could reduce our deficit materially by tightening up on our taxation of foreign operations.

Although we talk a great deal about the balance of payments, and everyone is concerned, we still do not know enough about the subject. Even our statistics are not much better than informed guesses as to what is actually going on. It appeared last year that we were doing very well—up until the fourth quarter. It is possible that there is something wrong with the fourth quarter figures. It is just as likely that there is something wrong with the figures for the first and second quarters of 1961. We simply do not know.

There are at least two things we do know about our balance-of-payments

figures. First, much of the short-term investment flow that we classify as "hot money" seems not to come back. Both the fourth quarter of 1960 and 1961 showed abnormally high flows of such funds. A lot of it never shows up as coming back—at least not in the same form. I am convinced that much of it gets overseas and is converted there into long-term investment of one kind or another.

This is not just a wild guess on my part. Many who are knowledgeable in this field think that a good part of what we classify as short-term investment going abroad is really long-term. It gets abroad and never comes back. In this connection, there was a very good article in *Business Week* on February 25, 1961, on this very point. According to this article:

U.S. corporations that found themselves last year with more cash than they cared to invest in the slack domestic market moved funds abroad as a preliminary to long-term investment. Such movements sometimes had a short-term air, because money was put into short-term European securities while waiting for a long-term opportunity.

Second, it is not possible to know very much about any set of figures when such a large "errors and omissions" item is necessary to make debits and credits balance. This balancing "errors and omissions" figure for 1960 was 20 percent. For 1961 it was about as bad.

In my opinion, we do not know as much about our true balance-of-payments position and what really causes it as our tables would lead one to think. I think it likely that our capital outflows of different types have been understated in recent years.

That we do not know very much about what is going on is readily admitted by our Department of Commerce people who are supposed to keep up with international transactions. Here is an excerpt from the June 1962 Survey of Current Business in an article discussing the recent trends in the balance of payments.

A large part of the improvement in the overall balance cannot be explained from the data so far available. The balance on unrecorded transactions shifted from net payments of \$565 million in the last quarter of 1961 to net receipts of about \$260 million in the first quarter of this year. A part of the \$825 million shift can be attributed to seasonal factors, but even after adjustment for these the shift amounted to about \$620 million from net payments of about \$400 million to net receipts of about \$220 million.

Although this shift reversed an almost equally large shift from the third to the fourth quarter of 1961, the prevailing tendency of unrecorded transactions still seems to indicate an excess of payments. The net receipts balance for the first quarter of 1962, therefore, seems to reflect some special circumstances, which may have led to unrecorded inflows of foreign funds or repatriations of American capital.

I think at this point I might say that the Congress should be somewhat critical of the Department of Commerce for not keeping up with balance-of-payments statistics and foreign investment properly. Those individuals who are supposed to keep up with investment flows simply did not have the authority to go out and get the information. It was

not until April of this year that the Department began to require reports on international movement of funds by U.S. corporations, even though we have had a law authorizing such a requirement on the books since 1945. Only one really good study has been made of investment flows and foreign investments, and that was for the year 1957. Even this was not published until 1960.

Be that as it may, we must try to analyze the situation on the basis of such statistics as we have, uncertain as they are. We do not know how much gold we are losing and how much our liquid liabilities to foreign countries and international institutions are increasing.

We do know something of the part which is being played by private overseas investment. We know something of its effect on our domestic economy as well as on our balance of payments. Many are not yet willing to acknowledge the role which is being played by the rapid buildup of U.S.-owned manufacturing facilities in Europe in the sluggishness of the domestic economy and the deficit in our balance of payments. We must examine this matter closely and take such action as is in the public interest.

One thing which that 1957 study by the Commerce Department did show, however, was the lag in repatriation of earnings from manufacturing activities abroad, that is, from subsidiary operations. About one-half of our receipts from direct investment overseas in 1957 was from petroleum operations. Only one-fifth was from manufacturing. But one-third of our investment is in manufacturing, and the profits are said to be large—at least it is claimed by those who are going there that the profit margin is considerably higher in Europe than in the United States. This shows conclusively, it seems to me, that earnings from manufacturing abroad are not being repatriated as are earnings from some other types of investment. One reason is that our tax laws allow deferral for subsidiaries. In branch form, as is the case with petroleum and mining generally, there is more repatriation. Removal of the deferral privilege should help us to repatriate more funds from manufacturing and thus clear up a part of our payments deficit. The other, and associated, reason for lack of repatriation lies in tax haven operations.

Last year, Secretary Dillon made a very forceful presentation to the Ways and Means Committee on the need for tightening up on the taxation of foreign activities. Particularly useful were the figures which he used showing the breakdown of investment and dollar flows by geographical areas and types of activities. His figures showed an absolute deficit on European operations. I am sorry to say that his presentation has been attacked on the basis of figures of an altogether different sort furnished by certain other witnesses before the Ways and Means Committee.

THE HEINZ STATISTICS

Mr. President, I have already referred to Mr. Heinz' statistics, but I should like to go into that subject now in more detail.

Despite some pretty good statistics which Secretary Dillon got together and

presented, the testimony presented by some witnesses who have come before the Ways and Means Committee and the Finance Committee has sought to show that all types of foreign activities, tax haven ones included, make positive contributions to the balance of payments.

Some of the testimony presented strains credulity. In fact, some of it is so incredulous that certain witnesses refused to come before the Finance Committee in person to defend their statistics and line of reasoning.

One of these bits of questionable testimony was presented to the Ways and Means Committee by Mr. H. J. Heinz II.

There are several things wrong with this testimony. I have tried diligently to get points of interest cleared up, and have been totally unsuccessful in getting Mr. Heinz or anyone else to come before the Finance Committee and defend or even explain this whole procedure.

It would appear that this 19-company group represented by Mr. Heinz had its origin in the International Chamber of Commerce and that companies were selected for the good showing which they could make for the period under review. Taking the most charitable view of the matter, these companies are wholly unrepresentative of those which have been responsible for the vast increase in tax haven operations which have sprung up in the last 5 years. These companies have, by and large, mature foreign investments.

Mr. Heinz said that he represented 19 companies in compiling and presenting his statistics and that these U.S. corporations represented "somewhat over 5 percent of the total U.S. investment in manufacturing abroad."

These companies are American Machines & Foundry Co., Armco International Co., Cabot Corp., Continental Can Co., Corn Products Co., Eastman Kodak Co., General Electric Co., Goodyear International Corp., H. J. Heinz Co., Merck Sharp & Dohme International, Monsanto Chemical Co., Otis Elevator Co., Pfaudler Permutit Co., Pfizer International, Inc., Ritter Co., Inc., Taylor Instrument Cos., Texas Butadiene & Chemical Corp., The Procter & Gamble Co., and Union Carbide Corp.

Mr. Heinz further states that "the companies" I have just mentioned had asked him to appear "as their spokesman." Mr. Albert E. Sawyer, an accountant, "was retained" to gather the statistical data used.

Did the managers of this group of companies just happen to get together for this purpose? After examining some of the statistics cited, I became most curious to learn just who first retained Mr. Sawyer, who paid him, who contacted the particular companies, and how many other companies' books or statements were examined and discarded because they did not fit a predetermined pattern.

Interestingly enough, these companies seem to have little in common. An odd fact with which one is struck is that, in the case of several of the companies listed, the companies are subsidiaries of a parent U.S. corporation. I wondered whether the inclusion of data for all the

foreign subsidiary operations of the parent U.S. corporations would have altered the pattern.

Armco, for example, has a large operation in Canada as well as other foreign operations which do not appear to be a part of Armco International.

I do not know the reason why each of these 19 companies was selected for this list, or why only these were included. A brief examination raises some interesting questions. For example, the General Electric Co. appears to have repatriated \$7.9 million from foreign earnings of \$8.4 million from its nonconsolidated subsidiaries in 1959. This is a very high percentage of repatriation. Otis Elevator changed its bookkeeping in 1960. As a result its foreign subsidiaries paid three dividends in that one year. Though I do not know whether these untypical facts caused these companies to be included, one can see that if a company is selected which has a large inflow of funds usually, or for one particular year, it would, of course, distort, the statistics for a small sample like this, making the summary or conclusion more unrepresentative and untypical of the general facts.

It was noted by members of the Ways and Means Committee that there had been a sharp increase in the outflow of new money from these U.S. corporations in 1960. Mr. Heinz was asked about this and promised to furnish an answer. So far as I have been able to determine, he never did.

With the knowledge that these figures may present a distorted picture, let us examine them in some detail.

Let us consider, first, dividends repatriated by these subsidiaries. The foreign subsidiaries owned by these 19 companies sent home during the 1957-60 period, according to Mr. Heinz, \$141 million more in dividends than the parent companies sent abroad in new money. Multiplying this by 20, since according to Mr. Heinz these companies represent about 5 percent of U.S. manufacturing abroad, we would conclude that all foreign U.S. manufacturing subsidiaries sent home, during this 4-year period, \$2.8 billion more in dividends than they took out of the country in new money. This is a rather large figure, particularly when we compare it with our official figures. According to our official statistics all our foreign direct investment, branch and subsidiary of all types combined, sent home only \$2.2 billion more than they took out during these same 4 years. Furthermore, as I have pointed out, subsidiaries, at least those in Europe and Canada where our principal manufacturing activities are located, according to our official statistics caused an actual drain on the balance of payments.

Our official statistics appear, as I have said, to understate outflows, but no matter how inaccurate they are, or in which direction, they could not conceivably be this far off. Petroleum alone accounts for half our inflow, yet Mr. Heinz would have us believe that manufacturing subsidiaries contribute billions of dollars on the plus side of the balance of payments through dividends remitted.

To pin this down, let us look at the year 1957. As I have pointed out, we

do have good statistics for that year, based on compulsory reporting. According to these figures for 1957, compiled by the Commerce Department, all our foreign direct investment activities sent home \$2,249 billion in earnings and profits. About half of this came from petroleum. Only about one-fifth of it, or \$429 million, came from manufacturing. Yet Mr. Heinz claims that foreign subsidiaries of his 19 companies sent home in 1957 \$64.8 million in dividends. Extrapolating this figure, one would assume that all manufacturing subsidiaries would have remitted dividends in 1957 in the amount of \$1.296 billion. This misses the mark by a factor of 3.

Mr. Heinz' other figures appear just about as unreliable. He piles on hundreds of millions of dollars in dividends, fees, and exports which he attributes to the activities of foreign subsidiaries of these U.S. manufacturing corporations.

Let us look at the export figures which Mr. Heinz cited. He claimed that these 19 companies, representing about 5 percent of our foreign manufacturing, had exports generated by their own direct foreign investments in 1960 of \$595.1 million. Multiplying this by 20, we would conclude that all foreign direct investment activities of U.S. manufacturing corporations for that year accounted for about \$12 billion in exports. But our total nonagricultural exports in 1960 amounted to only about \$14 billion.

These export figures seem so outlandish that the Treasury Department asked the Commerce Department to try to arrive at some proper comparable figure. The Commerce Department queried our larger manufacturing companies and got replies from 155 of them, accounting for 80 percent of all manufacturing investments abroad. These companies credited their foreign subsidiaries with generating \$2.7 billion in exports in 1960.

To credit almost 90 percent of our nonagricultural exports to the activities of the direct foreign investment activities of U.S. manufacturing corporations, which appears to be the implication of Mr. Heinz' testimony, certainly strains logic. Yet some people seemed impressed.

Yet some persons still seemed impressed. Some of my colleagues in the Senate have spoken to me about some individual company or representative of some individual company who came and showed that his investment abroad helped the United States. Undoubtedly there are individual examples—extremes in both directions. What I am trying to give is a composite, a summary, conclusions, a look at the total picture, and to examine the whole matter, rather than individual examples.

The same types and amounts of exports can be, and are, generated by aggressive selling, by licensing arrangements, or by any other form of exposure of a foreign buying public to American products. For example, Borg-Warner licensed a South African company to produce one of its refrigerators. The licensee purchased from Borg-Warner other types and sizes of refrigerators produced in the United States to round out its line. As a result, Borg-Warner

has increased its exports of refrigerators to South Africa from 600 to 3,500 per year.

There is no more logic in crediting large amounts of exports cited by Mr. Heinz to subsidiary activities than there is in crediting to a wholesaler's retail activities all the goods sold through retail stores which he happens to own directly. The wholesaler might well have sold a larger quantity of goods had he closed his own retail chain and wholesaled to 8 or 10 competing retailers.

It so happens that these companies cited by Mr. Heinz also show a large income from royalties and licensing and management fees. In the case of these companies it is claimed that these fees originate in their own subsidiaries. The implication is that without subsidiaries there are no fees of this sort to be collected abroad by U.S. corporations. This is not at all correct.

Many U.S. corporations collect large amounts of fees of this type from foreign operations other than their own subsidiaries. I do not have a breakdown on these statistics, but I would invite attention to an article which appeared in the Wall Street Journal on June 14, 1961, in which certain companies' licensing arrangements are detailed. It was pointed out in this article that a great many of our large companies use licensing arrangements in preference to setting up foreign subsidiaries. Bendix Corp., for example, is said to have over 400 licensing agreements in effect abroad and to have received about \$2.9 million in royalties in 1960. According to this article there are now more than 12,000 licensing agreements in effect between American companies and foreign companies. In my opinion, a representative list of U.S. companies would show a large amount of royalties and licensing fees originating in foreign companies neither owned nor controlled by an American corporation. It is wholly unjustifiable to bleed any part of these fees off into tax havens.

Now, I am not accusing Mr. Heinz of coming to the Congress with deliberately distorted statistics. Special pleading is not unusual even if that should have been the case. But several points need to be cleared up and I was keenly disappointed that Mr. Heinz refused to come before the Finance Committee to defend and up-date his statistics.

I wrote Mr. Heinz to request some of the information I needed to clear up certain points in my own mind.

Mr. President, I ask unanimous consent to have printed in the RECORD at this point my letter to Mr. Heinz and his response.

There being no objection, the correspondence was ordered to be printed in the RECORD, as follows:

APRIL 17, 1962.

DEAR MR. HEINZ: You will recall that last year you presented testimony to the House Ways and Means Committee, on behalf of some 19 companies, on the tax reform proposals of President Kennedy. Your testimony at that time seemed to have a marked effect on the committee and was widely reported in the press. Since that time, as you undoubtedly know, the House has passed the tax reform bill, H.R. 10650, and this measure

is now the subject of hearings before the Finance Committee of the Senate.

Since your testimony, presented on behalf of these 19 companies, was one of the most important parts of the testimony before the Ways and Means Committee on those proposals relating to the taxation of operations abroad, I had assumed that you would appear before the Finance Committee to go over the same or similar testimony and bring the statistics you presented up to date to include the year 1961. I was keenly disappointed to learn that you will not appear before the Finance Committee.

In view of the fact that you will not appear before the Finance Committee, I wonder if you would be good enough to supply certain information to me for my study in connection with this bill.

First, I would like to know who organized your group. You testified in the name of the Industry Committee on Foreign Investments. Is this a permanent organization? When was it organized, and who are its officers? Who employed Mr. Sawyer? How many other companies' books were examined in the process of selecting these 19 for which statistics were presented? Where was Mr. Sawyer employed in 1960, and where and by whom is he employed now?

Second, I note in your testimony before the Ways and Means Committee, that you were questioned about the large increase in the outflow of funds for investment abroad in 1960 over 1959. You were to furnish an explanation, but had not done so by the time the hearing went to press. I would like this information, and, further, I would like to have figures for 1961 for these companies comparable to those you presented for past years.

Third, a number of the companies in your group have licensing agreements as well as subsidiaries abroad. Could you furnish some comparison of the exports generated by subsidiaries and by licensees. Specifically, I note that Goodyear has what are called manufacturing arrangements in several foreign countries. Are these licensing agreements, and what exports do they generate, if any? Also Eastman Kodak reported sales to foreign subsidiaries in 1960 of \$64 million, and sales to dealers of \$49 million. What are the arrangements with these dealers, and how do they operate?

Fourth, in your own company it appears that selling, general and administrative costs are being shifted rather heavily to the parent corporation. For instance, on a gross profit of \$72 million by the U.S. corporation selling, general, and administrative expense amounted to \$61 million, leaving an operating profit of \$11 million. On the other hand, on a gross profit earned by foreign subsidiaries of \$60 million, your company showed selling, general and administrative expenses of only \$40 million, leaving an operating profit of \$20 million. These figures are from form 10-K for your fiscal year ending May 3, 1961. I note that you have a Swiss subsidiary, but your foreign tax was \$8.9 million, certainly a substantial figure. It would be helpful to me and to the Finance Committee to have an explanation of the above figures.

Fifth, Otis Elevator changed its fiscal year in 1960 and, as a result, paid three dividends in that year amounting to \$3 million from total reported foreign earnings of \$4.7 million. I would like to know what the comparable figures were for 1961.

Sixth, I am unable to find any information on the Cabot Corp. except that it owns 41 percent of Texas Butadiene, another of the companies in your list of 19. Is the Cabot Corp. an industrial company? I am unable to find it listed in "Moody's Industrial Manual for 1961."

Seventh, the Texas Butadiene French sales and investment operation raises a

number of questions. Is the 25 percent of sales being permanently invested in France completely free of U.S. tax? Is this being written off as a sales commission through its Canadian and other foreign subsidiaries? Also, did the export figures you gave include the full price of these French exports? What part of the price was actually remitted currently?

Eighth, Merck's report for 1960 shows \$6.5 million remitted from earnings of \$10.5 million. This was a considerable step-up from remittances for other recent years. Is the step-up in remittances continuing through 1961 and into 1962? There appears to be a rather large number of subsidiaries owned by a Panama subsidiary. Is this a new development, a reorganization?

Ninth, General Electric's Jelco subsidiary does a large foreign engine leasing business through a great many foreign subsidiaries. How were these earnings handled in your statistics? Is there any foreign insurance or reinsurance operation in connection with Jelco's or GE Credit Corp.'s operations, foreign or domestic?

Tenth, Pfizer's figures seem not quite to add up. That company's consolidated 10-K for 1960 shows earnings of \$38.9 million by the U.S. company and its more than 60 active branches, subsidiaries, and affiliates operating in more than 40 countries, on which U.S. tax of only \$6.9 million and foreign taxes of \$5.8 million were paid. This seems to be a rather large earnings-to-tax ratio. Research and development expense was shown as \$13 million. Was all this charged to the U.S. parent corporation? Royalties in the amount of \$4 million were received. How much of this was received and retained abroad in a tax haven? There is a particularly intriguing statement in this company's 10-K to the effect that, "No provision for Federal income dividend tax in respect to the subsidiary companies' earnings retained at December 31, 1960, is included in the consolidated statements, inasmuch as it is considered that such earnings are essential to the continued operation of the subsidiaries' business." It would appear that foreign subsidiary earnings were about \$24 million, of which only \$4 million was repatriated. Does the above-quoted statement mean that the other \$20 million is being invested in bricks, mortar, and machinery abroad, and will never become subject to U.S. tax?

Eleventh, how were operations involving mining, oil, gas, hydroelectric generation, and so on, handled in your statistics for these supposedly industrial companies? I note specifically that Union Carbide has a power-generating facility in Norway, as well as extensive mining and, perhaps, oil and gas operations; Armco has mining operations and also handles many allied products through its foreign subsidiaries; Monsanto has a large subsidiary, the Lion Oil Co.

Twelfth, four of the companies you stated you represented were either subsidiaries or divisions of larger U.S. corporations. How much of your data came from the parent corporations of these subsidiaries?

As I believe you can see from just the few brief facts and questions outlined above, your testimony before the Ways and Means Committee needs clarification and amplification in many respects. I would hope that you will be able to appear before the Finance Committee before the end of the current hearings, now tentatively scheduled to terminate on May 3, 1962.

I shall look forward to hearing from you at an early date, and would like your permission to make your reply a part of the record of the hearings before the Finance Committee.

APRIL 24, 1962.

DEAR SENATOR GORE: I have your letter of April 17 and am pleased to reply to the questions which are within my capacity.

In your paragraph first, you have asked about the organization of the 19-company committee. I enclose herewith a brief history of this group entitled "Memorandum re 19 Companies," which I think is responsive to your questions. The ad hoc group of 19 companies which submitted its data in a joint presentation through me to the House Ways and Means Committee has performed its function of testifying and has no reason for continued existence as a committee. I have not been delegated to speak for the 19 companies on any matters outside of the statements I have presented to the Congress.

In your paragraph fourth, you raised some questions concerning the Heinz Co. You will find our answer in the memorandum entitled "H. J. Heinz Co. Reply to Senator Gore's Inquiry" attached.

In paragraphs 2d to 12th, excepting paragraph 4th, you inquire as to matters of which I have no personal knowledge.

I have asked Mr. Sawyer, the public accountant who helped present the data received from the 19 companies, for information in respect to your second question. He informs me that the increase in outflow for foreign investment from \$30.5 million in 1959 to \$61.3 million in 1960 was spread between 9 of the 19 companies. He also informs me that he has no data for 1961 pertaining to capital outflow.

In respect to your paragraph third, Mr. Sawyer advises me that the figures he has contain no breakdown for exports generated by licensing agreements.

In regard to paragraph 12th, Mr. Sawyer advises me that 6 of the 19 companies were international or oversea subsidiaries or divisions. In each case the data used in the 19-company study came from the subsidiary or division.

With respect to some of the general remarks that you have made in reference to the 19-company study, may I refer you to the statement I have filed today with the Committee on Finance, a copy of which I attach hereto.

I am entirely agreeable to your publishing this letter and the two annexed memorandums in the record of the Senate Finance Committee hearings on H.R. 10650.

Sincerely,

H. J. HEINZ II.

MR. GORE. Mr. President, it seems to me that Mr. Heinz has completely failed to support, defend, justify, or render credible the statistics he presented to the Ways and Means Committee. Therefore, I am left to fall back on the Treasury's statistics which show, among other things, that manufacturing subsidiaries in Europe cause a current net drain on our balance of payments.

DRESSER AND THE EXPORT TRADE CORPORATION

Now I want to talk about a provision in section 12 of the bill which is directly related to the pending amendment.

There is one escape valve in the tax haven provision in the bill which I find most distressing because it puts the official stamp of congressional approval on one of the most indefensible of the tax haven types of operation, that type whereby profits earned in the United States are bled off to a tax haven corporation untaxed by the United States. This will make possible the continuation of a practice which is typified by a corporation I have taken some pains to look into. I should like to detail its operations and show how these operations can continue under the terms of this bill; indeed, to show how the bill was tailored to fit the operations of a particular company.

I refer now to a company with whose representatives I and my staff have had repeated conferences, and with whose officials I have had considerable correspondence, but about whose operations there is still much mystery. I refer to Dresser Industries, Inc.

This company manufactures, sells, leases, and services oilfield equipment. Most of its manufacturing is done in the United States, but it does some manufacturing abroad, mainly through licensees rather than through subsidiaries.

Of course, not all the ramifications of this company's operations are known to me. That more is going on than I am aware of is pretty well borne out by the fact that this company refused to come before the Committee on Finance, even when specifically invited to do so. I should like to read the telegram sent to me by Mr. H. N. Mallon, chairman of the executive committee of Dresser Industries, Inc.:

DALLAS, TEX., June 29, 1962.

Senator ALBERT GORE,

U.S. Senate, Committee on Finance, Senate Office Building, Washington, D.C.:

Following telegram sent to Mrs. Elizabeth B. Springer:

"Regret inability to appear before Senate Finance Committee on July 2 or 3 as requested by Senator GORE. I will be pleased to confer with Senator GORE at early date to give him such information with respect to foreign operations of Dresser Industries as he may desire."

H. N. MALLON,

Chairman of Executive Committee,
Dresser Industries, Inc.

I might add that it was not for lack of opportunity that the company did not appear. The corporation vice president who handles legal matters, together with an outside tax specialist, who represents the corporation in setting up many of its tax-dodging maneuvers, were in Washington several times during the course of the hearings before the committee. In fact, they came to my office the last day of the hearings, but after the chairman had adjourned and concluded the public hearings. When asked by one of my assistants why they did not testify before the committee, these gentlemen said that they did not want to get into a situation in public which they might not be able to control.

When asked if that meant that they were not sure "what Senator GORE has on you," they replied in the affirmative.

Let me hasten to say that I am not trying to indict this one corporation. I am not going to single it out just because I think its method of operation is unique. Such is not the case at all. I fear this case is typical of many others. But this company has been active in attempting to persuade certain Senators and members of the executive branch that its operation should be continued untaxed. So we find written into the bill this export trade corporation provision to encourage a harmful type of tax haven operation when the bill, according to its supporters, is designed to cut off tax haven operations. At least two other companies, Westinghouse and Cargill, were as active as this one in trying to maintain this most lucrative loophole in the tax laws. It is with regret and great disappointment that I have noted

the Treasury's willingness to go along with this procedure. In fact, the Treasury sponsored, behind the scenes, this amendment which was approved by the Finance Committee.

If in detailing the operations of this corporation I make some errors, I wish it clearly understood that I sought full information; that at my suggestion officials of Dresser Industries, Inc., were invited to testify. I requested them to testify. I wrote letters asking for information. I have given the company's officers opportunities to explain several points which have troubled me. When I became convinced that they would not come before the Committee on Finance and publicly defend their method of operation, I wrote a letter to a vice president in which I asked a number of specific and pertinent questions.

Madam President, I ask unanimous consent to have printed at this point in the RECORD my letter of July 10, 1962, to Mr. J. D. Mayson, vice president and secretary, Dresser Industries, Inc., and the attached questions.

The PRESIDING OFFICER (Mrs. NEUBERGER in the chair). Without objection, it is so ordered.

The letter and questionnaire are as follows:

JULY 10, 1962.

Mr. J. D. MAYSON,
Vice President and Secretary, Law Department, Dresser Industries, Inc., Republic National Bank Building, Dallas, Tex.

DEAR MR. MAYSON: Mr. Lynch has told me of your visit to the office last week, and I am sorry I was not in. I am also sorry to learn that you feel I have done an injustice to Dresser Industries by requesting that Mr. Mallon testify before the Finance Committee.

It so happens that I feel Mr. Mallon could have contributed materially toward clearing up several important points which might have been of assistance to the Finance Committee in its consideration of the tax reform bill.

Mr. Lynch has informed me that you have volunteered to answer, on behalf of Dresser Industries, any specific questions which I might have concerning the organization and operation of Dresser's foreign activities. In the hope that you will answer these questions as fully and directly as possible, I am attaching a list of questions which I consider relevant.

I look forward to an early reply.

Sincerely yours,

ALBERT GORE.

QUESTIONS SUBMITTED BY SENATOR ALBERT GORE TO J. D. MAYSON, VICE PRESIDENT, DRESSER INDUSTRIES, INC.

1. What is the organization of Dresser Industries, Inc., for foreign operations?

2. What is the relationship between or among Dresser, A.G. (Vaduz), Dresser, A.G., Zug, and Dresser, A.G. (Zuerich)? List the subsidiaries (if 50 percent or more of stock owned by Dresser and/or any of its subsidiaries) of each, the country of incorporation, and the location of the head office. Which of these, if any, exist primarily for tax or currency reasons?

3. How many employees does Dresser, A.G. (Vaduz) have? In what country, or countries are these employees physically located?

4. Give the information requested in 3, above, for Dresser, A.G., Zug.

5. Give the information requested in 3, above, for Dresser, A.G. (Zuerich).

6. Give the information requested in 3, above, for each subsidiary of the foreign corporations named in 3, 4, and 5 above.

7. What was the net profit, after payment of the appropriate foreign income tax, in each of the past 6 years, for the following foreign corporations:

- (a) Dresser, A.G. (Vaduz)?
- (b) Dresser, A.G., Zug?
- (c) Dresser (France) S.A.?
- (d) Dresser (Great Britain), Ltd.?
- (e) Dresser Italy, S.p.A.?
- (g) Petro-Tech Argentina, S.A.I.C.I.F. y de M.?

(h) Petro-Tech del Peru, S.A.?

(i) Dresser, A.G. (Zuerich)?

(j) Dresser (Germany), GmbH?

8. List the dividend paid by each of the corporations listed in 7, above, for each of the past 6 years, to its parent corporation.

9. Do employees of any of the corporations listed in 7, above, negotiate sales or perform service in any foreign countries? Does any part of the commission, fee, royalty, or other collections by, or as the result of the efforts of, these employees, go directly to any parent foreign corporation? In other words, do the Swiss or Liechtenstein corporations realize income, other than dividend income, as a result of the efforts of employees of their subsidiary corporations?

10. Have any earnings or net profits of any foreign subsidiary (other than dividends), ever been transmitted to the U.S. parent corporation? Have any of these funds been accorded a U.S. tax rate less than the regular corporate rate? Has any U.S. corporation, whether or not a part of Dresser Industries, ever borrowed directly or indirectly from Dresser's Swiss or Liechtenstein subsidiary corporations?

11. Your form 10-K for the year ended October 31, 1961, shows income before taxes of \$14,526,276. Net earnings of foreign subsidiaries appear to be \$5,812,954. Is this latter figure before or after the payment of the appropriate foreign income taxes?

12. I see no indication in your form 10-K of any reservation for future U.S. income tax on any foreign subsidiary earnings. If your bookkeeping is honest, and not overstating your after-tax earnings and assets, this would indicate that there is no intention of ever repatriating any of last year's almost \$6 million of foreign subsidiary earnings other than the \$125,000 actually repatriated. Do you intend to repatriate any of these earnings, and if so, in what form?

13. What types of investments were made with the retained earnings of foreign subsidiaries last year? In what countries?

14. In 1959 or 1960 Dresser collapsed its Western Hemisphere corporation, presumably to take advantage, tax free, of the cash which had been collected, and because it could do better in the future, taxwise, by using the Liechtenstein-Swiss tax haven hookup. Do you plan any other such maneuvers. Have you, during the past 6 years, collapsed any other subsidiaries, either domestic or foreign?

15. It would appear that your company paid out in dividends last year about \$5.6 million. Since total after tax consolidated earnings were about \$10 million, and foreign subsidiary earnings were about \$6 million, only \$125,000 of which appears to have been repatriated, it would seem that Dresser paid out in dividends considerably more than it had available domestically from current earnings. Furthermore, beginning in 1964, your long-term financing calls for a repayment of \$3,450,000, with annual repayments of between \$3 and \$4 million per year thereafter through 1976. This would indicate the necessity of repatriating considerable sums of money from foreign subsidiary earnings during the period 1964-76. In what form do you plan to repatriate this money, and from which foreign subsidiaries?

16. The statement of earnings in form 10-K for the fiscal year ended October 31, 1961, shows the following:

Revenue from "services and other"-----	\$30,047,320
Revenue from "interest"-----	1,838,863
Revenue from "royalties"-----	1,961,260

Of the above amounts, how much represents revenues received by foreign subsidiaries? How much was received directly by the Swiss and Liechtenstein corporations?

17. What income tax—Liechtenstein, Swiss, and/or cantonal—was paid last year by each of your Swiss and Liechtenstein subsidiaries? What effective rate does this represent?

18. Describe the operations of the Panexco Trading Corp. Is it still in existence? Was or is it a successful operation?

19. How many bank accounts do your various foreign subsidiaries have? In what countries are they located? How much was in each account on October 31, 1961? What other liquid assets do your foreign subsidiaries hold? Are any of these assets in the United States?

20. Does Dresser maintain a file of important intracompany memorandums, and if so, would you be willing for a member of my staff to visit your head office and inspect this file?

21. In 1959 did you advance the claim that Dresser A.G. (Vaduz) had "saved" Dresser Industries some \$4.5 million in taxes during the period 1953-58 and that Dresser International, Inc., had saved the company \$376,000 during the same period?

22. On another occasion, did you claim that Dresser, A.G., was "a tax gimmick and nothing more," and did you plead with the top corporate management to have everyone cooperate in an effort to give the appearance of substance to its operations?

23. Has the legal department ever been accused of attempting to run Dresser's foreign business?

24. In 1959 or 1960, was there a dispute within Dresser's top management as to a proper organization for foreign operations? Was there a feeling on the part of some that too much effort was being directed toward tax savings or avoidance, to the detriment of good management? What was the outcome of this dispute, if there was one?

Mr. GORE. Madam President, I wish to read the reply of Mr. J. D. Mayson, under date of July 17, 1962:

DRESSER INDUSTRIES, INC.,
Dallas, Tex., July 17, 1962.

The Honorable ALBERT GORE,
U.S. Senate,
Washington, D.C.

DEAR SENATOR GORE: Thanks for your letter of July 10, 1962, and the questions concerning Dresser Industries which you attached. Your letter was received yesterday morning, and I have contacted the various people in our organization who will supply the information necessary to answer your questions. As I am sure you realize, some of this information must come from overseas and, therefore, our reply will not be as prompt as if everything was available here in Dallas.

However, I wish to assure you that we will let you hear from us at the earliest possible date.

Please give Mr. Lynch our regards.

Very truly yours,

J. D. MAYSON.

On August 2, 1962, I received a further letter from Mr. J. D. Mayson, which reads, as follows:

DRESSER INDUSTRIES, INC.,
Dallas, Tex., August 2, 1962.

The Honorable ALBERT GORE,
U.S. Senate,
Washington, D.C.

DEAR SENATOR GORE: With further reference to your letter of July 10 and my letter of July 17, 1962, I want to let you know that we have now accumulated in Dallas a substantial amount of the information which you have requested, and are proceeding to correlate and check it. As soon as we have put this information in proper form, you may expect to hear from us.

With best regards, I am,
Very truly yours,

J. D. MAYSON.

When I learned that the bill was being called up, I sent a telegram to the corporation on August 21, requesting as much information as was available. On Monday, August 27, I received the following reply to my telegram:

DRESSER INDUSTRIES, INC.,
Dallas, Tex., August 24, 1962.

HON. ALBERT GORE,
U.S. Senate,
Washington, D.C.

DEAR SENATOR GORE: With further reference to our letters to you of July 17 and August 2, and with reference to your August 21 telegram which we received Wednesday morning, this will confirm that we are proceeding to correlate and check for accuracy the great amount of data we have assembled in response to the numerous questions set forth in your letter of July 10.

As you know, while our principal office is in Dallas, Tex., Dresser, A.G., together with its subsidiaries, have offices and/or employees in Argentina, Brazil, Colombia, France, Germany, Great Britain, Greece, India, Iran, Italy, Japan, Lebanon, Libya, Liechtenstein, Mexico, Netherlands, Peru, Switzerland, Thailand, Trinidad, and Venezuela, and it has taken us a considerable amount of time and effort to compile the necessary information.

As indicated to you previously, we are desirous of maintaining the spirit of cooperation which has existed between your office and our company. However, in reviewing the questions which you have asked, a full and meaningful response would require the submission on our part of highly confidential business statistics and data. Accordingly, the management of Dresser Industries has decided to request outside counsel to analyze and review the questions transmitted with your letter of July 10, together with our final response thereto. As soon as the compilation of the data is completed and the analysis and opinion of counsel received by the management of the company, we shall be in touch with you again.

Very truly yours,

J. D. MAYSON.

Madam President, it is not necessary to know much about this company, to realize that its profit structure is awry. Anyone can look at the form 10-K filed by this corporation with the SEC and see that something is wrong somewhere in the way its profits are shifted from the United States into its tax-haven subsidiaries.

The total assets of this corporation are in excess of \$200 million, while the assets of the foreign subsidiaries amount to about \$25 million of this amount. But how were earnings split up? Foreign earnings were more than two-thirds of U.S. earnings. But foreign assets are only about one-seventh of U.S. assets. Surely something is out of line somewhere.

Incidentally, Madam President, I am strongly suspicious that section 6 of this bill was dropped as part of an arrangement which will permit Dresser Industries and others to enjoy a tax dodge. As recently as the appearance of the Secretary of the Treasury before the Senate Finance Committee on May 10 of this year, section 6 of the House version was still being advocated strongly by the Treasury Department. This section was endorsed by Assistant Secretary Surrey in a letter to the Senator from Delaware [Mr. WILLIAMS] on May 17.

But what do we find about the arrangement made on this export tax-haven gimmick? We find that the committee report, on page 90, has this language:

With the limitations it is not expected that the allocation rule in present law (sec. 482) will be needed in many cases involving export trade corporations.

Here, Madam President, we find another instance in which the majority committee report seeks to give tax relief that is not specifically provided by the terms of the bill. I hope some Member who signed the majority report will be willing to explain this.

The existing section 482 is, of course, difficult to apply. The improved section 482, as set out in section 6 of this bill, might have proved embarrassing.

There must be some reason that is not stated in the report, and has not been given to the committee, why section 6 of the House version of the bill, which was so earnestly and so vigorously advocated until so recently by the Treasury Department, is now completely stricken from the bill by means of the committee amendment now pending before the Senate.

Now, Madam President, to return to our case study. Officials of this corporation do not like to have their foreign tax-haven operations classified as a "sham," but I am having trouble classifying them in any other way.

Indeed, I have seen what purported to be a copy of a memorandum sent from a vice president of this company to other high corporate officials, in which this vice president warned that the Liechtenstein-Swiss tax-haven operation was "a tax gimmick and nothing more," and he urged everyone to cooperate in an effort to give the appearance of substance to its operations. I have reason to believe this document and several others which I had the privilege of seeing to be genuine. There has been no denial from this corporate official that he did, in fact, make such a statement as the one I have quoted.

Now let us see just how this export trade corporation amendment in this bill was tailored to fit the operations of this particular corporation—Dresser Industries, Inc., of Dallas, Tex. Here is how Dresser Industries operates abroad for tax-haven purposes:

The U.S. parent corporation, its U.S. subsidiaries, and a few foreign subsidiary corporations manufacture capital goods—relatively large and high-priced items of equipment and supplies used by the buyers in their operations and not for resale to con-

sumers. Their foreign customers, in many countries, are usually corporations, often very large corporations. Ordinarily these foreign customers deal, directly or indirectly, with the producing corporations in the United States (or with the foreign manufacturing subsidiaries), and usually prefer to take title to the goods in the United States or in the foreign country where the items are manufactured.

The parent corporation organized an international subsidiary under the laws of Liechtenstein which, nominally at least, performs the marketing operations throughout the world (except in the United States and Canada) for the parent corporation and its U.S. and foreign manufacturing subsidiaries. The Liechtenstein corporation also performs, nominally, various services with respect to the many foreign licensees of the parent—collecting royalties and fees, transmitting technical information and assistance, etc. But since Vaduz, Liechtenstein is not deemed a "respectable" address, there is another subsidiary of the parent company which is organized under the laws of Switzerland and has an office there. This company does not act as a principal, but is merely the agent of the Liechtenstein corporation, providing, for a small fee, an office and the handling of correspondence, records, advertising materials, etc. Liechtenstein does not have an income tax, so that the profits of the Liechtenstein corporation are free from tax until they are transmitted as dividends to the U.S. parent corporation. Switzerland and its cantons impose income taxes on income earned in Switzerland, but since the services performed by the Swiss subsidiary are only those which a few employees perform in a small office, and since the fee paid by the Liechtenstein corporation for those office services is only slightly more than the cost of the services, the taxes paid to Switzerland and its cantons is negligible.

Although it employs few, if any, salesmen, and the sales of the products of the U.S. parent company or its U.S. subsidiaries are either made directly by the U.S. companies or by independent foreign distributors, the Liechtenstein company receives a commission of 15 percent of the selling price, out of which it pays 5 percent to the independent foreign distributors. For its services (whatever those may be) in dealing with foreign licensees and collecting royalties and fees for the use of the U.S. corporations' patents, formulas, trademarks, and know-how the Liechtenstein corporation receives 80 percent of the royalties and fees.

It is evident that the profits thus allocated to the Liechtenstein corporation are grossly disproportionate to the real value of what little work that corporation does. In fact, among themselves, officers of the parent corporation have admitted that the Liechtenstein corporation is nothing more than a tax device, and that it has no real substance. They have directed subordinates to so handle correspondence, sales documents, etc., as to make it appear that the Liechtenstein corporation is a functioning, commercial organization, even though, in actuality, transactions are handled as if there were no such foreign company.

The amendment of the Senate Finance Committee to section 12 would specifically permit the continuation of the tax dodge which I have described, and the pending amendment, to eliminate tighter language for section 482 of the code, would give this procedure an assist.

There is another Swiss holding company of Dresser which owns, and bleeds off profits from, some operating subsidiaries in high-tax foreign countries.

By such bizarre arrangements, this United States corporation can claim that

its tax haven subsidiary is "responsible" for millions of dollars of United States exports; and officials of this company have come to Members of the Senate and made such a claim.

In reality, the tax haven subsidiary is not doing anything more than bleeding off most of the profit from the sale of exports and is thereby actually reducing the inflow of funds which ought to be repatriated annually as a result of these sales.

Most of the funds should remain in the United States instead of being funneled into a foreign tax haven, but the committee amendment now pending would make it possible to continue this kind of tax dodge by this company and a few others.

Interestingly enough, I have not been able to find out how this corporation gets funds back home when it needs cash. Last year, out of \$5.8 million of foreign earnings, only \$125,000 in dividends came back to the U.S. But the company paid out practically its entire domestic earnings in cash dividends. With a heavy long-term indebtedness which will require repayments of between \$3 and \$4 million per year between 1964 and 1976, a great deal of money is going to have to be brought home one way or another.

Mr. MORSE. Madam President, will the Senator yield?

Mr. GORE. I yield.

Mr. MORSE. I wish to take only a moment to thank the Senator from Tennessee for the work he has done in the best interests of the American taxpayers in his opposition to various sections of the bill and in his various proposals to improve the bill, which have been uniformly voted down. I am sure the Senator is not surprised by the defeats he has suffered in connection with the bill.

Mr. GORE. I was surprised at the one yesterday in connection with expense account abuse. I sincerely believed that I could convince the Senate that the present practice was wrong, and that the Senate would not vote for the committee amendment. I still believe that if I could have had the attention of my colleagues for a few moments I might have been able to convince them. But the Senator knows how difficult, complicated, and involved are the subjects in the current bill, and, I am sorry to say, how uninteresting the discussion upon such subjects appears to be. Nevertheless, I did have hopes that I could win that one fight, and that we could defeat that committee amendment.

The President of the United States, in his first state of the Union message, had dramatically called attention to the attack upon the very moral fiber of our country involved in this widespread abuse, the tax avoidance through expense account manipulations, clothing and disguising expenditures for personal pleasure and benefit in business functions and purposes.

I thank the Senator very much for his generous remarks. Perhaps I was naive in hoping we could win that fight, but I did have that hope.

Mr. MORSE. Madam President, will the Senator yield?

Mr. GORE. I yield.

Mr. MORSE. It is very refreshing to me to find that the Senator from Tennessee was surprised. I think, however, it would have been a more apropos phrase or word to say he was hopeful, as I was hopeful, but not surprised. However, in my judgment, the bill has reached such a stage in its development in the Senate that it can best be described as a bonanza bill for tax dodgers who ought to be paying taxes on the basis of their ability to pay, but who are going to use the bill to duck out on their tax responsibilities.

The bill has reached such an unacceptable form that I serve notice tonight that under no conditions will the Senator from Oregon vote for the bill in its present form. I think the bill is a disservice to this administration.

Mr. GORE. I cannot vote for the bill in its present form; and the adoption of the pending committee amendment would make it even worse.

I say advisedly that the pending amendment is a special interest amendment. It would permit the continuation of the kind of tax dodge which for the past 30 minutes I have been describing to the Senate.

I say to my distinguished colleague the senior Senator from Oregon that what I have been saying this afternoon is the result of 3 years of work. The work has not been too inviting or pleasant. It has been drudgery. It has been aimed at the solution of one of the problems which plague our people; the mass movement abroad of industry and jobs, and in many instances whole factories.

I know that the amendment which I have proposed would not completely solve that problem, but it would eliminate the tax subsidy for such movement abroad of industries, jobs, and factories.

Upon the election of President Kennedy, I was invited to confer with him on fiscal, economic, and other matters. I visited in his home in Georgetown. After we became engrossed in a discussion, he very kindly closed the door, and no one else came in while we conferred for perhaps more than an hour on this subject.

The President expressed his very great interest in it. Among his very first recommendations to the Congress was a recommendation that the preferential tax treatment of income earned abroad be eliminated.

Finally, there is before the Senate the pending bill, which would make some improvements. I am glad to acknowledge that. I am constrained to believe—I like to believe—that I am partially responsible for some of the worthwhile provisions in the bill. I would that the bill were better.

The pending amendment is a bad amendment. It should not be adopted. The bill would be better without the amendment.

In this difficult, uninteresting, complicated discussion of the afternoon I have not been able to reach enough of my colleagues to persuade them to vote against the committee amendment. I

shall nevertheless proceed in the hope, however faint that hope may be, that a sufficient number of my colleagues will read the RECORD tomorrow and will support amendments to improve the bill.

Returning to the export trade corporation amendment, note how this "escape valve" fits into the picture. It was specifically tailored to fit Dresser Industries, Westinghouse and Cargill.

According to this provision of the bill, "export-trade income" is not to be included in income of foreign subsidiaries on which tax will be paid currently by their U.S. parent corporations.

This "export-trade income" consists of the net income from:

First. Sale of exports to unrelated persons.

Second. Commissions and fees for the use of export property.

Third. Commissions and fees on patents, secret processes, and so forth.

Fourth. Interest received from export trade assets.

The Dresser tax haven subsidiary gets its income in just these ways.

Of course, there are limitations. One can only bleed off 10 percent of gross receipts. Now, what kind of limit is that? There are not too many industrial corporations which make a profit of more than 11 or 12 percent of gross sales.

And there is another, alternate, limitation, that of 1½ times "export promotion expenses." In other words, on this basis there is a guarantee of a tax-free ride on a 50-percent profit, based on the cost of running the oversea operation.

Madam President, this is a specific provision of the export trade corporation amendment which ties in with the pending amendment, and which was offered late in the consideration of the bill and only after Dresser Industries, Cargill, and Westinghouse had been very busy. When this amendment was suggested it had a familiar name among those "in the know," which identified it as the special interest amendment for the particular group and character of taxpayers to which I am referring.

I can hear the proponents of this amendment object, "Even though it looks like we are giving these people a free ride on 10 percent of sales or 50 percent of operating costs," as it will be argued, "very little use will be made of this tax dodge because the amounts on which U.S. tax will be avoided must be invested in export trade assets."

But what are "export trade assets"? They include:

First. Working capital.

Second. Inventory.

Third. Facilities for handling, transportation, packaging and servicing.

Fourth. Evidences of indebtedness for the sale of exports.

I repeat the last: "Evidences of indebtedness for the sale of exports."

There are no real limitations there. It includes everything but manufacturing. It even includes credit expansion.

Would it not be wonderful for that corporation if a domestic corporation could escape taxation on the profit it makes from all sales on credit? Would that not be wonderful? I fear, insofar

as my little business is concerned, that constitutes the great bulk of the sales.

As I said, the amendment would specifically put the stamp of congressional approval on one of the worst types of tax havens or tax dodges—the type in which profits are removed directly from under the U.S. tax jurisdiction and into a tax haven country to escape indefinitely, and perhaps forever, any payment of U.S. taxes. That is the worst sort of tax haven abuse, so far as equity and the balance of payments are concerned. Yet that is what will be specifically endorsed by the pending amendment together with other provisions of section 12.

These provisions are contained in the committee amendments recommended to the bill.

The question now specifically before the Senate concerns section 482 of the code which would be amended by section 6 of the bill. The amendment is in the nature of a more specific formula than the one now found in section 482.

The purpose of section 482, which is very general in its wording, is to enable the Internal Revenue Service to make sure that taxpayers do not shift profits or losses, income or expense, among different taxable organizations in such a way as unduly to minimize the taxes paid by various economic units representing one set of economic interest. The wording of the section is very general:

In any case, two or more organizations, trades or businesses (whether or not incorporated, whether or not organized in the United States, and whether or not affiliated) owned or controlled directly or indirectly by the same interests, the Secretary or his delegate may distribute, apportion or allocate gross income, deductions, credits, or allowances between or among such organizations, trades, or businesses, if he determines that such distribution, apportionment or allocation is necessary in order to prevent evasion of taxes or clearly to reflect the income of any of such organizations, trades or businesses.

Mr. President, when the Secretary of the Treasury came before the Ways and Means Committee in 1961 and before the Finance Committee earlier this year, he endorsed the need for strengthening section 482. At no time, however, has it been claimed by any spokesman for the administration, to my knowledge, that section 482 was a major tool, or one on which chief reliance could be placed for enforcing the collection of proper taxes. Such is not its purpose. The section is particularly hard to apply when, as is the case so often in dealings between a domestic corporation and one of its foreign subsidiaries, only one set of books is available to the agent, and the U.S. taxpayer is uncooperative. Unfortunately, this is often the case.

When section 482 is to be used to allocate income or expenses among domestic taxpayers, and this is its more common use, the books of all taxpayers concerned are available to the agent and he can often use or threaten to use section 482 to good advantage.

But the Secretary of the Treasury felt that, particularly in the case of taxpayers one of which was domestic, and many of which are foreign, the present

wording of section 482 did not give the agent a sharp enough tool for the operation required.

The report of the Ways and Means Committee had this to say about the problem:

VII. ALLOCATION OF INCOME BETWEEN RELATED FOREIGN AND DOMESTIC ORGANIZATIONS

(Sec. 6 of the bill and sec. 482(b) of the code)

A. Reasons for provision

Under present law, foreign corporations which are controlled by domestic corporations or other persons are not taxed by the United States on their foreign source income. Thus, United States imposes no tax with respect to the profits of such a corporation when they are earned although it does impose a tax on the domestic shareholders of this corporation when they receive dividend distributions from it. This taxation at the time of distribution, rather than at the time the income is earned by the foreign corporation, has become known as "tax deferral." U.S. corporations, it is believed, may sell goods to their controlled foreign subsidiaries at less than a fair price to avoid a U.S. tax on what should be their full profit for such sales. Similarly, in other cases it is believed that foreign-controlled subsidiaries have sold goods to their domestic parent at more than the fair market price. The effect of such transactions is to understate the taxable income of the domestic corporation subject to U.S. tax and to overstate the income of the foreign subsidiary. Thus, to the extent the U.S. tax rate is above that imposed by the foreign country or country involved, tax deferral is achieved with respect to this diverted income during the period of time the income is held abroad. The Secretary of the Treasury, in his testimony last year on this subject, stated:

"This is not simply a question of allocating the profits of foreign operations to tax haven countries. It is a problem that significantly affects U.S. taxation of domestic profits. The technique that is used for diverting profits from one company to another among European affiliates is also used to divert income from U.S. companies to foreign affiliates. Income that would normally be taxable by the United States is thrown into tax haven companies with the object of obtaining tax deferral. This is done, for example, by placing in a Swiss or Panamanian corporation the activities of the export division of a U.S. manufacturing enterprise. A very substantial volume of exports is required merely to offset the loss in foreign exchange which the retention abroad of export profits entails."

Present law in section 482 authorizes the Secretary of the Treasury to allocate income between related organizations where he determines this allocation is necessary "in order to prevent evasion of taxes or clearly to reflect the income of any such organizations." This provision appears to give the Secretary the necessary authority to allocate income between a domestic parent and its foreign subsidiary. However, in practice the difficulties in determining a fair price under this provision severely limit the usefulness of this power especially where there are thousands of different transactions engaged in between a domestic company and its foreign subsidiary.

Because of the difficulty in using the present section 482, your committee has added a subsection to this provision authorizing the Secretary of the Treasury or his delegate to allocate income in the case of sales or purchases between a U.S. corporation and its controlled foreign subsidiary on the basis of the proportion of the assets, compensation of the officers and employees, and advertising, selling, and sales promotion expenses attributable to the United States and attributable to the foreign country or countries

involved. This will enable the Secretary to make an allocation of the taxable income of the group involved (to the extent it is attributable to the sales in question) whereas in the past under the existing section 482 he has attempted only to determine the fair market sales price of the goods in question and build up from this to the taxable income—a process much more difficult and requiring more detailed computations than the allocation rule permitted by this bill.

The bill provides, however, that the allocation referred to will not be used where a fair market price for the product can be determined. It also provides that other factors besides those named can be taken into account. In addition, it provides that entirely different allocation rules may be used where this can be worked out to mutual agreement of the Treasury Department and the taxpayer.

Madam President, even as late as his appearance before the Finance Committee on May 10, 1962, the Secretary endorsed the tightening up of the section 482 formula, and on May 17, 1962, Assistant Secretary Surrey wrote to the Senator from Delaware a letter in which he pointed out how effective the new language in section 482 would be in dealing with any difficulties which might arise between U.S. mainland taxpayers and their operations in the Virgin Islands.

Madam President, I ask unanimous consent that the letter which appears on page 4392 of the hearings be printed at this point in the RECORD.

There being no objection, the letter was ordered to be printed in the RECORD, as follows:

MAY 17, 1962.

HON. JOHN J. WILLIAMS,
U.S. Senate,
Washington, D.C.

DEAR SENATOR WILLIAMS: This is in response to your question at the hearings Friday, May 11, 1962, on whether the Virgin Islands could be used as a tax haven. You were concerned in particular about Harvey Alumina Virgin Islands, Inc., a Virgin Islands corporation which is a wholly owned subsidiary of Harvey Aluminum, a domestic corporation. The subsidiary has entered a contract with the Virgin Islands under which the inducements, such as free land and exemption from real estate tax, commonly offered by local governments in the United States, are granted. One of the additional inducements granted by the Virgin Islands is a subsidy based on income tax liability.

In general, the Virgin Islands taxes corporations created in the Virgin Islands at full Internal Revenue Code rates on the income from all sources. Under section 934, added in 1960, however, the Virgin Islands may grant subsidies based on the tax liability of a Virgin Islands corporation 80 percent of whose gross income is from sources within the Virgin Islands and 50 percent of whose gross income is from the active conduct of a trade or business in the Virgin Islands. Although section 934 in itself would not preclude all tax haven operations, Virgin Islands law provides that the subsidy based on income tax liability can be granted only with respect to income from the construction, ownership, or operation of new housing projects, factory buildings, or hotels. In the case of the Harvey Aluminum subsidiary a nontaxable subsidy equal to 75 percent of the income tax liability over a period of 16 years is granted on the condition that the subsidiary construct and operate a plant costing \$15 million and produce at 50,000 tons of alumina from bauxite ore.

Such substantial production is not considered a tax-haven operation in the case of foreign countries even though the country in which the production takes place grants special writeoffs, or reduced rates. Such operations in foreign countries would continue to obtain deferral under H.R. 10650. The Virgin Islands incentive program is comparable to those provided by many foreign countries.

A problem will exist, however, in making certain that the prices paid by the domestic parent corporation to the subsidiary for alumina to be further processed in the United States will not shift to the Virgin Islands income which is properly attributable to the United States. This problem, just as in the case of transactions between other related domestic and related foreign corporations, will be dealt with under the amendments to section 482 made by section 6 of the bill. The Virgin Islands government cooperates completely in providing the necessary information.

Sincerely yours,

STANLEY S. SURREY,
Assistant Secretary.

Mr. GORE. Mr. President, but in the meantime, Dresser Industries, whose tax haven tax dodges I have outlined for the Senate, Westinghouse, and Cargill began to push the Treasury to endorse an escape valve which would allow them to continue the type of operations in which they have so profitably indulged overseas. This escape valve is the export trade corporation provision contained in the Finance Committee version of this bill.

When these corporations were trying to drum up support in the Senate for their pet provision, they asked that it be specified in the bill that their operations be exempt from the operation of section 482. They knew that it would be relatively easy for any good agent to show that they did not have the substance to their oversea operations which would warrant their draining off 10 percent of gross sales into Switzerland or some other tax haven country, there to escape U.S. taxation.

The bill does not provide any such blanket exemption from section 482 for these corporations, but the Finance Committee report, on page 90, does say:

With the limitations it is not expected that the allocation rule in present law (section 482) will be needed in many cases involving export trade corporations.

In the meantime, for reasons best known to others than myself, the Treasury decided to drop this much more definite and much tougher language which the bill had proposed to put into section 482 of the Internal Revenue Code. I can only conclude, in the absence of a good explanation, that this tightening up of section 482 was dropped because of the pressure of those taxpayers who can now escape any effective enforcement under the existing section 482.

Mr. PROXMIRE. Madam President, will the Senator yield for a question on the last point he has raised?

Mr. GORE. I yield.

Mr. PROXMIRE. I should like to have him clarify it for me. On page 90 of the report the Senator quotes the majority report as saying:

With the limitations it is not expected that the allocation rule in present law (section

482) will be needed in many cases involving export trade corporations.

What does that mean?

Mr. GORE. This sentence refers to the limitations spelled out in the two preceding paragraphs which are subject matters of the amendments recommended by the Finance Committee. If the Senator will read the two preceding paragraphs, Nos. 1 and 2, he will see that it is stated:

1. 1½ times "export promotion expenses," (attributable to the otherwise excluded income) or

2. 10 percent of gross receipts of the export trade corporation from the sale, installation, operation, maintenance or use of the property from which it derives the income which otherwise is excluded. (In the case of commissions or fees, this 10 percent is measured on the same basis on which the commissions or fees are based.)

Having added this to the bill, the committee then says that with these limitations which it recommends it is not expected that the allocation rule in present law, section 482, will be needed in many cases involving export trade corporations.

Perhaps I should read further from the report:

The export trade income which is to be deferred also is limited to the portion of this income which is invested by the export trade corporation in "export trade assets" (or, more specifically, by the portion of the increase in investments in such assets which is attributable to export trade income which constitutes foreign base company income). Any amount of export trade income where U.S. taxation has been deferred because of such investments, will subsequently be taxed if there is a decrease in export trade assets.

This provision is intended to continue tax deferral in the case of corporations engaged in export trade who are selling abroad products produced, grown, or extracted in the United States.

Does that make it plain for the Senator?

Mr. PROXMIRE. I thank the Senator.

Mr. GORE. I read further:

This is intended as an encouragement to export trade. Nevertheless, limitations are imposed to provide that the income attributed to the export trade corporation is in line with the income actually generated by such activity. This is the function of limiting the export trade income to 1½ times export promotion expenses or 10 percent of gross receipts from the property, whichever is the lesser. Also, the provision is intentionally limited to the extent to which the export trade income receiving the special treatment is used for the expansion of the export trade business, itself.

Madam President, I have now addressed the Senate for approximately 3 hours on this difficult, technical, and complicated subject, to which I and dedicated members of my staff have devoted 3 years of work and study. It really is a heartbreaking experience to see amendments such as the Committee on Finance has approved, offered at the last minute, to take care of special interests, which create and perpetuate such a loophole for tax dodgers.

It is also a disappointment that the subject is so complicated that this discussion is not of great interest.

I believe I have no real choice but to let the amendment be adopted viva voce, and hope that after my colleagues in the Senate have had an opportunity to read the Record tomorrow, I may then offer an amendment to the original text, which would improve the bill.

The PRESIDING OFFICER. The question is on agreeing to the committee amendment on page 52, beginning in line 1.

Mr. MANSFIELD. Madam President, I suggest the absence of a quorum.

The PRESIDING OFFICER. The clerk will call the roll.

The legislative clerk proceeded to call the roll.

Mr. KERR. Madam President, I ask unanimous consent that the order for the quorum call be rescinded.

The PRESIDING OFFICER. Without objection, it is so ordered.

The question is on agreeing to the committee amendment on page 52, line 1.

The amendment, which was agreed to, is on page 52, line 1, to strike out:

SEC. 6. AMENDMENT OF SECTION 482.

(a) IN GENERAL.—Section 482 (relating to allocation of income and deductions among taxpayers) is amended by adding at the end thereof the following new subsection:

"(b) SALES AND PURCHASES WITHIN A RELATED GROUP WHICH INCLUDES A FOREIGN ORGANIZATION.—

"(1) IN GENERAL.—In applying subsection (a) to sales of tangible property within a group of organizations—

"(A) owned or controlled directly or indirectly by the same interests, and

"(B) at least one of which is a domestic organization and at least one of which is a foreign organization.

the Secretary or his delegate may allocate the taxable income of the group arising from such sales in the manner set forth in paragraph (2). This subsection shall not apply with respect to any sale of tangible property for which the taxpayer can establish an arm's-length price (within the meaning of paragraph (4)).

"(2) METHODS OF ALLOCATION.—

"(A) CONSIDERATION OF CERTAIN FACTORS.—Except as provided in subparagraph (B), the allocation referred to in paragraph (1) shall be made by the Secretary or his delegate by taking into consideration that portion of the following factors which is attributable to the United States and that portion thereof which is not attributable to the United States.

"(i) assets of the group, to the extent used in the production, distribution, and sale of the property,

"(ii) compensation of officers and employees, to the extent attributable to the production, distribution, and sale of the property, and

"(iii) advertising, selling, and sales promotion expenses (including technical and servicing expenses), to the extent attributable to the property.

Such method of allocation may also give consideration to other factors, including the special risks (if any) of the market in which the property is sold.

"(B) ALTERNATIVE METHODS.—If the taxpayer establishes to the satisfaction of the Secretary or his delegate that an alternative method of allocation clearly reflects the income of each member of the group with respect to the property referred to in paragraph (1), such alternative method shall be used (in lieu of the method provided in subparagraph (A)).

"(3) SPECIAL RULES.—In applying the method of allocation referred to in paragraph

(2)(A), the following rules shall be applied:

"(A) ADJUSTED BASIS OF ASSETS.—The values to be assigned to the assets referred to in paragraph (2)(A)(1) is their adjusted basis in the hands of the taxpayer or, if such basis is not available in the case of a foreign organization, then their book values, adjusted to approximate their adjusted basis.

"(B) INCLUDIBLE ASSETS.—The assets referred to in paragraph (2)(A)(1) include real property and tangible personal property (whether owned or leased by a member of the group), but do not include inventory and stock in trade.

"(4) ARM'S-LENGTH PRICE DEFINED.—For purposes of this subsection, the term 'arm's-length price' means—

"(A) the price at which tangible property similar or comparable to the property referred to in paragraph (1) generally is or can be sold in transactions in the same areas involving unrelated persons and made under similar conditions of sale; and

"(B) if subparagraph (A) does not apply, the price at which tangible property similar or comparable to the property referred to in paragraph (1) is sold in the same or other areas under similar circumstances and in transactions involving unrelated persons, with adjustment for material differences in quantity, marketing conditions (including customs duties and transportation costs), and other relevant factors.

Subparagraph (B) shall apply only if the adjustment referred to therein is properly determinable.

"(5) SALES COMMISSIONS.—The Secretary or his delegate shall by regulation prescribe rules for the allocation of commissions arising from sales of tangible property within a group of organizations described in paragraph (1). Such rules shall be consistent with the principles specified in the other paragraphs of this subsection.

"(6) GROSSLY INADEQUATE ASSETS, ETC., OUTSIDE UNITED STATES.—In allocating taxable income under this subsection, no amount shall be allocated to a foreign organization whose assets, personnel, and office and other facilities which are not attributable to the United States are grossly inadequate for its activities outside the United States.

"(7) INFORMATION NECESSARY FOR CONSIDERATION OF FACTORS.—In the case of any transaction to which paragraph (2)(A) applies, if—

"(A) the information submitted with respect to the group of organizations is insufficient for the proper application of the method of allocation set forth in the first sentence of such paragraph, and

"(B) upon request of the Secretary or his delegate, such group fails to furnish such additional information with respect to such transaction as may be reasonably supplied, the Secretary or his delegate may estimate the taxable income arising from such transaction and may allocate such taxable income among the members of the group or to any single member thereof.

"(8) TREATMENT OF FOREIGN TAXES.—

"(A) For purposes of this subsection, taxable income shall be determined without regard to any income, war profits, or excess profits taxes paid to any foreign country or to any possession of the United States.

"(B) Where the application of this subsection results in a decrease in the taxable income of any foreign organization and an increase in the taxable income of any domestic organization, then any of the taxes referred to in subparagraph (A) paid by such foreign organization and attributable to the taxable income so transferred shall be treated for purposes of this chapter—

"(1) as paid by such domestic organization, and

"(11) as not paid by such foreign organization."

(b) CLERICAL AMENDMENT.—Section 482 is amended by striking out "In any case of two or more organizations" and inserting in lieu thereof the following:

"(a) GENERAL RULE.—In the case of two or more organizations".

(c) EFFECTIVE DATE.—The amendments made by this section shall apply with respect to taxable years beginning after December 31, 1962.

SEC. 7. DISTRIBUTIONS OF FOREIGN PERSONAL HOLDING COMPANY INCOME.

(a) DEFINITION OF FOREIGN PERSONAL HOLDING COMPANY.—So much of subsection (a) of section 552 (relating to definition of foreign personal holding company) as precedes paragraph (2) is amended to read as follows:

"(a) GENERAL RULE.—For purposes of this subtitle, the term 'foreign personal holding company' for a taxable year beginning after December 31, 1962, means any foreign corporation if—

"(1) GROSS INCOME REQUIREMENT.—At least 20 percent of its gross income (as defined in section 555(a)) for the taxable year is foreign personal holding company income (as defined in section 553). For purposes of this paragraph, there shall be included in the gross income the amount includible therein as a dividend by reason of the application of section 555(c)(2); and".

(b) AMOUNT OF UNDISTRIBUTED INCOME.—Subsection (a) of section 556 (relating to undistributed foreign personal holding company income) is amended to read as follows:

"(a) DEFINITION.—For purposes of this part—

"(1) If the foreign personal holding company income of a foreign personal holding company exceeds 80 percent of its gross income, the 'undistributed foreign personal holding company income' of such company is its taxable income adjusted in the manner provided in subsection (b), minus the dividends paid deduction (as defined in section 561).

"(2) If the foreign personal holding company income of a foreign personal holding company does not exceed 80 percent of its gross income, the 'undistributed foreign personal holding company income' of such company is that amount which bears the same ratio to—

"(A) its taxable income adjusted in the manner provided in subsection (b), minus the dividends paid deduction (as defined in section 561), as

"(B) its foreign personal holding company income bears to its gross income."

(c) EFFECTIVE DATE.—The amendments made by this section shall apply only in respect to taxable years of foreign corporations beginning after December 31, 1962.

Mr. KERR. Madam President, I move that the Senate reconsider the vote by which the amendment was agreed to.

Mr. DIRKSEN. Madam President, I move to lay that motion on the table.

The motion to lay on the table was agreed to.

The PRESIDING OFFICER. The question is on agreeing to the committee amendment on page 121, line 2.

The amendment, which was agreed to, is on page 121, after line 2, to strike out:

(a) ENTIRE AMOUNT OF FOREIGN TAX BE TAKEN INTO ACCOUNT.—

(1) DEFINITION OF ACCUMULATED PROFITS.—So much of paragraph (1) of section 902(c) (relating to applicable rules for computing credit for corporate stockholder in foreign corporation) as precedes the semicolon is amended to read as follows:

"(1) The term 'accumulated profits', when used in this section in reference to a foreign corporation, means the amount of its gains, profits, or income computed without reduc-

tion by the amount of the income, war profits, and excess profits taxes imposed on or with respect to such profits or income by any foreign country or any possession of the United States".

(2) CONFORMING AMENDMENTS.—

(A) Section 902(a) is amended by striking out "which the amount of such dividends bears to the amount of such accumulated profits" and inserting in lieu thereof "which the amount of such dividends (determined without regard to section 78) bears to the amount of such accumulated profits in excess of such income, war profits, and excess profits taxes (other than those deemed paid)".

(B) Section 902(b) is amended by striking out "which the amount of such dividends bears to the amount of such accumulated profits" and inserting in lieu thereof "which the amount of such dividends bears to the amount of such accumulated profits in excess of such income, war profits, and excess profits taxes".

And, in lieu thereof, to insert:

(a) FOREIGN TAXES DEEMED PAID BY DOMESTIC CORPORATIONS.—Section 902 (relating to credit for corporate stockholder in foreign corporations) is amended to read as follows:

"SEC. 902. CREDIT FOR CORPORATE STOCKHOLDER IN FOREIGN CORPORATION

"(a) TREATMENT OF TAXES PAID BY FOREIGN CORPORATION.—For purposes of this subpart, a domestic corporation which owns at least 10 percent of the voting stock of a foreign corporation from which it receives dividends in any taxable year shall—

"(1) to the extent such dividends are paid by such foreign corporation out of accumulated profits (as defined in subsection (c)(1)(A)) of a year for which such foreign corporation is not a less developed country corporation, be deemed to have paid the same proportion of any income, war profits, or excess profits taxes paid or deemed to be paid by such foreign corporation to any foreign country or to any possession of the United States on or with respect to such accumulated profits, which the amount of such dividends (determined without regard to section 78) bears to the amount of such accumulated profits in excess of such income, war profits, and excess profits taxes (other than those deemed paid); and

"(2) to the extent such dividends are paid by such foreign corporation out of accumulated profits (as defined in subsection (c)(1)(B)) of a year for which such foreign corporation is a less developed country corporation, be deemed to have paid the same proportion of any income, war profits, or excess profits taxes paid or deemed to be paid by such foreign corporation to any foreign country or to any possession of the United States on or with respect to such accumulated profits, which the amount of such dividends bears to the amount of such accumulated profits.

"(b) FOREIGN SUBSIDIARY OF FOREIGN CORPORATION.—If such foreign corporation owns 50 percent or more of the voting stock of another foreign corporation from which it receives dividends in any taxable year, it shall be deemed to have paid the same proportion of any income, war profits, or excess profits taxes paid by such other foreign corporation to any foreign country or to any possession of the United States, on or with respect to the accumulated profits of the corporation from which such dividends were paid which—

"(1) for purposes of applying subsection (a)(1), the amount of such dividends bears to the amount of the accumulated profits (as defined in subsection (c)(1)(A)) of such other foreign corporation from which such dividends were paid in excess of such in-

come, war profits, and excess profit taxes, or

"(2) for purposes of applying subsection (a) (2), the amount of such dividends bears to the amount of the accumulated profits (as defined in subsection (c) (1) (B)) of such other foreign corporation from which such dividends were paid.

"(c) APPLICABLE RULES.—

"(1) ACCUMULATED PROFITS DEFINED.—For purposes of this section, the term 'accumulated profits' means with respect to any foreign corporation—

"(A) for purposes of subsections (a) (1) and (b) (1), the amount of its gains, profits, or income computed without reduction by the amount of the income, war profits, and excess profits taxes imposed on or with respect to such profits or income by any foreign country or any possession of the United States; and

"(B) for purposes of subsections (a) (2) and (b) (2), the amount of its gains, profits, or income in excess of the income, war profits, and excess profits taxes imposed on or with respect to such profits or income.

The Secretary or his delegate shall have full power to determine from the accumulated profits of what year or years such dividends were paid, treating dividends paid in the first 60 days of any year as having been paid from the accumulated profits of the preceding year or years (unless to his satisfaction shown otherwise), and in other respects treating dividends as having been paid from the most recently accumulated gains, profits, or earnings.

"(2) ACCOUNTING PERIODS.—In the case of a foreign corporation, the income, war profits, and excess profits taxes of which are determined on the basis of an accounting period of less than 1 year, the word 'year' as used in this subsection shall be construed to mean such accounting period.

"(d) LESS DEVELOPED COUNTRY CORPORATION DEFINED.—For purposes of this section, the term 'less developed country corporation' means—

"(1) a foreign corporation which, for its taxable year, is a less developed country corporation within the meaning of section 955 (c) (1) or (2), and

"(2) a foreign corporation which owns 10 percent or more of the total combined voting power of all classes of stock entitled to vote of a foreign corporation which is a less developed country corporation within the meaning of section 955(c) (1), and—

"(A) 80 percent or more of the gross income of which for its taxable year meets the requirement of section 955(c) (1) (A); and

"(B) 80 percent or more in value of the assets of which on each day of such year consists of property described in section 955 (c) (1) (B).

A foreign corporation which is a less developed country corporation for its first taxable year beginning after December 31, 1962, shall, for purposes of this section, be treated as having been a less developed country corporation for each of its taxable years beginning before January 1, 1963.

"(e) CROSS REFERENCES.—

"(1) For inclusion in gross income of an amount equal to taxes deemed paid under subsection (a) (1), see section 78.

"(2) For application of subsections (a) and (b) with respect to taxes deemed paid in a prior taxable year by a United States shareholder with respect to a controlled foreign corporation, see section 960.

"(3) For reduction of credit with respect to dividends paid out of accumulated profits for years for which certain information is not furnished, see section 6038."

Mr. KERR. Madam President, I move that the Senate reconsider the vote by which the amendment was agreed to.

Mr. BUSH. Madam President, I move to lay that motion on the table.

The motion to lay on the table was agreed to.

Mr. KERR. Madam President, a parliamentary inquiry.

The PRESIDING OFFICER. The Senator will state it.

Mr. KERR. Does that dispose of all committee amendments?

The PRESIDING OFFICER. All committee amendments have been disposed of. The bill, as amended, under the original agreement, is treated as original text for the purpose of amendment. Are there further amendments to be proposed?

Mr. KERR. Madam President, is the third reading in order?

Mr. KUCHEL. Madam President, I call up my amendment identified as "8-24-62—H."

The PRESIDING OFFICER. The amendment will be stated.

The LEGISLATIVE CLERK. On page 391, between lines 21 and 22, it is proposed to insert the following new section:

SEC. 27. EXCLUSION FROM GROSS INCOME OF CERTAIN AWARDS MADE PURSUANT TO EVACUATION CLAIMS OF AMERICAN-JAPANESE INDIVIDUALS.

(a) IN GENERAL.—No amount received as an award under the Act entitled "An Act to authorize the Attorney General to adjudicate certain claims resulting from evacuation of certain persons of Japanese ancestry under military orders", approved July 2, 1948, as amended by Public Law 116, Eighty-second Congress, and Public Law 673, Eighty-fourth Congress (50 U.S.C. App., secs. 1981-1987), shall be included in gross income for purposes of chapter 1 of the Internal Revenue Code of 1939 or chapter 1 of the Internal Revenue Code of 1954.

(b) EFFECTIVE DATE, ETC.—Subsection (a) shall apply with respect to taxable years ending after July 2, 1948. If refund or credit of any overpayment of Federal income tax resulting from the application of subsection (a) (including interest, additions to the tax, additional amounts, and penalties) is prevented on the date of the enactment of this Act, or within one year from such date, by the operation of any law or rule of law, the refund or credit of such overpayment may nevertheless be made or allowed if claim therefor is filed within one year after the date of enactment of this Act. In the case of a claim to which the preceding sentence applies, the amount to be refunded or credited as an overpayment shall not be diminished by any credit or set-off based upon any item other than the amount of the award referred to in subsection (a). No interest shall be allowed or paid on any overpayment resulting from the application of this section.

On page 391, line 22, strike out "27" and insert in lieu thereof "28".

Mr. KUCHEL. Madam President, in the early days of the Second World War, a group of American citizens of Japanese extraction, who lived in my State of California, as well as in the States of Oregon and Washington, were suddenly and summarily removed inland by the American Military Establishment. Behind them they left their homes and their businesses, their real property and their personal property, most of it improved, some of it in fee title, other under leasehold, representing, in every

instance, what they had been able to accumulate and save through long years of honest toil.

That act by the United States against some Americans was a cruel thing, and the American people ever since have hung their heads in shame as they recall it.

In the successful prosecution of the war against Imperial Japan, Nazi Germany, and Fascist Italy, no Americans fought more gallantly or more bravely than did the Nisei, who with valor and with courage wore the American military uniform and fought heroically for their beloved country, the United States of America. Many shed blood, many gave their lives for America.

At the war's end, Congress recognized the injustice which had been done, and legislation was passed by which a token payment by way of restitution might be awarded to those injured and aggrieved citizens. The distinguished senior Senator from Kentucky [Mr. COOPER] and the distinguished senior Senator from Washington [Mr. MAGNUSON] were Members of the Senate at that time and helped Congress pass that remedial legislation.

In the hearings which were held then, the Secretary of the Interior, Mr. Julius Krug, among others, testified that the Government of the United States needed to make some modicum of award to our fellow Americans who, when they were yanked away from their homes and their businesses, suffered a tragic loss and, when later they were permitted to return, found their homes in disarray, found their leaseholds broken, found their businesses completely destroyed.

So, in 1948, Congress passed the Japanese-American Evacuation Claims Act which established a procedure for handling the thousands of claims which had arisen from the forced evacuation of these American citizens. This act was amended 3 years later, in 1951, when Congress authorized the Attorney General to compromise and settle all claims up to three-quarters of the amount of compensable items, or \$2,500, whichever was less. Thus as a condition, precedent to an award, an individual had to agree to an automatic 25-percent deduction of his allowable items. Now, on top of this fact that a claimant automatically had to declare a smaller than actual loss, the Internal Revenue Service recently announced that these awards were subject to taxation. If the Internal Revenue Service were correct in its interpretation of the law, then the Government of the United States would be adding insult to the injury already done American citizens of Japanese extraction.

I have written to and spoken with the Commissioner of Internal Revenue, Mr. Mortimer M. Caplin, on this matter. To his eternal credit Mr. Caplin said, "Senator, you may say publicly that I look with great sympathy upon what you are trying to do."

One month ago I introduced an amendment to the bill now before the Senate which would prevent the Internal Revenue Service from taking away,

under the guise of taxation, a portion of the modest awards made by the Government under the 1948 act, as amended. Various bills seeking the same result were introduced in the House of Representatives, and one of them, H.R. 12719, as reported by the House Committee on Ways and Means, passed the House today.

Mr. MANSFIELD. Madam President, will the Senator yield?

Mr. KUCHEL. I yield.

Mr. MANSFIELD. It is my understanding that this proposal, which I think is meritorious, has the approval of the Internal Revenue Service; at least, the Internal Revenue Service looks upon it with favor.

Mr. KUCHEL. I am pleased to tell the majority leader that the Commissioner of Internal Revenue says that he is sympathetic to the proposed legislation.

Mr. MANSFIELD. The Treasury Department states that the bill is noncontroversial as well as nonpartisan.

Mr. KUCHEL. I think that is correct. I am pleased at the number of cosponsors who have voluntarily joined with me in offering the amendment.

Madam President, I ask unanimous consent that the names of the distinguished Senator from Kentucky [Mr. COOPER], the Senator from Colorado [Mr. CARROLL], and the junior Senator from Idaho [Mr. JORDAN] be added as cosponsors of the amendment.

The PRESIDING OFFICER. Without objection, it is so ordered.

Mr. MANSFIELD. As I read the report on the bill which passed the House, H.R. 12179, I note that it states:

This bill has been reported unanimously by your committee. The Treasury Department has indicated that although as a general rule it would not favor exempting awards from tax, under the special circumstances involved in these cases it does not interpose any objection to the bill.

I hope the committee will see fit to accept the amendment.

Mr. KERR. I refer to the language on page 2, line 11:

If the refund or credit—

And the language in line 16:

The refund or credit of such overpayment may nevertheless be made—

And on line 20:

The amount to be refunded or credited—

In order that there may be no doubt as to there being no refund involved, would the Senator from California be willing to delete the words "the refund or credit of such overpayment may nevertheless be made or allowed"?

Mr. KUCHEL. No. In all frankness, it is my understanding that the Internal Revenue Service has made this announcement, but so far there has been no imposition of the tax which it contends is due.

I think this language has been placed in the bill simply out of an abundance of caution, so that were there to be such a transaction, then the injured or aggrieved American would have a right to reclaim moneys.

Mr. MANSFIELD. Again, I read from the report of the House Committee on

Ways and Means under date of August 20, to accompany H.R. 12719, under the heading "General Explanation of Provisions."

The treatment described above is to apply to taxable years ending after July 2, 1948, the date of enactment of the Japanese-American Evacuation Claims Act. If any refund or credit (including interest, penalties, and so forth) of an overpayment of Federal income tax arising from the tax treatment described above, is prevented at the time of the enactment of this bill, or within the following 12 months, by any law or rule of law (whether or not a compromise or closing agreement), the refund or credit is, nevertheless, to be made if a claim is filed within 1 year after the date of enactment of this bill.

Where amounts are refunded or credited under this bill in cases where the period of limitations has run, these refunds or credits are not to be decreased by credits or setoffs for other items where the taxpayer paid less than the amount properly due. However, this does not prevent resulting adjustments (upward or downward) in other items which may have been increased or decreased as a result of the inclusion of the award in income.

Mr. KERR. Has the Senator from Montana read from the report or from the bill?

Mr. MANSFIELD. I have read from the report.

Mr. KERR. Does the Senator know whether the amendment before us is identical with the bill as passed by the House?

Mr. MANSFIELD. It is my understanding that it is.

Mr. KUCHEL. That is precisely correct.

Mr. KERR. If it is not, will the Senator amend the amendment in order to have it conform to the bill as passed by the House?

Mr. KUCHEL. I assure the Senator from Oklahoma that that is precisely the fact.

Mr. KERR. If the Senator can give that assurance, and if he will verify it by agreeing that if there is any difference, he will amend the amendment in order to have it conform to the bill as passed by the House—

Mr. KUCHEL. I do.

Mr. KERR. Madam President, with that assurance, I accept the amendment.

Mr. PROXMIRE. Madam President, will the Senator from California yield?

Mr. KUCHEL. I yield.

Mr. PROXMIRE. Can the Senator from California state whether the amendment will have any effect on the revenue or the receipts of the Government; and, if so, what the effect would be?

Mr. KUCHEL. There would be an effect on the revenue, because if the Americans to whom these awards were given by act of Congress were to have their awards subjected to tax, as the Internal Revenue Service now intends to do, to that extent some parts of the awards would be taken from these fellow citizens and the Treasury would consequently receive some additional revenue. But I do not believe that the Congress, in passing the 1948 act, contemplated that these awards would be subject to taxation. The Senator from

Kentucky [Mr. COOPER], who helped guide the original bill through the Senate, has confirmed this fact in conversations with me on this matter.

However, to answer the Senator's question: If this measure is enacted, it will prevent the Internal Revenue Service from taxing any part of the awards previously made by the Government under the Japanese-American Evacuation Claims Act of 1948, as amended.

Mr. PROXMIRE. Do I correctly understand that there is no estimate of what that would be?

Mr. KUCHEL. That is correct.

Mr. PROXMIRE. The bill has been passed by the House, has it?

Mr. KUCHEL. Yes, it has.

Mr. PROXMIRE. And the bill is now pending in the Senate, is it?

Mr. KUCHEL. I do not know whether it is yet here. My amendment was first introduced on July 31. It was modified on August 24 to conform with the language reported by the House Committee on Ways and Means on August 20. Thus my present amendment and its predecessor have been before the Senate for a month.

Mr. PROXMIRE. I wonder whether the tax bill should be a vehicle for additional bills. I have no objection to this one, but I wonder about adding it to the tax bill.

Mr. KUCHEL. This should be done, because this amendment relates to an urgent situation, and the amendment is in the public interest. Furthermore, the Senate probably is unanimously in favor of this provision; and I believe it to be my duty and also the duty of other Senators to have the bill, as passed, include this amendment.

Mr. PROXMIRE. Certainly it is my general feeling that it is bad policy to add to a tax bill amendments which relate to other matters.

Mr. KUCHEL. Yes; but I say this amendment does not constitute special legislation.

The PRESIDING OFFICER. The question is on agreeing to the amendment of the Senator from California.

The amendment was agreed to.

Mr. KUCHEL. Madam President, I move that the vote by which the amendment was agreed to be reconsidered.

Mr. DIRKSEN. Madam President, I move that the motion to reconsider be laid on the table.

The motion to lay on the table was agreed to.

Mr. KUCHEL. Madam President, I wish to say to my able friend, the Senator from Oklahoma [Mr. KERR] that I appreciate the grace with which he has accepted my amendment, and I thank him for it from the bottom of my heart. I am very grateful.

Madam President, I ask consent that the amendment just adopted, a copy of my letter to Commissioner Caplin, various editorials on this matter, and portions of an excellent memorandum on this subject prepared by the Japanese-American Citizens League be included at this point in the RECORD.

There being no objection, the material was ordered to be printed in the RECORD, as follows:

AMENDMENTS TO H.R. 10650 BY MR. KUCHEL (FOR HIMSELF, MR. BENNETT, MR. MAGNUSON, MR. JACKSON, MRS. NEUBERGER, MR. MORSE, MR. MCCARTHY, MR. CARROLL, MR. COOPER, MR. JORDAN OF IDAHO, AND MR. ENGLE) TO THE BILL (H.R. 10650) TO AMEND THE INTERNAL REVENUE CODE OF 1954 TO PROVIDE A CREDIT FOR INVESTMENT IN CERTAIN DEPRECIABLE PROPERTY, TO ELIMINATE CERTAIN DEFECTS AND INEQUITIES, AND FOR OTHER PURPOSES

On page 391, between lines 21 and 22, insert the following new section:

"SEC. 27. EXCLUSION FROM GROSS INCOME OF CERTAIN AWARDS MADE PURSUANT TO EVACUATION CLAIMS OF AMERICAN-JAPANESE INDIVIDUALS.

"(a) IN GENERAL.—No amount received as an award under the Act entitled 'An Act to authorize the Attorney General to adjudicate certain claims resulting from evacuation of certain persons of Japanese ancestry under military orders', approved July 2, 1948, as amended by Public Law 116, Eighty-second Congress, and Public Law 673, Eighty-fourth Congress (50 U.S.C. App., secs. 1981-1987), shall be included in gross income for purposes of chapter 1 of the Internal Revenue Code of 1939 or chapter 1 of the Internal Revenue Code of 1954.

"(b) EFFECTIVE DATE, ETC.—Subsection (a) shall apply with respect to taxable years ending after July 2, 1948. If refund or credit of any overpayment of Federal income tax resulting from the application of subsection (a) (including interest, additions to the tax, additional amounts, and penalties) is prevented on the date of the enactment of this Act, or within one year from such date, by the operation of any law or rule of law, the refund or credit of such overpayment may nevertheless be made or allowed if claim therefor is filed within one year after the date of enactment of this Act. In the case of a claim to which the preceding sentence applies, the amount to be refunded or credited as an overpayment shall not be diminished by any credit or set-off based upon any item other than the amount of the award referred to in subsection (a). No interest shall be allowed or paid on any overpayment resulting from the application of this section."

On page 391, line 22, strike out "27" and insert in lieu thereof "28".

U.S. SENATE,
August 1, 1962.

HON. MORTIMER M. CAPLIN,
Commissioner, Internal Revenue Service,
Department of the Treasury, Washington, D.C.

DEAR COMMISSIONER CAPLIN: I believe all Americans share the feeling that a grievous wrong was done to American citizens of Japanese ancestry when they were forcibly evicted, by military orders, during the Second World War from their homes and places of business on the Pacific coast. An embarrassed nation sought to rectify this constitutional and human wrong when Congress, in 1948, authorized the Attorney General to adjudicate the claims of persons of Japanese ancestry against the United States for losses arising from their forced evacuation.

The Federal Reserve Bank of San Francisco early in 1942 estimated that the real and personal property losses of the 110,000 evacuees would approximate \$400 million. When the evacuation claims program was liquidated by the Department of Justice in 1958, \$36,874,240.29 had been paid out; 26,552 claims had been considered.

When the Truman administration recommended this legislation in 1947, then Secretary of the Interior Krug succinctly stated the hectic conditions of the evacuation: "Merchants had to dispose of their stocks and business at sacrifice prices. In a setting

of confusion and hysteria, many evacuees sold personal possessions for a small fraction of their value. A large number had to accept totally inadequate arrangements for protection and management of property. Valuable leasehold interests had to be abandoned." Vandalism, theft, fires, and property damage were prevalent. Property records were sometimes inadequate, mislaid, or lost.

Three years after the passage of the 1948 act, the Department of Justice in 1951 recommended that Congress authorize the Attorney General to compromise and settle all claims up to three quarters of the amount of the compensable items, or \$2,500, whichever was less. Congress agreed to this change and it was approved by the President on August 17, 1951. As a condition precedent to the award, the applicant had to agree to an automatic 25 percent deduction of his allowable items. In addition, there was no appeal procedure.

Thus the claimant was faced with a choice of getting a little bit now and nothing later or, through other procedures including an action in the Court of Claims, waiting several additional years in the hopes of securing a greater amount, but quite possibly securing nothing. The "bird in the hand rather than two in the bush" philosophy is not new to human affairs. Many accepted these awards in full and complete settlement of their claims against the Government. Rising inflation, increasing age, the desire to get reestablished, and the fact that no interest was provided on any award made in the future were certainly material factors in making a determination to accept a smaller and probably inadequate amount.

Regardless of procedure, thousands of these claims have been settled, surveyed by the Internal Revenue Service, and closed. On many of these settlements the statute of limitations has already run.

A few of these claims, however, remain. The Internal Revenue Service apparently has announced that the awards made under the 1948 act, as amended, will now be subject to taxation.

I respectfully disagree with this decision. I do not believe that it can reasonably be construed as the intent of Congress. Such action by the Internal Revenue Service would compound a wrong already long and valiantly borne by American citizens of Japanese ancestry. That the original awards were inadequate, paltry, and late in terms of the damages actually inflicted is clear. At no time in the letters, records, and official hearings pertaining to this vexatious problem have officials of the Federal Government raised the question of subjecting these awards to taxation. The fact that the great majority of the claims are now closed and not subject to taxation would mean that discriminatory treatment is being applied to the remaining few for whom the statute of limitations has not yet run.

I am unable to find any testimony in the action of Congress regarding possible taxation of these awards. The nature of the awards themselves would, it seems to me, negate any such intention by the Congress. I urge you to resolve this matter administratively by overruling the prior position your Service has taken.

May I hear from you.

Very sincerely yours,

THOMAS H. KUCHEL,
U.S. Senator.

[From the San Francisco Chronicle, Aug. 9, 1962]

JUSTICE FOR THE NISEI ON INCOME TAX CLAIMS

In the midst of its larger business of promoting the general welfare, even when that seems to involve killing the President's legislative program, we trust Congress will find time before adjourning to do justice to the unjustly treated Nisei of World War II.

Remedial measures to exempt them from income tax compensation claims have been introduced by Senator THOMAS H. KUCHEL and Representative JOHN F. BALDWIN, of California. These bills resulted from the disclosure that the Internal Revenue Service was demanding tax payments on the claims which Congress had allowed the Nisei to make for losses suffered when they were sent to concentration camps during the war.

The mass evacuation from the Pacific coast of U.S. citizens of Japanese ancestry was a shameful episode for which a tax-exempt compensation is little enough reparation.

In an editorial commenting on the death last June of Gen. John L. De Witt, who was commander of the Western Defense Command during the war, we referred to this episode and noted that it was De Witt who ordered the mass evacuation of all Japanese. While it is true that the order went out from General De Witt's headquarters, it has been called to our attention that the historical record does not warrant the implication that he recommended concentrating the Nisei behind wire-mesh fences.

"Command Decisions," an official history of the episode published by the Office of the Chief of Military History, Department of the Army, discloses that General De Witt went no further than to recommend, in February 1942, that all Japanese should be evacuated from "category A" areas—Los Angeles County, San Diego, and most of the bay area. Under his plan, the Japanese-American citizens were either to accept internment voluntarily or relocate themselves outside these areas. The difference between this option and the forcible removal of Japanese citizens and aliens alike from the entire coast and their incarceration in camps is a substantial one. The official record shows that it was President Roosevelt and his Washington advisers, not De Witt, who were responsible for issuing the order concentrating the Nisei behind wire-mesh fences.

Be that as it may, it is only proper to point out that one of General De Witt's immortal contributions to American culture was delivered later on in testimony before a House Naval Affairs Subcommittee. "A Jap's a Jap," he said, "and it makes no difference if he is an American."

[From the Los Angeles Herald-Examiner,
Aug. 7, 1962]

RIGHTING SOME WRONGS

Heeding the outcries not only from our friends in the Philippines who helped us so much when we were sorely pressed in World War II but the indignation by the U.S. public as well, the House has passed a bill to pay \$73 million in war damage claims to the Philippines. The bill is now before the Senate and action there should be favorable.

Of course, this should have been done a long time ago, but the matter has dragged along. This was a case in which the people of the Philippines suffered war damages while actively aiding our military causes.

Last May the House defeated a similar measure and the public outcry went up that while this country is willing to give overseas aid to so-called neutrals who actually are on the Communist side, it is unwilling to pay its friends their justly deserved war bills.

Another instance in which a wrong should be righted involves the repayment of \$36.9 million to Japanese-American citizens who were deprived of their liberty and property during the relocation of these people on the Pacific coast during the scare that followed the bombing of Pearl Harbor.

Although they were repaid only one-tenth of what they claimed in damages, the Internal Revenue officials have now decided that the small amount repaid is taxable.

California's Senator THOMAS H. KUCHEL has introduced a bill which would make all compensation under the 1957 repayment act nontaxable.

Congress should act swiftly to pass this bill. Perhaps thus we will have two wrongs righted, that to the Philippines and that to loyal Pacific coast Japanese-American citizens.

[From the Los Angeles Times, Aug. 2, 1962]

INSULT ADDED TO INJURY

In the hysteria that followed Pearl Harbor, 80,000 U.S. citizens were deprived of their freedom and property. There was no proof of sabotage or disloyalty, but they were of Japanese ancestry.

An Executive order issued February 19, 1942, by President Roosevelt authorized the exclusion from the Pacific coastal areas of all German and Italian aliens and all Japanese aliens and citizens. A total of 135,000 persons of Japanese origin were thus forced to "relocation centers."

For 20 years non-Japanese Americans have been trying to forget this incident. In 1957 the Congress tried to make amends by passing the National Japanese Evacuation Claims Act.

Unfortunately the \$400 million in claims for property lost by the Nisei were settled for less than 10 cents on the dollar—\$36.9 million. Many Nisei, including members of the much-decorated 442d Combat Team must at times have thought that they would have been better off to have stayed in Japan and been rehabilitated as ex-enemies, for Congress was much more generous with Japan.

But none of us can now ignore the plight of these Nisei. Internal Revenue Service officials have discovered that Congress left a loophole in the compensation act so that the money paid out in claims is taxable.

This, as Senator KUCHEL said, "is adding insult to injury."

Senator KUCHEL this week introduced a bill to right the wrong. His measure would make all compensation under the 1957 act nontaxable. The bill should have high priority in the Congress.

We cannot undo the injury. But we can prevent the added insult.

[From the Los Angeles Examiner, July 24, 1962]

PILING AN INJUSTICE UPON INJUSTICE

The income tax bite now being put upon Japanese-American wartime evacuees from the west coast for compensation awards carries injustice to an extreme few can countenance. The Internal Revenue Service probably has no other recourse under existing law. But if the compensation law is that bad, remedial law is needed and should be promptly written.

The IRS ruling is that compensation awarded for property losses incurred in consequence of evacuation is in part taxable income. Comparison is made with lands seized for freeways. Conscience rejects that interpretation, if law doesn't. And if law doesn't, the statutes should be made to reflect conscience.

The evacuees were never compensated adequately for property losses. There was no indemnification at all for the months and years taken out of their lives, the hardships endured and the humiliation suffered.

The merits of evacuation are not being argued. The facts are. And the facts are that thousands of people with full rights of American citizenship were compelled to leave their homes and businesses and accept imprisonment. We called it relocation, but it was plain and simple incarceration.

Few Americans have easy minds about that now. Congress acknowledged injustice in enactment of the Evacuation Claims Act.

But indemnification seldom covered actual physical loss. Now, because Congress failed to exempt the compensation awards from income tax, IRS feels under compulsion to take back a good part of what was so negligently given.

Instead of the original wrong being righted, new wrongs are being pyramided upon it. Congress should start all over again in setting the record straight. The first thing needed is to put an end to the absurdity that Government can admit a wrong, offer indemnification for it, and then take it back in taxes. Bad as the original injustice was, this rivals it.

[Memorandum from the Washington office, Japanese American Citizens League]

NONTAXABILITY OF JAPANESE-AMERICAN EVACUATION CLAIMS AWARDS

This memorandum is to explain the background and the reasons for the proposed bipartisan amendment, by Senators THOMAS H. KUCHEL, CLAIR ENGLE, WALLACE F. BENNETT, WARREN G. MAGNUSON, HENRY M. JACKSON, WAYNE MORSE, MAURINE B. NEUBERGER, JOHN SHERMAN COOPER, JOHN A. CARROLL, and LEN B. JORDAN, to clarify the congressional intent that awards paid pursuant to the Japanese-American Evacuation Claims Act are not subject to tax. More specifically, the proposed amendment declares that "gross income does not include any amount received as an award" made under the Japanese-American Evacuation Claims Act of 1948, as amended.

The Japanese-American Citizens League (JACL) believes that the proposed amendment correctly states the congressional intent. JACL understands that this is a noncontroversial, bipartisan bill, to which neither the White House nor the Department of the Treasury, including the Internal Revenue Service, interposes any objection.

Identical legislation (H.R. 12719 (by Congressman CECIL R. KING, of California), as amended, H. Rept. 2254, August 20, 1962) was unanimously reported by the House Ways and Means Committee.

In the spring of 1942, the Army evacuated—with trial or hearing, and without individual charges, at a time when the courts were functioning—some 110,000 persons of Japanese ancestry from their homes, businesses, enterprises, employment, and associations on the west coast. Two-thirds of those evacuated were native-born citizens. The remaining third were immigrant alien Japanese who were denied naturalization privileges under Federal law.

These evacuees were permitted to take with them only what they could carry. Under the unique circumstances of evacuation, every evacuee lost something. Most lost almost everything that they had. The Federal Reserve Bank of San Francisco that spring estimated that the evacuees lost some \$400 million in that mass movement.

In July 1948 Congress enacted the Japanese-American Evacuation Claims Act (Public Law 80-886, 62 Stat. 1231 [1948]), authorizing the Attorney General to accept and adjudicate certain claims for damage to or loss of real and personal property suffered as a direct consequence of that 1942 evacuation.

Under the original statute, some 25,000 claims were timely filed, totaling some \$135 million in amount. That only one-third of the estimated loss was even claimed initially under the 1948 law suggests the very limited scope of the legislation in providing partial compensation for evacuation losses.

In 1949 only 21 claims were adjudicated, one of which was dismissed, and awards authorized in the amount of \$6,882, of some \$13,544 originally claimed. In 1950, 211 claims were adjudicated, of which 73 were dismissed. Of the original \$141,374 claimed by the 137 awardees, \$62,595 was authorized in awards.

In August 1951 Congress amended the act (Public Law 82-116, 65 Stat. 192 [1951]), authorizing the Attorney General to compromise and settle timely claims "up to three-quarters the amount of compensable items, or \$2,500, whichever was less." What this meant was that the evacuees in order to secure early and expeditious compromise settlements automatically forfeited 25 percent or more of their compensable awards.

By the end of fiscal 1955, 20,211 claims had been compromised and settled for awards totaling \$24,259,528. The original amount claimed was \$69,185,472. Claims adjudicated numbered 688, for which awards totaling \$1,421,396 were authorized, though the original claims amounted to \$3,404,503. More than a thousand claims for almost \$4 million were dismissed.

In July 1956 Congress further amended the act (Public Law 84-673, 70 Stat. 513 [1956]), to extend the compromise settlement procedure to awards up to \$100,000, and for other purposes.

When the Department of Justice terminated its administrative program in November 1958, it was announced that it had settled 26,552 claims and authorized awards totaling \$36,874,240. Nine claims were filed in the Court of Claims. All in all, including the amendments, 26,568 claims were filed for an aggregate amount of \$147,714,876. With only two claims still pending in the Court of Claims, a total of \$37,442,706 has been awarded pursuant to this law, as amended.

In summary about \$37½ million have been awarded, out of some \$148 million claimed under the law. And, the total originally claimed is about a third of the estimated \$400 million loss sustained in the evacuation.

Beginning late in 1959, the Internal Revenue Service began to question the tax liability of these evacuation claims awards. In September 1961, the Service decided that in the absence of any congressional statement to the contrary, certain of these awards were taxable on the theory that they are comparable to involuntary conversions of property or condemnations.

Although neither the House nor the Senate Judiciary Subcommittees on Claims, respectively, published their hearings on this subject, we have carefully reexamined the voluminous testimony before both these subcommittees and have found nothing to suggest that any of the Government departments involved, or private witnesses who testified, thought that the awards paid in accordance with this legislation would be subject to tax. Moreover, a reexamination of the floor debates in both the House and the Senate in the CONGRESSIONAL RECORD fails to suggest that any Member ever contemplated or intended that part or all of these awards should be considered as taxable. Quite to the contrary, the reports of the Judiciary Committees and the approving comments in both the House and the Senate suggest that these awards were to be considered as "acts of grace".

Furthermore, after the first adjudications were made and when the 1951 and 1956 amendments were being considered, no mention was made anywhere in the record that the awards, or any part thereof, should be subject to tax.

If the Internal Revenue Service felt that these awards might be subject to tax, we submit that it should have come forward at those opportunities to request congressional clarification on this matter, especially since the Attorney General, who was charged with the administration of the statute, was proceeding to adjudicate and to compromise and settle these claims on an entirely different conception of the congressional intent.

The original act, and the subsequent amendments, incidentally, were enacted

unanimously, without objection, in both Houses.

As suggested earlier, in his administration of the program, the Attorney General, in the absence of any specific direction on the matter, determined in his precedent-setting adjudications that these awards were "acts of congressional grace" or "acts of bounty," neither of which, we understand, is taxable.

In the light of this interpretation, the Department of Justice adjudicated and compromised and settled all except about 10 of the more than 26,500 claims filed.

If the Attorney General had interpreted the congressional intent as the Internal Revenue now appears to be doing, we suspect that the basis for determining the amount of the awards would have been significantly different from that which was followed. In this connection, it may be of interest that the Los Angeles and San Francisco newspapers quote former U.S. Attorney General William Rogers, under whose administration most of these claims were settled, as saying (Aug. 4, 1962) "It never had occurred to me that these partial awards were ever to be taxed."

Since the Department of Justice determined the amount of awards on the basis that the claims were "acts of grace" and not subject to taxation, we submit that it is most unfair, inequitable, and unjust for the Internal Revenue Service, after all these years, to now attempt to collect taxes on a theory that was not advanced or utilized by the Attorney General in his administration of the congressionally authorized program.

Although we are not attorneys, and certainly do not pose as tax experts, it appears patent to us that the military evacuation of 1942 cannot be compared reasonably to "involuntary conversions or condemnations," as these terms are generally understood.

Aside from the more obvious differences, it should be remembered that the 1942 mass movement was unprecedented in American history, was directed arbitrarily and solely against a single group of citizens and their parents simply on the basis of their ancestry, and that no other group of citizens or their parents in the same areas were similarly treated.

In "involuntary conversions" and condemnation proceedings, we understand that the private property owners have several rights, that among these are the time and opportunity to freely negotiate the settlement value and, if not satisfied with the Government offer, to appeal to the courts for the "just compensation" to which the Federal Constitution entitles them. Clearly, the circumstances of evacuation did not offer these alternatives to the evacuees.

Furthermore, the awards were paid from almost 10 to 15 years after the losses took place and at 1942, not 1958, values. The drastic personal, group, and community changes in the general economy, circumstances, and situations from 1942 to 1958 made the awards only partial at best. And, because of postwar inflation and other widespread developments, over which the evacuees had little or no control, it was impractical for the evacuees to attempt to replace exactly what they lost, especially since none of the awards were based on replacement value as of the time of the Government payments. An example of the great changes that have taken place on the west coast would be in former farmlands which are now suburban areas.

Indeed, the mere arithmetic of less than 10 cents being paid out in awards for every dollar lost in the evacuation (some \$37 million paid for the estimated \$400 million lost) suggests that the claims program was not intended to be one that would be further reduced by way of taxation.

In any event, the JACL, which has been intimately involved in this program since the

1942 evacuation itself, believes that the Congress that enacted this remedial and corrective "act of grace" should clarify its intent regarding the tax liability of the awards paid by the Government pursuant to congressional authorization.

LOBBYING EXPENSE DEDUCTIONS

Mr. KEFAUVER. Madam President, the provision in the tax bill which provides for deduction of lobbying expenses has been called a sleeper. This is certainly true because it was not proposed by the President and it was written into the bill by the House Ways and Means Committee even though hearings had not been held on the subject. The Treasury Department opposes it.

But it is more than just a sleeper. It is a sleeping giant. It will put lobbying at State, local and Federal levels on a completely new basis and mushroom the efforts of special interest groups to obtain favorable legislation.

If this becomes law, it will do away with a principle which has been in our tax laws since 1919. I do not believe the public should pay the cost of anyone's attempting to influence legislation. I therefore hope the Senate will act favorably on the amendment of my colleague from Tennessee Senator GORE, and the Senator from Illinois, Senator DOUGLAS, which seeks to strike this provision from the bill.

Like many other pieces of recent legislation favoring special interest groups, this has not received the public attention which it deserves. To me, it is a shocking and outrageous proposal that the public should pay, by reduced tax revenues, for lobbying activities for legislation to favor special groups. But, strangely enough, this drastic change in present law has received little attention in the press and I do not believe very many of the American people are aware of it. Section 3 of the bill would allow a deduction for expenses, including traveling expenses, incurred in carrying on any trade or business "in direct connection with appearances before, submission of statements to, or sending communications to, the committees or individual Members of Congress or any legislative body of a State, a possession of the United States, or a political subdivision of any of the foregoing with respect to legislation or proposed legislation of direct interest to the taxpayer."

This means that a corporation or any other business could take a tax deduction for the expenses of coming to Washington, hiring lobbyists or attorneys to prepare statements, or draft amendments, and even the cost of circularizing individual Senators or Representatives. It would have the same effect for lobbying activities before State legislatures and city councils.

Madam President, I hesitate to call this a giveaway because that seems to have the result of helping legislation rather than hurting it lately. But this bill unquestionably will result in a reduction of tax revenues to the Federal Government. I do not think anyone can estimate how much this might be because there is no way of telling. By making lobbying less expensive, it will undoubtedly encourage lobbying. In

fact, I will show in a moment that that is its apparent purpose. We can undoubtedly then expect increased lobbying activities and expect that money will be spent for lobbying which would otherwise have been spent in other ways. When one considers that this will operate to encourage lobbying before every city council and every State legislature as well as the Congress, it is impossible to guess what the total effects of this bill will be. But to the extent that tax deductions are taken for these lobbying activities, those taxpayers' liabilities are reduced and other taxpayers have a correspondingly greater burden. Thus, to the extent these deductions are taken, the cost is transferred to the general public.

This is not only unwise, in that it will mushroom lobbying activities for special interests, but I think it is unfair, and this is the reason why such concessions have never been made in previous laws.

I do not mean to say that lobbying is not a legitimate and often worthwhile activity. It assists Congress in having the aid and viewpoint of groups who are affected by legislation, but I cannot believe that there is such a shortage of lobbying activity that we need to encourage it by tax advantages. It is already unfortunate that there is no lobby for consumers and the public at large to represent their interests in legislation, but it will only compound the one-sided picture we often get if we allow tax incentives to encourage more and better lobbying.

Let us consider what the effects of this legislation might be. As Senator GORE and Senator DOUGLAS pointed out in their very fine minority views in the committee report, a State legislature might be considering a measure designed to decrease stream pollution. A manufacturing company which was perhaps dumping waste in the stream and would be affected by such a law could deduct the costs of sending its lawyers and officials to the State capitol, their room and lodging while staying there and legal fees for the preparation of testimony before committees, proposed amendments and promotional literature circulated to legislators. On the contrary, homeowners or members of the general public interested in pure water for drinking or recreational uses would have to finance their support of such a law entirely from their own pockets with no tax deduction.

Another example cited in the minority views would be that a businessman could deduct expenses of lobbying to change a zoning ordinance which affected his property, but the owners of residences who would also be affected would not benefit from reduced taxes for the cost of their preparing exhibits and briefs to oppose a change.

Let us consider some examples closer to home. A.T. & T. could have deducted from its taxable income the costs of its attorneys and public relations men in working for the communications satellite bill. Businessmen who were concerned with sugar quotas could have deducted the costs of lobbying on the Sugar Act. An American company

which wanted high protective tariffs to avoid competition from imports could deduct the cost of lobbying against the trade bill. These examples could be multiplied many times. And if this bill is enacted, we can expect that the intensive lobbying efforts to which we are often subjected will be multiplied greatly.

When one considers the sort of legislation on the books in the various States, many other examples occur. For instance, the liquor industry could deduct the cost of lobbying for liberalized liquor laws. In a State which has local option for gambling, operators of gambling establishments and manufacturers of gambling devices could pass on to the Federal Treasury a part of the costs of trying to get legalized gambling throughout the State. Individuals who opposed liberalized liquor or gambling laws could not deduct the costs of opposing such legislation.

Another provision of this section authorizes the deduction of that portion of the dues paid to an organization which is attributable to lobbying expenses. In other words, trade associations which conduct lobbying for special groups would now be able to solicit more and bigger dues on the inducement of the tax deduction. But contributions to the League of Women Voters by civic-minded citizens are still not deductible to any extent because it attempts to influence legislation. Thus, associations who represented special interests in legislative matters would be given an advantage over associations which concern themselves with matters of general public interest of a nonbusiness nature.

In the hearings before the Finance Committee, Mr. Stanley H. Ruttenberg, of the AFL-CIO, made a very persuasive argument against this provision. I would like to quote from his testimony on page 610 of the hearings:

I might just say on lobby expenses we strongly urge that this provision be removed from the bill. It is a provision which, in effect, would permit corporations of America to double their amount of expenditure on lobbying, and thereby increase substantially their lobbying activities.

We think that there is no reason to give them tax exemption for lobbying expenses any more than there is reason to give the individual worker who pays dues to his organization the right to deduct expenses for lobbying activities.

The corporation ought to be on the same basis as the individual. The tax-free institutions, the nonprofitable institutions like the U.S. Chamber of Commerce, National Association of Manufacturers, American Farm Bureau Federation, AFL-CIO, other organizations have tax-exempt status and, therefore, their expenditures can be made on various activities.

Only a minor proportion of the AFL-CIO's expenditures are made on lobbying but that fits within the concept of a tax-free organization.

But as far as an individual union member is concerned, any portion of his dues which are attributed to lobbying is not a deductible item on his income tax return just as expenditures by corporations should not be as they are not now an item for deductible allowances. Under this bill such lobbying expenditures now not deductible by corporations would be permitted to be deductible and we think this provision ought to be removed.

Unions represent and protect the workingman's interests in labor legislation and general legislation. The benefits they secure to him are as meaningful as those which business lobbyists secure for their interests. In fact, their interests may be directly opposed in some legislation. Why should not the workingman be allowed the same tax consideration for petitioning his representatives?

Madam President, under the general corporate tax rate of 52 percent, this deduction will cut in half the effective cost of lobbying. As Mr. Ruttenberg pointed out, this will enable them to double expenditures for lobbying with no effect on their profits.

Anyone who thinks this is not intended to accomplish just this result should study the testimony in support of it before the Finance Committee. At page 1960 of part 5, appears the testimony of Mr. George D. Webster, an attorney in the District of Columbia who appeared on behalf of the District Bar Association. He strongly urged enactment of this provision and the language of his testimony at the bottom of page 1961 is almost exactly the same as the language of the Finance Committee report on this provision at page 22 of the report. He said that it appeared anomalous to the association that legal fees for appearances of lawyers before legislative bodies or contacts with individual legislators are not deductible, while such appearances and contacts with tribunals or administrative officials are deductible. The committee report adopts the same language, leaving out only the words "to the association." Mr. Webster went on to say that his association believed that presentations to the legislative branch should not be discriminated against.

I am a member of the legal profession myself, but I do not believe we should raid the Public Treasury in order to increase the use of Washington lawyers for lobbying purposes. Mr. Webster also justified this provision as eliminating discrimination between lawyers' fees in presentations to the legislatures and lawyers' fees in appearances before courts and agencies. The two things are very different. In every court and in every agency, there is an adversary proceeding with someone representing both points of view. This is not true of lobbying for special interests. More often only one side of the picture is heard and the general public or the consumer, or whoever may be affected by the legislation on the other side, is not heard at all. It is for this reason that the costs should not be passed on to the public by tax reductions.

Madam President, in my opinion, this is one of the worst legislative proposals we have considered in a long time. It would increase the imbalance in what is already a deficit tax bill. But worse than that. It is discriminatory and it would multiply lobbying and the effects of lobbying by special interests. I strongly urge my colleagues in the Senate to join me in voting to remove it from the bill and keep present law.

The PRESIDING OFFICER. The bill is open to further amendment.

Mr. McCARTHY. Madam President, I call up my amendment identified as "8-25-62".

The PRESIDING OFFICER. The amendment will be stated.

The Chief Clerk proceeded to read the amendment.

Mr. McCARTHY. Madam President, I ask unanimous consent that the reading of the amendment be dispensed with, and that it be printed at this point in the RECORD.

The PRESIDING OFFICER. Without objection, it is so ordered.

The amendment offered by Mr. McCARTHY is as follows:

SEC. 12. CONTROLLED FOREIGN CORPORATIONS.

(a) IN GENERAL.—Part III of subchapter N of chapter 1 (relating to income from sources without the United States) is amended by adding at the end thereof the following new subpart:

"Subpart F—Controlled Foreign Corporations

"Sec. 951. Amounts included in gross income as the result of improper accumulations.

"Sec. 952. Earnings improperly accumulated.

"Sec. 953. Income from insurance of United States risks included in gross income.

"Sec. 954. Definitions included in gross income.

"Sec. 955. Rules for determining stock ownership.

"Sec. 956. Exclusion from gross income of previously taxed earnings and profits.

"Sec. 957. Special rules for foreign tax credit.

"Sec. 958. Adjustments to basis of stock in controlled foreign corporations and of other property.

"Sec. 959. Miscellaneous provisions.

"SEC. 951. AMOUNTS INCLUDED IN GROSS INCOME AS THE RESULT OF IMPROPER ACCUMULATIONS.

"(a) GENERAL RULE.—If a foreign corporation is a controlled corporation for an uninterrupted period of 30 days or more during any taxable year beginning after December 31, 1962, every person who is a United States shareholder (as defined in section 952(a)) of such a corporation and who owns (within the meaning of section 955(a)) stock in such corporation on the last day in such year, on which such corporation is a controlled foreign corporation shall include in his gross income, for his taxable year in which or with which such taxable year of the corporation ends, his pro rata share (determined under section 952(a)(2)) of the corporation's increase in earnings improperly accumulated.

"(b) LIMITATION ON AMOUNT OF PRO RATA SHARE OF EARNINGS IMPROPERLY ACCUMULATED INCLUDED IN GROSS INCOME.—For purposes of subsection (a), the pro rata share of any person who is a United States shareholder in the increase of the earnings of a controlled foreign corporation improperly accumulated shall not exceed an amount (A) which bears the same ratio to his pro rata share of such increase (as determined under section 952(a)(2)) for the taxable year, as (B) the part of such year during which the corporation is a controlled foreign corporation bears to the entire year.

"(c) COORDINATION WITH PROVISIONS RELATING TO FOREIGN INVESTMENT COMPANY AND FOREIGN INSURANCE OF UNITED STATES RISKS.—A United States shareholder who, for his taxable year is—

"(1) a qualified shareholder (within the meaning of section 1247(c)) of a foreign investment company with respect to which an election under section 1247 is in effect, or

"(2) as the result of the application of section 953 required to take an amount into income,

shall not be required to include in gross income, for such taxable year, any amount under subsection (a) with respect to such foreign investment company or with respect to income taken into account by such shareholder as the result of the application of section 953.

"SEC. 952. EARNINGS IMPROPERLY ACCUMULATED.

"(a) GENERAL RULES.—For purposes of this subpart—

"(1) AMOUNT OF INVESTMENT.—The amount of earnings of a controlled foreign corporation improperly accumulated at the close of any taxable year in the case of a corporation formed or availed of for the purpose of avoiding United States income tax is the aggregate amount of the investment in extraneous property at the close of the taxable year, to the extent such amount does not exceed the sum of (A) the earnings and profits for the taxable year, and (B) the earnings and profits accumulated for prior taxable years beginning after December 31, 1962.

"(2) PRO RATA SHARE OF INCREASE FOR YEAR.—In the case of any person who is a United States shareholder the pro rata share of the increase for any taxable year in the earnings of a controlled foreign corporation improperly accumulated is the amount determined by subtracting—

"(A) his pro rata share of the amount determined under paragraph (1) for the close of the preceding taxable year, reduced by amounts paid during the taxable year or treated as paid during that or prior years as a result of the application of section 951 or 953, from

"(B) his pro rata share of the amount determined under paragraph (1) for the close of the taxable year.

"(3) AMOUNT ATTRIBUTABLE TO PROPERTY.—The amount taken into account under paragraph (1) or (2) with respect to any property shall be its adjusted basis, reduced by any liability to which the property is subject.

"(b) DEFINITION OF INVESTMENT IN EXTRANEOUS PROPERTY.—For purposes of this subpart—

"(1) GENERAL RULE.—The term 'investment in extraneous property' means any money or other property (tangible or intangible) acquired after December 31, 1962, which is beyond the reasonable needs of the business.

"(2) PROPERTY NOT REQUIRING PREPONDERANCE OF EVIDENCE BY TAXPAYER.—Any property other than the following shall be considered property beyond the reasonable needs of the business unless the United States shareholder by the preponderance of the evidence shall prove to the contrary:

"(A) Any money or other property which is located outside the United States and is ordinary and necessary for the active conduct of a trade or business carried on almost wholly without the United States by the controlled foreign corporation.

"(B) Property which would qualify under subparagraph (A) except for the fact that it is located in the United States, but only if such property is—

"(i) obligations of the United States, money, or deposits with persons carrying on the banking business;

"(ii) property purchased in the United States for export to, or for use in, foreign countries;

"(iii) any loan arising in connection with the sale of property if the amount of such loan outstanding at no time during the taxable year exceeds the amount which would be ordinary and necessary to carry on the trade or business of both the lending corporation and the borrowing United States person had the sale been made between unrelated persons;

"(iv) any aircraft, railroad rolling stock, vessel, motor vehicle, or container used in the transportation of persons or property in

foreign commerce and used predominantly outside of the United States; or

"(v) the amount of assets of an insurance company equivalent to the unearned premiums or a reasonable allowance for policy and similar reserves, on outstanding business with respect to contracts which are not contracts described in section 953(c).

"(C) Stock and obligations owned by the controlled foreign corporation in another foreign corporation in which it owns at least 10 percent of the voting stock and 10 percent of the value of all classes of stock; but this subparagraph shall apply only if substantially all of the property of such other foreign corporation is ordinary and necessary for the active conduct of a trade or business engaged in by such corporation almost wholly without the United States.

"(D) Any investment which is required because of restrictions imposed by a foreign country, and any investment which, when made, was so required and which would result in substantial losses if withdrawn.

"(3) HOLDING OR INVESTMENT COMPANY.—The fact that any corporation is a mere holding or investment company shall be prima facie evidence that property held by it is 'investment in extraneous property'.

"(4) SITUS OF CERTAIN PROPERTY.—Property which is an obligation of, or pledges and guarantees made with respect to obligations of, United States persons shall be considered as property located in the United States.

"(5) REASONABLE NEEDS OF THE BUSINESS.—For purposes of this part, the term 'reasonable needs of the business' includes the reasonably anticipated needs of the business.

"Sec. 953. AMOUNTS INCLUDED IN GROSS INCOME WHICH IS INCOME FROM INSURANCE OF UNITED STATES RISKS.

"(a) GENERAL RULE.—If a foreign corporation is a controlled corporation on any day of a taxable year beginning after December 31, 1962, every person who is a United States shareholder (as defined in section 954(b)) of such a corporation who owns (within the meaning of section 955(a)) stock in such corporation on the last day, in such year, in which such a corporation is a controlled foreign corporation shall include in his gross income as a dividend, for his taxable year in which or with which such taxable year of the corporation ends his pro rata share (determined under subsection (b)) of the corporation's income derived from insurance of United States risks (as determined under subsection (c)).

"(b) PRO RATA SHARE OF INCOME DERIVED FROM INSURANCE OF UNITED STATES RISKS.—

"(1) IN GENERAL.—The pro rata share referred to in subsection (a) in the case of any United States person is the amount—

"(A) which would have been distributed with respect to the stock which such person owns (within the meaning of section 955(a)) in such corporation if on the last day, of its taxable year, on which the corporation is a controlled foreign corporation it had distributed pro rata to its shareholders an amount (i) which bears the same ratio to its income derived from insurance of United States risks for the taxable year, as (ii) the part of such year during which the corporation is a controlled foreign corporation bears to the entire year, reduced by

"(B) the amount of any distribution received by any other United States person during such year as a dividend with respect to such stock.

"(2) LIMITATION ON AMOUNT OF PRO RATA SHARE OF INCOME DERIVED FROM INSURANCE OF UNITED STATES RISKS INCLUDED IN GROSS INCOME.—For purposes of subsection (a), the pro rata share of any person who is a United States shareholder in a controlled foreign corporation's income derived from insurance of United States risks shall not exceed an amount (A) which bears the same ratio to his pro rata share of such income for the

taxable year, as (B) the part of such year during which the corporation is a controlled foreign corporation bears to the entire year.

"(c) INCOME FROM INSURANCE OF UNITED STATES RISKS.

"(1) GENERAL RULE.—For purposes of this section, the term 'income derived from the insurance of United States risks' means that income which is attributable to the reinsurance or the issuing of any insurance or annuity contract—

"(A) in connection with property or liability arising out of activity in, or in connection with the lives or health of residents of, the United States, or

"(B) in connection with risks not included in subparagraph (A) as the result of any arrangement whereby another corporation receives a substantially equal amount of premiums or other consideration in respect of any reinsurance or the issuing of any insurance or annuity contract in connection with property or liability arising out of activity in, or in connection with the lives or health of residents of, the United States,

and which (subject to the modifications provided by subparagraphs (A), (B), and (C) of paragraph (2)) would be taxed under subchapter L of this chapter if such income were the income of a domestic insurance corporation. This section shall apply only in the case of a controlled foreign corporation which receives during any taxable year premiums or other consideration in respect of any reinsurance or the issuing of any insurance or annuity contract described in this paragraph in excess of 5 percent of the total of premiums and other consideration received by it during such taxable year in respect of all reinsurance and issuing of insurance and annuity contracts.

"(2) SPECIAL RULES.—For purposes of paragraph (1)—

"(A) In the application of part I of subchapter L, life insurance company taxable income is the gain from operations as defined in section 809(b).

"(B) A corporation which would, if it were a domestic corporation, be taxable under part II of subchapter L shall apply paragraph (1) as if it were taxable under part III of subchapter L.

"(C) The following provisions of subchapter L shall not apply:

"(i) Section 809(d)(4) (operation loss deduction).

"(ii) Section 809(d)(5) (certain nonparticipating contracts).

"(iii) Section 809(d)(6) (group life, accident, and health insurance).

"(iv) Section 809(d)(10) (small business deduction).

"(v) Section 817(b) (gain on property held on December 31, 1958, and certain substituted property acquired after 1958).

"(vi) Section 832(b)(5) (certain capital losses).

"(D) The items referred to in—

"(i) Section 809(c)(1) (relating to gross amount of premiums and other consideration),

"(ii) Section 809(c)(2) (relating to net decrease in reserves),

"(iii) Section 809(d)(2) (relating to net increase in reserves), and

"(iv) Section 832(b)(4) (relating to premiums earned on insurance contracts),

shall be taken into account only to the extent they are in respect of any reinsurance or the issuing of any insurance or annuity contract described in paragraph (1).

"(E) All items of income, expenses, losses, and deductions (other than those taken into account under subparagraph (D)) shall be properly allocated or apportioned under regulations prescribed by the Secretary or his delegate.

"(F) The income derived from insurance of United States risks of any controlled foreign corporation for any taxable year shall

not exceed the earnings and profits of such corporation for such year.

"SEC. 954. DEFINITIONS.

"(a) CONTROLLED FOREIGN CORPORATION.

"(1) GENERAL RULE.—For purposes of this subpart, the term 'controlled foreign corporation' means any foreign corporation of which more than 50 percent of the total combined voting power of all classes of stock entitled to vote is owned (within the meaning of section 955(a)), or is considered as owned by applying the rules of ownership of section 955(b), by United States shareholders on any day during the taxable year of such foreign corporation.

"(2) SPECIAL RULE FOR INSURANCE.—For purposes only of taking into account income described in section 953(c) (relating to income derived from insurance of United States risks), the term 'controlled foreign corporation' includes not only a foreign corporation as defined by paragraph (1) but also one of which more than 25 percent of the total combined voting power of all classes of stock is owned (within the meaning of section 955(a)), or is considered as owned by applying the rules of ownership of section 955(b), by United States shareholders on any day during the taxable year of such corporation, if the gross amount of premiums or other consideration in respect of reinsurance or the issuing of insurance or annuity contracts described in section 953(c), exceeds 75 percent of the gross amount of all premiums or other consideration in respect to all risks.

"(b) UNITED STATES SHAREHOLDERS DEFINED.—For purposes of this subpart, the term 'United States shareholder' means, with respect to any foreign corporation, a United States person (as defined in section 7701(a)(30)) who owns (within the meaning of section 955(a)), or is considered as owning by applying the rules of ownership of section 955(b), 10 percent or more of the total combined voting power of all classes of stock entitled to vote of such foreign corporation.

"SEC. 955. RULES FOR DETERMINING STOCK OWNERSHIP.

"(a) DIRECT AND INDIRECT OWNERSHIP.—

"(1) GENERAL RULE.—For purposes of this subpart, stock owned means—

"(A) stock owned directly, and

"(B) stock owned with the application of paragraph (2).

"(2) STOCK OWNERSHIP THROUGH FOREIGN ENTITIES.—For purposes of subparagraph (B) of paragraph (1), stock owned, directly or indirectly, by or for a foreign corporation, foreign partnership, or foreign trust or foreign estate (within the meaning of section 7701(a)(31)) shall be considered as being owned proportionately by its shareholders, partners, or beneficiaries. Stock considered to be owned by a person by reason of the application of the preceding sentence shall, for purposes of applying such sentence, be treated as actually owned by such person.

"(3) SPECIAL RULE FOR MUTUAL INSURANCE COMPANIES.—For purposes of applying paragraph (1) in the case of a foreign mutual insurance company, the term 'stock' shall include any certificate entitling the holder to voting power in the corporation.

"(b) CONSTRUCTIVE OWNERSHIP.—For purposes of sections 951, 953, and 954, section 318(a) (relating to constructive ownership of stock) shall apply to the extent that the effect is to treat any United States person as a United States shareholder within the meaning of section 954(b) or to treat a foreign corporation as a controlled foreign corporation under section 954(a), except—

"(1) In applying paragraph (1)(A) of section 318(a), stock owned by a nonresident alien individual (other than a foreign trust of foreign estate) shall not be considered as owned by a citizen or by a resident alien individual.

"(2) In applying the first sentence of subparagraphs (A) and (B), and in applying

clause (i) of subparagraph (C), of section 318(a)(2) if a partnership, estate, trust, or corporation owns, directly or indirectly, more than 50 percent of the total combined voting power of all classes of stock entitled to vote of a corporation, it shall be considered as owning all the stock entitled to vote.

"(3) Stock owned by a partnership, estate, trust, or corporation, by reason of the application of the second sentence of subparagraphs (A) and (B), and the application of clause (ii) of subparagraph (C), of section 318(a)(2), shall not be considered as owned by such partnership, estate, trust, or corporation, for the purposes of applying the first sentence of subparagraphs (A) and (B), and in applying clause (i) of subparagraph (C), of section 318(a)(2).

"(4) In applying clause (i) of subparagraph (C) of section 318(a)(2), the 50-percent limitation contained in subparagraph (C) shall not apply.

"(5) The second sentence of subparagraphs (A) and (B), and clause (ii) of subparagraph (C), of section 318(a)(2) shall not be applied so as to consider a United States person as owning stock which is owned by a person who is not a United States person.

"SEC. 956. EXCLUSION FROM GROSS INCOME OF PREVIOUSLY TAXED EARNINGS AND PROFITS.

"(a) EXCLUSION FROM GROSS INCOME OF UNITED STATES PERSONS.—For purposes of this chapter, the earnings and profits for a taxable year of a foreign corporation attributable to amounts which are, or have been, included in the gross income of a United States person under section 951 or 953 shall not, when such amounts are distributed to (or would but for this subsection be included in the gross income of) such shareholder (or any other United States person who acquires from any person any portion of the interest of such United States shareholder in such foreign corporation, but only to the extent of such portion, and subject to such proof of the identity of such interest as the Secretary or his delegate may by regulations prescribe) directly, or indirectly through a chain of ownership described under section 955(a), be again included in the gross income of such United States person (or of such other United States person).

"(b) EXCLUSION FROM GROSS INCOME OF CERTAIN FOREIGN SUBSIDIARIES.—For purposes of sections 951 and 953, the earnings and profits for a taxable year of a controlled foreign corporation attributable to amounts which are, or have been, included in the gross income of a United States shareholder under section 951 or 953, shall not, when distributed through a chain of ownership described under section 955(a), be also included in the gross income of another controlled foreign corporation in such chain for purposes of the application of section 951 and 953 to such other controlled foreign corporation with respect to such United States shareholder (or to any other United States shareholder who acquires from any person any portion of the interest of such United States shareholder in the controlled foreign corporation, but only to the extent of such portion, and subject to such proof of identity of such interest as the Secretary or his delegate may prescribe by regulations).

"(c) ALLOCATION OF DISTRIBUTIONS.—For purposes of subsections (a) and (b), section 316(a) shall be applied by applying paragraph (2) thereof, and then paragraph (1) thereof—

"(1) first to earnings and profits attributable to amounts included in gross income under section 951 or 953, and

"(2) then to other earnings and profits.

"(d) DISTRIBUTIONS EXCLUDED FROM GROSS INCOME NOT TO BE TREATED AS DIVIDENDS.—Except as provided in section 957(a)(3), any distribution excluded from gross income

under subsection (a) shall be treated, for purposes of this chapter, as a distribution which is not a dividend.

"SEC. 957. SPECIAL RULES FOR FOREIGN TAX CREDIT.

"(a) TAXES PAID BY A FOREIGN CORPORATION.—

"(1) GENERAL RULE.—For purposes of subpart A of this part, if there is included, under section 951 or 953, in the gross income of a domestic corporation any amount attributable to earnings and profits—

"(A) of a foreign corporation at least 10 percent of the voting stock of which is directly owned by such domestic corporation, or

"(B) of a foreign corporation at least 50 percent of the voting stock of which is directly owned by a foreign corporation at least 10 percent of the voting stock of which is in turn directly owned by such domestic corporation,

then, under regulations prescribed by the Secretary or his delegate, such domestic corporation shall be deemed to have paid the same proportion of the total income, war profits, and excess profits taxes paid (or deemed paid if paragraph (4) applies) by such foreign corporation to a foreign country or possession of the United States for the taxable year on or with respect to earnings and profits of such foreign corporation which the amount of earnings and profits of such foreign corporation so included in gross income of the domestic corporation bears to the entire amount of the earnings and profits of such foreign corporation for such taxable year.

"(2) TAXES PREVIOUSLY DEEMED PAID BY DOMESTIC CORPORATION.—If a domestic corporation receives a distribution from a foreign corporation, any portion of which is excluded from gross income under section 956, the income, war profits, and excess profits taxes paid or deemed paid by such foreign corporation to any foreign country or to any possession of the United States in connection with the earnings and profits of such foreign corporation from which such distribution is made shall not be taken into account for purposes of section 902, to the extent such taxes were deemed paid by such domestic corporation under paragraph (1) for any prior taxable year.

"(3) TAXES PAID BY FOREIGN CORPORATION AND NOT PREVIOUSLY DEEMED PAID BY DOMESTIC CORPORATION.—Any portion of a distribution from a foreign corporation received by a domestic corporation which is excluded from gross income under section 956(a) shall be treated by the domestic corporation as a dividend, solely for purposes of taking into account under section 902 any income, war profits, or excess profits taxes paid to any foreign country or to any possession of the United States, on or with respect to the accumulated profits of such foreign corporation from which such distribution is made, which were not deemed paid by the domestic corporation under paragraph (1) for any prior taxable year.

"(b) SPECIAL RULES FOR FOREIGN TAX CREDIT IN YEAR OF RECEIPT OF PREVIOUSLY TAXED EARNINGS AND PROFITS.—

"(1) INCREASE IN SECTION 904 LIMITATION.—In the case of any taxpayer who—

"(A) either (i) chose to have the benefits of subpart A of this part for a taxable year in which he was required under section 951 or 953 to include in his gross income an amount in respect of a controlled foreign corporation, or (ii) did not pay or accrue for such taxable year any income, war profits, or excess profits taxes to any foreign country or to any possession of the United States, and

"(B) chooses to have the benefits of subpart A of this part for the taxable year in which he receives a distribution or amount which is excluded from gross income under

section 956(a) and which is attributable to earnings and profits of the controlled foreign corporation which was included in his gross income for the taxable year referred to in subparagraph (A), and

"(C) for the taxable year in which such distribution or amount is received, pays, or is deemed to have paid, or accrues income, war profits, or excess profits taxes to a foreign country or to any possessions of the United States with respect to such distribution or amount,

the applicable limitation under section 904 for the taxable year in which such distribution or amount is received shall be increased as provided in paragraph (2), but such increase shall not exceed the amount of such taxes paid, or deemed paid, or accrued with respect to such distribution or amount.

"(2) AMOUNT OF INCREASE.—The amount of increase of the applicable limitation under section 904(a) for the taxable year in which the distribution or amount referred to in paragraph (1)(B) is received shall be an amount equal to—

"(A) the amount by which the applicable limitation under section 904(a) for the taxable year referred to in paragraph (1)(A) was increased by reason of the inclusion in gross income under section 951 or 953 of the amount in respect of the controlled foreign corporation, reduced by

"(B) the amount of any income, war profits, and excess profits taxes paid, or deemed paid, or accrued to any foreign country or possession of the United States which were allowable as a credit under section 901 for the taxable year referred to in paragraph (1)(A) and which would not have been allowable but for the inclusion in gross income of the amount described in subparagraph (A).

"(3) CASES IN WHICH TAXES NOT TO BE ALLOWED AS A DEDUCTION.—In the case of any taxpayer who—

"(A) chose to have the benefits of subpart A of this part for a taxable year in which he was required under section 951 or 953 to include in his gross income an amount in respect of a controlled foreign corporation, and

"(B) does not choose to have the benefits of subpart A of this part for the taxable year in which he receives a distribution or amount which is excluded from gross income under section 956(a) and which is attributable to earnings and profits of the controlled foreign corporation which was included in his gross income for the taxable year referred to in subparagraph (A),

no deduction shall be allowed under section 164 for the taxable year in which such distribution or amount is received for any income, war profits, or excess profits taxes paid or accrued to any foreign country or to any possession of the United States on or with respect to such distribution or amount.

"(4) INSUFFICIENT TAXABLE INCOME.—If an increase in the limitation under this subsection exceeds the tax imposed by this chapter for such year, the amount of such excess shall be deemed an overpayment of tax for such year.

"SEC. 958. ADJUSTMENTS TO BASIS OF STOCK IN CONTROLLED FOREIGN CORPORATION AND OF OTHER PROPERTY.

"(a) INCREASE IN BASIS.—Under regulations prescribed by the Secretary or his delegate, the basis of a United States shareholder's stock in a controlled foreign corporation, and the basis of property of a United States shareholder by reason of which he is considered under section 955(a)(2) as owning stock of a controlled foreign corporation, shall be increased by the amount required to be included in his gross income under section 951 or 953 with respect to such stock or with respect to such property, as the case may be, but only to the extent to which such amount was included in the gross income of such shareholder.

"(1) IN GENERAL.—Under regulations prescribed by the Secretary or his delegate, the adjusted basis of stock or other property with respect to which a United States shareholder receives an amount which is excluded from gross income under section 956(a) shall be reduced by the amount so excluded.

"(2) AMOUNT IN EXCESS OF BASES.—To the extent that an amount excluded from gross income under section 956(a) exceeds the adjusted basis of the stock or other property with respect to which it is received, the amount shall be treated as gain from the sale or exchange of property.

"SEC. 959. MISCELLANEOUS PROVISIONS.

"(a) EARNINGS AND PROFITS.—For purposes of this subpart, the earnings and profits of any foreign corporation, and the deficit in earnings and profits of any foreign corporation, for any taxable year shall be determined according to rules substantially similar to those applicable to domestic corporations, under regulations prescribed by the Secretary or his delegate.

"(b) BLOCKED FOREIGN INCOME.—Under regulations prescribed by the Secretary or his delegate, no part of the earnings and profits of a controlled foreign corporation for any taxable year shall be included in earnings and profits for purposes of this subpart, if it is established to the satisfaction of the Secretary or his delegate that such part could not have been distributed by the controlled foreign corporation to U.S. shareholders who own (within the meaning of section 955(a)) stock of such controlled foreign corporation because of currency or other restrictions or limitations imposed under the laws of any foreign country.

"(c) RECORDS AND ACCOUNTS OF UNITED STATES SHAREHOLDERS.—The Secretary or his delegate may by regulations require each person who is, or has been, a United States shareholder of a controlled foreign corporation to maintain such records and accounts as may be prescribed by such regulations as necessary to carry out the provisions of this subpart."

"(b) TECHNICAL AND CLERICAL AMENDMENTS.—

(1) Section 551(b) (relating to foreign personal holding company income included in gross income of United States shareholders) is amended by adding at the end thereof the following new sentence: "The amount included in the gross income of any United States shareholder for any taxable year under the preceding sentence shall be reduced by such shareholder's proportionate share of the undistributed personal holding company income which is included in his gross income under section 951 or 953 (relating to certain amounts included in gross income of United States shareholders) for such taxable year as his pro rata share of the company's earnings improperly accumulated in income derived from insurance of United States risks, as the case may be.

(2) Section 901 (relating to foreign tax credit) is amended by striking out "section 902" and inserting in lieu thereof "sections 902 and 957".

(3) Section 902(e) is amended to read as follows:

"(e) CROSS REFERENCES.—

"(1) For application of subsections (a) and (b) with respect to taxes deemed paid in a prior taxable year by a United States shareholder with respect to a controlled foreign corporation, see section 957.

"(2) For reduction of credit with respect to dividends paid out of accumulated profits for years for which certain information is not furnished, see section 6038."

(4) Section 904(f) is amended to read as follows:

"(f) CROSS REFERENCES.—

"(1) For increase of applicable limitation under subsection (a) for taxes paid with respect to amounts received which were in-

cluded in the gross income of the taxpayer for a prior taxable year as a United States shareholder with respect to a controlled foreign corporation, see section 957(b).

"(2) For special rule relating to the application of the credit provided by section 901 in the case of affiliated groups which include Western Hemisphere trade corporations for years in which the limitation provided by subsection (a)(2) applies, see section 1503(d)."

(5) The table of subparts for part III of subchapter N of chapter 1 is amended by adding at the end thereof the following:

"Subpart F. Controlled foreign corporations."

(6) Section 1016(a) (relating to adjustments to basis) is amended—

(A) by striking out the period at the end of paragraph (18) and inserting in lieu thereof a semicolon; and

(B) by adding after paragraph (18) the following new paragraph:

"(1) to the extent provided in section 958 in the case of stock in controlled foreign corporations (or foreign corporations which were controlled foreign corporations) and of property by reason of which a person is considered as owning such stock."

(c) EFFECTIVE DATE.—The amendments made by this section shall apply with respect to taxable years of foreign corporations beginning after December 31, 1962, and to taxable years of United States shareholders within which or with which such taxable years of such foreign corporations end.

ORDER FOR ADJOURNMENT UNTIL 10 A.M. TOMORROW

Mr. MANSFIELD. Madam President, I ask unanimous consent that when the Senate concludes its session tonight, it adjourn to meet at 10 o'clock tomorrow morning.

The PRESIDING OFFICER. Without objection, it is so ordered.

INCORPORATION OF SEA CADET CORPS OF AMERICA

The PRESIDING OFFICER laid before the Senate the amendments of the House of Representatives to the bill (S. 1308) to incorporate the Sea Cadet Corps of America, and for other purposes, which were, on page 4, line 23, after "title" insert "and for not more than one year thereafter,"; on page 5, line 8, strike out "three" and insert "ten"; on page 5, line 9, strike out "fifteen" and insert "twenty-five"; on page 7, line 20, strike out all after "(a)" down through and including "standards." in line 23, and insert "The accounts of the corporation shall be audited annually in accordance with generally accepted auditing standards by independent certified public accountants or independent licensed public accountants, certified or licensed by a regulatory authority of a State or other political subdivision of the United States."

And to amend the title so as to read: "An Act to incorporate the Naval Sea Cadet Corps."

Mr. DIRKSEN. Madam President, the only amendments added by the House were amendments to require an audit of this corporation, which is a Federal corporation. I move that the Senate concur in the amendments of the House.

The PRESIDING OFFICER. The question is on agreeing to the motion of the Senator from Illinois.

The motion was agreed to.

REVENUE ACT OF 1962

The Senate resumed the consideration of the bill (H.R. 10650) to amend the Internal Revenue Code of 1954 to provide a credit for investment in certain depreciable property, to eliminate certain defects and inequities, and for other purposes.

ORDER OF BUSINESS FOR TOMORROW

Mr. MANSFIELD. Madam President, I ask unanimous consent that tomorrow, following the convening of the Senate at 10 a.m., under the order now entered, there be no morning hour; that the vote on the pending amendment be taken at 11 o'clock tomorrow morning, and that the time be divided equally between the Senator from Minnesota [Mr. McCARTHY] and the Senator from Oklahoma [Mr. KERR].

The PRESIDING OFFICER. Is there objection? Without objection, it is so ordered.

Mr. MANSFIELD subsequently said: Mr. President, previously I made a unanimous-consent request to the effect that tomorrow the Senate would vote on the McCarthy amendment at 11 o'clock. I should like to change that schedule now, due to circumstances the leadership had not foreseen, to 11:30 a.m., with the time to be equally divided between the Senator from Minnesota [Mr. McCARTHY] and the Senator from Oklahoma [Mr. KERR].

The PRESIDING OFFICER (Mr. TALMADGE in the chair). Is there objection to the unanimous-consent request? The Chair hears none, and it is so ordered.

Mr. MANSFIELD. Mr. President, I ask unanimous consent that at the conclusion of the vote on the McCarthy amendment, that the Senate lay aside the pending business temporarily and consider the independent offices appropriation bill, and that 2 hours be allowed for such consideration, and that at the end of not to exceed 2 hours, the Senate return to the consideration of the tax bill.

The PRESIDING OFFICER. Is there objection to the unanimous-consent request? The Chair hears none, and it is so ordered.

The unanimous-consent agreement was subsequently reduced to writing, as follows:

UNANIMOUS-CONSENT AGREEMENT

Ordered, That at 11:30 a.m. tomorrow (Friday, August 31, 1962), the Senate proceed to vote without further debate on the question of agreeing to the amendment proposed by Mr. McCARTHY, relating to controlled foreign corporations (printed as "8-25-62-B"), to the pending bill H.R. 10650, the Revenue Act of 1962; that the time between the meeting of the Senate at 10 o'clock a.m. and 11:30 o'clock be equally divided and controlled by Mr. McCARTHY and Mr. KERR; that immediately following the vote on the foregoing amendment the said bill be temporarily laid aside; that the Senate then proceed to consider H.R. 12711, the independent offices appropriation bill, for

a period not exceeding 2 hours, after which the consideration of H.R. 10650 shall be resumed. (August 30, 1962.)

Mr. McCARTHY obtained the floor. Mr. CARLSON. Madam President, will the Senator from Minnesota yield briefly to me?

Mr. McCARTHY. I yield, with the understanding that I do not lose the floor.

The PRESIDING OFFICER. Without objection, it is so ordered.

ADMINISTRATIVE DIFFICULTIES INVOLVED IN CURRENT TAXATION OF FOREIGN INCOME

Mr. CARLSON. Madam President, I wish to discuss what I believe to be some of the administrative difficulties involved in the current taxation of foreign income.

We have before us consideration of the proposed Revenue Act of 1962, which is replete with its knotty provisions for taxing shareholders currently on certain types of income which has been earned, but not distributed, by foreign subsidiaries of U.S. taxpayers—if I may be permitted to reduce their essence and intent to simple terms.

Instead of solving the problems presented by oversea operations of this kind, I feel this bill would legislate even more problems into existence. These problems arise partly because these features of the measure appear to be aimed more at regulating the foreign business of U.S. firms than to raising additional revenue, and partly because this proposed legislation has become a patchwork which attempts to correct inequities. But inequities still remain. Indeed, the entire bill is studded with outlandish provisions which will, if enacted into law, create a nightmare of administrative confusion for both taxpayers and the Internal Revenue Service.

I doubt very much that section 12 of the proposed legislation can meet very many of the requirements of a good revenue bill. I am far from convinced, for example, that the tax burden will be a fair and equitable one, particularly when I see such things as the penalty laid upon sales income as differentiated from manufacturing income.

This legislation falls far short of the basic requirement of administrative simplicity which is an important objective in drafting tax legislation. First, let us ask: is the plan easy to administer and the tax easy to collect? Emphatically, no. Not only the taxpayer's determination of the amount to be taxed but also the Internal Revenue Service's collection and auditing activities will be inundated in a sea of paperwork, creating a wasteland of fruitless records and conferences, leading only to arbitrary decisions which will clutter court calendars for years to come. Second, will the tax yield adequate revenue in terms of the cost of collection? The answer must again be no. As we all know, administrative costs run high, and unraveling the tangled knots which these sections are bound to produce will give a vast upward push to our administrative and collection costs.

A good indication of the problems which the tax bill will engender can be

found in the provisions of section 12, where an attempt is made to choke off the so-called tax haven loophole and remedy suitcase operation abuses. This section may well have the desired effect, but the burden of complying with the requirements of this proposal is not limited to those companies which abuse loopholes in the present tax legislation. The problems and costs of compliance are thrust indiscriminately upon all, including the Internal Revenue Service which will share the brunt of the administrative burden with the taxpayer.

The differentiation between so-called "sales" income—or income derived solely from products shipped by an American firm to a foreign subsidiary for resale in another country—and "manufacturing" income is designed, of course, to thwart loopholes and abuses, but in so doing it traverses a maze which may, in many cases, defy solution.

Theoretically, if less than 30 percent of the gross income of the subsidiary is derived from "sales" income, no U.S. tax will be imposed. On the surface this may seem like a reasonable, if somewhat arbitrary, yardstick to ease the administrative burden on a U.S.-controlled foreign subsidiary which is not being used to avoid taxes. But every controlled foreign corporation which does any "sales" business outside its country of incorporation would find it necessary to maintain product-by-product records of purchases from or sales to related corporations, tracing the flow of each product from source to destination. It would be asking a bit too much of the perspicacity of the businessman, in many cases, to expect him to know a year or more in advance what percentage of a foreign subsidiary's earnings might come from "sales" income.

Consequently, the accumulation of such special-requirement information would be necessary whether or not the sales income is eventually equal to 30 percent or more of the foreign corporation's gross income.

Again, complex and costly record-keeping would be required, so that information would be available, accumulated on a current basis, even though not used. Few, if any, foreign corporations maintain their records on the basis of U.S. concepts. To compute earnings and profits as required by section 12 of the bill, a complete transformation of accounting records back to the inception of the foreign subsidiary would be necessary.

In many instances, these records will simply not be available. In short, the Internal Revenue Service is being asked to insure compliance with a statute that often will prove impossible to enforce. We must remember that in situations where local foreign groups own a substantial interest in the corporation, considerable opposition may be leveled against the added accounting burdens imposed by U.S. tax laws. At best, the foreign interest would insist that the costs of additional recordkeeping be borne exclusively by the controlling shareholder in the United States. As a result, these expenses would relate to the U.S. income tax re-

turn, and, to the extent that they are deductible, would like any other ordinary and necessary business expenses be assumed in part by the U.S. Treasury.

Many U.S. companies for good business reasons have organized 100-percent owned foreign distribution subsidiaries to market their products more effectively abroad. Now these companies will be required to set up special purpose records to segregate their earnings by nature and type of income. Local managements will be watching these records closely to check on whether the foreign income will or will not be taxed to the U.S. shareholders currently. Where "sales" income approaches the critical point, each additional foreign sale will be weighed against the possibility of the tax on all "sales" income back in the United States. Although we are engaged in a great competitive struggle for export markets we are now proposing a whole complex of new rules and regulations to hamper this sales effort.

But what about the new provisions for the relief of export trade corporations? Do they avoid the administrative burdens? It is true that the U.S. stockholder would not be taxed currently if the foreign corporation qualifies but let us review briefly what it must establish to qualify:

First. To qualify as an export trade corporation its records must show that at least 90 percent of its income for the prior 3-year period came from sources outside the United States. Its records must also show that at least 75 percent of its income for the same prior 3-year period was from export trade income. But bear in mind that the 75-percent test does not apply if 50 percent or more of the income for the same prior 3-year period is derived from income from agricultural products grown in the United States.

Second. Its records must now reflect the new concept of export trade income. Export trade income results from the sale to an unrelated person; this means the records must separately reflect those sales where there is less than 50 percent common control. Now after it is determined that the sale is made to an unrelated person the records must show that the sale is for use outside the United States. Then, furthermore, the records must show that the export property was manufactured or otherwise originated in the United States.

Third. The records have established that we have an export trade corporation which has export trade income. But the U.S. shareholder may still be taxed on the undistributed income of the export trade corporation if the income arises from the marketing of goods manufactured by the U.S. shareholder. The U.S. shareholder is still taxed on this undistributed export trade income to the extent that it exceeds either of two other factors, which must be established by the records.

The first factor is $1\frac{1}{2}$ times export promotion expenses. The records must show that these export promotion expenses are incurred in connection with export trade income and specifically include salaries, rentals, depreciation, and

any other expenses related to the export trade income. But the records must exclude those expenses incurred in the United States, except where at least 90 percent of each category of expense is incurred outside the United States. So much for the first limiting test on the amount of export trade income which is not taxed currently to the U.S. shareholder.

The second factor limiting tax deferral on export trade income is also computed from records the taxpayer would be required to keep. The tax deferred income is limited to 10 percent of the gross receipts of the export trade income for the tax year. But even after all this, the special recordkeeping does not end here, if the U.S. shareholders is not to be taxed on the undistributed income of the export trade corporation.

Fourth. The records must also show that this income which we now have finally determined is actually invested in export trade assets. In other words, this income must be traced in the records into these specific assets: working capital needed to produce the export trade income; inventory of export property; facilities outside the United States for handling the export products, or evidence of debt executed by unrelated persons who buy export property.

Fifth. The recordkeeping problems which we have observed arise where the export trade company handles only goods manufactured by the U.S. shareholder-manufacturer. The complexity of the administrative problems is vastly increased where the trading company also markets goods of unaffiliated manufacturers. But the tremendous recordkeeping difficulties imposed by this situation defy description.

The administrative burdens involved in supporting export trade corporation relief are so great that taxpayers may be impelled to establish a new sales subsidiary in each separate country to which they export. This reorganization of sales activity would also avoid current taxation of the sales income to the U.S. stockholder. But think of the administrative burdens caused by multiplying sales organizations so that each separate country would have its own separate sales company. For example, instead of one sales company for the Common Market, there would be six sales companies for the Common Market; there would be a multiplicity of sales organizations in each primary marketing area in place of a single corporation. And this extra burden would be imposed at a time when we are trying to encourage exports.

It is not my purpose to dwell on the many cumbersome provisions dealing with the current taxation of foreign income. We have noted just a few of the absurdities which are readily apparent in the tax provisions under consideration. They are, however, typical of the administrative problems which these proposals would unleash for both the taxpayer and the Internal Revenue Service.

Adding up the more obvious problems which this proposed legislation would create leads us to the following conclusions: It will unduly burden the taxpayer

er by requiring him to develop and maintain special records to support his position; it will create a difficult audit problem for the Internal Revenue Service which may lead to a breakdown of audit control; it will be a source of needless controversy between the Service and the taxpayer; it will create a vast stream of litigation which would in turn delay the determination of liability for many years after the close of the tax year in question; and it will disrupt established business relationships in an intensely competitive worldwide business situation.

It is strange, indeed, that at the very time when we are faced with the avowed necessity for greater productivity, we suggest legislation which would siphon off productive manpower into nonproductive and unnecessary activity. So great is the impact of taxes on our economy that countless hours must be spent in determining the effect of taxes on all forms of contemplated business transactions, and in accumulating the information required for the proper administration of tax laws. How much more logical and effective it would be if the talent and effort devoted to tax administration could be directed to increasing the national production of goods and services or even to reducing the cost of production.

We cannot go on forever increasing our administrative burdens if we are to meet the challenge of foreign competition and keep our economy strong. Our foreign competitors are lean and hungry. We should be looking for ways to help business trim the fat from its operations rather than larding it on.

ARMY'S UTILIZATION OF SCIENTISTS AND ENGINEERS CRITICIZED

Mr. PROXMIRE. Mr. President, I have been concerned about the serious shortage of scientific and engineering manpower that we face. In connection with the space authorization earlier this year, I offered an amendment calling for an independent study of the manpower impact of our space effort. Just a few days ago I took part in a discussion with the Senator from Nevada [Mr. CANNON] on this problem, during his fine and thorough speech on the scientific and engineering manpower crisis.

This afternoon I would like to call attention to another aspect of this problem. It concerns the proper utilization of scientific and engineering personnel by our Armed Forces. On the basis of information given to me, it appears that the U.S. Army's critical skills and scientists and engineers programs are by no means affording a satisfactory way of making good use of scientific talent. Young men who are drafted may be assigned to these programs, where ostensibly their scientific skills will be used effectively. Each of these young men has as a minimum some graduate scientific or engineering training. Some have Ph.D.'s; many have master degrees.

Yet there are abundant indications that these able young men frequently waste their time, perform low priority

period of six years in the Standby Reserve of the Army Reserve, Naval Reserve, Marine Corps Reserve, Air Force Reserve, or Coast Guard Reserve."

TRADE EXTENSION ACT OF 1962— VIEWS OF TREASURY DEPARTMENT

Mr. KERR. Mr. President, the memorandum expressing the views of the Treasury on the Trade Extension Act of 1962, H.R. 11970, was not received by the Committee on Finance in time to be printed in the official hearings. I therefore ask unanimous consent that it may be printed in the RECORD.

There being no objection, the memorandum was ordered to be printed in the RECORD, as follows:

THE SECRETARY OF THE TREASURY,
Washington, D.C., August 15, 1962.

Hon. HARRY F. BYRD,
Chairman, Committee on Finance,
U.S. Senate, Washington, D.C.

DEAR MR. CHAIRMAN: Thank you for your letter of July 2, 1962, requesting a report on H.R. 11970, the Trade Expansion Act of 1962. The Treasury Department strongly favors this proposed legislation and urges its enactment.

I believe it to be vital for the President to have the authority which would be granted by this legislation. It would permit us to adjust our trade policies so as to give maximum support to the political, military, and economic aims of the United States. Expansion of our trade is important to our balance of payments and also in meeting the need for more rapid economic growth.

I enclose a memorandum which more fully sets forth the reasons for our support of H.R. 11970. I urge prompt and favorable consideration of the proposed legislation.

Sincerely yours,

DOUGLAS DILLON.

MEMORANDUM FOR SENATE FINANCE COMMITTEE ON PROPOSED TRADE EXPANSION ACT OF 1962 (H.R. 11970) TREASURY DEPARTMENT

The Treasury Department recommends approval of H.R. 11970, the Trade Expansion Act of 1962. It would provide authority which would enable the President to adjust our trade policies so that they can give maximum support to the political, military, and economic aims of the United States. It would contribute greatly to the accomplishment of our national financial objectives, especially to the solution of our balance of payments problem.

Although the United States has a large surplus of exports of goods and services over imports, that surplus is not large enough to meet our other payments. The commercial export surplus of goods and services (excluding exports financed with U.S. aid) was at an annual rate of \$4.6 billion in the first quarter of 1962 and was \$5.1 billion in 1961 and \$4.4 billion in 1960. Commercial surpluses of this magnitude, however, have not been large enough to finance all of the foreign undertakings, public and private, of the United States. The largest items for which provision had to be made in 1961 were: almost \$3 billion to support U.S. military forces abroad, \$2.5 billion for private long-term foreign investment, and \$1.3 billion of economic aid, not provided in the form of U.S. goods and services.

It has proved possible, however, by vigorous attention to the problem, to arrange substantial offsetting transactions. Military cash receipts amounted to \$400 million in 1961 and to more than \$200 million in the first quarter of 1962. Intensive administration efforts are expected to result in further substantial reductions in net dollar outlay

for military expenditures abroad and economic assistance. Almost \$700 million was received in the form of special debt prepayments to the United States in 1961 and substantial further prepayments are being received in 1962. The basic deficit of the United States, which includes all international transactions except the unrecorded items and movements of U.S. private short-term capital, was approximately \$400 million in 1961 as compared with \$1.9 billion in 1960.

Unrecorded transactions, and various types of short-term capital movements, involved additional outflows of \$2 billion in 1961. The overall deficit in the U.S. balance of payments was a little less than \$2.5 billion, compared with \$3.9 billion in 1960. Unrecorded and short-term capital transactions appear to have been more favorable during the first half of 1962. Looking at the data now available, the overall deficit in the first half seems to have been at an annual rate somewhere between \$1 billion and \$1.5 billion.

As the domestic economy grows, American demand for imports will become greater. Despite our best efforts, outlays abroad for the national defense, aid and investment will continue to be large. If these payments are to be met, the United States must export more. The necessary expansion of exports can occur only if, through negotiations, the doors to major foreign markets—and especially the new and expanding Common Market of Western Europe—are opened wider for U.S. products.

The six countries which formed the European Economic Community have now established their common external tariff, and are expected to bring it into full effect when their "transitional period" is over, at the latest by the end of 1969. Also, they are rapidly reducing the tariffs which apply to their trade with one another and are committed to eliminate them altogether by the end of 1969. Their common agricultural policy, and the terms of continued association with newly independent countries which were formerly European colonies, are rapidly taking shape. The United Kingdom is expected to join the European Economic Community, and others may well follow. The resulting expanded Common Market will constitute a giant new economic unit within the free world. If U.S. exports are to be expanded to the necessary extent, liberal access to the Common Market is absolutely essential.

Efforts to achieve balance in the international payments of the United States must not be viewed as a battle in which we can win a decisive victory and then relax. This is a campaign which must be waged successfully year after year. To ensure favorable conditions for that continuing campaign, we must show, by determined action now, the direction American trade policy is going to take. Then foreign governments will know that the United States is resolved to obtain liberalized access to foreign markets for its products and is prepared to bargain realistically for such access. Moreover, investors can then begin without delay to base their forward planning on the premise that it will be economically feasible to supply European markets with products from American factories and farms.

Trade negotiating authority like that which has recently expired would be completely inadequate for the solution of the problems we face, for several reasons. First, if our negotiating authority continues to be subject to unduly narrow and unrealistic procedures for item-by-item determination of possible injury, the basic intention to create authority for broad negotiations covering a wide range of commodities would be frustrated. The Common Market countries, which have found across-the-board techniques the only practicable method for their own tariff negotiations, cannot be expected

to take much interest in further item-by-item bargaining on narrowly selective lists of commodities. Second, if American products are to be competitive with European products, all of which are to gain the right to move, free of duty, across European borders, substantial tariff action is needed. If reductions cannot exceed the 20 percent authority under which negotiations have taken place in the past, at best only marginal changes in our trading prospects could be achieved. Third, tariff reduction by broad categories offers the best way of assuring reciprocity—of obtaining from the Common Market full value in tariff cuts for U.S. reductions.

If broad and substantial mutual tariff reductions by the Common Market and the United States are effected and if American producers, through appropriate tax and other measures, are put on a comparable footing with their European competitors, the resulting expansion of two-way trade can be expected to increase significantly the commercial trade surplus of the United States—with corresponding benefit to the balance-of-payments position.

Commercial merchandise exports of the United States have been \$17.7 billion, and imports have averaged about \$14.6 billion, in each of the last 2 years, giving an annual merchandise trade surplus of about \$3 billion for these years.

Exports in 1961 to the Common Market were about \$3.5 billion and imports \$2.2 billion, giving a surplus of \$1.3 billion. A major part of the surplus resulted from the movement of agricultural goods, which Europe does not export in significant amounts. Even for nonagricultural goods, however, our exports in 1961 to the Common Market countries were valued at \$2.4 billion, and our imports at \$2 billion, giving us a surplus of \$400 million.

The trade surplus gives the United States a favorable basis for improvement of its balance of payments through reciprocal reduction of tariffs. The scope for improvement is greatest in trade with European countries, which have surpluses, arising from transactions other than trade, which they could use readily to finance larger U.S. merchandise trade surpluses.

If tariffs on our exports and imports are reduced to a comparable extent, the natural assumption would be that exports and imports would rise by the same percentage. As a result, the American trade surplus would become larger.

Conditions now evident, and likely to persist for a number of years, make it more likely, however, that American exports to Western Europe would rise by a greater percentage than the exports of Western European countries to the United States. European labor resources and productive capacity are being strained to support present rates of production. The rapid rise of real incomes and the high rate of capital formation prevailing in the European economy may be expected to exert strong pressure toward absorption of increases in output in domestic markets. In addition, European demand may be particularly strong and persistent for products which the United States already has the plant capacity and the labor force to supply in quantity. This is particularly true of (1) machinery associated with the advanced labor-saving methods already well established in the United States, (2) equipment resulting from our intensive research and development programs, and (3) consumer goods which have not been available in Europe, but are coming into use as incomes of ever-larger groups rise toward the American level.

The trade expansion bill is also important in meeting the need for more rapid economic growth. Our principal domestic economic problem is how to stimulate increasing production and jobs. A million and a half

new jobs must be created every year during the present decade to provide for the expected increase in our labor force. In addition, more than a million jobs are needed if unemployment is to be reduced from its present unacceptable level of more than 5½ percent, to a more tolerable level of 4 percent. Finally, there must be employment opportunities for the millions of workers whose present jobs will be affected by advancing technology in the years ahead.

The proposed trade program is designed to be a key portion of our whole effort to meet the need, both for more employment, and for better employment of all our resources. With new trade legislation we may look forward to substantial increases in a wide range of American exports. These will be in lines of production in which we have now, or in which we can achieve, our greatest competitive strength. These will be branches of industry and of agriculture in which our advanced technology and high skills find their greatest role.

Increases of imports, as well as of exports, will result from the reciprocal reduction of tariffs. In a resilient, expanding economy, there will be a minimum of damage from those increased imports. The reduction in tariffs and any resulting increase in imports will be gradual over a period of years. Most of the adjustment to import competition will take place, unnoticed, as part of the dynamic readjustment of our economy which goes on constantly. If the American labor and capital which may have been gradually displaced by imports could be identified, they would not be found idle, but rather, busily engaged in new enterprises, using new methods, furnishing new services, or producing new products, many of them for export markets.

The Treasury Department has particular responsibility for several phases of the administration's general program to stimulate faster application of technical achievements, and to strengthen emphasis upon facing the challenges, and winning the rewards, of more rapid economic growth. While helping to achieve the goals we have set for our domestic economy, these measures will strengthen our ability to meet international competition.

One measure, designed by the Treasury Department to encourage business generally, and to assist it in modernization of machinery and equipment, is the investment credit proposal which the Finance Committee has considered. A second measure is the Treasury Department's recent publication of new guidelines for depreciation in all industries. Substantial reductions in the suggested useful lives of equipment were made, effective immediately.

Revision of depreciation schedules and the investment credit can powerfully assist American manufacturers to modernize and to sell at competitive prices at home and abroad. These tax reforms should be especially valuable to U.S. producers who are, for competitive reasons, forced to speed their replacement of existing equipment with more efficient machinery.

A third tax measure is now proposed. It appears as section 317 of the Trade Expansion bill. Firms found to be eligible for adjustment assistance as a consequence of increased imports could be given tax relief in the form of a 5-year carryback of net operating losses, as contrasted with the usual 3-year carryback. The additional carryback provided by the adjustment assistance provisions of the bill would permit a firm suffering a net operating loss resulting from import competition to receive a refund of taxes paid in previous years. The firm, in accordance with its readjustment plan, would be able to use such tax refunds to finance new investments designed to restore profitable operation.

The impact of imports will be gradual enough to allow almost all of the readjustment to be accomplished through normal retirements of workers, through normal write-offs and abandonment of obsolete production equipment, and the like, just as is the case in response to domestic competition. The adjustment assistance provisions, plus the escape clause, which will be retained, are intended to take care of the cases of hardship that are likely to arise.

The annual expenditure for adjustment assistance to firms would, of course, be very limited in the period before new tariff reductions have been made. Outlays are not expected to exceed \$25 million, however, even in the 5th year, by which time the program will be in full operation. As the program is continued over a period of years, any outlays for loans to firms would be offset to an increasing extent by repayments on prior loans. The additional expenditures arising from benefits to workers under the bill are not expected to exceed \$20 million annually after 5 years.

If the United States does not press for wider trading opportunities, what developments should be expected? Perhaps our principal trading partners would not, in general, resort to increased tariffs against us, or any other deliberate action to curtail our trade opportunities. But, if internal tariffs in the Common Market disappear, and if we have not been able to bargain down the outside tariff wall of the Common Market, it may well prove impossible for the United States to avoid serious shrinkage of our trade surpluses from levels which are already proving inadequate.

H.R. 11970 has been carefully developed to meet the need for more far-reaching trade negotiations, consistent with our goals for the economy of the United States. The trade adjustment program for which this legislation would provide appears financially sound, and can be expected to furnish, at reasonable cost, justified assistance to firms and their employees encountering unusual difficulty in adjusting to changes in tariff rates. Trade legislation of this scope is essential for the achievement and maintenance of a reliable balance between the foreign payments and receipts of the United States in the years ahead.

REVENUE ACT OF 1962

The Senate resumed the consideration of the bill (H.R. 10650) to amend the Internal Revenue Code of 1954 to provide a credit for investment in certain depreciable property, to eliminate certain defects and inequities, and for other purposes.

MR. MCCARTHY. Mr. President, the amendment I am offering is a partial substitute for the Finance Committee's provision relating to controlled foreign corporations, taxes to U.S. shareholders of controlled foreign corporations, and their share of the profits of these corporations which are accumulated beyond the reasonable needs of the business. The profits unreasonably accumulated are taxed to the U.S. shareholders only to the extent of earnings and profits accumulated in taxable years beginning after December 31, 1962. The concepts and procedures followed in determining when profits are accumulated beyond the reasonable needs of the business follow, to the extent feasible, the same concepts provided under present law in taxing domestic corporations on earnings unreasonably accumulated, although the tax imposed is different.

In general terms, the amendment provides that property, other than the following, will be considered property beyond the reasonable needs of the business unless by the preponderance of the evidence proved to the contrary:

First. Property located outside the United States which is ordinary and necessary to a business carried on by the controlled corporations almost wholly without the United States.

Second. Certain specified property necessary to the trade or business outside the United States, even though located in this country. Thus, the amendment would permit the funds to be held in Government obligations and bank accounts in the United States for the foreign business. Similarly, property may be held here for the foreign business if it is purchased for export, if it represents a reasonable loan arising from the foreign business, if it represents certain specified types of transportation equipment used partially within but largely without the United States, or if it represents certain assets of insurance companies.

Third. Stocks or bonds owned by controlled foreign corporation in another foreign corporation in which it has at least a 10-percent interest.

Fourth. Any investments which are required because of restrictions imposed by a foreign country. This would include investments even though not immediately associated with a trade or business if they arise from compensation paid to a company for expropriation of its foreign business or a part of such business.

In addition to taxing to the U.S. shareholders accumulations beyond the reasonable needs of the business, this amendment also taxes to these U.S. shareholders in the case of a controlled foreign corporation income such a company earns from insurance of U.S. risks. This provision in my amendment is practically the same as the first feature of the controlled foreign corporation provisions in the bill as reported by the Finance Committee.

As indicated in the committee report, this is designed to tax what is essentially U.S. insurance business which, through one device or another, has been either issued to, or transferred to, foreign corporations in order to avoid the U.S. corporate income tax on underwriting gains.

I repeat and stress, my amendment is essentially the same in this respect as the provision in the bill as reported by the Finance Committee.

The controlled foreign corporation provision in the Finance Committee versions of this bill in the case of controlled foreign corporation taxes to U.S. shareholders:

First. Income from insurance abroad of U.S. risks;

Second. Income from passive investments, such as dividends, interest, royalties, etc;

Third. Income from sales subsidiaries of U.S. concerns which are incorporated in countries other than that where the principal operations of the foreign business are carried on;

Fourth. Service income from subsidiaries of the basic foreign corporations; and

Fifth. Earnings from foreign operations which are invested in U.S. property which is unrelated to the basic foreign business.

This amendment taxes income from insurance abroad of U.S. risks in substantially the same manner as the Finance Committee bill. In addition, since investments in U.S. property are likely to be classified as beyond the reasonable needs of the business, this amendment essentially treats earnings reinvested in U.S. property in the same manner as the Finance Committee provision.

The basic difference between my amendment, which is cosponsored by the Senator from New York [Mr. JAVITS] and the Finance Committee provision is that the amendment would substitute a tax on funds accumulated beyond the reasonable needs of the business for a tax on investment income, income from sales subsidiaries and income from service subsidiaries.

Questions have been raised as to the effect of the Finance Committee provision, and this amendment, on what has sometimes been described as runaway movie productions. These generally are foreign corporations set up for the production of either a single or a series of motion picture productions. Once the motion pictures are produced, they may be sold to another corporation, or they may be held by the corporation in question for the receipt of movie rental income. Under the Finance Committee provision, if after the sale of the movies the funds were invested in stocks or securities, this income would be taxed to the U.S. shareholders. If the productions were not sold but instead were held for the receipt of rental income, once this income reached 30 percent or more of the total income of the corporation, the Finance Committee provision would tax this income to the U.S. shareholders.

This amendment, if the movie productions were sold and the proceeds invested in stocks or securities, would tax this income to the U.S. shareholders as income beyond the reasonable needs of the business, in the same way it would be taxed under the Finance Committee provision. This would also be true if the films were held for the receipt of rental income unless these proceeds were used in the production of further movies or were used to purchase movies so that the business of the corporation was viewed as leasing motion picture films. It is clear, however, that an unreasonable accumulations tax, coupled with section 15 of the bill which taxes the accumulations of a foreign corporation made in the future at ordinary income tax rates when the foreign operation is liquidated or its stock is sold, would tax earnings from motion picture productions as ordinary income either currently as earned or at the time of the liquidation of the foreign enterprise.

Mr. President, the Committee on Finance held extensive hearings on the question of the manner in which income of domestic corporations which control subsidiaries in foreign countries should be treated; as to how the taxes might be

properly determined, and as to how they might be imposed. The deliberations received a great deal of attention in the financial press of the country, as well as in the general popular press.

I ask unanimous consent to have printed in the RECORD a series of editorials and articles which appeared in the newspapers of this country over the period of the past month or two, touching upon the question of the taxation of foreign income.

One is from the Washington Post and Times Herald and is entitled "Taxation of Foreign Income."

Another is from the Cincinnati Enquirer and bears the title in the form of a question, "Why Cut Our Own Throats?"

A third is from Business Week of May 5, 1962, and makes reference to the provisions of the bill with the lead statement, "Too Confused for Words."

Another is from the New York Herald Tribune, written by Donald I. Rogers, entitled "Hobbling Business."

Another is from the Wall Street Journal and is entitled "How Not To Succeed in the World."

Another is from the Journal of Commerce, with the general title of "Taxing Foreign Earnings."

One is from the Baltimore Sun and relates to the question of "Overseas Investment."

Another is from the Vineland (N.J.) Times Journal and is entitled "Keeping Up With the Times."

One is from the Daily Commercial News of San Francisco, Calif., and is entitled "We Need a Spur—Not a Brake."

Another is from the Camden Chronicle of Camden, S.C., and is entitled "Could Cost Jobs."

One from the Christian Science Monitor is in the form of an article written by George H. Favre and is entitled "Tax Policy in Perspective."

There is a special report from the U.S. News & World Report entitled "Other Side of Overseas Dollars—the Dollars That Flow Back."

From Time magazine, the section on public policy, is an article dealing with the topic of "Those Foreign Profits."

From the Los Angeles (Calif.) Times is an editorial entitled "What Makes the Tax Bill Bad."

The final article is from the Toronto Financial Post, which opens up with the observation, written by John G. McDonald, "Here's Where United States Aids Rivals in Other Markets."

There being no objection, the articles and editorials were ordered to be printed in the RECORD, as follows:

[From the Washington Post, June 3, 1962]

TAXATION OF FOREIGN INCOME

The legislative debate over the taxation of foreign income points to the conclusion that the benefits that might flow from the legislation proposed by the Treasury would fail to compensate for the damage it might do. The Treasury wants to tax the income of American foreign subsidiaries in industrial countries when it is earned, instead of, as now, when it is received. It also wants to block the use of so-called tax havens abroad. The Treasury argues that the legislation would make the tax law neutral as between domestic and foreign investment, strengthen the

balance of payments, and stimulate investment and employment at home.

The House, in voting on the bill, left the present tax deferral largely in being, but went along on the closing of tax havens. In presenting the project to the Senate Finance Committee, the Treasury stresses its preference for ending the deferral, but seems reconciled to getting only the tax haven provisions.

Continued freedom for foreign investment, except for specific tax haven abuses, seems to be the logical conclusion to be drawn from the debate between the Treasury and the taxpaying corporations. This debate has proceeded at a remarkably high intellectual level, in commendable contrast to much of the discussion over the tax bill. The companies no doubt have tended to overstate their case. But their fundamental points they have made to stick.

It has become clear that the improvement in the balance of payments probably would be smaller than had been supposed and in any case short lived. The reason is that while the outflow of capital might diminish, so would exports in the form of sales to subsidiaries. In the longer run, foreign income forgone would outweigh any gains from reduced capital outflow.

The neutrality of the tax impact between domestic and foreign investment at which the Treasury aims would destroy the competitive equality between American subsidiaries and their foreign rivals. If the latter are taxed less heavily, they will outcompete the American firms. The present law, moreover, does not involve a deliberate subsidization of foreign investment. It is the logical application of the principle which rules for domestic taxes that income is not to be taxed before it is received.

The fear that some jobs and some sales will be lost if American firms supply their foreign markets from abroad instead of by exporting is probably realistic. But to try to protect American industry and labor by means of the tax law would constitute a new form of protectionism that ill accords with the liberal principles embodied in the trade legislation sponsored by the administration. In any case, the effort to protect jobs and sales may prove futile if the products meanwhile have ceased to be competitive.

The outlook for investment in the less developed countries will suffer if investment in the industrial countries is penalized, even though those countries are now exempted from the legislation. The investor can hardly fail to notice the handwriting on the wall telling him that some future turn of the tax screw will probably reach him even there.

The issue then boils down to a simple question. Is the balance-of-payments situation so desperate that in order to get some quick relief the United States must sacrifice the unquestioned benefits of foreign investment? The time may come, if we mishandle our affairs, when we can no longer afford to build up our investment position in some of the world's fastest growing economies. But it does not look as if that time had arrived now.

[From the Cincinnati Enquirer, May 6, 1962]

WHY CUT OUR OWN THROATS?

The old fable about the man who killed the goose that laid the golden eggs should be recalled by Members of the U.S. Senate before they proceed with that part of the administration tax bill that would tax American companies on profits of overseas subsidiaries before they are distributed in the form of dividends.

Foreign trade, the outflow of gold, and related subjects are difficult for the man in the street (sometimes even Wall Street) to comprehend.

But to state the question simply, the fable about the goose that laid the golden eggs is very directly applicable to the proposed change in a long-standing tax rule.

U.S. BUSINESS MUST COMPETE ON AN EQUAL FOOTING

About the only way that American capital can compete in many areas of the world, or stimulate economic growth, is to do business on equal footing with foreign-owned companies beyond our borders. This means getting behind tariff barriers, or enjoying comparable tax status. In fact it is the only way in which the American free enterprise system can venture much-needed development in the so-called high risk areas—the emerging and developing countries.

The foreign aid programs of the United States have achieved wonders in various critical zones—prominent examples being Western and Southern Europe and the Far East after World War II. But there isn't enough money in the U.S. Treasury—presently almost \$300 billion in debt—to “prime the pump” all over the globe, advance civilization generally, and reduce the tensions that may lead to war or bloody revolutions by the attainment of a markedly better standard of living for the free world.

But here we come to a paradox. An administration that pleads for foreign aid, and proposes costly Alliances for Progress as a means of combating communism, now espouses a tax rule that would be ruinous to the development of foreign industrialization by private American investors.

Part of the contradiction—perhaps a very large part—stems from lack of understanding of the way in which our foreign enterprises are set up and work.

And far too many people—in and out of Government—believe things that simply are not so in this complicated field.

The worst of these misconceptions is that American-developed plants overseas are a drain on our gold reserve, or take jobs and business away from our domestic enterprises.

The fact of the matter, as pointed out earlier this year by the U.S. News & World Report, is that the volume of dollars flowing into the United States from the operations of foreign subsidiaries is more than twice as great as the amount flowing out of the United States to foreign subsidiaries.

Why so? Our privately owned businesses abroad provide markets for American machinery, materials, products, royalties, fees, etc., as well as dividends to American investors.

The statistics on this are somewhat startling. In the last 15 years Eastman Kodak sent abroad about \$13 million in foreign investments. Dividends received from their foreign operations have totaled \$101 million—and Eastman Kodak has sold \$532 million in American-made goods to its foreign subsidiaries.

Another good example is the Procter & Gamble Co., which in the last decade sent abroad for investment \$11 million. But this relatively small amount (by Government standards), plus money borrowed and re-invested abroad, set up a market for \$243 million in American raw materials, finished products, and equipment from the United States for use in overseas subsidiaries. In addition, \$47 million was paid in dividends to Procter & Gamble in this country (and upon which, of course, they paid the regular taxes to the U.S. Government).

Neil McElroy, chairman of the board of Procter & Gamble, who has served as Secretary of Defense and knows both sides of the picture, made an excellent presentation of the case for continuing unfettered foreign investment of American capital in an appearance before the House Ways and Means Committee last year. He made these basic points:

Our country's interests are well served by legitimate business activity abroad.

The type of development that Procter & Gamble has been pursuing for 45 years, and much more actively since World War II, is an effective cold war weapon that deserves encouragement, not discouragement. (Most other nations do encourage such commercial development abroad.)

Such foreign subsidiaries improve our balance of payments and provide domestic employment.

Mr. McElroy also made the very telling point that this is about the only way that American free enterprise can penetrate many foreign markets.

That's what we mean about killing the goose that has been laying the golden eggs.

This is how the administration tax proposal would strike at the heart of our commercial and industrial enterprises abroad: The U.S. overseas subsidiary would pay to the country in which it operates the same taxes paid by its competitors in the same country. In addition, it would be required to pay to the U.S. Government any difference between its foreign tax and the U.S. corporation tax of 52 percent on profits. If, for example, the subsidiary paid a 30-percent tax overseas, then it would pay an additional tax of 22 percent to the U.S. Government. For many, it would mean the loss of ability to compete with others doing business in that country. For others, it would mean a crippling of growth.

To conserve American dollar investment, most such subsidiaries begin in a small way, and grow with the expansion of plants and development of markets made possible by the profits they earn. Their growth potential depends wholly upon their retained profits—unless we continually ship money overseas to support this means of getting our share of the world's trade.

THIS COULD BECOME ANOTHER COMMUNIST VICTORY

It cannot be stressed too strongly that the system followed now and in the past has not constituted a “tax loophole,” or made possible a “tax haven” abroad for American business. As dividends accrue to American investors—once profits overseas have built up the business—they are taxable in the United States.

If we scuttle our overseas businesses, by making it impossible for them to grow competitively or venture into the high-risk underdeveloped areas, we will be handing communism a great economic victory—and the American taxpayer a bill he cannot possibly pay.

[From Business Week, May 5, 1962]

TOO CONFUSED FOR WORDS

As any teacher of English composition will tell you, an idea that can't be expressed in clear, precise language is likely to be a poor idea. By this standard, the administration's proposals for taxing the earnings of foreign subsidiaries of U.S. corporations must count as one of the poorest ideas that has come along in some time. The more tax lawyers read the fine print of the bill that has passed the House and is now under consideration by the Senate Finance Committee the more they wonder just what its various clauses do mean.

In fact, the bill is so ambiguous that some businessmen have concluded that bad draftsmanship alone cannot explain the fuzziness of the language. They suspect that the Treasury is deliberately creating obscurities so that it can have a free hand later to interpret the language as it pleases.

Even if the Treasury gets the benefit of the doubt on this point, the fact remains that the bill is full of confusions, complexities, and unresolved questions. One of its clauses apparently would set a boobytrap for U.S. directors of foreign corporations by forcing them to reveal information that foreign law forbids them to disclose. Another might put

a heavy penalty on the liquidation of foreign subsidiaries after the bill has passed.

This sort of vagueness is a tipoff to the fact that neither the Treasury nor the Congress has decided just what the new legislation is supposed to do or how it should do it. As the bill stands, it is neither a measure to raise revenue nor an effective device to limit the flow of U.S. capital abroad. It is an arbitrary change in the rules of the game that would produce endless litigation and perpetual confusion.

For this—if for no other reason—the Senate should reject the proposals out of hand. If the law is to be changed, companies with a vital stake in overseas operations at least are entitled to know what the changes are and what purpose they are supposed to serve.

[From the New York Herald Tribune,
May 18, 1962]

HOBBLING BUSINESS

(By Donald I. Rogers)

Even as Treasury Secretary Douglas Dillon was addressing top-level European bankers in Rome, urging them to restrain the flood of multimillion dollar European bond flotations on Wall Street, the Senate Finance Committee was considering the administration's tax bill which would impose indiscriminate penalties on all American companies that compete for foreign markets through subsidiary operations overseas.

On the surface it appears as though the liberal Kennedy administration is pushing for drastic conservative revisions in American foreign economic policy, revisions that would curtail American expenditures abroad and at the same time discourage American risk capital from helping to finance foreign enterprises.

It is part of an administration maneuver, however, to increase the pressure on Britain to join the European Common Market and simultaneously clear the way for eventual entry into the Common Market by the United States. It is a planned evolution in the international economy to supplant America's gigantic foreign aid program.

While it is possible to understand the motives of the central planners, it is not so easy to fathom what appears to be an absolute disregard for American business during the transitional period.

The tax bill, for instance, which would drastically change the taxing procedures on foreign income of American business, was presumably initiated to curb “tax havens” which some tax experts had estimated cost the United States hundreds of millions of dollars annually. The general impression was that the object of the pursuit was the elusive income of U.S. movie stars.

Unfortunately, this scouting of foreign tax havens is part of a trade program fostered by the administration that businessmen generally hold to be sound.

As the tax bill now stands, however, many business leaders feel it would nullify the broad aims of the generally acceptable Kennedy foreign trade programs. It is also a complete reversal of the policy of previous administrations and Congress itself which encouraged American investments abroad, holding them to be of greater value than unrestrained foreign aid.

The business leaders believe that if the bill becomes law, the effect will be to reduce total employment in the United States, curtail the manufacture of goods in the United States for export abroad, sharply decrease what is presently the largest favorable factor in the U.S. balance of payments, and put American business at a grave disadvantage in competition with the aggressive producers of other countries for world markets.

Heretofore the official American policy has been to encourage direct American investments overseas. The apologetic and sympathetic Washington press corps has tried to

plant the idea that tax provisions had been devised to encourage investment in the rebuilding of Europe after the war and that consequently these provisions are no longer valid or necessary. The truth is the basic provisions involved have been part of the U.S. income tax law since it was enacted in 1913, nor were they changed in substance during the Marshall plan period.

Tough European competitors, of course, like the idea of imposing additional tax handicaps on American business. Mr. Dillon told the House Ways and Means Committee that the finance ministers of the six Common Market countries were "good enough to give us the general tenor of their thinking."

While European competitors heartily approve steps to decrease the effectiveness of American business, it is notable that no similar measures have been proposed by their governments with respect to their own industries. In fact their tax policies have been in the opposite direction—to encourage expansion of their businesses abroad.

It would appear, then, that our American Government is more concerned with the vigor of foreign businesses than of its own businesses. It is also obvious that additional heavy tax burdens on American overseas business would greatly abet the increasing economic competition of the Communists.

Congress is being asked to approve a policy which is: (1) Detrimental to American business; (2) beneficial to foreign businesses in competition with American business; and (3) greatly beneficial to the state-owned Communist industries which seek to "bury us."

This may be liberal, but it is hardly constructive.

The loss or curtailment of foreign markets inevitably would mean a decline in U.S. exports with loss of production jobs and a rise in unemployment in this country. A schoolchild should know that the way to provide more jobs in American factories is not to pull out of the great world marketplace but to compete more successfully in it.

Can either President Kennedy or Dr. Dillon honestly believe that a cutback in American exports will improve the aggravating gold problem?

[From the Wall Street Journal, Apr. 27, 1962]

HOW NOT TO SUCCEED IN THE WORLD

The administration's foreign tax proposals, according to Treasury Secretary Dillon, "are not directed against foreign investment as such." They are only intended to stop perhaps 10 percent of it—that portion of the capital outflow which "is induced by tax reasons."

One part of the Treasury's concern here seems to be the possibility of actual tax avoidance on income earned abroad. But that is a minor problem which requires no new legislation.

More importantly, the administration is apparently under the impression that present law is "inequitable" because it permits some kind of "privilege" or "preference" for the stockholders of U.S. firms operating abroad. As it is now, for example, the earnings of American-owned foreign corporations are not taxed until they are returned to this country as dividends. In Mr. Dillon's view, this "deferral privilege" is what "induces" excessive direct investment abroad.

Yet this provision was not put into the law to let people duck any taxes or get away with anything else. It was written long ago with the idea in mind that it might foster, without revenue loss, American business activity abroad.

That is exactly why businessmen are disturbed about the effects of terminating this "privilege," as the Treasury is trying to get Congress to do with regard to industrialized nations like those in Western Europe. Here is what Ellsworth C. Alvord, chairman of the

Taxation Committee of the U.S. Council of the International Chamber of Commerce, told the Senate Finance Committee just a couple of days ago:

"What * * * deferral has done is to permit U.S. subsidiaries to operate under conditions more nearly equal to their rivals in the West European countries by permitting them to finance a larger part of their investments out of retained earnings."

"If the administration proposals become law," he went on, "the American businessman will find his foreign subsidiary struggling to compete with businessmen from countries which levy no tax at all on foreign income, or grant preferential rate differentials to foreign income * * *. [Those countries] want their businessmen to succeed in the competitive struggle for world markets."

So whatever the administration may argue, the Treasury's foreign tax proposals inevitably constitute an attack on American private foreign investment. And herein lies an even deeper confusion of approach.

The administration is unhappy about this outflow because it thinks it increases our serious international payments deficit; boosting exports, on the hand, improves our payments position. Yet, over the years, the net return on foreign investment exceeds outflow. So the Treasury is taking at best a shortsighted view.

Moreover, it is by no means necessarily a case of either investments or exports. In many ways, the two go together. A foreign investment often increases the demand for exports from this country. The investment may necessitate parts or equipment from the United States. More broadly, investment stimulates economic activity and hence demand for all kinds of American goods. Certainly both investments and exports are needed in that competitive struggle which is so rapidly intensifying in the world.

The payments deficit and resultant gold flow is a real and urgent problem, but the heart of it is the Government's own prodigious foreign spending. Instead of making any serious effort to curb that spending, the administration prefers to attack the gnat of tax "inducements" and in the process swat everybody who is trying to do business abroad.

This confused and contradictory course is a curious way to preserve the Nation's economic position in the world, let alone improve it.

[From the Journal of Commerce, May 16, 1962]

TAXING FOREIGN EARNINGS

The more we think about the administration's push to tax undistributed earnings of foreign affiliates the less sense we can see in it. We don't believe that even if the tax is enacted it will cause much difference in American corporation policy respecting foreign investment—which certainly has not been heavily influenced by the ability to defer taxes on earnings on such outlays until they are brought home. But the proposed tax will be some kind of a hindrance for American foreign investment.

The projected tax upon foreign earnings is officially justified on several grounds. It will produce more tax income. Even the Treasury puts this prospective income gain at only \$145 million; others have said that it will be only \$80 million a year.

It will aid the U.S. balance-of-payments deficit. This assertion is questionable; if policy of corporations is not likely to be changed, the only gain would be the \$145 million or \$80 million, which is peanuts when the deficit runs into billions.

The other argument is that by removing the tax incentive, such as it is, on corporate subsidiaries in developed countries and leaving it on in underdeveloped nations, more private capital will be channeled to the un-

derdeveloped. This seems to presuppose that by a minor wiggle of the tax finger, investments in Britain or France will automatically shift to Ghana or Guinea. That's nonsense.

A still further and minor argument is that tax havens abroad are meretricious and should be ended.

If they are meretricious, why continue them as respects underdeveloped nations? Sin is supposed to be bad per se, not according to where you do it. Furthermore, there is some distortion of truth in labeling places where you invest as tax havens when in reality you are merely deferring, not avoiding the taxes.

We think the administration has been again inept in really presenting a good case for the tax on foreign earnings. It should have tied in the proposal to a larger picture much more expertly and sensibly than it did.

It might have said, for example, that under his foreign trade program, President Kennedy is going to seek reciprocal tariff concessions, to the end that American exports will enter Europe's common markets on more favorable terms than they do now.

Negotiation of tariff concessions is of course inconsistent with the idea that the U.S. Government will subsidize by tax concessions the establishment of foreign plants which in effect will avoid the foreign tariff levies. When you have a plant in the Common Market producing your goods within their tariff walls you naturally escape payment of import duties.

The only substantial relationship of this foreign overseas direct investment to the balance of payments is that it is one factor influencing a capital outflow, which won't be reversed even if the alleged tax advantage is given up.

We suspect that for reasons of logic the administration will have to stand pat but that it won't in the end consider this tax on foreign earnings something crucial, which it certainly isn't. We do think it could have made a better case for the idea without throwing around so many red herrings.

[From the Baltimore Sun, May 7, 1962]

OVERSEA INVESTMENT

One of the most controversial features of the administration's tax bill is the proposed change in treatment of overseas subsidiaries of American corporations. The provisions may not seem as comprehensible or of as much moment as the restrictions on expense accounts or withholding of taxes on dividends and interest. But the tremendous expansion of business into foreign countries and the proposed revision of the foreign trade program make the question increasingly important.

The administration bill has three main purposes. It would tighten controls on transactions between parent companies and subsidiaries designed primarily to evade taxes in this country—as, for example, where the parent company "exports" potential profit by charging subsidiaries less than reasonable prices. It would tax income earned by foreign subsidiaries not returned to this country and not immediately reinvested in the overseas business. This is the heart of the revision for, under present law, the income is not taxable until it is returned to the parent company in this country. And by curbing these and other artificial incentives to setting up overseas corporations the bill is designed to encourage more direct exports from the United States.

In broad outline and to a degree difficult to define, these are laudable objectives. Most responsible businessmen who have testified on the bill strongly support restrictive measures against the operation of paper overseas subsidiaries whose only real purpose is to evade taxes. But they worry about the bill as written. They are afraid that the effect of it will be substantially to inhibit

the establishment and operation of legitimate overseas subsidiaries.

As they point out, these American owned foreign corporations buy rather heavily from the United States and so increase exports and contribute to a favorable balance of payments. They return well over \$2 billion a year in dividends and interest to this country, an additional factor in strengthening the balance-of-payments position. Finally, a good many foreign markets for particular goods are difficult to penetrate with expensive American exports, produced at higher cost to which shipping charges and tariffs are added. If American firms are to capture their share of foreign business, they will have to do it both by exports and, in some cases, by putting overseas production plants right in the market concerned.

The administration and business would undoubtedly agree on these broad objectives—the elimination of real abuses and the maintenance of healthy overseas subsidiaries of American corporations. The argument comes on detail. The House Ways and Means Committee made some changes in the original administration draft but the bill was whipped through the House under strong political pressure. Now, in the Senate, committee experts have a last chance to sort out many of the complexities before the measure becomes law.

[From the Vineland (N.J.) Times Journal, May 8, 1962]

BETTER THAN CHARITY

If the foreign tax provisions of House bill 10650 would result in less American investment in industrial growth of the so-called underdeveloped nations, as the Owens-Illinois Glass Co. claims, these provisions ought to be changed.

Owens-Illinois's president Ray Mulford told the Senate Finance Committee chairman by Senator HARRY F. BYRD that the provisions "will place American corporations doing business overseas through foreign subsidiaries at a competitive disadvantage with foreign-owned corporations operating in the same markets."

Mulford said that his company agreed on the need to end "tax havens" overseas—investments used by some Americans only as a means of dodging U.S. taxes. But the double-tax provisions of the proposed legislation—passed by the House of Representatives on March 29—could dry up the supply of U.S. risk capital abroad.

One of the provisions would require that an American corporation report to the U.S. Treasury Department on the basis of pre-tax earnings of a foreign subsidiary, whereas "only that portion of the after-tax earnings paid in dividends is available to the American company." In other words, the corporation first would have to pay taxes on its earnings to the country in which the subsidiary business is located. Then it would have to pay to Uncle Sam taxes on the same gross earnings, instead of on the net earnings after the foreign taxes had been paid.

There are a number of other provisions which are highly complicated. What's important about them is that they ought not discourage U.S. investment abroad. For in the long run of history it's a lot better to invest in another nation and help it to help itself than to pour charity through its lips. A mendicant often feels no love for his benefactor; a real business partnership is a better basis for lasting friendship on the international level.

[From the Daily Commercial News, San Francisco, Calif., May 7, 1962]

WE NEED A SPUR—NOT A BRAKE

To keep its own economic health, the United States must face up to the realities of worldwide competition.

That is the view of the head of an American oil company (Standard Oil Co., New Jersey) which operates on an international scale. To quote him directly, "We must regard economic competition from our friends and allies in the free world with the same viewpoint which we apply to competition amongst ourselves—as a spur, an incentive, a stimulant, leading us to innovation, research, cost reduction, improvement of efficiency in every direction."

Government policy, to say the obvious, will have a great deal to do with the ability of American industry to achieve such objectives and to compete in the world markets. This spokesman is much concerned, and with every reason, over current proposals for changing the method of taxing income from foreign operations. Shareholders of American corporations pay individual income taxes only on dividends received—that is, money in hand. They don't pay income taxes under these proposals on earnings which are plowed back into the expansion of U.S. plant facilities. But U.S. shareholders in foreign operations, with respect to certain types of foreign business earnings, would be required to do just that.

The inevitable result would be discouragement to foreign investment—and a serious handicap to American companies which are trying to compete in the markets of the world. Why the checkrein on U.S. investments abroad?

[From the Camden Chronicle, Camden, S.C., Apr. 30, 1962]

COULD COST JOBS

American business, large and small, is solidly behind the objectives which the administration says will be achieved by its foreign trade policy. But these very objectives are imperiled by the radical changes demanded in the taxation of overseas subsidiaries of American companies.

Those American businessmen who are best informed on such operations, see only disaster ahead—both at home and abroad—in the proposed reversal of tax law that has served the Nation well for 40 years. And they have been flocking to Washington to offer their testimony to the Senate Finance Committee against provisions of House bill 10650 that would tax the income of such companies as earned at the source, and not as heretofore, when such income was remitted to the United States. Furthermore, the proposed rules impose double taxation by considering the foreign tax paid on such income as if it were cash received in the United States.

Administration spokesmen solemnly declare that this legislation will reduce unemployment, promote exports, check the outflow of gold, correct tax abuses—and out of the other side of their mouths calmly admit this new tax burden is designed to discourage U.S. business from investing abroad. Which it certainly will.

Actually, American overseas operations increase jobs at home, and the greater their success, the greater their demand for machinery, components and finished products made in the United States. And since American business goes abroad to compete with foreign firms in their own markets, not to make goods that can be profitably exported from here, the jobs it creates abroad would not otherwise exist in the United States. Thus the charge of "exporting American jobs" is fallacious.

During 1960, foreign subsidiaries of U.S. firms sold \$2.7 billion of American-made products abroad and sent goods to the United States that amounted to only one-sixth of that volume. From 1950 through 1960 direct U.S. foreign investment totaled \$12 billion—and generated a return of \$20.5 billion in earnings to the United States.

In view of the growing competitive struggle of the North Atlantic trading community for the markets of the Western World, a worse time could hardly be chosen for throwing a roadblock in front of the American team—even though, as the Secretary of the Treasury has naively reported, the finance ministers of six Common Market countries are in favor of it.

What more do the Senators need to know?

[From the Christian Science Monitor, May 21, 1962]

TAX POLICY IN PERSPECTIVE

(By George H. Favre)

BOSTON.—From a long-term point of view, justification for the Treasury's bid to tax undistributed earnings of American corporations' overseas subsidiaries has never been easy to find.

Even accepting at face value the argument of Secretary of the Treasury C. Douglas Dillon that overseas investments do not begin to act favorably in the Nation's balance of payments for 14 or 15 years, the move is open to attack as being shortsighted.

Returns from investments made 14 or 15 years ago and now beginning to flower (according to Mr. Dillon's own estimates) could be expected at least to cancel the outflow of future investments.

FIGURES CHALLENGED

But now Mr. Dillon's figures have been challenged by some practical economists with firsthand knowledge of international financing. The challenge will give congressional opponents of the Treasury proposal some factual ammunition in their fight against allowing the provision to be passed as part of the administration tax-reform bill.

A closely reasoned report on the subject, made independently and submitted to Congress by the Standard Oil Co., of New Jersey, has challenged the whole basis of Mr. Dillon's figuring on impact of overseas investments on the U.S. balance of payments.

The oil company's economists, specialists in international finance, dispute Mr. Dillon's use of official figures in describing flow of funds for investment purposes in and out of the United States, Europe, and Canada.

SUBSTITUTION ASSERTED

The economists have no quarrel with Mr. Dillon's figures for investment outflow but assert that he "substituted calculated figures of his own for the inflows." Briefly, Standard Oil people argue that Secretary Dillon permitted true inflow figures from investments made in any single year to be canceled but outflows initiated in later years for unrelated projects.

The effect, says Standard Oil, is to draw an unwarranted and pessimistic picture of the impact of such investment on the country's balance-of-payment account.

The company economists would, instead, add together annual earnings and related exports (goods and services) generated by average investment—which Mr. Dillon figures at 14.7 percent and 10.3 percent, respectively. The 25-percent return that these two figures total, after the year of first investment, should thus offset the initial outflow in the balance-of-payment accounts within a 4- or 5-year period.

After that, the investment would represent a net inflow in the balance-of-payment account, says Standard Oil, which considers its way the "normal method" of evaluating investments.

The Standard Oil findings tend to corroborate case-history testimony compiled by 19 major U.S. corporations, which submitted their export-import figures for a study to show actual impact of their overseas operations. The study, conducted by Prof. Emile Benoit of Columbia University's Graduate School of Business, showed that their opera-

tions abroad actually had resulted in a positive inflow in the country's balance-of-payment account.

Opponents also argue that the Treasury's position is inconsistent with past practice, in which the Federal Government actively encouraged businesses to set up shop overseas by not taxing profits earned abroad until they were brought back to this country. The earlier Government position was taken in order to spur the economic development of Europe after the war.

COMPANIES WARY

Now, say these firms, they would be unfairly penalized for having cooperated earlier. Meanwhile the Treasury still proposes to permit unrepatriated earnings from firms investing in economically underdeveloped areas to go untaxed. But with the about-face on tax benefits for firms which invested in Europe and Canada, companies now may be wary of how long the remaining inducement might remain in the tax laws.

Strong as the immediate economic arguments are against the Treasury position, the one least defensible in documented figures may yet be strongest in force of logic. That is the proposition that any effort that would discourage expansion overseas by private investment must in the long run tend to contradict the administration's thesis for its No. 1 legislative fight, the President trade bill.

For President Kennedy's trade program is based on the assumption that the cold war is a long-term struggle, that it will ultimately be fought on the economic front, and that the major card in the West's favor is to develop the strongest possible economic bonds between the Atlantic community nations.

It can be cogently argued that any measures that would restrict freedom of international movement by private industry are basically nationalist in tendency and veer away from the long-term goal of a wider and economically more closely integrated West.

[From U.S. News & World Report, Jan. 15, 1962]

OTHER SIDE OF OVERSEA DOLLARS

New facts are coming to light on how this country is affected by the big and growing operations of U.S. companies abroad.

President Kennedy had been told that firms moving to industrial countries were exporting both capital and jobs, taking out of the country far more dollars than they returned to the United States.

The President proposed that tax laws be changed to discourage American companies from expanding operations in developed nations overseas.

A study by the Government itself, however, plus studies by individual companies, now is putting an entirely new light on that picture.

Facts available to the President told only part of the story. They related solely to dollars of capital invested abroad by American companies and dividends returned by these companies. They took no account of materials and machinery purchased in the United States by these American companies. They also gave no weight to payments of royalties and other fees by U.S. companies abroad.

A special survey by the U.S. Commerce Department permits a more complete story to be told. This study covered operations of 155 U.S. manufacturing companies, located mainly in developed countries. The study, in turn, is backed by examples of actual experience of individual American companies.

The accompanying chart gives you at a glance the main points turned up in the survey.

Note that these 155 companies, on an overall basis, returned to the United States from

their manufacturing subsidiaries \$1.3 billion more than they withdrew from the United States in 1960.

The operations of these companies thus are shown to have added to the financial strength of the United States. Supplies of dollars in this country were built up, not drained away.

The Commerce Department survey covered a large sample of manufacturing companies. If all American companies abroad were counted—from trading subsidiaries to oil drilling—the favorable effect on the United States shown by the Commerce survey, industry officials say, would be much larger.

For example, these officials estimate that all U.S. companies overseas buy a total of \$5 billion worth of American goods each year—as against only \$1.8 billion worth shown in the sample survey.

Similarly, total payments to the United States from foreign-earned royalties, license payments, management fees and the like are estimated to be running at the rate of \$400 million annually—as against only \$148 million shown in the manufacturing survey.

EXPORTS THAT AREN'T

Not all of the sales of American goods to U.S. companies abroad are a net addition to U.S. exports. Without U.S. firms overseas, for example, foreign producers would be doing more business—and, presumably, importing more from other countries, including the United States. Likewise, companies in the United States could earn some income from foreign royalties and license fees without actually having subsidiaries abroad.

By being on the scene overseas, however, U.S. companies are pictured as building up sales that directly boost U.S. exports. Many of these sales, industry surveys show, would not be made if American firms were not able to battle foreign firms on the scene.

The stimulation to U.S. exports attributed to American companies overseas is only part of the story.

These overseas subsidiaries also send back to the country a large chunk of the profits earned abroad, plowing the rest back to build up the business—and the base from which to make even bigger profits in the years ahead. In addition, these subsidiaries send back earnings from royalties, license and management fees, and the like.

Add these all together, and the total inflow of dollars to the United States from foreign operations far exceeds the amount of dollars sent out by these companies to build up foreign facilities and to buy goods made abroad by their subsidiaries.

A LOOK AT THE RECORDS

To show you the big U.S. gain, net, from foreign operations, consider these examples from special studies by individual firms.

In the last 15 years, Eastman Kodak has sent about \$13 million out of the United States as foreign investment. However, dividends received from foreign operations have totaled \$101 million. Moreover, Eastman Kodak sold U.S.-made goods worth \$532 million to its overseas companies. Purchases from its foreign subsidiaries in the same period came to only \$29 million.

Or consider International Telephone & Telegraph. In 10 years, I.T. & T. has remitted to the United States, net \$215 million. That's the amount of dividends and other receipts after deducting the outflow of capital for new investment. On top of that, I.T. & T. showed net exports to subsidiaries of \$175 million. Total gain for the U.S. balance of payments, company officials say, was close to \$400 million.

Take the case of Joy Manufacturing Co. In the 10½ years ended last March, Joy has invested \$17.7 million abroad. Return flow—from exports to subsidiaries, royalties,

engineering fees, interest and dividends—was \$168 million.

Against a total outflow of \$15 million for foreign investment, American Machine & Foundry has generated an inflow since 1956 of more than \$42 million. This includes purchases of materials from the United States, royalties, management fees and dividends.

Proctor & Gamble in the 10 years ended in 1960, sent abroad for investment \$11 million. In that period the company borrowed abroad and reinvested abroad \$67 million. But note this: Proctor & Gamble returned to the United States, in those years, \$47 million in dividends, and purchased \$243 million worth of raw materials and equipment from the United States for use in overseas plants.

Minnesota Mining & Manufacturing, between 1951 and 1960, made an investment of \$12 million in foreign operations. However, in that 10-year period, the company brought into the United States—through exports to subsidiaries, royalties, technical fees, dividends—about \$62 million. The company says that its operations have thus made a favorable contribution to the U.S. balance of payments by a ratio of 5 to 1.

Or take the example of Abbott Laboratories. In 5 years, 1956–60, Abbott's exports from the United States exceeded its imports by \$50 million. Abbott also received from abroad loan repayments dividends, and miscellaneous income of \$9.3 million—making a total inflow into the United States of \$59.3 million. The total outflow of dollars from the United States in this period—in foreign investments and loans—was only \$2.2 million. Result: A net favorable balance for the United States of more than \$57 million.

IF THE UNITED STATES CLAMPS DOWN

Says one business executive: "The Kennedy administration's moves to clamp down on foreign investment will hurt, not help, the balance of payments."

Despite the gains from the operations of U.S. companies overseas, this question is being asked: Why don't U.S. firms stay in this country and simply export goods abroad?

The answer given by industry officials: U.S. firms cannot compete with foreign companies unless they get inside tariff walls and meet local competition.

WHERE SALES WERE GAINED

Here are some examples of companies that have gotten sales through foreign subsidiaries that they otherwise would have lost. The result was to stimulate exports from the United States to those subsidiaries abroad.

American Machine & Foundry's subsidiary in Italy recently was awarded a \$9 million contract to build and equip a tobacco-processing plant there. About \$5 million was paid to the U.S. parent company for engineering services and equipment; the rest went to the Italian subsidiary for locally supplied items. The company says it would not have gotten the contract, in the face of foreign competition, without its subsidiary in Italy.

Texas Instruments estimates that it would export less than 10 percent of what it now sells abroad if it were not manufacturing abroad.

General Electric's foreign subsidiaries are usually equipped with American machinery. Local managers must provide acceptable excuses for the use of foreign machinery or even of foreign-made components in finished products.

Hewlett-Packard, west coast electronics firm, reports that its foreign sales are double what they would have been if the company had not decided to operate abroad. Every 2 weeks Hewlett-Packard exports a cargo

plane load of high-value parts to its European plants.

JOBS IN DANGER?

Businessmen claim that the administration's tax proposals will add to this country's unemployment problems.

The reason given: Tougher tax treatment on the earnings of foreign subsidiaries of U.S. firms will slow down expansion of companies abroad. As a result, there will be reduced exports of raw materials and equipment to overseas plants, hurting export industries.

Company officials also warn that the administration's proposed tax-haven legislation will result in a smaller flow of capital to the underdeveloped areas. This would be the reverse of the administration's aim to get more capital into such areas.

Reason cited by company officials: Capital investment in high-risk areas, such as Asia, Africa, and Latin America, comes, in large part, from earnings of U.S. firms in tax-haven countries, where taxes are relatively low. If you tax earnings in Europe more stiffly, businessmen say, less capital will be available to flow to underdeveloped areas.

All these arguments—backed by additional facts now coming to light—are presenting a new picture of the impact on the U.S. companies operating abroad.

[From Time magazine, May 25, 1962]

THOSE FOREIGN PROFITS

In Washington this week the Senate Finance Committee will begin debating a New Frontier tax proposal with far-reaching consequences in foreign trade. The argument swirls around the manner in which U.S. firms should be taxed on their overseas profits. Of all the Kennedy administration's economic measures, none has evoked such vehement and unanimous opposition from U.S. business.

PAYMENT IN FULL

Already passed by the House, the administration's proposal would radically change the rules under which U.S. business operates abroad. At present, a firm pays U.S. corporate income tax only on whatever part of its foreign earnings it "repatriates" to the United States as dividends. Earnings kept abroad are free of U.S. tax—which encourages U.S. corporations to use a substantial part of their foreign profits to expand their overseas operations.

The administration wants to make most foreign profits taxable when earned, rather than when repatriated. U.S. subsidiaries operating in such economically advanced foreign nations as Britain and the Common Market countries would pay the full 52-percent U.S. corporate tax on all earnings—less whatever they paid in local income tax. Payment of U.S. taxes could still be deferred in underdeveloped nations, where the administration wants to encourage U.S. private investment. The administration bill has three professed purposes: to clamp down on U.S. firms that channel their overseas earnings into foreign tax havens, to slow the alleged "export of jobs" created by U.S. investment abroad, and to narrow the gap in the Nation's balance of payments by restricting the outflow of U.S. investment capital.

SACRIFICING THE MARKET

Few businessmen are prepared to defend publicly the increasingly popular U.S. corporate practice of funneling foreign earnings into semfictional subsidiaries in such low-tax areas as Switzerland, Liberia, Panama, Bermuda, or the Bahamas. In the single year of 1960, the undistributed earnings of U.S. subsidiaries in such tax havens increased by 100 percent to \$122 million. But businessmen argue that passing the new tax bill to get at the tax havens would amount to rolling out a cannon to kill a mouse. The Government would gain perhaps \$85 million a year in tax revenues, but in doing so, say

the businessmen, it would discourage U.S. firms from plowing most of their overseas earnings back into expansion.

Opponents of the administration bill contend that the vast majority of foreign subsidiaries are set up not to dodge taxes but to develop new markets that cannot be served from U.S. plants because of tariffs, transport costs, higher U.S. production costs—or the simple difficulty of selling at long range. With stiffer tax rules, U.S. businessmen would be faced with a hard choice: either they would have to concede many of these markets to hustling and lower-taxed competitors from Europe and Japan, or they would have to export even more dollars than they now do to keep their foreign plants competitive.

MATCHING THE NEWLY MIGHTY

Even the Government recognizes that investment abroad has helped rather than hurt the U.S. balance of payments. Since 1951 U.S. businessmen have sent \$13 billion overseas in capital investment and have brought back \$20.2 billion in earnings. Investment abroad also stimulates U.S. exports of raw materials, machines, and spare parts to feed the foreign branches. In 1960, the latest recorded year, the United States imported \$475 million worth of products from U.S.-owned foreign companies, while exporting \$2.7 billion worth of U.S. products to them. These figures weaken U.S. labor's thesis that investment abroad generates unemployment at home.

Criticism of the administration bill has already produced one significant modification of it in the House Ways and Means Committee: the bill now provides that foreign profits of U.S. companies would not be taxed so long as they are reinvested in the same line of business, either in the country where they were earned or in a less developed country. But the critics are still not appeased. The language of the House provision, they contend, is dangerously vague; it does not make clear, for example, whether a drug company could reinvest in a related chemical operation.

Above all, however, businessmen argue that the legislation runs contrary to the administration's expressed ambition to bind the U.S. and European economies closer together. With new markets and newly mighty competitors rising within the Common Market, many businessmen are convinced that the United States must rapidly expand its capital base abroad or face an economic decline similar to Britain's after she was forced to sell off most of her foreign investments in World War II. "The President's tax bill," says International Milling Co. President Atherton Bean, "is nothing other than a new and sophisticated economic isolationism."

[From the Los Angeles (Calif.) Times, May 17, 1962]

WHAT MAKES THE TAX BILL BAD

While the U.S. Senators study the omnibus tax bill with confusion and misgiving, the report goes around in Washington that the administration already is preparing a bill for a sizable income tax cut across the board. This would be a bill for next year, introduced this summer, possibly for its effect on the November election.

Such a tax cut has much to recommend it, but we shall discuss its possible salutary effects on the economy at another time. Meanwhile, the rumor that such a proposal is being prepared permits the inference that the administration is having second thoughts about the bill now being considered, even fearing that the Senate will cut it to pieces.

The Senate ought to perform some amputations, for there are things in the bill which are pernicious and there is really no public enthusiasm over any of its prescriptions.

The most objectionable features of the bill are these:

1. A provision to require the withholding of 20 percent of all dividend and interest payments to cover the income tax which may be due on these payments.

2. A provision to require American shareholders in foreign corporations to pay a tax figured on their proportionate shares of the undistributed profits of the foreign corporations.

The first of these provisions would work a hardship and even bring a loss to many small stockholders who in their old age depend, often to a large degree, on their dividend payments. There are about 18 million shareholders in the United States, more than there are members of all the labor unions.

If the 20 percent withholding tax is too much, the taxpayer can claim a refund, just as he does when he is overtaxed through the regular withholding of part of his wages or salary. But the bookkeeping is complex and puts an additional burden on old persons who would otherwise be exempt from income tax. Among persons in this category are many whose minimum comforts can be sustained only if they regularly receive the full amount of their dividend and interest payments. The year-long deferral of payment of 20 percent is a clear and present threat of hardship from a Government which is everlastingly protesting its concern over their welfare. Moreover, if the shareholders are in the class whose interest payments are compounded several times a year, they will never have the full advantage of the withheld 20 percent, for the compounded interest cannot be figured on the part that is kept back at the Government's pleasure.

The argument for this obnoxious provision is that the rightful tax on dividends often is lost to the Government because people do not report it. It's a lame argument. It implies that a large body of Americans are dishonest, deliberately ignoring the instructions of their income tax returns.

The requirement that American shareholders in foreign corporations pay taxes on earnings in which they do not share was contrived by the administration (as Treasury Secretary Dillon confessed to the Senate Finance Committee), to discourage foreign investment. This must seem astonishing to the uninitiated, who have been told ever since the war that American private investment abroad is the ideal device for fostering a strong, free international economy.

The administration argues that this is a necessary measure for curbing the flight of gold. It also has a disingenuous argument, aimed at laymen, that the measure is intended to catch tax dodgers.

Mr. Dillon let a cat out of the bag when he testified before the House Ways and Means Committee that the Common Market countries advised the U.S. Government to resort to this kind of taxation to discourage American investment among them. They apparently were the first ones to say that this was the way to restore the balance of payments (arrest the flight of gold) that is, by keeping American private money at home.

They could, of course, have helped to prevent the flight of gold from America by paying a little toward the support of the American military establishments in NATO, by sharing foreign aid costs, even by lowering their tariffs to let more American goods in and thus let more money come back to the United States. But the proposal to drive out American investors comes easiest to them. They don't need American investment any more, they like the idea of a balance of payments favoring Europe, and they do not think they will have it so long as dividends go home to American investors—as they will eventually, despite the pretensions of the U.S. tax collectors that if they don't get their money now the investors will discover ways to cheat them.

So when the seventh veil is removed this provision of the tax bill seems to stand as another concession to foreign friends at the expense of Americans. In international affairs our Government often treats us as the world's second-class citizens.

[From the Toronto Financial Post, Mar. 10, 1962]

HERE'S WHERE UNITED STATES AIDS RIVALS IN OTHER MARKETS

(By John G. McDonald)

The way things are shaping up, it is clear that 1962 will be an active year for tax legislators.

The British Chancellor of the Exchequer has already given notice that he will introduce a new tax on short-term capital gains derived from dealings in securities and real estate.

In the United States the House Ways and Means Committee issued another announcement last week concerning "tax haven" legislation that will be included in the House bill (not yet released). General approach will be to tax U.S. shareholders currently on their "share" of the earnings of foreign subsidiaries, if at least 20 percent of the income of the subsidiaries is made up of interest, dividends, rents, royalties, income from patents and copyrights, and "export income."

"Export income" is defined as income from the sale of goods by a controlled foreign corporation outside of the country in which it is incorporated, where the goods are not manufactured by the corporation and where more than 20 percent of such corporation's income (other than "passive" income) consists of such "export income."

Needless to say, the Republican members of the committee oppose the bill. Congressman J. W. BYRNES issued a statement saying:

"The bill seeks to build a 'Berlin wall' in the tax laws to keep the American businessman at home. The bill would deny to American business the right enjoyed by its foreign competitors to go into any area of the free world where there might be a market, a source of raw materials, or the workers needed to make the business a success.

"The policy of the bill is a policy of * * * isolationism as to American-owned business. [It] adopts the outrageous proposition that American business should surrender to foreign competition in the world market."

It is certainly clear, in the field of foreign trade, that a foreign corporation controlled by Canadians—or an overseas trade corporation in Britain—will have a decided advantage over its U.S.-owned competitors after the New Frontier people in Washington achieve their ends.

The new law will also serve to trim American sails in Europe, increase the downward pressure on the U.S. dollar, and indirectly assist Britain's entry in the Common Market.

The point is, of course, that businessmen regard taxes as costs, and try to keep them down. Government taxmen, on the other hand, are indignant over foreign investment of "our" money by the businessmen who went out and earned it in the first place.

Let's hope that Ottawa encourages Canadian business to take full advantage of the mistakes south of the border.

Mr. McCARTHY. Mr. President, I wish to read for the RECORD certain portions from the editorial published by the Toronto Financial Post, written by John G. McDonald.

Mr. McDonald says:

The way things are shaping up, it is clear that 1962 will be an active year for tax legislators.

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derived from dealings in securities and real estate.

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Mr. McDonald also says:

"The bill seeks to build a Berlin Wall in the tax laws to keep the American businessman at home. The bill would deny to American business the right enjoyed by its foreign competitors to go into any area of the free world where there might be a market, a source of raw materials, or the workers needed to make the business a success.

"The policy of the bill is a policy of * * * isolationism as to American-owned business. [It] adopts the outrageous proposition that American business should surrender to foreign competition in the world market."

It is certainly clear, in the field of foreign trade, that a foreign corporation controlled by Canadians—or an overseas trade corporation in Britain—will have a decided advantage over its U.S.-owned competitors after the New Frontier people—

Of course, this includes us—

in Washington achieve their ends.

The new law will also serve to trim American sails in Europe, increase the downward pressure on the U.S. dollar and indirectly assist Britain's entry in the Common Market.

The point is, of course, that businessmen regard taxes as costs, and try to keep them down. Government taxmen, on the other hand, are indignant over foreign investment of "our" money by the businessmen who went out and earned it in the first place.

I note that the "our" is in quotes.

The concluding remark by Mr. John G. McDonald, who reports on the taxes in the Toronto Financial Post, is:

Let's hope that Ottawa encourages Canadian business to take full advantage of the mistakes south of the border.

This I assume to be an objective view. At least, it is a view which could not be considered as prejudiced in favor of the United States. The recommendation is that the Government of Canada takes special note of what the United States is doing to encourage Canadian businessmen to take full advantage of the mistake which, in his judgment at least—a judgment which I share to some extent—we seem to be prepared to make at this time.

Mr. President, between April 24 and about May 11 of this year approximately 75 witnesses testified before the Senate Finance Committee on the foreign income provisions of the Internal Revenue Act for 1962. Of that number more than 70 testified in opposition to the provisions of the bill with regard to the taxation of the foreign income of American corporations. I do not mean to argue that because 70 to 75 witnesses were op-

posed to the provisions and only 2 or 3 witnesses were in favor of them, that in itself is an argument in opposition to the provisions of the bill as reported by the Senate Finance Committee and as those provisions were originally recommended by the Treasury Department itself. However, I believe that most of the witnesses were reliable and responsible people. Most of them are from the American business community. Some of them are economists and business specialists and specialists in international trade.

It is true that there are some corporations, some American businesses, which have used and are continuing to use oversea organizations of various kinds as a device for evading taxes, or at least for the postponement of the payment of taxes. I believe that the provisions in my amendment would come close to collecting the taxes from corporations which are truly tax-haven corporations. Few would continue to evade and escape. I believe that the judgment on this question must be made in the light of the overall effects of the proposals that are here being made, rather than on the basis of whether or not one or two dishonest people or dishonest firms that are seeking to avoid the payment of American taxes are to be caught.

Mr. JAVITS. Mr. President, will the Senator yield?

Mr. McCARTHY. I am glad to yield.

Mr. JAVITS. I should like, first, to express my satisfaction with the Senator's typical courtesy in joining me as a sponsor of his amendment. I have a similar amendment which was proposed to the committee, of which the Senator is a distinguished member. I shall speak in due course in support of the amendment.

I wished to interrupt the Senator at this point because what the Senator is saying is very pertinent. He speaks about the effort which one or two or three firms are making to avoid taxes, and the effort that is made to eliminate such avoidance. We can never completely cure that situation, because there will always be some lawyers, some accountants, and some firms figuring out how to defraud the Government, and we must avoid the effort that is being employed in this manner to throttle the whole American effort overseas.

When it comes my turn to speak, I shall try to demonstrate how unfairly this provision would work for the people in whom the Senator and I are interested; namely, the new firms, the young firms, the adventurous firms that are going into the foreign market.

This also has its effect upon the program of expansion of trade on the part of the United States. It would be most harmful, it seems to me, and we would be cutting off our nose to spite our face in dealing with the company which is trying to use this tax haven, and we would materially thwart the national purpose. It is a very significant point, and I am glad the Senator is making it.

Mr. McCARTHY. I agree with the Senator. It is very much like saying

that we ought somehow to outlaw or hamper the operations of all savings and loan associations because we have found that 1 or 2 percent of them have acted illegally or imprudently and have abused the trust which was placed in them. I am sure none of us would go to the point of saying that because of this situation, the whole industry should be destroyed or hampered or hindered.

Mr. JAVITS. Mr. President, will the Senator yield further?

Mr. McCARTHY. I yield.

Mr. JAVITS. It is said—and I believe it to be very important to have this recorded—that no country, neither the United States nor any other country, has tried, except in the case of a foreign personal holding company, to establish this kind of tax consequences, because one happens to own stock in a company operating overseas.

Mr. McCARTHY. The Senator is correct. The Treasury seems to be proceeding as though it were proceeding against a personal holding company. There is a different kind of problem in that instance, in contrast to what we are dealing with here.

Mr. JAVITS. The Senator is exactly correct.

Mr. McCARTHY. To follow the same rules or same standards or the same procedures, or the same methods, could be disastrous.

Mr. JAVITS. It is very interesting that the Senator and I, quite without knowledge of each other's purposes, should have come to the same end point as to how to tighten the control in the matter of unreasonable accumulation of earnings. Does not the Senator feel with me that if we had that, the ideal automatic control, without constricting or destroying what we are really trying to control—because we are not placing almost complete authority in the Collector of Internal Revenue—the courts probably would hold that the burden of showing that the amount retained is actually needed would in this case be on the taxpayer, unlike a domestic situation, in which the burden is on the collector?

If we assume that, are we not giving flexible power to the Treasury, to enable it fully to come abreast of any possible or conceivable imposition upon the Government, without at the same time by force of law automatically strangling these activities?

Mr. McCARTHY. The Senator is correct. The precedents in this field place the burden of proof upon the taxpayer. He must justify and defend himself against the charge of unreasonable accumulation. We know that even in dealing with domestic business and industry there is need for some degree of flexibility in the manner in which tax laws are applied. When we move into what is, in a sense, almost a lawless international competition, there is all the more reason why there should be flexibility in the way the law is administered, so that our businessmen competing in this field will not be put in an unfair position.

Mr. JAVITS. Knowing as we do so well how taxes are avoided, no matter how well we write the laws, with the help of high-priced talent employed for that

purpose, I believe that our provision, which gives the collector the opportunity by regulation or by administration to keep abreast of the situation all the time, would likely tighten the situation more than a set of strict rules would, because very astute gentlemen, studying them day by day and year by year, would find effective ways in which to avoid them."

Mr. McCARTHY. I think the Senator is quite correct. This was one of the arguments made for the action of the Senate committee in connection with the amendment which was under some discussion this afternoon, with regard to the present section 482, wherein the House attempted to write a rather restrictive formula on the basis of which allocations of income would be made. It was decided that it would be much better to leave some discretion to the Treasury Department. If we were to lay down four or five rigid standards, there would be more cases in which they could not be applied or in which they could be evaded, than there would be cases in which such standards would be helpful.

Mr. JAVITS. I should like to make a further observation, if the Senator will permit me to do so. Does not the Senator feel with me—as I have felt ever since I entered this complex and important field—that what we are dealing with is much more a foreign policy matter than a tax matter, and that we really ought to look at the situation from that standpoint, rather than from the tax point of view?

Mr. McCARTHY. I agree with the Senator. It is particularly important that we move hesitantly in this area at this time, because the whole complex international trade and international competition situation, which reflects politics as much as economics, is in a condition of flux. We anticipate the Common Market. It may be that the best thing that could happen for us in the United States in 4 or 5 years would be to have American investments within the Common Market, because there is some evidence that the first action will be one that will be somewhat restrictive in terms of international trade, after which there may well be a freer flow of trade. We must also consider the matter of the undeveloped countries where we seek to trade. Another factor to be considered is the Alliance for Progress. We must also consider the question of competition with the Soviet bloc itself. The weight of the argument is certainly against our taking this kind of rather drastic action, which does not have the support of reasoned argument or sound historic judgment.

Mr. JAVITS. I thank the Senator. I express my satisfaction at our unity in this very important matter, and my great interest at our having arrived at almost the same conclusion without consultation.

Mr. McCARTHY. Two Senators of good judgment can come to the same conclusion, even though one of them is a member of the Finance Committee, with whom the Finance Committee disagrees, and the other is not on the committee and has not heard the same testimony and evidence. I do not know what

significance there is in terms of justifying or sustaining the interesting statement of thinking along the same lines, but I am glad we are in agreement at this point.

Mr. JAVITS. I thank the Senator.

Mr. McCARTHY. Mr. President, since 1913, when the income tax law was first enacted, U.S. subsidiary corporations have been permitted to compete with local host governments. Subsidiary U.S. corporation income taxes were paid in the United States on those earnings until they were received in the United States as dividends. At that time they were subject to the ordinary tax imposed on dividends in the United States. No government, the United States or any other, so far as I know, ever asserted the right to levy taxes on the undistributed profits of nonresident or foreign subsidiaries except as in the case, to which reference was made earlier, of foreign personal holding companies, which is something quite different from a business or industry engaged in trade or commerce overseas.

But now the Treasury—this action has been sustained in part by the House of Representatives and sustained in part by the Committee on Finance, although neither the House Committee on Ways and Means nor the Committee on Finance has gone as far as the Treasury originally recommended—proposes to impose a tax on the undistributed earnings of subsidiaries and controlled corporations engaged in business overseas. What is proposed, I am sure, because I listened to the debate and the speech made earlier today by the Senator from Tennessee [Mr. Gore], is extremely complicated, as a reading of the report or the record of the hearings in this field will disclose. I believe the witnesses who have appeared have made it quite clear that responsible American businessmen are greatly concerned over the potential effects of the provisions of the proposed legislation on business health. They are concerned about its potential effect upon their ability to compete overseas, along with their concern about the effect of the legislation in terms of implementing, at home, the balance of payments, and particularly the future of our country's businessmen in the intensive competitive field of international trade today.

As a matter of fact, the record of the consideration of this legislation is one not of retreat, but certainly of departure from the original position. So far as there was a beginning in this field, it was the result of the original recommendations from the Treasury. They set forth some definitions. They proposed to eliminate all tax deferrals for what was called tax-haven income, which is defined as passive incomes from sales or service not directly derived from manufacturing. It included purchases from related persons and sales to related persons.

We moved from that to the action taken in the House, where some modifications were made. So far as tax havens were concerned, it was proposed to eliminate deferral for income derived from insurance and U.S. risk income from patent rights, patent incomes, and

sales income, unless invested in less developed countries. So there was both a retreat and an escape. Most investments in U.S. property would be taxed.

The Committee on Finance has departed from the original administration position and also from the position taken by the House of Representatives by way of moderating or modifying or making application of attempts to collect taxes on these incomes somewhat less severe—perhaps I should say more workable. It proposes to eliminate the deferral for income derived from insurance, U.S.-risk, foreign-based net income, of whatsoever nature, only when foreign-based company income is less than 30 percent of the total income of a subsidiary.

This will apply unless income is reinvested in less developed country corporations or in the country in which the subsidiary is located. The intent is to make the effect of the legislation somewhat less severe.

So far as export trade corporations are concerned, the tax deferral is to be conducted with specific limitations for private foreign corporations which derive 90 percent of their gross income for the prior 3-year period from sources without the United States, and which derive 75 percent—50 percent in the case of agricultural products—or more of its gross income from export trade.

I think this summary of what has happened to the proposed legislation since the original proposal of the Treasury, as it passed through the House Committee on Ways and Means, through the House, and the Committee on Finance, and came to the Senate floor, indicates first of all, that it was fully conceived, in the first instance, as it is now conceived; but in order for it to be effectively administered under the terms of the legislation as it now stands, the net effect would be that it would not accomplish the purposes which have been set out for it; and, in a sense, all the objectives claimed for it would not be accomplished.

At this point I should like to take up certain statements—I hesitate to call them allegations—with respect to the claim that has been made about the whole question of tax evasion and avoidance on the part of American businesses which have subsidiaries overseas. One of the charges is that tens of thousands of U.S. companies have gone abroad to avoid U.S. taxes, or that American companies have gone abroad in great numbers to avoid U.S. taxes. Perhaps "tens of thousands" is to set the number too high.

The total number of American firms engaged in foreign trade is estimated at about 3,000. Of this number, approximately 900 have foreign subsidiaries. Virtually all of these are legitimate businesses which annually report the financial condition of their businesses to the Commissioner of Internal Revenue.

A second charge that has been made is that American industry, according to statements made to some Members of the Senate, is that American industry is satisfied with the provisions of the bill as reported by the Committee on Finance. This is not true. Some

American businesses are reported to prefer to have what is in the bill now to what was in the House bill. Some American businesses have indicated to Senators that they would rather have what is in the bill than to run the risk of rocking the boat or stirring up trouble. Most American businesses engaged in oversea operations would prefer not to have the provisions of the Finance Committee bill as it now stands, but would prefer to use the method which I am proposing in my amendment, to provide for action against the unreasonable accumulation of profits.

Mr. MORTON. Madam President, will the Senator from Minnesota yield?

The PRESIDING OFFICER (Mrs. NEUBERGER in the chair). Does the Senator from Minnesota yield to the Senator from Kentucky?

Mr. McCARTHY. I yield.

Mr. MORTON. Would the amendment apply to the foreign subsidiaries of domestic corporations the same tax measures which apply to domestic corporations? It would do so, would it not?

Mr. McCARTHY. That is correct; it would apply the same rule.

Mr. MORTON. Therefore, would not the amendment cure the abuses of tax havens which have been pointed out to us?

Mr. McCARTHY. In my opinion it would cure all the abuses we can reasonably expect to cure, and it would not do the harm which would be done under the bill as proposed by the Finance Committee amendment.

Mr. MORTON. Is it not true that the treatment of foreign subsidiaries by means of the Finance Committee amendments would not be conducive to the entry of a new company into this field?

Mr. McCARTHY. In my opinion the amendments proposed by the Finance Committee are most acceptable to foreign subsidiaries overseas, and would make it very difficult for a company which needs to expand its operations overseas or is in need of establishing such operations.

Mr. MORTON. Madam President, I support the argument the Senator from Minnesota is developing and I intend to support his amendment.

If I may use an illustration which I used in the committee, in my opinion, the present situation is such that if 10 people wish to start a trucking corporation, with 5 stockholders in Minnesota and 5 stockholders in Kentucky, and if the corporation is successful and makes \$100,000, and decides to pay out \$25,000 in dividends and to keep the other \$75,000, to be spent in expanding the business and in purchasing more trucks and employing more people, one of the States—I shall not say which one—could say, "Oh, no; you must pay the tax on what was not distributed by you."

If that happened in this country, would not it be unconstitutional?

Mr. McCARTHY. I think so. But if a firm were operating in State A and in State B, State A might say, "We are sorry to say it, but since your expansion will be in State B, not in our State, we will have to impose our corporate tax

on the part of your income that you will be expending in State B."

Mr. MORTON. I think the Senator's point is a good one and should be seriously considered in connection with the amendment, because this situation goes far beyond the amendment, and goes to the basis of our taxation traditions.

Mr. McCARTHY. It is a departure from a practice and principle that has been in existence and has been accepted and acknowledged ever since the income tax was enacted into law in 1913.

Mr. MORTON. I wish the Senator's amendment well, and I shall support it.

Mr. McCARTHY. I thank the Senator from Kentucky.

Madam President, although public hearings were not held on the amendment which is known as the Kerr amendment to the amendment of the Finance Committee, as a substitute for the amendment acted on by the House, those who testified before the Finance Committee were nearly unanimous in their opposition to the provisions from which the Kerr amendment was developed. Specifically, industry opposed the violation of the 50-year-old principle that income is not taxable until it is received. The Finance Committee's proposals would penalize companies in less developed countries which have low tax rates. Also, it would penalize companies which are being expanded or are paying off their indebtedness—as the Senator from Kentucky has pointed out. It works against companies such as the Ford Motor Co. The witnesses testified that that would be the case in the United Kingdom, which has a corporate tax rate of 53.75 percent, or in Germany, which has a corporate tax rate of 51 percent.

I ask unanimous consent to have printed in the RECORD the testimony of various witnesses before the Finance Committee who testified not in regard to the effect of the amendments as included in the version reported by the Senate Finance Committee, but in regard to the amendments included in the version on which we acted, which version is, I think, in principle essentially the same as the one that was reported. I think the testimony of these witnesses for the most part runs against the amendments as finally adopted by the Senate Finance Committee and reported to the Senate.

There being no objection, the excerpts from the hearing were ordered to be printed in the RECORD, as follows:

Dow Chemical Co., Tyrone Gillespie: "More than 3,000 people and more than \$70 million in investment in the United States are directly employed in support of our foreign activities. Should foreign investment become unprofitable due to Government intervention, our judgment is that 60 percent or more of the domestic people and facilities supporting foreign sales might be idled."

Minnesota Mining & Manufacturing Co., Robert H. Tucker: "In 1951, a handful of our people handled our total foreign business. Today, 1 out of every 10 employees in our domestic factories owe their jobs to the fact that we are exporting products to foreign countries. Our experience is that exports are increased by foreign manufacturing operations. Business begets business."

Abbott Laboratories, George R. Cain: "Our foreign investments were not made at the expense of our exports from here, but rather because exports became difficult or impossible, due to trade barriers, tariffs, legislation, or arbitrary decisions protecting or favoring local industry in foreign nations, establishment of local factories and plants by competitors, etc."

"It is significant that Abbott Laboratories International Co.'s employment in Chicago, as a result of its increased capital investments abroad, rose 50 percent in the last 6 years."

"In addition, a large number of scientists, engineers, technicians, researchers, manufacturing and other personnel are now employed by our parent company, as a result of our expansion in foreign markets made possible by our increased investment abroad."

Joy Manufacturing Co., J. D. A. Morrow: " * * * In 1961, nearly one-third of the employment at (Joy Manufacturing Co.'s) Franklin (Pa. plant) was derived from * * * exports. The Treasury asserts that such cases are exceptional and not representative and should be disregarded. Here again the Treasury ignores the facts published by the Department of Commerce, which show that in 1960, out of \$18,900 million of exports, \$2,695 million went to or through foreign manufacturing subsidiaries of American corporations. These are not the statements of private industry, these are the Federal Government's own official figures."

Goodyear Tire & Rubber Co., Frank T. Quirk: "When domestic rubber companies decide to locate a plant overseas, most of the equipment for the plant is shipped from the United States and is made by American workmen. If further expansion is curtailed by revised tax provisions, not only will the foreign markets be taken over by foreign competitors but the machinery, equipment and supplies for their new plants will come from foreign producers."

"There are numerous examples in our industry where the annual purchases of replacement equipment, machinery, materials, and supplies to keep foreign plants operating represent more than the total U.S. dollar investment of the same company overseas. These purchases, amounting to many millions of dollars each year, provide work for thousands of people and are advantageous in our balance of payments position."

Pfizer International, John J. Powers, Jr.: "The key point is that those who say that direct business investment abroad results in the export of American jobs are simply wrong. For this to be true it would have to be demonstrated either (a) that such investments have been made for the purpose of producing goods for import into the United States in lieu of producing such goods in the United States, or (b) that U.S. direct investments abroad have produced goods for sale abroad which could otherwise have been exported from the United States. The facts do not significantly bear out either of these assumptions."

"For example, U.S.-owned manufacturing subsidiaries in Canada and Western Europe had total sales in 1960 of \$18.2 billion, of which only \$259 million was exported to the United States. It is preposterous to charge that U.S. business has gone abroad for the specific purpose of reselling a grand total of 1.4 percent of production back to the United States, or that \$259 million of such imports from foreign subsidiaries could cause any appreciable loss of jobs. Using ratios (jobs to sales) cited by labor officials, \$259 million of sales could mean about 30,000 jobs, or less than one-twentieth of 1 percent of the U.S. labor force—assuming that the goods represented by the \$259 million would have been made in the United States. But this assumption is not justified, for if U.S.-owned subsidiaries in Western Europe and Canada had not sold these goods

to the U.S. market, it is more likely that other foreign companies would have supplied the goods, not U.S. factories. Thus it is hardly justifiable to say that the imports cited were responsible for the loss of any significant number of jobs."

"While U.S.-owned facilities in Canada and Western Europe were selling \$259 million of goods to the United States in 1960, these same subsidiaries were importing \$1,246 million worth of goods from the United States. Using the same job-sales ratio, these exports from the United States created more than 100,000 jobs."

Harnischfeger Corp., Frederick Salditt: "Prior to our active participation in overseas investment and manufacture, the exports of our U.S. products lagged slightly behind the exports of our entire industry. With the advent of our active overseas manufacturing program, which involved the use of foreign subsidiaries' reinvested profits, etc., our exports of U.S.-produced goods have steadily increased. They have substantially surpassed the average for our industry, which has generally been on a steady to downward trend."

"This means that we have been able to maintain rather steady domestic employment and even increase it in some of our plants during a most difficult and competitive period. As a matter of fact, during the years 1958-59, we probably would not even have been a domestic taxpayer at all had it not been for our foreign operations and exports, and we most certainly would have employed fewer people in the States of Wisconsin and Michigan."

Sprague International Ltd., William M. Adams: "Although the argument has been propounded that the establishment of foreign manufacturing facilities exports U.S. jobs, our experience indicates that this is just not so. I cannot give you an accurate figure of how many of our employees owe their jobs directly to export, but I can tell you that, in many instances, lines would have been temporarily closed or restricted and employees laid off had it not been for the welcome export business that came into the house at that time."

"In other words, foreign plants stimulate exports and exports tend to cancel out the slack periods that occur from time to time domestically."

Pfandler Permutit, Inc., William G. von Berg: "It is a peculiar fact that in spite of our build-up of foreign manufacturing facilities, our export volume from plants in the United States did not suffer, but instead showed a tendency to increase. The reasons are several."

"First of all, we supply frit, a compound used in the glassing operation, to our foreign plants."

"Second, special parts and components are supplied from our U.S. plants to our factories abroad. As the activity of our foreign plants increase, so do our exports of frit, parts, and components."

"Third, as overseas customers became accustomed to our equipment and familiar with its advantages, orders for equipment in sizes which could not be made by our foreign plants were transferred to the larger U.S. plants for manufacture."

Dresser Industries, Inc., H. Neil Mallon: "In addition to the significant contribution which Dresser's export trade has made to our country's balance of payments, during the past 3 years over 5,800,000 man-hours of factory labor have been devoted to the production of export products. There is no way to determine how many additional man-hours of labor are attributable to our export trade as the result of our purchase of materials, components, supplies and services from others. If we assume that our suppliers sales require the same number of man-hours per dollar as did ours, this additional

employment due to our exports amounted to 3,405,000 man-hours."

"We hope to continue to do our part in improving the balance of payments and in promoting full employment. We cannot do so unless we will be competitive with foreign manufacturers who already enjoy many advantages not available to us."

As John L. Connolly, general counsel of the Minnesota Mining & Manufacturing Co., pointed out in his testimony: "First of all, a substantial part of the investment is normally spent promptly for capital goods and services in the United States with a consequent return of dollars. Secondly, once the foreign activity is established, it usually generates additional exports in the form of materials, parts, services, and even finished goods. These exports in all likelihood would not occur if the investment had not been made. Thus, the short-run improvement that could be expected in our balance of payments from the proposed legislation is more apparent than real."

Pharmaceutical Manufacturers Association, Kenneth C. Royall: "A survey of 10 of the members of the association, which included several of the larger members, over the years 1956 through 1960 shows that the total inflow from these subsidiaries to the United States was \$618,600,000 and the total outflow was only \$78,500,000. Total inflow exceeded total outflow by \$540,100,000, or by a ratio of 7.9 to 1. Official Government statistics show that over the same period the average annual exports of all medicinal and pharmaceutical products were \$273 million and the average annual imports were only \$16 million. These amounts of inflow will be no longer available if this legislation is enacted, because there will be no foreign market."

Joy Manufacturing Co., J. D. A. Morrow: " * * * (Joy's figures show) total 11-year parent company investment and advances to foreign subsidiaries of about \$7,400,000 and dollar expenses of operating abroad of \$11 million, a total dollar outflow of, roughly, \$18,400,000. Please note that these outlays brought \$170 million of exports in those 11 years, 60 percent of which went to or through our manufacturing subsidiaries abroad. In addition, payments of \$7 to \$8 million of engineering fees, royalties, dividends, and interest make a total net favorable balance of payments of \$159 million, and the U.S. Treasury collected more than \$16 million of income tax from these operations. Is that showing unfavorable to the U.S. balance of payments? Gentlemen, hundreds of other American foreign subsidiaries would present similar results if you had their figures."

Corn Products Co., Warren S. Adams: "We are a food company primarily. This means we operate on a low margin of profit. * * * There is in Europe tremendous competition in the food industry. We have to meet this competition and we have to invest money in Europe in the process. For us the Treasury's proposals mean not that we shall no longer invest money in Europe, but that a significant part of the investments we will have to make to protect our present investment there will be more costly than heretofore, and, thus, return less profit for remission to the United States."

Sprague International, Ltd., William M. Adams: "As a business grows, more working capital is needed. At present, this is supplied from foreign sources in local currency that has been earned abroad. Therefore, if this bill passes, the parent company will have to supply this capital from U.S. dollars instead of foreign currency and, furthermore, will have to earn twice as many dollars as would be the case using local funds. How this is going to help the balance of payments is beyond me."

International Flavors & Fragrances, Inc., Eugene P. Grisanti: "If this bill is passed in its present form, it would seem far more

likely that such funds, in the majority of cases, would be reinvested, and not necessarily in new business in the less developed countries where so many uncertain risks are faced, but in the expanding businesses where the existing subsidiaries are already situated. Funds which may well have been kept idle until the time was ripe to make a decision whether to repatriate them as dividends, or to invest in plant expansion, will be forced into plant expansion instead before the end of the tax year to escape the tax."

Pfizer International, John J. Powers, Jr.: "Treasury's ultimate position is that while direct investment abroad may, in the long run, have a beneficial effect on the balance of payments, it nevertheless has a short-term deleterious effect. This is simply a recognition of the obvious fact that a dollar invested today will not be returned until some time later. Thus, it follows that if the dollar were not invested, then during the period it would have taken to return it, the balance of payments would be favorably affected. But later, when the return from dividends, interest, exports, royalties, fees, etc., would have exceeded the prior capital outflow, the balance of payments would be permanently hurt, and to a far greater extent than it had been temporarily helped. The farmer who is short of money can cut down on his expenses by not planting seed in the spring. But where will he stand at harvest time?"

"Pfizer International has really been in operation only since 1951. In the period 1951 through 1961, Pfizer operations have resulted in a net inflow to the United States of about \$250 million. This is despite the fact that it is only in very recent years that we have begun to pay substantial dividends to the parent company. Prior to that time, nearly all profits earned abroad were reinvested. In the face of such a circumstance we nevertheless achieved this highly favorable balance because we exported almost \$200 million of U.S.-made goods to Pfizer foreign subsidiaries and because we brought home some \$50 million additional in dividends, royalties, fees, etc. Now that our investment has begun to mature and large dividends are being brought home, we are returning dollars at an annual rate of \$45 million. The parent company has not made any direct dollar investments abroad in many years and it is the policy of our company that its international organization provide its own financing."

Abbott Laboratories, George R. Cain: "For the 5-year period 1956-60, Abbott's exports from the United States exceeded its imports by \$50 million. Abbott also received from abroad loan repayments, dividends, and miscellaneous income in the amount of \$9.3 million—making a total inflow into this country of \$59.3 million."

"The total outflow of dollar from this country by Abbott, during the same 5-year period, in foreign investments and loans was only \$2.2 million. This gives our country a net favorable balance of \$57.1 million. * * *

"Proponents of the foreign income provisions apparently would not understand how a company can expand its foreign operations rapidly with so little outflow of U.S. capital. The answer is simple and well known to all who have had international business experience. Foreign plants can be and are financed very heavily through the use of locally borrowed money in addition to earnings retained overseas. Thus, we increase our base upon which greater future earnings are built. These earnings redound to the benefit of the U.S. Treasury as well as our own shareholders. This is accomplished without a heavy immediate or long-term drain on U.S. capital."

The Machinery & Allied Products Institute: "The establishment of a permanent operation overseas serves to facilitate contacts with foreign customers and by giving

the company greater local identification helps to penetrate markets which could not otherwise be penetrated. One company, with which we are familiar, prior to 1959 was unable to penetrate the German market to any significant degree. However, as a result of establishing an operation in that country it now finds that its German customers are not only willing to purchase from the German-based company unit, but, because of the greater local identification established by the U.S. company as a result of its German subsidiary, it now exports in substantial volume to the German market products which it is manufacturing in the United States."

Caterpillar Tractor Co., E. W. Kuhlman: "I wish to point out that none of our products are completely manufactured abroad; many of the components such as engines, transmissions, etc., are produced in our U.S. factories and exported to our foreign plants. If we did not manufacture the product abroad, the sale would not be made at all by us but would be made by a foreign competitor who would use no components manufactured in the United States. The significance of this factor is emphasized when it is noted that (1) our exports to Great Britain in 1960 were over four times those of 1950, the year before our subsidiary began operation; (2) our exports to Australia in 1960 were more than double those of 1955 when the subsidiary was formed; (3) our exports to Brazil in 1960 were more than five times those of 1956 when manufacturing began in Brazil."

Clark Equipment Co., Walter E. Schirmer: "Exports from Clark's U.S. plants in 1955 totaled \$5,500,000, consisting solely of machines and parts to distributors. By 1961 such sales had increased to \$12,500,000 and in addition component sales to manufacturing affiliates rose to \$10,500,000, for a total of \$23 million total exports from U.S. plants, excluding Canada. While total sales of Clark products overseas in 1955 therefore was only \$5,500,000, in 1961 this figure has risen to \$88 million including \$65 million sales of the Clark manufacturing affiliates. * * *

"Clark's program of investment overseas, far from being detrimental to our U.S. investment program, has produced profits for the parent company both in the sale of components, never sold overseas prior to this program, plus finished machines and service parts. This has provided increased funds in the parent company available for investment in facilities and working capital. During the years 1955-56 the parent company has invested in U.S. facilities and working capital \$40 million, and in that same period has invested in Clark International \$1 million. * * *

"Thus, it is obvious that the Clark foreign investment program has not in any way interfered with our domestic program, nor has it to any material extent affected our balance of payments, since the earnings of the parent company on its overseas exports has exceeded by far the original investment in International."

International Economic Policy Association: "A large part of the world is not available as a market for increased U.S. exports for cash. The Iron Curtain countries are a limited potential market for trade expansion for the near-term future; the underdeveloped countries do not have the resources to buy for cash—they are candidates for gifts and grants and so-called long range, 50-year low or no-interest loans. Therefore, our chance of selling more for cash is restricted pretty much to industrialized Western European countries and Japan."

"The question is: Can these exports be increased, not on a reciprocal, but a one-way unilateral basis by between \$3 and \$4 billion? With regard to Common Market countries, this much expansion in exports would require an almost 100-percent increase

over 1961 products of \$3.6 billion. * * * In total the immediate prospects do not come up to our needs."

"It is not, therefore, enough merely to exhort American industry to export more, because it is not likely that the total solution of the balance-of-payments problem will lie in this field in the foreseeable future, as long as we have to maintain our Military Establishment and the scale of foreign aid expenditures at levels comparable to the present. Therefore, the United States must think in terms of a long-range solution to this problem by expanding U.S. earning power abroad in ways other than exports; namely, the sale of services, and the making of investments on which growing amounts of earnings may accrue and, in the normal course of business activity, be repatriated to the United States. The encouragement of private investments abroad in hard, convertible currency countries must become one of the major objectives of the administration, with as much emphasis as given to the encouragement of exports."

As Mark H. Berens, of Mayer, Friedlich, Spiess, Tierney, Brown & Platt, told the Senate Finance Committee: "I cannot see that it is in our national interest to induce American investment operating in developed areas to be customarily in a minority position. American controlled foreign investment has meant greater cooperation of foreign enterprise with American policies, as for example the very noticeable pressure in other countries to cooperate with the U.S. embargo of certain trade with the Soviet-Sino bloc."

Ellsworth C. Alvord, speaking for the U.S. Council of the International Chamber of Commerce, noted: "Reinvestment of profits in a developed foreign country would be limited to the same trade or business in which the foreign corporation is already engaged. This is an incredible requirement. It serves no apparent policy or equity purposes, yet it places a tax penalty on dynamic and progressive business practices. It penalizes switching to new products. It could conceivably be interpreted as penalizing the opening of new branches of the corporation's old business. It is unbelievable that Congress would saddle this sort of a restriction on American-owned businesses in the European Common Market at the very time when this area is on the threshold of the greatest growth in economic activity and competition that it has ever experienced."

Harnischfeger Corp., Frederick Salditt: "We, meaning ourselves, and all U.S. industry, must be able to deliver our products to the foreign purchaser competitive as to quality, price, terms and service. Our real foreign competitors (by this I don't mean overseas subsidiaries or licensees of U.S. companies) are a very formidable group and are becoming more so. Generally they have various official means of assistance at their disposal encouraging exports, and in no case that I know of do they actually have roadblocks and hurdles thrown in their path to make exporting more difficult."

"We and other U.S. companies have had to go into overseas manufacturing to remain competitive and to hold markets which we would otherwise lose completely. Our overseas manufacturing and investments have helped maintain and increase our exports from this country. In our business these two things are inseparable. The utilization of tax deferral methods has helped provide the wherewithal to do this and to keep our overall costs, both overseas and indirectly in this country, in line so that we can maintain our position and fend with our competition with some measure of success. Anything which discourages this kind of foreign investment by taking away one of the many tools which industry needs in this fight just as surely makes for less rather than more U.S. exports. We have enough problems just staying competitive, and if

we are not competitive you may be sure that we will not export at all in the not too distant future."

International Economic Policy Association: " * * * unequal and inequitable tax treatment of income on U.S. investment in European subsidiaries may diminish the earning power of American companies operating there, to the extent that their foreign-owned competitors, enjoying more favorable tax treatment, may undersell, through competitive price reductions, the products of American-owned companies in Europe. Thus, the income on past investments, which the Treasury, in its assumptions, takes as a fixed item, uninfluenced by the current tax proposals, may in fact diminish, thereby reducing the amount of future earnings that may be repatriated."

Mayer, Friedlich, Spiess, Tierney, Brown & Platt, Mark H. Berens: " * * * no other major commercial nation taxes unremitted divided income to domestic shareholders (other than in personal holding company situations), nor do any have any legislation inhibiting the use of international trading, leasing, servicing, and licensing companies. Many give special tax preferences to foreign business income. Almost all of these nations have much larger per capita external investment and per capita export trade than does the United States. Moreover, their tax systems persisted through balance of payments crises far worse than we are now experiencing."

Pharmaceutical Manufacturers Association, Kenneth C. Royall: " * * * we would predict that if these provisions are enacted it will become virtually impossible for members of the Pharmaceutical Manufacturers Association to do business abroad. The Treasury Department has taken the opposite view. It has said that under these provisions American industry can continue to do business abroad because, as it states, the present demand for the products of foreign subsidiaries will continue as a demand for the exports from American industry."

"This assumption, we assert, is in error, certainly with respect to our particular industry. The proposed provisions will to a large extent dry up the foreign operations of the association's members."

"The reasons are simple. Foreign law and foreign competition require our individual members to conduct their foreign activities through foreign subsidiaries. The health codes and economic development programs of many foreign countries require that the final manufacturing and packaging processes occur in the country where the product will be sold."

"Even where there are no legal restrictions, foreign custom and prejudice require these processes to occur in the country where the product will be sold. For example, it is common knowledge that a French doctor will not prescribe for his patients a drug designated as American if a similar French drug is available. Nevertheless, as much of the manufacturing process as is possible or practical now occurs in the United States. But there is a limit to how far we can go. Without a substantial subsidiary in a foreign country and without foreign packaging, the market for our American products would be greatly reduced or—as to some important products—would disappear."

Price Waterhouse & Co., O. Kenneth Pryor: "It is not healthy for the future of our own economy to reason that if a U.S.-owned enterprise has to bear a greater tax burden than its competition, all that happens is that it may have to pay this additional tax from U.S. earnings, or from new capital. In either event, funds otherwise available for investment at home are taken away."

Clark Equipment Co., Walter E. Schirmer: "Following the overall profitability of Clark's program in industrialized countries such as France, West Germany, Great Britain, and

Belgium, it was possible to provide, out of these earnings, for a substantial investment in Brazil, a less developed country. This investment now amounts to almost \$10 million, no portion of which has come from the parent U.S. company. It is by far our largest single investment, and almost one-half of it was the purchase of machinery, tools and supplies here in the United States. Such an investment in a country such as Brazil requires greater capital, and a much greater risk because of dependence upon untrained labor, insufficient supplies either in quantity or quality of materials, lack of local capital, governmental instability, and other deficiencies. This plant was started early in 1957 and did not make any profits whatsoever until June, 1961. It will be at least several more years before our earlier losses can be wiped out and the entire operation considered satisfactory."

"As an officer and director of our parent company, I can assure you that no such investment of after-tax parent company earnings would ever have been risked in this project."

"If H.R. 10650 becomes law, I am not qualified at this time to say what its exact overall effect will be on our company, but certainly it is going to reduce materially our earnings from our oversea operations. This will, of course, cause a substantial reduction in our overall foreign investment program, with the major reduction taking place in the less-developed countries, where we will undoubtedly curtail any further expansion because of the risks involved."

Owens-Illinois Glass Co., R. H. Mulford: "Instead of stimulating American business to invest more money in the so-called undeveloped countries, it (the bill) would cut down the amount of risk capital available for such ventures. Profits from subsidiaries in developed countries make it possible to take the much greater risks in undeveloped countries. This bill not only discourages further investment in the countries which supply the risk capital, but it also puts an unreasonably short time limit on investment of oversea earnings in undeveloped countries before they are eroded by U.S. taxes."

Minnesota Mining & Manufacturing Co., Robert H. Tucker: "U.S. industry feels it has been a partner with the U.S. Government in raising the technological and living standards of other countries through our private investment programs. It has been U.S. foreign trade policy to increase exports * * * and yet a tax bill has been designed which will tend to reduce the amount of U.S. exports. As a representative of a company engaged in foreign trade for many years, it is my firm belief that many sections of this bill relating to foreign activities will have a practical effect which will run directly counter to what I have understood to be the U.S. Government's foreign trade policy."

The Machinery and Allied Products Institute: "It should be emphasized that earnings brought back to this country will normally not be transferred to underdeveloped areas. We have been informed by some companies that top management is extremely reluctant to approve new investment of capital in countries of South America, Asia, or Africa from earnings generated within the United States because of the relatively high risk accruing to such investments."

For 28 State and Regional Chambers of Commerce, John L. Connolly: "American investments and business operations in the highly developed countries have brought benefits to the underdeveloped countries. Improvements in production and marketing in other highly developed countries, as well as in the United States, have lowered the prices of goods and services, brought new products into being, and increased the availability of new productive facilities and techniques for the underdeveloped countries."

"The profits of American business in the more highly developed countries have provided surplus funds which may be invested in these countries or the underdeveloped countries. The increased prosperity in the highly developed countries to which American business investments have contributed also make it possible for these countries to share with us the foreign aid programs for the benefit of the underdeveloped countries."

International Flavors & Fragrances, Inc., Eugene P. Grisanti: "If it is a worthy objective to foster investment in the less developed countries, must an American company be penalized by an extra tax burden, unless it does so? This is, in essence, what the tax bill does. United States businesses were once encouraged to assist in rebuilding and investing in the devastated economies of Western Europe after World War II. Will the American companies who now respond to the call to invest in the less developed countries, after a decade or more has passed, be penalized for their initiative, as this tax bill seeks to penalize those who have responded to a previous call."

Committee of 18 New York tax lawyers: "The bill's provisions in respect of foreign income are so complex, overlapping and replete with unprecedented tests that it is difficult to analyze them. The members of this group submitting this report are experienced in matters of tax law; they have spent over 40 hours in group discussion and countless hours of individual study reviewing the contents of the aforementioned sections."

"Despite this, the practical problems of working with the proposed legislation are so immense that the group has found it difficult to understand the bill and impossible to measure its full impact. So many new concepts are included in the bill that a definitive technical analysis by tax practitioners has been virtually impossible. The complexity of its provisions can only cause uneven and arbitrary enforcement and administration of the bill. Skilled tax practitioners will undoubtedly find technical loopholes."

"On the other hand, many U.S. entrepreneurs will by chance find themselves caught by extremely harsh provisions of the bill which by proper planning could have been avoided. Revenue agents cannot be reasonably expected to understand the provisions or to enforce them uniformly. Thus, the impact of the bill will be haphazard."

"The immense complexity of the proposed legislation can only occasion immense and unprecedented difficulty and cost of administration and compliance. The administration of section 13, as now drafted, would require, to mention a few of the worst, regular determinations: whether a foreign corporation is controlled at any time during the year; whether a taxpayer directly or indirectly owns 10 percent of the voting power or total value of the shares of a controlled foreign corporation; whether patents, copyrights, and exclusive formulas and processes were substantially developed, created or produced in the United States; amounts of royalties to be imputed to exploitations of such U.S. source intangible rights; whether fees are for services or for the exploitation of intangible property rights; where the ultimate destination of goods is; where certain goods are deemed to have been manufactured; whether earnings are reinvested in substantially the same trade or business; and whether investments in property are ordinary and necessary to the active conduct of a trade or business as to be qualified property. Each of these determinations normally will be difficult and costly, and frequently will be virtually impossible."

"In reading it, one is impressed with the highly complicated and uncertain language employed, which will take years to clarify, and has the feeling that it was concocted

in great haste and without due consideration of all of the phases of U.S. foreign operations.

"The result can only be long-drawn-out controversy, years of uncertainty as to the tax liabilities of major segments of our business community, and possible eventual dictatorial imposition of tax liabilities with no adequate opportunity for appeal or review.

"Under present law, if the foreign subsidiary were a branch instead of a subsidiary, not only would its income and earnings be taxable to the parent corporation, as this act would have it, but also its losses would be available to the parent corporation to offset other taxable income. But if the proposed act is passed, there is no provision at all for the utilization of a foreign subsidiary's losses by the American parent corporation to offset other taxable income. It is very possible for the parent corporation to be taxed on income or earnings of the subsidiary which were not paid to it in the year of taxation and which will never be paid to it because of subsequent losses by the subsidiary."

Corn Products, Co., Warren S. Adams: "The transparency of the neutrality concept is quite clear. In one breath it is stated that 'neutrality is a fundamental principle of taxation in the United States.' In the very next breath the same spokesman says 'historically we have not adhered to the tax neutrality concept as it relates to domestic and foreign corporate income.' And in still another breath we are told that this fundamental principle, which is honored far more in the breach than in the observance, should be followed as far as investments in developed countries are concerned, but should be disregarded as far as investments in underdeveloped countries are concerned—someone in the executive department making the determination from time to time as to which country falls into which category.

"In addition, there is the problem of the constitutionality of the proposals. To tax one on income that has not been received and, indeed, may never be received, as for instance, if subsequent losses wiped out dividends paying ability, would seem to deny due process."

International Economic Policy Association: "Contrary to the claim of the administration that current taxation of foreign profits of foreign corporations will produce tax neutrality, the proposal will add another inequity in the law by burdening American business overseas with a heavy U.S. tax when their competitors are not so burdened."

Price Waterhouse & Co., O. Kenneth Pryor: "No one can quarrel with espousal of 'equity' or 'equality,' or with the removal of 'special privilege' and 'preferential treatment.' But the facts are that these proposals would create burdensome inequities and inequalities and no case has been made that 'special privileges' or 'preferential treatments' generally exist.

"These earnings could not even be offset by losses of the same foreign corporation in other years; or by current losses of other controlled foreign corporations. Thus, inequitable as it would be, the domestic corporation could owe an income tax in an amount that would be greater than the total income actually realized by it and its foreign affiliates."

Clark Equipment Co., Walter E. Schirmer: "But between whom do they wish to assert this neutrality? If our foreign competitors pay lower taxes, the imposition of higher U.S. taxes on the earnings of our foreign companies will not impose such neutrality between these Clark foreign companies and their local foreign competitors. A controlled foreign corporation of Clark domiciled completely overseas and carrying on no business in the United States receives no services from the United States so any tax charged on its

income not transferred to the United States is certainly not tax neutrality.

"Many of the provisions of this legislation have questionable legality, and may be considered by some countries a violation of existing tax treaties."

Adrian A. Kragan, professor of law, Berkeley, Calif.: "In the event that an accretion to wealth in and of itself can be considered as income for U.S. income tax purposes, we would only need to consider whether the proposal to measure an income tax by such accretion accorded the taxpayer due process of law. In essence this is the much considered and discussed question of whether realization is necessary in order to have income within the meaning of that word in the 16th amendment of the U.S. Constitution.

"The focal point for any discussion of the doctrine of realization is the classic *Eisner v. Macomber* case. In *Eisner v. Macomber* there was, in my opinion, a clear and unequivocal statement that income of a corporation could not be taxed to the shareholder without a receipt of that income by the shareholder, i.e., that realization in some measure is essential to the definition of income for Federal income tax purposes.

"The Supreme Court of the United States has never seen fit to overrule the fundamental doctrine enunciated in the case. In fact, even where the court has distinguished *Eisner v. Macomber*, it has actually or impliedly recognized the continuing validity of the definition insofar as realization is concerned.

"The doctrine that the corporate entity is an entity distinct and apart from that of its shareholders is one of long standing in Anglo-American law and in our Revenue system. The Supreme Court in *Eisner v. Macomber* placed this doctrine on a constitutional footing when it stated that the income of a corporation was not income to a shareholder within the meaning of that term in the 16th amendment.

"The Supreme Court has indicated that this constitutional prohibition does not exist when the corporate entity is not a real entity, when the corporate entity is in effect a mere form without substance.

"We are dealing in the area of taxation with a constitutional definition of income enunciated by the Supreme Court and with the apparently established right of the taxpayer under the due process clause of the Constitution to be free from compulsory taxation on that which is not and cannot be obtained or enjoyed by him. Whether the shareholder has sufficient 'control' to be an 'insider' for the purposes of the Securities and Exchange Act or has sufficient 'control' to be considered as falling within the reach of the Public Utility Holding Company Act is not relevant in the instant situation where established specific constitutional questions must be resolved.

"In the cases decided since *Collector v. Hubbard*, which have determined that the corporate entity should be disregarded and corporate income attributed for tax purposes to the shareholders, there was no doubt that actual command of the corporate income existed in the shareholders.

"This actual command of the income is the essence of the Treasury's own regulation on constructive receipt of income (Reg. 1-452.2 (a)). However, the provisions of section 13 of H.R. 10650 would allow the taxation of income to shareholders who had no command of the income and no possibility of acquiring actual control of it. Under the provisions of section 13, a shareholder who owned 10 percent of the voting power of a foreign corporation and who had no relationship with the other shareholders, no representation on its board of directors, and no actual power to determine its policies

would be considered to have constructively received income of the corporation which as a matter of actual fact he might never receive or have command over. Further, this attribution might occur even though the corporation could not have distributed the income to its shareholders by reason of the law of the country of its organization.

"The fact that the shareholder happened to be an American and that 51 percent of the total corporate shares were held by Americans is hardly a sufficient basis upon which to conclude that he had actual control over the corporate income. It cannot be logically reasoned that the remaining American shareholders were subject to his domination and control as if they were members of his family for it is manifest that shareholders who possess only a common nationality do not have the same common economic interests as do members of a natural family group. With respect to the 10-percent American shareholder, there is in my view no difference between a situation where 41 percent of a 51-percent American majority is in the hands of unrelated Americans and one where all the shares other than his 10 percent are in the hands of foreign shareholders.

"The attribution of the income of a bona fide operating corporation as provided in section 13 of H.R. 10650 would appear to attribute the income of A to B in violation of constitutional principles."

Mayer, Friedlich, Spiess, Tierney, Brown & Platt, Mark H. Berens: "In most of the developed countries, the effective tax rates (for domestic income) are from about 5 to 25 percentage points below the American corporate rate, which means that if this legislation is adopted, American investors in the long run must either divest themselves of their majority position in foreign corporations operating in developed areas or retain a smaller portion of the market than they would if their tax cost were equal to competitors in the same markets.

"This choice is even more acute to the extent that the legislation inhibits use of international trading, leasing and service companies, or of companies exploiting intangible rights on an international basis. Such so-called tax haven companies must compete with foreign financed enterprises performing the same type of activities at rates seldom exceeding 15 percent. It is these types of international companies that most effectively have developed U.S. exports in competition with foreign made products."

State and regional chambers of commerce, John L. Connolly: "We are opposed to placing all taxpayers operating in these countries in a straitjacket because of tax evasion by some."

Corn Products Co., Warren S. Adams: "The Treasury's tax proposals will bite this company to the tune of \$2 million a year. And, yet, I know of nothing reprehensible that we are doing in the foreign field by way of playing games with the U.S. Treasury.

"We think it only fair and honest that it be conceded that sufficient law exists today to meet most of such abuses—as the shell corporation or the intercompany loan that, in fact, is not a loan, or downright dishonesty in the failure to report transactions."

Clark Equipment Co., Walter E. Schirmer: "We certainly agree with the proponents of the bill that tax deferral should not be obtained by so-called 'paper companies' in sham operations. However, the U.S. Treasury now has the necessary preventive controls available to control such situations, if properly exercised."

Mr. McCARTHY. Madam President, it is said that many American industries establish operations abroad in order to

avoid taxation. I say these developments occur primarily for other reasons, not for taxation reasons.

One charge which is made is that tens of thousands of U.S. companies have gone abroad to avoid U.S. taxes.

Madam President, an estimated total of 3,000 American firms are engaged in foreign trade. Of these, approximately 900 have foreign subsidiaries. Virtually all of these are legitimate businesses which annually report all financial data to the Commissioner of Internal Revenue. Most abuses are in the area of individuals who have incorporated bank accounts. These can be stopped through the unreasonable accumulations approach, without hitting legitimate overseas operations.

Another charge which is made is that American industry is satisfied with the provisions of the Kerr amendment.

But this is not so. Although public hearings were not permitted on the Finance Committee amendment, American industry—and its representatives, such as the National Association of Manufacturers and the U.S. Chamber of Commerce—testified before the Finance Committee with near unanimity against the provisions parent to the Finance Committee amendment. Specifically, industry is opposed to the violation of the 50-year-old principle that income is not taxed until it is received. The Finance Committee proposals penalize companies in the less developed countries which have relatively low income tax rates. Also, they work against small companies and medium-sized companies which have not yet built or paid for their plant and equipment or repaid their indebtedness. They work in favor of large corporations, such as Ford Motor Co., which already have established large facilities abroad in high income tax countries, such as the United Kingdom, which has a 53.75 percent corporate tax rate, and Germany, which has a 51 percent corporate tax rate.

Another charge is that whole industries like the typewriter industry go abroad to avoid taxes. This results in the export of thousands of U.S. jobs.

However, first, these industries do not produce abroad for tax reasons, but rather for other economic reasons. Second, if American companies did not go abroad to produce, the U.S. market would be taken over by foreign-owned firms—Olivetti, and so forth—and the United States would lose dividends, interest, royalties, and so forth.

Another charge is that section 12 is needed to stop movie producers and movie stars from setting up incorporated "pocketbooks" abroad to avoid U.S. taxes.

But the McCarthy amendment would accomplish this purpose without injuring legitimate U.S. business abroad. Accumulations would not be allowed for the purpose of avoiding U.S. taxes.

Another charge is that the present draft as amended by the Finance Committee makes special concessions for underdeveloped countries and is consistent with *Allianza* program, and so forth.

However, while it does allow for reinvestment of the earnings of underdeveloped country corporations in underdevel-

oped countries, the present draft is not consistent with *Allianza*, and so forth, in the following respects: First, it does not allow for reinvestment in underdeveloped countries of earnings from developed countries; second, the Kerr sliding-scale amendment treats underdeveloped countries—which usually have lower effective tax rates—worse than it treats developed countries, the burden of repatriation or taxation consequently could be much heavier on the low-tax countries.

The Finance Committee export trade corporation amendment is more confining in less developed countries, because of the promotion expense limitation. In developed countries, competition usually necessitates greater promotion expenses and results in less limitation than is imposed in less developed countries, which have greater risk but usually lower promotional expense.

The sixth allegation is that the present section 12 provides protection for qualified investment in countries whose designation may be changed from "underdeveloped" to "developed."

This is true only as to qualified investment already made. Protection is not given to committed investment which would be qualified. Let us assume that a corporation had committed itself to a \$5 million investment program to be completed over 5 years. If only \$1 million had been invested when the country designation was changed by the President, this would be the only part of the investment protected, even though it might be worthless unless the commitment for the other \$4 million were fulfilled.

I cite this as a special example of the kind of confusion which would be injected into American business overseas if this committee amendment were adopted.

The seventh allegation is that section 12 would not make U.S. business noncompetitive. This being an income tax, the fact that it would have to be paid means that we have already successfully competed. That is the allegation.

Obviously, it would not make all American businesses noncompetitive, but it would put all of them at a competitive disadvantage, and in some cases make them noncompetitive. Obviously, we measure the success of a business venture in terms of earnings after taxes, whether we use them for dividends, reinvestment, replenishing inventories, or increasing promotion expenses. If a U.S. subsidiary in Europe must pay 52 percent on all earnings and is competing with a Swiss subsidiary of a German parent which is paying a tax of only 10 to 15 percent, it has less earnings available for replenishing inventories, hiring more salesmen, buying more advertising space, and conducting other activities which would make it a more effective competitor.

If we were to think of a 1-year basis and say this is successful because, despite the tax law, there is a profit, or say that only when there is a profit is a tax to be imposed, we might make a case. The fact is that it has to be based on a projection of operations over a longer period

of time. To make this kind of argument is to attempt to distract the attention of the Senate away from the real question which should be its concern.

The eighth allegation is that the use of "tax haven" subsidiaries is unique to American business and should be eliminated as an artificial incentive. I put the words "tax haven" in quotation marks because the term has come to take on a connotation far beyond what in many cases it should carry.

The answer is deserving of the Senate's consideration. According to Treasury Department figures, U.S. corporations have 1,025 subsidiaries in Switzerland. Five European countries, with a smaller total gross national product than the United States, have an estimated 1,474 Swiss subsidiaries.

I cite this to make the point that, far from being unique to American business, they are even more widely used abroad than in the case of our country. Second, instead of being artificial incentives to tax avoidance, foreign based sales companies are essential to maintaining the competitive position of U.S. business in world trade, particularly in the Common Market area. They will become, I think, much more important in that area as the Common Market develops, as they have in the recent past.

The ninth allegation is that there is no reason why U.S. corporations operating abroad should not pay the same taxes and bear the same burden of paying for government as U.S. companies operating here at home.

This would seem to be a compelling argument unless one looked beyond the superficial and immediate period. In the first place, these are not two different classes of companies. Corporations doing overseas business are domestic companies that do a substantial amount of the total domestic business, for the most part, and pay U.S. taxes.

Second, they bear the same burden under present law when the foreign earnings are available to the U.S. parent as domestic earnings do. When these earnings are repatriated they are subject to the same tax as if earned in this country.

Third, even Secretary Dillon, in making the same statement, related the tax burden which should be borne to the receipt of equivalent or equal services from the U.S. Government. U.S. companies do not receive equivalent services from the U.S. Government on unremitted earnings of foreign affiliates as they do with respect to domestic earnings.

The argument could be made that it is impossible to establish a ratio or proportion and say they should pay so much or repatriate so much. The fact is that they do not receive the same service on unremitted earnings.

A further consideration is that it is an altogether different kind of competitive situation. To say that they should pay the same taxes as firms doing business in the United States pay is to be utterly unreasonable and to neglect the basic facts of the situation—first, that they do it on what is repatriated; second, that they do not receive the same services;

third, that they are operating in a different kind of competitive situation.

All these factors should be taken into account as we consider the possibility of changing the tax law in this regard.

The tenth allegation is that foreign investment should be discouraged because of its adverse effect on the balance of payments. The adverse effect results from a time lag of 10 to 15 years between the export of capital and the return on the investment. So the argument runs.

If one were to take a section out of time, I suppose there would be strength in the argument. We must base it either on the overall record or on the historical record of investment overseas and the return of capital or investment. On that basis, if we look at the record in recent years—the last 12 years of the postwar period—the record shows that foreign investment does not adversely affect the balance of payments. Except for the year 1957, the inflow to the United States of dividends and interest on U.S. investments abroad has exceeded the outflow from direct investments in every year since 1950. Over the 12-year period mentioned, the net inflow to the United States—the excess over what went out by way of investment—has been \$8,552 million.

I ask unanimous consent that a table showing the record in each year from 1950 through 1961 may appear at this point in the RECORD.

The PRESIDING OFFICER (Mrs. NEUBERGER in the chair). Is there objection?

There being no objection, the table was ordered to be printed in the RECORD, as follows:

SCHEDULE A

Dollar inflow and outflow to direct investment—Companies abroad, 1950–61
[In millions of dollars]

Year	Direct investment outflow	Dividends and interest inflow	Net inflow
1950	621	1,294	673
1951	528	1,492	964
1952	850	1,419	569
1953	751	1,442	721
1954	664	1,725	1,061
1955	779	1,912	1,133
1956	1,859	2,120	261
1957	2,482	2,249	-233
1958	1,181	2,140	959
1959	1,372	2,206	834
1960	1,694	2,348	654
1961	1,681	2,637	956
Total	14,432	22,984	8,552

NOTES

1. Data from Department of Commerce. See p. 3.
2. Covers all areas and all activities, branches, and subsidiaries.
3. Unremitted branch earnings are included in both "Outflow" and "Inflow" columns.

Mr. McCARTHY. Certainly, this is the best evidence, in my judgment, to answer the charge that this tax program should be adopted because the record foreign investment should be discouraged because of its adverse effect on balance of payments.

The record, taken as a whole, shows that there has been a net gain over the period of 11 or 12 years of more than \$8 billion.

It is argued that if investment abroad were curtailed there would be more to invest within the United States, and that such added investment in the United States would provide more jobs in the United States, whereas the investment abroad is equivalent to the exporting of jobs.

I submit that these allegations are made without any real attention to the economic facts of life in this picture. I assume that there are some limited areas in which there has been some export of jobs. It is impossible to sort out the cases in which that would be true.

Again, one must look at the overall picture on the basis of competent testimony and on the basis of the record, to come to some reasonable conclusion. The conclusion at which I have arrived, after participating in the hearings on this bill and giving the subject most careful study—because certainly I am concerned about possible export of jobs, about unemployment, and about the flight of industry, when those things occur—is that the tax program as recommended would prevent the loss of jobs in America. I am convinced that it would contribute to an increased solving of the problem of unemployment and would not cause the loss of jobs to Americans.

I speak, of course, of the program I am recommending.

In my judgment, direct investment in business operations abroad has created substantial employment in the United States. I should like to cite some of the facts given in the testimony which was presented to our committee.

Abbott Laboratories testified that company employment in Chicago rose by 50 percent in 6 years as a direct result of the increased capital investments abroad. This, they said, would not have happened without their oversea outlets.

Dow Chemical representatives testified that more than 3,000 employees in the United States are directly employed in support of their foreign sales.

Dresser Industries, to which reference was made earlier today, testified that "additional employment due to our exports amounted to 3,405,000 man-hours."

Minnesota Mining & Manufacturing Co., which is a most reputable firm in my State, said:

Exports are increased by foreign manufacturing operations. Business begets business. In 1951 a handful of our people handled our total foreign business. Today, 1 out of every 10 employees in our domestic factories owe their jobs to our foreign operations.

The statement by the witness from the Minnesota Mining & Manufacturing Co., at least with reference to what it has to say about the balance of payments, is particularly deserving of the attention of Members of the Senate. Certainly to the extent that it gives additional data in regard to the flow of investments, the return of capital, and the return of income to the United States, it has a special bearing upon the debate in the Senate today.

I have no reason to question this testimony, or to believe that this is not a

reasonably accurate judgment on their part, or that it is not an honest conclusion and an honest statement of their judgment with regard to the possible effects of the proposed tax change.

Cutting back on growth abroad would result not in greater U.S. production but in curtailed U.S. production as a result of lower levels of exports to support the oversea subsidiary operations. It will not improve the balance of payments. It will not create jobs but may well destroy them.

Madam President, I ask unanimous consent to have printed in the RECORD exhibit A, which makes reference to a statement made by the Assistant Commissioner for Compliance of the Internal Revenue Service, particularly with respect to section 482 of the present law, dealing with the allocation of earnings of controlled corporations; schedule A, to which I referred earlier, regarding dollar inflow and outflow to direct investment; and schedule B, regarding dollar inflow and outflow to direct investment abroad.

There being no objection, the exhibit and schedules were ordered to be printed in the RECORD, as follows:

EXHIBIT A: ASSISTANT IRS COMMISSIONER FOR COMPLIANCE SAYS PRESENT LAW NOT USED TO FULL POTENTIAL

In a speech before the American Management Association on Thursday, April 26, 1962, William H. Loeb, Assistant IRS Commissioner for Compliance, made the following statements:

Present tax law allows IRS to reallocate income among the related corporations where necessary to prevent evasion of taxes. These reallocation decisions are subject to court review, but the courts have ruled IRS can reshuffle income if the intercompany prices are higher or lower than would be charged if the corporations weren't related. This is known as the arm's-length rule.

He added that perhaps IRS hasn't yet "used the full potential" of the law that allows it to reallocate income. "In the future we intend to utilize that potential to the fullest extent possible," he said. He added IRS will be helped in this by a 1960 law requiring more detailed reporting of foreign transactions by U. S. taxpayers.

SCHEDULE A

Dollar inflow and outflow to direct investment—Companies abroad, 1950–61
[In millions]

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1950	\$621	\$1,294	\$673
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1961	1,681	2,637	956
Total	14,432	22,984	8,552

NOTES

1. Data from Department of Commerce. See p. 3.
2. Covers all areas and all activities, branches, and subsidiaries.
3. Unremitted branch earnings are included in both "outflow" and "inflow" columns.

SCHEDULE B

Dollar inflow and outflow to direct investment abroad—Pfaudler Permutit, Inc.

[In thousands]

	10 years (Jan. 1, 1952, to Dec. 31, 1961)	
	Amount invested abroad	Amount of income received in United States (before U.S. income taxes)
Western Europe.....	\$40	\$2,385
Far East.....	164	1,364
Western Hemisphere (outside United States).....	1,088	450
Total.....	1,292	4,199

(During the delivery of Mr. McCARTHY's remarks:)

Mr. KEATING. Madam President, will the distinguished Senator from Minnesota yield?

The PRESIDING OFFICER. Does the Senator from Minnesota yield to the Senator from New York?

Mr. McCARTHY. I yield to the distinguished Senator from New York.

Mr. KEATING. Madam President, I ask unanimous consent that my remarks be printed at the conclusion of the remarks of the Senator from Minnesota.

The PRESIDING OFFICER. Without objection, it is so ordered.

Mr. KEATING. Madam President, I wish to express my support of the amendment offered by the distinguished Senator from Minnesota. As he knows, it is a matter in which I have had a deep interest. I believe he has fashioned an amendment which should be agreed to.

It strikes me that section 12 of this bill is in direct conflict with the objectives of the pending trade bill and with our overall effort to strengthen and expand the economic ties that bind the free world.

Our investments overseas allow us to get into markets from which we might otherwise be excluded. They help our allies and the free world to grow and prosper. They earn money for American shareholders; in the final analysis, they result in a net inflow of gold back into the United States. Finally, they create work for American workers who make parts for products assembled overseas, and who are engaged in all of the other work connected with the transactions by foreign subsidiaries.

There are, of course, people who take undue advantage of this privilege. They are like tax chisellers" anywhere. We must use a fine toothed comb to ferret them out. It would be a great mistake to adopt a broad, comprehensive, new, and unwise tax principle simply to avoid abuses in this area. The amendment of the junior Senator from Minnesota is so carefully worded that he meets that proposition, it seems to me, properly. His amendment would toss out the dirty bath water but save the baby.

Every other nation which does business in world markets and which earns capital overseas permits deferral of overseas income until repatriated. If we restrict our American firms from

doing this, we will seriously threaten their ability to compete. It would be a wonderful thing for their competitors—but it would be a very bad turn of events for us and our industries and our workers.

Let me cite a comment by a Canadian newspaper reporter writing in the Toronto Financial Post. He says this bill will put our U.S. firms overseas at a big disadvantage.

He says in part:

It is certainly clear, in the field of foreign trade, that a foreign corporation controlled by Canadians—or an oversea trade corporation in Britain—will have a decided advantage over its U.S.-owned competitors.

The new law will also serve to trim American sails in Europe, increase the downward pressure on the U.S. dollar and indirectly assist Britain's entry in the Common Market.

Then he says:

Let's hope that Ottawa encourages Canadian business to take full advantage of the mistakes south of the border.

Another source of expert opinion which I respect in this area is former Assistant Secretary of the Treasury Dan Throop Smith. His testimony before the Finance Committee on this point was most lucid. He said in part:

American parent companies usually establish foreign subsidiaries to maintain a position in foreign markets or to secure a position in new markets. They do not establish foreign operating subsidiaries as an alternative to expansion at home for production of export commodities. When foreign markets become large enough and foreign conditions for production good enough, production is going to take place abroad. There are plenty of local companies able and anxious to expand to meet domestic requirements in foreign countries, and plenty of large corporations in other major industrial countries able and anxious to set up their own foreign subsidiaries, and active in doing so. If our country is to get its rightful competitive share in the expanding income of the world, our business firms must be free to compete where production is taking place.

And, again he sums the situation up neatly when he says:

American-owned subsidiaries abroad are in competition with other businesses abroad; they are not primarily in competition with domestic production in the United States.

Madam President, the evidence I have seen and the people I have talked to have convinced me that this amendment is highly desirable. It is a complicated and difficult subject, but the essential question is, are we to compete or retreat. I favor competition. I want our Nation's private industries to continue to show the world that American "know-how" and ingenuity—both at home and abroad—have got what it takes.

For those reasons I am glad to support the amendment offered by the distinguished Senator from Minnesota, and I am grateful to him for allowing me to intrude on his time.

Mr. McCARTHY. I appreciate the support of the Senator from New York.

Mr. JAVITS. Madam President, I ask unanimous consent that my remarks may follow those of the Senator from Minnesota [Mr. McCARTHY] as they relate to the amendment which I jointly sponsor with him.

The PRESIDING OFFICER. Without objection, it is so ordered.

Mr. JAVITS. I have every hope that tomorrow Senators will read the RECORD of tonight, because we shall then have only a relatively short of time for debate. I shall do my utmost to summarize why the approach which is taken by the Senator from Minnesota [Mr. McCARTHY] and myself in respect to making the taxation of the earnings of foreign subsidiaries a matter cognizable under the unreasonable cumulation of surplus provisions of the law, rather than by direct taxation and imputation to the American stockholder, is superior in every way to the scheme which is contained in the bill. It seems to me that our proposal rests upon four arguments.

First. The essential competition with foreign operators in the foreign field.

Second. The fact that the provision in the bill will work adversely with respect to new firms which do not have an established and long-standing pattern of operations abroad.

Third. It makes a distinction, which will turn out to be invidious to our own national interest, between developed nations and less developed nations.

Fourth. Because the so-called escape valve which the Committee on Finance has established in order to make the provision more palatable will not act as such because it is based upon the fundamental proposition of taxing corporate earnings to shareholders before distribution. This is something the United States has never done in terms of operations of this nature, except possibly with respect to personal holding companies, which we are not arguing about here, and something which no other country has done. Yet we must compete in international investment with the nationals of all other countries.

One thing which the Senator from Minnesota did not discuss, but which I should like to refer to, is that much was made in the hearings about the balance of payments. Very elaborate tables were submitted by the Secretary of the Treasury, in which he endeavored to show that there was too long a time lag between oversea private investment and repatriation through earnings, of that investment. I challenge that concept and invite Senators to examine in that regard the rather important and, I think, proper analysis which appears on pages 3891 to 3907 of the record of the hearings. The analysis demonstrates, in my view, the fallacy of the Secretary's arguments on that score. I shall obtain, and offer tomorrow in the debate, precise figures which were developed before the Joint Economic Committee, and which indicate how this gap is rapidly being closed and how advantageous we already begin to see will be the income from overseas to private investments by American investors and Americans who operate through subsidiaries overseas. The gap is closing very rapidly. The increase is quite marked. I shall take great pleasure in presenting those figures to the Senate tomorrow.

Now I shall comment upon the points which I have stated. First, as to com-

petition with foreign operators, it has already been made clear that we are engaged in a profound struggle in the world. We are not alone in the world. We are deeply affected by world affairs, and must have important and material world sources to dispose of our exports. Those exports are made up not only of goods and services which we sell abroad; they are also made up of parts and other equipment which we send to American subsidiaries which manufacture overseas in a very important way.

In addition, we do not wish to be disadvantaged in our competition for export markets, which are very often heavily supplied by foreign subsidiaries producing under favorable conditions. Our exports cannot compete unless we encourage the establishment of subsidiaries and investments abroad. The factor of competition is critically important, both to our world position and to the exporting of our surplus. Also, we must remember that we cannot write the tax bill in such a way as to confound and bedevil our international interest in the expansion of trade abroad, which we shall deal with in another bill which will follow rather rapidly on the heels of this one. Yet, it strikes me that that is precisely what we are doing in this situation.

The second provision drafted by the Committee on Finance is adverse to the new premise, that essentially, at least with one of the escape valves, which is generally considered the major one of the escape valves, is a provision under which the overall foreign company tax paid with respect to U.S. operations "is not substantially below what the U.S. tax would be on the income." This completely disregards the competitive factor which I have described. It completely disregards the higher taxes paid by U.S. citizens for reasons quite apart from income which they earn from the foreign operations or which accrue from foreign operations. That also is really an escape valve only for a corporation which has established a longstanding practice in this regard and is only advantageous to it. It does not serve the needs of small and new firms at all, which will be hit by the principle of taxing corporate earnings to shareholders before distribution, which continues unless the corporation comes under the escape valve.

Mr. CURTIS. Madam President, will the Senator from New York yield?

Mr. JAVITS. I yield.

Mr. CURTIS. Is it not true that the so-called escape valve will lessen the dollar impact on certain taxpayers, but will not eliminate the basic objection to the faulty premise upon which the Treasury has based the whole scheme?

Mr. JAVITS. The Senator is exactly correct; not only the false premise, but the unprecedented premise.

Mr. CURTIS. And the unconstitutional premise.

Mr. JAVITS. That will certainly be argued. I have little doubt that it could be considered as taxing income which is imputed and not received, or even accrued.

Mr. CURTIS. One of the most distinguished legal authorities in the coun-

try, Prof. Adrian A. Kragen, professor of law at Berkeley, Calif., has written an excellent paper on this subject. I believe his conclusions are sound. When I spoke on this subject last Saturday, I placed Professor Kragen's statement in the RECORD, and it appears on page 16536 of the RECORD of August 25, 1962. To say the least, we are inviting controversy and lawsuits by this action, and that will mean tax uncertainty; and uncertainty will destroy plans for going ahead with business. I thank the Senator from New York for yielding.

Mr. JAVITS. I thank the Senator from Nebraska for his very pertinent and wise observations, which are extremely helpful to the total argument.

I should like to deal now with a subject which is perhaps most native to me in terms of my experience in Congress, that is, the basic distinction which is made, or attempted to be made, in the proposed legislation between investments or subsidiaries which operate in developed countries and those which operate in less developed countries.

Let it be clear that the income which we are talking about as it comes from the less developed countries must not only be income which is derived from those countries as a practical matter, but also must be the result of income which comes from a reinvestment in those countries. It must be derived from and reinvested in those countries. I think the distinction here is not only artificial but is also likely to be very damaging, for the reason that the main thrust of our present effort to equalize the situation in terms of exports between ourselves and the European Common Market is today directed toward the investments in these very subsidiaries in the European Common Market countries, which tomorrow will be much more powerful, for I have no doubt that the British and the members of the so-called Outer Seven—the European Trade Association—will become members of it. This proposed tax law loads the situation against the very companies which right now should be encouraged, in order to protect the American position in this way, rather than be discouraged and penalized by it.

Furthermore, we are trying to get the developed countries to share with us the responsibility for foreign aid to the less developed countries; and one of the big ways we can do that is by doing business in the developed countries in a creative way, in the effort to work out those arrangements with businesses in those countries. But this committee amendment would go in exactly the opposite direction, by placing a heavy penalty on that operation. In addition, the committee amendment would prevent the supplying from the developed countries to the less developed countries which these firms will wish to do, because the test would be that the investment must have been attributable to one in a less developed country. Therefore, our whole effort to help in the development of the less developed countries would be thwarted by these tax provisions.

It seems to me this committee amendment is completely inconsistent with the whole basic policy we are adopting with

respect to world economic cooperation, with respect to our trade policy, with respect to our investment policy, with respect to the relationships between American businesses and foreign businesses, and with respect to the competition between American businesses and foreign businesses.

As I developed in the course of my colloquy with the Senator from Minnesota, it will not produce more taxes. On the contrary, I am more and more becoming convinced that it will produce less taxes, whereas the flexibility and the power available under our amendment with respect to the unreasonable accumulation of surplus will give the Collector of Internal Revenue an infinitely greater opportunity to keep up with the developments of business and industry in their legal aspects as they relate to the tax law, and to do so in a more effective way than he could under such a fixed provision of the tax law which would enable keen minds—which always are directed to studying the tax laws—to find new means of evasion and circumvention.

So I think the committee amendment is unwise and violates the definite policy of our country; and I think the amendment of the Senator from Minnesota [Mr. McCARTHY] and myself is infinitely to be preferred. For all these reasons, and also for the pragmatic reasons of producing more taxes for our country and aiding in the giving of encouragement to the less developed countries, I hope the Senate will see the wisdom of our amendment, and will adopt it.

Tomorrow, I shall further buttress the arguments in favor of this amendment, by producing additional material, as submitted in the Joint Economic Committee and elsewhere.

I thank the Senator from Nebraska for his courtesy; and I yield the floor.

Mr. CURTIS. Mr. President, will the Senator from New York yield?

The PRESIDING OFFICER (Mr. Hickey in the chair). Does the Senator from New York yield to the Senator from Nebraska?

Mr. JAVITS. I yield.

Mr. CURTIS. The Senator from New York pointed out that by means of the establishment of foreign subsidiaries, certain exports are fed from this country—for example, parts, replacements, raw materials, and many other things. Is it not true that, in addition, our exports are enhanced, once such a subsidiary is established in another country, by reason of the operation of the subsidiary there and the establishment of its working force and its sales force there?

Mr. JAVITS. The Senator from Nebraska is correct; and that adds to American investments in business, especially those of this character. It must be remembered that tax havens will be as definitely thwarted if the Internal Revenue Service is able to exercise the powers provided by our amendment as they will be if it is able to take advantage of the purely mechanical features of this committee amendment. In other words the catching of the rascals will not be done more effectively by means of the committee amendment.

Mr. CURTIS. As for the catching of the rascals and the so-called escape procedure benefits, such a concern might be able to evade taxes as easily under the committee amendment as under the present provisions of law, might it not?

Mr. JAVITS. Exactly so, whereas our amendment has the added virtue of making it possible for the Collector of Internal Revenue to reach out and to deal with any new schemes.

Mr. CURTIS. Precisely.

Mr. President, section 12 of the pending measure establishes a new and unprecedented method of taxation, by attributing income to a taxpayer based on the profits realized by a foreign corporation of which it is a stockholder. The administration attempts to justify such a course by reference to the Personal Holding Company Act. This is unwarranted, inasmuch as we are dealing with active business enterprises which are in reality owned by millions of our own citizens. There are serious questions as to the constitutionality of such a procedure; and I discussed this question in my remarks on the Senate floor on August 25.

Mr. President, I ask unanimous consent to have printed in the RECORD three brief excerpts from the material I used on Saturday, taken from the brief by Adrian A. Kragen, professor of law, Berkeley, Calif.

There being no objection, the excerpts were ordered to be printed in the RECORD, as follows:

In *Eisner v. Macomber* there was, in my opinion, a clear and unequivocal statement that income of a corporation could not be taxed to the shareholder without a receipt of that income by the shareholder, i.e., that realization in some measure is essential to the definition of income for Federal income tax purposes.

The Treasury over a long period has attacked that concept and has consistently urged the overruling of *Eisner v. Macomber*. Despite such urging the Supreme Court of the United States has never seen fit to overrule the fundamental doctrine enunciated in the case. In fact, even where the Court has distinguished *Eisner v. Macomber*, it has actually impliedly recognized the continuing validity of the definition insofar as realization is concerned. Thus, in *Commissioner v. Glenshaw Glass Co.* (1955) 384 U.S. 426, the Court in distinguishing *Eisner v. Macomber* stated (pp. 430-431):

"The Court was there endeavoring to determine whether the distribution of a corporate stock dividend constituted a realized gain to the shareholder, or changed 'only the form, not the essence,' of his capital investment. Id., at 210. It was held that the taxpayer had 'received nothing out of the company's assets for his separate use and benefit.'"

My examination of the decisions of the Supreme Court of the United States has resulted in my opinion that *Eisner v. Macomber* is still the controlling authority on the issue of the necessity for realization for the purpose of the determination of income under our income tax laws. Therefore, I must conclude that an attempt to tax a shareholder in general on the undistributed profits of the corporation on the theory of accretion is of very dubious constitutionality under article 1, section 2, clause 3, and article 1, section 9, clause 4.

This memorandum indicates at least in my opinion that there are serious doubts as to the validity under the Constitution of

the basic provisions of section 13 of H.R. 10650. The testimony before the House Ways and Means Committee and, I assume, before this committee indicates considerable difference of opinion as to the efficacy of this legislation to meet the problem, if one exists. In other sections of the bill, H.R. 10650 has taken steps to tighten up the tax treatment given to income from foreign sources and to preclude the use of devices to attribute improperly income to foreign sources. The bill also provides for the Treasury request for more extensive reporting requirements with respect to certain foreign corporations. These new weapons in the hands of the Treasury may enable it to meet adequately the problem to which its request is directed without plunging into the doubtful and exceedingly controversial area of the attribution to shareholders of the income of bona fide operating corporations organized under the laws of foreign countries.

Mr. CURTIS. Mr. President, I have also referred to them in the individual views contained in the Report No. 1881 submitted by the Committee on Finance in collaboration with the senior Senator from Kansas, the senior Senator from Utah, the senior Senator from Maryland, and the junior Senator from Kentucky.

I discussed the economic implications involving the taxation of foreign source income in my remarks on the Senate floor on April 17, 19, 25, 27, May 1, 4, 8, and 10. Apparently, many of the objections I raised have had some impact upon the administration, inasmuch as the original proposals recommended by the Secretary of the Treasury in his appearance before the Committee on Finance have been drastically modified. It is of some significance that the version of H.R. 10650 which was passed by the House of Representatives only permitted the deferral of income for a foreign subsidiary if its earnings were reinvested in the same trade or business. This limitation necessarily restricts the opportunities of U.S. firms to take advantage of new technological developments and to integrate both vertically and horizontally so as to maximize their competitive opportunities.

The Secretary of the Treasury, Mr. Dillon, was not too happy with the measure adopted by the other body. In fact, in his appearance before the Committee on Finance on April 2, he urged that the House bill be amended in order to completely eliminate any deferral. He said:

H.R. 10650, as passed by the House of Representatives, apart from tax havens, deals only peripherally with tax deferral for foreign income, another important tax preference now accorded foreign, as compared with domestic, corporate income. It responds to the President's recommendation in this area only insofar as it specifies that the undistributed foreign income of U.S. subsidiaries operating abroad will be subject to U.S. tax as it is earned unless it is reinvested in substantially the same trade or business already conducted by the firm in question, or in a less developed country.

By not treating the tax deferral issue fully and directly, the bill still retains a substantial tax advantage for investment abroad rather than at home. The privilege of deferring U.S. taxes until income is repatriated as dividends should simply be eliminated for our subsidiaries in advanced industrial countries, as the President has requested. (Revenue Act of 1962, hearings before the Com-

mittee on Finance, U.S. Senate, 87th Cong., 2d sess. H.R. 10650, pt. 1, p. 99.)

Mr. President, the many witnesses who appeared before the Committee on Finance clearly showed that deferral was necessary if American firms were to maintain a competitive position in markets abroad. In order to satisfy the administration's demand for a bill that would at least attempt to establish an unconstitutional principle of taxing earnings which have not been constructively received from a foreign subsidiary, new language was adopted in section 12 of the pending bill in the hope that it would satisfy some of the objections so that the President could claim a legislative victory. In essence, section 12 permits complete deferral for those operations that are conducted solely within a single country. Rather than simplifying the already complex language of the bill, a new formula has been added which levies a tax dependent upon the dividends received from foreign subsidiaries and the rate of taxation prevailing in other countries.

In actual practice, Mr. President, this provision will make it extremely difficult for many taxpayers to properly determine their liabilities at the time their returns are filed.

However, the escape valve which was adopted by the Committee on Finance to secure acceptance for section 12 virtually eliminates its effect on those businesses whose activities are conducted entirely within a single country.

On May 11 when Secretary Dillon appeared before the Committee on Finance, I posed the following question:

How does it benefit anybody to require seven foreign corporations when one would be more efficient? (Revenue Act of 1962, hearings before the Committee on Finance, U.S. Senate, 87th Cong. 2d sess., H.R. 10650, pt. 10, p. 4319.)

Secretary Dillon replied that he had no intention of requiring the establishment of seven corporations. He conceded that one would be more efficient, but that the U.S. parent should then pay a tax merely because it had chosen to operate in a more efficient manner and hence be in a better position to meet competition.

Mr. President, the position of the administration in connection with our foreign economic policy is contradictory, and we are apparently working at cross purposes. On the one hand, the administration suggests an isolationist tax policy which it wishes to combine with an internationalist trade expansion program. The emergence of the European Economic Community is one of the most important developments in our era. Our Government played a significant role in urging its formation, and we are now suggesting that countries in other parts of the world should also disregard national boundaries insofar as trade and economic matters are concerned. From the standpoint of strengthening the economic potential of the free world, the European Economic Community is an important development, and the Congress can welcome the added strength which this new economic block of nations provide.

My studies of this legislation have convinced me that the investment of U.S. capital overseas promotes exports and creates additional jobs in the United States. I would have no interest in any proposal that could deprive an American worker of gainful employment or destroy the investments of our citizens in enterprises located within our own borders. However, measures to protect American workers are not the pending business before the Senate. When the Trade Expansion Act is reported, we should assure that the Congress retain adequate powers so that American jobs are not destroyed. If the economic potential of the European Economic Community, which may ultimately include the nations that are now in the European Free Trade Association—namely, Austria, Denmark, Norway, Portugal, Sweden, Switzerland, and the United Kingdom—is fully developed, it would certainly be unfair to require that a U.S. firm must establish a separate operation in every one of these countries so as to avoid the punitive effects of section 12. It is not an accident that many U.S. firms have chosen Switzerland as their base for European operations. It provides banking and commercial facilities that are unrivaled by any other European country. It is centrally located and readily accessible. However, if the base of all European operations had been located within any one of the countries in the European Economic Community, the provisions of this bill would be just as onerous. It should be remembered that two of the largest international firms are the Shell Oil group and the Unilever group, which operate under the British Overseas Trading Corporation Act as well as a similar law enacted in the Netherlands. In each instance, tax deferral on foreign operations is permitted. U.S. subsidiaries could avail themselves of similar privileges in either the United Kingdom or the Netherlands, rather than establishing base companies in Switzerland, if section 12 of the pending measure is not adopted by the Senate. It is ironic that on June 20, the Under Secretary of the Treasury, the Honorable Henry H. Fowler, in an address before a regional conference of the Commerce Department at Atlanta, Ga., said:

This need to expand our export trade is the basic reason behind President Kennedy's trade program. The fantastic growth of Western Europe in the last decade has created vast new markets for just the kind of goods that our own manufacturers are so skilled and experienced in producing. New cars, new highways, new shopping centers, new suburban developments—all these are characteristic of the rapidly expanding European scene. As the Common Market takes in new members, and as this self-stimulating growth continues, these markets will grow also.

It is essential for the maintenance of U.S. export trade that we have a part in this future. If we fail to maintain our access to European markets at this critical time when new trade patterns are being evolved, when new customers are forming preferences, we may find ourselves at some later date unable to regain that access, no matter what concessions we may be prepared to offer, because the pattern may have been set without us. This goes much deeper, of course, than customer preferences. It encompasses

the whole range of business relationships, both here and abroad. Firms will be either geared to deal with the United States, or not. Furthermore, the more we allow this new pattern to be set without us, the more difficulty we will have in dealing with a Europe whose own special interests will have become accustomed to a Europe-oriented market, and which may look upon exports from the United States as a disturbing and threatening influence.

Mr. President, the views stated by Secretary Fowler explain the need for U.S. direct investment, as we cannot develop these markets without intimate contact with our customers. Products must be designed and produced to meet their particular preferences. As Secretary Fowler so clearly stated, if we fail to maintain our access to these markets at this critical time, no matter what we may attempt later will prove of little value. Rather than seeking to attribute the growth in our investments in Western Europe to tax inducements, it should be recognized that many firms have sought to secure a position within the European Economic Community which will ultimately have immeasurable benefit for the American economy. Their activities will provide more jobs that will expand exports, that will promote economic growth, and ultimately will make a substantial contribution to our balance-of-payments position.

Mr. President, the enactment of section 12 cannot produce any significant revenue, but it may force some firms to ultimately readjust their corporate structures, and if need be, establish subsidiaries within each of the principal countries of the Common Market. However, this will weaken their competitive position, since there is no evidence that any other developed country intends to handicap its own producers by the enactment of legislation that cannot promote the true interests of its citizens.

The July 6 issue of Life magazine contains an interesting exchange of correspondence between Mr. David Rockefeller, the chairman of the board of the Chase Manhattan Bank, and President Kennedy. Mr. Rockefeller's letter was written at the express request of the President. In discussing the balance-of-payments problem, Mr. Rockefeller said:

The hard truth is, Mr. President, that the only way to achieve a solid solution to our balance-of-payments problem, one which is consistent with the key role of the dollar in international monetary affairs, is through time-honored methods—through an expansion of exports, an appropriate level of interest rates, and through maintaining confidence (both here and abroad) in the soundness and integrity of the dollar. Moreover, every aspect of the balance of payments cannot help but be influenced profoundly by the basic health of the American economy.

President Kennedy's reply continued to refer to the need to deter direct investment abroad. In the President's message to the American people on August 13, he again referred to these objectives. He said:

We need to enlarge our export markets through the trade expansion bill so that we can sell abroad, so that we can get into the great Common Market which is being built up, so that we won't have our money

going abroad to invest in plants overseas, but invest here in this country.

By lightening tax burdens, as the Common Market countries have done so successfully, and they have full employment and an economic growth rate twice ours, it will improve the competitive position of American business, encourage investment at home instead of abroad and improve our balance of payments.

Mr. President, certainly all of us wish to encourage investments in this country and to promote economic growth, but I find it difficult to accept the premise that investments abroad in any way impede the normal development and growth of our own economy. In fact, in the statements which I have previously made on the floor, I have clearly shown that such investments are complementary, and not competitive with our own efforts. It is a great disservice to promote the reduction of tariff barriers on one hand and at the same time impose additional penalties on those firms which seek to penetrate new and growing markets for American products. Mr. Fowler in his address in Atlanta, Ga., to which I have already referred also said:

I might also add, in a similar vein, that U.S. business operating abroad should not neglect to fully explore possibilities for procuring their supplies, equipment, and services from American sources on an economical basis.

All the testimony before the Committee on Finance and previously before the Committee on Ways and Means has shown that the establishment of direct investment by our citizens abroad provides a ready market for supplies, equipment, and services from American sources.

Should the Senate enact the provisions suggested by the administration as embodied in section 12 of this bill, there would be less opportunity for U.S. businessmen to follow Secretary Fowler's advice. It is precisely to encourage the opportunities to use American source materials and talent that U.S. firms have established foreign operations.

In this same address, Secretary Fowler made another significant proposal. He said:

American firms might also explore and seek out more fully opportunities for borrowing abroad, especially in support of the operations of their own foreign branches and subsidiaries, instead of relying as heavily as they do on the easy alternative of seeking funds from familiar American sources.

Again, Mr. President, this is precisely the course which has been followed by many U.S. firms with foreign operations. For example, the annual report of the General Motors Corp., for the year 1961 shows that a total of \$144 million of debt has been contracted by foreign subsidiaries which will be due during the period 1963 through 1977.

A large portion of these funds were secured from foreign sources. Insofar as the capital base is broadened by the use of funds borrowed locally, the ultimate profits to be remitted to U.S. equity shareholders are increased, and of course, the U.S. Treasury receives its share of such profits based on a 52-per-

cent tax less the applicable foreign tax credit.

Regardless of escape valves, section 12 represents a complete departure from the concepts which have governed our income tax laws since 1913. No less an authority than the Assistant Secretary of the Treasury, Mr. Stanley S. Surrey, unequivocally supported the concept to tax deferral in the statement he presented to the Committee on Ways and Means on July 8, 1959, in its consideration of H.R. 5, 86th Congress.

Mr. President, I ask unanimous consent that the justification for both the foreign tax credit and tax deferral in terms of tax equality and the recognition of the claims of foreign countries may be printed at this point in the RECORD.

There being no objection, the justification was ordered to be printed in the RECORD, as follows:

THE BASIC PERSPECTIVE—PRESENT U.S. TAX TREATMENT OF FOREIGN INCOME

A few words regarding the present U.S. tax treatment of foreign income are in order, since it forms the perspective necessary to a consideration of current issues and proposals. This treatment may be summarized as follows:

1. Basic standard of tax equality: The basic standard under our income tax, to be followed as far as possible, is the necessity of maintaining equality among American taxpayers whereby taxpayers with equal amounts of income pay the same tax. To the extent that this standard is seriously breached, so that preferences and favoritism replace equality, the income tax deteriorates as an effective fiscal instrument.

2. Jurisdiction based on residence and nationality: As respects foreign income, observance of this basic standard requires that the foreign income of U.S. taxpayers be taxed as well as their domestic income. Accordingly, our jurisdictional basis for taxation must go beyond geographical jurisdiction and rest also on residence and nationality. In this we are not unique, for other mature income tax systems also stress both source, jurisdiction, and residence.

3. Foreign tax credit accommodation to foreign source jurisdiction: While residence and nationality, including domestic incorporation, thus support income taxation, recognition must be paid to the fact that we live in one world and that the foreign income of our citizens and corporations may therefore be subject to taxation at the foreign source. The *modus vivendi* for that recognition under our system is the foreign tax credit mechanism. Under this credit, a foreign income tax paid is treated as payment to the extent of the U.S. tax on the foreign income, so that only a tax representing the difference between the foreign tax rate and the U.S. tax rate must be paid to our Treasury Department. It is this foreign tax credit which accommodates our need to stress nationality jurisdiction, so as to achieve the objective of equality among our citizens and corporations, with the need of foreign countries to stress source jurisdiction if they are to protect their revenue structures. The accommodation permits the foreign country of source to obtain revenue and also permits the United States to maintain the standard of equality at home since the taxpayer's tax burden is still at our domestic level (unless the foreign rate is higher than our rate). This accommodation is possible because of the revenue yielded by our Treasury Department to the extent of the credit granted. It is this foreign tax credit mechanism therefore which makes international trade and investment possible under our income tax system, and that of other mature income tax

systems as well which stress equality of tax burden. While the credit mechanism is complicated, it is thus absolutely vital to our tax system.

4. Tax deferral accommodation to foreign source jurisdiction: A second accommodation to international activity is represented by our grant of deferral of taxation on foreign source income until that income is returned to the United States. The mechanism of deferral is the recognition accorded to foreign incorporation. Under this mechanism, foreign subsidiaries of American corporations are treated as separate entities and thus essentially outside the reach of the U.S. tax system. The income of these foreign subsidiaries is thus free of U.S. tax until paid out as a dividend to the parent, or distributed in liquidation.

The above two accommodations—the foreign tax credit mechanism and the foreign subsidiary tax deferral mechanism—have supporting justifications which are readily understood and which are capable of rational support. (Statement by Stanley S. Surrey, Foreign Investment Incentive Act, hearings before the Committee on Ways and Means, House of Representatives, 86th Cong., 1st sess., H.R. 5, pp. 535-537.)

Mr. CURTIS. Our Government must adopt a consistent policy in keeping with our position of world leadership. We cannot encourage foreign investment at one time and deter it later when it suits the whim of a new administration.

If we are to maintain our position of financial and commercial leadership in the Western World, we must abandon isolationist economic policies. This does not mean that we should not provide adequate protection for those domestic industries which are essential to our economy, but this historically has been accomplished by tariffs rather than by deterring investment. We can achieve a higher rate of economic growth, create more new jobs, and improve our balance of payments position by abandoning any attempt to hamper U.S. firms in their competitive efforts in world markets. After all, the United States has no power to unilaterally alter the climate in other countries, and our competitors abroad will be the true beneficiaries of the enactment of punitive taxes on foreign source income of American citizens.

Taxes are a necessary cost of doing business, and our Congress should not impose a burden on the activities of corporate entities established in other countries which happen to be controlled by U.S. nationals that their competitors do not bear. If we pursue such a course in due time, our balance of payments will deteriorate, and we will lose our position of world leadership. In the individual views which I submitted with a number of my colleagues, we referred to the fact that President Chiari of Panama had advised President Kennedy that the administration's tax proposals represent "undue interference in the internal affairs of Panama." He also stressed that these measure are "almost equivalent to economic aggression."

The New York Journal of Commerce in its issue of June 12 commented on the fact that the Swiss had also become concerned at the repeated characterization of their country as a tax haven by the U.S. Government. In this instance, they instituted retaliatory measures by holding back work permits for American

executives. Without a work permit, no visa can be issued, and already some U.S. companies reportedly have had to change their operating plans because they were not able to locate their executives in Switzerland.

Those of us who believe in a free economy, which is responsive to the laws of supply and demand and open competition in free markets abhor government policies which attempt to dictate the decisions of management by indirect methods such as are found in section 12 of the pending bill.

Our balance-of-payments problem is one for continuing concern, but it cannot be corrected by temporizing with remedial measures that fail to meet the true problem.

Federal expenditures currently represent more than 20 percent of the national income. In addition, taxpayers must support State and local governments. They supply many of the essential services which under our system of decentralized governmental responsibility are extremely important, and they should continue to do so. However, the total cost of government—Federal, State, and local—must be factored into the prices of all the goods and services which we sell. If the Congress would concentrate on reducing the cost of Government, it would make a direct contribution to price reductions that would automatically increase our exports and improve our balance-of-payments position.

It is impossible to accomplish the objectives sought by the administration through punitive taxation on foreign investment. Such action will merely result in the loss of opportunities for our citizens in the new expanding economic markets to which Mr. Fowler referred.

Mr. President, it is my considered judgment that section 12 is unconstitutional in that it ignores corporate entities. Its enactment would provide the basis for new concepts of taxation in domestic matters. In the long run, the enactment of this provision will harm our balance-of-payments position. It will destroy American jobs and reduce our exports.

Mr. President, it should be rejected by the Senate as it is unsound and unworkable.

The amendment offered by the distinguished Senator from Minnesota and the distinguished Senator from New York is much preferable. I shall support it.

It may erroneously be argued by some persons that to support the McCarthy amendment would jeopardize the position of the Senate in the conference because it might be conceded that the version of the Senate Committee on Finance as represented by the Kerr amendment was better than the bill as reported by the House. I wish to point out that if the McCarthy amendment is adopted and the bill goes to conference, it will still be possible for the conferees to accept the McCarthy amendment, or to accept the House version, either one with an amendment, in which case the Kerr amendments would be in order.

I do not believe the argument as to procedure should cause the Senate to refuse to take the best possible course. I believe that would be done by the adoption of the McCarthy amendment.

Mr. President, I make the point of no quorum.

The PRESIDING OFFICER. The clerk will call the roll.

The legislative clerk proceeded to call the roll.

Mr. KERR. Mr. President, I ask unanimous consent that the order for the quorum call be rescinded.

The PRESIDING OFFICER. Without objection, it is so ordered.

Mr. HARTKE. Mr. President, yesterday action was taken in the Senate on the question of whether or not the U.S. Government should withhold taxes on earnings from dividends and interest. Consistently during the time the bill was before the Finance Committee, I was one of the small group who voted in favor of providing tax equality and equity of treatment for the people who are paying their taxes, and to have the people who earn their living by wages or salaries treated the same as people who earn their living by clipping coupons or who obtain their method of livelihood from dividends or interest. Only four other Senators on the Finance Committee shared this opinion.

I was rather surprised, because, frankly, this was the only part of the tax bill which did not change the tax law. It changed the tax procedure, but it had absolutely nothing whatsoever to do with the tax law. The procedural method really meant that there would be a new method of acquiring for the Treasury some of the taxes which were, either intentionally or unintentionally, not being paid.

I have always felt that there has been a consistent and glaring inequity arising from the treatment of wage earners, or persons who earn their living by obtaining salaries or wages in factories or other kinds of similar work, as compared to those persons who obtain their livelihood by living off what they have, or what they have acquired in the past, or through inheritance, savings, or other means.

Equal treatment under the tax laws should be the aim of every Senator. I hoped, and believed, this would be true. I suppose those who thought otherwise felt that perhaps there might be an additional imposition of burden on some persons, but certainly the burden placed on wage earners has not been as light as it has been on those who clip coupons. The expenses of operating the Government are the responsibility of all. The expenses should be borne by all. They should be shared equally and fairly, according to the laws which we write. The debt which we have incurred, principally because of the war—but, for whatever reason—is a bona fide debt of the United States, representing the difference between what has been paid in taxes in the past and what we have not been able to receive by way of taxes. The difference between the two represents the debt. It is a bona fide debt which is owed by all,

and everybody should pay his fair share under the law.

This was what we were attempting to do when we tried to provide for withholding of taxes on dividends and interest in the provision which was presented by the House, and which failed in the Senate Finance Committee, and then failed here on the floor yesterday.

I still think we could take a giant step forward, because most of the opposition which arose to this particular portion of the bill came from the element of the people who had accumulated savings and who had deposited funds into savings and loan institutions or into banks. In other words, basically the opposition was that it was said that a burden would be placed upon those institutions which were providing services for people, by taking their savings as accumulated through the years, namely, the banks which had taken those amounts and were paying interest.

With respect to the people who received income from dividends on stocks or interest on bonds, there was not much talk. That is a different segment of the people. I had occasion to talk with some of the business people who are basically involved in the field of those individuals who own bonds. I asked them how much of an additional burden it would be on them if they were required to withhold the taxes on the dividends they paid or to withhold the interest on the bonds. They explained to me that for all practical purposes the machinery was already set up for the individual corporations, for the purpose of computing all these items, and that there would be no great difficulty in that regard.

I went to the Treasury Department and asked, in view of the action taken on the floor of the Senate yesterday, which confirmed the previous action taken by the Finance Committee, whether the Treasury would be in favor of attempting to hold on to a part of what I thought was a worthwhile principle, to take another giant step forward by providing for the withholding of taxes on dividends from stocks and on interest on bonds.

Therefore, when the occasion arises and I have the opportunity to present the amendment to the Senate—hopefully tomorrow—I shall call up the amendment at the desk. The amendment in effect would say to the Senate again, "If you want to balance out this tax bill by including in it an amount of from \$350 to \$400 million, which would more than offset the loss of revenue which would be occasioned under the bill, this is the way to do it." This would give Senators an opportunity again to vote on this proposal.

This is the first of a series of six amendments which I plan to offer. I have been told that there is not much chance that the Senate will pass such an amendment. Frankly, I shall wait to see, and find out, as a result of action by the Senate.

In line with this proposal, I feel, as I have always felt—I am not a newcomer to this particular principle—that the wage earners should be treated exactly

the same as the coupon clippers. The wage earners, in respect to the matter of taxation, ever since the bill was passed in 1942, have had their taxes withheld.

Under the social security laws, we see that the same discrepancy appears in respect to the treatment of people. The social security law, enacted for the benefit of individuals, provided for them a method of taking care of themselves in their older years. However, the law also provided a method whereby the people, in a way, are kept from attempting to provide for themselves. The law forces retirement upon them or else forces a condition upon them.

In the previous Congress I offered an amendment which in some ways would have relaxed that provision. It had a basic purpose. If a person has been a wage earner and if he received social security benefits, under the old law—the law in existence when I came to the Senate—he could not earn more than \$1,200 a year, or more than \$100 a month, unless he was willing to forfeit some of his social security benefits. However, if an individual received income from interest or from rents, or was clipping coupons from bonds, or receiving dividends on stock, he could earn any amount, an unlimited amount, and still draw his social security payments.

This disparity again demonstrates the fact that there are two sets of rules and two different standards for people, depending upon their status in life.

During the previous Congress I was able to obtain the passage of an amendment which increased the amount a person could earn under the social security law to \$1,500, and which provided that 50 percent of the amount between the \$1,200 and the \$1,500 should not be included in the computation of earnings.

Again, in the Finance Committee I was able this last year to secure an additional increase of the amount to \$1,750, with the result that a person can earn up to \$1,200 and still receive his social security payments, and, if the person should earn up to \$1,750, the difference between the \$1,200 and the \$1,750, or \$550, would be considered income only to the extent of 50 percent.

Frankly, I think the entire amount should be eliminated from consideration. I think the wage earner should be treated in the same fashion as the coupon clipper, as I have said.

This would be a tremendous step forward. I know it will be opposed, because of the effect it would have upon the social security fund.

As I previously indicated, I did not come to this conclusion only lately. In a few minutes I shall indicate that possibly not every Senator who now believes in this system was of such conviction not so long ago.

In respect to elderly people, I propose to offer a different amendment. For the sake of the record, the withholding on dividends from stocks and interest on bonds is an amendment which is now printed and is at the desk. The amendment about which I have just spoken, on the question of the earning limitations under social security, was an

amendment to H.R. 12580 which I offered June 29, 1960.

I state this for the sake of making sure that people do not believe these are things I thought up last night or dreamed about in an election year.

S. 3249 is another bill which I introduced in the Senate and which I propose to attempt to have apply to the pending tax bill. This proposal calls for the elimination of the capital gains tax on the sale of a residence by a person who is over the age of 62. We know that as people go through life their status changes. Some individuals have large families, which grow older, and the younger members of the family move away and establish homes of their own, and frequently the older people are left with a much larger residence than the housewife prefers to take care of.

This proposal in substance would eliminate from the present capital gains tax any tax whatsoever on a person over the age of 62 if he should sell his residence—strictly his residence. To enforce that provision there would be a requirement that the person would have to live in his home at least 5 years prior to the time of sale.

The tax on such sales creates quite a hardship even today, for the people who have to pay the capital gains tax, because in many cases the people who are selling the properties have raised large families and are living upon their savings, in the latter part of their lives, or upon social security benefits.

As I shall indicate in a few minutes, some people have only lately come to the conclusion that this happens to be a good proposal.

S. 602 is another bill I introduced, which I propose to call up as an amendment. When the bill was introduced by me in the Senate, I hoped there would be complete hearings. We had some indication on an education bill that there might be hearings in this session. Unfortunately that seems to have passed by. The hearings were not held.

I am not complaining about that, because I know that much important legislation has been considered during the session, and there have been a lot of hearings.

Many people today worry about education expense and activities with respect to sending children to school or to college. We have learned of many cases of individuals who have provided for themselves while going to college.

Contrary to the time when I went to school, the truth is that today many college students are married. In some cases they are attempting to provide for one another, as they provide funds for themselves to go through college. At the same time, we know of many parents who are struggling to send their children through school.

I feel it would be only fair to give an allowance to those people, since we did not pass a scholarship aid bill, of which I fully approve. I feel that we should allow an additional exemption of \$600 for any individual who is a full-time student in school. I would propose that that exemption apply to the student himself, or to a spouse, or to a taxpayer who

is the father or the parent of a student attending school. I propose that there be allowed an additional exemption of \$600 while the student is a full-time student in a college or university.

Another amendment which I intend to call up is an item about which I spoke when I had occasion to be with my delightful, intelligent and wonderful colleagues on the other side of the aisle, the chairman of the Republican Central Campaign Committee. I hope that I can obtain from him the same support on the measure on the floor of the Senate. At that time I indicated that I thought the broad base of political expenditure should be borne by more people. We ought to encourage individuals of all sorts, ranks, and income to participate in the elections, not only financially, but also with their votes. But in order to help them participate financially, I have submitted my proposal.

We find many such people feel that they have the burden of caring for their own lives. They do not feel that they can contribute to a political campaign. We have long recognized that contributions to charitable organizations and many items of that sort are legitimate deductions for income tax purposes. I talked with representatives of the Treasury Department about this subject. I have the assurance that the Treasury Department is not opposed to the provision and, frankly, looks upon it sympathetically. They would welcome it as a part of the tax bill.

My amendment would permit any individual who made a political contribution to the party committee of his choice or to an individual candidate of his choice in any general or special election to deduct up to 50 percent of his contribution, with a tax credit up to an amount not exceeding \$10. Those filing joint returns would be entitled to a tax credit up to \$20.

In other words, an individual who might contribute \$15 to a political campaign would be entitled to receive \$7.50 as a tax credit. A person who contributed \$20 would be entitled to receive a tax credit of \$10. If a husband and wife wished to contribute \$40, between them they could deduct \$20.

The final amendment which I intend to call up is commonly referred to as H.R. 10. I introduced a separate bill under the title of S. 197. Again I wish to indicate that I am not a Johnny-come-lately to that proposed litigation. I supported it in the Senate Finance Committee. At the time I introduced the measure, on January 6, 1961, it was one of the first bills introduced in the Congress. At the same time I introduced the bill, the gentleman from New York, Representative EUGENE KEOGH, introduced a bill on the same subject on the House side. In fact, they were companion bills introduced on the same day.

S. 197 is a bill which would provide pensions for self-employed people. The bill was reported to the Senate. It has been passed by the House. The bill has been passed in modified form by the Senate Finance Committee and is now

on the Senate Calendar. I had hoped that the leadership would find it within their means to call up the measure for action before this. It has not been done.

The estimated cost of the proposed program is about \$180 million.

I wish the Senate to know that if we should pass the tax bill with all the amendments which I have submitted, the result would be a surplus so far as the Treasury is concerned. So I do not feel that anyone could ever say that I am in favor of budget "busting." I believe in a balanced budget. That is exactly what the bills would do. Some have come forward and talked about budget "busting" on one hand while they made no attempt to provide income on the other hand. I was very interested that one of our late converts was the distinguished minority leader, the Senator from Illinois [Mr. DIRKSEN]. He indicated a few days ago that he had six amendments that he intended to offer. The last program which I talked about was the so-called H.R. 10 or my bill S. 197. I do not know why the Senator suddenly has become so interested in that program. I did not notice that he urged passage of the bill or its being called up for consideration. He was within his right not to do so. He certainly has a right to take up measures if and when he pleases, or, at his pleasure, not to do so at all.

Another one of the items upon which I hope I can have the support of the Senator from Illinois is the matter of political contributions, inasmuch as the designated leader of his campaign committee this year is the distinguished Senator from Arizona [Mr. GOLDWATER], who has indicated publicly that he thought it was a fine plan and he would be interested in joining with us.

The other item to which the minority leader seems to have been lately converted—at least, I share with him the feeling that it is a good bill and I welcome him to join me in support of the measure—is the bill (S. 3249), which would eliminate the capital gains tax on the sale of a residence by the elderly. A big difference is that the Senator suggested a change in his amendment. He would change the age from 62 to 60. I would not be inclined to quibble about that. We might split the difference at 61, if the Senator so desired. If he feels that 60 years is a proper age and has become convinced of the propriety of such action, it would be wonderful. I do not question his sincerity in any regard whatsoever, in view of his late conversion of those programs. I know it is an election year. But I feel that it is sometimes interesting to compare what happens in election years and what happens in other years.

I call attention to the proposal to increase the earnings limitation to \$1,800, which is the subject of an amendment which I submitted back on June 29, 1960, which I followed through in the last session in the Finance Committee, and which I indicated has been considered in both the Finance Committee and on the floor of the Senate.

On June 26, 1961, when the same substantive question was before the Senate,

I asked for a yea-and-nay vote on the amendment which I had submitted, and it is recorded on page 10515 of the RECORD of June 26. I notice that in the yea-and-nay vote No. 83 the distinguished minority leader found himself not in a position to support that principle.

I am looking forward with great interest and hope to an explanation of the change of heart. I hope that the Senator will be able to convince the many Republicans who joined him at that time, and that he will be able to exert his influence to have them join with those of us on the Democratic side who voted to help people who make their earnings from wages or salaries.

I wanted to point that matter out to the Senate so that we may avoid being caught in the hurry and scurry of all the motions that come during debate, and may be able to devote our time to the substantive issues of the amendments, and obtain a result which will be beneficial to the people in our country who need to be considered.

I think it is very important for us to remember that all people, whether they make their living from wages, salaries, or, if they are more fortunate, from stocks and bonds, should be treated alike.

I think it is important for us to be consistent in our concern for those who are drawing social security benefits in the so-called golden years of their lives, and to be concerned about individuals who are attempting to better their education and those who are interested in attempting to make a real contribution to the worthwhile political life and future of America. I am looking forward to what tomorrow may bring. I thank the Senate.

Mr. MILLER. Mr. President, I wish to say a few words in support of the amendment offered by the distinguished Senator from Minnesota [Mr. McCARTHY], which I intend to support. I make this statement with the realization that there may be a few difficulties which I will have with the amendment, and which I hope may be clarified during the course of discussion with the Senator from Minnesota. Nevertheless, the adoption of the amendment would go a long way toward relieving most of the difficulties I have with the bill with respect to its proposed taxation of foreign income.

Then Senate bill contains significant changes in the foreign income provisions of the bill as passed by the House. These changes are helpful in limiting the scope of the bill and in eliminating or ameliorating some of the technical and administrative problems and some of its unduly harsh effects. I recognize that much commendable work has gone into these revisions in a conscientious effort to improve the bill. I therefore regret that I am compelled to express the view that, even as revised, the bill does not effectively distinguish between such tax avoidance devices and legitimate business operations conducted outside the United States and, further, that the foreign income provisions are unworkable, are unduly penal in their impact on the foreign business of U.S. persons, and would have many consequences that

are clearly adverse to the interests of the United States.

As in the case of the House bill, merely reading the new draft will suffice to demonstrate its utter complexity. Even the most sophisticated become lost in the forest of its technicalities: its phraseology is vague at critical points; precedents for its construction and application are lacking because of the novelty of its concepts; and it seeks to resolve vital and difficult problems by the expedient of delegating authority to issue regulations. Moreover, it still requires that U.S. shareholders obtain from abroad detailed historical and current information which must be prepared according to American accounting and tax concepts unknown to foreign accountants. I seriously question whether a law of such complexity could be applied and administered in an effective and reasonably evenhanded way.

The provisions are still unduly harsh in many respects in imposing burdens of taxation and compliance much more extensive than in the case of domestic operations, particularly as they affect individual shareholders of foreign corporations. Although section 15, dealing with gain on sale of stock or liquidation of controlled foreign corporations, would limit the taxes payable by individual shareholders on the gain, no limitation of any kind has been placed upon current taxation of income to individual shareholders under section 12. Further, no provision has yet been made to permit adjustment of or exemption for legitimate business arrangements established in reliance upon existing law, particularly with respect to present contractual commitments or indebtedness abroad which could not be met if heavy new taxes are to be imposed.

The provisions as amended still have numerous consequences that seem clearly undesirable. They impose upon U.S. persons doing business abroad burdens which their vigorous foreign competitors do not bear. This is especially true because the bill, like the House bill, taxes profits from certain foreign transactions considered to lead to possible reduction in foreign income taxes, though the transactions do not themselves involve U.S. taxes or taxpayers. Under present economic conditions, it seems unwise indeed to shackle American business with a complex scheme of new taxes which cannot be imposed by Congress upon our foreign competitors and which in effect protects not the U.S. tax system but the tax systems of the countries of our competitors.

WORKABILITY OF THE BILL

I do not believe that the provisions of the bill are workable, even though they represent an appreciable improvement over the bill as passed by the House. The basic approach of bill section 12 seems inherently so complex that amendments which leave intact its fundamentals will not suffice.

Foreign business operations are necessarily complicated because of the wide variations in foreign statutes and administrative controls; in foreign methods of business organization, marketing, financing, and accounting; and in treaties

among foreign countries and with the United States. Consequently, any approach to the problem of imposing taxes currently upon the income of foreign corporations from active foreign businesses necessarily presents many complications. Yet, in lieu of a clear and simple policy that might be superimposed upon this involved business and legal background, the bill adopts a multiplicity of difficult new tax concepts and techniques.

The bill, in effect, disregards the separate entity of foreign corporations for certain purposes. In taxing shareholders of foreign corporations on undistributed income of active businesses, the bill adopts techniques that present a variety of difficult problems for which there is no meaningful precedent. These techniques include—

First. Taxing U.S. shareholders of a foreign corporation as if they had received distributions of certain items of its gross income—reduced by allocable deductions—that are not in excess of earnings, without regard to whether or when the corporation pays dividends.

Second. "Hopscotching," which in the case of a chain of foreign entities involves taxing U.S. shareholders of the parent foreign corporation as if they were owners of shares in each of the corporations further removed in the chain.

Third. Exempting from tax such shareholders—or certain identified successors—with respect to subsequent distributions of earnings previously taxed under the above concepts.

In addition to the difficulties inherent in computing the amount of income or earnings of a corporation that is not itself a U.S. taxpayer, the problems necessarily raised by the techniques used in the bill include, among others: determining stockholders' shares of undistributed income where there are different classes of stocks with different dividend rates and preferences—a problem which, I might add, I find present in the pending amendment—resolving inconsistent determinations made by revenue agents or courts with respect to the same corporation in cases involving different shareholders; allowing for offsetting losses of the same or affiliated foreign corporations; limiting the impact of the tax burden on shareholders who are individuals; and adjusting the treatment of subsequent distributions to account for previously taxed undistributed income. The adjustments for previously taxed undistributed income include a variety of difficulties incident to "hopscotching," changes in stock ownership, and the computation of foreign tax credits. The foreign tax credit problems are further complicated by the payment of foreign taxes withheld at the source when there is an actual distribution of earnings that had previously been taxed to U.S. shareholders.

The bill multiplies the problem of taxing undistributed income by its dependence upon many new and involved classifications of gross income, and separate allocations to each such class of expenses, losses of the same or affiliated foreign corporations, other deductions,

and foreign income taxes. With respect to all of these calculations, each U.S. shareholder having a 10-percent stock interest would be entitled to be heard separately.

In addition to the complications necessarily resulting from the involved concepts and techniques of the bill, the difficulties in understanding and applying the bill are increased by the fact that most of the many terms used would be entirely new to the tax law and are to a very large extent vague.

Some idea of the complexity of the provisions of the bill can be obtained by simply noting the number and nature of the entirely new terms that would be added to the Internal Revenue Code by bill section 12 alone, even after the significant improvements of the committee amendments.

In addition, there are numerous definitions and formulas in bill section 12 that are related to the new terms. Many of these involve imprecise words such as "substantial part," "the effect of substantial reduction," "substantially similar to," and "similar property right." It requires no oracle to predict that if enacted a principal effect of the bill would be costly administrative controversy and litigation for years to come.

Indeed, I suggest that if these foreign income provisions of the bill become law, the first qualification for any new applicant for a position as an Internal Revenue agent with the Treasury Department will be that he be a genius.

Many major questions as to doubtful technical soundness, inequitable application, and administrative unworkability lie below the surface of the bill. As suggested by the foregoing discussion, the bill involves an extraordinary number of difficult problems of interpretation. In addition to the general authority that the Treasury has to issue interpretive regulations, section 12 alone contains 16 express grants of authority to the Secretary or his delegate to develop the substantive rules by regulations. Yet even this extensive delegation of rulemaking power leaves important substantive problems that are not covered by either statutory rules or express delegation of administrative authority.

Such broad delegation by Congress of the power to develop substantive rules of taxation raises serious difficulties quite apart from the general question of legislative policy. Where legislative draftsmen have been unable to produce guiding principles that are clear, technically satisfactory, and administratively workable, it should not be assumed that even the ablest draftsmen of regulations can solve the myriad of problems in presently unexplored areas.

An important question also arises as to when taxpayers will be given some idea of the nature of the law that, beginning in 1963, would govern their operations. In a number of important areas final regulations have not yet been issued with respect to the Internal Revenue Code adopted by Congress nearly 8 years ago. A statute with material gaps in its terms that is to be filled in by administrative action after its ef-

fective date may be just as inequitably retroactive as if the introduction and enactment of the bill itself had occurred on the date of such administrative action. And, of course, no matter how relevant to a meaningful discussion of the bill, it is impossible to discuss here the propriety and effect of these presently nonexistent regulations.

Among the broadest delegation provisions of the bill the provision for the determination of earnings and profits, which controls the amount of income subject to tax, "according to rules substantially similar to those applicable to domestic corporations, under regulations prescribed by the Secretary or his delegate."

This also is one of the difficulties I have with the pending amendment; but, as I have stated, the pending amendment goes a long way toward relieving most of the problems which are inherent in the present section 12.

These rules would have to correlate subpart F with most of the other provisions of the Internal Revenue Code in the context of the special techniques for taxing to various shareholders foreign adjusted gross income whether or not distributed. This correlation involves many difficult problems, including questions of inconsistent positions of shareholders, determining the persons who have the power to make (and the timing and procedures for making) essential tax elections, and further related questions that arise upon transfers of stock to or from either a foreign shareholder or another U.S. shareholder.

The committee amendments leave many important technical problems unsolved, and in a number of instances create new technical difficulties.

As an illustration of the difficulties in resolving the complications of the bill, it may be noted that the following problems relating to bill sections 12 and 15, have either not been dealt with at all in the bill, or have not adequately been resolved:

Determination of shareholders and attribution of ownership.

Determination of subpart F income.

Determination of earnings and profits.

Determination of amount of investment in property.

Necessity of maintaining separate accounts for different shares and shareholders.

Lack of adequate consolidation of income and loss among corporations and years.

Inappropriate treatment of intercompany transactions.

Taxation of deemed distribution as ordinary income but deduction of losses only on disposition and then as capital losses.

Inadequate correlation of section 12 with foreign personal holding company provisions and possibility of double tax.

Discriminatory treatment of non-corporate shareholder.

Disallowance of foreign tax credit to non-corporate shareholder.

Relief from tax of income subject to prior debt or other commitments.

Lack of provisions permitting tax-free readjustment of corporate structures.

Determination of "pro rata share."

Failure to reduce income for distributions to non-United States shareholders.

Double taxation of income under bill sections 12 and 15.

Difficulty of allocating expenses to items of income.

Inappropriate effect of liabilities and methods of financing upon determination of investment in property.

Taxation of income "owned" by other persons.

Use of attribution rules to tax income but not to secure foreign tax credit.

Application of bill to corporations not controlled after December 31, 1962.

Creation of unwarranted presumption re earnings and profits.

Mr. President, the bill would impose taxes on U.S. shareholders whose foreign corporations engage in transactions that reduce foreign taxes, even though those transactions do not evade or avoid U.S. taxes or themselves have any conceivable adverse effect on the revenues of the United States. Indeed, any reduction in foreign taxes increases funds available for distributions subject to U.S. tax and decreases offsetting foreign tax credits on such distributions. Taxing income which has not actually been received and taxing it though it may never actually be received is a severe penalty.

This is another problem which exists in the pending amendment; but, as I have previously stated, it is only one of a few problems compared with the myriad of problems which exists in the present bill.

Congress must provide adequate rules or administrative authority to protect the U.S. revenues from sham devices that reduce taxes on income from U.S. sources. However, the bill would tax a person who owns an interest in a corporation which engages in a transaction designed to minimize taxes payable to a foreign nation in a manner permitted by the laws of that nation and customarily employed by its citizens and corporations. Thus it would "protect" the revenue of foreign nations beyond their own desires. These nations are sovereign and it is fair to assume that they and not we are best equipped to determine in what way and to what extent their revenues should be protected. The United States may cooperate with them in the revision of their laws and administration, or may negotiate with them treaties which would bring their citizens and ours under comparable rules. But I believe that the effect of the bill in penalizing our own citizens and corporations for transactions which reduce foreign taxes in a manner permitted by foreign laws and administration is wrong in principle. Its effect would be to impose substantial disadvantages on the foreign enterprises of U.S. citizens and corporations.

I cite an example: A is a Belgian corporation owned 75 percent by U.S. shareholders and 25 percent by Belgian nationals. B is a Belgian corporation owned 100 percent by Belgian nationals. The two companies are in competition manufacturing agricultural chemicals in Belgium for use in the Middle East. A

and B each sells its products to its Swiss subsidiary at cost plus 5 percent. The Swiss subsidiaries resell the chemicals and invest their profits (after relatively low Swiss taxes) in needed expansion of inventories and in providing financing for customers.

Under the bill, the Swiss selling subsidiary of A is a "controlled foreign corporation." Its profits are "foreign base company income" and the U.S. shareholders of A would be taxed on 75 percent of these profits as dividend income. The shareholders of B would not be subject to similar tax.

The net effect would be that the foreign enterprise owned by Americans must operate under a tax system which is much more burdensome than that under which its foreign-owned competitor operates. A substantial part of the earnings of the American-owned business could not be used for the requirements of the business but would have to be distributed for payment of the shareholders' taxes.

I do not believe that the penalty for reducing foreign taxes can be justified on the ground that U.S. business activities will be promoted by discouraging foreign enterprises. Experience of businessmen who are planning foreign operations indicates that they seldom really have a choice between establishing a business outside the United States, on the one hand, and, on the other hand, establishing the same business within the United States, or expanding an existing business so that it can export abroad. Experience indicates that American business generally establishes enterprises abroad only when the practical alternative is to let a foreign market be exploited by foreigners.

The avoidance of U.S. taxes through foreign corporations can and should be dealt with. However, the bill should not impose a U.S. tax based on foreign tax results. I believe therefore that the income of a foreign corporation should not be subjected to the rules of subpart F except to the extent that (a) the corporation is used to reduce taxable income from U.S. sources by transactions involving an affiliated U.S. person which enable that person to understate the gross income it earns or to claim deductions to which it would not otherwise be entitled; or (b) the foreign corporation accumulates funds beyond the reasonable present and anticipated needs of its business in order to avoid the U.S. tax which would be imposed on its shareholders were its profits distributed.

I may point out that this is exactly what the pending amendment of the junior Senator from Minnesota would do. That is why it conforms substantially to my position in regard to this matter.

Surely there can be no need or justification for putting foreign enterprises owned by U.S. shareholders at a competitive disadvantage merely because they are conducted so as to reduce their foreign tax burdens.

INEQUITABLE TREATMENT OF NONCORPORATE SHAREHOLDERS UNDER BILL SECTION 12

Section 12 of the bill taxes income earned by a controlled foreign corpora-

tion to an individual or to an estate or trust at individual income tax rates ranging up to 91 percent. No credit for foreign taxes paid by the corporation is available to him.

This treatment would impose severe hardships and would certainly not be equal to the tax treatment afforded U.S. stockholders of domestic corporations. If the business which produced the income were conducted by a foreign branch of a U.S. corporation owned by the individual, the income would be taxed only at the corporate rate, less foreign tax credits, unless it were actually distributed. The income remaining after corporate taxes could be plowed back into the business of a U.S. corporation, and no individual income tax would be payable until his stock would be sold or the company liquidated. Even then the tax would be at capital gains rates.

If undistributed income of a foreign corporation is to be taxed to a U.S. shareholder, I believe that it should not in any event be taxed more severely than undistributed income of a domestic corporation. The amendments to section 15 of the bill, which relates to gain on the sale or exchange of a foreign corporation's stock, proposed by the Treasury recognize the need for more equitable treatment in this respect when an individual disposes of his stock, but no relief whatever for shareholders who are individuals has been provided under bill section 12.

The inequitable position in which an individual shareholder of a controlled foreign corporation is put under the bill is made even more troublesome as a result of the lack of correlation between section 12 and the foreign personal holding company provisions. The bill retains unchanged the proposed amendment of section 551(b) of the code, which amendment is designed to prevent taxation of individual shareholders on the same income under both the foreign personal holding company provisions and section 12. This is especially disturbing in view of the greatly enlarged scope of the foreign personal holding company provisions under the bill. Moreover, in view of the differences in calculations of income taxed under foreign personal holding company provisions and under those of section 12, individual stockholders would be subjected to the administrative burdens of making calculations under both provisions and would be liable for income tax under those provisions that impose the higher tax.

THE CONCEPT OF "U.S. PROPERTY"

The bill includes in section 956 a definition of "U.S. property," the acquisition of which results in the imposition of a tax on shareholders under subpart F. Presumably, section 956 reflects a view that a purchase of "U.S. property" by a controlled foreign corporation should be treated as the equivalent of an actual distribution of earnings or that the purchase evidences an improper accumulation.

These provisions do not appear well directed toward the problems of either "constructive" dividends or improper accumulations. The exceptions to the

definition of "U.S. property" should in any event be expanded to include any property reasonably necessary to the trade or business of the corporation acquiring it. For example, it would certainly seem preferable for a foreign corporation making temporary investments of working capital to be permitted to purchase U.S. Treasury bills—as the pending amendment of the distinguished Senator from Minnesota provides—rather than encouraged to purchase foreign short-term obligations. Similarly, if a foreign corporation is employed to accumulate funds unnecessarily and avoid U.S. income tax on U.S. shareholders, the effect of section 956 is to encourage the corporation to purchase foreign investment securities rather than U.S. investment securities. In such cases, section 956 does not strike at the accumulation; it simply encourages the retention of funds offshore with presumably adverse effects on our balance of payments.

CONCLUSION

In conclusion, it is my view that the only important U.S. tax problems arising from the use of American-owned foreign corporations involve (a) allocations of income and deductions in transactions with affiliated persons subject to U.S. taxes, and (b) unwarranted accumulations of earnings to avoid U.S. taxes on distributions to shareholders.

The provisions of the bill are not well designed to identify and deal with these or any other U.S. tax problems. Moreover, the burden that would be imposed by the bill on our foreign business would be substantial. The concepts and techniques of the bill are so highly complex that I doubt that reasonable technical solutions for its defects can be devised. In any event, I am convinced that the bill could not be equitably and uniformly administered, because it would be impossible for most revenue agents and taxpayers to understand and apply its provisions.

I therefore regretfully conclude that the foreign income provisions of the bill, even as revised by the Treasury draft, would have a seriously adverse effect on foreign operations of American business.

I therefore regretfully conclude that the foreign income provisions of the bill, and particularly those contained in section 12, would have a seriously adverse effect on foreign operations of American business.

Mr. President, I have a fairly long discussion of some of the technical problems that exist in various subsections of section 12. In the event that the pending amendment is adopted, of course, these technical problems will disappear. In the event the pending amendment is not adopted, we will have with us all of these technical problems, and at that time I would find it necessary to discuss them. In the interest of brevity, I ask unanimous consent that this discussion be included as a part of my remarks at the conclusion of my statement.

The PRESIDING OFFICER. Without objection, it is so ordered.
(See exhibit 1.)

Mr. MILLER. Mr. President, finally, it would be my preference that the taxa-

tion of foreign income provisions of the bill be completely deleted and that this entire matter be given special and long-time consideration by the respective taxing committees of the Congress next year; that it be considered as one separate problem, rather than as one of many problems that are contained in the omnibus tax bill. But, failing that, as I have said, the next best thing we can do is to adopt the pending amendment, and at least minimize the number of problems that would be created by the pending bill.

EXHIBIT 1

TECHNICAL DISCUSSION OF SECTION 12 (CONTROLLED FOREIGN CORPORATIONS)

AMOUNTS INCLUDED IN GROSS INCOME OF U.S. SHAREHOLDERS (SEC. 951)

Section 951(a)(1): This section sets forth the amounts to be included in the gross income of persons who are "U.S. shareholders" (i.e. 10-percent shareholders) of a controlled foreign corporation.

The bill does not do anything toward defining what is the pro rata share of a U.S. shareholder who holds noncumulative preferred stock of a controlled foreign corporation or who holds the common stock of a controlled foreign corporation which is subordinate to an issue of cumulative preferred stock upon which no dividend is declared during the year in question or which is in arrears.

If A sells stock of a controlled foreign corporation to B, earnings and profits of the year of sale may be taxed to A under section 1248(b), and taxed again to B as subpart F income for the year.

As in the House bill, it remains doubtful whether the amount includible in gross income of a U.S. corporate shareholder under this section is treated as a dividend for personal holding company purposes.

It may not be entirely clear under this section whether in order to be taxed a person must be a 10-percent shareholder on the last day of the taxable year, or whether it is enough that the person owning stock on the last day shall have been a 10-percent shareholder on any day of the taxable year.

Section 951(a)(2): The pro rata amount taxable to a U.S. shareholder is reduced only by distributions to some other U.S. person during the taxable year as a dividend on the particular stock in question. It would seem that any distributions during the year on a stock should reduce the pro rata shares of tainted items allocable to a U.S. person who holds that stock at the critical date. Furthermore, the result of the provisions in their present form could be to tax two U.S. persons on the same income.

Example: X, a U.S. corporation, owns P, a Panamanian subsidiary which owns S, a Brazilian corporation. P sells all the stock of S to A, a U.S. citizen, under arrangements by which current income to the date of sale is paid out to P as a dividend. The S dividend will be taxed to X as subpart F income and the earnings of S (already taxed to X) will be taxed again to A if they are subpart F income.

Section 951(a)(3) and (4): Unlike section 951(a)(2), dealing with subpart F income, there is no reduction of either the pro rata share of previously excluded subpart F income withdrawn from investment or the pro rata share of investment in U.S. property by reason of distributions received by other persons during such year as a dividend. Section 951(a)(1) should specifically provide that all income taxable under that section should be reduced by distributions during the year (and, as noted above, by other amounts treated as dividends under section 1248) in lieu of the more limited

provision of section 951(a)(2), which is applicable only to subpart F income.

Sections 951(a)(2), 951(a)(3), and 951(a)(4): These provisions of the bill apparently are intended to deal with a case in which a foreign corporation is a "controlled foreign corporation" during part of the year but is not during the remainder of the year. (See comment under section 957(a) below.) In order to limit the amount taxable to U.S. shareholders as subpart F income in such a case, these provisions reduce the amount otherwise taxable as subpart F income to a fraction of the total. This fraction is the same as the fraction of the year during which the foreign corporation was "controlled." This rule would not produce a correct result when control of a foreign corporation shifts between foreigners and U.S. shareholders during the year and the company's subpart F income is not realized proportionately during the two periods.

Example: X corporation is a foreign corporation on a calendar taxable year. On January 1 it is owned entirely by U.S. shareholders. Between January 1 and June 30 X has no subpart F income. On June 30 the U.S. shareholders sell their interests in X to a group of nonresident aliens. Between July 1 and December 31 X has subpart F income. Under section 951(a)(2) half of this subpart F income is taxable to the former U.S. shareholders.

Provision should be made permitting U.S. shareholders who acquire or sell control of a foreign corporation to be treated as though the taxable year of the foreign corporation had commenced or terminated at the date of acquisition or sale.

SUBPART F INCOME DEFINED (SEC. 952)

Section 952(b): The wording is identical with section 952(a)(2) of the House bill. This section excludes from subpart F income the income derived from sources within the United States of a foreign corporation engaged in trade or business in the United States. Where a foreign corporation is not engaged in trade or business within the United States and receives fixed or determinable periodic income from U.S. sources, within the meaning of section 881(a), then it would appear that a tax would still be imposed upon the foreign corporation under section 881(a) and a second tax might be imposed upon its U.S. shareholders under proposed section 951. A possible approach to the problem of imposing a second tax on section 881(a) income might be to provide a deduction from the gross amount of such income equal to twice the amount of U.S. tax paid thereon. This would reduce the amount of such income taxable under subpart F by excluding such part thereof as in effect might be considered to have already borne a U.S. tax at a 50-percent rate.

Section 952(c): This is a new section which is apparently intended to meet the criticism that the House bill contains no provisions with respect to allowance of losses. Section 952(c) permits the carry-forward of post-1962 losses of a controlled foreign corporation against its subsequent earnings. It makes no provision for the carryback of losses. Thus where a controlled foreign corporation is initially successful but ultimately incurs a loss (as in the case of expropriation by foreign governments), the U.S. shareholders would be required to pay a tax at ordinary income rates with respect to the undistributed income of the profitable years without receiving the benefit of any carryback with respect to the subsequent year in which such income was ultimately lost.

Section 952(c) is technically deficient. Under this section, the subpart F income of any controlled corporation may not exceed the earnings and profits of the corporation for the current year reduced by the amount

by which (1) the sum of the deficits in earnings and profits for prior years beginning after December 31, 1962 exceeds (2) an amount equal to the "earnings and profits described in section 959(c)(3)" accumulated for taxable years beginning after December 31, 1962 (including the current year). Presumably under this section "earnings and profits described in section 959(c)(3)" means earnings and profits which are not taxed under section 951. When there are earnings and profits in the current year which are not taxed under section 951, this provision does not work as intended.

Example: In 1963 a corporation has a deficit in earnings and profits of \$400,000. In 1964 the corporation has earnings and profits of \$400,000, consisting of subpart F income of \$300,000 and other income of \$100,000. Since the deficit in 1963 is just equal to the earnings in 1964, it would be expected that no amount would be taxable in 1964. Under the limitation set forth in section 952(c), the limitation on subpart F income in 1964 would be determined as follows: the earnings and profits for the current year of \$400,000 would be reduced by (1) the deficit for 1963 of \$400,000 minus (2) the nonsubpart F income in 1964 of \$100,000, i.e., \$300,000 (\$400,000—\$100,000); therefore, subpart F income of \$100,000 would be taxed even though the deficit in 1963 was equal to the entire earnings and profits of 1964.

This anomalous result would be corrected if section 952(c)(2) merely provided for the deficits of prior years to be reduced by an amount equal to the earnings and profits described in section 959(c)(3) accumulated for prior taxable years beginning after December 31, 1962. This would eliminate the double counting of earnings and profits of the current year.

It should also be noted that the section does not permit the carryforward of losses incurred prior to 1963.

The reference in subparagraph (2) of this section to accumulated earnings and profits of the type described in section 959(c)(3) should explicitly provide that such earnings should be reduced by distributions that are not excluded from gross income under section 959. It may not be clear that the word "accumulated" by itself accomplishes this result.

In the last sentence of the section, it should also be made clear that the deficit will be excluded only if it was previously taken into account in computing subpart F income; one way of accomplishing this would be to add the words "and thereby reduce subpart F income" to the end of the sentence.

Section 952(d): This is another new subsection dealing with losses. It permits losses within a single chain of controlled foreign corporations to be applied against earnings of other foreign corporations within the same chain, "in such manner as the Secretary or his delegate shall prescribe by regulations." Among the problems which the regulations would have to face would be questions of prorating as between shareholders having preferred and common stock or having varying interests during the year or having varying interests in the various corporate links in the chain of corporations; prorating as between foreign corporations which came under U.S. control at different times during the year; and resolving competing interests of shareholders with respect to the carryforward of losses within a single corporate entity (under sec. 952(c)) or attribution of the losses to another corporation in the chain (under sec. 952(d)). It is questionable whether substantive problems of this magnitude should be or can be delegated to the Secretary's discretion without legislative guidelines.

It seems unfair to impose a tax on U.S. shareholders of the parent with respect to

undistributed income from a submember of the chain, without giving the taxpayer any indication of the manner in which losses are to be attributed within the chain. The essential drafting difficulty here stems from the statutory device of attributing to the U.S. shareholder directly the undistributed income of a foreign subsidiary in which the U.S. shareholder owns no shares. It would appear preferable to adopt either the system of hypothetical distributions upward in the chain (the link system) which is used in existing section 555(b) with respect to foreign personal holding companies, or to provide a method under which the U.S. taxpayers would be given the election, subject to suitable safeguards, to determine the income of all the foreign corporations in a chain or in an affiliated group on a consolidated basis similar to the one available to domestic corporations. If this hopscotching method is adhered to, it would be desirable to enlarge section 952(d) so as to (i) permit attribution of losses between affiliates as well as between members of a single chain, (ii) make it clear that losses so applied may be carried forward under section 952(c), and (iii) establish standards for the Secretary to follow.

FOREIGN BASE COMPANY INCOME (SEC. 954)

Section 954(b)(1). This new section would exclude from foreign base company income "dividends and interest" received from certain qualified investments in less developed country corporations, providing such dividends and interest do not exceed the increase in such investments for the taxable year. If the purpose is to permit earnings from an investment from one less developed country to be withdrawn for reinvestment in another less developed country, then the subsection should not be limited to dividends and interest but should extend to all subpart F income received from a less developed country, such as royalties, gains from the sale of the stock of a less developed country corporation, foreign base company sales income, or foreign base company service income.

Section 954(b)(3): This paragraph, which is similar to section 952(e)(6) of the House bill, imposes a special rule where the foreign base company income is less than 20 percent, or more than 80 percent of gross income. The interrelation between sections 954(b)(3), 954(b)(1), and 955(a)(1)(A) should be clarified. As presently worded, it is not certain whether interest and dividends from certain less developed country investments which qualify for exclusion under section 954(b)(1), are included in the numerator in applying the percentage tests of section 954(b)(3).

Section 954(b)(4): This new paragraph provides an exception for any item of income of a controlled foreign corporation if the Secretary is satisfied that "the creation or organization [of the corporation] receiving such item under the laws of the foreign country" of incorporation does not have the effect of "substantial reduction" of income, war profits, excess profits or "similar taxes".

Section 954(b)(4) represents an attempt to limit the complex provisions of the proposed statute to cases of tax avoidance. As discussed in part I, it is suggested that this provision should be amended so that the reference to reduction of taxes applies only to U.S. taxes. Whatever the decision on this question of policy may be this section should be technically clarified in a number of respects. The taxpayer should have the right to establish his right to the exception by the preponderance of the evidence instead of leaving the determination entirely to the discretion of the Secretary. In addition, the section should be clarified so as to refer to the transaction giving rise to the income, rather than the "creation or organization" of the corporation.

Section 954(b)(5): There are some of the difficulties which would be involved in de-

termining which deductions would be properly allocable in determining foreign-base-company income. The present bill would give the Secretary authority to promulgate regulations to determine the allocation of deductions to four different types of tainted income. This is another instance in which the statute seeks to sidestep difficult problems by delegating their solution to the Secretary. It would seem preferable to face these problems from the outset, in order to help ascertain whether the statute would be workable in practice. In particular, it should be made clear that any excess of expenses, losses and deductions allocable to one category of subpart F income over the income in that category should be charged against other categories of subpart F income. Merely allowing such excesses to reduce earnings and profits will not suffice, since they may be absorbed by earnings from sources which do not constitute subpart F income.

Section 954(b)(5) should be clarified so as to refer to expenses and losses as well as deductions (as is done in section 953(b)(5) with respect to certain insurance income), and to permit the various elections as to depreciation, etc., of the kind available to domestic corporations (as appears to be intended in section 962(a) with respect to determination of earnings and profits).

Section 954(c)(2): As in the case of section 952(e)(3) of the House bill, this section would include all rents in foreign base company income without regard to whether they constitute more than 50 percent of gross income, subject to the exceptions of sections 954(c)(3) and 954(c)(4)(B) (see below). These exceptions are responsive in part to our original comments (hearings, pp. 3179-3180), but do not deal at all with the problem of rents which have been "locked in" to cover debt or commitments of a foreign corporation. One way to handle the "lock in" problem generally would be to expand new section 962(b) (blocked foreign income) to include restrictions or limitations imposed under loan agreements or other commitments necessary for the business.

Consideration should also be given to the desirability of excluding rent where it constitutes the principal income of the foreign corporation, as is done with respect to personal holding companies under the 50-percent limitation of present section 543(a)(7). If the purpose of removing the 50-percent limitation is to prevent rental income from sheltering other foreign base company income, this could be accomplished simply by excluding rental income from "gross income" for the purposes of the computation in section 954(b)(3).

Section 954(c)(3): This is a new paragraph which excludes dividends, interest, rents and royalties from foreign base company income if they are both (A) "derived in" the active conduct of a business, and (B) not received from a related person. The listed items of income may be received in connection with, or as an ordinary incident to, a manufacturing or other operating business, but it is not clear that the phrase "derived in" would cover these cases. Moreover, the exception from the exclusion under (B) should be limited to the case where the related person is a U.S. person. A transfer of items between related persons in connection with an active foreign business should not be the occasion for imposing a U.S. tax unless it involves the shunting of income from, or increasing the deductions of, a U.S. person.

Section 954(c)(4): This is a new paragraph which excludes dividends, interest, rents, and royalties from foreign base company income if received from a related person under certain described circumstances. In the case of dividends and interest, the payor must be organized under the laws of the same country as the payee and, in addition, the payor must have substantial assets used in its

business in such country. In the case of rents, royalties, and "similar amounts" the payor must be paying for the use of property located in the country in which the recipient corporation is organized. It is assumed that the theory behind the exclusion is that under the laws of most foreign countries the payment of the item under the circumstances described will not result in a reduction of foreign taxes. As stated above, it does not seem desirable to use the avoidance of foreign taxes as an occasion for imposing U.S. taxes; it would be preferable to disregard foreign-to-foreign intercompany transactions entirely.

Special provisions should be made for property of the type which is necessarily used within or between two or more countries, such as ships or planes. The reference to a corporation "created or organized" under the laws of a particular country should be expanded to include a corporation treated as a resident under such laws.

Section 954(d)(1): This section defines foreign base sales income in terms similar to section 952(e)(2) of the House bill. It would deprive U.S. controlled foreign corporations of the benefits of using a sales subsidiary or affiliate which is incorporated outside the country from which it buys or to which it sells. This is apparently intended to make it difficult for U.S. controlled business conducted abroad to minimize foreign taxes, even though such benefits are freely available to their foreign competitors.

Section 954(d)(2): This is a new section. It provides that in "situations * * * through a branch or similar establishment outside the country of incorporation of the controlled foreign corporation has substantially the same effect as if such branch or similar establishment were a wholly owned subsidiary corporation, deriving such income," then, under regulations to be prescribed, the income attributable to the "carrying on of such activities" is to be treated as income derived by a wholly owned subsidiary and shall constitute foreign base company sales income of the controlled foreign corporation.

The entire provision is vague and uncertain in the extreme. Its application and operation are so uncertain that comment upon the provision is most difficult.

Many foreign countries do not tax corporations organized under their laws with respect to income attributable to branches located in other countries. The Treasury may regard operation under laws of this as a method of avoiding foreign taxes which this provision is intended to penalize. If so, this would represent an extreme instance of the Treasury's concern regarding the payment of foreign taxes which are not required by the countries involved. In such cases it would appear that section 954(d)(2) might well lead those countries not taxing branch income to impose a "soak-up" tax on United States controlled corporations organized under their laws, but not on their foreign competitors.

This provision, if it were to remain in the bill, would create innumerable problems. For example, should the "branch" be treated as a corporation which has been organized under the laws of the country in which the putative parent is organized, or in which the branch is actually located, or elsewhere? How would it be possible at one and the same time to treat the income of the branch as "income derived by a wholly owned subsidiary" and as constituting foreign base company sales income of the putative parent? What part of the income of the branch is to be so treated?

Section 954(d)(3): This new section contains a definition of "related person," which substantially expands the language of the last sentence in section 952(e)(2) of the House bill. In determining stock owner-

ship, the new section incorporates the rules of direct and indirect ownership of section 958(a) and the attribution rules of section 958(b). In view of the incorporation of the rules of section 958, it is confusing for section 954(d)(3) to refer again to "ownership, directly or indirectly."

Section 954(e): This new section defines "foreign base company services income" as meaning any income derived "in connection with" the performing or furnishing of "technical, managerial, engineering, architectural, scientific, skilled, industrial, commercial or like services" which are performed for a related person "for or in connection with business activities carried on by such related person outside the country under the laws of which the controlled foreign corporation is created or organized." The meaning and scope of this new section is obscure. For example, it is not clear whether the section covers services performed (for a related person) outside the country of incorporation of the corporation rendering the service, or whether it refers to services performed anywhere in connection with business carried on by the related person outside such country of incorporation. It is also not clear what kind of business enterprises would be included under such broad terms as "managerial," "industrial," "commercial," and the "like," or whether income derived "in connection" with such services for a related person would include compensation received from an unrelated third party.

The language of section 954(e) seems broad enough to encompass marketing companies and sales agencies of the kind described in section 954(d)(1). If an item of income should fall under both section 954(e) and 954(d)(1), then under section 954(b)(6) the allocation of the item would be determined by regulations to be prescribed. This adds still another element of uncertainty to the statute, since the exceptions set forth in section 954(d)(1) are not the same as those in section 954(e).

WITHDRAWAL OF PREVIOUSLY EXCLUDED SUBPART F INCOME FROM QUALIFIED INVESTMENT (SEC. 955)

Under the provisions of sections 954(b)(1) and 954(f) a controlled foreign corporation can exclude from subpart F income certain dividends and interest received from less developed countries and reinvested in those countries. When the investment is withdrawn, sections 955 and 951(a)(1)(A)(ii) would tax the previously excluded income to U.S. shareholders as a new category of income, called "previously excluded subpart F income withdrawn from investment in less developed country corporations for such year." The technique of creating a new category of income (rather than treating the withdrawal as subpart F income in the year of withdrawal) results in serious complexities and incongruities.

Section 955(a)(1): It is not clear under this section whether interest and dividends would be considered to have been excluded from foreign base company income under section 954(b)(1) (and therefore potentially taxable under section 955) if they were received in a year in which there was no foreign base company income because all of the foreign base company income (including such dividends and interest) was less than 20 percent of the gross income of the controlled foreign corporation.

The word "foreign" is omitted after the word "controlled" in the second line of this provision in the committee print.

Section 955(a)(2): This section defines a decrease in qualified investments, and limits the amount of such decrease to "the sum of the earnings and profits for the taxable year and the earnings and profits accumulated for prior taxable years beginning after December 31, 1962."

Under the quoted language it is entirely unclear whether a deficit existing at the beginning of the taxable year may be applied to reduce or eliminate earnings and profits of that year. Moreover, even if a deficit may be so applied, there seems to be no reason why its treatment under section 955(a)(2) should differ from its treatment under section 952(c). The latter section expressly provides that subpart F income is to be taxed only to the extent of untaxed earnings and profits less prior deficits. Section 955(a)(2), however, would seem to permit the taxation of section 955 withdrawals if there are any accumulated earnings and profits, whether or not they have been taxed.

Example: In 1963 corporation X (wholly owned by U.S. shareholders) has \$300,000 of subpart F income and \$300,000 of dividends and interest excluded from subpart F income under section 954(b)(1). In 1964 X has a \$300,000 operating loss. In 1965 X has neither current earnings and profits nor a current loss, and withdraws from investment the \$300,000 previously excluded from subpart F income. Since X has accumulated earnings and profits of \$300,000 (\$600,000 from 1963 less the \$300,000 loss of 1964), the withdrawal would be taxable under section 955(a)(2). Thus, taxes have been imposed on \$600,000 of income, even though X's accumulated earnings and profits through the year of withdrawal were only \$300,000.

The incongruity of the rules provided by section 955(a)(2) is illustrated by the different result which would occur were the tax-free distribution made prior to the year of section 955 withdrawal.

Example: Same facts as in the preceding example, except that in 1964 X distributes \$300,000 to its U.S. shareholders. The distribution is tax free under section 959, but results in a reduction of earnings and profits. The section 955 withdrawal in 1965 is likewise tax free, because there are no accumulated earnings or profits at the beginning of 1965.

Under section 955(a)(2), the amount of any decrease in qualified investments is to be adjusted by eliminating decreases resulting from net losses on qualified investments which are "disposed of" during the taxable year. It is not clear whether an investment which has become worthless during the taxable year (and which would thereby contribute to the decrease in qualified investments) has been "disposed of" for the purposes of the above adjustment. Section 955(a)(2) should be revised to clarify this point.

Section 955(a)(3): This section purports to define pro rata share of amount withdrawn. The definition says only that a person's pro rata share is his pro rata share. It contributes nothing toward resolving this important question. See our comments under section 951(a)(1) above.

Section 955(c)(1)(B): This section requires that 80 percent or more in value of the assets of a less developed country corporation consist of certain assets. These assets include "property used in such trades or businesses and located in less developed countries." It is not clear that accounts receivable from customers located in countries outside less developed countries are "property" located in less developed countries, even though the receivables grew out of a trade or business conducted in a less developed country.

Section 955(c)(1)(C): There seems to be no reason for requiring that a less developed country corporation be incorporated under the laws of such a country if it meets the other tests of section 955(c)(1).

INVESTMENT OF EARNINGS IN U.S. PROPERTY (SEC. 956)

Section 956(a)(1): In defining the amount of earnings invested in U.S. property, this section limits such amount to the extent it

would have "constituted a dividend (determined after the application of section 955(a)) if it had been distributed." I would have thought the reference would be to section 959(a) rather than section 955(a), so that an investment in U.S. property would not be taxed if it could only be made out of earnings available for tax-free distribution under section 959.

The reference to "property held, directly or indirectly" is obscure and should be clarified.

Section 956(a)(2): This section deals with the "pro rata share" of an increase in the earnings of a controlled foreign corporation invested in U.S. property. I have observed earlier, the term "pro rata share" requires clarification. The section would tax an increase in investment in U.S. property even though attributable to earnings and profits accumulated before January 1, 1963. This represents a marked change from the parallel provisions of section 953 of the House bill, which limited the tax to earnings and profits accumulated after December 31, 1962. In this important respect it seems clear that section 956 is not "with technical changes, substantially the same" as the parallel provisions of the House bill.

Section 956(b)(1): This section defines "U.S. property" as tangible property located in the United States, stock of a domestic corporation, or an obligation of a U.S. person, if "acquired after December 31, 1962." If the purpose of section 956 is to impose a tax with respect to U.S. investments which are tantamount to dividends by reason of benefits conferred upon related U.S. persons, then the section should apply only to such investments. On the other hand, if the purpose of section 956 is to strike at investments which evidence unreasonable accumulations, then there would seem to be no reason to limit it to U.S. property or to apply it to investments made in connection with the business of a controlled foreign corporation.

The reference to property "acquired after" December 31, 1962, is not clear. For example, if securities held prior to December 31, 1962, are exchanged in a tax-free reorganization, it is not clear when the securities resulting from the refunding transaction have been "acquired."

It should also be noted that the restriction of the definition to property acquired after December 31, 1962, would bar replacement of existing U.S. investments upon their maturity or sale after December 31, 1962. As a result, the statute would tend to force capital out of the United States as well as to bar its flow into the United States. The advisability of these provisions seems highly doubtful in the light of our balance-of-payments problem.

Section 956(b)(2)(A): This section would exclude from the definition of "U.S. property" any "money, or deposits with persons carrying on the banking business, located in the United States." In view of the phrasing, it would appear that the deposits, as well as the money, must be "located" in the United States. This would raise substantial doubts with respect to the potential taxability of deposits made with a foreign branch of a U.S. bank, even though there would be no question if the deposit had been made at the home office of the U.S. bank. This result was probably unintended. It is suggested, accordingly, that section 956(b)(2)(A) be worded to read as follows:

"(A) money, or deposits with or obligations, pledges, and guarantees of persons carrying on the banking business;"

Section 956(b)(2)(C): This is an exception which is apparently intended to permit sales to U.S. persons on usual credit terms. The wording of the exception is singularly awkward and gives rise to numerous questions of construction. In particular, it is not clear whether the exception would apply

in the case of a sale made to an unrelated person.

An exception should be provided for any obligation arising in the ordinary course of business. In the absence of such an exception, obligations arising from the performance of services for a U.S. person or obligations for rentals due under leases to U.S. persons would be treated as if they were investments in U.S. property under section 956(b)(1)(C), even though the services were performed or the rental property was located entirely outside the United States.

Section 956(c): This section states that a controlled foreign corporation shall be considered "as holding an obligation of a United States person if it is a pledgor or guarantor of such obligation." It is assumed that the word "it" refers to the controlled foreign corporation, but this is not clear. If this assumption is correct, the section would prevent a tax haven company, for example, from guaranteeing a loan by a foreign bank to the tax haven company's U.S. parent based on funds of the tax haven corporation accumulated in the foreign bank. If such is the intent, this should be made clear by deleting the word "it" and substituting in its place the words "the controlled foreign corporation." This was the thrust of the original section 953(b)(4).

If the word "it" were to be construed to refer to "United States person," it is believed that it would raise very serious unintended problems. For example, it is a common banking practice abroad for a bank to guarantee obligations of various kinds between its customers. A number of these transactions would be exempted under section 956(b)(2)(C). Many other similar problems arise in connection with sales of property and if the guarantee of a foreign branch of a U.S. bank in such transactions would convert the obligation guaranteed into U.S. property, it would not only put the bank branch at a competitive disadvantage but would raise difficult problems for its customers who were controlled foreign corporations.

CONTROLLED FOREIGN CORPORATIONS (SEC. 957)

Section 957(a): The bill as passed by the House also presented substantial difficulties in determining the facts necessary for identification of a controlled foreign corporation. The incidence of these problems has been substantially reduced under the bill by the proposed limitation on attribution through corporations and by the disregard, for purposes of the definition, of U.S. persons whose owned or attributed stock interests are less than 10 percent. However, serious problems could still arise for a minority shareholder who must determine whether the number of remaining shares held by or attributed to U.S. persons is such as to place the corporation in the category of a "controlled foreign corporation." Even though only 10 percent shareholders (actual or attributed) are counted for this purpose, the counting may be complicated or impossible because of registration of the remaining stock in numbered accounts or "street" names, the use of bearer shares, the difficulties of applying the attribution rules, and the fact that "control" might exist on only 1 day in the year.

Moreover, despite the 10-percent limitation it is still possible for situations to arise in which a corporation will be treated as "controlled" by U.S. persons although it is in fact controlled by foreigners.

Example: A U.S. publicly held corporation owns 40 percent of the stock of foreign corporation X. The remaining 60 percent of X stock is owned by a foreign corporation which is owned by foreigners except that 20 percent of its stock is owned by an American. X is deemed to be a "controlled foreign corporation" under sections 957 and 958, al-

though Americans do not have effective control.

As set forth in the bill, a foreign corporation would seem to be a "controlled foreign corporation" for the entire taxable year if the ownership test is met on any one day. This is inconsistent with sections 951(a)(2), 951(a)(3) and 951(a)(4) where a U.S. shareholder is taxed only with respect to the portion of the year that the foreign corporation is a "controlled foreign corporation". This section should specifically provide that a foreign corporation is a "controlled foreign corporation" only during the period in which the ownership test is met.

Section 957(c): The other basic change in what constitutes a controlled foreign corporation is in the exclusion of certain corporations organized in U.S. possessions. This is a desirable change. The parenthetical reference in sections 957(c)(1) and 957(c)(2) seems unnecessary.

RULES FOR DETERMINING STOCKOWNERSHIP (SEC. 958)

Section 958(a): Under section 958(a), a U.S. person is treated as owner not only of stock he actually owns, but also of stock he indirectly owns through a foreign corporation, foreign partnership, foreign trust, or foreign estate. This section has been made applicable not only for the purpose of taxing U.S. persons (as the corresponding provision in the House bill was) but also for the purpose of determining whether a U.S. person is a "U.S. shareholder" and whether a corporation is a "controlled foreign corporation." No reason has been given or is apparent for making this change.

Section 958(b): This is the same as former section 955(b) of the House bill except for the change embodied in section 958(b)(4). The latter section narrows the attribution of stock ownership through a corporation to a situation where the stockholder owns 10 percent or more of the stock directly or indirectly. Unfortunately, a similar limitation has not been introduced into section 958(a). Since sections 958(a) and 958(b) serve the same statutory purposes (determining who is a "U.S. shareholder" and determining if a foreign corporation is "controlled"), the failure to include the 10 percent limitation in section 958(a) largely negates the change made in section 958(b). For this reason, section 958(a) should be restricted to its original purpose.

EXCLUSION FROM GROSS INCOME OF PREVIOUSLY TAXED EARNINGS AND PROFITS (SEC. 959)

Section 959: This section is identical to section 956 of the House bill except for the occasional substitution of the word "shareholder" for "person," and the major difficulties continue to be the same.

Whether a distribution of earnings or an investment of earnings in U.S. property results in the realization of taxable income by a person subject to Federal income taxation will depend upon whether such earnings were previously included in the taxable income of a "U.S. shareholder" who owned the shares now owned by the person whose income tax liability is in issue. Shares which are otherwise identical may therefore have different tax attributes depending upon how they were previously owned. If the purposes of section 959 are to be served, administrative problems of almost insuperable complexity will be encountered, especially in tracing and identifying shares of a public corporation which may be registered in street name and purchased and sold through brokers.

Example: A, a U.S. citizen, acquires one hundredth of 1 percent of the stock of X, a foreign corporation. The value of his investment is about \$10,000. X company has acquired over a number of years control of several foreign corporations owning rental prop-

erty in various foreign countries. X acquired the stocks of its subsidiaries from other foreign corporations, from U.S. corporations, from trustees and executors of estates here and abroad, etc. Subsidiaries of X sell properties (realizing no net gain), and distribute the proceeds to X. Then X distributes a dividend of \$1,000 to A.

To the extent that the rental income of the underlying companies was taxed to U.S. persons in previous years through the stock which X has acquired, A should receive his \$1,000 tax free under section 959(a) when the rule of section 958(a) is taken into account. However, it may be prohibitively expensive for A to examine the past shareholdings of the companies now underlying X (and the shareholdings of the companies of which they were once subsidiaries).

Moreover, there may be no reason for the management of X to provide A with information or assist him in securing it. X may not be a "controlled foreign corporation". A and other U.S. shareholders taken together may have a very small fractional interest in X. Their problems would not stem from the status X as a "controlled foreign corporation," but from the fact that they receive cash and the fact that some of the subsidiaries of X were at one time or other controlled foreign corporations whose income was taxed to U.S. citizens and is now being taxed again.

In the case described, a revenue agent faced with the statute, the lack of proof and A's cash receipt would have to include in A's gross income the \$1,000 cash distribution by X. Despite the elaborate technical machinery of section 959, the same income could, in practice, be taxed twice.

Section 959(b) excludes previously taxed earnings from gross income "for purposes of the application of section 951(a)" when distributed through a chain of ownership through other controlled foreign corporations. Such distributions should also be excluded from gross income for the purposes of section 551 of the Internal Revenue Code. Absent such an exclusion, distributions of previously taxed income through a chain of foreign corporations may be taxed again as foreign personal holding company income.

SPECIAL RULES FOR FOREIGN TAX CREDIT (SEC. 960)

Section 960: Section 957 of the House bill, providing special rules for the foreign tax credit, has been renumbered as section 960 of the bill. Some of the problems in the section are:

Under section 960, no credit for foreign taxes is available to individual U.S. stockholders in controlled foreign corporations.

Attribution rules are used to compute income elsewhere in subpart F, but are not used to determine eligibility for the foreign tax credit in section 960.

Section 960(a)(3) should be correlated with the gross-up provisions of the bill, for otherwise a domestic parent may be required to include income of a controlled foreign corporation in its gross income twice in order to obtain a foreign tax credit.

It is not clear whether section 960(a)(4) is intended to mean that inclusions in gross income are not ordinarily to be considered as dividends.

Section 960(b) should be extended to apply to successors in interest and provision for prior year limit should be made.

Section 960(b)(2)(A) should be clarified so as to include appropriate amounts grossed-up in determining the amount of increase in the section 904 limitation.

Section 960(b)(2) should be modified to take into account in the year of distribution, in addition to the increase in the section 904 limitation for the year of taxability, the carryovers and carrybacks resulting from such limitation for the year of taxability.

Section 960(b)(2) will require keeping prior years open for long periods of time, for purposes of that section, since the section 904 limitation in the year of distribution will be determined in the light of that limitation in the year of taxability.

Section 960(b)(4): This provision does not yield the correct result in cases such as the following:

Example: Under section 951(a) the 1963 income of A corporation (a foreign corporation) is taxed to X corporation, a U.S. corporation. In 1964 X corporation receives a tax-free distribution from A corporation. In 1964 X corporation also realizes taxable foreign income from source B. X corporation increases its section 904 limitation under section 960(b)(1) and (b)(2). After doing so, X has the following items for 1964:

U.S. income tax liability	\$1,000
Foreign tax credit under sec. 901 arising from source B income after applying sec. 904	500
Increase in limitation under sec. 960 (b) arising from tax-free distribution by A corporation	700

The statute is intended to permit X to employ the \$700 increase in its credit limitation under section 960(b) so as to eliminate its net liability of \$500 for 1964 and also claim a \$200 "refund." The statute, however, does not operate because the \$700 increase in the section 904 limitation which arises under section 960(b) does not exceed the tax of \$1,000 imposed for 1964. The statute should read:

"The tax imposed by this chapter for such year reduced by any credits allowable under any provisions of this chapter other than credits arising out of or allocable to the increase in the limitation arising under section 960(b)."

ADJUSTMENTS TO BASIS (SEC. 961)

This section provides for increases in basis of stock of a controlled foreign corporation by amounts included in gross income under section 951(a). It is submitted that the basis increase provision does not go far enough.

Example: X, a U.S. citizen, owns all the stock of P, a Panama corporation, which owns all the stock of S, a Swiss corporation. S has subpart F income charged to X under section 951. Under section 961(a) the basis of the P stock is increased, but not the basis of the S stock in the hands of P. A sale of S stock by P would thus increase the earnings and profits of P and the increase could form the base for further taxes (for example under sec. 956) imposed upon X, essentially stemming from the same income already taxed.

It is submitted that the basis of the S stock in the hands of P should also be increased under these circumstances.

MISCELLANEOUS PROVISIONS (SEC. 962)

Section 962(a): This section provides that earnings and profits of a foreign corporation are to be computed for purposes of subpart F according to rules "substantially similar" to those applicable to domestic corporations, under regulations to be prescribed by the Secretary or his delegate. This section leaves unanswered specific questions with respect to elections, accounting methods and fiscal periods affecting the computation of earnings and profits.

Section 962(b): This section provides that under regulations to be prescribed "no part of the earnings and profits of a controlled foreign corporation for any taxable year shall be included in earnings and profits for purposes of sections 952, 955 and 956" if it is established that such part could not be distributed because of currency or other restrictions or limitations.

It is presumed that this section is intended to prevent the inclusion of blocked income in the taxable income of a U.S.

shareholder of a controlled foreign corporation. It will not always accomplish this purpose.

Example: A controlled foreign corporation has \$300,000 of operating income from country A which is not blocked and \$300,000 of subpart F income from country B which is blocked. Section 962(b) excludes the blocked income from earnings and profits. Section 951(a)(1)(A)(i) and section 952(c) require the U.S. shareholder to include in his taxable income the amount of subpart F income not in excess of earnings and profits of the taxable year. Subpart F income is \$300,000 and earnings and profits are likewise \$300,000. The shareholder would be required to include \$300,000 in his taxable income.

The result in the foregoing example was presumably not intended and the section should be redrafted. Moreover, it would appear imperative that blocked income be completely excluded from all calculations of gross income, earnings and profits and taxes paid until it is unblocked. Otherwise the 20-80 ratio of section 954(b)(3) and the operation of the foreign tax credit provisions would be materially distorted.

TECHNICAL AND CLERICAL AMENDMENTS

Bill section 13(b): This section is the same as section 13(b) of the House bill. This section was intended to relieve the stockholders of foreign personal holding companies from imposition of a second tax under section 551 with respect to any subpart F income on which they will be taxed under section 951. This section is technically deficient and fails to accomplish its purpose. The failure to correct these deficiencies is particularly troublesome because the scope of the foreign personal holding company provisions has been broadened by bill section 7.

Mr. McCARTHY. Mr. President, will the Senator yield for a question?

Mr. MILLER. I am happy to yield to the Senator from Minnesota.

Mr. McCARTHY. I commend the Senator from Iowa for the remarks he has made, particularly on the technical difficulties that will arise if this section of the bill is adopted. I quite agree with his statement that the entire section should be given prolonged study and that we should not act upon it at this time.

In the past, on technical provisions, even in simple areas like domestic excise taxes, long studies, running a year or two, ordinarily have been made. In this case, the House Ways and Means Committee had the bill for about a year and a half, but in the course of that time it dealt with five or six very complicated areas of taxation.

On the Senate side, we have had the bill only about 2 months in the Finance Committee, because we have had to deal with other pressing and difficult pieces of legislation.

In the committee I voted to refer the whole section to the Joint Committee on Internal Revenue Taxation for a study of 6 months. Another motion was made for a study of 90 days. I thought 6 months was a reasonable time. The motion was defeated.

I think it best now not to act on it. There is no great emergency or press. But since I do not believe that course of action is likely to be followed, I think the amendment I am offering would tighten up some of the very obvious tax-haven or tax-avoidance devices.

Though there may be technical problems even in carrying out the terms of my amendment, at least we have established rules to guide our actions with regard to unreasonable accumulation, and we leave the procedure somewhat flexible, so the Treasury can work out some prudent rules by which it may act. This would be at least a kind of compromise, interim proposal, after which we might decide that we had better call the whole thing off, or have a year's study, at the end of which time we might decide to call it off again.

I thank the Senator for his remarks and support.

Mr. MILLER. I thank the Senator from Minnesota. Let me add to what he has just said that I think he has well pointed out why it has been so difficult for the Congress itself, and particularly for the members of the House Ways and Means Committee and the Senate Finance Committee, to tackle this very complex section of the law and the bill in an adequate manner.

He has pointed out that the House spent about a year on this subject; that in the Senate Finance Committee it required at least 2 months, and even then the efforts of the members were diffused among the very many sections of this very long, complicated tax bill—not concentrated merely on the section we are speaking about now.

Mr. McCARTHY. Mr. President, if the Senator will yield, is the Senator familiar with the section dealing with taxes on insurance companies? He knows from experience in tax law that the problem of trying to tax insurance companies is one of the most complex we face in this country, and this is one area of the legislation with which we had to deal.

Mr. MILLER. I agree with the Senator.

I hope my comments this evening will not be interpreted as being a criticism of the members of the Finance Committee. Having been in the tax business some 20 years, I know there is a limitation on the ability of human beings, no matter how skilled they are, to handle problems of such great complexity as are involved in the bill. But the point I am making is that if we have this problem with respect to the members of the Finance Committee in drawing up the basic law, we should think of the great administrative problems that will descend upon the legislation and regulation officials in the Commissioner's office if the Congress passes the bill with these complex sections in it, including the complex section on insurance companies, as the Senator has mentioned. The Internal Revenue Service would be told: "Now, go to work and write the regulations." It seems to me it would require years to issue various sets of regulations, going through the established testing devices, before good regulations could be formulated.

We can relieve the Treasury Department and its staff of a great amount of unnecessary workload if we delete such a section as this and replace it with the Senator's amendment, which, as he has pointed out, has the background of

settled court decisions and regulations in the matter of what is "unreasonable accumulation."

Does not the Senator agree that there will be plenty of material to work on, for the regulation purposes, without this section being added to the burdens, if we delete it from the bill?

Mr. McCARTHY. I certainly do.

Mr. MILLER. I thank the Senator from Minnesota for his remarks.

I yield the floor.

(During the delivery of Mr. McCARTHY's remarks:)

Mr. McCARTHY. Madam President, I yield to the Senator from Rhode Island [Mr. PASTORE] with the understanding that his remarks will be printed in the RECORD following the conclusion of my remarks.

Mr. PASTORE. And, Madam President, I ask unanimous consent that the Senator from Minnesota not lose his right to the floor by so doing.

The PRESIDING OFFICER. Without objection, it is so ordered.

THE TEXTILE PROGRAM

Mr. PASTORE. Madam President, this morning's Washington Post and Times Herald contains an editorial which attacks the textile program announced by the President a year ago last May, accuses the industry of "blackmail" in urging its implementation, and the administration of "appeasement" in carrying it out.

I ask unanimous consent that the editorial may be printed in the RECORD at this point.

There being no objection, the editorial was ordered to be printed in the RECORD, as follows:

SELF-DEFEATING TACTICS

In its efforts to secure the passage of the Trade Expansion Act the administration appears to have ignored a lesson which every victim of blackmail has learned through painful experience. Once paid off, blackmailers refuse to stay "bought."

In order to appease the strongly protectionist elements in the cotton textile industry a long-term cotton textile agreement was negotiated at Geneva this year which, when fully implemented, would oblige its signatories to place quotas on cotton exports to the United States when requested to do so. But this concession failed to satisfy the domestic cotton interests, and they are now busily lobbying for an additional 8½-cent "equalization" tariff on cotton-textile imports.

Having been burned by the cotton interests, the administration is taking still another step along the primrose path of appeasement. Myer Feldman, deputy special counsel to the President, informed the National Association of Wool Manufacturers that—

"Limitation of textile imports to prevent market disruption is an essential element of administration policy. We intend to implement this policy with regard to all textiles, and particularly to prevent market disruption such as would result from an increase over current levels of exports. The functions of the Interagency Textile Committee have just been expanded to cover all textiles."

This implied commitment to extend the protectionist quota system to woollens comes at a time, when that industry is experiencing rising sales and high profits.

The willingness of the administration to buy off the protectionist opposition with piecemeal concessions is causing growing suspicion abroad and alienating the supporters of the Trade Expansion Act at home. According to the terms of the original cotton agreement, negotiated at Geneva in 1961, the base period of imports is specified as a guaranteed minimum. But the program appears to be administered in such a way as to establish that base level as a maximum above which "market disruption" is automatically presumed. Cotton imports are now cut off without attempts to determine public damage, and as a result a suit has been filed which challenges the constitutionality of the cotton quota agreements.

The administration has made remarkable progress in breaking down traditional protectionist sentiment and garnering nationwide support for the Trade Act which now has an excellent chance of passing the Senate. When passed, the act will empower the President to enter into negotiations for the lowering of international tariff barriers, but his chances of success will be severely limited if his hands are tied by the concessions which are now being made to the enemies of freer world trade.

Mr. PASTORE. Madam President, the President's textile program of May 1961 follows in essential respects the recommendations of the special Subcommittee of the Committee on Commerce on which the Senator from New Hampshire [Mr. CORTON], the Senator from South Carolina [Mr. THURMOND], and I served. Our investigations and extensive hearings began in 1958; were held again in 1961 and 1962. The subcommittee held hearings in Washington, D.C., in the principal textile producing States, and in New York. We listened to representatives of management and labor for the domestic textile and apparel industries, as well as to importers, exporters, and representatives of the various departments of our Government.

The Post has overlooked the fact that both President Kennedy and former Vice President Richard Nixon in 1960 recognized the serious import problem confronting all branches of the textile industry. Each pledged himself to remedy the situation which was eroding one of our basic industries and damaging the national economy.

Following further study in February and March of 1961 by the President's Cabinet Subcommittee, made up of representatives of the Departments of State, Treasury, Commerce, Agriculture, and Labor, the President on May 2, 1961, announced a special program for the textile industry, and said:

It is our second largest employer. Some 2 million workers are directly affected by conditions in the industry. There are another 2 million persons employed in furnishing requirements of the industry at its present level of production. Two years ago, the Office of Defense Mobilization testified that it was one of the industries essential to our national security. It is of vital importance in peacetime and has a direct effect upon our total economy. All the studies have shown that unemployment in textile mills strikes hardest at those communities suffering most from depressed conditions.

Among the seven points of the President's program, the following are relevant here:

First. Direction to the Department of State to call a conference to seek an in-

ternational understanding "which will provide a basis for trade that will avoid undue disruption of established industries." This direction applied to all of the textile industry, although to date such understandings cover only cotton goods.

Second. In addition, the President also recognized the inequity of the adverse differential in raw cotton costs between domestic and foreign mills. He directed the Department of Agriculture to make recommendations to eliminate or offset the cost to the U.S. mills of this differential. The Department of Agriculture requested the Tariff Commission to establish such an offset fee on November 13, 1961, and the Tariff Commission is expected to make its recommendations soon.

Third. The President also said that an application by the textile industry for action under the national security provisions of the Trade Act would be carefully considered on its merits. Such an application has been made and is currently pending.

The program for the fiber-textile-apparel industry, affecting 4 million American workers, is basic and far reaching. The President, as well as industry and labor, are to be congratulated and not maligned for facing up to these realities.

Ten months of experience with the short-term Geneva arrangement on cotton textile trade has proven the wisdom of the President's request through the Agriculture Department for a fee to offset the cotton cost differential of over 30 percent in the price of cotton. I should like to state a few examples:

Imports of cotton yarn during the first 6 months of this year totaled 17 million pounds, or over three times higher than 1961 and over twice as high as 1960. Imports of heavy fabrics, such as sheeting, containing a large amount of cotton relative to total cost, have more than doubled since last year. In fact, during the short-term arrangement which expires on September 30, 1962, imports of all cotton manufactures, including apparel, will be at least 25 percent above the disruptive levels which existed during the base period in the arrangement, namely, fiscal year 1961.

Experience has proved the wisdom of the request to the Tariff Commission for an offset fee to help alleviate a situation so destructive of American jobs and American plants. Within the past 2 weeks, three cotton mills have been forced to close down. One is in my own State of Rhode Island, another in Alabama, and only today one in Massachusetts. The hundreds of workers involved in each case are now looking for employment which may well be impossible to find in these areas.

Since 1947, as the imports of textiles have risen from insignificant amounts to over a billion square yards annually, over 400,000 textile jobs have been permanently closed. Over 850 mills have closed. Not all of this is due to imports; some is caused by a loss of exports, and some by rapidly rising productivity in the industry.

But imports have contributed a major share and constitute a heavy burden on

the industry. It is essential that the cotton textile arrangement be enforced and carried out so as to prevent the high levels of fiscal year 1961 from rising higher, causing further disruption, hardship and liquidation. To do this, the President's program must be carried out in full, including the offset fee.

The Post objects to the President's carrying out his program for other textiles as well as cotton to prevent market disruption, unemployment, and hardship in those industries. I know about wool textiles. My State, as well as many others, has a heavy stake in this segment of the industry. Our domestic mills are practically the sole consumers for the wool grown by the sheep men in the United States. This industry, since the end of World War II, has been reduced in size by more than one-half. Employment has dropped from 180,000 to 70,000 workers. Mills which provided

the sole or principal source of employment in many communities have been wiped out. Three hundred and sixteen mills have permanently closed.

But, what is the picture in relation to imports? It is conservatively estimated that imports this year will be 60 percent higher than last year, and will even exceed the record year 1960 by close to 25 percent.

Within this rising total are heavy and serious concentrations in yarns and in better fabrics. We have just received last month's import figures. They are the highest month on record in the history of wool textile imports into the United States.

Imports of apparel rose particularly sharply and these displaced not only the worker in the textile mill but the worker in the apparel plant. The administration has waited much too long to call an international conference to provide a basis for trade in wool textiles.

When the President announced his textile program, wool textile imports equaled about 19 percent of domestic production, but unless prompt and affirmative action is taken, imports this year will amount to 25 percent of domestic production.

The Post asserts that the industry is experiencing rising sales and high profits. There is no evidence of this.

In fact, only last week another mill in my own State of Rhode Island had to close down, displacing about 450 people.

I ask unanimous consent to have printed in the RECORD at this point a list of textile mill liquidations between January and August of this year, prepared by the Textile Workers Union of America, AFL-CIO.

There being no objection, the list was ordered to be printed in the RECORD, as follows:

TEXTILE WORKERS UNION OF AMERICA, RESEARCH DEPARTMENT, NEW YORK, N.Y.

Textile mill liquidations, January-August 1962

	Date	Product	Miscellaneous	Employees	Union
Massachusetts: J. P. Stevens & Co., Hampton Mills, Easthampton..... Ames Textile Corp., Sutton's Mills, North Andover.....	Announced March 1962..... February 1962.....	Dye and finish..... Woolens.....	Consolidating at North Star Mills in Maine.	315 200	TWUA
Connecticut: Burlington Industries, Princeton Knitting Mills, Watertown..... Parke-Davis & Co., Bay Division, Bridgeport.....	do..... do.....	Knit pile fabrics..... Surgical dressing.....	Moving to Greenwood, S.C.	500 140	
Rhode Island: New England Lace Mills, Pawtucket..... Burlington Industries, S. Blumenthal & Co., Valley Falls..... Berkshire Hathaway Co.: Bourne Mills Division, Tiverton..... Coventary Mill, Anthony.....	Equipment, auction in February 1962..... February 1962..... April 1962..... Announced August 1962.....	Levers laces..... Worsted and mohair yarns..... Cotton linings, sateens..... Broadwoven cottons.....	Purchased by Pontiac Weaving March 1962. Consolidated at other mills..... do.....	225 630 390	TWUA TWUA
New York: Jos. Bancroft & Sons, Albert D. Smith, Textile Division, West New Brighton..... Faith Mills, Averill Park..... Percy Kent Bag Co., Buffalo..... Mohasco Industries, Firth Carpet Co., Auburn..... Wilson Athletic Goods Manufacturing Co., Buffalo.....	February 1962..... June 1962..... do..... September 1962..... August 1962.....	Blank and shade cloth, industrial fabrics, fabrics..... Wool knit underwear..... Fabric bags..... Carpets and rugs..... Golf bags.....	Purchased July 1962 by Souhan Textiles..... do..... do..... do..... do.....	120 160 50 400 75	TWUA TWUA TWUA TWUA TWUA
New Jersey: Velvet Textile Corp., Lodi.....	March 1962.....	Finishing velvets.....	Consolidated at Glastonbury, Conn., plant.	45	TWUA
Pennsylvania: American Beauty Fabrics, Allentown..... Universal Dye Works, Philadelphia..... Ferdinand W. Mostertz & Sons, Philadelphia.....	April 1962..... June 1962..... July 1962.....	Cotton and Latex goods..... Dye sweaters and hosiery..... Upholstery fabrics.....	Forced out by highway construction. Consolidated at Greenville, S.C.	35 100 125	TWUA TWUA TWUA
Wisconsin: Rock River Woolen Mills, Janesville..... Chippewa Falls Woolen Co., Chippewa Falls.....	February 1962..... January 1962.....	Woolen fabrics..... Woolen garments.....	Consolidated at Brownwood, Tex.	200 150	TWUA TWUA
Alabama: Indian Head Mills, Cordova.....	Announced August 1962.....	Coarse cottons.....		760	TWUA

¹ January 1962.

² August 1962.

Mr. PASTORE. Curtailment, beginning about 2 months ago, is spreading throughout the industry. J. P. Stevens & Co. has announced curtailment in eight mills in North Carolina and South Carolina.

I have before me a newspaper. It is the Daily Mountain Eagle, which is published in Jasper, Ala., and is dated Friday, August 3, 1962. A big headline states, "Indian Head Mills Co. To Discontinue Operations at Cordova Manufacturing Firm."

The Indian Head mills in Cordova, Ala., have closed permanently. Two woolen mills in Massachusetts have closed. According to the press the Cone Mills in North Carolina have announced curtailment and Burlington industries

has reduced production. The press announced that Cannon Mills states that "curtailment is imminent." It is reliably reported to me that many wool textile mills have orders for only a few weeks of production and face curtailment or shutdown before this Congress adjourns.

The President's program is designed to solve a problem important not only to the 4 million workers in fibers, textiles and apparel, but to the other workers who supply the fuel, transportation, chemicals, machinery and other supplies and services needed by this basic industry.

This is not appeasement. This is not blackmail. This is a well thought out response to a basic national problem.

This is indicative of the responsible way in which the President will exercise the broad powers requested in the trade expansion bill.

Madam President, I am perfectly willing to take cognizance of the fact that the Washington Post is published in the Capital City where we do not have mills. We do not have manufacturing and other industrial concerns to an great extent. The chances are that the individual who wrote the editorial sits in his ivory tower and does not know the situation in other States of the Union. But if he would take the time to travel and to read some of the editorials that have been published in my State, he would have a better understanding of how serious the situation is.

Digest of CONGRESSIONAL PROCEEDINGS

OF INTEREST TO THE DEPARTMENT OF AGRICULTURE

OFFICE OF
BUDGET AND FINANCE

(For information only;
should not be quoted
or cited)

Issued Sept. 4, 1962
For actions of August 31, 1962
87th-2d, No. 157

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HIGHLIGHTS: Senate passed independent offices appropriation bill. Sen. Javits commended holding of World Food Congress. Sen. Moss urged enactment of Youth Conservation Corps bill. Senate passed measure for National School Lunch Week. Rep. Breeding inserted Secretary's statement regarding vote on wheat referendum.

SENATE

1. **INDEPENDENT OFFICES APPROPRIATION BILL, 1963.** By a vote of 65 to 5, passed with amendments this bill, H. R. 12711 (pp. 17247-63, 17266-73, 17278-90). Conferees were appointed (p. 17290). By a vote of 14 to 68, rejected an amendment by Sen. Young, O., to strike out the item of \$93,800,000 for construction of civil defense shelters in Federal buildings and provide, instead, \$10,000,000 for civil defense research studies (pp. 17258-63). The committee report includes the following statement regarding limitations on indirect expenses of research projects for agencies included in this bill:

"Section 304 of the General Provisions of the act as passed by the House limits the payment of indirect expenses in connection with research projects to a maximum rate of 25 percent of the direct costs. This limitation is applicable to research projects supported by grants. The committee strongly supports the action of the House in establishing a maximum rate of 25 percent since it will permit agencies, such as the National Science Foundation, to approve the payment of indirect costs on the basis of a flat rate percent which is equitable to both the Federal Government and the colleges and universities. The committee feels that the current flat rates being used by agencies should be adjusted

so that colleges and universities will be reimbursed for indirect expenses in connection with research projects at a flat rate which is a reasonable approximation of average costs."

2. SCHOOL LUNCH WEEK. Passed with amendment S. J. Res 211, to provide that the week beginning on the second Sunday of October each year shall be designated as National School Lunch Week. p. 17295
3. YOUTH CONSERVATION CORPS. Sen. Moss urged enactment of legislation, during this session of Congress, to provide for the establishment of a Youth Conservation Corps. p. 17307
4. WORLD FOOD CONGRESS. Sen. Javits commended the World Food Congress to be held in Washington, D.C., in June 1963, and praised the U. N. Food and Agriculture Organization "as one of the oldest and most effective organizations of the United Nations." pp. 17243-4
5. TAXATION. Continued debate on H. R. 10650, the proposed Revenue Act of 1962. pp. 17232-43, 17300-06
6. MINERALS. Conferees were appointed on H. R. 10566, to provide for the withdrawal and orderly disposition of mineral interests in certain public lands in Pima County, Ariz., and H. R. 8134, to effect a statutory withdrawal of certain former Taylor Grazing Act lands near Phoenix, Ariz., from all forms of entry under the public land laws. House conferees have already been appointed on these bills. p. 17246
7. SAFETY. Passed without amendment S. J. Res. 222, to provide for the designation of the period Oct. 1962 to Oct. 1963 as National Safety Council Fiftieth Anniversary Year. p. 17299
8. COURTS. The Judiciary Committee reported with amendments H. R. 1960, to amend title 28 of the U. S. Code relating to the jurisdiction of the U. S. district courts (S. Rept. 1992). p. 17314
9. NOMINATION. Received the nomination of Willard Wirtz to be Secretary of Labor. p. 17315
10. ELECTRIFICATION. Sen. Metcalf criticized the electric power rates of the Montana Power Company as "exorbitant", and inserted several items to support his position. pp. 17311-4
11. ADJOURNED until Tues., Sep. 4. p. 17315

HOUSE

12. WHEAT. Rep. Breeding inserted a statement by Secretary Freeman regarding the wheat referendum which says in part, "I would interpret this referendum as a specific demand for better action on farm legislation than we have seen to date." p. 17223
13. PUBLIC WORKS. Rep. Gross objected to returning S. 2965, the public works bill, to the House in order to make a technical correction in the House amendments. pp. 17214-5
14. APPROPRIATIONS. Received the conference report on H. R. 11151, the legislative appropriation bill (H. Rept. 2316). pp. 17213-4, 17230

~~PRIVATE BILLS AND RESOLUTIONS~~

~~Under clause 1 of rule XXII, private bills and resolutions were introduced and severally referred as follows:~~

~~By Mr. HUDDLESTON:~~

~~H.R. 13048. A bill for the relief of Dimitrios~~

~~Bountouvas; to the Committee on the Judiciary.~~

~~By Mr. McFERRIN:~~

~~H.R. 13049. A bill for the relief of Mrs. Olga Bernice Bramson Gilfillan; to the Committee on the Judiciary.~~

~~H.R. 13050. A bill for the relief of the heirs of Darva Calazans and others; to the Committee on the Judiciary.~~

~~By Mr. TOLL:~~

~~H.R. 13051. A bill for the relief of Wallace J. Knerr; to the Committee on the Judiciary.~~

Senate

FRIDAY, AUGUST 31, 1962

The Senate met at 10 o'clock a.m., and was called to order by the President pro tempore.

The Chaplain, Rev. Frederick Brown Harris, D.D., offered the following prayer:

O God, whose word is hidden in the framework of the world, which shines in the mind of man, and is made flesh in the Holy One who unveils Thy heart: We can know Thee only in part, as in a glass darkly; but we know what goodness is, and we believe that Thou art good; we know what justice is, and we believe that Thou art just; we know what love is, and we believe that Thou art love, and that that love will not let us go.

Help us to yield our flickering torch to Thee, to give Thee back the life we owe, that in Thine ocean depths its flow may richer, fuller be.

May new days bring new visions of Thy truth, new surprises of Thy love, and an ampler service to our fellow men. May our homes be more hallowed, our work more sacramental, as the life in Thee unveils to us its worth and its wonder.

We ask it in the name of Jesus Christ, our Lord. Amen.

THE JOURNAL

On request of Mr. SMATHERS, and by unanimous consent, the reading of the Journal of the proceedings of Thursday, August 30, 1962, was dispensed with.

MESSAGES FROM THE PRESIDENT

Messages in writing from the President of the United States were communicated to the Senate by Mr. Miller, one of his secretaries.

EXECUTIVE MESSAGES REFERRED

As in executive session,

The PRESIDENT pro tempore laid before the Senate messages from the President of the United States submitting sundry nominations, which were referred to the appropriate committees.

(For nominations this day received, see the end of Senate proceedings.)

COMMITTEE MEETINGS DURING SENATE SESSION

On request of Mr. SMATHERS, and by unanimous consent, the following subcommittees were authorized to meet during the session of the Senate today:

The Permanent Subcommittee on Investigations, of the Committee on Operations.

The Subcommittee on Arts, of the Committee on Labor and Public Welfare

REVENUE ACT OF 1962

The PRESIDENT pro tempore. The Chair lays before the Senate House bill 10650, the Internal Revenue Act of 1962.

The Senate resumed the consideration of the bill (H.R. 10650) to amend the Internal Revenue Code of 1954 to provide a credit for investment in certain depreciable property, to eliminate certain defects and inequities, and for other purposes.

The PRESIDENT pro tempore. The question is on agreeing to the McCarthy amendment as a substitute for section 12, relating to controlled foreign corporations.

The time, until 11:30 a.m., is to be equally divided, and controlled by the Senator from Minnesota [Mr. McCARTHY] and the Senator from Oklahoma [Mr. KERR].

Mr. SMATHERS. Mr. President, I yield 2 minutes to the Senator from Nebraska [Mr. CURTIS].

The PRESIDENT pro tempore. The Senator from Nebraska is recognized for 2 minutes.

Mr. CURTIS. Mr. President, one of the erroneous arguments advanced by the supporters of punitive taxation against American firms investing abroad is that such investment "exports American jobs." Supposedly whenever an American firm builds a plant and produces abroad, it replaces with foreign-made goods products which otherwise would have been exported from the United States to that foreign market. Furthermore, American firms are supposed to go abroad to take advantage of "cheap labor" and "lower taxes" and to import foreign-made products into the United States.

Both these charges are absolutely false. Not a single shred of evidence was introduced into the House or Senate hearings on the tax bill to back them up. The reason why no evidence was introduced is that little, if any, exists, and plenty of evidence proves the opposite to be true.

U.S. private foreign investment does not export jobs. It creates jobs for American workers here in the United States.

The Senate Commerce Committee recently studied this very matter. Its report, "The United States and World Trade—Challenges and Opportunities," June 26, 1961, states:

U.S. foreign investment does not on the whole—certainly not on balance—mean the export of American jobs any more than the introduction of labor-saving equipment at home really destroys employment. American companies manufacturing abroad are not, necessarily, making things which displace American exports or which are sent back to the United States to take the place

of American goods in the home market. * * * So far as Europe is concerned, it appears that in the great majority of cases foreign plants have been established or expanded to reach a market which could not reasonably be served through normal exportation.

U.S. firms invest abroad only if they cannot sell their proper share of a foreign market through exports. Those that can export profitably do so until they begin to lose markets to local foreign manufacturers. When those foreign firms, taking advantage of local economics, begin to produce and outsell the exports of American firms, the American firm must either give up the market or manufacture locally in competition. The Commerce Committee's report emphasizes:

• The question, therefore, is really not whether these products will be manufactured abroad but by whom.

Stated in another way, U.S. foreign manufacturing investment comes only after export sales are lost or are about to be lost or when exports are not really possible in the first place. The U.S. firm that invests abroad must invest abroad or not have any share of the market.

Foreign manufacturing investment saves American jobs that might otherwise be lost to a foreign-owned competitor in a foreign market. The foreign plant will, in most cases, buy its capital equipment, its semimanufactured components, and its raw materials from the United States—and in each case increase the number of American jobs. The existence of an American-owned subsidiary will also lead to an increase in U.S. exports of allied products not manufactured abroad by the investor—goods which might otherwise not be permitted entry or which would not normally be exported because of lack of sufficient volume of themselves. Finally, the existence of the foreign plant will cut the volume, productivity, and profit of foreign competitors and thus tend to keep foreign manufacturers out of the American market.

The Commerce Department has provided dramatic figures to show just what the job-creating or job-loss effect of foreign manufacturing investment actually is. U.S.-owned manufacturing subsidiaries in Canada and Western Europe had total sales of \$18.2 billion in 1960. Of that massive figure, only 1.4 percent or \$259 million represented imports into the United States. Even assuming that those same products could have been manufactured competitively in the United States, a very doubtful assumption for the overwhelming percentage of them, they displace only 30,000 jobs. But the same

subsidiaries that sold \$259 million worth of foreign-made goods in the United States, purchase \$1.25 billion worth of goods from the United States—creating or maintaining more than 100,000 jobs for American workers. The effect of U.S. private foreign investment in manufacturing thus creates 70,000 jobs. These are the facts, substantiated by the Department of Commerce and the Senate's own committee. Yet, I repeat, not one shred of evidence has been given substantiating the false charge that foreign manufacturing investment "exports" jobs.

Look at specific case examples showing how individual U.S. corporations that have invested heavily abroad during the past decade have increased their own exports tremendously. Theoretically the job-export allegation should show that those companies investing heavily abroad have lost exports because of the expansion of foreign plants.

Consider the Clark Equipment Co. In 1955, when this firm had no foreign investment, it exported \$5.5 million worth of goods. By 1961, it had a chain of foreign affiliates, and exports reached \$23 million. Taking into account the sales of the foreign affiliates, Clark's foreign sales jumped to \$88 million. In 1955, 1 out of 21 of this company's employees were involved in foreign business; in 1961, the figure jumped to 1 out of 9.

Consider the Beckman Instruments Co. In 1959 U.S. exports were \$4.3 million, and production of foreign plants was \$1.4 million. The estimate for 1962 show a jump in U.S. exports to \$8.9 million and in foreign production to \$3.2 million. But more interesting are the changes in the firm's employment figures. On July 1, 1958, Beckman employed 2,628 American and 307 foreigners. On January 1, 1962, it had 4,468 American employees and 543 foreign ones. Production by foreign plants more than doubled, but U.S. exports did the same thing, and 1,840 U.S. jobs were created in the process.

Two more good examples: American Machine & Foundry began investing in foreign manufacturing plants in 1956. Now it has 10 units abroad. Yet, exports rose from \$3.9 million in 1956 to \$16 million in 1961. And Willys Motors in the 1955-60 period invested \$10.38 million abroad, but the overwhelming percentage of it, \$7.93 million, is in the form of American-made machinery. During that period, Willys exported \$151.2 million worth of component parts to its foreign assembly plants, yet its export of built-up vehicles and of spare parts remained practically constant.

One of the most significant cases is H. J. Heinz. Many years ago Heinz introduced canned baked beans to England. Today its plant each year remits as dividends more dollars than were originally invested in it and also purchases each year raw beans from the United States in a value greater than the original investment. The importance of foreign investment by American food processing firms cannot be underestimated. For example, Heinz in the 10

years ending June 1961, invested \$10.7 million in equity and/or loans to foreign subsidiaries. At the same time its foreign subsidiaries purchased \$36.7 million of American-grown agricultural products.

These case studies could be multiplied over and over again. A host of other American firms could all be given as examples of corporations that have invested heavily in recent years in foreign markets and have at the same time, increased their U.S. exports and at the same time increased the U.S. work force mightily. Practically every American company that has invested in foreign plants has sharply boosted their exports and work force. Practically every American company that has invested heavily abroad has created American jobs where none before existed.

The foreign provisions of the Revenue Act of 1962 will seriously damage American private investment and by so doing will slow the creation of new jobs for America's farmers and workers—these will go to foreigners when foreign manufacturers put American firms out of business in foreign and domestic markets. The foreign provisions of the act must be deleted.

Mr. President, either the top leadership in the Treasury do not understand the American economy, or they are ignoring the facts of life as presented by all the witnesses before the House Ways and Means Committee and before the Senate Finance Committee.

I express the hope that the President will call in some leadership that will be in tune with the American idea of business and can be more realistic about these things.

Mr. GORE. Mr. President—

Mr. SMATHERS. I yield 1 minute to the Senator from Tennessee.

The PRESIDENT pro tempore. The Senator from Tennessee is recognized for 1 minute.

Mr. GORE. Mr. President, to show how utterly unsupportable are the statements and conclusions which the distinguished junior Senator from Nebraska [Mr. CURTIS], has just uttered, I ask unanimous consent to have printed at this point in the RECORD an article from the Anglo-American Business Journal.

The PRESIDENT pro tempore. Is there objection?

Mr. CURTIS. Mr. President, reserving the right to object—

Mr. SMATHERS. Mr. President, we are proceeding under controlled time; so I yield 1 more minute to the Senator from Tennessee, in order that the Senator from Nebraska may ask him a question.

The PRESIDENT pro tempore. The Senator from Tennessee is recognized for 1 more minute.

Mr. CURTIS. No, Mr. President; I was reserving the right to object.

I wonder whether the distinguished Senator from Tennessee, in his statement that my utterances were ridiculous and unfounded, is disregarding the preponderance of the evidence submitted by American businessmen to the Senate Finance Committee.

Mr. GORE. I have regarded all the evidence, not merely the special pleading which seems to have so impressed my friend, the Senator from Nebraska.

Mr. CURTIS. Oh, Mr. President, I think every time a taxpayer appears, he is a special individual. The people back home have an interest in our Government, and their interest is worth respecting.

Mr. GORE. The parties referred to are not people back home; they are people who are interested in tax dodging by foreign investments.

Mr. CURTIS. I do not know whether I shall object or not, Mr. President, to the Senator's request. But I wish to point out that a tax dodger is someone who earns income in the United States, and, by a gimmick, "hikes" it abroad, to avoid taxes.

Mr. GORE. Well, the pending bill makes that possible.

Mr. CURTIS. It does not. That is the trouble with it; it gives to the tax dodger every benefit of the honest operating company.

Mr. President, I withhold objection.

The PRESIDENT pro tempore. Is there objection to the request of the Senator from Tennessee?

There being no objection, the article was ordered to be printed in the RECORD, as follows:

AMERICAN EXPORTS FROM BRITAIN—A NEW SURVEY OF 120 U.S. MANUFACTURING SUBSIDIARIES OPERATING IN THE UNITED KINGDOM

American manufacturing enterprises based in the United Kingdom are continuing to make solid and constructive contribution to Britain's export effort and payments balance.

This is the story that emerges from export performance data gathered by the American Chamber of Commerce in London from chief management executives of the leading American manufacturing subsidiaries in the United Kingdom. Results of a recent survey which included hard figures from 120 chamber member companies of American parentage show that 26 percent of them exported from 41 to 100 percent of their entire production during the first half of 1961.

Thirty percent of these American owned companies shipped 21 to 40 percent of their output abroad during the first 6 months of last year. The remaining 44 percent of the group sampled by the chamber sold up to 20 percent of their production in overseas markets.

Additionally, 15 firms reported that they estimated their contributions in indirect exports were of much greater importance to the British economy than the direct export figures indicate. These makers of components and subassemblies supply British customers whose products in turn are prime sellers in world market.

The majority of U.S. subsidiaries in this category estimated that inclusion of their indirect exports in their totals would be sufficient to more than double their direct export performance. Two companies which reported no direct imports noted that their entire production finds its way to export markets in this manner.

Proper evaluation of figures and percentages requires comparison to convey meaning, and it is by using a yardstick of past performance and by measuring against current available data on exports of British industry generally that the scope of American-financed contribution becomes significant.

In his 1954-55 study, "American Investment in British Manufacturing Industry"

(George Allen & Unwin, 1958), Prof. John H. Dunning, of the University of Southampton, revealed that 152 American manufacturing subsidiaries in the United Kingdom reported the following export performance: 26.2 percent of them exported 41 to 100 percent of their production; 41.3 percent sold 21 to 40 percent of output to foreign markets, and 32.5 percent recorded export sales up to 20 percent.

It can be assumed that many of the companies in the Dunning study are identical with those sampled in the chamber survey, although a number of firms in the current sample have been established during the past 8 years. This is worth noting because recently the United Kingdom Government has tended to relax its entry requirements for foreign direct investment in manufacturing enterprises. Formerly the dollar shortage in the United Kingdom made it mandatory that the prospective investor's product be a vital dollar saver on the domestic market and a prodigious seller overseas.

With easier entrance for the newcomer and with more affluent domestic consumers to be tapped by both the neophyte and the long-established companies, it might be expected that the current export graph would drop precipitously below the 1954 mark. This has not been the case.

Measured against contemporary performance of British industry generally, the American manufacturers in the United Kingdom appear to run slightly ahead of the current. The Federation of British Industries export supplement to "Industrial Trends Enquiry No. 12," released for publication on October 13, 1961, shows that 492 United Kingdom manufacturers with annual exports amounting to more than £10,000 line up in this manner: 12 percent deliver more than 50 percent of their output overseas; 28 percent export 25 to 50 percent; 31 percent sell 10 to 25 percent abroad; 17 percent export 5 to 10 percent, and 12 percent record export sales of less than 5 percent.

Comparable figures for the 120 American firms in the United Kingdom are: Exports over 50 percent, 19 percent of the companies; 25 to 50 percent, 29 percent of the companies; 10 to 25 percent, 36 percent of the total, and in the 5 to 10 and less than 5 percent categories, 5 and 10 percent of the companies, respectively.

Again, in the FBI inquiry it can be expected that a majority of the U.S. companies are included, but it should be remembered that the FBI includes among its members this country's largest concerns and its most formidable exporters. On the other hand, with the exception of a small minority of the U.S. financed companies, the American firms supplying information for the chamber study class themselves in the small to medium sized brackets. Notwithstanding this, American industry in Britain has been credited by numerous British authorities with employing nearly 1 in every 20 workers employed in United Kingdom manufacturing industry today.

Enlarging on this, Sir Miles Thomas, chairman of Monsanto Chemicals, Ltd., in a talk he gave at a chamber luncheon meeting in mid-1959, said:

"I wonder if any of you read some relevant and extremely interesting figures in the Times recently? There are roughly 400 U.S. subsidiaries and Anglo-American companies in the United Kingdom and they employ about 375,000 people. Impressive figures, but—and it's a very considerable but—these people only represent about 4 percent of our total labor force. And the total value of the output of those 400 or so companies, at around £1,200 million, is about 5.5 percent

of the gross output for all United Kingdom manufacturing industry for 1957.

"A further fact was that, at the present time, U.S. representation in United Kingdom industry is confined almost entirely to industries supplying products which were first developed on a significant scale in the United States, if not actually discovered there.

"Let me take three more points, all from the same source. Between 1950 and 1957 U.S. subsidiaries and Anglo-American firms accounted for something like 7.5 percent of the net capital expenditure of all British manufacturing industry. Secondly, such firms have access to the benefits of more research and development than all United Kingdom industry (on private account) combined. Finally, these firms currently supply between 10 and 12 percent of all United Kingdom manufacturing exports and one-third of the exported goods commercialized within the last two decades."

Further emphasis on the impact of the contribution of direct American investment on the British economy can be drawn from a statement made recently by Carl Gilbert, chairman of the Gillette Co., of Boston, at the convention of the National Foreign Trade Council in New York. He stated that of the 3 million overseas workers employed by U.S. industry only about one in every hundred is a U.S. citizen. Rough calculations in the United Kingdom show that this ratio is, for Britain, entirely unrealistic. The British labor participation, from the managing director's desk to the apprentice's bench, in American manufacturing industry in the United Kingdom comes much nearer complete saturation.

Returning to data compiled from answers to the chamber's questionnaire, two outstanding trends come to light.

1. Additional manufacturing facilities established by the U.S. parent within the Common Market or in other areas where various conditions make local manufacture unavoidable have cut into exports from a number of the United Kingdom subsidiaries; and

2. Domestic United Kingdom sales have in numerous cases increased sufficiently to downgrade export percentage figures, although actual exports have remained static, or even improved.

Consolidation of answers to the questionnaire which asked respondents for a simple "percentage figure which your exports represented in relation to your total sales for the first half of 1961 compared with the corresponding period of 1960, together with two or three main areas of their destination, e.g., the Far East, Middle East, Western Hemisphere, and Western Europe," gave the following picture:

A total of 23 concerns directly exported between 50 and 100 percent of their total sales in each of the two periods (January to July 1960, 1961). These companies manufacture specialized lines of capital goods and consumer durables for which there is a relatively limited market in the United Kingdom. They possess either their own world marketing organizations or highly qualified distributors. The majority of them—15—registered increases in their export sales for the 1961 period; the increases varied from 13 to 0.4 percentage points.

The remaining companies in this group indicated decreases in their export business during the first half of 1961. One of the causes mentioned being the type of business involved (often consisting of large contracts) does not lend itself to meaningful comparisons between given periods. In some cases the total volume of exports was up in the 1961 period, although the percentage was less, compared with 1960.

The destinations of the exports of the companies in the 50 to 100 percent category were worldwide, the percentages by markets having varied considerably between the two periods. In the rough order of importance the destinations were Europe, Far East, and Australia, South America, Middle East, and Africa.

The group showing exports ranging between 25 and 50 percent in each of the 2 periods consisted of 35 companies. Of these, 19 indicated increases of a few points in most instances during 1961. The decreases shown by the balance of the group were also of minor magnitude, while the percentage of total sales was lower in some cases during the 1961 period, the actual amounts were greater. Again the marketing areas were more or less worldwide, that is, Europe, South America, the Far East, Middle East, Africa, and North America.

The largest group in the sample comprised the 43 companies which exported from 10 to 25 percent of their total sales in the 1961 period. Barring a few exceptions these concerns were also in the same category in 1960. The export sales of 22 of the companies increased in the 1961 period; the highest of an individual company having been from zero in 1960 to 17 percent of total sales in 1961. The smallest increase recorded was from 20.2 percent in 1960 to 20.4 percent in 1961.

The firms reporting reduced sales in 1961 numbered 19, the reductions in most cases being small. Reasons given for some of the reductions were the opening of other overseas plants by the parent companies concerned, due to the unavoidable need in many countries to set up local manufacturing operations. Here again several of the companies confided that in actual fact there were appreciable increases in the export sales during the 1961 period, though the percentages were slightly diminished owing to a proportionately slightly greater increase in the consolidated sales. The percentage of exports to the several areas of destination varied considerably in many cases, but in general the principal areas were Euproe, Far East, Middle East, Africa, and the Americas.

There were only seven companies in the group exporting from 5 to 10 percent of their total sales, two of these enterprises having reported decreases in such sales during the 1961 period. One of the companies showing a decrease explained that the relatively low percentage in the 1961 period under review was due to the fact that an associated firm in a Common Market country began to supply that area. The other company stated that while its export business has been growing, the lower percentage export figure in January-July 1961 was chiefly due to unusually high exports in the corresponding period of 1960. Destinations in general were Europe, the Middle East, and Far East.

The group having less than 5 percent of direct export sales consisted of 12 concerns, 4 of which reported decreases in the 1961 period. The differences in all cases were small, and the areas of destination were Middle East, Africa, Europe, and the Far East. A few of these companies have been established in the United Kingdom only a short while, and others reported the fact that sales in the United Kingdom materially affected the export figures.

Finally, an aggregate of 70 companies reported export sales running at 20 percent of total sales during both periods; 53 firms showed export business ranging from 25 to 100 percent in the first half of both 1960 and 1961, and no less than 39 U.S. subsidiaries stated that their export shipments were at the level of 40 percent or more of their output during both periods in question.

Export performance

[All figures in percentages]

**120 U.S. MANUFACTURING SUBSIDIARIES IN
BRITAIN, 1961**

Exports.....	To 21	20 to 40	41 to 100
Companies.....	44	30	26

**152 U.S. MANUFACTURING SUBSIDIARIES IN
BRITAIN, 1954**

Exports.....	To 20	21 to 40	41 to 100
Companies.....	32.5	41.3	26.2

492 UNITED KINGDOM MANUFACTURERS, 1961

Exports....	To 5	5 to 10	10 to 25	25 to 50	50 to 100
Companies....	12	17	31	28	12

120 U.S. MANUFACTURING SUBSIDIARIES, 1961

Exports....	To 5	5 to 10	10 to 25	25 to 50	50 to 100
Companies....	10	5	36	29	19

Mr. SMATHERS. Mr. President, I suggest the absence of a quorum, and I ask unanimous consent that the time required for the quorum call be charged equally to both sides.

The PRESIDENT pro tempore. Without objection, it is so ordered; and the clerk will call the roll.

The legislative clerk proceeded to call the roll.

Mr. GORE. Mr. President, I ask unanimous consent that further proceedings under the quorum call be dispensed with.

The PRESIDING OFFICER (Mr. PROXMIER in the chair). Without objection, it is so ordered.

Mr. GORE addressed the Chair.

The PRESIDING OFFICER. Does the Senator from Florida yield the Senator from Tennessee time?

Mr. GORE. May I have 4 minutes?

Mr. SMATHERS. I yield 4 minutes to the Senator from Tennessee.

The PRESIDING OFFICER. The Senator from Tennessee is recognized for 4 minutes.

Mr. GORE. Mr. President, indignant editorials are sweeping across the country. Telegrams are beginning to arrive. I hope the country is awakening to what is happening to the public interest in the course of consideration and action on the pending tax bill.

I should like to read a portion of an editorial in the Washington Post of today which deals with the expense account amendment. The editorial is entitled "The Tax Chiselers' Friends":

The tax chiselers who fail to report dividend and interest income and those privileged few who enjoy everything that a fat "business" expense account can buy should give public thanks to the U.S. Senate. They have received a gift which may cost the Treasury—and those of us who are not in a position to share the loot—as much as \$968 million.

There is ample evidence that business expense accounts have been employed as a device for padding costs and providing a tax-

free supplement to the incomes of corporate executives and independent proprietors. Every expense-account dollar received by a person in the 50-percent tax bracket is the equivalent of \$2 of taxable income, and the Treasury estimates that the expense-account loopholes in the present tax laws cost it at least \$250 million a year. By allowing deductions for entertainment that is merely "associated" with business the Senate's bill will permit the Treasury to recoup no more than \$60 million.

Mr. President, I should like to read a portion of an editorial in today's New York Times which deals with the expense account amendment. The title of the editorial is "The Mutilated Tax Bill."

Although the Senate has not yet completed its consideration of the tax revision bill, there is no doubt about the shape in which it will emerge. It is accepting the Finance Committee's handiwork, which produced a mutilated and distorted version of the administration's original bill.

*** Instead of cutting out business entertainment expenses, which would also have added to the Treasury's revenues, it proposes to go easy on deductions.

Mr. President, I have read the particular sentences of the editorials dealing with expense accounts, but I ask unanimous consent that the texts of both editorials be printed in the RECORD at the conclusion of my remarks.

The PRESIDING OFFICER (Mr. YOUNG of Ohio in the chair). Is there objection to the request by the Senator from Tennessee? The Chair hears none, and it is so ordered.

(See exhibit No. 1.)

The PRESIDING OFFICER. The time of the Senator from Tennessee has expired.

Mr. GORE. Mr. President, may I have 1 more minute?

Mr. SMATHERS. I yield the Senator an additional minute.

The PRESIDING OFFICER. The Senator from Tennessee may proceed for an additional minute.

Mr. GORE. Mr. President, the committee amendments are now to be considered original text and the bill is open to amendment, so there will be a rebut on the expense account amendment. There will be a rebut between the public interest and the special interests.

I invite Members of both parties to join. I invite President Kennedy to enter the ring on behalf of the American people and against the special interests that want to preserve the right to clothe their personal expenses with a business outlay and thus continue the widespread abuse of expense accounts.

EXHIBIT 1**THE TAX CHISELER'S FRIENDS**

The tax chiselers who fail to report dividend and interest income and those privileged few who enjoy everything that a fat "business" expense account can buy should give public thanks to the United States Senate. They have received a gift which may cost the Treasury—and those of us who are not in a position to share the loot—as much as \$968 million.

In defeating the withholding tax on dividend and interest income the Senate rejected a plan to enforce effectively existing laws, and not a radical new fiscal device. The Treasury is presently being defrauded of \$778 million a year in taxes on unreported

dividends and interest payments, and yet only 20 Senators voted to enforce the law and place dividend and interest payments on the same footing with wages and salaries from which taxes are withheld.

There is ample evidence that business expense accounts have been employed as a device for padding costs and providing a tax-free supplement to the incomes of corporate executives and independent proprietors. Every expense-account dollar received by a person in the 50-percent tax bracket is the equivalent of \$2 of taxable income, and the Treasury estimates that the expense-account loopholes in the present tax laws cost it at least \$250 million a year. By allowing deductions for entertainment that is merely "associated" with business the Senate's bill will permit the Treasury to recoup no more than \$60 million.

If anything can be said in defense of the Senate's sorry performance it is that by refusing to close loopholes it has reduced tax revenues at a time when they have been inhibiting economic growth. Such an apology, however, is reminiscent of Bernard Mandeville's "Fable of the Bees" (1714) in which he argues that "private vices" are in fact "public benefits." Several lines of an earlier doggerel which forms an introduction to that work are especially appropriate:

Such were the blessings of that state;
Their crimes conspir'd to make them great;
And virtue, who from politics
Has learn'd a thousand cunning tricks,
Was, by their happy influence,
Made friends with vice: And ever since,
The worst of all the multitude
Did something for the common good.

THE MUTILATED TAX BILL

Although the Senate has not yet completed its consideration of the tax revision bill, there is no doubt about the shape in which it will emerge. It is accepting the Finance Committee's handiwork, which produced a mutilated and distorted version of the administration's original bill.

Instead of a relatively simple tax credit incentive for business spending on new plant, the Senate has approved a complicated provision that is much less satisfactory. Instead of automatic withholding of interest and dividend income, which would have helped to offset the loss stemming from the tax credit, it has passed a weak provision requiring only the reporting of such payments. Instead of cutting out business entertainment expenses, which would also have added to the Treasury's revenues, it proposes to go easy on deductions. Instead of plugging up loopholes on earnings abroad, it is still leaving escape hatches.

The House bill, itself a pale facsimile of the administration's recommendations, would not involve the loss of revenues that the Senate is willing to accept. So when it goes into conference, the White House and its supporters in Congress will have to seek a compromise that would tighten the Senate's proposals and add to the tax take. The incentive credit is needed most, and the bill should be approved on that account alone, yet every attempt must be made to make up for the loss that will be incurred.

This is important because the administration's promise to undertake major tax reforms will include measures to increase taxes. Its failure to obtain even moderate increases through revision of the tax structure, which it viewed as a forerunner of a thorough overhaul, illustrates the magnitude of the task before it. Despite all its defects, the present bill has one merit. It is the first step, admittedly feeble and halting, on the road to tax reform.

Mr. MCCARTHY. Mr. President, I have, of course, listened with some interest to the Senator from Tennessee as he has quoted from editorials which indi-

cate that those of us who favor the position of the committee are in favor of tax chiseling. The statement from the editorial is somewhat consistent with the statements in supplemental and minority views, as well as statements which have been made on the floor of the Senate with regard to the action taken by the Finance Committee, to the end that those of us, for example, who were not in favor of withholding were condoning tax evasion.

I should like to believe that those who use words like "condoning tax evasion" are not quite sure as to the exact meaning or connotation of the word "condone," that they are not really charging that we are protecting tax evaders or that we approve such action. If this were the case, I suppose I should have to make a kind of countercharge, since the testimony before our committee was that in addition to the income from interest and dividends which is not reported and therefore not subjected to a tax there is some additional \$20 billion of income received in this country which is not reported for tax purposes. I could charge, therefore, that because the Senator from Tennessee has not recommended some kind of withholding provision or some other kind of device by which we could get at that \$20 billion, he is condoning tax evasion.

Certainly I would not make that charge, because I know the Senator could make the very proper answer that if he were satisfied that there was a reasonable and workable method by which we could get at that \$20 billion and see to it that the taxes owed on it were paid—some of it is wages, some of it is the ordinary profit of the self-employed, some of it is in the form of fees paid to professional men—he would be in favor of such a method. But I think he would say that in his judgment there is no workable way at the present time by which we could get at that income.

We could, I suppose, appoint an Internal Revenue Service man to keep books for every doctor and businessman in America. That would be a workable method. Probably it would be an effective method. But it would be an unreasonable approach to the problem.

So I do not charge that the Senator from Tennessee is condoning tax evasion merely because he has made no proposal by which we might reach out to the self-employed who, according to the Treasury Department reports, have \$20 billion of income not reported for tax purposes.

I think the Senator ought to allow those of us who have decided that the withholding approach is not feasible, is not as clearly workable as some people say, the right to say that we ought to try the reporting method as an intermediate device, at least. If that does not work, he can then come before the Senate to say, "Very well. You have tried it. There is some limitations on the withholding approach, but I think, on balance, it ought to be tried."

But to say in the report that we condone tax evasion because we do not support or oppose a particular method, I think is to be somewhat unfair to the members of the Finance Committee.

Mr. SMATHERS. Mr. President, will the Senator yield?

Mr. McCARTHY. I yield to the Senator from Florida.

Mr. SMATHERS. I wish to associate myself with the remarks made by the able Senator from Minnesota.

There are 130 million savings accounts in America. These savings are in insurance policies, in savings and loan institutions, commercial banks, as well as in credit accounts.

I do not believe that those people are all cheaters, chisellers, tax avoiders, or tax dodgers. The Senator from Tennessee can call them that if he wishes to, but the Senator from Florida does not call them that. These people had no knowledge that they were required to report such income for tax purposes. Many of these accounts are small. No one is condoning tax avoidance. The notification system will prove adequate to inform these individuals of the amount of interest they receive which should be reported on their returns for tax purposes.

I think, in regard to this problem, as we have said previously and as the Senate Finance Committee believes, if these people know they are to report the \$8 of interest they get a year for tax purposes, the majority of them will do so.

The Senator can speak for his constituents in Tennessee. So far as I am concerned, I do not charge the savers in Florida with being tax chisellers and tax dodgers, even though the Senator from Tennessee might wish to say that about his own constituents, and even though the Washington Post might wish to say that about the people of the District of Columbia.

I associate myself with the remarks by the Senator from Minnesota.

Mr. McCARTHY. Mr. President, I add, with reference to the action taken by the committee with respect to expense accounts, that this is a very difficult area in which to legislate. The basic law, I think, establishes quite clearly that no businessman is to charge off as a business expense what is not a business expense.

The significant action taken by the committee, I think, was to reject the Cohan rule, under which the burden of proof with regard to deductions was placed on the Government, and to turn it back and to say that the businessman who takes a deduction must justify it, himself. This, together with existing practices and existing regulations, and some minor changes in the language in the amendment as the committee recommended it to the Senate, I think will give to the Internal Revenue Service genuine and effective weapons to be used to get at those who are really tax dodgers, those who are not paying the taxes on the income on which they should pay taxes, and those who are taking deductions which are not legal, which are not justified, which are not warranted.

Certainly I think the intent of the committee—and that intent will be sustained by the Senate, I believe—is quite clear. With proper and thorough administration, the worst abuses will be eliminated.

Mr. GORE. Mr. President, will the Senator yield?

Mr. McCARTHY. Yes, I yield to my friend from Tennessee.

Mr. GORE. The "rebut" which I have suggested will be on the provisions in the bill which would permit the continuation of expense account abuses. Lest there be some mistake about the existence of abuses, I wish to call the Senator's attention once again to the fact that in the first tax message to the Congress by President Kennedy he said:

In recent years widespread abuses have developed through the use of the expense account.

He went on to say:

This is a matter of national concern, affecting not only our public revenues, our sense of fairness and our respect for the tax system, but our moral and business practices as well. This widespread distortion of our business and social structure is largely a creature of the tax system, and the time has come when our tax laws should cease their encouragement of luxury spending as a charge on the Federal Treasury. The slogan "It is deductible" should pass from the scene.

He said also:

In other cases deductions are obtained by disguising personal expenses as business outlays.

What I have pointed out and proven unmistakably is that the provision of the Senate amendment, as described in the Senate committee report, permits continuation of expense account abuses. Neither the ranking Republican member, nor the Senator in charge of the bill, the Senator from Oklahoma [Mr. KERR], would defend the provision of the report but it has now been voted into the bill. It would permit continuation of the very kind of expense account abuses of which the President complains and described as a national concern. I shall offer an amendment to correct the bill in these regards. I invite the President, and every Democrat and every Republican Senator to choose sides and determine whether he wants to defend the public interest against these special interest provisions now in the bill.

Mr. McCARTHY. I am glad the Senator has given me the simple choice between the public interest and special interest. That is the choice he has been giving to us for about 2 months. I think I have been making my choices on the basis of a somewhat responsible conscience and as one who is reasonably informed and is as much concerned about corruption in Government or corruption in our country as the Senator from Tennessee.

I do not say that he has proven his case with the absoluteness that he declares he has proven it. The subject has been considered in the committee and it is now being considered on the floor of the Senate. I will be glad to have another vote on the issue.

The debate has reached the point at which the best commentary I can recall is that of Mr. Dooley, a political commentator who lived back around the beginning of this century. He wrote some rather good things on life in America and American politics. One of his essays was entitled "National Housecleaning."

Hennessey opened the discussion, saying:

It looks to me as though this country was goin' to th' divvie.

Dooley said:

Put down that magazine."

I might have said to my friend the Senator from Tennessee, "Will you put down the New York Times and the Washington Post? Put aside those editorials."

Mr. Dooley then said:

Now d'ye feel betther? I hought so.

Then the story continues for several pages. Finally the conversation got around to the question of housecleaning. I should like to quote for the RECORD what Mr. Dooley had to say upon that subject:

"It reminds me, Hinnissy, iv th' time I lived at a boardin'-house kept be a lady be th' name iv Doherty. She was a good woman, but her idee iv life was a combination iv pneumony an' love. She was niver still. Th' sight iv a spot on th' wall where a gintelman boorder had laid his head after dinner would give her nervous prostration. She was always polishin', scrubbin', sweepin', airin'. She had a plumber in to look at th' dhains twice a week. Fifty-two times a year there was a revolution in th' house that wud've made th' Czar iv Rooshya want to go home to rest. An' yet th' house was niver really clean. It looked as if it was to us. It was so clean that I always was ashamed to go into it unless I'd shaved. But Mrs. Doherty said no; it was like a pig-pen. 'I don't know what to do,' says she. 'I'm worn out, an' it seems impossible to keep this house clean.' 'What is th' trouble with it?' says he. 'Mad-am,' says me frind Gallagher, 'wud ye have me tell ye?' he says. 'I wud,' says she. 'Well,' says he, 'th' trouble with this house is that it is occupied entirely be human bein's,' he says. 'If 'twas a vacant house,' he says, 'it cud aisily be kept clean,' he says.

I would suggest that the Senator from Tennessee, who is quite properly concerned about what he thinks is corruption and what in some cases is real corruption and, at least in his judgment, the lack of regard for what he considers to be the facts and the failure of the rest of the Senate to respond to that pressing need, that in his spare time he give some attention to Mr. Dooley.

Mr. GORE. Mr. President, will the Senator yield?

Mr. McCARTHY. I am glad to yield to the Senator from Tennessee.

Mr. GORE. I have enjoyed the portions of the delightful essay read by the distinguished, scholarly Senator from Minnesota. He read some very pertinent references to human beings, people, and house cleaning.

I am willing to put down the editorials. But what I wish to raise ever before the Senate concerning this issue is the public conscience. It must be outraged by the action of the Senate in approving an amendment which would permit a continuation of the widespread and scandalous abuses and tax avoidance through the "disguising of personal expenses as business outlays," as the President said.

It is not for the junior Senator from Tennessee to suggest a house cleaning. I am suggesting, not a house cleaning, but some soul searching on the part of the Members of this body, in which

the voice of the people is theoretically spoken. I am suggesting that the representatives of the people speak the true voice of the people. It is not the American people as a whole who benefit by the special gimmick of abuse of expense accounts. It is a privileged few, largely the corporate insiders who, as the President has said, disguise personal expenses with business outlays. It may well be that if Senators do not heed the public conscience, it may occur to the American people to do some house cleaning themselves. The junior Senator from Tennessee did not suggest it, but since the distinguished Senator has read that delightful literary gem, it might occur to the American people.

Mr. McCARTHY. It may well be, but I think it is a fair proposition that we should not be prejudiced by the Senator from Tennessee, who seems to have discovered that he is the voice of the people. He may have a special gift. I do not have this gift. There are some people who seem to have what the Scripture terms the power of discernment of spirits, or the reading of spirits, in that they understand and speak the will of the people. There are Members of the Senate who say they speak for the majority of the people of the country. I do not know how they have discovered that. On the other hand, I think it is best to proceed by examining a problem and by coming to a mastery of the many facts that are available, and on that basis to make a reasonable judgment.

That has been the procedure in the Finance Committee, to examine all the facts. I believe we are aware of the problem of the abuse of the expense account, and we have tried to give the Internal Revenue Service the kind of authority which we think we ought to give to them, and give it to them in a measure—not perhaps by way of arbitrary, absolute power, because there is always danger in handing over that kind of power to an executive agency—to give them, in other words, a reasonable extension of power, with some clarification of the bill, so that they can proceed in an intelligent way.

It was the intention of the majority of the committee to take action that will be effective.

It is rather distressing to find in the Senate that it is considered to be almost undemocratic to vote with the majority. I rather had the impression that it was one of the fundamental tenets of democracy that the majority position was to be given not only attention, but that it also was credited with some moral strength, and that it was accepted that if people were given information, there was enough good will, so that there would be progress toward a good society.

We have apparently reached the point where we must apologize for voting with the majority. It is as though by doing that we were violating the democratic processes.

Mr. GORE. Mr. President, will the Senator yield?

Mr. McCARTHY. I yield.

Mr. GORE. In the case of the expense account amendment an apology to the American people might well be in order.

Mr. McCARTHY. I do not intend to apologize. The Senator from Tennessee certainly owes several apologies, but I will not insist on them. I am not disturbed by his criticism. I think the Senate is called upon to justify its action to the people, but not called upon to apologize for anything the Finance Committee has done with regard to the bill, or what the Senate has done on the bill. It may be that some explanation may be necessary.

Mr. PROXMIRE. Mr. President, will the Senator yield?

Mr. McCARTHY. I yield.

Mr. PROXMIRE. Is it correct to say that the amendment of the Senator from Minnesota deals with section 12?

Mr. McCARTHY. That is correct.

Mr. PROXMIRE. As I understand, the estimates that have been made show that the Finance Committee version would gain revenue over the present law of \$85 million. Is that correct?

Mr. McCARTHY. Yes; that is a rough estimate. It is a very rough estimate. I have little basis for it.

Mr. PROXMIRE. Does the Senator from Minnesota have any information for the Senate as to how his amendment would affect Treasury revenues?

Mr. McCARTHY. A very rough estimate shows that the increase would be about \$50 million.

Mr. PROXMIRE. It would be a reduction of \$35 million below what the committee recommends, would it not?

Mr. McCARTHY. Yes.

Mr. PROXMIRE. I thank the Senator.

Mr. McCARTHY. I yield 5 minutes to the Senator from New York.

Mr. JAVITS. Mr. President, it is my belief that the provisions contained in section 12 of the committee version of the tax bill would discourage the consideration of economic advantage as the basis for oversea investment decisions by U.S. business. As the result of the "escape clause" provisions, the discouragement of such considerations would affect most heavily new investors who had not yet built up an earning base overseas and would need to accumulate a larger amount of earnings for capital reinvestment.

Bluntly speaking, the effect of this section would be to cause the very thing which the administration is trying to avoid: It would make tax considerations paramount in investment decisions.

Further, it would do the opposite of what the administration claims for it: It would soon worsen our balance-of-payments situation and it would place U.S. businesses—investors and exporters—at a serious disadvantage in their competition with foreigners for a foreign economic base and for export markets.

Although it is freely conceded by the administration that the returns from our oversea investments exceed the annual outflow, I should like to refresh our memory and therefore ask unanimous consent to insert in the RECORD the latest statistics, showing that from 1950 through 1961 dividend and interest income from our oversea investments exceeded the outflow of new capital by a total of \$8.6 billion. In 1962 alone, the difference came to \$1.2 billion. These

are U.S. Department of Commerce figures.

There being no objection, the table was ordered to be printed in the RECORD, as follows:

Dollar inflow and outflow to direct investment companies abroad, 1950-61

[Millions of dollars]

Year	Direct investment outflow	Dividends and interest inflow	Net inflow
1950.....	621	1,204	673
1951.....	528	1,492	964
1952.....	850	1,419	569
1953.....	751	1,442	721
1954.....	664	1,725	1,061
1955.....	779	1,912	1,133
1956.....	1,859	2,120	261
1957.....	2,482	2,249	(233)
1958.....	1,181	2,140	959
1959.....	1,372	2,206	834
1960.....	1,694	2,348	654
1961.....	1,467	2,672	1,205
Total.....	14,218	23,019	8,601

NOTE.—(1) Data from Department of Commerce. (2) Covers all areas and all activities, branches, and subsidiaries. (3) Unremitted branch earnings are included in both outflow and inflow columns.

Mr. JAVITS. Mr. President, the administration contends that it is investment in Western Europe which is not producing a sufficient return as compared to outflow. The facts are that the dividend and interest inflow from the European Economic Community countries has steadily increased between 1950 and 1961 from \$22 million annually to \$197 million—a ninefold increase. In the meantime, investment outflow to that area has increased from \$59 million in 1950 to \$270 million in 1961—less than a fivefold increase. It is clear that a further large increase in returns will occur when our more recent investments begin to pay off fully in the near future. But these investments must be kept competitive by a continued, economically based program of expansion. We cannot afford to let decisions taken in response to tax considerations hamper this program, lest our investments become unproductive and contract our ability to earn foreign exchange. Mr. President, I ask unanimous consent to have inserted in the RECORD Commerce Department statistics on our investments in the European Economic Community and the United Kingdom.

There being no objection, the statistics were ordered to be printed in the RECORD, as follows:

Dollar inflow and outflow on direct investment in the European Economic Community members and the United Kingdom, 1950-61

[Millions of dollars]

Year	Dividends and interest inflow	Direct investment outflow	Net inflow
1950:			
United Kingdom.....	73	49	24
European Economic Community.....	22	59	(37)
1951:			
United Kingdom.....	74	21	53
European Economic Community.....	29	28	1
1952:			
United Kingdom.....	78	(19)	97
European Economic Community.....	32	8	24

Dollar inflow and outflow on direct investment in the European Economic Community members and the United Kingdom, 1950-61—Continued

[Millions of dollars]

Year	Dividends and interest inflow	Direct investment outflow	Net inflow
1953:			
United Kingdom.....	90	(3)	93
European Economic Community.....	33	36	(3)
1954:			
United Kingdom.....	114	15	99
European Economic Community.....	51	16	35
1955:			
United Kingdom.....	149	32	117
European Economic Community.....	82	76	6
1956:			
United Kingdom.....	210	282	72
European Economic Community.....	70	145	75
1957:			
United Kingdom.....	173	172	1
European Economic Community.....	83	96	(13)
1958:			
United Kingdom.....	192	63	129
European Economic Community.....	81	106	(25)
1959:			
United Kingdom.....	231	190	41
European Economic Community.....	134	180	(46)
1960:			
United Kingdom.....	217	589	(371)
European Economic Community.....	144	282	(138)
1961:			
United Kingdom.....	258	188	70
European Economic Community.....	197	270	(73)

Mr. JAVITS. Mr. President, these data do not include the other direct earnings of dollars deriving from U.S. overseas investments—from exports directly to subsidiaries, from capital goods which we export to build the overseas factories in which we invest, from royalties and from direct transfers.

Above all, however, it gives no indication of the subtle but all-pervasive factors which accompany our holdings overseas and which are primary determinations of our international economic power. These relate primarily to the presence of U.S. goods, factories, technicians, and interests overseas, and to the increasing amount of vital information which we gather by our very daily contacts with our overseas competitors in their own environments. On this last point, I wish to make just one remark: After World War II—and right up until now, as far as the developing nations are concerned—we had to bring their people over here to show them our techniques of doing business or we had to send our personnel into their countries. This was an important part of foreign aid and it was necessary because they had little of their own sources of information over here.

Mr. President, now the time has come for us to learn from them. Let us not cut off the sources of our own information.

Mr. President, this matter of the tax on foreign operations of American business suffers from one thing more than from anything else, and that is the obvious inability, because it seems like a complicated subject, to make clear how vitally important it really is in terms of

the country and in terms of the country's business community. I know of very little that has roused the business community as much as this, and quite justly so. It involves not only business operations in terms of its own economic possibility, but it involves as well the capability of the United States to wage the struggle in the cold war. It involves also competition between American business and the business of other countries.

Perhaps the best example that is available is what I have ascertained—and which is of great economic importance—namely, the fact that the excess of the net return from our investments abroad, that is, our private investments abroad, aggregates \$8½ billion since 1950. Let me repeat that, because I believe it is a critical figure—\$8½ billion in net income has been received in the United States over and above foreign private investments in a 12-year period. The income from private investments abroad is now running in the area of \$2,700 million a year.

Every year since 1950—with the exception of one year, 1957—the inflow of dividends and interest from private U.S. investments overseas has exceeded the outflow by a tremendous amount.

Secondly, we are meeting very keen competition from all the nations abroad, especially from the industrialized nations.

We are living in a working and active world, and it seems to me it would be most unwise to disadvantage ourselves in this way by this kind of provision.

Let us remember that no matter what escape valves are provided here, the fact is that basically this tax law, which we would be enacting, would impose an obligation upon businessmen, whether corporate or personal, which is unusual and unprecedented.

Therefore, whatever else we do by way of exemptions, the fundamental approach is wrong and will stifle and inhibit foreign private investment, which it is to the interest of our Nation to encourage.

Let us see, for example, how U.S. business will be hurt. I speak of all U.S. business, not only personal holding companies, but all business.

It will be hurt, first, because the exclusion for overseas manufacturing subsidiaries only covers income from sales in the country of manufacture, and U.S. firms, in order to sell throughout the Common Market would have to manufacture in each country. Their competitors, on the other hand, could sell throughout the Common Market area from one large, efficient, centrally located plant.

Second, U.S. firms attempting to sell throughout the Common Market area would be faced with paying a current tax of at least 52 percent on the sales profits. European companies, on the other hand, may sell, for example, through a Swiss subsidiary, and pay a current tax of between 10 and 15 percent, with the remainder of their profits available for increased advertising, pro-

motion expenses, replenishing of inventories, and so forth.

Let us remember that under the system which would be established by the bill, if it is passed, we would not even allow for amortizing on debt and other responsibilities of that character, for which very important reserves are necessary, let alone the question of development. So by that, and by the so-called minimum distribution test, incorporated in the bill, American business, as contrasted with European business, would be disadvantaged.

And, most important, this whole tax provision would be very bad for new firms, one of the great problems. We have to let the right hand know what the left hand is doing. In other words, what we do with the tax bill will directly and materially affect the trade bill, which will come right along on the heels of the tax bill. This tax provision will inhibit the very thing we are trying to encourage; namely, to have more companies engage in foreign trade and foreign productivity, which the trade bill is designed to encourage. The Senator from Minnesota [Mr. McCARTHY] gave the figures yesterday. It is absolutely remarkable, and few people realize it, that only 5 percent of American companies are actually engaged in any foreign operation. We want to have more engage in it. Yet this very tax bill will inhibit new concerns, as against more established concerns, because the real effect of the so-called escape valve is to make it easier to operate within the confines of this bill for firms which have well-established operations and have been operating for a very long time, but will make it practically impossible for newly established firms, which do not have such a background in that regard, to operate.

Finally, there is an artificial distinction between developed countries and less developed countries. For example, the bill does not allow a flow of earnings from the industrial countries, where the most capital can be divided into underdeveloped countries, because it requires the income, in order to be free of this very onerous tax burden, not only to be earned in underdeveloped countries, but to originate from investment which was made there. So it is a double inhibition, emphasizing the difficulty of causing a flow of earned capital to take place between developed country A and underdeveloped country B.

It seems to me that if there was anything which instructed us to turn down this particular provision, it was that absolutely artificial distinction which runs counter to everything our country is trying to do, which is to stimulate American private investment abroad. It seems to me this has been much maligned and much too little understood in terms of its value to the whole American struggle for freedom abroad. It is very clear—and every analysis shows it, whether it be the analysis of the United Nations, of the International Bank for Reconstruction and Development, of the International Finance Corporation or of the Inter-American Development Bank—that if we depend for the development of underdeveloped countries upon capi-

tal put up by governments, including the U.S. Government, we will never make it, and that our struggle against communism will be in very grave jeopardy and will very likely be unsuccessful in terms of the development of the less developed countries.

For example, can any Senator say to himself, legitimately and honestly, that the U.S. Congress will vote more than, roughly, \$2 billion a year, which we are now voting, for economic aid? We all know that Congress will not do that. As a matter of fact, it will not, because that amount just seems to fit the congressional conscience. Yet that amount is not enough—every survey shows it—to gear up and move forward a standard of living in the less developed countries in an amount which would at least be satisfactory in relation to the advance in developed countries. The big justification is that developed countries are developing faster, and the underdeveloped countries, in relation to the developing countries, are practically standing still.

In other words, the situation of dissimilarity, which is too often phrased in terms of imperialism, although it is not, is being emphasized and accented, instead of being reduced.

The bill, by its inhibitions and restrictions, tries to achieve a minor national objective which is almost myopic in its influence. All we need to look at are the tax consequences, which, as has just been explained, amount to a few tens of millions of dollars a year, to see the insignificance of this objective compared to the potential damage to the trade program, the whole foreign investment program, and the whole development of the underdeveloped areas program, which represent a political objective which can be looked at in terms of billions of dollars, because it involves the defense and security of the United States and the rest of the free world. It is completely overlooked, but is very urgent, in this particular tax provision.

So I emphasize, again and again, the importance of this provision. Here we are trying to get a private enterprise system into the foreign aid picture, to take its proper part, to help the load to be carried, and to make available resources which are absolutely essential to success.

It is the people who invest, whose business judgment and ability this provision will inhibit or not inhibit. Especially am I concerned by the fact that it inhibits the very new, the very young, the very ambitious elements which we should be encouraging to move into this field.

By way of alternative, the amendment offered by the Senator from Minnesota [Mr. McCARTHY] and me deals with this problem in a most rational way. It catches the personal holding company tax haven at the complete discretion of the collector of internal revenue. He is the person who can start the proceeding with respect to an improper accumulation of earnings in any country in the world, so far as Americans are concerned. The burden of proof is then not upon the collector but upon the person from whom he is seeking to collect. It seems to me that that would

be a very tight way to administer this provision so as to get the most out of it. It should catch every one of the people who we think are guilty of improperly avoiding or evading the payment of taxes. At the same time, it will not warp or destroy the economic system, so far as economic policy is concerned.

Mr. President, the situation is important enough to warrant every Senator being in his seat when the vote is taken. Senators must understand that the political and economic consequences will be far more important than the tax consequences which will flow from making a mistake of this nature, especially as we have a very feasible, practical, realistic alternative to juxtapose to it. As now in the bill, this provision would not be in the national interest—apart from taxes, where it does not mean very much either way. I hope very much that the amendment which has been proposed by the Senator from Minnesota [Mr. McCARTHY] and me will be adopted.

As the bill now is before us, it is proposed that, with one and the same motion, with complete blindness to what is really at stake, we pass a law which can have very little financial effect in absolute terms on the question of tax revenue, but could completely inhibit, abroad, the national policy of the United States, which is to encourage oversea private investment.

Mr. President, in view of the absence of most Senators from the Chamber, I suggest the absence of a quorum.

The PRESIDING OFFICER. To whose time will the time for the quorum call be charged?

Mr. JAVITS. Mr. President, I ask unanimous consent that the time for the quorum call not be charged to either side.

The PRESIDING OFFICER. Is there objection? The Chair hears none, and it is so ordered. The clerk will call the roll.

The legislative clerk proceeded to call the roll.

Mr. KERR. Mr. President, I ask unanimous consent that the order for the quorum call be rescinded.

The PRESIDING OFFICER (Mr. METCALF in the chair). Without objection, it is so ordered.

Mr. MAGNUSON. Mr. President—

The PRESIDING OFFICER. Does the Senator from Oklahoma yield time? The time is under control.

Mr. KERR. I yield 2 minutes to the Senator from Washington.

The PRESIDING OFFICER. The Senator from Washington is recognized for 2 minutes.

Mr. MAGNUSON. Mr. President, I wish to ask the distinguished Senator from Oklahoma a question.

On pages 295 and 296 of the bill, in the definition of the term "patronage dividend," it is stated that a patronage dividend is a payment "determined by reference to the net earnings of the organization from business done with or for its patrons."

In a case which has been called to my attention—it involves the manufacture of plywood in the Pacific Northwest, and

many of the companies are cooperative organizations—the cooperative renders services for the patron. I wanted to be sure that in the opinion of the Senator from Oklahoma the phrase "business done with or for its patrons" includes services with or for patrons.

Mr. KERR. I think it is clear, both under the interpretation of a patronage dividend under present law and also under the words "business done with or for its patrons," that services rendered with or for patrons are included. Business done is not necessarily limited to products sold to or purchased for patrons. Business done also includes services performed for patrons, as well.

Mr. MAGNUSON. I thank the Senator from Oklahoma.

Mr. McCARTHY. Mr. President, if the Senator will yield, let me say I think this is a reasonable and desirable interpretation of the language; and I believe that any other interpretation would create an impossible distinction.

Mr. MAGNUSON. I thank the Senator.

Mr. KERR. Mr. President, a parliamentary inquiry: What is the time situation?

The PRESIDING OFFICER. The Senator from Minnesota has no time left. The Senator from Oklahoma has 25 minutes remaining.

Mr. MILLER. Mr. President, will the Senator from Oklahoma yield 2 minutes to me?

Mr. KERR. I yield 2 minutes to the Senator from Iowa.

The PRESIDING OFFICER. The Senator from Iowa is recognized for 2 minutes.

Mr. MILLER. I thank the Senator from Oklahoma.

Mr. President, if I may have the attention of the Senator from Minnesota [Mr. McCARTHY], I wish to ask him a question: On page 5 of his amendment, paragraph (b) (1) refers to "money or other property" "beyond the reasonable needs of the business."

And in line 19, subparagraph (2) refers to "reasonable needs of the business."

But beginning in line 22, in defining "reasonable needs of the business," the amendment provides:

(A) Any money or other property which is located outside the United States and is ordinary and necessary for the active conduct of a trade or business.

And on page 8, in line 5, we find a heading "Reasonable Needs of the Business."

For the purpose of establishing the legislative history in regard to his amendment, I ask the Senator from Minnesota, whether, in line 24, the statement "a trade or business" should mean "the trade or business."

Mr. McCARTHY. Yes, it is my interpretation that it should mean "the trade or business," instead of "a trade or business," in order to be consistent with the legislative history which has been made.

Mr. MILLER. Then let us say there is a corporation in a manufacturing business, and that it has some accumulated funds, and invests them, let us say, in a rental type business or in a

hotel operation. Would that be outside the scope of the exception?

Mr. McCARTHY. I think if it were a manufacturing operation or a sales operation, it probably would not be allowable under the terms of Act.

Mr. MILLER. Suppose it manufactures shoes and wishes to diversify by beginning the manufacture of fishing-tackle equipment.

Mr. McCARTHY. I am not sure how it would be interpreted. The Senator from Iowa, in his remarks last night, pointed out that the language of the bill has not been interpreted, and that there are any number of new terms. The distinctions between "a" and "the" and between a manufacturing operation and a distribution operation have not been clearly made.

The PRESIDING OFFICER. The time yielded to the Senator from Iowa has expired.

Mr. MILLER. May I have 1 more minute?

Mr. KERR. I yield 1 more minute to the Senator from Iowa.

The PRESIDING OFFICER. The Senator from Iowa is recognized for 1 more minute.

Mr. MILLER. Then, for the sake of the legislative history, since we are trying to enable American enterprises to compete with their counterparts in foreign countries, cannot we interpret the amendment to mean an investment in the same line of business or in a diversified line of business which would enable the corporation to compete effectively with its competitor?

Mr. McCARTHY. Certainly that is the purpose I have in mind in my amendment. The reason we proposed the unreasonable accumulation approach, rather than the technical and confined amendment proposed by the committee, was that, in my judgment, this would be a related activity and it would not be unreasonable to use earnings for that purpose.

Mr. MILLER. In other words, if it is designed to enable them to diversify, and diversification is necessary in order to enable them to compete, it should be encouraged?

Mr. McCARTHY. Yes, it should be encouraged.

Mr. KERR. Mr. President, I yield myself 5 minutes.

Mr. McCARTHY. Mr. President, I have a question on the time. I had control of the time on this side. I think I had used 15 minutes, when I yielded 5 minutes to the Senator from New York.

The PRESIDING OFFICER. Does the Senator from Oklahoma yield time?

Mr. KERR. I yielded 3 minutes to the Senator from Iowa.

Mr. McCARTHY. I asked a question about the time.

Mr. KERR. Mr. President, a parliamentary inquiry. What is the situation on the time?

The PRESIDING OFFICER. The time of the Senator from Minnesota has expired. The Senator from Oklahoma has the remaining time. The vote will take place at 11:30.

Mr. KERR. Mr. President, the pending amendment would practically de-

stroy the opportunity for constructive improvement overseas in taxation of American corporations doing business overseas. The amendment would create a very substantial drain on our balance of payments. The amendment would legalize foreign tax havens to the fullest extent. The amendment would encourage all existing tax havens to continue and encourage others to be created, because it permits the accumulation of earnings in foreign-owned corporations, and once they reinvest them, they cannot be reached for American taxation.

The amendment not only exports jobs, it not only increases the drain on our balance of payments; it perpetuates the very sad and adverse situation that the foreign tax provisions in the bill were calculated to cure.

The House tried to do two things: First, eliminate tax havens; second, tax the income of a foreign corporation as it earns it, rather than as it pays it back to this country in dividends.

The committee amendment took out all provisions that would tax foreign income as it was earned, and permitted it to remain on a reasonable basis, and to be taxed when it came back, but it put incentives in the bill to bring the money back. It put an incentive in the bill to increase jobs by permitting a foreign sales corporation to keep a considerable part of its earnings so long as it bought American products and sent the money back to America to pay for those products, sustaining jobs in this country and, in the end, our balance of payments and gold position.

The pending amendment would adversely affect that situation, because it exempts those earnings from taxes so long as they are kept over there and reinvested over there. It involves nearly \$100 million a year.

The pending amendment would cost from \$80 to \$100 million a year, and that amount would be kept in foreign tax havens owned by American companies and used to expand their operations overseas and increase their manufacturing over there, instead of over here; increase jobs over there instead of over here; increase the drain on our gold reserve, rather than reverse the flow and bring it back here.

I yield back the remainder of my time to the Senator from Montana [Mr. MANSFIELD].

Mr. MANSFIELD. Mr. President, if I may, under the procedure in effect, I yield 5 minutes to the Senator from Minnesota [Mr. McCARTHY], and I will then have 10 minutes.

Mr. McCARTHY. Mr. President, I appreciate the courtesy of the Senator. There was some misunderstanding about the granting of time, as a consequence of which time was charged against me which should not have been charged against me.

Mr. President, I am in almost complete disagreement with the general statements which have been made by the Senator from Oklahoma in his concluding remarks. I hope that Members of the Senate, in the course of this debate, have had occasion to examine some of the testimony and some of the judg-

ments that have been passed on this section of the bill.

I have looked around at Senators' desks and at the books of hearings piled up on them. I do not find that the order in which they have been piled on the desks has been disturbed on very many desks. The piles of hearing records, running from volume 1 to 11, in most cases have not been disturbed in any way, so, unless Members of the Senate have been reached either by statements made on the floor or by communications sent to their offices, I am afraid they may be moved to act on recommendation without full study.

I regret that this is the case, because, in my judgment, this amendment is not so highly technical that it could not be understood but that the technical aspects of what is being proposed by the committee have not been worked out.

The Senator from Iowa [Mr. MILLER] made a statement on the floor which, should have been read, or at least should have been scanned, because, as one who has worked on the technical side of tax law and tax administration for many years, he made telling points about the difficulty of administering the kind of proposal being made to the Senate in the amendment by the Senate committee.

In addition, I hope Senators have had occasion to read the remarks of the Senator from Nebraska in this connection, in the two major points he made: First, the constitutional questions which are raised by this proposal; and second, some mistakes in drafting are misunderstanding. One of them I learned—section 963—in consultation with the staff of the Committee on Internal Tax Revenue, was not known to them. It relates to the question of tax credit on foreign taxes. Although the Treasury said they knew it was in, and that it was not an accident on their part, yet the staff of the Committee on Internal Revenue Taxation said they did not know until last evening that it was in. If the Treasury knew it—and it is a drastic change in policy, letting the Treasury determine what foreign taxes can be determined or credited against the taxes of American corporations—this information should have been given out, and at least the staff of the Committee on Internal Revenue Taxation should have known about it.

Finally, I hope Senators will give some attention to the remarks of the Senator from New York [Mr. JAVITS], who touched particularly on the question of our competition with foreign corporations engaged in business in those countries where we hope American industry, business, and finance may become more operative and active than they have in the past.

It is my opinion that much more study should have been given to the proposals that has been given to them by the Finance Committee.

Mr. President, the August 25, 1962, amendment now before the Senate would be a substitute for the Committee on Finance provision with respect to controlled foreign corporations which now occupies 71 pages of the bill. Instead of the complex and unworkable

provisions of the Kerr-Treasury amendments, the August 25, 1962, amendment would substitute a tax on earnings impossibly accumulated beyond the reasonable needs of the foreign business. It is to be a simple, straightforward adoption of the unreasonable earnings approach we now use in sections 531 to 537 of the code for domestic corporations which improperly accumulate earnings to avoid the payment of additional income tax by their shareholders.

All of the court decisions and precedents which have been developed over many years in the domestic area on this matter of unreasonably accumulated earnings will now be available to make clear rules for taxation of improperly accumulated foreign income. It must be said for this amendment that, should Senators vote for it, they will be clear on exactly what they have supported.

This is in direct contrast to the Treasury proposal, even without the complicated and untried Kerr amendments, which was described by a group of New York tax lawyers as follows:

As in the case of the House bill, merely reading the new draft will suffice to demonstrate its utter complexity. Even the most sophisticated become lost in the forest of its technicalities: its phraseology is vague at critical points; precedents for its construction and application are lacking because of the novelty of its concepts; and it seeks to resolve vital and difficult problems by the expedient of delegating authority to issue regulations * * *. We seriously question whether a law of such complexity could be applied and administered in an effective and reasonably even-handed way.

The concepts and techniques of the bill are so highly complex that we doubt that reasonable technical solutions for its defects can be devised. In any event, we are convinced that the bill could not be equitably and uniformly administered because it would be impossible for most revenue agents and taxpayers to understand and apply its provisions.

We therefore regretfully conclude that the foreign income provisions of the bill, even as revised by the Treasury draft, would have a seriously adverse effect on foreign operations of American business.

By contrast, the August 25, 1962, amendment is designed as concisely and clearly as possible to strike at tax abuses, in the use of controlled foreign corporations, or "incorporated pocketbooks" or "tax havens" by U.S. shareholders. It would levy a U.S. tax on any unreasonably accumulated profits held abroad by U.S. shareholders. To the extent that a controlled foreign corporation had \$1 abroad which it could not prove by a preponderance of evidence was actually needed in its business, such dollar would be immediately taxed to the shareholder in the United States.

This is no new and untried theory—as is the case with the Kerr amendments. This is a tried and proven approach, used for many years in the domestic area, following proven concepts under present law. Its constitutionality would not be seriously questioned because, like the foreign personal holding company provisions of the code, it is designed to stop tax evasion by improperly accumulating income abroad. Since 1937 this type of legislation to stop

tax evasion has been considered constitutional, as opposed to the Kerr amendments which would tax foreign income to the U.S. shareholders whether or not tax evasion is involved. It is this type of indiscriminate treatment of taxpayers—the good being punished with the bad—which can be avoided by not adopting the Kerr amendments and the present section 12.

The August 25, 1962, amendment together with a vigorous enforcement of the Treasury's powers under sections 482 and 6046, will stop all of the flagrant abuses pointed up by the Treasury Department's assertions. The Treasury now has the authority, seldom used, to prevent abuses of intercompany pricing, intercompany charging of expenses, intercompany loans, and the diversion of U.S. income to a controlled foreign corporation. It may have been a last minute realization of this Treasury authority under section 482 which caused the Senator from Oklahoma [Mr. KERR] to move the deletion of section 6 of H.R. 10650 as it was passed by the House.

The Treasury also now has the authority under sections 6038 and 6046 to obtain full financial data on all foreign subsidiaries of U.S. corporations so that secrecy of foreign bank accounts or financial data is now penalized by fine and imprisonment as a violation of our Internal Revenue Code. With this new reporting data, no foreign operations of U.S. taxpayers can be withheld from the Treasury Department, which must now step up its program of enforcement rather than push for new, complicated, and unworkable tax laws.

The August 25, 1962, amendment is clear. A vote for it can be cast with a full knowledge that it is understandable to taxpayers and tax collectors. The Chamber of Commerce of the United States announced this morning that it fully supports this amendment because it is consistent with the proposed Trade Expansion Act. On the other hand, the chamber as well as other business organizations which will bear major responsibilities under the Trade Expansion Act strongly oppose the Treasury tax proposals and the Kerr amendments as being antithetical to the trade bill.

The Committee for Export Expansion Through Subsidiaries Abroad, a group of 64 small- and medium-sized companies engaged in export trade, supports the August 25 amendment and has no doubt been to you to solicit your support. These companies, as many publicly testified, do not wish to be put in the same category with the tax haven operators, nor should they be. President Kennedy has said that he does not wish to penalize legitimate American-owned overseas business which will strengthen our trade and currency in future years. It is to this objective that the August 25, 1962, amendment is dedicated.

I am advised by the Joint Committee on Internal Revenue Taxation staff that the August 25 amendment will produce at least \$50 million in additional tax revenue in 1963 or 1964—as opposed to the Treasury-Kerr proposals which are estimated to collect \$80 million in the early years, but in the following years

the August 25 amendment will result in greater tax revenue than the Treasury-Kerr proposals because U.S. foreign trade will be allowed to remain competitive and not be diminished or destroyed by unreasonable limitations such as the present section 12 before the Senate.

The PRESIDING OFFICER. The time of the Senator from Minnesota has expired. The Senator from Montana has 10 minutes remaining.

Mr. MANSFIELD. Mr. President, this amendment would be an abandonment of, rather than a substitute for, legislation ending the rapidly increasing tax haven abuse. This amendment, to tax only funds unreasonably accumulated abroad, would leave entirely untouched almost all tax haven income.

It would lose between \$80 and \$100 million.

It would encourage the flight of American capital.

It would be more likely to injure than to aid our balance of payments.

It would encourage the retention of capital abroad to provide jobs for foreign workers while 5.3 percent of our working force is idle.

I cannot believe that the Senate wants to endorse tax havens by adopting this amendment.

The only tax haven income which would still be covered by the amendment would be income derived from insurance abroad of U.S. risks.

The amendment would fail to tax the principal forms of tax haven income. It would not even touch tax haven income channeled into foreign sales subsidiaries. These corporations are artificial entities deliberately separated from the principal foreign operations. The reason for their existence is to siphon income into tax shelter countries, such as Switzerland, Liechtenstein, and the like which have especially low rates of tax. Nor would this amendment catch tax haven service income which has been diverted to tax shelter countries. Nor would this amendment touch holding companies used as a receptacle to draw off earnings that should be returned to the United States.

The Treasury estimates that the committee provision will raise \$85 million a year. The Treasury says this amendment would raise practically nothing. What company cannot find some excuse for using its earnings abroad? The amendment would only be a sanctuary for the tax avoiders and a trap for the unwary.

I want this next statement I am making to be clearly understood. If we take this so-called unreasonable accumulations tax to conference, I am convinced that the House conferees would not accept it. Instead, they then would have to insist on their own much harsher provisions, which not only would reach tax haven operations but also would seriously affect manufacturing and other operating companies. This would mean that all the good work which the Finance Committee has done to shape a workable provision—but one which curbs the tax haven abuses and them only—might be lost.

While this amendment would fail to tax U.S. shareholders on tax haven in-

come, it nevertheless would invite revenue agents to try to tax operating companies by imposing their judgment as to what capital a taxpayer needs in his business.

Why do we want an amendment that would interfere in any way with established manufacturing operations abroad? The approach of this amendment was examined by the Finance Committee and, after extensive consideration, rejected.

Although it would be a tremendous nuisance, this unreasonable accumulations tax would be of very little revenue significance, since most overseas companies can find some place to invest funds in operations whether they are needed or not. It would be very easy for companies to find one way or another of diversifying or expanding their business. Of course the unwary may be caught—for example, a few small, closely-held companies. But, I am informed, they are of little significance in the foreign investment area. In short, the amendment would do little that is constructive.

Let no one think that the present code provisions for an accumulated earnings tax on domestic corporations is a precedent here. The penalty tax on accumulated earnings in the domestic area is aimed at a completely unrelated problem—the avoidance of surtax rates upon dividends to individual shareholders. Its application has thus been limited in practice to the small closely held corporation.

I am also convinced that an unreasonable accumulations tax on foreign operations would not be in the national interest. The Finance Committee amendment, through the export trade corporation provision, would provide special encouragement for the export of U.S. products and in this way would create jobs here at home. But Senators will find no such provision as this under the amendment. Actually, the amendment now before us would export jobs. Let me show Senators how. First, foreign subsidiaries under present law tend to hold funds abroad, where the foreign tax rate is less than our domestic rate. But at least now there is no pressure on them to reinvest these earnings in expanding and diversifying their foreign operations. They may take their time in deciding whether to use their earnings abroad or repatriate them. But if the Congress should see fit to enact this unreasonable accumulation tax, this would actually place pressure on the companies to immediately reinvest these earnings abroad—to shift production and jobs from this country to foreign countries. The new investment in foreign production would, of course, worsen our balance of payments position. The Finance Committee's tax haven legislation, on the other hand, would encourage investment here at home and help our balance of payments.

In conclusion, let me urge Senators not to adopt this amendment. It would not reach the basic tax haven types of operation. It would present many difficult administrative problems. It would encourage the export of jobs.

Once the bill reached conference it would almost surely be rejected if this amendment were adopted, since the House conferees would insist upon reaching tax haven income. This means we might well end up with the much harsher House version of this provision which would go beyond tax havens to reach operating companies.

I am informed that if the pending amendment should be adopted, it would mean that instead of providing between \$80 million and \$100 million in revenue for the Government, the amount might well be in the vicinity of \$2 million.

Mr. President, I urge the rejection of the amendment. I yield the remaining time to the Senator from Ohio [Mr. LAUSCHE].

The PRESIDING OFFICER. The Senator from Ohio may proceed.

Mr. LAUSCHE. Mr. President, I contemplate voting against the amendment offered by the Senator from Minnesota. I shall do so for several reasons.

First. I believe that every reasonable effort should be made to eliminate the tax havens which admittedly exist in foreign countries. In my judgment, the House and the Senate committee have striven to reach that objective.

Second. I am alarmed by the constant evidence, at least in my own State, of industry moving into foreign countries, knowing that it can put itself in a better competitive position in those countries, proclaiming it does not intend to manufacture abroad and ship to the United States. Intermittently evidence appears that the purpose not only is to compete in the world markets, but also to compete in domestic markets.

Third—and this is not a reason for the casting of my vote—the discussions which have been had clearly indicate the need for doing something domestically to place ourselves in a better position in competition for world markets. In my opinion, our conduct in the Congress has been of a nature to induce placing ourselves in a less favorable competitive position. But that is not one of the aspects of the discussion.

To repeat, first, I wish to eliminate tax havens. Second, I do not wish to give inducement to American industry to settle abroad, taking jobs from American workers and providing them for the workers in foreign countries.

The PRESIDING OFFICER. All time has expired.

Mr. DOUGLAS. Mr. President, a parliamentary inquiry.

The PRESIDING OFFICER. The Senator will state it.

Mr. DOUGLAS. Have the yeas and nays been ordered?

The PRESIDING OFFICER. The yeas and nays have not been ordered.

Mr. KERR and Mr. DOUGLAS requested the yeas and nays.

The yeas and nays were ordered.

The PRESIDING OFFICER. The question is on agreeing to the amendment of the Senator from Minnesota. All time having expired, the clerk will call the roll.

The Chief Clerk proceeded to call the roll.

Mr. HUMPHREY (when his name was called). On this vote I have a pair with

the senior Senator from Missouri [Mr. SYMINGTON]. If he were present and voting, he would vote "nay." If I were at liberty to vote, I would vote "yea." I therefore withhold my vote.

The rollcall was concluded.

Mr. HUMPHREY. I announce that the Senator from Nevada [Mr. BIBLE] and the Senator from Mississippi [Mr. EASTLAND] are absent on official business.

I further announce that the Senator from New Mexico [Mr. ANDERSON], the Senator from Alaska [Mr. GRUENING], and the Senator from Missouri [Mr. SYMINGTON] are necessarily absent.

On this vote, the Senator from Alaska [Mr. GRUENING] is paired with the Senator from Mississippi [Mr. EASTLAND]. If present and voting, the Senator from Alaska would vote "yea" and the Senator from Mississippi would vote "nay."

I further announce that, if present and voting, the Senator from New Mexico [Mr. ANDERSON] would vote "nay."

On this vote, the Senator from Minnesota [Mr. HUMPHREY] is paired with the Senator from Missouri [Mr. SYMINGTON]. If present and voting, the Senator from Minnesota would vote "yea" and the Senator from Missouri would vote "nay."

Mr. KUCHEL. I announce that the Senator from Maryland [Mr. BEALL], the Senator from Utah [Mr. BENNETT], the Senator from Connecticut [Mr. BUSH], the Senator from Arizona [Mr. GOLDWATER], the Senator from New Hampshire [Mr. MURPHY], the Senator from Massachusetts [Mr. SALTONSTALL], and the Senator from Wisconsin [Mr. WILEY] are necessarily absent.

The Senator from Vermont [Mr. PROUTY] is detained on official business, and if present and voting, would vote "nay."

On this vote, the Senator from Maryland [Mr. BEALL] is paired with the Senator from Utah [Mr. BENNETT]. If present and voting, the Senator from Maryland would vote "yea" and the Senator from Utah would vote "nay."

On this vote, the Senator from Connecticut [Mr. BUSH] is paired with the Senator from New Hampshire [Mr. MURPHY]. If present and voting, the Senator from Connecticut would vote "yea" and the Senator from New Hampshire would vote "nay."

The result was announced—yeas 21, nays 65, as follows:

[No. 228 Leg.]

YEAS—21

Bartlett	Fong	Miller
Bottom	Hickenlooper	Morton
Capehart	Hruska	Mundt
Case	Javits	Scott
Curtis	Keating	Thurmond
Dirksen	Kuchel	Williams, N.J.
Engle	McCarthy	Young, N. Dak.

NAYS—65

Alken	Cooper	Holland
Allott	Cotton	Jackson
Boggs	Dodd	Johnston
Burdick	Douglas	Jordan, N.C.
Butler	Ellender	Jordan, Idaho
Byrd, Va.	Ervin	Kefauver
Byrd, W. Va.	Fulbright	Kerr
Cannon	Gore	Lausche
Carlson	Hart	Long, Mo.
Carroll	Hartke	Long, Hawaii
Chavez	Hayden	Long, La.
Church	Hickey	Magnuson
Clark	Hill	Mansfield

McClellan
McGee
McNamara
Metcalfe
Monroney
Morse
Moss
Muskie
Neuberger

Pastore
Pearson
Pell
Proxmire
Randolph
Robertson
Russell
Smathers
Smith, Mass.

Smith, Maine
Sparkman
Stennis
Talmadge
Tower
Williams, Del.
Yarborough
Young, Ohio

NOT VOTING—14

Anderson
Beall
Bennett
Bible
Bush

Eastland
Goldwater
Gruening
Humphrey
Murphy

Prouty
Saltonstall
Symington
Wiley

So Mr. MCCARTHY's amendment was rejected.

Mr. KERR. Mr. President, I move that the vote by which the amendment was rejected be reconsidered.

Mr. MANSFIELD. I move to lay that motion on the table.

The motion to lay on the table was agreed to.

Mr. JACKSON. Mr. President, I should like to ask the Senator in charge of H.R. 10650 a question with respect to that bill.

I refer to subsection (f) of section 8 of the bill, election for multiple-line company to be taxed on total income. It is my understanding that if a company which has always filed its return as a mutual marine insurance company makes this election, it will be consistently taxed on a stock company basis for all prior years, as well as future years, and will not be taxed as a mutual fire and casualty company for any years preceding the effective date of the election.

Is my understanding correct?

Mr. KERR. The Senator's understanding is correct. It is the intent of this section to assure that a company which has been taxed as a mutual marine insurance company for 5 years or more will continue to be taxed on a stock company basis for all years. When this amendment was under consideration by the Senate Finance Committee, I was assured by Mr. Stanley S. Surrey, Assistant Secretary of Treasury, that a company which has always filed its returns as a mutual marine insurance company on a stock company basis under section 831, and which makes this election, will be taxed on a stock company basis for all prior years as well as future years.

Mr. JACKSON. I thank the Senator.

WORLD FOOD CONGRESS

Mr. JAVITS. Mr. President, I would like to call the attention of my colleagues to the World Food Congress which our Government will host in June 1963 in Washington, D.C.

This congress will be the 20th anniversary of the first international food congress held at Hot Springs, Va., in 1943. Out of this first congress was born the idea of an international organization designed to study world food problems and alleviate world hunger. At a subsequent world food meeting in Quebec in 1946, this organization known as the Food and Agriculture Organization, or FAO, for short, was officially launched.

Today, with headquarters in Rome, Italy, and with some 1,300 personnel on

duty throughout the world, under the leadership of its Director General, B. R. Sen of India, the FAO is serving humanity as one of the oldest and most effective organizations of the United Nations.

Over this span of 20 years, FAO experts have worked in food deficit areas of the world in an effort to combat causes of world hunger. They have brought nations and areas together to deal with pests and disease; and to work out soil and conservation problems of all kinds that affect food supply and nutritional standards, and which know no territorial jurisdiction. Many of these problems have been effectively dealt with by means of international cooperation under the leadership of FAO. Many more remain yet to be solved and are rapidly worsening under the pressure of expanding populations.

In spite of all that has been done about it, hunger remains as man's oldest and greatest enemy. Yet, this problem is capable of solution. Studies which FAO has compiled on population trends and sources of food supply, prove that the earth can feed her people, if the world can but make use of the existing reservoir of agricultural knowledge and productive capacity.

How then, can we allow fully one-half of the world's population to suffer the misery of hunger and malnutrition, when this problem is capable of a solution? The solution is to help the underdeveloped and underfed countries themselves to acquire the agricultural techniques and methods needed to produce enough of the right kinds of food to improve their health and living standards.

It was this thought of both developed nations and developing nations working together in a cooperative approach to alleviate world hunger, that motivated the Food and Agriculture Organization to launch its 5-year freedom from hunger campaign in 1960. All 104 member-countries of FAO have been asked to participate with their own national committees and nearly 50 have already done so.

In January the United States established a nongovernmental, nonpartisan, nonprofit American Freedom From Hunger Foundation in Washington, D.C., to furnish leadership for the campaign in this country. Its trustees were invited to serve, without compensation, by the President. They include citizens from all areas of the American community—agriculture, business, labor, industry, education, charity, religious, and public service. Ex-President Truman is the honorary chairman.

This foundation seeks sponsors for projects in food production in the developing nations of Latin America, Asia, and Africa. American groups and organizations and firms of all kinds are asked to make tax-exempt contributions of money, goods, and technical services, needed to initiate projects in these food-deficit areas.

However, this is only a part of the campaign. It is most essential to stimulate an interest and knowledge on the part of the American people in the problems of world hunger. Organizations and groups who can help out in

this information and education program are asked to become members of the foundation.

These member organizations will play an important part in the forthcoming World Food Congress. The Congress is nongovernmental and delegates, who attend from over 100 countries, are the community leaders of their respective countries. This is a people's approach to a solution of the problems of world hunger; not a government approach. It represents an opportunity for the people of the United States to meet with the people of developing countries to try to work out a solution to the greatest problem that faces mankind.

In the words of Director General B. R. Sen, "One man's hunger and want is every man's hunger and want. One man's freedom from hunger and want is neither a true nor a secure freedom until all men are free from hunger and want."

It is my hope that Americans everywhere will respond to this challenge and let our friends in the developing countries know that we are interested in their welfare; that we will help them to help themselves according to the work of the American Freedom From Hunger Foundation and the World Food Congress.

INDEPENDENT OFFICES APPROPRIATIONS, 1963

The PRESIDING OFFICER. Under the unanimous-consent agreement previously entered into, the Senate will now proceed to the consideration of H.R. 12711, making appropriations for the independent offices, which the clerk will state by title.

The LEGISLATIVE CLERK. A bill (H.R. 12711) making appropriations for sundry independent executive bureaus, boards, commissions, corporations, agencies, and offices for the fiscal year ending June 30, 1963, and for other purposes.

TRANSACTIONS TAX ON SILVER

Mr. MAGNUSON. Mr. President, the Senate has before it the independent offices appropriation bill. By unanimous consent, in order to keep the legislative situation as it was asked for by the leadership, the independent offices appropriation bill is now the pending business.

However, I wish to discuss a provision in the tax bill, and I shall take this time to do so. Several other Senators also are interested in this question, and we desire to discuss it at this time before further action is taken on the appropriation bill.

Mr. President, on November 26, 1961, the President by Executive order terminated Treasury sales of the Government's free silver stock and at the time both he and Secretary Dillon indicated that Congress would be requested to repeal the silver purchase laws and the silver transfer tax to restore a free market in silver.

These proposals from the White House are a recognition of the painfully obvious fact that our unhealthy silver market is in need of help.

Repeal of the Silver Purchase Act entails major policy considerations of fiscal, economic, and monetary importance and has been described by some of my colleagues as "highly controversial." Joiner of this proposal with the suggested repeal of the tax on silver transfers is unfortunate to the extent that the repeal of the tax on silver transfers may be unnecessarily delayed.

The silver transfer tax was originally imposed under the Silver Purchase Act of 1934 as a device to protect the Government against speculation in the Treasury program to purchase foreign silver and was subsequently incorporated in the Internal Revenue Code of 1954—10 years later. It is an uncontroverted fact that the Government has not bought a single ounce of silver since 1941 and for that reason it no longer needs the protection of this act.

I understand from officials of the Treasury Department that the Treasury does not intend to buy any silver at any time in the foreseeable future.

While the expense of administering this tax cannot be accurately determined, it is estimated that funds in excess of \$60,000 per annum are necessary to this end. Collection of this tax during fiscal year 1961 dropped to \$14,000. Having outlived its purpose, the tax is a deterrent to the normal channels of trade.

It is one of the built-in provisions which had some reason back in 1934, but absolutely no reason now. The cost to administer this act is four or five times greater than the \$14,000 which is collected.

The effect of this tax is to prevent the operation of a futures market to deny the user, dealer, refiner, or miner of silver an opportunity to protect his operation against otherwise unavoidable market risks. For example if a user of silver makes a profit on a sale of silver scrap generated in his processing operation because the market price of silver has advanced since his original purchase, he must pay a 50-percent tax on the profit realized unless he promptly buys an equivalent amount of refined silver, thus preventing him from using his own judgment as to the quantity of silver he should hold in inventory. If on a subsequent sale of scrap he sustains a loss because the market price of silver has declined, he has no way to offset this loss against the profit realized on the previous sale.

They are the people represented by the distinguished Senator from Maryland [Mr. BUTLER] and the distinguished Senator from Rhode Island [Mr. PASITORE].

There is no question that the silver transfer tax put an end to the development of New York as the principal market, and at the same time caused London to exist as the most important clearing point for international silver trade. No other commodity, regardless of its intrinsic value or importance to the public welfare is subject to similar taxation.

My intention was to offer an amendment at this session to carry out the recommendation of the President and the

Treasury Department to repeal the tax on silver transfers. I, together with many other Senators who are interested in the problem, discussed the situation with the Treasury, and the Treasury submitted a suggested amendment and discussed it with the Committee on Finance. Some 30 Senators have joined with me in cosponsoring the amendment.

However, there seems to be some misunderstanding in one segment of the industry as to the effect of such a repeal. That segment is comprised of those who finally buy the silver and process it into silver plate, silver ornaments, and articles of that kind. There is no misunderstanding on the part of the President of the United States, the Treasury Department, the miners, those who refine silver, or the group who make the silver into bullion or wire and then, in turn, sell it to manufacturers in Rhode Island, Maryland, New York, and other places. What has happened is that those manufacturers are now at the mercy of the London silver market as against the American market, and they cannot make their plans.

In all fairness, I should say that no hearings were held on this question. The proposal is tied into the Silver Purchase Act. What those who make silver plate or buy bullion or wire or silver sheet are talking about is not this tax. They want to put this tax together with the silver purchase tax. They are two different taxes. This is a complicated problem and involves fiscal policies of the U.S. Government which are well established by the Treasury Department. The people whom the Senator from Rhode Island and the Senator from Maryland represent should be heard.

I have spoken with many of the Senators who have joined with me as cosponsors of the amendment. I observe in the Chamber the distinguished Senator from Montana [Mr. MANSFIELD] and also the distinguished Senator from Idaho [Mr. CHURCH], whose State is vitally interested in this question, because it produces a greater amount of silver than is produced in any other State in the Union. We shall not offer the amendment at this time, but I thought I should place in the RECORD a letter from about 15 Senators who are interested in this question, in which they suggest this course of action. Then we may have a better understanding of the problem and can take up the whole silver question in January.

I have spoken with the distinguished chairman of the Committee on Finance the Senator from Virginia [Mr. BYRD]. I feel certain that that committee will be sympathetic to considering the problem.

Much has been said about business and economic conditions in the United States. Some persons have said that the economy is not moving forward fast enough and is not advancing as it should; that the gross national product, percentage-wise, is not as high as it should be. These are two built-in factors which are causing a part of the trouble. The repeal of the transfer tax would provide flexibility in the silver market and allow the purchasers of silver to make their plans. I do not know whether this pro-

with amendments on page 1, at the beginning of line 5, to insert "may be issued a visa and"; and in line 10, after the word "Act," to insert a colon and "And provided further, That this exemption shall apply only to a ground for exclusion of which the Department of State or the Department of Justice has knowledge prior to the enactment of this Act."

The amendments were agreed to.

The amendments were ordered to be engrossed, and the bill to be read a third time.

The bill was read the third time, and passed.

DARIO TACQUECHEL

The Senate proceeded to consider the bill (H.R. 7582) for the relief of Dario Tacquechel, which had been reported from the Committee on the Judiciary with an amendment in line 4, after the name "Dario", to strike out "Tacquechel" and insert "Tauechel".

The amendment was agreed to.

The amendment was ordered to be engrossed, and the bill to be read a third time.

The bill was read the third time, and passed.

The title was amended, so as to read: "An act for the relief of Dario Tauechel."

CERTIFICATES OF HONORABLE DISCHARGE IN LIEU OF CERTIFICATES OF DISENROLLMENT, COAST GUARD RESERVE

The Senate proceeded to consider the bill (H.R. 2292) to authorize the Secretary of the Treasury to issue certificates of honorable discharge in lieu of certificates of disenrollment to certain persons who served as temporary members of the United States Coast Guard Reserve during World War II, which had been reported from the Committee on Commerce with amendments on page 1, line 6, after the numerals "763", to strike out "Honorable discharge" and insert "Certificate of"; on page 2, line 1, after the word "issue", to strike out "a certificate of honorable discharge" and insert "an appropriate certificate of honorable service"; in line 7, after the word "honorable", to strike out "discharge" and insert "service"; and in the first line after line 12, after the numerals "763", to strike out "Honorable discharge" and insert "Certificate of honorable service".

The amendments were agreed to.

The amendments were ordered to be engrossed, and the bill to be read a third time.

The bill was read the third time, and passed.

The title was amended, so as to read: "An Act to authorize the Secretary of the Treasury to issue certificates of honorable service in lieu of certificates of disenrollment to certain persons who served as temporary members of the United States Coast Guard Reserve during World War II."

BILL PASSED OVER

The bill (H.R. 11217) to amend section 6112 of title 10, United States Code, was announced as next in order.

Mr. MANSFIELD. Over.

The PRESIDING OFFICER. The bill will be passed over.

NATIONAL SAFETY COUNCIL 50TH ANNIVERSARY YEAR

The joint resolution (S.J. Res. 222) providing for the designation of the period October 1962 through October 1963 as "National Safety Council 50th Anniversary Year" was considered, ordered to be engrossed for a third reading, was read the third time, and passed, as follows:

Resolved by the Senate and House of Representatives of the United States of America in Congress assembled, That the President is authorized and requested to issue a proclamation designating the period October 1962 through October 1963 as "National Safety Council Fiftieth Anniversary Year," and calling upon the governments of the States and communities and the people of the United States to join in observance of this significant occasion and to increase their efforts to reduce the number of accidents in homes, in industry, in public places, and on our streets and highways.

The preamble was agreed to.

NATIONAL GUARD PARTICIPATION IN REENACTMENT OF BATTLE OF ANTIETAM

Mr. MANSFIELD. Madam President, in view of the fact that a time limitation is involved, I move that the Senate proceed to the consideration of calendar 1944, Senate bill 3613.

The motion was agreed to; and the bill (S. 3613) to provide that participation by members of the National Guard in the reenactment of the Battle of Antietam shall be held and considered to be full-time training duty under section 503 of title 32, United States Code, and for other purposes, was considered, ordered to be engrossed for a third reading, read the third time, and passed, as follows:

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That (a) any member of the Army National Guard of the United States or the Air National Guard of the United States who, in his status as a member of the National Guard, voluntarily participates in the reenactment of the Battle of Antietam shall, while participating in and while proceeding directly to and from any such reenactment, pageant, or ceremony, be held and considered to be engaged in full-time training duty under a call or order to perform training under the provisions of section 503 of title 32, United States Code; but no such member shall be entitled to any pay or allowances from the Federal Government on account of his participation in any such reenactment, pageant, or ceremony.

(b) With respect to the transportation of members described in subsection (a) of this section, maximum utilization shall be made of transportation facilities issued to National Guard units by the Federal Government, and

in any case in which such facilities are inadequate for such purpose, transportation facilities of the Armed Forces may be used to the extent deemed practicable by the Secretary of Defense.

EXECUTIVE SESSION

Mr. MANSFIELD. Madam President, I move that the Senate proceed to the consideration of executive business, to consider the nominations on the Executive Calendar, beginning with the new reports.

The motion was agreed to; and the Senate proceeded to the consideration of executive business.

The PRESIDING OFFICER (Mrs. NEUBERGER in the chair). If there be no executive reports of committees, the nominations on the Executive Calendar, beginning with the new reports, will be stated.

POSTMASTERS

The legislative clerk proceeded to read sundry nominations of postmasters.

Mr. MANSFIELD. Madam President, I ask unanimous consent that these nominations be considered en bloc.

The PRESIDING OFFICER. Without objection, the nominations will be considered en bloc; and, without objection, they are confirmed.

DIPLOMATIC AND FOREIGN SERVICE

Mr. MANSFIELD. Madam President, I move that the Senate proceed to the consideration of the nomination for the Diplomatic and Foreign Service.

The PRESIDING OFFICER. Without objection, the nomination will be stated.

The legislative clerk read the nomination of Charles E. Bohlen, of the District of Columbia, a Foreign Service officer of the class of career ambassador, to be Ambassador Extraordinary and Plenipotentiary of the United States of America to France.

The PRESIDING OFFICER. The question is on agreeing to the motion that the Senate proceed to the consideration of this nomination.

The motion was agreed to; and the Senate proceeded to consider the nomination.

Mr. MANSFIELD. Madam President, I wish to state, for the record, and at the request of the distinguished Senator from South Carolina [Mr. THURMOND], that he is opposed to this nomination, and wishes to be so recorded.

The PRESIDING OFFICER. The question is, Will the Senate advise and consent to this nomination?

The nomination was confirmed.

Mr. MANSFIELD. Madam President, I ask unanimous consent that the President be immediately notified of the confirmation of all nominations confirmed this day.

The PRESIDING OFFICER. Without objection, the President will be notified forthwith.

PROTOCOL MODIFYING AND SUPPLEMENTING CONVENTION FOR AVOIDANCE OF DOUBLE TAXATION AND PREVENTION OF FISCAL EVASION WITH RESPECT TO TAXES ON INCOME—REMOVAL OF INJUNCTION OF SECRECY

Mr. MANSFIELD. Madam President, I ask unanimous consent that the injunction of secrecy be removed from Executive G, 87th Congress, 2d session, the protocol between the United States and Japan, signed at Tokyo on August 14, 1962, modifying and supplementing the convention for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income signed at Washington on April 16, 1954, as supplemented by the protocol signed at Tokyo on March 23, 1957, and as modified and supplemented by the protocol signed at Tokyo on May 7, 1960, transmitted to the Senate today by the President of the United States, and that the protocol, together with the President's message, be referred to the Committee on Foreign Relations, and that the President's message be printed in the RECORD.

The PRESIDING OFFICER. Is there objection? The Chair hears none, and it is so ordered.

The message from the President is as follows:

To the Senate of the United States:

With a view to receiving the advice and consent of the Senate to ratification, I transmit herewith the protocol between the United States and Japan, signed at Tokyo on August 14, 1962, modifying and supplementing the convention for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income signed at Washington on April 16, 1954, as supplemented by the protocol signed at Tokyo on March 23, 1957, and as modified and supplemented by the protocol signed at Tokyo on May 7, 1960.

I transmit also for the information of the Senate the report by the Secretary of State with respect to the protocol and a copy of each of the two notes and each of the two letters, with accompanying memorandum, referred to in and enclosed with that report.

It is hoped that the Senate will be able to give consideration to the protocol transmitted herewith, together with the 1960 protocol which is under consideration in the Committee on Foreign Relations, with a view to their ratification as soon as possible.

JOHN F. KENNEDY.

THE WHITE HOUSE, August 31, 1962.

LEGISLATIVE SESSION

Mr. MANSFIELD. Madam President, I move that the Senate resume the consideration of legislative business.

The motion was agreed to; and the Senate resumed the consideration of legislative business.

REVENUE ACT OF 1962

Mr. MANSFIELD. Madam President, I move that the Senate resume the con-

sideration of H.R. 10650, the Revenue Act of 1962, which was laid aside temporarily, for the consideration of other business.

The motion was agreed to; and the Senate resumed the consideration of the bill (H.R. 10650) to amend the Internal Revenue Code of 1954 to provide a credit for investment in certain depreciable property, to eliminate certain defects and inequities, and for other purposes.

Mr. COTTON. Madam President, I offer the amendment which I send to the desk and ask to have stated.

The PRESIDING OFFICER. The amendment will be stated.

The LEGISLATIVE CLERK. At the end of the bill it is proposed to add the following new section:

SEC. 28. EFFECTIVE DATE OF AMENDMENT TO SECTION 1374 (b).

The amendment made by section 2(b) of Public Law 86-376 (73 Stat. 699) shall take effect on September 2, 1958.

Mr. COTTON. Madam President, this is an amendment to correct a technicality in the law. I understand that the amendment is acceptable to the manager of the bill and also to the senior minority member of the committee. I hope I am correct in stating that they are willing to accept the amendment.

Mr. KERR. Madam President, the Senator from New Hampshire is correct; and, Madam President, the amendment is acceptable to the Treasury. I recommend its adoption.

The PRESIDING OFFICER. The question is on agreeing to the amendment of the Senator from New Hampshire.

The amendment was agreed to.

Mr. COTTON. Madam President, I ask unanimous consent to have printed at this point in the RECORD a statement on the amendment, which I send to the desk.

There being no objection, the statement was ordered to be printed in the RECORD, as follows:

BRIEF EXPLANATION OF AMENDMENT TO H.R. 10650 INTRODUCED BY MR. COTTON

In the Technical Amendments Act of 1958 the Congress enacted subchapter S, relating to small business corporations. Under these provisions a qualified small business corporation can elect to have its income taxed directly to its shareholders and to have its net operating losses passed through directly to its shareholders. As initially enacted in 1958, section 1374 allowed a shareholder of an electing small business corporation to deduct his pro rata share of the corporation's net operating loss for his taxable year in which or with which the taxable year of the corporation ends. However, a shareholder who dies before the end of the corporation's taxable year was deprived of his share of the net operating loss which occurred in the corporation's taxable year in which he died because there was no taxable year of the corporation that ended with or within the abbreviated taxable year of the shareholder. Because of this, section 1374 was amended by section 2(b) of Public Law 86-376, 86th Congress, 1st session, to make it clear that in such a case a deceased shareholder will not be denied his pro rata share of the electing small business corporation's net operating loss. This amendment, however, was made effective only from the day after the date of the enactment of Public Law 86-376. This was September 24, 1959.

The purpose of the proposed amendment is to make the effective date of this particular

provision of Public Law 86-376 September 2, 1958, the date of the original enactment of subchapter S, in order that shareholders of an electing small business corporation who died prior to September 24, 1959, are also not denied their pro rata share of the net operating loss of the electing small business corporation occurring in the year of the shareholder's death.

Mr. SPARKMAN. Madam President, I call up my amendment identified as "8-25-62-A."

The PRESIDING OFFICER. The amendment will be stated.

The LEGISLATIVE CLERK. After section 21 of the bill, relating to treaties, it is proposed to add the following new section:

SEC. 22. DEDUCTION FOR DEPRECIATION BY TENANT-STOCKHOLDER OF COOPERATIVE HOUSING CORPORATION.

(a) ALLOWANCE OF DEDUCTION.—Section 216 (relating to deductions by tenant-stockholders of a cooperative housing corporation) is amended by—

(1) amending the heading thereof to read as follows:

"SEC. 216. DEDUCTION OF TAXES, INTEREST, AND DEPRECIATION BY COOPERATIVE HOUSING CORPORATION TENANT-STOCKHOLDER."; and

(2) adding at the end of section 216 the following new subsection:

"(c) So much of the stock of a tenant-stockholder in a cooperative housing corporation as is allocable, under regulations prescribed by the Secretary or his delegate, to a proprietary lease or right of tenancy in property subject to the allowance for depreciation under section 167(a) shall, to the extent such proprietary lease or right of tenancy is used by such tenant-stockholder in a trade or business or for the production of income, be treated as property subject to the allowance for depreciation under section 167(a)."

Mr. SPARKMAN. Madam President, this amendment follows the policy of section 216 of the Internal Revenue Code of 1954 that a tenant-stockholder of a cooperative housing corporation be treated in a manner consistent with that of the owner of improved real property. It makes it clear that when such a tenant-stockholder leases all or part of his interest in the property of such corporation and thereby uses such property in a trade or business or for the production of income, such portion of the basis of his stock as is allocable to a proprietary lease or right of tenancy in property subject to the allowance for depreciation shall itself be treated as property subject to the allowance for depreciation.

Mr. DOUGLAS. Madam President, will the Senator from Alabama yield for a question?

Mr. SPARKMAN. I yield.

Mr. DOUGLAS. Am I correct in understanding that this amendment is designed to permit those who purchase apartments in a cooperative, or who become members of a housing cooperative, to obtain loans from building and loan associations?

Mr. SPARKMAN. No; this has no connection with savings and loan associations. As it stands now, persons who own apartments, we will say in a building that is condominium—

Mr. DOUGLAS. The Puerto Rican system—horizontal slices of an apartment.

Mr. SPARKMAN. That is correct. If a person rents out that kind of property, he can deduct depreciation and expenses, and so forth; but the person who owns almost the identical same thing in a cooperative housing cannot do that. This amendment puts those persons on a par with the others.

Mr. DOUGLAS. I think this is a constructive amendment.

Mr. JAVITS. Madam President, will the Senator yield for a question?

Mr. SPARKMAN. I yield.

Mr. JAVITS. This amendment, of course, seeks to take account of the legal form of organization which represents a proprietary lease and a stock interest, which is a quite usual form of organization, for example, in New York City, for cooperatives. As a matter of fact, I happen to have one of those, myself. So what this amendment would do, as the Senator has explained in response to the Senator from Illinois, is treat property owners the same across the board, regardless of the form of legal organization of the cooperative, with respect to the availability of deductions for interest, and so forth.

Mr. SPARKMAN. That is correct.

Mr. SMATHERS. Madam President, will the Senator yield?

Mr. SPARKMAN. I yield.

Mr. SMATHERS. As I understand the amendment, it merely permits those persons who buy cooperative apartments and call them their homes to get the same advantage of the tax deduction for depreciation, and so forth, as people who own their own homes.

Mr. KERR. In the event they rent them out.

Mr. SPARKMAN. Yes; in the event they rent them out. It places all property ownership on the same level.

Mr. KERR. Madam President, the amendment has been submitted to the Treasury. It has been submitted to members of the committee. The Senator from Oklahoma feels it is a worthy amendment, and recommends its adoption.

The PRESIDING OFFICER. The question is on agreeing to the amendment of the Senator from Alabama.

The amendment was agreed to.

Mr. KERR. Madam President, I move that the vote by which the amendment was agreed to be reconsidered.

Mr. JAVITS. Madam President, I move to lay that motion on the table.

The motion to lay on the table was agreed to.

Mr. SPARKMAN. Madam President, on behalf of Senators JAVITS, BEALL, LAUSCHE, CASE, and myself, I call up my amendments identified as "8-30-62-G."

The PRESIDING OFFICER. Does the Senator wish the amendments to be read?

Mr. DOUGLAS. Madam President, I wonder if we may have an explanation of the amendment.

Mr. SPARKMAN. Madam President, I ask unanimous consent that the amendments be printed without their being read.

The PRESIDING OFFICER. Without objection, it is so ordered.

The amendments ordered to be printed in the RECORD are, as follows:

On page 74, line 18, after the comma strike out "and".

On page 74, line 20, after the comma insert "and certificates of deposit in, or obligations of, a corporation organized under a State law which specifically authorizes such corporation to insure the deposits or share accounts of member associations,".

On page 74, line 24, strike out "and" before "(v)".

On page 74, line 25, after "clause (iii)" and insert ", and (vi) property used by the association in the conduct of the business described in subparagraph (B)".

On page 75, line 9, after "or" insert "real property used primarily for church purposes,".

On page 75, line 10, after "property" insert "or real property used primarily for church purposes, or property acquired through the liquidation of defaulted loans described in this clause".

On page 75, line 11, strike out "70" and insert "60".

On page 75, line 17, strike out "units, or" and insert "units or real property used primarily for church purposes,".

On page 75, line 19, after "units" insert "or real property used primarily for church purposes, or property acquired through the liquidation of defaulted loans described in this clause".

On page 75, line 24, strike out "27" and insert "36".

On page 76, line 2, beginning with the comma, strike out all through "(c)" in line 9.

On page 76, line 11, strike out "none" and insert "not more than 3 percent".

On page 76, line 12, strike out the closing quotation marks and after line 12 insert the following: "At the election of the taxpayer, the percentages specified in this paragraph shall be applied on the basis of the average assets outstanding during the taxable year, in lieu of the close of the taxable year, computed under regulations prescribed by the Secretary or his delegate."

Mr. SPARKMAN. Madam President, I offer this amendment to make certain minor changes in the definition of a domestic building and loan, primarily designed to permit a more reasonable investment in loans on multifamily dwellings.

First of all the amendment would permit the inclusion of "property acquired through liquidation of defaulted loans" in the appropriate residential categories under paragraph (D).

My amendment would also increase permissible apartment lending by 9 percentage points.

Mr. DOUGLAS. Madam President, if the Senator will yield, from what to what? May I ask what the present limit is?

Mr. SPARKMAN. There is no limitation under existing law, but this amendment would increase by 9 percentage points what the bill would do.

Mr. DOUGLAS. What does the bill have in it?

Mr. SPARKMAN. Twenty-seven.

Mr. KERR. Madam President, if the Senator will yield, the bill has in it 70 percent of 90 percent to be invested in residential units of four or less.

Mr. DOUGLAS. That is the conventional type, but what about more than four?

Mr. KERR. If the Senator will listen, I will explain it. The amendment would require that 60 percent of 90 percent be invested in the one to four type, and therefore another 10 percent of 90 percent could be invested in more than four-family units.

Mr. SPARKMAN. Yes, but there is a further restriction under subparagraph (E) which would limit multifamily loans to 36 percent, which is 9 percent more than the 27 percent in the bill as reported.

Mr. KERR. That is correct; 9 percent more.

Mr. SPARKMAN. It is 27 percent in the bill, and the amendment would raise it to 36 percent.

Mr. DOUGLAS. What is it before the bill is passed?

Mr. SPARKMAN. There is no limitation as far as tax law is concerned.

Mr. DOUGLAS. Is there no limitation or no permission?

Mr. SPARKMAN. There is no limitation.

Mr. DOUGLAS. In practice, have not the building and loan associations confined themselves to loans on dwellings of from one to four units?

Mr. SPARKMAN. No. It all depends upon the community. I would say "Yes" to the question of the Senator with respect to the type of housing we have in the particular area of my hometown, but my guess would be that as to a building and loan association in the city of Chicago, the Senator would find—

Mr. KERR. That it is already lending more than this language provides.

Mr. DOUGLAS. I would like to wait for the final explanation of the Senator from Alabama.

Mr. SPARKMAN. I shall be glad to proceed.

The present limitations in paragraphs (D) and (E) on page 75 have the effect of limiting an association's investment in apartment loans to between 15 percent and 20 percent of assets.

Today some 30 percent of all residential construction is in the apartment category and such construction is on the upturn. The proportion has doubled since the 15 percent of 1959.

As land becomes more costly and difficult to get, buildings tend to extend higher into the air. That is what has happened.

This is due to urban renewal, increased urbanization, and increases in the number of elderly families. The resources of the savings and loan business are vitally needed to finance multifamily housing. Federal law in recent years has been amended generally to provide more assistance to multifamily housing. This new restriction would exert a contrary influence.

Ideally, all types of housing should be treated equally, but reasonable flexibility could be accomplished by increasing permissible apartment lending by 9 percentage points over the committee bill. This would enable substantial multifamily financing, but still maintain a distinction as established by the Senate Finance Committee.

The amendment would also permit real property used primarily as a church and being held by a savings and loan association to be treated the same as a loan secured by one- to four-family property under subparagraph (D).

My amendment would also permit a very limited—3 percent of assets—ownership of private corporate stock by savings and loan associations. This is necessary because State and Federal associations currently have authority to make minor investments in certain closely related service organizations and quasi-public corporations. Last year the Congress, under the sponsorship of Senators FULBRIGHT and ERVIN, enacted legislation to permit Federal associations to make limited investments in State business development commissions. There are various State enacted savings and loan corporations and insurance funds which are serving a worthy purpose, and there is a trend for the establishment of service corporations to acquire electronic accounting equipment for the use of participating institutions. A 3-percent exemption would be sufficient to permit these worthy investments, but not in any way suggest any change in the basic function of savings and loan institutions.

The last part of my amendment would permit a savings and loan association to elect the percentages under the bill to be applied on the basis of its average outstanding assets during the year, rather than at the end of the taxable year.

This amendment has no revenue consequences and is simply a technical perfecting amendment. I understand that the managers of the bill have no objection to my amendment.

I may say this amendment likewise has been cleared with the Treasury. As a matter of fact, it was at the suggestion of the Treasury that I reintroduced the measure that I had introduced several days ago, in that we have changed the percentages and we do make it possible to take care of such situations as I have mentioned among savings and loan associations in several States, for instance, in the State of Maryland.

Let us consider the situation in the State of Maryland, or in the State of Ohio. The State of Ohio has a very fine insurance program of its own. This amendment would permit the making of the necessary deposits in statewide insurance corporations without affecting its eligibility for special tax consideration under the bill. It is necessary to have certificates of deposit, as I think they are called.

Mr. JAVITS. Madam President, will the Senator yield?

Mr. SPARKMAN. Before I yield, I wish to say that the Senator from Florida [Mr. SMATHERS] has been greatly interested in this amendment, and his name should have been included as a cosponsor of the amendment. I hope that it may appear in the RECORD that the Senator from Florida is a cosponsor of the amendment.

Mr. SMATHERS. Madam President, will the Senator yield?

Mr. SPARKMAN. I yield.

Mr. SMATHERS. I thank the able Senator. In the committee we discussed the problem as to what should be the limitations with respect to these operations. We tried at that time to get some language in the bill, as we discussed it, but, frankly, we were not able to do so at that time. I am glad the Senator from Alabama, who has taken such an interest in this problem for so long a time, has offered the amendment. I associate myself with him.

Mr. DOUGLAS. Madam President, will the Senator yield?

Mr. SPARKMAN. I yield to the Senator from Illinois.

Mr. DOUGLAS. This is a very important amendment, which is brought up with very few Senators in the Chamber. It would result in a further intensification of the change in the functions of building and loan associations, and I think it should be scrutinized very carefully.

Building and loan associations were originally organized by groups of neighbors who combined their savings in order to provide individual homeownership. This was thereafter broadened to include not merely the individual home, but also buildings of not more than one to four housing units, when the owner was to be the occupant of one of the apartments, frequently serving as the janitor. That extension was constructed, but it was intended to provide mutual associations for the purpose of promoting homeownership.

The investments of the building and loan associations were in the field of homes which were individually owned. They have been a very constructive force in American life. Again and again on the floor of the Senate I have defended the building and loan mutuals. I think they are a most constructive force.

In the process of time a great many changes have crept into the building and loan associations. Many of them have become larger. In many instances, the neighborhood quality has been lost. In many instances, while ostensibly the depositors and shareholders are those who direct the business, the control passes to an inner group, with all the difficulties this sometimes involves.

To complicate the problem still further, stock building and loan associations have grown up, particularly in California, where they have driven interest rates up and where much speculation has been carried on of a none-too-savory character.

Now it is proposed to increase the zone of commercial investments of the building and loan associations, divorced from any ownership. If this were to finance the purchase of cooperative apartments or condominiums I would most heartily agree.

The Senator from Illinois comes from the second largest city in the United States. We well recognize the importance of apartments and multifamily housing units and buildings. I think there should be a greater extension of this in the suburbs, as a matter of fact, than is now the case.

Mr. SPARKMAN. Of course, eventually there will have to be.

Mr. DOUGLAS. But in this connection I point out that if 36 percent of the assets could be invested in commercially operated apartments and 3 percent of the assets could be invested in State development associations, the building and loan associations would, more and more, be permitted to become a type of bank, not a mutual association of prospective homeowners.

This may be proper. This may be the way we should move. I certainly do not want to agree to the amendment, with only five Senators on the floor at 7:25 o'clock in the evening. I think it should be scrutinized very carefully.

Mr. SPARKMAN. We are not seeking by the amendment to extend the savings and loan association authority. There is nothing in the amendment which would extend the savings and loan association authority beyond what it is today.

Mr. DOUGLAS. It would be extended from 27 percent to 36 percent.

Mr. SPARKMAN. No. The bill would put a limitation on the authority of savings and loans associations to invest. The language of the bill would not affect what is allowed today under the basic law. That basic law came from the Banking and Currency Committee.

Mr. DOUGLAS. I think we should scrutinize that law carefully.

Mr. SPARKMAN. What we have said is, "It is all right to have a restriction—"

Mr. DOUGLAS. When did that law come from the Committee on Banking and Currency?

Mr. SPARKMAN. Provisions regarding the various powers given to the savings and loan associations came from the Committee on Banking and Currency.

Mr. DOUGLAS. When?

Mr. SPARKMAN. The amendment to which I referred a moment ago is an example. The savings and loan associations were authorized to invest one-half of 1 percent in making loans to State development corporations or local development corporations.

Mr. DOUGLAS. The Senator from Illinois would agree to that, but that is only a sprinkle of salt.

Mr. SPARKMAN. Yes.

Mr. DOUGLAS. That is only one-half of 1 percent.

Mr. SPARKMAN. That is one of the provisions.

Mr. DOUGLAS. When did we provide that a very large percentage of assets could be invested in commercially run apartment buildings? When was that done?

Mr. SPARKMAN. Under the existing tax law there is no limitation on the savings and loan associations as to multifamily buildings. The bill would provide a limit of 27 percent. We said, in effect, "A limitation is all right, but the proposed limitation would be too restrictive." We agreed to 36 percent.

I say to the Senator from Illinois that these figures were drawn up with the agreement of the Treasury Department.

Mr. DOUGLAS. The Treasury Department is not interested in homeownership. It is interested in financial

solvency. I happen to be interested in homeownership.

Mr. SPARKMAN. The ownership of an apartment or a unit of an apartment is as much ownership as ownership of a single family dwelling.

Mr. DOUGLAS. If this were confined to cooperative housing or to a condominium I would agree with the Senator, but apparently the amendment proposes that there be commercial investment, like that of a commercial bank, of up to 36 percent of the assets, and plus 3 percent to be used for development.

Mr. SPARKMAN. For these special purposes.

Mr. DOUGLAS. That means the figure could virtually go up to 40 percent for purposes other than those originally intended.

Mr. SPARKMAN. No. The 3 percent to which the Senator refers includes such amounts as would have to be used to buy furniture and office equipment. That is a necessary expense of operation.

Mr. DOUGLAS. There is a great difference between making loans to enable people to purchase cooperative apartments and making loans to real estate operators who operate apartment houses as a commercial venture.

The building and loan associations certainly were intended to promote homeownership. I am not acquainted with the technique of the savings bank institutions, which are the opposite number, in a sense, of the building and loan associations on the Atlantic coast.

Mr. SPARKMAN. May I make a comment at that point?

Mr. DOUGLAS. It may be that they have such powers.

Mr. SPARKMAN. They have. The bill would not limit them in any way.

Mr. DOUGLAS. I understand.

Mr. SPARKMAN. I am not in favor of limiting them. They have rendered an excellent service in financing home mortgages.

Mr. DOUGLAS. The mutual savings banks on the Atlantic seaboard differ from the building and loan associations in the remainder of the country, in that the mutual savings banks, as I understand, are associations of savers. They primarily put their investments in real estate because that was a very handy thing to do. But their purpose was not primarily to promote home ownership. Their purpose was to find safe investments for their depositor members.

It may well be that there should be no restrictions on the mutual savings banks. I am not saying that there should be. I am not very well acquainted with the mutual savings banks because there are not many of them out west. But I do know something about the savings and loan institutions; and, as one who has believed in them, worked for them, and has tried to protect them, and yet not wanted to give them unfair privileges, I say we should consider for a time before we put them in the business of loaning on commercial real estate.

Mr. KERR. Madam President, will the Senator from Alabama yield to me?

Mr. SPARKMAN. I yield to the Senator from Oklahoma.

Mr. DOUGLAS. I am always glad to yield for a question, although I always wonder what is coming.

Mr. KERR. I have never started on a more friendly basis.

Mr. DOUGLAS. I assure the Senator from Oklahoma that is mutual and reciprocal.

Mr. KERR. As I understand, under existing law there is no restriction.

Mr. DOUGLAS. Perhaps there should be.

Mr. KERR. I am not talking about that. But under existing law there are no restrictions on the building and loan associations here in Washington, New York City, Chicago, or other cities in the matter of the lending of their money on apartment buildings.

Mr. DOUGLAS. That statement has come as a surprise to me. I have been a member of the Subcommittee on Housing of the Committee on Banking and Currency as long as I have been in the Senate. I think the Senator from Alabama [Mr. SPARKMAN] will agree that I have tried to attend quite regularly and have taken my duties and obligations seriously.

Mr. SPARKMAN. The Senator from Illinois has been a very effective and efficient member.

Mr. DOUGLAS. I am somewhat surprised at the proposal. I was startled when the Senator from Alabama said that already 30 percent of the housing was in multifamily housing.

Mr. KERR. Madam President, will the Senator yield?

Mr. SPARKMAN. I yield.

Mr. KERR. The Senator was present when the bill was reported from the Finance Committee. A suggestion as to a restriction was made. It was agreed not that we would change the restriction in the existing law, but that we would place one in the bill with reference to building and loan associations which is not now in the law.

After we took that action, the distinguished Senator from Alabama and others who seemed to know more about this subject than did the Senator from Oklahoma came to the Senator from Oklahoma and said, "You gentleman have placed a restriction in the law that has not been in it and is not in it. You have actually made it possible not only to slow down, but to stop the present trend toward lending money by the building and loan associations to apartments, in connection with the building of apartment houses."

The Senator from Oklahoma discussed the subject with the gentlemen who were talking with him. He discussed it with representatives of the Treasury Department, and with some members of the committee. Had he thought that the Senator from Illinois was interested in it, he certainly would have discussed the subject with him. He found no objection on the part of anyone, and felt that the proposed amendment would be constructive.

Mr. DOUGLAS. I heard about the amendment this afternoon when Mr. Coan courteously came to my office to discuss it with me.

Mr. KERR. If it is the purpose of the Senator that no action be taken on the proposal tonight, I know of nothing that we can do. It is the pending business. We shall have to let it go over.

Mr. JAVITS. Madam President, will the Senator yield to me?

Mr. SPARKMAN. Certainly.

Mr. JAVITS. I believe I can clarify the situation. The savings and loan associations in the East, including New York, would be seriously affected.

Mr. DOUGLAS. Are there many in the State of New York?

Mr. JAVITS. There are a great many. Hundreds of millions of dollars are on deposit.

Mr. DOUGLAS. They are mutual savings banks also.

Mr. JAVITS. No, we have savings and loan associations, which are also mutual. That is the point I wish to make to the Senator. It is a subject of great complaint to me and to my colleague [Mr. KEATING].

To be realistic, the amendment would not establish a relaxation. It would establish a restriction. The question is, What shall be the character of the restriction? Let us be clear on that point. The present definition of the law is that a domestic building and loan association is one the substantial business of which is confined to the making of loans to members. That is all. Everyone who deposits \$5 in the bank is a member.

We are really dealing with a new situation. The savings and loan associations which the Senator envisaged were originally associations of small groups of members, doing for housing what credit unions did for small loans.

Mr. DOUGLAS. They preceded credit unions.

Mr. JAVITS. It was the same general idea. However, what has happened is that those institutions have become very large thrift institutions, competing with mutual savings banks and with each other. The Senator may have noticed in the press that there has been great competition for deposits by savings and loan associations.

Mr. DOUGLAS. I believe we have noticed that in Maryland.

Mr. JAVITS. In Maryland and in California. They give depositors more interest to attract deposits to their institutions. There has been a development of that character. That is, they have become competing thrift associations with banks and with other savings and loan associations.

Second, the market for loans has naturally changed from almost exclusively the private house, which was its original purpose, or the small two-, three-, or four-family house, to the multifamily dwelling.

Naturally as these institutions have attracted more assets they have had more loaning power.

I should like to add one other fact which has not been mentioned.

Every savings and loan institution that is a State savings and loan institution is under State control and under the State jurisdiction of its banking superintendent. The Federal savings and

loan institutions are under Federal control and Federal inspection. That applies to both Federal and State because it relates to taxes. We can reach them through income taxes.

People have come to us and to Senators from other States—for example, to the Senators from Maryland [Mr. BEALL and Mr. BUTLER], the Senators from Delaware [Mr. WILLIAMS and Mr. BOGGS], or the Senators from other Eastern States—and have pointed out that under our rather lower interest rate situations—

Mr. DOUGLAS. By "lower" what does the Senator mean?

Mr. JAVITS. By "lower" I mean lower rates on mortgages. They are able to earn enough money, if they are restricted they would be under the new restrictions. I point that out to the Senator because I do not think he gave that full credit in his discussion. They are able to earn enough money. With the new restriction, which they have never had before, which would be imposed upon them, they would have to go out of business. No matter what we do or say about it, there is an intolerable pressure upon them.

When I came into this situation and took it up with other Senators who are similarly situated, such as the Senator from Alabama [Mr. SPARKMAN] and some other Senators, it became clear to us that there had to be some alleviation, though not of the situation in which the institutions find themselves today. They are fine now. They would be glad if there were no change in the law. They would be happy if the bill were killed. But there had to be an alleviation of the situation in which the committee amendment would put them, because for the first time there would be a restriction.

I think there is some justice to the restriction in the sense that competition between thrift associations, such as mutual savings and savings and loan associations should be somewhat regulated so that the savings and loan associations would be preponderantly in the real property field. I am inclined to agree with that. But we cannot strangle them in the process. Therefore, we must give them a little more flexibility, which they need in order to operate—especially the eastern concerns. Eastern institutions do not earn the large interest on mortgages which earned in the Far West, not only because of State restrictions but also because of competition, which is good. We have to give them a little more flexibility.

The amendment of the Senator from Alabama would give them the very minimum they feel they need. They feel they need more. But I decided it would be very difficult to have any amendment to the bill approved, with my stalwart friend here holding the ramparts, and therefore I felt it was better to go along with what might be done and which the institutions could conceivably live than to try for something more.

That is the story in a nutshell. I agree with the Senator from Oklahoma that no "hidden ball" tricks are involved. If

the Senator feels disquieted about it and does not feel satisfied with any explanations that have been made, let the Senator think about it. I assure the Senator that I have told him everything I know about it.

Mr. DOUGLAS. I am sure of the good faith of the Senator from New York, but I point out that this may be the shape of things to come, so to speak. If no restrictions have been imposed in the past on the percentage of the assets that a building and loan association can invest in commercial real estate—

Mr. SPARKMAN. Oh—

Mr. DOUGLAS. May I finish this paragraph?

Mr. JAVITS. The Senator means rentable housing.

Mr. DOUGLAS. Yes.

Mr. SPARKMAN. I would like to clear that up.

Mr. DOUGLAS. May I please finish this paragraph without being interrupted?

Mr. SPARKMAN. I would like to clear up this point.

Mr. DOUGLAS. The Senator can clear it up after I have finished the paragraph.

Mr. SPARKMAN. Very well. I will yield to the Senator to finish the paragraph.

Mr. DOUGLAS. Very well. If there have been no restrictions in the past on the proportion of the assets of a building and loan association—

Mr. SPARKMAN. That is exactly the point I wish to correct.

Mr. DOUGLAS. The Senator has stated that there are no restrictions.

Mr. SPARKMAN. So far as the present tax law is concerned. Actually, the States have different limitations. One State may have one limitation, and another State may have another limitation. So far as the use of the assets of the associations is concerned, there is a limitation. On Federal associations, the limitation is 20 percent—not to exceed 20 percent. That is in the law.

Mr. DOUGLAS. They do about half the business.

Mr. SPARKMAN. They would not be affected by this proposal.

Mr. DOUGLAS. This applies purely to States, then?

Mr. SPARKMAN. It says "not to exceed" this amount.

Mr. DOUGLAS. Not to exceed 36 percent?

Mr. SPARKMAN. Yes.

Mr. DOUGLAS. So the States can go up to 36 percent?

Mr. SPARKMAN. Unless the State laws prohibit it.

Mr. DOUGLAS. But the Federal institutions can handle up to that amount?

Mr. SPARKMAN. No; they cannot.

Mr. DOUGLAS. Then this is restricted to State institutions?

Mr. SPARKMAN. It is restricted to the tax definition. It is the definition for tax purposes that is involved.

Mr. JAVITS. Madam President, will the Senator yield?

Mr. SPARKMAN. I yield.

Mr. JAVITS. It does not affect the other type of restrictions.

Mr. KERR. The Senator is one of the smartest men on the floor. Will he let me try to help?

Mr. DOUGLAS. I fear the Senator from Oklahoma when he starts to help.

Mr. KERR. Under the bill we are saying that an institution of a certain character shall pay a certain rate of tax. It does not say that a building and loan association under Federal charter can do this.

Mr. DOUGLAS. In other words, through the taxing power the Senator would control the lending power. Is that correct?

Mr. SPARKMAN. We are saying that any institution that does not go above this situation will be taxed at a certain rate, rather than at the regular corporate rate.

Mr. DOUGLAS. That means that they will get favorable tax privileges if they lend up to 36 percent.

Mr. KERR. Now they are not taxed at all.

Mr. DOUGLAS. They can get favorable tax privileges which are accorded now to building and loan associations and granted to savings banks?

Mr. SPARKMAN. But—

Mr. DOUGLAS. I believe that is correct. Through the taxing power the Senator would alter the lending power.

Mr. JAVITS. If the Senator would put a semicolon at the end of that sentence and add "if permitted by the State or Federal regulatory authorities, as the case may be," that would be correct. In other words, it is correct to say that, if there is added "if permitted by the State or Federal regulatory authority, as the case may be." That is a correct statement, but not otherwise.

Mr. KERR. Under existing law, they are not taxed.

Mr. SPARKMAN. On this basis.

Mr. DOUGLAS. Madam President, this is a highly complicated subject. We are witnessing a very rapid transformation of the purposes and practices of the building and loan associations. They started as mutuals, and they are increasingly becoming stock associations.

Mr. SPARKMAN. No.

Mr. DOUGLAS. Yes, their stocks have been growing. Mutuals have been growing to the point that even within large mutuals membership control has been diminishing.

Now I have learned for the first time—I was probably uninformed not to know this before—that they are going into the field not only of home ownership, but also of commercial apartment buildings of more than four units. It is one thing to lend to a homeowner, even if he is a one-fourth homeowner. It is another to lend to a commercially owned apartment which acts as landlord and leases out apartments to tenants. That is a very different thing. I would like to retain as much individual home ownership as we can. Granted the importance of apartments—and I am aware of the importance of apartments perhaps even more than most Members of the Senate are—I would not like to see building and loan associations transformed into great real estate renting companies.

Mr. JAVITS. Madam President, will the Senator yield?

Mr. SPARKMAN. I yield.

Mr. JAVITS. I share the Senator's view. I do not care whether he will let this amendment go through tonight or not, although I am interested in the amendment. If the Senator has any disquietude about it, I do not wish to talk him out of it.

I point out to him that the difficulty with the Senator's position is that if we want to have competition for the thrift dollar, which encourages thrift—and the savings and loan associations are very fine competitors and they are very keen in attracting depositors—if we are to let them stay in business—and they are adversely affected if the bill goes through, I say to the Senator—then we are supplementing the pool of money which is available of 64 percent of their lending power. Let us take the Senator's figure, although it is not true. Let us not be myopic, though. Let us look at that percentage, but let us also look at the fact that the 64 percent is to be devoted to one- and four-family house loans.

The situation is one in which we either encourage and help these kinds of outfits to stay in business—and the fact is that they are competing for the thrift dollar just as mutual savings banks are—or we make it difficult for them to stay in business.

What the Senator is talking about has already happened; it is not happening because of the bill.

The eastern companies are very largely mutual companies, but there are some States—California is one of them—in which it is possible to have building and loan stock companies.

Mr. DOUGLAS. Yes. There have been some serious abuses in the neighboring State of Maryland.

Mr. JAVITS. State regulation is all important. I repeat to the Senator that whatever we do on the tax bill, the institutions are functioning, and the situation which we face will not be made or unmade by the tax bill. What we can make or unmake is the extent of the competition in certain areas where they are put out of competition if the new definitions remain as they are.

Mr. DOUGLAS. I hope the Senator from New York will not take it amiss—he is a good friend and we have been allies on most subjects—if I say that I believe that his point of view is myopic. He is looking at the savers, at the institutions which require capital. He is not looking at the ultimate end, which is to try to promote as much home ownership as possible.

Mr. JAVITS. I respectfully differ.

Mr. DOUGLAS. I do not wish to be an obstructionist, in spite of the comments which the Senator from Oklahoma has made.

Mr. KERR. Those were other times.

Mr. DOUGLAS. Yes. This is a very important subject. It may be that we should approach it through the housing laws of the country, rather than through the tax laws.

Mr. SPARKMAN. I find myself in complete agreement with the Senator on that point. That is why I offered the

amendment. We saw this restriction in the basic law, and we are trying to loosen it up a bit.

Mr. KERR. When the Senator called the matter to my attention I felt that his position had merit, and I agreed with it. If the Senator from Illinois wants the matter to go over, we will put it over.

Mr. SPARKMAN. I assure my good friend from Illinois—and of course I have no objection to having it go over for additional discussion—that there are no hidden tricks in this matter.

Mr. DOUGLAS. I have never charged that there were. However, all this signifies an extraordinary change in the type of investments made by building and loan associations.

Mr. SPARKMAN. This amendment does not change it, except insofar as the committee bill placed a restriction upon what is already authorized by the basic law.

Mr. KERR. And defined the institution which would be subject to a certain tax.

Mr. SPARKMAN. And defined the institution which would be subject to a certain tax. It does not in any way provide that a certain percentage shall not be used. The law still stands that Federal savings and loan associations cannot lend more than 20 percent on multi-family use housing.

Mr. KERR. Would it be agreeable to adopt the amendment but not move to reconsider, so that the amendment would then be subject to a motion to reconsider?

Mr. DOUGLAS. I am not certain as to that.

Mr. KERR. Then let us leave it as the pending business and adjourn.

Mr. DOUGLAS. Before adjourning, since the Record has some importance, I should say that in the bill we place restrictions on the amount which the building and loan associations can invest because of the great tax privileges which building and loan associations enjoy.

Mr. SPARKMAN. That is correct.

Mr. DOUGLAS. Even with the increases which the bill puts into effect—and I think properly so—on building and loan associations and mutual savings banks, those institutions will still enjoy privileges in comparison with commercial corporations and banks.

Mr. SPARKMAN. It is my understanding that the American Bankers Association favors the provision relating to savings and loan associations and mutual savings banks. Also, I have received letters and telegrams from numerous banks in my State asking me to support the bill.

Mr. KERR. Madam President, I move—

Mr. SPARKMAN. Just a moment, please. Let me yield to the Senator from Chicago.

Mr. DOUGLAS. Madam President, I happen also to be a Senator from Illinois. I live in Chicago. Incidentally, I polled a larger vote downstate than any other Democrat who has ever run for office in Illinois.

Mr. SPARKMAN. I believe we can go further and say that the Senator from Illinois polled the biggest vote in the State of Illinois that anyone has ever polled.

Mr. DOUGLAS. I am very happy to represent, in part, the whole State of Illinois, not merely the city of Chicago. I do not believe the Senator from Alabama represents merely Huntsville, Ala.

Mr. SPARKMAN. I apologize to the Senator from Illinois.

Mr. DOUGLAS. Madam President, it is always possible to stir up tempests in teapots in these matters late at night.

In return for the tax privileges which we give to building and loan associations, I think we are entitled to try to promote as much as possible one of the original purposes of such associations; namely, home ownership, in the changing conditions of city life.

Mr. SPARKMAN. I agree with the Senator, if the regulating is done under the basic law. I do not believe that after the basic law has been placed on the statute books, the Committee on Finance should seek, by restrictive legislation, effectively to change the basic law. That is exactly what we are trying to avoid by the amendment.

Mr. JAVITS. That is the best argument I have heard tonight. The Senator is absolutely correct.

Mr. SPARKMAN. I have adopted the argument made by the Senator from Illinois. He said so a few minutes ago.

Mr. KEATING. Madam President, will the Senator from Alabama yield?

Mr. SPARKMAN. I yield.

Mr. KEATING. I favor the amendment, but I shall not prolong the debate.

Mr. DOUGLAS. One Senator cannot stop this drift. I have already tried, as hard as I could, to improve the bill. I do not pretend to know everything. These thoughts and queries came to my mind, and I thought it proper to express them. I know that I shall probably not be able to stop this measure on any vote of the Senate. I am ready to have a vote. With the information which I now have I will vote in the negative. I may be mistaken, but with the information I have, I will vote in the negative. Then I hope that the Senator from Alabama, as chairman of the Subcommittee on Housing of the Committee on Banking and Currency, will examine into this issue.

Mr. KEATING. Madam President, will the Senator from Alabama yield?

Mr. SPARKMAN. I yield.

Mr. KEATING. I still insist that I shall not prolong the debate by stating my own views. The Senator from Alabama knows that we have worked together on this amendment and that I favor it.

I have been requested by the distinguished senior Senator from Maryland [Mr. BEALL] to place at this point in the Record a statement with reference to one particular phase of the amendment in which he is especially interested, and in which the State of New York may in the near future be interested.

Mr. JAVITS. Madam President, will the Senator yield?

Mr. KEATING. I yield.

Mr. JAVITS. The junior Senator from Maryland had asked that I make this request, but I am glad that my colleague from New York has done so. The part in which the Senator from Maryland is interested is that which relates to the mutualization of insurance within the State. If the Senator from Maryland were here, he would maintain that position. I am certain that he will be gratified that the amendment is being adopted.

Mr. KEATING. Madam President, I ask unanimous consent that the statement of Senator BEALL be printed at this point in the RECORD.

There being no objection, the statement was ordered to be printed in the RECORD, as follows:

STATEMENT BY SENATOR BEALL

This amendment is concerned with the definition of a domestic building and loan association in section 6(c) of H.R. 10650, as amended by the Finance Committee. Specifically, the problem relates to current efforts by Maryland savings and loan associations to invest in mutual, nonprofit company to insure their accounts.

The background of this problem begins with the enactment of chapter 131 of the Laws of Maryland of 1962. This bill authorized the creation of a nonprofit mutual corporation which would have as its purpose the insuring of free share deposits in savings and loan associations regularly doing business in the State of Maryland. This corporation is called Maryland Savings-Share Insurance Corp.

The Governor has appointed an interim board of directors for the corporation; the boards has been meeting constantly since the first of June and has devised a tentative draft of bylaws, rules, and regulations; applications for membership in the corporation have been sent to all Maryland savings and loan associations; at the present time, 230 associations have applied for membership, representing free share deposits in excess of \$175 million.

Under the proposed bylaws, rules, and regulations, each savings and loan association will be required to make a capital contribution to the insurance company in an amount equal to 2 percent of its free share deposits. Upon making this contribution (the bylaws permit it to be paid in installments, in the first instance), the contributing association will become an insured member. It will receive in exchange for its capital contribution a certificate of deposit, the face amount of which will equal the amount of capital contributed to the insurance company. Any association may, of course, withdraw its capital contribution by giving notice in accordance with the bylaws, rules and regulations, and, thereafter, its free share deposits will no longer be insured.

Section 6(c) of H.R. 10650, which defines a domestic building and loan association, makes it clear that such associations may invest in obligations of the United States or of a State or local subdivision and in stock or obligations of a corporation which is an instrumentality of the United States or of a State or local subdivision. The bill also provides that except for these stock investments, an association may not invest its assets in stock of any corporation.

The problem here is whether or not the certificate of deposit which will be received by all Maryland savings and loan associations in exchange for their capital contributions to the insurance company would qualify as a permitted investment under the definition contained in subparagraph (C) of section 6(c) of the revenue bill of 1962. A

secondary problem is whether or not such certificates of deposit would be considered as "stock of any corporation" within the meaning of subparagraph (F) of section 6(c) of the revenue bill of 1962. Of course, if the Internal Revenue Service answered the second question in the affirmative, it would mean virtual disaster for all Maryland savings and loan associations who became members of the insurance company.

Ohio has a mutual insurance company very similar to the new Maryland corporation. It is my understanding that New York State will soon have one.

I know that Congress does not intend to disqualify a legitimate savings and loan association from the tax benefits contained in the revenue bill of 1962 merely because it was a member of the Maryland Savings-Share Insurance Corp., and had received, as a result of that membership, a certificate of deposit in exchange for its capital contributions. Accordingly, my amendment will make it clear that any savings and loan association may join a State-sponsored nonprofit mutual corporation which has as its purpose the insuring of free share deposits.

The PRESIDING OFFICER. The question is on agreeing to the amendment offered by the Senator from Alabama [Mr. SPARKMAN].

The amendment was agreed to.

Mr. KERR. Madam President, I shall not move to reconsider the vote by which the amendment was agreed to, believing that it would be well to leave that question open until Tuesday.

Mr. DOUGLAS. Madam President, I appreciate what the Senator has said. It is very gracious of him. This is a highly difficult subject. We are exploring a technical field. It may well be that I am mistaken. I have been mistaken before. It may be that I am right.

Mr. KERR. The distinguished Senator from Illinois has a greater knowledge of this subject, and of many other subjects, than does the Senator from Oklahoma. If he does happen to be wrong, he would still be wrong fewer times than the Senator from Oklahoma has been wrong.

Mr. DOUGLAS. The Senator from Oklahoma is very kind.

Mr. JAVITS. Madam President, I should like to have a colloquy with the Senator from Oklahoma, because it would dispose of the mutual savings bank and savings and loan association aspect of the bill. I now propound the following question to the Senator from Oklahoma:

It is my understanding that under the existing Treasury Regulations, section 1.593-1(c), amounts credited by mutual thrift institutions to qualifying reserves for losses in compliance with requirements of State law or regulations are deemed to have been credited to the reserve for bad debts. Would this use of the bad debt reserve deduction be continued in effect under this particular provision?

Mr. KERR. It is my understanding that it would. It is intended to continue the rule of Treasury Regulations, section 1.593-1(c), under the new law, and amounts credited pursuant to such or similar regulations will be deemed to have been credited to the reserve for losses on qualifying real property loans. It is expected that, as under present

regulations and rulings, these institutions will keep records which will make it possible to identify amounts thus credited.

Mr. JAVITS. To identify them?

Mr. KERR. To identify them.

Mr. JAVITS. I thank the Senator.

COMMUNICATIONS SATELLITE LAW

Mr. KERR. Mr. President, the President of the United States has signed into law the communications satellite bill, which the Senate passed August 17 after much debate and travail.

The action of the President offers us encouragement and strengthens our resolve at a time when all Members of the Senate can use generous portions of these. The signing of this bill will also, I believe, generate a renewal of confidence on the part of all the American people in our democratic processes. The people will be reassured that their Congress can come to grips with unprecedented and extremely difficult economic opportunities arising from our wondrous new space technology. We have not only come to grips with the problems and opportunities; we have brought forth a blueprint by which this Nation can move ahead.

The course of human events becomes ever more complex. The expansion of scientific and technical knowledge has introduced complication after complication into the enterprises that make up our free economy and in their relations with government.

No one will argue, I am sure, with the statement that the communications satellite technology posed for the people and Congress a great challenge and a great opportunity. Here on the Senate floor, despite many days of hearings and exhaustive study and drafting by three committees, this bill provoked an amazing filibuster. Then came the more amazing application for the first time in 35 years of the rule which limits debate.

But now, from the perspective provided by the passage of only a brief span of time, we can point proudly to both the strife of battle and the victory at its end which will lead to the establishment of a communications satellite system.

Insofar as the communications satellite issue is concerned, a reasonable and tolerant calm now possesses the minds of all who debated and wrestled over it. The signing of the bill signifies the remobilization of our physical and mental resources in a renewed effort to go forward as efficiently and expeditiously as possible in our program for the development of space for peaceful purposes.

This enactment stands as an historic turning point in the space program. It gives us our best chance to reinforce and increase our undisputed lead over Soviet Russia in the most important contest to establish a worldwide system of communications based on earth-orbiting satellites.

Mr. President, in my judgment, this new communications satellite law also provides dramatic evidence to the American people that our free enterprise system and our democratic processes of

Digest of CONGRESSIONAL PROCEEDINGS

OF INTEREST TO THE DEPARTMENT OF AGRICULTURE

OFFICE OF
BUDGET AND FINANCE

(For information only;
should not be quoted
or cited)

Issued Sept. 5, 1962
For actions of Sept. 4, 1962
87th-2d, No. 158

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HIGHLIGHTS: Senate committee voted to report roads bill. Senate committee voted to approve House amendments to public works acceleration bill. Sen. Bartlett urged greater fire protection for forest lands. Sen. Wiley commended cheese industry. Rep. Lindsay urged greater protection against radioactive contamination of food.

HOUSE

1. FORESTRY. Passed without amendment S. 1878, to add certain lands to the Wasatch National Forest, Utah. A similar bill, H. R. 7195, was laid on the table. This bill will now be sent to the President. p. 17323
2. FARM PROGRAM. The "Daily Digest" for Aug. 31 states, "Conferees, met in executive session to resolve the differences between the Senate- and House-passed versions of H. R. 12391, proposed Food and Agriculture Act of 1962, but did not reach final agreement, and will meet again on Monday, September 10." p. D799
3. SAMOA. Both Houses agreed to without amendment H. Con. Res. 519, requesting the President to return H. R. 10062, to extend the application of certain laws to American Samoa, in order to allow the Clerk of the House to correct the enrollment. pp. 17320, 17399
4. AWARDS. Reps. Gross, Ray, and Ford objected to consideration of H. R. 4055, to authorize the payment of a monetary award to recipients of the National Medal of Science. This bill was stricken from the Consent Calendar. p. 17323

5. VETERANS. At the request of Rep. Weaver, passed over without prejudice H. R. 9962, to provide an extension of the period within which certain educational programs must be begun and completed in the case of persons called to active duty during the Berlin crisis. p. 17324
 6. RESERVOIRS. Passed without amendment H. R. 11799, defining the interest of local public agencies in water reservoirs constructed by the Government which have been financed partially by such agencies. p. 17326
 7. PERSONNEL. Passed as reported H. R. 2079, to amend the Classification Act of 1949 to authorize the establishment of hazardous-duty pay in certain cases. pp. 17326-7
 8. RADIOACTIVE CONTAMINATION. Rep. Lindsay urged a stepped-up program of effective countermeasures to combat radioactive contamination and said, "I think that a thorough public congressional investigation may be in order to determine how much cooperation between Federal and State health programs exists at the present time." pp. 17338-44
 9. PARKS. The Subcommittee on National Parks of the Interior and Insular Affairs Committee voted to report to the full committee with amendment H. R. 11781, to redesignate the Big Hole Battlefield National Monument and to revise the boundaries thereof. p. D804
- SENATE
10. ROADS. The Public Works Committee voted to report with amendments (but did not actually report) H. R. 12135, the proposed Federal-Aid Highway Act of 1962, which includes authorizations for forest highways and forest development roads and trails. p. D802
 11. PUBLIC WORKS. The Public Works Committee voted to rereport (but did not actually report) S. 2965, the public works acceleration bill. The "Daily Digest" states that the committee "agreed to recommend that the Senate agree to the House amendment to S. 2965" (p. D802). This bill, as passed by the House, had been referred to the committee earlier in the day (p. 17349).
 12. TAXATION. Continued debate on H. R. 10650, the proposed Revenue Act of 1962 (pp. 17349-50, 17361-415, 17420-1). By a vote of 16 to 49, rejected an amendment by Sen. Proxmire to eliminate public utilities from the investment credit provisions provided in the bill (pp. 17365-96).
 13. FORESTRY. Sen. Bartlett discussed the danger of forest fires to our timber resources, reviewed the progress made in the control of forest fires, and stated that "it is necessary that the public lands receive the most intensive protection possible." pp. 17351-3
 14. CHEESE. Sen. Wiley commended the domestic cheese industry, particularly for its development of American blue cheese which he stated "is today the most popular blue mold cheese in the country." pp. 17355-6
 15. APPROPRIATIONS. The Appropriations Committee reported with amendments H. R. 12870, the military construction appropriation bill for 1963 (S. Rept. 1994). p. 17349
 16. FAIRS. Sen. Javits inserted a speech on plans for the N. Y. World's Fair in 1963-4, "The Biggest Box Office in History." pp. 17359-60

Senate

TUESDAY, SEPTEMBER 4, 1962

The Senate met at 10 o'clock a.m., and was called to order by the President pro tempore.

The Chaplain, Rev. Frederick Brown Harris, D.D., offered the following prayer:

Our Father, God, whose paths are mercy and truth, who knowest our down-sitting and our up-rising, and who understandeth, afar off, the thoughts of our hearts: At the beginning of another week, we pause in the busy rush of the legislative process, to ask that the deliberations of these hours may reflect the guidance of Thy Spirit.

When work, worry, and hopes deferred take their constant toll of our human resources, as laborers together with Thee, grant us, we implore, a sense of an untapped spiritual reservoir. Restore our souls with the joyous assurance of Thy salvation. Search us, O God, and know our hearts; try us, and know our thoughts, and see if there be any wicked or perverse way in us, for we would come to this high and holy hill of the people's weal with pure hearts and clean hands, not lifting up our souls unto vanity.

We ask it in the dear Redeemer's name. Amen.

THE JOURNAL

On request of Mr. MANSFIELD, and by unanimous consent, the reading of the Journal of the proceedings of Friday, August 31, 1962, was dispensed with.

LIMITATION OF DEBATE DURING MORNING HOUR

On request of Mr. MANSFIELD, and by unanimous consent, statements during the morning hour were ordered limited to 3 minutes.

COMMITTEE MEETINGS DURING SENATE SESSION

On request of Mr. MANSFIELD, the following committees or subcommittees were authorized to meet during the session of the Senate today:

The Subcommittee on Patents, Trade Marks, and Copyrights of the Committee on the Judiciary.

The Committee on Post Office and Civil Service.

SUBCOMMITTEE MEETING DURING SENATE SESSION TOMORROW

Mr. MANSFIELD. Mr. President, I ask unanimous consent that the Subcommittee on Labor of the Committee on Labor and Public Welfare may be permitted to sit during the session of the Senate tomorrow.

The PRESIDENT pro tempore. Without objection, it is so ordered.

EXECUTIVE COMMUNICATIONS, ETC.

The PRESIDENT pro tempore laid before the Senate the following letters, which were referred as indicated:

REPORT ON CONSTRUCTION AT LANGLEY RESEARCH CENTER, HAMPTON, VA.

A letter from the Acting Administrator, National Aeronautics and Space Administration, Washington, D.C., reporting pursuant to law, on the construction of a low frequency environmental noise facility at the Langley Research Center, Hampton, Va.; to the Committee on Aeronautical and Space Sciences.

REPORT ON MANGANESE

A letter from the Chairman, U.S. Tariff Commission, Washington, D.C., transmitting, pursuant to law, a report of that Commission's investigation concerning manganese (with an accompanying report); to the Committee on Finance.

PAYMENT OF CLAIM OF UNITED KINGDOM OF GREAT BRITAIN AND NORTHERN IRELAND

A letter from the Under Secretary of the Navy, transmitting a draft of proposed legislation to authorize payment of a claim made by the Government of the United Kingdom of Great Britain and Northern Ireland (with an accompanying paper); to the Committee on Foreign Relations.

DISPOSITION OF EXECUTIVE PAPERS

A letter from the Administrator, General Services Administration, Washington, D.C., transmitting, pursuant to law, a report of the Archivist of the United States on a list of papers and documents on the files of several departments and agencies of the Government which are not needed in the conduct of business and have no permanent value or historical interest, and requesting action looking to their disposition (with accompanying papers); to a Joint Select Committee on the Disposition of Papers in the Executive Departments.

The PRESIDENT pro tempore appointed Mr. JOHNSTON and Mr. CARLSON members of the committee on the part of the Senate.

PETITION

The PRESIDENT pro tempore laid before the Senate a letter in the nature of a petition from the United States Army Mothers and Wives Club, of Burbank, Calif., signed by Melva Devine, president, relating to the reduction of airmail package rates to Army APO's, which was referred to the Committee on Post Office and Civil Service.

REPORTS OF COMMITTEES

The following reports of committees were submitted:

By Mr. STENNIS, from the Committee on Appropriations, with amendments:

H.R. 12870. An act making appropriations for military construction for the Department of Defense for the fiscal year ending June 30, 1963, and for other purposes (Rept. No. 1994).

By Mr. MONRONEY, from the Committee on Commerce, with amendments:

S. 2773. A bill to amend section 503 of the Federal Aviation Act to provide substantive Federal law relating to the validity of conveyances which affect title to or interests in civil aircraft of the United States and related equipment (Rept. No. 1995).

BILL INTRODUCED

A bill was introduced, read the first time, and, by unanimous consent, the second time, and referred as follows:

By Mr. CHAVEZ:

S. 3692. A bill for the relief of Warena Allahverdi; to the Committee on the Judiciary.

STANDBY AUTHORITY TO ACCELERATE PUBLIC WORKS PROGRAMS OF FEDERAL, STATE, AND LOCAL PUBLIC BODIES—REFERENCE OF HOUSE AMENDMENTS TO COMMITTEE ON PUBLIC WORKS

Mr. KERR. Mr. President, Senate bill 2965, entitled "An act to provide standby authority for accelerated Federal public works programs for the Federal Government and State and local public bodies," was passed by the Senate some months ago, and went to the House of Representatives. It has been returned to the Senate with amendments, and is on the Vice President's desk. I ask unanimous consent that the bill be immediately referred to the Committee on Public Works.

The PRESIDENT pro tempore. Without objection, it is so ordered.

REVENUE ACT OF 1962—AMENDMENTS

Mr. KERR. Mr. President, I submit amendments, intended to be proposed by me, to the bill (H.R. 10650) to amend the Internal Revenue Code of 1954 to provide a credit for investment in certain depreciable property, to eliminate certain defects and inequities, and for other purposes. I ask that the amendments be printed and lie on the table. I ask unanimous consent that a statement in explanation of the amendments be printed in the RECORD.

The PRESIDENT pro tempore. The amendments will be received, printed, and will lie on the table; and, without objection, the statement will be printed in the RECORD.

The statement presented by Mr. KERR is as follows:

STATEMENT BY SENATOR KERR

I am submitting today several amendments to the foreign income provisions of H.R. 10650 as reported by the Committee on Finance. These changes are necessary to correct certain inequities and defects which

have been called to my attention since the bill was reported. The following is an explanation of the changes made by the amendments:

1. **Earned income exclusion:** One of the amendments would provide that the new earned income exclusion limitations of \$20,000 and \$35,000 for U.S. citizens residing abroad would apply to advance salaries paid before December 31, 1962, for services to be rendered after December 31, 1962. This is necessary in order to prevent evasion of the new law. For example, a highly paid employee, especially one who has a controlling stock ownership in the corporation for which he works, may be able to have his entire salary of \$150,000 a year for the years 1963 and 1964 advanced to him before December 31, 1962. If these salaries were paid after December 31, 1962, under the new law the maximum amount which could be excluded for each of these 2 years because of foreign residence would be \$35,000. Clearly, the same result should apply to the employee's salary for such years whether the salary is advanced to him prior to December 31, 1962, or paid to him after December 31, 1962.

2. **Improvement of less-developed-country corporation exceptions:** Another of the amendments would improve the exceptions available for less-developed-country corporations under section 9 ("gross-up"), section 12 (controlled foreign corporations), and section 15 (gain from certain sales or exchanges of stock in certain foreign corporations). Under the language of the bill as reported, the benefit of these exceptions would not be available to certain corporations even though they meet the income and asset requirements for a less-developed-country corporation merely because such corporations had their place of incorporation in a developed country. Under this amendment, corporations which meet the income and asset requirements for a less-developed-country corporation would not be technically disqualified merely because of their place of incorporation.

A related change in section 15 would make the exception for less-developed-country corporations available for the profits of those years in which a company qualified as a less-developed-country corporation even though the company did not qualify during all the years the stock was held.

Another change would also make the less-developed-country corporation exception to section 15 available for the profits of a holding company for less-developed-country corporations. This would conform these rules to the gross-up exception rules.

The amendments would also remove certain inequities and cure certain defects in the definition of qualified investments in less developed countries for purposes of section 12. Income from the investments described in section 955(b), even though constituting base company income, will not be taxed if reinvested in similar qualified investments in less developed countries. Under the bill one type of qualified investment is an obligation of a 10-percent owned less-developed-country corporation having a maturity of at least 5 years or more at the time of its acquisition. It has been called to my attention that this required period may be unduly long to accomplish the purpose of preventing very short-term loans from qualifying for the reinvestment deduction. The amendment would reduce this period to a 1-year requirement.

Under the bill, there is no holding period requirement with respect to qualified investments in less developed countries and it has been called to my attention that it is possible to acquire such investments at the close of a year and dispose of them immediately following the close of the year. The amendment would prevent the possibility of such sham investments by providing that

otherwise qualified investments in less developed countries would not qualify if they were held for a period of less than 6 months.

A final related change in section 955(b) (3) would provide that an election to treat investments made after the close of the taxable year and on or before the close of the following taxable year (or such further period as allowed under regulations) shall be binding for future years. This amendment will require that a controlled foreign corporation elect to value its investments in less developed countries on a consistent annual basis and not have the opportunity to shift back and forth between differing valuation dates. This would conform the rules under this section to the rules in a similar provision relating to investments in export trade assets which is described below.

3. **Time allowed under investment requirements for export trade companies:** Another of the amendments would provide that export trade companies will have a full year, or such further time as may be granted by the Secretary or his delegate, in which to invest export trade profits in fixed export trade assets such as warehouses or equipment. Under the bill as reported, only 75 days after the close of a year is allowed for the making of such investments. Since the decision to acquire such fixed facilities often requires a substantial period of time and since the actual acquisition of such facilities will generally require further substantial periods of time, it is believed that this change is appropriate. Further, it conforms these rules to the reinvestment in less developed country rules.

4. **Clarification of section 15 (liquidation of foreign corporations)** to prevent its circumvention through interposition of holding company: Because the use of less developed country operations is permitted and because it is possible that, under some circumstances, the provisions of section 15 could be avoided for technical reasons simply through the interposition of a foreign or domestic holding company. The amendments would make it clear that where appropriate the new law would apply to gain attributable to the stock of foreign corporations irrespective of whether such stock were sold directly or whether stock of an intervening holding company were sold.

5. **Clarification of business interest exceptions to section 10 (separate limitation on foreign tax credit with respect to certain interest income):** Section 10 of the bill corrects certain inducements that now exist under the foreign tax credit mechanism for the movement of funds abroad to earn interest income. There is excepted from the section a number of normal business transactions giving rise to interest which are unrelated to the problem that the section is designed to correct. Among these exceptions are interest derived from any transaction which is directly related to the active conduct of a trade or business in a foreign country or possession of the United States. The amendments would make it clear that this exception also applies to interest derived from obligations received upon the sale or exchange of such a foreign trade or business.

Section 10 also has an exception for interest received from a corporation in which the U.S. taxpayer owns at least 10 percent of the voting stock. The amendments would make it clear that this exception also applies to interest received from obligations which were received as a result of the sale or exchange of securities in such a corporation.

Mr. KERR. Mr. President, I also submit an amendment to H.R. 10650, and ask that it be printed and lie on the table.

The PRESIDENT pro tempore. The amendment will be received, printed, and lie on the table.

Mr. KERR. Mr. President, this amendment to H.R. 10650 would change the special transitional loss—contained in new section 821(f)—in two ways. First, it would create the special loss carryforward only out of losses computed without regard to policyholder dividends. Secondly, the special loss carryforward could only be applied against statutory underwriting income rather than total taxable income.

Mr. CURTIS submitted an amendment, intended to be proposed by him, to House bill 10650, supra, which was ordered to lie on the table and to be printed.

ADDRESSES, EDITORIALS, ARTICLES, ETC., PRINTED IN THE APPENDIX

On request, and by unanimous consent, addresses, editorials, articles, etc., were ordered to be printed in the Appendix, as follows:

By Mr. WILEY:

Statement prepared by himself on eight-point anti-Communist program.

By Mr. MUNDT:

Editorial entitled "NFO Has a Laudable Aim, But We Don't Believe Their Holding Action Will Work," published in the Sioux Falls (S. Dak.) Argus-Leader on August 30, 1962.

By Mr. WILLIAMS of New Jersey:

Resolution adopted by the Knights of Lithuania 49th annual convention, at Newark, N.J., relating to Captive Nations Week, and expressing hope to Lithuania's freedom.

The PRESIDENT pro tempore. Morning business is in order. If there is no further morning business to be submitted, morning business is closed.

REVENUE ACT OF 1962

Mr. MANSFIELD. Mr. President, I ask unanimous consent that the unfinished business be laid down and be made the pending business.

The PRESIDENT pro tempore. Without objection, the Chair lays before the Senate the unfinished business.

The Senate resumed the consideration of the bill (H.R. 10650) to amend the Internal Revenue Code of 1954 to provide a credit for investment in certain depreciable property, to eliminate certain defects and inequities, and for other purposes.

GOLD MINING

Mr. BARTLETT. Mr. President, we like to build up the image of Uncle Sam as a kindly old gentleman, thoughtful and always helpful and considerate of his own people. This gives us a feeling of well-being, of satisfaction, and probably of self-contentment.

Mr. President, I do not propose to poll the goldmining industry in order to discover what the image of Uncle Sam is among employers and miners. I am rather sure I know the result beforehand. I fear that the image would be found to be somewhat tarnished.

If so, Mr. President, that would be understandable, for I do not know of any other group of people in the entire history of the United States who have been

fact which would very affirmatively entrench our presence there and give reassurance to the West Berliners, who are understandably concerned, as is shown by the street activity which they undertook, and which we can understand, considering the provocations to which they have been subjected, but which nevertheless have the threat of making American policy on the streets of Berlin, which we cannot have.

Therefore, I believe we must show initiative through activities and actions which are affirmative and are tangible and which at the same time will bring assurance to the city of West Berlin, because it will serve notice on the Russians of our determination, which we have already expressed, and will also present to them the firm governmental organization indicating that we intend to take action to back up words, by means which they can understand.

I have suggested three courses of action, namely, the incorporation of West Berlin into the Federal Republic of Germany; an embargo by NATO against trade with East Germany; and some action through the United Nations, which would bring before the world in a most dramatic way the difference between the situation in East Berlin and West Berlin.

Again I repeat that the State Department planners probably have a number of other ideas on the planning board. However, the time has come for us to move and not sit still and wait for the next Russian action before we react.

REVENUE ACT OF 1962

The Senate resumed the consideration of the bill (H.R. 10650) to amend the Internal Revenue Code of 1954 to provide a credit for investment in certain depreciable property, to eliminate certain defects and inequities, and for other purposes.

Mr. DIRKSEN. Mr. President, if it is in order to ask, what is the pending question before the Senate?

The PRESIDING OFFICER (Mr. HART in the chair). The bill is before the Senate. There is no amendment pending.

Mr. DIRKSEN. Mr. President, I call up my amendments "8-23-62—I."

The PRESIDING OFFICER. The amendments will be stated for the information of the Senate.

The LEGISLATIVE CLERK. On page 391, between lines 21 and 22, it is proposed to insert the following new section:

SEC. 27. EXCLUSION FROM GROSS INCOME OF GAIN FROM SALE OF RESIDENCE BY INDIVIDUAL AGE 60 OR OVER.

(a) EXCLUSION FROM GROSS INCOME.—Part III of subchapter B of chapter 1 of the Internal Revenue Code of 1954 (relating to items specifically excluded from gross income) is amended by renumbering section 121 as 122, and by inserting after section 120 the following new section:

"SEC. 121. GAIN FROM SALE OR EXCHANGE OF RESIDENCE OF INDIVIDUAL WHO HAS ATTAINED AGE 60.

"(a) GENERAL RULE.—In the case of an individual, gross income does not include gain from the sale or exchange after December 31, 1961, of property used by the taxpayer as his principal residence, if—

"(1) the taxpayer has attained the age of 60 years before such sale or exchange occurs, and

"(2) such property has been used by the taxpayer as his principal residence for a period of not less than 5 years at the time such sale or exchange occurs.

"(b) PROPERTY HELD JOINTLY BY HUSBAND AND WIFE.—In the case of property held by a husband and wife as joint tenants or as tenants by the entirety, the age requirement contained in subsection (a) (1) and the use requirement contained in subsection (a) (2) shall be treated as having been met by both the husband and the wife if it is met by either spouse.

"(c) PROPERTY USED IN PART AS PRINCIPAL RESIDENCE.—In the case of property only a portion of which is used by the taxpayer as his principal residence, subsection (a) shall apply to so much of the gain from the sale or exchange of such property as is determined, under regulations prescribed by the Secretary or his delegate, to be attributable to the portion of the property used by the taxpayer as his principal residence.

"(d) INVOLUNTARY CONVERSIONS.—For purposes of subsection (a), the destruction, seizure, requisition, or condemnation of property, occurring after December 31, 1961, shall be treated as the sale or exchange of such property."

(b) TABLE OF CONTENTS.—The table of sections for such part is amended by striking out

"Sec. 121. Cross references to other Acts."

and inserting in lieu thereof

"Sec. 121. Gain from sale or exchange of residence of individual who has attained age 60.

"Sec. 122. Cross references to other Acts."

(c) TECHNICAL AMENDMENTS.—(1) Section 1033(h) of the Internal Revenue Code of 1954 (relating to involuntary conversions) is amended by adding at the end thereof the following new paragraph:

"(3) For exclusion from gross income of gain from involuntary conversion occurring after December 31, 1961, of residence of taxpayer who has attained age 60, see section 121."

(2) Section 1034 of such Code (relating to sale or exchange of residence) is amended by adding at the end thereof the following new subsection:

"(k) CROSS REFERENCE.—

"For exclusion from gross income of gain from sale or exchange after December 31, 1961, of residence of taxpayer who has attained age 60, see section 121."

(d) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 1961.

On page 391, line 22, strike out "27" and insert in lieu thereof "28".

Mr. DIRKSEN. Mr. President, I wish to modify the amendments.

On page 2, line 6, strike out "1961" and insert "1962."

I wish to make the same modification on page 4, line 7; to strike out "1961" and to insert "1962."

The PRESIDING OFFICER. The Senator has a right to modify his amendments.

MILWAUKEE SENTINEL SUPPORTS PROXMIRE ON CUTTING RETIREMENT AGE

Mr. PROXMIRE. Mr. President, the Milwaukee Sentinel recently carried a concise and thoughtful editorial supporting my proposal to reduce the social security retirement age from 62 to 60, with a corresponding reduction in the benefits.

Mr. President, the serious, nagging problem of unemployment drags on in spite of general economic improvement. I feel that in spite of the very sincere efforts of the Congress and the administration there is no evidence we are making any real progress in solving it.

Mr. proposal would play a moderate part in helping to solve unemployment.

I hope that the Congress will give serious consideration to my proposal.

I ask unanimous consent that the excellent, thoughtful editorial from the Milwaukee Sentinel be printed at this point in the RECORD.

There being no objection, the editorial was ordered to be printed in the RECORD, as follows:

RETIREMENT AT 60

There is much to be said for Senator PROXMIRE's proposal to lower the optional retirement age under social security to 60.

Any person electing to retire at 60 would have a one-third reduction in the benefits he would have received if he had continued working to age 65. PROXMIRE has been told by the Social Security Administration that with the one-third reduction there would be no increased costs to the social security fund and no increase in social security taxes. At present the earliest age for retirement is 62.

Under PROXMIRE's proposal, a man and wife who would get \$180 a month if they retired at 65 would get \$120 if they retired at 60.

The number of workers who could afford to take advantage of the earlier retirement would not be large, but each one doing so would open up a job for some younger person. We agree with PROXMIRE that there would be a relatively small but nevertheless significant effect on our persistent unemployment problem.

THE TAXPAYERS' "BLACK FRIDAY" FROM A RED-INK CONGRESS

Mr. PROXMIRE. Mr. President, the closing session of the Senate before the Labor Day weekend I think can properly be called the taxpayers' "black Friday" because massive increases in nonmilitary spending shot through the Senate crushing economy amendments by overwhelming margins.

The runaway-spending attitude of the Congress, supported by a topheavy majority of both Republicans and Democrats, is shown by the following:

First. The Senate virtually doubled the Government's most inexcusable subsidy, the helicopter giveaway, which subsidizes the affluent passengers who take helicopters between airports in major cities.

In doing so for the first time it threw the subsidy open to all cities, guaranteeing that the size of this subsidy will vastly increase in coming years. It overwhelmed a Proxmire amendment to kill the subsidy by a voice vote that almost blew the top off the Capitol.

Second. The Senate forced the Veterans' Administration to take \$8 million more than its Administrator said he could efficiently use or than the Kennedy administration requested or the House allowed. The Senate killed my amendment to cut this VA spending back to the Administration request by a 56 to 22 vote.

Third. On the big item in the bill the Senate approved a soaring jump in space

spending from \$1.7 billion last year to \$3.7 billion this year in the NASA budget, for nonmilitary space appropriations. In doing so the Senate showed its spending temper when it rejected a Proxmire amendment based on demonstrated waste in the space program.

The amendment would have pared the space budget by 5 percent below the budget estimates, or \$180 million. It lost by a resounding 66 to 4 votes.

Fourth. Finally the Senate demonstrated how feeble is its concern for economy when a motion by the Senator from Iowa [Mr. MILLER] to recommit the bill to reduce it by \$289 million to the House figure was crushed by a 57 to 12 margin.

The irony of this sad spending performance is that this appropriations so vastly increasing Federal nondefense spending was called up in the middle of consideration of a tax bill which Congress has converted from a measure that, as recommended by the administration, would have increased revenue by \$500 million to one that will lose \$500 million.

This Congress is well on its way to becoming the biggest, bipartisan, Democratic-Republican, red-ink operation in history.

Mr. President, I suggest the absence of a quorum.

The PRESIDING OFFICER. The clerk will call the roll.

The legislative clerk proceeded to call the roll.

Mr. MANSFIELD. Mr. President, I ask unanimous consent that the order for the quorum call be rescinded.

The PRESIDING OFFICER (Mr. PROXMIRE in the chair). Without objection, it is so ordered.

KIM JUNG IM—BILL INDEFINITELY POSTPONED

Mr. MANSFIELD. Mr. President, on Friday last the Senate passed the bill (H.R. 9589) for the relief of Kim Jung Im. It is my understanding that on the basis of word received since that time, administrative relief has been granted the beneficiary of the bill. I therefore ask unanimous consent that the votes, by which the bill was ordered to a third reading and passed be reconsidered, and the bill indefinitely postponed.

The PRESIDING OFFICER. Is there objection? The Chair hears none, and it is so ordered.

ORDER FOR ADJOURNMENT UNTIL 9 A.M. TOMORROW

Mr. MANSFIELD. Mr. President, I ask unanimous consent that when the Senate adjourns tonight—late, I hope—that it adjourn to meet at 9 a.m. tomorrow morning.

The PRESIDING OFFICER. Without objection, it is so ordered.

Mr. MANSFIELD. Mr. President, I suggest the absence of a quorum.

The PRESIDING OFFICER. The clerk will call the roll.

The legislative clerk called the roll, and the following Senators answered to their names:

[No. 234 Leg.]

Aiken
Byrd, W. Va.
Dirksen
Gore
Hayden
Hill
Holland

Hruska
Javits
Kerr
Mansfield
McGee
Pearson
Proxmire

Robertson
Smith, Maine
Stennis
Talmadge
Young, N. Dak.
Young, Ohio

Mr. MANSFIELD. I announce that the Senator from Nevada [Mr. BIBLE], the Senator from Minnesota [Mr. HUMPHREY], the Senator from Washington [Mr. MAGNUSON], the Senator from Utah [Mr. MOSS], the Senator from Maine [Mr. MUSKIE], the Senator from Florida [Mr. SMATHERS], the Senator from Massachusetts [Mr. SMITH], the Senator from Texas [Mr. YARBOROUGH], the Senator from Pennsylvania [Mr. CLARK], the Senator from Mississippi [Mr. EASTLAND], and the Senator from Oregon [Mrs. NEUBERGER] are absent on official business.

I further announce that the Senator from New Mexico [Mr. ANDERSON], the Senator from Alaska [Mr. GRUENING], the Senator from Wyoming [Mr. HICKEY], and the Senator from Missouri [Mr. SYMINGTON] are necessarily absent.

Mr. DIRKSEN. I announce that the Senator from Maryland [Mr. BEALL], the Senator from Utah [Mr. BENNETT], the Senator from South Dakota [Mr. BOTTOM], the Senator from Connecticut [Mr. BUSH], the Senator from Indiana [Mr. CAPEHART], the Senators from New Hampshire [Mr. COTTON and Mr. MURPHY], the Senator from Arizona [Mr. GOLDWATER], the Senator from Idaho [Mr. JORDAN], the Senator from California [Mr. KUCHEL], the Senator from Kentucky [Mr. MORTON], the Senator from Massachusetts [Mr. SALTONSTALL], the Senator from Pennsylvania [Mr. SCOTT], the Senator from Wisconsin [Mr. WILEY] and the Senator from Delaware [Mr. WILLIAMS] are necessarily absent.

The PRESIDING OFFICER. A quorum is not present.

Mr. MANSFIELD. Mr. President, I move that the Sergeant at Arms be directed to request the attendance of absent Senators.

The motion was agreed to.

The PRESIDING OFFICER. The Sergeant at Arms will execute the order of the Senate.

After a little delay, Mr. ALLOTT, Mr. BARTLETT, Mr. BOGGS, Mr. BURDICK, Mr. BUTLER, Mr. BYRD of Virginia, Mr. CANNON, Mr. CARLSON, Mr. CARROLL, Mr. CASE, Mr. CHAVEZ, Mr. CHURCH, Mr. COOPER, Mr. CURTIS, Mr. DODD, Mr. DOUGLAS, Mr. ELLENDER, Mr. ENGLE, Mr. ERVIN, Mr. FONG, Mr. FULBRIGHT, Mr. HART, Mr. HARTKE, Mr. HICKENLOOPER, Mr. JACKSON, Mr. JOHNSTON, Mr. JORDAN of North Carolina, Mr. KEATING, Mr. KEFAUVER, Mr. LAUSCHE, Mr. LONG of Missouri, Mr. LONG of Hawaii, Mr. LONG of Louisiana, Mr. MCCARTHY, Mr. McCLELLAN, Mr. McNAMARA, Mr. METCALF, Mr. MILLER, Mr. MONRONEY, Mr. MORSE, Mr. MUNDT, Mr. PASTORE, Mr. PELL, Mr. PROUTY, Mr. RANDOLPH, Mr. RUSSELL, Mr. SPARKMAN, Mr. THURMOND, Mr. TOWER, and Mr. WILLIAMS of New Jersey entered the Chamber and answered to their names.

The PRESIDING OFFICER (Mr. PELL in the chair). A quorum is present.

REVENUE ACT OF 1962

The Senate resumed the consideration of the bill (H.R. 10650) to amend the Internal Revenue Code of 1954 to provide a credit for investment in certain depreciable property, to eliminate certain defects and inequities, and for other purposes.

Mr. MANSFIELD. Mr. President, I am about to propound a unanimous-consent request.

I ask unanimous consent that on the pending Dirksen amendments time be limited to 1 hour, one-half hour to be under the charge of the Senator from Illinois, the minority leader, and one-half hour to be under the charge of the Senator from Oklahoma [Mr. KERR].

Mr. FULBRIGHT. Mr. President, reserving the right to object, when would the vote come under this request?

Mr. MANSFIELD. In 1 hour or less.

Mr. FULBRIGHT. Beginning when?

Mr. MANSFIELD. Right now.

Mr. GORE. Mr. President, reserving the right to object, this limitation in no sense applies to H.R. 10, does it?

Mr. MANSFIELD. No; only to the pending amendments.

The PRESIDING OFFICER. Is there objection?

Mr. MILLER. Mr. President, reserving the right to object, may I be advised what the proposed unanimous-consent agreement is?

Mr. MANSFIELD. One hour on the amendments, a half hour to a side. It has been cleared with the Senators directly interested. I thought there was no objection to it.

The PRESIDING OFFICER. Is there objection?

Mr. MILLER. Mr. President—

Mr. MANSFIELD. Mr. President, I ask unanimous consent that the time allotted be 20 minutes, 10 minutes on a side.

Mr. MILLER. For each amendment pending?

Mr. MANSFIELD. No; on the pending amendments.

The PRESIDING OFFICER. Is there objection? The Chair hears none, and it is so ordered.

Mr. MANSFIELD. Mr. President, is time running?

The PRESIDING OFFICER. Time is running.

Mr. DIRKSEN. Mr. President, I yield 3 minutes to the distinguished Senator from Kansas [Mr. CARLSON].

The PRESIDING OFFICER. The Senator from Kansas is recognized for 3 minutes.

Mr. CARLSON. Mr. President, I had made arrangements to discuss with the Senator from Oklahoma an understanding I have with regard to some language in the report. I would not like to use this time, which is running against the time of the Senator from Illinois, until the Senator from Oklahoma is on the floor. He stepped out of the Chamber only for a few moments.

I shall be glad to proceed with my discussion of section 3 of H.R. 10650. First, with a brief reference to some of the legislative history surrounding the adoption of this section in the House of

Representatives. Except for a minor change in the Senate Finance Committee, this section is the same as enacted by the House of Representatives.

I have been advised when section 3 was discussed by Chairman WILBUR D. MILLS of the House before the House Rules Committee on March 20, 1962, he was careful to exclude from the advertising ban the so-called institutional advertising. Regarding advertising for or against legislation, Chairman MILLS was careful to point out that that was included in the ban, but further on in his testimony before the House Rules Committee, he stated that:

A company may want to get its name before the people and buy space in national magazines and tells us all we ought to be against sin and be for motherhood. That kind of thing can be deducted, but to put an ad in the paper that the people ought to write their Congressmen to be against H.R. 9000 would not be allowed under existing prevailing regulations.

I subscribe to this limited application of section 3 in this measure, but feel we should be very careful not to eliminate advertising having to do with good will and, in a broader sense, real public services. In light of this background, I should like to ask my distinguished colleague, the ranking majority member of the Senate Finance Committee, the following questions:

First. Would a company be denied the right of tax deduction for costs incurred in carrying advertising that promotes the sale of savings bonds?

Mr. KERR. The answer is "No."

Mr. CARLSON. Second, would a company be denied the right to charge off the costs of ads having to do with blood bank donations, the prevention of forest fires, or Community Chest contributions?

Mr. KERR. No.

Mr. CARLSON. Third, would an insurance company be denied the right to a tax deduction for promoting highway safety, as a part of their advertising campaign?

Mr. KERR. The answer would be "No" if unrelated to pending or proposed legislation.

Mr. CARLSON. Fourth, would a roadbuilding machinery company be permitted deductions on a general plea for improved highways?

Mr. KERR. The answer is "No," if unrelated to pending or proposed legislation.

Mr. CARLSON. Fifth, I have in my hand an advertisement of a bank in Virginia comparing our system with that of the Communist. Will the cost of this ad be excluded under section 3?

Mr. KERR. The answer to that question is "No" if it is unrelated to pending or proposed legislation.

Mr. CARLSON. I agree with my distinguished colleague that the answer to all of these questions is generally "no," and in light of this, I have one more question: Is it not the intent of this legislation to prohibit advertising that deals specifically with a legislative proposal arising under local, State or national law when the advertising is directed against such a measure by title or number?

Mr. KERR. The answer to that question is "Yes."

Mr. CARLSON. I am satisfied with those answers. I thank the Senator from Oklahoma. I am satisfied both with the contents of section 3 and the legislative history accompanying it.

I ask unanimous consent that I may have placed in the RECORD at this point an extract from a statement by the chairman of the House Ways and Means Committee, the Honorable WILBUR D. MILLS, when he appeared before the Rules Committee of the House and discussed this matter.

There being no objection, the extract was ordered to be printed in the RECORD, as follows:

EXTRACT OF STATEMENT BY HON. WILBUR D. MILLS, MARCH 20, 1962, WASHINGTON, D.C.

(Hearings before the Committee on Rules on H.R. 10650, a bill to amend the Internal Revenue Code to provide a credit for investment in certain depreciable property, to eliminate certain defects and inequities, and for other purposes.)

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Mr. MILLS. Read the report particularly with respect to this. I think you will like it.

Mr. MADDEN. I went over that last night and I did not cover it all. Is there something in here so that the big lobbies that come to Washington can have the taxpayers pay for their lobbying expenses?

Mr. MILLS. Any expenses of this sort that are incurred in lobbying are disallowed, or supposed to be.

Mr. MADDEN. There is something in here.

Mr. MILLS. Do you mean this additional section in the bill, section 3? That has to do with appearances before committees of Congress, yes.

Mr. MADDEN. Does that include expenses for people to come to Washington and entertain, and whatnot, so that they can conduct a lobbying action?

Mr. MILLS. That involves the right of appeal to people, I think, to Congress. Does it not? Here they can fight a case all the way through the courts, through the Supreme Court. They can deduct those expenses if they are incident to a business.

Mr. MADDEN. I am not talking about court procedure. I am talking about the propaganda that goes out, advertising expenses on propaganda on legislation.

Mr. MILLS. Let me talk about that a second. They can do all that. That is admitted, isn't it? A man's business is in jeopardy, it is in the court. He can deduct the expenses incident to the protection of his business in that respect.

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Mr. MADDEN. Pertaining to legislation?

Mr. MILLS. No, in court, all the way through the Supreme Court.

Mr. MADDEN. In a lawsuit. Go ahead.

Mr. MILLS. Say he is also in jeopardy in a business way before a department of Government. Say it is the Federal Communications Commission. He is in the television business or radio business, he can deduct all the expenses for any appearance before the Commission in preservation of his business, but that same individual cannot even come to Washington to appeal to the Congress not to pass a bill that it is hearing or considering in committee that drives him out of business.

Mr. MADDEN. There has been a lot of publicity in the newspapers and magazines against a piece of legislation or for a piece of legislation.

Mr. MILLS. That is not involved here. This is limited to appearances before Con-

gress, the committees of Congress, Members of Congress, the cost of preparing material for these appearances. That is what is involved here. No entertainment or anything of that sort.

Mr. MADDEN. But in regard to propaganda and publicity and advertising for or against legislation, they can deduct that?

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Mr. MILLS. That is not involved here and they cannot deduct it.

Mr. MADDEN. Nothing is mentioned in this bill about that?

Mr. MILLS. They cannot deduct it under treasury regulations, unless it is institutional type. A company may want to get its name before the people and buys space in national magazines and tells us all we ought to be against sin and for motherhood.

That kind of thing can be deducted. But to put an ad in the paper that the people ought to write their Congressman to be against H.R. 9000 would not be allowed under existing prevailing regulation.

Mr. CARLSON. I thank the Senator from Oklahoma.

The PRESIDING OFFICER. The question is on agreeing to the amendments of the Senator from Illinois.

Mr. DIRKSEN. Mr. President, the pending amendments are very simple.

Mr. KERR. Mr. President, will the Senator yield?

Mr. DIRKSEN. I yield.

Mr. KERR. Is there a copy of the Senator's amendments available?

Mr. DIRKSEN. Yes; they are printed.

Mr. KERR. Will the clerk identify the amendments?

Mr. DIRKSEN. The amendments are identified as "8-23-62-I."

They provide for a very simple amendment. They provide that taxpayers who are over 60 years of age who sell the residences that have been their primary residences for 5 years or more shall be exempted from the payment of capital gains taxes on the gains that may result from such sales or exchanges.

I offered this about a year ago. The provision came to my attention in connection with a hearing which was held in St. Louis by a subcommittee of the Special Committee on Aged and the Aging. Suggestions were made at the meeting at that time that in order to provide some direct benefit for our aged this would be, by all odds, one of the most acceptable approaches one could find.

It follows, of course, what results from the great tradition of the American family. A family is established. There are children. Homes are enlarged. New homes are occupied to accommodate larger families. Then, in due course, the youngsters establish families of their own. So, very often, there is a building on a rather expensive lot which is no longer necessary for an aged couple or for an aged individual, whether it be a widow or a widower. Yet, with respect to the sale, such a piece of property might have developed some real value, and it might be impossible to sell the property without paying the customary capital gains tax under existing law.

To me that looks like a burden which might well be removed from our aged people. That is the purpose of the amendment. Beyond that there is not much which needs to be said.

With respect to cost, it is obviously impossible to determine what the cost would be to the Treasury. There is no way of developing a statistic to show how many homes might be sold by aged people in respect to which a capital gains would eventuate.

I discussed this with the Secretary of the Treasury, very informally and very briefly, and he indicated to me that it had merit and that it was hoped perhaps next year something could be done with this proposal.

It has been languishing now for some time. I had hoped that something could be done now. Since it is a tax matter, it is entirely germane to the bill presently before the Senate.

When I first offered this proposal, there was a variety of very favorable editorial comment from all sections of the country. I had hoped that perhaps the committee could see fit to accept the proposal. It needs no discussion beyond that.

I can think of no better way to provide some benefits for our aged citizens than to exempt them from the payment of this capital gains tax, because it would mean some money in their purses to tide them over if they are in straitened circumstances.

With that explanation, Mr. President, there is little I need add. I remember how tearful were the pleas when we were discussing medicare on this floor not too long ago.

I think this is one of the times when some of the tears can well be redeemed by the approval of the amendments before the Senate.

I think that just about exhausts the time I have allowed myself.

Mr. KERR. Mr. President, I know what the distinguished Senator from Illinois has in mind. There are other amendments before us which go generally to the same purpose.

I should like to suggest to the Senator from Illinois a compromise, to see how he would feel about it. If he has a copy of the amendments before him, I think I can identify this.

On page 2, line 8, change "60" to "65."

On page 2, between lines 12 and 13, insert a new subsection, as follows:

(b) LIMITATION TO \$30,000.—The amount of gain which is not recognized as the result of subsection (a) shall not exceed the same proportion of such gain which \$30,000 is of the total sales price of such property.

Change "(b)" to "(c)" at line 13, page 2.

Change "(c)" to "(d)" at line 20, page 2.

Change "(d)" to "(e)" at line 5, page 3.

And, of course, the effective date should be December 31, 1962, wherever "1961" appears in the amendments.

Mr. DIRKSEN. The date has already been changed.

Mr. KERR. If the Senator would be willing to change his amendments to that basis, Mr. President, I would be glad to recommend that they be adopted.

Mr. DIRKSEN. Mr. President, I would not object to the changes. I

suggested age 60, trying to keep it in line with what I thought was a present trend. Certainly the age of 65 does fit with the present concept in so far as legislation of this kind is concerned.

Moreover, the design is to help those upon whom the capital gains tax would be a burden. I would have no objection to the \$30,000 limitation.

In view of my discussion with the Treasury, if the provision needs liberalization, that could be achieved, I think, when there is a further look at tax revision next year.

I believe we ought to make a beginning, and ought to do so now.

Mr. KERR. If the Senator will look that over, to be sure that he and I understand what we are talking about, I think the staff has provided accurate language. We can submit it to the staff again, in order to effectuate what we have discussed.

Mr. PROXMIRE. Mr. President, will the Senator yield?

Mr. DIRKSEN. Mr. President, the effective date, which appears in four different places, has already been modified by my motion.

I yield to the Senator from Wisconsin.

Mr. PROXMIRE. As I understand the amendments, as modified, they would apply only to the home selling for \$30,000, or that portion of the sales price less than \$30,000 of a home which is sold?

Mr. KERR. No. There is to be a \$30,000 limitation. If the sales price of the house did not exceed \$30,000, the capital gain in its entirety would be exempt. I believe that is the purpose.

Mr. DIRKSEN. It would be entirely exempt.

Mr. KERR. If the sales price did not exceed \$30,000, the entire capital gain would be exempt.

The sales price might exceed \$30,000. Let us say the sales price is \$40,000. Then three-fourths of the capital gain would be exempt. If the sales price were \$50,000, then three-fifths of the capital gain would be exempt. If the sales price were \$60,000, one-half of the capital gain would be exempt.

In other words, the amount of the gain which would be exempt, if the sales price were above \$30,000, would be in direct proportion as \$30,000 is to the total sales price.

Mr. PROXMIRE. I have one other question.

As I understand the modification of the amendments, it would limit the provision to people over the age of 65, rather than over the age of 60.

Mr. KERR. Those 65 or over would be covered.

Mr. PROXMIRE. As I understand the present tax law, it permits double deductions for people over the age of 65. Instead of having \$600 exemptions, they have \$1,200 exemptions; do they not?

Mr. KERR. The Senator is correct.

Mr. PROXMIRE. Is it not correct that some 75 to 80 percent of the people over the age of 65 pay no income taxes now?

Mr. KERR. I am not in a position to answer that question.

Mr. McNAMARA. Mr. President, will the Senator yield for a question?

Mr. KERR. I yield to the Senator.

Mr. McNAMARA. Does the proposition offered by the Senator from Illinois and the Senator from Oklahoma require that this be a one-shot operation? It could not be repeated over and over?

Mr. KERR. Well, it could not be repeated very often, because under the language of the Senator's amendments, as I understand, they would be applicable only if the owner had the home 5 years.

Mr. McNAMARA. A man might own several pieces of property.

Mr. KERR. This would apply only to the home.

Mr. McNAMARA. By going from one to another he could repeat the operation.

Mr. DIRKSEN. It would have to be his primary residence.

Mr. McNAMARA. I would expect the amendment to be spelled out, to limit it as the law is limited with respect to special benefits on the purchase of a home, or with respect to educational benefits—to one opportunity.

Mr. MANSFIELD. Mr. President, will the Senator yield?

Mr. DIRKSEN. I yield.

Mr. MANSFIELD. I think the Senator from Michigan has made a good point. I think that intent ought to be made clear in the debate which is now going on.

Mr. McNAMARA. I would have no objection to the amendment, if that limitation were included.

Mr. DIRKSEN. The arithmetic would be against any individual who would try to make it a repeating operation. First, we have to start with 65. Second, it must be the taxpayer's primary home. Third, he must have occupied the dwelling for a period of 5 years.

Let us assume that there had been one such operation. The taxpayer acquiring another home would probably have to be well over 70 before he could sell it and undertake to realize another capital gain. He would have to qualify the dwelling as a home for a period of 5 years.

Mr. KERR. Mr. President, I believe that answers the Senator's question.

Mr. McNAMARA. I think it answers it. What the Senator, in effect, said is that, as a practical matter, it would work out. So why not limit the provision to one home? I think it would make sense.

Mr. MANSFIELD. I think the debate has shown that to be the intent.

Mr. KERR. Mr. President, if we are going to agree to the amendment with reference to a homeowner, the provisions in the bill seem to the Senator from Oklahoma to be sufficiently restrictive, so that it would be a remote possibility that one taxpayer would receive the benefit of the amendment more than once. But, so far as I am concerned, if I were going to accept the amendment, and pursuant to its provisions a person made a sale of a home after he or she was 65 years of age, and then acquired another home and occupied it as a primary residence and home for a period of 5 years or longer and made a sale, I would see no reason for the provision being applicable again.

Mr. McNAMARA. I thank the Senator.

The PRESIDING OFFICER. The question is on agreeing to the amendment as modified.

The amendment, as modified, was agreed to.

Mr. PROXMIRE. Mr. President, I call up my amendments numbered "8-30-62-C" and ask that it be stated by title.

The PRESIDING OFFICER. The amendments of the Senator from Wisconsin will be stated.

The CHIEF CLERK. Amendments proposed by the Senator from Wisconsin designated "8-30-62-C."

Mr. PROXMIRE. Mr. President, I ask unanimous consent that the reading of the amendments be dispensed with.

Mr. KERR. Mr. President, reserving the right to object, I should like to see a copy of the amendments.

Mr. PROXMIRE. They are amendments "8-30-62-C."

Mr. KERR. I have no objection, if the Senator will explain them.

The PRESIDING OFFICER. Without objection, the amendments will be printed in the RECORD.

The amendments offered by the Senator from Wisconsin are as follows:

On page 15, beginning with line 11, strike out all through line 15 on page 16.

On page 16, line 16, strike out "(4)" and insert "(3)".

On page 19, beginning with line 23, strike out all through line 12 on page 20.

On page 20, line 13, strike out "(3)" and insert "(2)".

On page 20, lines 15 and 16, strike out "or any change in use described in paragraph (2)".

On page 20, line 18, strike out "(or change in use)".

On page 20, line 19, strike out "(4)" and insert "(3)".

On page 20, line 21, strike out "(3)" and insert "(2)".

On page 22, lines 13 and 14, strike out "transportation, communications, electrical energy, gas, water, or sewage disposal" and insert "transportation or communications".

On page 25, after line 11, insert the following:

"(7) PUBLIC UTILITY PROPERTY.—

"(A) Public utility property (as defined in subparagraph (B)) shall not be treated as section 38 property.

"(B) For purposes of subparagraph (A), the term 'public utility property' means property used predominantly in the trade or business of the furnishing or sale of—

"(i) electrical energy, gas, water, or sewage disposal services,

"(ii) gas through a local distribution system,

"(iii) telephone service, or

"(iv) telegraph service by means of domestic telegraph operations (as defined in section 222(a)(5) of the Communications Act of 1934, as amended; 47 U.S.C., sec. 222(a)(5)),

if the rates for such furnishing or sale, as the case may be, have been established or approved by a State or political subdivision thereof, by an agency or instrumentality of the United States, or by a public service or public utility commission or other similar body of any State or political subdivision thereof."

Make necessary changes in cross-references to the paragraphs renumbered by the preceding amendments.

Mr. PROXMIRE. Mr. President, the amendments would eliminate utilities from the investment credit provisions and privileges provided in the bill. The bill as presently drafted would permit a 3-percent credit for utilities. My amendment would eliminate that. It is in accordance with the recommendation of the Treasury and the Kennedy administration. It would reduce the revenue lost under the bill by \$225 million, according to Treasury estimates. The case that has been made by the Treasury in favor of the amendment in my judgment is extremely strong.

There is no question that utilities are regulated monopolies legally obligated to serve public needs, and to construct facilities on a demand basis to meet public requirements.

STUDY SHOWS FALLACY OF INVESTMENT CREDIT APPLICATION TO ELECTRIC UTILITIES

There is a very excellent and scholarly study by Avram Kesselgoff and Franco Modigliani which supports that position. The study, which is recognized among economists as one of the most competent in the area, was made in 1957, and I wish to quote very briefly from the conclusions of the study:

The main hypothesis of our model is that investment outlays are primarily determined by the relation between the demand for electricity and the amount of capacity required to satisfy this demand economically.

The article points out that the industry is characterized by these particular elements, which make it clear that demand rather than common cost factors or tax factors is mainly responsible for investment. The article states:

Of primary relevance among these characteristics are (a) the long planning and gestation period for investment; (b) the presence and quantitative importance of indivisibilities in fixed assets; (c) the rapid growth of the demand for electrical energy; (d) the impossibility of storing the product; and last but not least (e) the influence of institutional factors resulting from public regulation of the industry.

The final conclusion of the study is as follows:

On the basis of our statistical analysis, we cannot reach a definite conclusion concerning the influence of interest rates on investment; however, the evidence strongly suggests that in this industry, where fixed assets are of great longevity, the cost of borrowed funds was not an important factor. In general, cost considerations appeared to play a minor role in the decisions of the utilities—a finding which may again reflect the way the "fair return on the fair value" principle is applied in the industry.

Of course, that is the only way in which the investment credit could have an effect in providing an incentive for investment. Cost considerations appear to play a minor role.

Mr. President, I ask unanimous consent that the details of the study be printed at this point in the RECORD.

There being no objection, the article was ordered to be printed in the RECORD, as follows:

PRIVATE INVESTMENT IN THE ELECTRIC POWER INDUSTRY AND THE ACCELERATION PRINCIPLE

(By Avram Kesselgoff and Franco Modigliani)

This inquiry is part of a more comprehensive investigation of investment behavior, carried out under a grant of the Merrill Foundation for Advancement of Financial Knowledge. In the companion studies of this investigation, extensive use was made of data on entrepreneurial expectations and plans.¹ Unfortunately, reliable and systematic information of this type is limited exclusively to the postwar period, relatively brief and abnormal in many respects. Thus it was thought desirable to supplement the studies based on business anticipations in the postwar period with an intensive analysis of historical data on investment in fixed capital in selected industries prior to the last war. In this analysis an attempt was made to isolate the causal factors underlying investment decisions without the benefit of the intermediate link represented by data on expectations and plans.

The present paper is concerned with the electric power industry only.² The most important considerations that led us to focus our attention on this industry are (a) its heavy capital requirements, (b) the homogeneous character of its physical output and productive capacity (c) the availability of abundant economic accounting and operational data of a relatively high degree of uniformity.

The electric power industry can be divided into two segments: (1) Privately owned utility companies which now provide about 80 percent of total public energy supply and (2) other electric power facilities mainly owned by the Federal, State, and local governments which account for the remaining 20 percent.³

Since the primary objective of this study is to throw light on the behavior of private investment, the analysis will be restricted here to fluctuations in the capital expenditures of private electric utility companies. Because of the impossibility of separating new investments from reinvestments—a great many installations in the electric power industry being at the same time replacements, extensions, and improvements—gross expenditures on plant and equipment will be used in this paper as the variable to be explained.

The statistical analysis, unless otherwise indicated, is based on time series of industry aggregates for the period 1926-41.⁴

¹ See I. Friend and J. Bronfenbrenner, "Business Investment Programs and Their Realization," Survey of Current Business, December 1950, and "Plant and Equipment Programs and Their Realization," Studies in Income and Wealth, vol. XVII; F. Modigliani and O. H. Sauerlender, "Economic Expectations and Plans of Firms in Relation to Forecasting," Studies in Income and Wealth, vol. XVII; R. Eisner, "Interview and Other Survey Techniques and the Study of Investment," Studies in Income and Wealth, vol. XIX, and "Expectations, Plans and Capital Expenditures: A Synthesis of Ex Post and Ex Ante Data," Proceedings of the Conference on Expectations, Uncertainty and Business Behavior, sponsored by the Social Science Research Council.

² Another study on investment in the telephone industry is forthcoming.

³ The percentages mentioned above refer to the year 1953.

⁴ A similar study for the electric power industry based on cross-section data will be published separately.

BASIC HYPOTHESES AND TESTS

It is a commonly accepted view in economic theory that the flow of capital expenditures depends on the relation between the anticipated productivity of money spent on additions to plant and equipment and the cost of funds, which is mostly identified with long-term interest rates after some allowance for risk. This view, however, is purely formal and is of doubtful value in a statistical analysis because of the lack of direct information on the anticipated productivity of capital. It has been frequently suggested that the productivity of capital can be approximated by the level of realized profits. This suggestion may have merits in dealing with competitive industries, although even in this case several assumptions must be made. In a competitive industry a shift to the right of the demand schedule or a reduction in costs should tend initially to increase profits. If the change in cost or demand conditions is regarded as permanent, the initial increase in profits (above the levels prevailing in other industries) would tend to bring about expansion of production and, therefore, investment by the existing firms and/or by new entrants. However, in monopolistic industries a high level of realized profits (i.e., a high average productivity of capital) need not be a reliable measure of the marginal productivity of investments, which presumably controls capital outlays; indeed the high level of profits may simply reflect the successful exploitation of the monopoly power which may be "spoiled" by an expansion. These considerations apply with particular force to regulated industries, such as electric utilities, where firms are usually without direct competition in their service areas and are subject to various controls which greatly affect, directly and indirectly, the level of their profits and the conditions under which the profits are obtained. It is not surprising, therefore, to find that profits and interest rates alone completely fail to account for investment behavior of electrical utilities. This is shown by equations (1) and (2) based on data for 1924-41.

(1)

$$(I/A)_t = 18.9 - .162(II'/A)_t + 62.9r_t \\ (\pm .805) \quad (\pm 42.7) \\ R = .22 \quad S = 122.0$$

(2)

$$(I/A)_t = 297 - .909(II'/A)_{t-1} + 61.7r_{t-1} \\ (\pm .570) \quad (\pm 35.0) \\ R = .38 \quad S = 115.5$$

where

I = aggregate gross expenditures on plant and equipment in private electrical utilities, measured in millions of dollars;

A = construction costs for plant and equipment in the electric light and power industry, 1911: 1.00;

II' = aggregate net income before interest deduction of private electrical utilities, measured in millions of dollars. Since the purpose of the present test is to determine the influence of the rate of interest on investment, interest charges were added to net income.⁵

r = annual yield averages of new bonds.

The numbers in parentheses below the regression coefficients are standard errors; R is the multiple correlation coefficient, and S is the standard error of estimate; both statistics are adjusted for degrees of freedom.

It can be seen from equation (1) that current profits and the cost of borrowed new money account for only a negligible proportion of the variation in investment; furthermore, the estimated coefficients of both vari-

ables have signs opposite from what would have been expected on a priori grounds, and they are not significantly different from zero at the 5 percent level.⁶ Equally unsatisfactory results are obtained in equation (2), where lagged income and interest rates were used in order to make some allowance for the time that may be required to carry out investment decisions.⁷

A major reason for these poor results is to be found in the influence of institutional factors. Because of their monopolistic character which may lead to abuses, electric utilities are subjected to various regulations. The most important among them, having a direct bearing on the problem under consideration, are controls over profits and rates. Generally, profits in the electric power industry are governed by the "cost plus" principle with the specific recognition that investors are entitled to a "fair return on a fair value." In practice the application of this principle is a complicated procedure which requires the determination of the utilities' operating expenses, taxes, depreciation, and the value of property, which is most frequently fixed by State commissions and courts. The rate of return, as a rule, is computed on the overall rate base, and no increase in rates is granted on the basis of insufficient return on a part of investment. As a result, the return on new investments frequently is not estimated by utilities. Equally relevant in this connection is the fact that once capital expenditures are made, the commissions usually support the utilities' capitalization. However, when the demand for electrical power expands, no increase in the utilities' profits through an increase in rates is possible. The regulatory measures on the books will prevent electric utilities from exploiting this situation. On the contrary, since electric utilities are under obligation to meet the expanded demand, they can be expected to provide additional facilities which might result in reduced rates through reduced costs. But if a company, in its search for profit, decreases its costs to the extent that it obtains a considerable increment in earnings, the regulatory bodies can initiate an investigation and eliminate the whole increment. It may be observed here that the development of these practices applied by regulatory authorities in profit and rates determination have been greatly facilitated by a rather low price elasticity of demand for electrical energy.⁸

⁵ It would have been interesting to repeat the test of equations (1) and (2) using as the dependent variable net investment (outlays for additions to capacity) instead of gross investment. Unfortunately data for such a test are not available. There are reasons to believe, however, that this substitution could not affect significantly the conclusions suggested by the test. In the first place the electric power industry is relatively young and the major types of plant and equipment it employs have a very long service, ranging from 20 to 50 years. (Cf. Bulletin F, rev. ed. January 1942, of the Bureau of Internal Revenue, U.S. Treasury Department.) Accordingly, in the period under consideration expenditures on replacements were relative unimportant. This is precisely the finding of the investigation reported by Michael Gort in *Journal of Business of the University of Chicago*, xxiv (July 1951), 188. According to Mr. Gort, "Of the six categories (of investment) the first, additional capacity for load growth, completely dominated all others in all the budgets seen."

⁷ Poor results are also obtained when only current income, or income lagged 1 year, after deducting interest payments, is correlated with investment.

⁸ See Emery Troxel, "Economics of Public Utilities" (New York, 1947), 429-431.

The protective as well as the restrictive nature of controls, as they are exercised in the electric power industry, greatly reduces the importance of past or current profits as a decisionmaking variable in planning investment. However, as a source of investible funds and as a factor reflecting short run business expectations, profits probably are of some significance in the investment process and, therefore, should be considered in the analysis; their effect may be expected to become apparent only when other major investment determinants are taken into account.

In order to formulate a satisfactory hypothesis as to these other major determinants, one must take into account four essential characteristics of the industry which have been mentioned in the previous discussion: (a) the strong upward secular trend in the demand for electricity; (b) the legal obligation of the companies to satisfy the demand for electric power in the areas in which they have a franchise; (c) the expectation of the companies, founded on precedent and legal provisions, that the regulatory bodies will include the new investment in the rate base and will be willing to establish such rates as to insure an adequate return on the expanded property; (d) the confidence of the companies, justified by the growing demand and the monopolistic nature of the market, that such rates can be enforced.⁹ These characteristics strongly suggest that the major determinant of investment in this industry is to be found along the lines indicated by the acceleration principle, i.e., in the relation between existing production, distribution, and transmission facilities and the facilities required to satisfy efficiently the current and prospective demand for electric power.

To translate this relation into a specific hypothesis capable of empirical testing, it will be useful to introduce the notions of "actual" and "optimum" annual rates of utilization of capacity.

The actual rate of utilization in a given year t is defined as the ratio of kilowatt-hours sold in that year, denoted by P , to kilowatts of installed capacity, S ; it is, therefore, represented by $(P/S)_t$. The upper theoretical limit of this rate, is, of course, equal to the number of hours per year or 8,760. However, for a variety of reasons the technologically feasible and economically advantageous rate of utilization tends to be well below this ceiling.

First, the demand for electricity from a given source, like most other demands, exhibits characteristic and systematic patterns of daily and seasonal peaks and troughs. However, in contrast with many other commodities, electric power cannot, at present, be stored on a commercial basis and must, therefore, be produced at the instant it is demanded. Hence, facilities have to be geared to peak sales and generally cannot be utilized continuously and fully throughout the year. Moreover, in order to insure reliable and orderly service, suppliers must have enough reserve equipment for the replacement of any unit of equipment which becomes incapacitated for mechanical reasons. Finally, since this growing industry also enjoys economies of scale, when an expansion is undertaken, it is profitable (in the sense that it reduces costs over time) to add more capacity than is expected to be required in the immediate future. Hence,

⁹ It is this last characteristic together with the related characteristic (a) that sharply distinguishes the electric utilities from the other major regulated public utility; namely, railroads. In the latter industry, because of the strong competition from other means of transportation, it may be impossible to enforce a system of rates insuring an "adequate" return.

⁵ See T. Haavelmo, "The Effect of the Rate of Interest on Investment," this Review, xxiii (February 1941), 49-52.

for this reason, too, it is generally advantageous for companies to carry on the average a certain margin of overcapacity.¹⁰

On the basis of these considerations, the optimum rate of utilization at a given point of time will be defined as the maximum number of kilowatt-hours per year which it is economically desirable to produce for sale per kilowatt of installed capacity, under the conditions (technology, pattern of demand, etc.) prevailing at that point of time. This optimum rate, varying over time, will be denoted by $(P/S)_t$.

In terms of these concepts, we propose to test the hypothesis that the major factor controlling the rate of investment by private electric utilities is their endeavor to maintain the rate of utilization of capacity at the optimum level. It should be observed that capacity, as measured by kilowatts installed, does not include all the facilities of the industry. However, capacity so defined is a component which can be measured with a minimum of ambiguity and constitutes, in fact, the principal part of the facilities to which all other parts of the capital stock are largely geared.

Let us assume for the moment that additional capacity can be provided in about 1 year. Then, on the basis of the hypothesis put forth above, we should expect investment in a given year to be an increasing function of the difference between the ratio of demand anticipated a year hence to presently existing facilities, on the one hand, and the optimum rate of utilization of capacity, on the other. Neglecting other factors temporarily, this hypothesis can be approximated by a linear function as follows:

(3)

$$I_t = a[AP_{t+1}/S_{t-1} - (P/S)_t]$$

where I_t is investment, in real terms, in a given year t ; AP_{t+1} , output anticipated in the given year for the next year, $t+1$; S_{t-1} , the amount of capacity in existence in the previous year; and a , a proportionality constant, reflecting the intensity of response to the stimulus to invest as well as the cost of providing additional capacity.

Since we have no direct information on anticipated output, AP_{t+1} , it is necessary to introduce some hypothesis as to how this variable might be approximated. Methods frequently used by electric utilities for estimating prospective demand are based on their past experience and amount roughly to an extrapolation of the sales trend. Since the latest information available on output is P_{t-1} , then, if demand is assumed to grow at a constant rate of i percent per year, we may write

$$AP_{t+1} = (1+i)^2 P_{t-1}.$$

This leads by substitution in equation (3) to:

(4)

$$\begin{aligned} I_t &= a[P_{t-1}(1+i)^2/S_{t-1} - (P/S)_t] \\ &= a(1+i)^2[P_{t-1}/S_{t-1} - I/(1+i)^2(P/S)_t] \\ &= a'[P_{t-1}/S_{t-1} - (1-\gamma)(P/S)_t] \end{aligned}$$

where $a' = a(1+i)^2$ and $\gamma = 1 - I/(1+i)^2$.

Equation (4) is also consistent with another hypothesis on the formation of anticipations of future demand and the method of providing capacity to meet this demand. Instead of making explicit forecasts of fu-

ture sales and deriving from them estimates of capital requirements, companies might adopt investment programs designed to provide a "normal" margin of reserve capacity over and above that needed for current demand. This idea can be formalized by introducing the notion of a "critical" rate of utilization of capacity, say $(P/S)_t$, some γ percent below the optimum rate $(P/S)_t$. Then whenever the current actual rate of utilization exceeds $(P/S)_t = (1-\gamma)(P/S)_t$, companies may be expected to invest in order to reestablish the proper cushion of excess capacity. For instance, if γ were .20 and $(P/S)_t$ were 4,000 hours, an increase in the actual average rate of utilization of capacity beyond 3,200 hours would call for additional investment. The procedure described is a flexible way of allowing for the anticipated growth of demand, since the availability of reserve capacity permits the utility to meet increased demand while additional capacity is being provided. Clearly this type of behavior can be represented again by an equation of the form (4), and the expression $(1-\gamma)(P/S)_t$ in the bracket on the right-hand side can be regarded as the critical rate of utilization of capacity. Thus equation (4) is consistent with either approach to the determination of capital requirements, or with any mixtures of these two types or closely related ones.¹² While our equation need not describe accurately the behavior of any individual firm, it may be hoped to provide a reasonable approximation to aggregate behavior.

In order to make our description of the investment process in the electric industry more realistic, we must, however, take into account the actual time period of planning, ordering, and installing of new generating capacity. According to information gathered directly from the industry, the length of this period under normal conditions can be estimated at about 2 years, on the average. Since the length of the gestation period plays an important role in our analysis, an attempt was made to test the reliability of this information by means of the following indirect test.

If about 2 years are required to complete an installation of new generating capacity, then part of investment expenditures in a given year, t , would represent outlays for the purpose of bringing to completion projects started in the year before. These outlays, which we shall call "completion expenditures" or simply "completions," should result in additions to generating capacity within year t itself, denoted by ΔS_t . Another part of current outlays would be generated by the initiation of new projects or "starts" and would result in additions to generating capacity in the following year, ΔS_{t+1} . Under these conditions total investment in year t should be closely correlated with, and largely accounted for by, ΔS_t and ΔS_{t+1} . Equation (5), based on these three variables for the period 1924-41, yields a confirmation of this expectation.

¹² Note that under the type of investment behavior implied by our second formulation, the actual rate of utilization would usually be above the critical rate, because of the growth of demand occurring during the gestation period. In fact, if demand were growing at a fairly steady rate, we might expect the coefficient γ to be such that the actual rate of utilization would tend, on the average, to be close to the optimum rate. The difference between the two alternative hypotheses leading up to equation (4) is, therefore, less significant than might appear at first sight, and it is quite conceivable that in many cases utilities might rely simultaneously on both approaches.

(5)

$$\begin{aligned} (I/A)_t &= 101 + .057\Delta S_{t+1} + .074\Delta S_t \\ (\pm .015) & \quad (\pm .015) \\ R &= .935 \quad S = 46.3 \end{aligned}$$

where $(I/A)_t$ represents gross investment expenditure in year t in millions of deflated dollars; ΔS_t and ΔS_{t+1} , capacity installed in year t and $t+1$, respectively, in thousands of kilowatts.

It is hardly necessary to point out that this is essentially a "technical" and not a "behavior" equation. First, it relates investments in the year t to events occurring after that year, and second, it does not contain factors determining decisions to add to capacity. The fact that the coefficients of both variables are reliable statistically and their relative magnitude plausible, is, however, of significance. It confirms that it is both reasonable and useful to regard investment in year t as consisting of two major components, starts and completions, each of which must be taken into consideration.¹³

Since completion expenditures in year t are generated by starts of year $t-1$, we can account for this component by using equation (4), after replacing in it P_{t-1}/S_{t-1} by P_{t-2}/S_{t-2} . As for outlays on starts, we may measure the incentive to initiate new projects by means of the ratio P_{t-1}/S_{t-1} , corrected for the dampening influence of projects started in year $t-1$ which are not yet reflected in S_{t-1} but will shortly result in additional capacity. Since starts of year $t-1$ are assumed to depend on P_{t-2}/S_{t-2} , we propose to measure the net incentive in year t by means of the difference $(P_{t-1}/S_{t-1} - P_{t-2}/S_{t-2})$. In so doing we recognize that P_{t-2}/S_{t-2} has the following double and partly offsetting effect on investment in year t : on the one hand, the larger the volume of projects in year $t-1$ the greater will be expenditures required for the completion of these projects in year t ; on the other hand, the larger the volume of the projects started in year $t-1$, the smaller will be, ceteris paribus, the necessity to initiate new projects in year t . Thus when the lag between decisions to invest and the corresponding investment outlays is taken into account, our hypothesis becomes:

$$I_t = f[(P/S)_{t-2}, [(P/S)_{t-1} - (P/S)_{t-2}], (P/S)_t].$$

(6)

If $(P/S)_t$ were constant, this relation would contain only two explanatory variables. However, we have evidence that the ratio $(P/S)_t$ rose gradually over time, that is to say, an increasing flow of services was obtained from a given stock of capital. The main factors responsible for this increase are consolidation and integration of markets for electric energy, along with the development of new uses for such energy and incentive rates. As a result, coincidental peaks were greatly reduced and idle capacity and excess reserves were rendered more flexible in both space and time, a process that led to a gain in the average annual rate of utilization of capacity from 1926 to 1941 of a little more than 30 percent. Of course, it would have been ideal to know exactly the value of $(P/S)_t$ at each point of time. Unfortunately this information cannot be obtained directly from engineering data. One possible solution consists in approximating $(P/S)_t$ by some function of time.¹⁴

¹³ A lack of data on replacements made it necessary to relate in equation (5) gross expenditures to net additions to capacity. Since, however, additional capacity for load growth was predominant during the period under consideration, the indicative value of the test is not greatly affected.

¹⁴ An alternative solution will be advanced on p. 37.

¹⁰ This idea has been aptly developed by H. B. Chenery in "Overcapacity and Acceleration Principle," *Econometrica*, xxii (January 1952), 1-28.

¹¹ In this study we shall consistently measure demand by output. Demand so defined exceeds sales by the loss of energy in the process of transmission and the use of energy by the utilities themselves; it may be regarded as the amount of production necessary to meet the given sales.

$$(P/S)_t = \phi(T) \quad (7)$$

Substituting (7) into (6) we obtain:

$$I_t = F[(P/S)_{t-2}, [(P/S)_{t-1} - (P/S)_{t-2}], T]. \quad (8)$$

We shall also add to this expression the variable, Π_t , representing net income plus depreciation in year t . This variable may be expected to play the role of an enabling factor, to the extent that it can be a source of funds from current operations for investment purposes, and of a controlling factor, to the extent that the net income component might reflect shortrun business expectations and lead to the cancellation, postponement, or acceleration of investment plans. Thus, after adjustment of the variables I and Π for price changes, our basic hypothesis, when expressed in a linear form, becomes:

$$(I/A)_t = \delta_0 + \delta_1(\Pi/A)_t + \delta_2[(P/S)_{t-1} - (P/S)_{t-2}] + \delta_3(P/S)_{t-2} + \delta_4 T + E_t \quad (9)$$

where E is the random disturbance. The least-square estimates of the parameters are:

$$\begin{aligned} (I/A)_t &= -495 + .661(\Pi/A)_t \\ &\quad (\pm .234) \\ &+ .253[(P/S)_{t-1} - (P/S)_{t-2}] + .225(P/S)_{t-2} \\ &\quad (\pm .038) \quad (\pm .024) \\ &\quad -21.3 T \\ &\quad (\pm 2.4) \\ R &=.972 \quad S=29.3 \quad K=2.24. \end{aligned} \quad (10)$$

Judged by statistical criteria, the parameters of equation (10) seem to be reliably estimated. The value of K , which is the measure of the autocorrelation of E , is high enough so that the hypothesis that the residual variation is random with respect to time cannot be rejected.¹⁵ Taken together, the four explanatory variables account for about 95 percent of the annual variation in capital expenditures in the period under consideration. The most important of the variables are those representing the yearly rates of utilization of capacity and T , reflecting the gradual increase in the optimum rate of utilization of capacity and possibly also other influences.¹⁶ The net income plus depreciation variable, $(\Pi/A)_t$, also was found significant. It may be observed, however, that when equation (10) is modified by replacing $(\Pi/A)_t$ with $(\Pi/A)_{t-1}$ the new estimates are:

$$\begin{aligned} (I/A)_t &= -451 + .321(\Pi/A)_{t-1} \\ &\quad (\pm .226) \\ &+ .261[(P/S)_{t-1} - (P/S)_{t-2}] \\ &\quad (\pm .050) \\ &+ .252(P/S)_{t-2} - 22.2 T \\ &\quad (\pm .026) \quad (\pm 2.4) \\ R &=.959 \quad S=35.4 \end{aligned} \quad (II)$$

In this equation, the coefficient of regression of Π/A decreases by a little more than 50 percent, becomes statistically less reliable, and the total correlation falls below that of equation (10).¹⁷ On the contrary, the coefficients of regression of the other variables show a high degree of stability. Since at least 1 year is required to carry out large-scale investment programs, these results are not inconsistent with the hypothesis that profits are not a key variable in major investment decisions.

On the whole, our analysis so far indicates that the most satisfactory explanation of fluctuations in capital expenditures in the electric power industry for the period of

1926-41 is provided by equation (10). It is not without interest, however, to review at this point some other hypotheses tested which throw additional light on the process of investment decisions.

FURTHER TESTS ON THE ROLE OF PROFITS, INTEREST RATES, OTHER VARIABLES

An attempt was made to take into account the structure of investment in the electric power industry. The available data allow the splitting of total investment into plant expenditures and equipment expenditures. This breakdown of total investment outlays, however, can be done only crudely and our estimates are subject to a very considerable margin of error. Yet the attempt appears worth while because the two components of investment may be expected to be affected by somewhat different influences.

Our hypothesis of a 2-year gestation period appears acceptable in the case of investment in plant but probably is less reasonable for equipment expenditures. Accordingly equation (9) can be used without further modification to explain outlays on plant.

The results are shown in equation (12).

$$\begin{aligned} (I'/B)_t &= -195 + .155(\Pi/A)_t \\ &\quad (\pm .107) \\ &+ .123[(P/S)_{t-1} - (P/S)_{t-2}] \\ &\quad (\pm .017) \\ &+ .116(P/S)_{t-2} - 11.9 T \\ &\quad (\pm .011) \quad (\pm .82) \\ R &=.979 \quad S=13.3 \quad K=2.43 \end{aligned} \quad (12)$$

where I' denotes plant expenditures in millions of dollars; and B , the plant construction cost index (1911:1.00).

These results are again quite favorable and are generally very similar to those of equation (10) both in form and interpretation. The only difference worth noting is that the coefficient of profits is considerably lower and its standard error is relatively greater. This indicates that the influence of profits, Π/A , on investment in plant is weak, a finding to be expected on a priori grounds. Once the construction of a plant is started, a utility might find it advantageous to carry it to completion regardless of current fluctuations in profits, rather than to incur losses from halting the construction. Such a situation seems to have existed, for instance, in 1930 when many companies, disregarding a decrease in their incomes, preferred to complete their plants under construction rather than to abandon them entirely.

In the case of equipment, the lag between decision and outlays is likely to be shorter. Hence spending, both for expansion and replacement, should be primarily influenced by the rate of utilization of capacity in the immediately preceding year $(P/S)_{t-1}$. In addition, because of the complementarity between plant and equipment, we might expect equipment outlays to depend also on current expansion of plant, which can be approximated by plant expenditures $(I'/B)_t$. Finally, because equipment can be procured, on the average, on relatively short notice, and previous commitments can be canceled with smaller loss than in the case of construction underway, we should expect current profit to be of greater relevance than in equation (12). The resulting hypothesis explaining expenditures on equipment and its statistical test is as follows:

$$\begin{aligned} (I''/C)_t &= -155 + .286(\Pi/A)_t \quad (13) \\ &\quad (\pm .082) \\ &+ .034(P/S)_{t-1} + .802(I'/B)_t \\ &\quad (\pm .009) \quad (\pm .051) \\ R &=.985 \quad S=11.0 \quad K=1.63 \end{aligned}$$

where I'' represents estimated equipment expenditures, and C is the price index of equipment (1911:1.00).

The data appear to support our hypothesis. This is evidenced by the very high multiple correlation coefficient and by the fact that

the coefficients of all the variables have relatively small standard errors. In particular the coefficient of profits is larger than in equation (12) both in absolute terms and relative to its standard error. This suggests that the importance of the profit variable in equation (10), pertaining to total investment, can be attributed mainly to its significant role in the determination of equipment expenditures.

It may be noted that in equation (13) we have used as one of explanatory variables current expenditures on plant $(I'/B)_t$. Since this variable is part of the total investment outlays that we are interested in explaining, it might appear that equation (13) could be of little use in forecasting. Such a conclusion would not be warranted, however, since for purposes for forecasting, the unknown value of $(I'/B)_t$ could be replaced by the known value computed from equation (12). This substitution, in fact, may be used also in estimating the coefficients of equation (13) and has some merit from the statistical point of view. It amounts to recognizing, in the estimating procedure, that equations (12) and (13) represent a system of simultaneous stochastic difference equations in which $(I'/B)_t$ and $(I''/C)_t$ are jointly determined variables.¹⁸ This procedure was, therefore, actually employed to obtain an alternative estimate of the coefficients of equation (13), and the results were found to be very nearly the same as those reported above.

It must be pointed out, however, that because of the crudeness of the estimates of the plant and equipment breakdown of total investment, great reliance cannot be placed on equations (12) and (13). The main reason for reporting the results, tentative as they are, is for the light they may throw on the behavior of the two components of investment and especially on the role of profits as a decision variable.

A full inquiry into the investment process should include an exploration of the effect of the rate of interest. While factual investigations in various industries do not indicate that the interest rate has a marked influence on capital spending, there are theoretical reasons to believe that this variable might affect investments in long-lived assets, especially when financed with outside funds.¹⁹

Electric utilities have large capital investments of great longevity. Because they make capital commitments, on the average, of \$5 to \$7 in order to produce a yearly revenue of \$1, the rate of utilities' capital turnover is low. This fact, as well as regulatory practices, makes it impossible for them to finance extensive construction programs by means of retained earnings and/or depreciation accruals alone. The available data indicate that during the second half of the 1920's approximately 75 percent of the funds came from the capital market and the remaining 25 percent from internal sources.²⁰ During the second half of the 1930's the utilities had recourse to capital market funds for only about 20 percent of their total

¹⁸ This statement implies that $(\Pi/A)_t$ can be treated as an exogenous variable, an assumption which we regard as not too unrealistic for a single industry.

¹⁹ See George W. Terborgh, "Dynamic Equipment Policy" (New York, 1949). Lawrence Klein found the effect of the rate of interest on investment decisions in the railroad industry to be significant. See his "Studies in Investment Behavior" (National Bureau of Economic Research). Although, from the viewpoint of "rational" behavior, the origin of funds should not affect investment decisions of management, it seems to be, empirically, a factor of importance.

²⁰ Eli Winston Clemens, "Economics and Public Utilities," 119.

¹⁵ K is the ratio of the mean-square successive differences to the variance of the residuals.

¹⁶ See p. 375 below.

¹⁷ Unsatisfactory results are also observed when $(\Pi/A)_{t-2}$ is used in the similar test.

financial requirements. This lesser reliance on external financing is due partly to the lower level of their investments and partly to a shift from the retirement to the depreciation method of accounting which resulted in a greater availability of funds from internal sources.²¹ In the postwar period when the utilities undertook a huge building program in order to meet the tremendously increased demand for electricity, the capital market again became the major source of their financing.

These observations suggest that, at least in the case of electric utilities, there might be some opportunity for interest rates to play a role in investment decisions. Yet there is surprisingly little evidence to support such a conclusion. While changes in interest rates may have had some influence on the form of financing, they do not appear to have exerted a significant stimulating or restraining effect on investments. In fact a cursory examination of the record shows that utilities (not unlike many other industries) usually drew heavily on external sources to finance their investments in periods when interest rates were high but reduced their demand for outside funds when interest was low.²²

This lack of data supporting the proposition that interest rates influence investment decisions in the electric power industry may be due to the overshadowing influence of other variables whose importance was brought out by the earlier analysis. Therefore, in order to test the effect of interest rates on capital expenditures, we revised equation (10) by adding the variable r , annual yield average of new bonds lagged one year, and replacing $(II/A)_t$ with $(II'/A)_{t-1}$, the net operating income plus interest charges.²³ The statistical estimates of the parameters are:

$$\begin{aligned} (14) \\ (I/A)_t = & -780 + .282(II'/A)_{t-1} \\ & (\pm .207) \\ & + .300[(P/S)_{t-1} - (P/S)_{t-2}] \\ & (\pm .060) \\ & + .295(P/S)_{t-2} + 33.3r_{t-1} - 16.7T \\ & (\pm .038) (\pm 35.1) (\pm 5.6) \\ R = .959 \quad S = 35.3. \end{aligned}$$

In this equation the regression coefficient of r is smaller than its standard error and, furthermore, its sign is contrary to what would be expected on theoretical grounds.²⁴ This test also, therefore, fails to support the hypothesis that interest rates play a significant role in the investment process.²⁵

This negative result may reflect, to a

²¹ It may be observed that during the 1930's the utilities not only paid off large amounts of their notes payable and unsecured loans, but also accumulated large cash holdings.

²² Huge utility borrowings during the 1930's represented to a great extent refunding operations for the purpose of reducing capital costs.

²³ See footnote 5.

²⁴ The large standard error and the positive sign of the coefficient of r may be partly due to a very high negative correlation between the variables r and T ($-.89$). While this intercorrelation reduces the reliability of our finding, it does not seem to affect the general nature of our conclusion. Although the sign of the coefficient of r in this equation is correct the coefficient itself is still unreliable.

²⁵ This conclusion, however, is subject to a limitation which should be carefully noted. In our model the behavior of demand up to year t was taken as a datum; the only conclusion warranted by our test, therefore, is that, given the previous history of demand, interest rates are not an important factor. But this history of demand may depend on interest rates, since these certainly affect the price of electricity, which, in turn, may

considerable extent, the regulatory bodies' policies and practices. When a company makes bona fide additions to plant and equipment, it is fairly confident that the State commissions will fix rates adequate to cover all the costs of the services and to yield an average return on the new investment.²⁶ Moreover, although the regulatory authorities can influence expenditures for capital additions through the control of security issues and capital ratios, it is not likely that a company with a balanced capital structure would be prevented from raising the necessary funds on the capital market for its legitimate investment, whatever is the level of the prevailing interest rates.²⁷ Under these practices the rate of interest as an element of cost does not seem to have much opportunity to influence investment decisions.

Slightly better results are obtained when r and II'/A are related to the year of investment.

$$\begin{aligned} (I/A)_t = & -493 + .580(II'/A)_t + .261 \\ & (\pm .213) \quad [(P/S)_{t-1} - (P/S)_{t-2}] \\ & (\pm .049) \\ & + .259(P/S)_{t-2} - 20.8r_t - 22.5T \\ & (14') \\ & (\pm .025) (\pm 26.8) (\pm 4.3) \\ R = .970 \quad S = 30.6. \end{aligned}$$

Another hypothesis considered in our investigation is that, in addition to variables contained in equation (10), the substitution of capital for labor may also affect investment expenditures of electric utilities. The ratio of A/W , where A is electric light and power construction cost index (1911:1.00), and W , average hourly wages measured in cents, may be used as an indicator of the incentive for such substitution. When this variable is added to equation (10) the following results are obtained:

$$\begin{aligned} (15) \\ (I/A)_t = & -799 + .626(II/A)_t \\ & (\pm .241) \\ & + .277[(P/S)_{t-1} - (P/S)_{t-2}] \\ & (\pm .050) \\ & + .202(P/S)_{t-2} + 130(A/W)_{t-1} - 17.0T \\ & (\pm .037) (\pm 157) (\pm 5.5) \\ R = .971 \quad S = 29.8 \end{aligned}$$

The coefficient of A/W is small relative to its standard error and it has the wrong sign. We can, therefore, find no evidence that the relation between capital goods prices and wage costs exerts a significant influence on investment in this industry.²⁸ The result is

be expected to affect demand. A more comprehensive test of the effect of interest would require an analysis of the quantitative importance of this factor in the price of electric energy, as well as of the price elasticity of demand, which is beyond the scope of this study. If the demand for electricity is inelastic, as is frequently stated, then even the roundabout influence of interest may well be negligible.

²⁶ As already noted, this policy on the part of regulatory bodies is possible because the electric power industry is still growing and has a very great potential market for its output.

²⁷ Since 1930 there has been a tendency on the part of the State commissions to use more extensively their powers in the financial field. In 1935 the Public Utility Holding Company Act empowered the Securities Exchange Commission to prescribe capital ratios for corporations subject to its jurisdiction.

²⁸ It may be argued that in this test one should consider not only the price of capital goods but also the cost of funds, which affects the carrying cost of the productive facilities. For this reason we consider using as a variable in this test rA/W instead of A/W (although this might exaggerate the role of interest). However, an inspection of the data suggested that the results would not be significantly different from those reported when A/W is used.

less surprising than the one relating to interest rates. The industry under consideration is highly mechanized with large physical assets in relation to the labor employed and its technology does not appear to offer much scope for substitution between capital and labor.²⁹

REFORMULATION OF BASIC EQUATION, EXCLUDING TIME

The basic equation (10) was found to yield estimates in close agreement with investment experience in the years covered by the study. Yet the results obtained cannot be considered entirely satisfactory, either as an explanation of the past or as a tool for forecasting, without some exploration of the role and significance of the time trend used in the equation.

The time variable is introduced in empirical econometric analysis for reasons of expediency, as a convenient proxy for known or unknown influences. Obviously, more meaningful structural equations are obtained when proxy variables are replaced, whenever possible, by the specific factors which they are supposed to represent. Even if these factors can only be measured crudely, the equations which include them may be expected to provide a better description of the mechanism of economic decisions and to produce more accurate extrapolations to points of time considerably removed from the period of observation.

The major justification we have advanced for the inclusion of the time variable in equation (10) is the gradual increase in the optimum rate of utilization of capacity from 1926 to 1941, made possible by the various developments discussed above. In order to attempt to measure this factor directly we shall have to recast our hypothesis.

We may assume that in any given year t , the investment program of the electric power industry will aim at providing a total capacity which will be denoted $(PS)_{t+1}$ with the superscript $t+1$ used as a reminder that the capacity resulting from capital expenditures in year t will be partly available only in the following year. The addition to capacity implied by the program is thus $(\Delta PS)_{t+1} = (PS)_{t+1} - S_{t-1}$ where S_{t-1} is actual capacity in the preceding year. Part of this increase in capacity will be caused within the year t by the current completion of previous starts and part by new projects with a short gestation period. Let us denote S'_t total capacity expected by the end of year t (after allowance for any reduction in the stock of capital goods due to retirements). Then the amount of additional capacity which must be started in year t for completion in year $t+1$ will be $(PS)_{t+1} - S'_t$. On the assumption that investment expenditures in constant dollars required in the year $t+1$ to complete such projects, denoted $(I^c/A)_{t+1}$, will be proportional to the added capacity we may write: $(I^c/A)_{t+1} = a_1[(PS)_{t+1} - S'_t]$. It follows that completion expenditures in year t will be: $(I^c/A)_t = a_1[(PS)_{t+1} - S'_{t-1}]$. In this equation the quantity S'_{t-1} is not directly observable but can be approximated by S_{t-1} . We therefore have:

$$(16) \\ (I^c/A)_t = a_1[(PS)_{t+1} - S_{t-1}].$$

Besides expenditures on completions, there will be in year t some expenditures on starts, i.e., new projects which will result partly in expansion of capacity in the same year t and partly in an increase in capacity in the following year. These expenditures will again

²⁹ It is interesting to note that Lawrence Klein did not find the substitution of capital for labor important in the investment process even in the railroad industry where there would appear to be more basis for substitution both because of the technology and because of the constant pressure to reduce costs in order to withstand the competition of other means of transportation.

be assumed proportional to the difference between the amount of capacity which appears desirable in year t , $(PS)_{t+1}$, and the amount of capacity which will be in existence in the year t upon the completion of projects carried over from the previous year. Since, by definition, the completion of the preceding year's investment program is supposed to produce a total capacity of $(PS)_{t-1}$, expenditures on starts, denoted by $(I/A)_t$, can be written:

(17)

$$(I/A)_t = a_2[(PS)_{t+1} - (PS)_{t-1}].$$

Total investment expenditures in year t thus will be:

(18)

$$(I/A)_t = (I^c/A)_t + (I^e/A)_t \\ = a_1[(PS)_{t-1} - S_{t-1}] \\ + a_2[(PS)_{t+1} - (PS)_{t-1}].^{30}$$

In this equation $(PS)_{t+1}$ and $(PS)_{t-1}$ are variables on which we do not have direct information; they can, however, be readily expressed in terms of other variables by making use of the fundamental hypothesis underlying equation (10). According to this hypothesis, the investment policies of the electric utilities are directed toward the maintenance of a certain optimum ratio between the latest rate of production and capacity, denoted by $(P/S)_t$. Hence the amount of capacity we should expect the industry to aim for in year t will be:

(19)

$$(PS)_{t+1} = P_{t+1}/(P/S)_t = P_{t+1}(S/P)_t$$

where $(S/P)_t$ denotes the reciprocal of $(P/S)_t$ and represents the desirable amount of capacity per unit of output. Substituting from (19) into (18) we now obtain:

(20)

$$(I/A)_t = a_1[P_{t-2}(S/P)_t - S_{t-1}] \\ + a_2[P_{t-1}(S/P)_t - P_{t-2}(S/P)_t].$$

This equation, however, requires one important modification. In years when the demand for electricity falls below its previous peak, excess capacity may develop and the first term of equation (20) may become negative. In such cases the negative value should be replaced by zero, since it would be meaningless to assume that the existence of excess capacity in year $t-1$ will lead to negative completion expenditures in year t . Or to formulate this more precisely, the quantity $(PS)_{t-1}$ of equation (18), the amount of capacity planned in year $t-1$, can no longer be identified with the optimum amount of capacity $P_{t-2}(S/P)_t$ as suggested by equation (19) and should instead be replaced by S_{t-1} . Thus when $P_{t-2}(S/P)_t < S_{t-1}$, equation (20) becomes:

(20a)

$$(I/A)_t = a_2[P_{t-1}(S/P)_t - S_{t-1}].$$

The two special cases represented by equations (20) and (20a) may be consolidated in the following more general statement: our basic hypothesis is described by equation (18) with $(PS)_{t+1}$ defined by equation (19) and $(PS)_{t-1}$ defined as follows:

(19a)

$$(PS)_{t-1} = [P_{t-2}(S/P)_t, \text{ if larger than } S_{t-1} \\ S_{t-1}, \text{ otherwise.}^{31}$$

³⁰ It should be noted that the two terms of equation (18) are not quite symmetrical. This is due to the fact that the first measures expenditures on projects carried over from the previous year whereas the second measures spending on projects started in year t , part of which may be completed within year t .

³¹ In this formulation, the second term of equation (18) is allowed to assume negative as well as positive values, in contrast with the first term which is allowed to assume only positive or zero values. This asymmetry is justified by the considerations mentioned in footnote 30 and by the additional assumption that only major expansion projects typically involve a long gestation period. A

The variable $(S/P)_t$ appearing in the equations (19) and (19a) is not directly observable. Its changing value over time, however, can be approximated. Since in the electrical utilities industry there is little incentive to cancel major projects once started because of the favorable long-term outlook and the high cost of cancellation, we may assume that $(PS)_{t+1}$ is equal to the actual amount of capacity in year $t+1$, S_{t+1} . Then, on the basis of equation (19), we obtain:

(21)

$$(PS)_{t+1} = S_{t+1} = P_{t+1}(S/P)_t.$$

This equation can be rewritten as follows:

(22)

$$(S/P)_t = S_{t+1}/P_{t+1}.$$

In other words, the optimum rate of utilization in any given year may be measured by the ratio of actual capacity a year later to output lagged 2 years behind capacity. The lag reflects, of course, the interval between investment decisions and the capacity generated thereby. Since S_{t+1} , and hence the ratio S_{t+1}/P_{t+1} is not known in year t , it will be replaced in the statistical analysis by the latest known ratio, S_{t-1}/P_{t-1} . Because generating capacity was utilized with increasing intensity over the period under consideration, this ratio exhibited a declining trend. While there were occasional reversals in the direction of the ratio, these must be regarded as related chiefly to cyclical changes in demand and reflecting, therefore, temporary excess capacity. It thus appears that the trend value of $(S/P)_t$ in any given year t can be approximated best by the lowest previous ratio of capacity to lagged output, which we will denote by $(S_{t-1}/P_{t-3})^L$.

Substituting this term in equation (22) we have:³²

(23)

$$(S/P)_t = (S_{t-1}/P_{t-3})^L.$$

Equation (23) represents the basic relation we have used in estimating the optimum amount of capacity per unit of output.³³

negative value for the second term indicates, of course, excess capacity in year t which may be expected to exert a depressing influence on capital outlays, tending to reduce expenditures below the level required to maintain capacity intact. It may be argued that we are not going far enough in recognizing the asymmetrical influence of under- as against overcapacity on investment expenditures. Positive and negative values of the second variable of equation (18) may well have a different quantitative effect, and one should, therefore, estimate two separate coefficients, one for positive and one for negative values. Whatever the theoretical merits of this argument, the number of years in which the second term of (18) is negative is so small in the period under observation that it would be impossible to secure a reliable estimate of the appropriate coefficient. Furthermore, the asymmetrical effect on investment of under- versus over-capacity is already recognized in our formulation through the definition (19a).

³² We might also have measured $(S/P)_t$ in terms of $(S_t/P_t)^L$, the ratio of capacity to output of the same year. If our model is substantially correct, however, the measure we have proposed should be more reliable, since, in contrast with the suggested alternative, it should not be significantly distorted by unforeseen short-run variations in demand. An examination of the data reveals considerably less pronounced short-run fluctuations around the falling trend of $(S_{t-1}/P_{t-3})^L$ than around that of $(S_t/P_t)^L$, thus confirming our expectations.

³³ Some further adjustment of data was necessary for part of the decade of the 1930's. Because of the depressed conditions and the resulting widespread unintentional excess capacity, during this period $(S_{t-1}/P_{t-3})^L$ tends to overestimate the desir-

In addition to the gradual increase in the optimum rate of utilization of capacity, another factor that appears to contribute to the downward trend in capital outlays in electrical utilities is a gradual decline in the ratio of plant to equipment expenditures, which prevailed through most of the period studied. This decline may be attributed to two major causes. In the 1920's when the industry was new and looking forward to an almost unlimited expansion, utilities tended to build a great deal of basic plant capacity in excess of immediate needs. As a result, although additions to plant facilities continued in subsequent years, relatively larger amounts were spent on equipment than on plant. It was not until 1940 and 1941, when the production of energy rose substantially above the 1929 level, that plant expenditures began once more to gain in relation to those on equipment. Another cause of the downward trend was found in the greater longevity of plant as compared with equipment, a factor of significance in the early stages of an industry's development when expenditures for replacement are concentrated mainly on equipment.

In order to take into account this last factor we shall incorporate in our equation the ratio of plant to equipment expenditures (both measured in constant dollars); namely

$$(I^P/B/I^E/C)_t^{34}$$

After the further inclusion of the profit variable $(\Pi/A)_t$, whose importance was suggested in previous sections, and with substitutions from (19), (19a), and (23), our equation becomes:

$$(I/A)_t = a_0 + a_1[P_{t-2}(S_{t-1}/P_{t-3})^L - S_{t-1}] \\ + a_2[(P_{t-1} - P_{t-2})(S_{t-1}/P_{t-3})^L]$$

(24)

$$+ a_3[I^P/B/I^E/C]_t + a_4(\Pi/A)_t + U_t$$

where U_t is a random term.

When the hypothesis expressed in (24), an alternative to that in equation (10), is tested, the outcome is as follows:

$$(I/A)_t = -300 + .205[(P_{t-1} - P_{t-2})(S_{t-1}/P_{t-3})^L] \\ (\pm .045) \\ + .281[P_{t-2}(S_{t-1}/P_{t-3})^L - S_{t-1}] \\ (\pm .132) \\ (25)$$

$$+ 4.18[I^P/B/I^E/C]_t + .441(\Pi/A)_t \\ (\pm .98) (\pm .422)$$

$$R = .935 \quad S = 43.0 \quad K = 1.98$$

where the starts and completions variables are measured in 10,000 kilowatts and the ratio of plant to equipment expenditures is expressed in percentages.

Considering the nature of the approximations made in the process of reformulation of equation (10), these results appear quite satisfactory and are in agreement with our supposition that the time trend in equation (10) reflects primarily the two factors we have explicitly recognized in (24).

EXTRAPOLATION TESTS

A final test of the reliability of our results is provided by a check on the predicting ability of equations (10) and (25) outside the sample, 1926-41.

In the years preceding 1926 adequate information is available only for 1924 and

able amount of capacity per unit of output and therefore cannot be used as a direct measure of $(S/P)_t$. Accordingly, from 1932 to 1940, $(S/P)_t$ was approximated by interpolating linearly between the values of $(S_{t-1}/P_{t-3})^L$ in 1931 and 1939 and extrapolating to 1940. These adjustments, however, do not affect the basic logic of our approach.

³⁴ The value of this ratio is generally not known at the beginning of year t . Since the ratio changes very gradually over time, one can utilize for forecasting purposes, as a good first approximation, the actual ratio of the previous year.

1925. In the table below, actual values of investment (deflated) for these 2 years are compared with the values calculated by extrapolating our regression equations.

TABLE 1.—Actual and computed expenditure on plant and equipment, deflated, 1924 and 1925

[In millions of dollars]		
	1924	1925
Actual.....	426	397
Computed: Equation (10).....	447	400
Computed: Equation (25).....	437	416

It is apparent that the results of this test are quite favorable. For both equations the computed values are close to the actual experience both in terms of level and of year-to-year movements.

In attempting to carry out a similar test for years after 1941, several difficulties arise. For obvious reasons one cannot make use of the war years 1942-45. But even the years immediately following the war could not provide a satisfactory basis for a test, as there is reason to believe that, at least up to 1950, investment behavior was seriously disrupted by transitory conditions, reflecting the aftermath of the war and the effect of the Korean hostilities. There is, in particular, considerable evidence to suggest that throughout the above-mentioned years the electric power industry was unable to grow fast enough to bring capacity to desired levels, because of actual limitations on the supply of materials and equipment and probably also because of limitations on the rate at which firms can afford to grow. A meaningful extrapolation test can, therefore, be carried out at best beginning with 1951 and ending with 1955, the last year for which the required statistical information is presently available. Such a test is clearly a severe one since it involves extrapolating 10 to 15 years beyond the period underlying our equations.

An extrapolation over an interval of time as long as this raises serious questions particularly in connection with equation (10) because of the negative time trend appearing in it. From the previous analysis we have seen that this trend reflects in part a gradual increase in the efficiency with which capacity was being utilized during the period of observation. This trend appears to have considerably subsided if not altogether ceased in recent years, the major opportunities for more efficient utilization consistent with present technology having been largely tapped. The negative trend reflects also a gradual decline in the ratio of plant to equipment expenditures, occurring through most of the interwar period. Unfortunately, there exist no reliable estimates of the breakdown of total investment expenditures into plant and equipment for recent years, but there are indications that the declining trend in this ratio has actually been reversed in the course of the major expansion program of the postwar period.

Thus, there seems to be no ground for extrapolating the negative time trend of equation (10), at least for the 1950's. Just how far (if at all) the trend should be extrapolated beyond 1941 is an issue which cannot be precisely settled. It is worthy of note, however, that the answer to this question affects only the level of the "computed" series and not the direction of its yearly movements. Hence, even in the absence of a precise answer, we can still test how well equation (10) accounts for the year-to-year movement of investment in recent years. Accordingly, in table 2 below, two sets of computed values are presented for equation (10), obtained respectively by extrapolating, and not extrapolating, the time trend beyond the period of observation.

TABLE 2.—Actual and computed expenditures on plant and equipment, deflated, 1951-55

[In millions of dollars]					
	1951	1952	1953	1954	1955
Actual.....	464	551	579	555	514
Computed: Equation (10), time trend extrapolated.....	270	318	284	295	213
Computed: Equation (10), time trend not extrapolated.....	490	552	539	572	511
Computed: Equation (25).....	445	553	597	563	488

It is apparent that a mechanical extrapolation of the time trend yields rather poor results: the computed values consistently underestimate investment with the discrepancy showing a systematic increase from year to year. When, however, the time trend is not extrapolated, the results are considerably improved. As noted above, the actual level around which the computed values fluctuate is not too important in this connection. However, the fact that, except for the minor dip in 1953, the year-to-year movements correspond fairly closely to those of actual investment is of some significance. It suggests that, while the negative time trend is no longer operating, the basic mechanism embodied in hypothesis (10) still provides a reasonably good explanation of the forces making for fluctuations in investment.

This conclusion is supported by the results of the extrapolation test for equation (25), given in the last row of the table. For the purpose of this test, in estimating the desired ratio of capacity to output through the lowest previous ratio $(S_{t-1}/P_{t-3})^L$, years preceding 1949 were disregarded. This procedure was dictated by the consideration that some of the extremely low ratios observed in the war years and the early postwar period reflected the inability of the industry to expand capacity as rapidly as demand was growing;³⁵ their use therefore, would seriously underestimate the desired ratio. As a matter of fact, since 1949 the ratio has never fallen again to the low levels prevailing in some of the postwar years.³⁶ Another difficulty that had to be faced in extrapolating (25) is the absence of reliable estimates on the breakdown of total investment outlays into plant and equipment, to which reference has been made earlier. Lacking precise information, the extrapolation had to be based on an admitted crude estimate of the average value of the ratio in the relevant

³⁵ The inability of the industry to expand its capacity is indicated, for instance, by the sharp decline in the margin of reserve capacity in the wartime and early postwar years. Only by about 1953 did the margin rise again to levels considered adequate to insure an uninterrupted flow of electrical energy.

³⁶ It is possible that the ratio remained somewhat abnormally low even after 1949—possibly as late as 1953. Beyond 1953 this phenomenon is unlikely to have been significant, as suggested by various considerations such as the abatement of investment outlays in 1954 and 1955. To the extent that $(S_{t-1}/P_{t-3})^L$ underestimates the desired ratio of capacity to output, the figures shown in the last row of the table would be unduly low. However, the error from this source cannot be substantial, since, between 1949 and 1955 the ratio (S_t/P_{t-2}) fluctuated within very narrow limits. Measured in kilowatts per 1,000-kilowatt hours of output, the ratio has a lowest value of 0.236 in 1953 as against a peak value of 0.246 in 1954, a fluctuation of only about 4 percent. See also footnote 37.

years, a fact that reduces somewhat the conclusiveness of our test.³⁷ Even if one keeps this qualification in mind, the results of the extrapolation test appear rather favorable. Considering the standard error of estimate of equation (25), there seems to be no ground for rejecting the hypothesis that the equation fits the recent postwar experience at least as well as it fitted the period of observation.

SUMMARY AND CONCLUSIONS

In this study we have developed and tested a model which appears to provide an acceptable explanation of investment decisions in the electric power industry. The main hypothesis of our model is that investment outlays are primarily determined by the relation between the demand for electricity and the amount of capacity required to satisfy this demand economically. This hypothesis, needless to say, is nothing else but the familiar acceleration principle. If properly understood, this "principle" is, of course, a broad concept which cannot be applied mechanically, as has sometimes been done in the past. In the present study the acceleration principle was adapted to our specific needs by taking into account a number of characteristics peculiar to the industry studied.

Of primary relevance among these characteristics are (a) the long planning and gestation period for investment; (b) the presence and quantitative importance of indivisibilities in fixed assets; (c) the rapid growth of the demand for electrical energy; (d) the impossibility of storing the product; and last but not least (e) the influence of institutional factors resulting from public regulation of the industry.

The first of these characteristics gives rise to a relatively long lag between capital spending and its principal determinants in our model and causes year-to-year fluctuations in investment to be influenced not only by the rate of change of demand (as in the classical interpretation of the acceleration principle) but also by the change in the rate of change. The next three characteristics, in conjunction with the first, make it advantageous for utilities to plan their in-

³⁷ After extensive, though not very conclusive, consultations with experts and industry sources, the ratio of plant to equipment expenditure was estimated at 100 percent. This figure is roughly the same as the average value of the ratio in the period 1926-29 (namely 98 percent) in the course of which the industry underwent an expansion of dimension comparable to the postwar one. It is possible that the chosen figure is somewhat on the high side, which would tend to impart an upward bias to the computed values shown in the last row of table 2. This bias is, however, unlikely to be too serious especially since it is in the direction opposite to the possible bias arising from the factors discussed in footnote 35. As a check, the figures of the last row of table 2 were recomputed, assuming for the ratio of plant to equipment expenditure a value of 90 percent, and for the desired ratio of capacity to output a value of 0.245 which is the actual value of S_t/P_{t-2} in 1955. The following results are obtained for the years 1951 to 1955 respectively: 424, 535, 590, 609, 539. These figures do not agree with actual investment quite as closely as those obtained in table 2; the average absolute error is somewhat higher (25 instead of 15) and the 1953 turning point is missed by 1 year. However, the differences are not too great, and the fit is actually improved in 2 years out of 5. Furthermore, the average absolute error of 25 still compares favorably with a standard error of estimate of 40.

vestments so as to provide a normal margin of spare capacity over and above the capacity required to meet immediate needs; this margin in turn makes it possible to take care of the growth of demand which may, and normally does, occur during the long gestation period.

Over the years studied, we have also found a marked downward trend in the relation between investments and changes in demand. This trend appears to reflect primarily a gradually more effective utilization of capacity, technological progress (including, probably, improved marketing techniques), and a relative decrease in plant as compared with equipment expenditures. The latter development is likely to be an important feature of capital-intensive industries as they reach a more mature stage in their growth. In the electric power industry, however, this phenomenon reflected also the overexpansion of plant in the 1920's. Two alternative formulations of our basic hypothesis have been advanced to describe this downward trend. In the first, embodied in equation (10), we have introduced the time variable to represent this trend. The equation was found to give very satisfactory results in the period of observation and immediately neighboring years. It was also found to account rather well for year-to-year variations in investment in the long-run extrapolations when a proper adjustment is made for changes in the behavior of the factors underlying the time trend. In the second formulation—equation (25)—we have attempted to measure directly the factors for which the time variable was supposed to be a proxy. In spite of the crude nature of our measures the results were again quite satisfactory for the period of observation; furthermore, the model apparently stood the test of extrapolation to the postwar years well enough to suggest that its explanatory value is not merely historical.

The acceleration principle is also somewhat modified by the influence of profits—probably as a source of funds and a measure of the short-run business outlook. This influence is, however, not very pronounced; it manifests itself not in the planning but in the realization phase of the investment process, tending to stimulate capital expenditures in prosperity and retard them in depression. One may conjecture that the far greater role played by the accelerator mechanism as against profits in explaining investment behavior in the electric utilities industry reflects partly the institutional conditions under which firms operate—their obligation to meet the demand in the geographical regions in which they have a franchise and the customary support of their capitalization by the regulatory bodies whenever "legitimate" capital outlays are made. It would, therefore, be hazardous to extend our findings to industries having characteristics similar to those of the electric power industry but which are not in a sheltered position.

On the basis of our statistical analysis, we cannot reach a definite conclusion concerning the influence of interest rates on investment; however, the evidence strongly suggests that even in this industry, where fixed assets are of great longevity, the cost of borrowed funds was not an important factor. In general, cost considerations appeared to play a minor role in the decisions of the utilities—a finding which may again reflect the way the "fair return on the fair value" principle is applied in the industry.

APPENDIX—SYMBOLS AND SOURCES OF DATA

I = gross plant and equipment expenditures by privately owned electric utilities measured in millions of current dollars. George Terborgh, "Estimated Expenditures for New Durable Goods, 1919–38," Federal Reserve Bulletin, September 1939, 732, for 1924–36. J. B. Epstein, "Electric Power Output and

Investment," Survey of Current Business, May 1949, 23, for 1937–41. Statistical Bulletin, 1955, Edison Electric Institute, 55, for 1951–55.

I' = gross plant expenditures by privately owned electric utilities, measured in millions of current dollars. George Terborgh, "Estimated Expenditures for New Durable Goods, 1919–38," Federal Reserve Bulletin, September 1939, 732, for 1926–36. J. B. Epstein, "Electric Power Output and Investment," Survey of Current Business, May 1949, 23, for 1937–41. For 1939, 1940, 1941, the estimates are obtained by splitting Epstein's aggregates into plant and equipment, on the basis of ratios of plant-to-equipment expenditures given by F. Dirks in "Durable Goods Expenditures in 1941," Federal Reserve Bulletin, April 1942, 317.

I'' = gross equipment expenditures by privately owned electric utilities, measured in millions of current dollars. George Terborgh, "Estimated Expenditures for New Durable Goods, 1919–38," Federal Reserve Bulletin, September 1939, 733, for 1926–36. J. B. Epstein, "Electric Power Output and Investment," Survey of Current Business, May 1949, 23, for 1937–41. For 1939, 1940, 1941, the estimates are obtained by splitting Epstein's aggregates into plant and equipment, on the basis of ratios of plant-to-equipment expenditures given by F. Dirks, in "Durable Goods Expenditures in 1941," Federal Reserve Bulletin, April 1942, 317.

A = total electric light and power construction and equipment cost index, 1911:1.00, Engineering News—Record, April 22, 1943, 100, for 1924–41. Statistical Bulletin, 1955, Edison Electric Institute, 69, for 1951–55. These data are given by region. The separate indexes are combined into a U.S. index by forming a weighted sum of the regional estimates with the weights proportional to regional population estimates from the nearest census. The index is published for January and July of each year. An annual index is computed from a weighted sum of beginning of year, middle of year, and end of year figures. The weights are 0.25, 0.50, and 0.25 respectively.

B = electric light and powerplant construction cost index, 1911:1.00. Source: *ibid.*

C = electric light and power equipment cost index, 1911:1.00. Source: *ibid.*

II' = electric utility companies' net income and interest payments, in millions of dollars. Statistical Bulletin, 1942, Edison Electric Institute, 39. Statistical Bulletin, 1955, Edison Electric Institute, 57, for 1951–55.

II = electric utility companies' net income and depreciation, in millions of dollars. Same source as II' , for 1926–41. Statistical Bulletin, 1955, Edison Electric Institute, 57, for 1951–55.

r = yield averages on newly issued light, power, gas bonds. Moody's Utilities, 1947, p. a5.

P = output of electrical energy by private companies, in millions of kilowatt-hours. Statistical Bulletin, 1942, Edison Electric Institute, 10, for 1924–41. Statistical Bulletin, 1955, Edison Electric Institute, 14, for 1941–55.

S = generating capacity of electric utility companies, in thousands of kilowatts. Statistical Bulletin, 1942, Edison Electric Institute, 5, for 1924–41. Statistical Bulletin, 1955, Edison Electric Institute, 6, for 1951–55.

W = average hourly earnings in the electric power industry, in cents. Economic Almanac, 1941–42, 306.

Mr. PROXMIRE. In addition, a very careful study of the telephone industry, which is another vital part of the utility segment of the industry that is included in the bill, was made by an economist named Paul Clark in 1953 in a very fine series of studies of the American economy by Vasily Leontieff. The study by

Mr. Clark also concludes that in the telephone industry the investment credit incentive would have very little effect.

Mr. Clark concluded that there are particular reasons why investment in the telephone industry is primarily dependent on demand not cost. If this is true the investment credit could not increase investment because the investment credit can only work through reducing tax cost. The reasons given by Clark for telephone investment depending on demand, not cost, are as follows:

First, its productive process is heavily capital-intensive, with little scope for substitution of other inputs, and its product cannot be produced for inventory. This means that investment decisions are dominated by essentially rigid technological relationships. Second, the demand for telephone service has risen steadily and rapidly throughout the history of the industry, so that investment designed to expand capacity has bulked large in the investment program, technological improvements have been introduced primarily as alternative techniques for expansion, and it has been economical to build ahead of demand. Third, the telephone industry is essentially a monopoly, and is subject to public utility regulation. Its investment is little affected by the reactions of oligopolistic rivals, and must be adequate to meet demand at commission-determined prices.

These favorable characteristics, however, are clearly not limited to the telephone industry. The other public utilities, which together provide a significant fraction of total investment in our economy, are similar in most of these respects.

I ask unanimous consent that the study by Mr. Clark on investment in the telephone industry be printed at this point in the RECORD.

There being no objection, the article was ordered to be printed in the RECORD, as follows:

CHAPTER 7—THE TELEPHONE INDUSTRY: A STUDY IN PRIVATE INVESTMENT

(By Paul G. Clark)

I. INTRODUCTION

The study presented here is an attempt to test a simple theory of private investment, called the capital-requirements theory, against the investment practice in the telephone industry. The theory has been derived in a form suitable for integrating investment and disinvestment in capital equipment into interindustry input-output analysis. Therefore, although the study also has more general implications, in the context of this volume it is significant primarily as an empirical investigation of the validity of a theory suitable for this purpose.

The course of discussion will be as follows. In section II the capital requirements theory is developed as a modification of the pure acceleration principle. In section III the procedures currently followed in reaching investment decisions in the Bell System are outlined, and the theory is tested qualitatively against these procedures. In section IV the coefficients of the capital-requirements theory are calculated statistically from data for the telephone industry, and the theory is tested quantitatively by evaluating the reasonableness of the statistical results. In section V certain conclusions are drawn as to the empirical validity of the capital-requirements theory, and as to its usefulness in input-output analysis.

II. THE CAPITAL-REQUIREMENTS THEORY OF PRIVATE INVESTMENT

A. The pure acceleration principle

A distinctive strand in the theoretical analysis of private investment is the accelera-

tion principle. The essential assumption of the principle in its pure form is that the firm must maintain for technological reasons a fixed ratio between its output and its stock of capital equipment. It follows from this assumption that the firm must undertake changes in its stock of capital equipment, i.e., must undertake net investment, in accordance with changes in its output. The principle in this pure form can be stated algebraically as follows:

$$\begin{aligned}(7, 1) \\ K_t &= kO_t \\ (7, 2) \\ \Delta K_t &= k\Delta O_t\end{aligned}$$

in which

O_t = the firm's output in time period t ,
 K_t = the firm's stock of capital equipment at the end of the period,

ΔO_t = the difference between the firm's output in t and its output in $t-1$,

ΔK_t = the difference between the firm's stock of capital equipment at the end of t and its stock at the end of $t-1$, and

k = the fixed technological ratio which the firm is assumed to maintain between its output and its stock of capital equipment.

Both theoretical considerations and empirical tests, however, suggest that the pure acceleration principle is subject to several important qualifications as a realistic theory of private investment.

First, the pure acceleration principle implies that the firm is able to adjust its stock of capital equipment instantaneously to increases in demand for its output, but in practice a construction period of some length must usually intervene between the decision to purchase additional capital equipment and its actual installation. The firm might react to the time required for construction in either of two ways: by postponing investment decisions until additional demand actually materializes, thus postponing its ability adequately to meet the demand until after the construction period; or by making investment decisions on the basis of its expectations of what the demand will be after the construction period, thus beginning the construction process in advance of expected changes in demand. The latter reaction is assumed in the capital requirements theory.

Second, the pure acceleration principle implies that the firm adjusts the capacity of its stock of capital equipment precisely to its output, but in practice a margin of spare capacity is commonly provided. One reason for maintaining some spare capacity is that demand is expected to fluctuate, and that the firm wishes to be able to handle temporary increases in demand without undue delay. This motive is particularly strong in cases in which the essential assumption of the pure acceleration principle is most realistic—cases in which the technological relation between capacity and capital equipment is quite rigid. Another reason for maintaining some spare capacity is that demand is expected to follow an upward secular trend, and that there are economies in making a small number of large installations of capital equipment rather than a large number of small installations. The significance of the margin of spare capacity depends, of course, on whether it is regularly varied, or is kept at some normal level. The latter practice is assumed in the capital requirements theory, and means that the ratio between the firm's output and its stock of capital equipment depends on the firm's decision to maintain a normal margin of spare capacity, as well as on the technological relation between capacity and capital equipment.

Third, the pure acceleration principle is perfectly symmetrical with respect to increases and decreases in output, but actually the firm frequently is unable to react in the same way to decreases in demand for its out-

put as to increases. If demand rises, the firm can usually expand its stock of capital equipment as rapidly as the fixed ratio to output requires, although at times it may be restricted by supply shortages. If demand falls, on the other hand, the firm frequently cannot contract its stock of capital equipment rapidly enough to maintain a fixed ratio to output, since it can contract only as fast as retirement because of wear and tear and obsolescence permits. The firm might, of course, simply junk the equipment, or sell it at distress prices, but this acceptance of capital loss is usually not worth while, since the cost of retaining idle capital equipment is usually small relative to possible future returns if and when it can be used again. If demand falls, therefore, the firm frequently cannot make its net investment as negative as the pure acceleration principle asserts, but instead accumulates excess capacity. Moreover, if demand then rises, the firm need not make any positive net investment until this excess capacity has again been brought into use. The pure acceleration principle should be modified to take account of this asymmetry in the firm's reaction to increases and decreases in demand.

Fourth and finally, the assumed ratio between the firm's output and its stock of capital equipment is changed from time to time by technological developments. This qualification does not destroy the usefulness of the principle, provided that the technological changes are discontinuous, and that the ratio remains stable from one technological change to the next. This qualification does suggest two modifications in the form of the principle, however, (1) since a technological change typically leads the firm to modify its purchases of new capital equipment, but not immediately to scrap and replace all its obsolescent plant, the principle should be stated in terms of ratios between changes in the firm's output and changes in its stocks of capital equipment, rather than in terms of ratios between the firm's total output and its total stocks; (2) since a technological change directly affects a particular type of capital equipment, the principle should be stated in terms of a set of ratios, one for each of the various types of capital equipment.

B. The capital requirements theory

The acceleration principle in its pure form is thus not sufficiently realistic to warrant confidence. If it is modified to make allowance for the four qualifications just discussed, however, it can provide the basis for a more realistic, yet still simple, theory of private investment—the capital requirements theory.

The first modification of the pure acceleration principle introduces the firm's expectations of future demand. The firm is conceived to adjust its stock of capital equipment to the demand which it expects to prevail after the construction period. Algebraically, equation (7, 1) becomes:

$$\begin{aligned}(7, 3) \\ K_{t+1} &= kO^e_{t+1}\end{aligned}$$

and equation (7, 2) becomes:

$$\begin{aligned}(7, 4) \\ \Delta K_{t+1} &= kO^e_{t+1} - K_t\end{aligned}$$

in which

O^e_{t+1} = the expected output in the period $t+1$, the length of the period is the time required for construction.

Once the firm's demand expectations have been introduced into the theory, however, it is necessary to find a relation between these subjective expectations and some measurable objective variables. Here a variant of Metzler's expectations coefficient may serve as a simple hypothesis. The expectations coefficient is defined as the ratio between the expected proportional change in output from the current period to the next period, and the actual proportional change from the last

period to the current period. Thus the expected output in the next period equals the output in the current period, plus a positive or negative increment which depends upon the expectations coefficient and the actual proportional change from the last period to the current period. Algebraically,

$$\begin{aligned}(7, 5) \\ \epsilon &= O^e_{t+1} - O_t / O_t / O_t - O_{t-1} / O_{t-1} \\ (7, 6) \\ O^e_{t+1} &= O_t [1 + \epsilon(O_t - O_{t-1} / O_{t-1})]\end{aligned}$$

in which

ϵ = the expectations coefficient.

Note that if the coefficient is 0, future output is expected to be the same as current output; if the coefficient is +1, the current proportional trend is expected to continue; if the coefficient is -1, the current proportional trend is expected to reverse itself.

The question may arise how the effect of uncertainty of the future may be recognized in this treatment of expectations. On the assumption that a firm becomes less willing to undertake investment if the uncertainty surrounding future yields increases, the effect of greater uncertainty can be represented by a smaller expectations coefficient for future output, so that a given increase in demand from the last period to the current period leads the firm to undertake less net investment than it would if the future were more certain.

The second modification of the pure acceleration principle provides for a normal margin of spare capacity. One fixed ratio, or capital coefficient, depending on technological considerations, is assumed to exist between the stock of capital equipment and its capacity. Another fixed ratio, or spare-capacity coefficient, depending on the firm's decision to maintain a normal margin of spare capacity, is assumed to exist between the capacity of the capital equipment and the output which the firm expects to produce. Algebraically, equation (7, 3) is modified to read:

$$\begin{aligned}(7, 7) \\ K_{t+1} &= \beta C_{t+1} \\ (7, 8)\end{aligned}$$

and

$$C_{t+1} = \gamma O^e_{t+1}, \quad \gamma > 1$$

in which

β = the capital coefficient,

γ = the spare-capacity coefficient, and

C_{t+1} = the capacity of the stock of capital equipment, defined in the same units as output.

Equation (7, 4) is modified to read

$$\begin{aligned}(7, 9) \\ \Delta K_{t+1} &= \beta \gamma O^e_{t+1} - K_t = \beta \gamma (O^e_{t+1} - 1/\gamma C_t)\end{aligned}$$

The third modification of the pure acceleration principle recognizes the asymmetry between the firm's reaction to a decrease in expected output and its reaction to an increase. This is accomplished by assuming that the firm's net investment cannot be more negative than its retirement of capital equipment because of wear and tear and obsolescence, and that such retirement is technologically determined as a fixed fraction of its stock of capital equipment. In the algebraic statement equation (7, 9) is subjected to the limitation that

$$\begin{aligned}(7, 10) \\ \Delta K_{t+1} &\geq -R_{t+1}\end{aligned}$$

in which

$-R_{t+1}$ = the firm's retirement, conceived as a negative flow.

It should be noted that if this limitation becomes operative in any period, the firm will be left with a capacity relative to its expected output greater than that indicated by the spare-capacity coefficient. If expected output subsequently rises, positive net investment will be undertaken only to the extent that expected output exceeds the nor-

mal fraction of capacity indicated by the spare capacity coefficient. The firm's retirement in turn is determined by

$$(7, 11)$$

$$-R_{t+1} = -\rho K_t$$

in which

$-\rho$ = the retirement coefficient.

This assumption regarding retirement is a simple one, subject to a number of qualifications in practice. Retirement due to wear and tear is determined most rigidly for capital equipment with a well-defined service life. Even with a well-defined service life, however, retirement depends on the age distribution of the capital equipment, and on the degree of past utilization of its capacity, as well as on the current stock. On the other hand, the more durable the capital equipment the more variable its service life, until some types, given proper maintenance and spare-parts replacement, are essentially immortal. Finally, retirement due to obsolescence depends in part on the firm's policy regarding the rate of introduction of technological improvements. Thus a complete theory would have to introduce other variables affecting retirement in addition to the stock of capital equipment. Nonetheless in the capital-requirements theory a fixed retirement coefficient has been assumed, partly because retirement enters the theory primarily as a limitation on negative net investment, and partly because it seems worth while to test the simple assumption before developing a more complex one.

The fourth modification of the pure acceleration principle, suggested by the necessity of admitting technological change into the theory, defines the capital and spare-capacity coefficients as incremental coefficients, relating changes in expected output, capacity, and capital stock, rather than as average coefficients, relating total expected output, capacity, and capital stock. In other words, the capital-requirements theory is stated in terms of equation (7, 9), rather than in terms of equations (7, 7) and (7, 8). When a technological change occurs, the firm introduces it by modifying its purchases of new capital equipment of the various types; its net investment as determined by equation (7, 9) is modified by abrupt changes in β and γ . The firm does not immediately scrap and replace all its obsolescent equipment, however; its total stock of equipment and total capacity are not determined immediately by equations (7, 7) and (7, 8) using the changed β and γ , but only gradually as all its obsolescent equipment is replaced.

The necessity of recognizing technological change suggests another modification, which defines the capital, spare-capacity, and retirement coefficients so that they apply to particular types of capital equipment, rather than to all types lumped together. Algebraically, all the coefficients and stocks (but not expected output) in equations (7, 9), (7, 10), and (7, 11) are rewritten to read:

$$(7, 12)$$

$$\Delta K^a_{t+1} = \beta^a \gamma^a (O^e_{t+1} - 1/\gamma^a C^a_t), \quad \Delta K^a_{t+1} \geq -R^a_{t+1}$$

$$(7, 13)$$

$$-R^a_{t+1} = -\rho^a K^a_t$$

in which the superscript

a refers to a particular type of capital equipment, and similar superscripts are used for other types.

Here a definitional problem is raised. If the types are defined narrowly, as physically identical units, then a technological change must be conceived as the introduction of an entirely new set of coefficients. If the types are defined broadly, however, as physically different units performing a similar func-

tion (which requires that they be measured in terms of value), then a technological change can be conceived as the alteration of the old set of coefficients. This broader definition is adopted here.

The capital-requirements theory as now formulated may be summarized in the following basic hypotheses, which are to be tested against actual practice in the telephone industry: (1) The firm's demand estimates depend via a fixed expectations coefficient upon the recent trend of its output. (2) The firm's net investment depends via a fixed capital coefficient and a fixed spare-capacity coefficient upon these demand estimates. (3) The firm's retirement depends via a fixed retirement coefficient upon its present stock of capital equipment. The second and third hypotheses are conceived to apply to each particular type of capital equipment. In the algebraic statement, these basic hypotheses are

$$(7, 6)$$

$$O^e_{t+1} = O_t [1 + \epsilon (O_t - O_{t-1}/O_{t-1})]$$

$$(7, 12)$$

$$\Delta K^a_{t+1} = \beta^a \gamma^a (O^e_{t+1} - 1/\gamma^a C^a_t), \quad \Delta K^a_{t+1} \geq -R^a_{t+1}$$

$$(7, 13)$$

$$-R^a_{t+1} = -\rho^a K^a_t$$

C. The relation of the capital-requirements theory to a more general theory

The capital-requirements theory, although more complex than the pure acceleration principle, is still quite simple. What then is the relation between this simple theory and a more general theory, based on the profit-maximizing equilibrium of the firm? Without going into detailed analysis, the question can be answered generally by indicating the principal alternative assumptions which are made in the two theories.

A more general theory usually assumes that in all markets the firm can sell, buy, and borrow either unlimited quantities at going prices, or varying quantities at varying prices as indicated by sloping supply and demand curves. On the other hand, the capital-requirements theory assumes that in the market for output the firm can sell only a limited quantity at the going price, and that the price is accepted as a stable parameter of its decisions. In other words, a sloping demand curve exists, but because of conventional price-setting, it can be represented simply by the quantity demanded. The theory assumes as before that in the markets for capital equipment, for other inputs, and for capital funds the firm can buy and borrow unlimited quantities at going prices, or at rising prices as indicated by sloping supply curves; and in addition that these prices or supply curves are so related that it is profitable to purchase whatever amount of capital equipment is required to produce the output which the firm can sell.

The production function assumed in the more general theory usually contains continuous decreasing marginal rates of substitution among inputs for given outputs, and among outputs for given inputs; and continuous decreasing marginal rates of transformation between input combinations and output combinations, i.e., decreasing returns to scale. In the capital-requirements theory, however, the production function contains fixed coefficients relating the firm's output to the stocks of various types of capital equipment in use, and hence relating its capacity to its total existing stocks. In addition, the firm as a matter of policy is supposed to maintain normal margins of spare capacity as fixed fractions of total capacity in the various types of equipment.

Although both theories adopt the hypothesis that the firm seeks to maximize its profit, the consequence of profit maximiza-

tion differs. In a more general theory, profit maximization consists in purchasing additional units of capital equipment up to the point at which the expected profit from the marginal unit falls to zero. In the capital-requirements theory, on the other hand, profit maximization consists in purchasing additional units of capital equipment up to the point at which the sum of the additional outputs which they can produce equals the expected total increase in output in the next period. The expected profit from the marginal unit remains positive, but if the firm purchased still more units, their output could not be sold in the next period.

The particular assumptions of the capital-requirements theory also mean that changes in the rate of interest and in the prices of output, of capital equipment, and of other inputs, have no effect upon the firm's investment. There can be no substitution effect so long as the production function contains fixed coefficients relating the firm's output to the stocks of various types of capital equipment in use, and the firm maintains normal margins of spare capacity. There can be no expansion effect so long as the firm's output is limited by a sloping demand curve and a conventional price; a change in any of these prices causes a change in profit, but not in investment.

It may be noted at this point that in two respects the capital-requirements theory is actually more complete than the more general theory as often formulated. It attempts to explain both the formation of expectations regarding future demand and the determination of retirement. The simpler capital-requirements theory also has certain advantages for empirical investigations. To begin with, it suggests a smaller number of relevant economic factors. In questioning businessmen about their investment decisions, a smaller number of variables reduces the problem of multicollinearity. The capital-requirements theory also specifies linear relationships among its variables, which eases the statistical analysis. Most important of all, a number of existing empirical investigations of private investment have indicated that the relevant economic factors suggested by the capital-requirements theory are of major importance, while the additional factors suggested by a more general theory can be readily neglected.

III. A QUALITATIVE ANALYSIS OF TELEPHONE INVESTMENT

A. The method

The capital-requirements theory is tested in the course of this study of telephone investment in two different ways. In this section it is tested qualitatively by examining the procedures followed in reaching investment decisions in the Bell System, and judging whether these procedures can be approximated by the fixed coefficients of the theory. In the next section a quantitative test is made by calculating coefficients from statistical data for the entire industry, and evaluating the reasonableness of the computed coefficients.

The importance of the qualitative analysis presented in this section should be emphasized. Not only is it a direct observation of investment procedures which can be compared in its own right with the procedures envisioned in the capital-requirements theory, but also it provides a basis for the subsequent quantitative analysis. The procedural information serves as a guide for various details of the statistical calculations, and the chronology of technological developments in the industry serves as a standard for evaluating the statistical results.

The information for this qualitative analysis was obtained primarily in interviews with members of the staff of the American Tele-

phone & Telegraph Co.¹ An attempt was made to avoid some of the common shortcomings of the questioning technique by relying upon interviews rather than questionnaires, so that ambiguous questions and answers could be reexplored; and by placing the emphasis upon procedures rather than motives, which is feasible in a large institutionalized organization. It may be, however, that the resulting qualitative description lays insufficient stress upon the judgment used in weighing less tangible considerations than those discussed here. The final statement, of course, is my own responsibility.

B. Demand estimates in the Bell System

The first stage of the investment process in the Bell System consists in estimating future demand. These demand estimates are made by the commercial departments of the associated operating companies, and by corresponding personnel in the American company's long-lines operating department, with procedural assistance from the staff of the American company.

The basic demand estimates are stated in terms of three interrelated variables—the number of lines, the number of main telephones, and the number of total telephones. These three variables are in ascending order of size, the number of main telephones being larger than the number of lines because it includes main telephones on multiparty lines, and the number of total telephones being larger than the number of main telephones because it includes extension telephones. Therefore once one of the variables is estimated independently, the others can be calculated from it by the use of appropriate ratios. The common practice is to take the number of main telephones as the independent estimate. The ratios used in calculating the other two variables are obtained largely from past records, but modified by expected future changes. Thus they vary somewhat from year to year, and also between exchanges. From these basic estimates of lines, main telephones, and total telephones, more detailed estimates, broken down among all the various classes of telephone service, are derived by the use of still other ratios. In smalltown exchanges, for example, the number of business telephones is often calculated in this way from the estimated number of residence telephones. In metropolitan areas, on the other hand, the number of business telephones is estimated directly.

The complete demand estimates are of two types, depending upon the use to which they are put. The first type, the general planning estimates, are usually made for a period of 3 years in advance, although the period may be shortened or lengthened according to the confidence which the analysts place in the expected future trends. They are

made annually, and reviewed and modified quarterly, or whenever a more detailed special-project estimate has been made. Their main purpose is to serve as a rough guide in determining when an expansion of capacity in a particular exchange will be required. The second type, the special-project estimates, are made whenever an expansion of capacity in a particular exchange is planned in detail. They are more elaborate than the general planning estimates, and are fitted to the particular projects under consideration. Their chief purpose is to help determine, in conjunction with the policy of building ahead of demand, how much capital equipment is required; and hence the number of years for which demand is forecast depends upon the period of building in advance which is applied to that particular type of capital equipment.

The basic technique applied in making all of these demand estimates is a field survey of each individual exchange. The commercial departments of the associated companies have staffs of development engineers, each of whom is responsible for making the periodic demand estimates for certain exchanges. The development engineer's analysis is usually based on a sample of typical streets or blocks, and involves the consideration of two factors. He must forecast the number of new families. This part of his analysis is usually based on existing or prospective building programs. He must also forecast the increase in development, or percentage of families with telephones. This part of his analysis is usually based on prospective personal incomes of individuals and prospective business conditions, plus such less tangible considerations as changes in telephone habits, e.g., changes due to servicemen's wartime experience with long-distance calls.

Demand estimates formed in this way obviously contain large subjective elements. Their reliability depends on the reliability of the development engineer's judgment regarding future building programs, personal incomes, and business conditions; and also on the reliability of his judgment upon the relations which exist between these factors and the demand for telephone service. The advisory staff of the American company recognize this fact, but feel that subjective methods of this sort are the most dependable methods available. Therefore, although they suggest that the development engineer make his assumptions and his line of reasoning explicit, so that his estimate can be modified if either is later found to be in error, they encourage him to rely primarily upon his own judgment, using statistical trends and correlations as only one element to be considered. Rough consistency of the assumptions and reasoning applied in the various exchanges is obtained in the course of consultations among the development engineers. There is also some evidence that a general feeling of optimism regarding future expansion of demand for telephone service has prevailed, which probably has affected these subjective estimates.² Such optimism is of course natural in view of the steady increase in number of telephones actually experienced.

Although the basic technique used in making demand estimates is the field survey, statistical methods are used to supplement this technique. Statistical projections for the entire area of an associated company are frequently used as a check on the totals emerging from forecasts in the individual exchanges. Economic statisticians on the

staff of the American company, besides providing various data, also periodically make general studies of business conditions, and general statistical projections for the entire Bell System. These are circulated and discussed with personnel of the associated companies.

Moreover, a technique based upon trend extrapolation was used by the long-lines department in its demand estimates made in the fall of 1930. The American company stated in reply to criticism of these estimates³ that five factors had been considered in making them: (1) Long-lines messages had had an average annual rate of growth of 13.5 percent in the period 1915–29; (2) They had had an annual rate of growth of 18 percent in 1928 and 1929; (3) In the first half of 1930 they had been 6.5 percent above the first half of 1929, and in the last half of 1930 they had been only slightly below the last half of 1929; (4) In the 1921 depression they had merely failed to increase over 1920, and in 1922 they had increased 17 percent over 1921; (5) A majority of economists and business forecasters had predicted recovery in the first half of 1931, which would have made the 1929 depression similar to the 1921 depression. The company presented the data from which these considerations were derived in the form of a semilogarithmic chart, upon which were plotted index numbers on a 1910 base of long-lines toll traffic, local stations, local traffic, national production, and national population, all compared to exponential reference trends of 1 percent up to 10 percent. The company also stated that the pattern of the past had apparently re-established itself after the depression, for long-lines messages had increased 20 percent in 1936 over 1935, and 29 percent in 1937 (based on 7 months' experience) over 1936.

In summary, demand estimates in the Bell System are based primarily upon field studies in each individual exchange, i.e., upon subjective methods, supplemented and checked by statistical calculations. Representing the formation of these estimates by a simple device like the expectations coefficient, as in the capital-requirements theory, is only an approximation. Nonetheless, a natural tendency for subjective forecasts to be influenced by current trends, plus the use of supplementary statistical analysis relying explicitly upon trend extrapolation, suggest that the expectations coefficient is a useful approximation. To this extent the first basic hypothesis of the capital requirements theory—that demand estimates depend via a fixed expectations coefficient upon the recent trend of output—is supported by the Bell System procedures.

C. Determination of required capital equipment in the Bell System

The second stage of the investment process in the Bell System consists in determining the additional amounts of capital equipment required to handle the estimated demand. These calculations are handled by the engineering departments of the associated companies and corresponding personnel in the long-lines department, again with procedural assistance from the staff of the American company.

One feature of the engineering is that a new installation of capital equipment must be decided upon a certain period of time before it is needed in service, because of the time required to engineer, manufacture, and install new capital equipment. The construc-

¹ Published materials which relate to investment procedures in the Bell System, and which were also consulted, include: Federal Communications Commission, "Investigation of the Telephone Industry in the United States," H. Doc. No. 340, 76th Cong., 1st sess., Government Printing Office, Washington, 1939. Ibid., "Special Investigation Docket," No. 1, 1936, exhibit No. 135, "Long-Lines Department, Financial and Operating Summary"; exhibit No. 580, "Long-Lines Department, Property Not Used and Useful"; exhibit No. 2096-G, "Effect of Control Upon Telephone Service and Rates." American Telephone & Telegraph Co., "Comments on the Telephone Investigation," 1937, No. 31, "Comments on Exhibit No. 135"; No. 32, "Comments on Exhibit No. 580," Ibid., "Annual Reports," 1913–48.

² American Telephone & Telegraph Co., "Annual Reports," 1919, p. 43; 1925, p. 8; 1935, pp. 10–11.

³ Federal Communications Commission, "Docket," Exhibit No. 580, "Long-Lines Department, Property Not Used and Useful," pp. 11–14. American Telephone & Telegraph Co., "Comments," No. 32, "Comments on Exhibit No. 580," pp. 16–24.

tion period varies according to the size of the job, but it is now roughly a year for automatic switchboards, 6 months for manual switchboards, 9 months for repeaters (amplifiers, which restore the strength of the signal over long lines), 3 months for new cable on an existing pole line, and 2 years for a major new pole line requiring a new right-of-way. The necessity of allowing for these construction periods is in keeping with the capital-requirements theory.

Another, and quite important, feature of the engineering stage is the practice of building ahead of demand—of providing in each new installation of capital equipment a certain margin of spare capacity. This is accomplished by taking the demand estimate for several years in the future as the measure of the capacity which is to be provided in the new installation. The appropriate period of building ahead of demand varies from one type of capital equipment to another, the criterion in each case being the relative cost of a single installation with large capacity and of a succession of installations with small capacity. Detailed studies are made in applying this criterion, and for each type of equipment a period of building in advance is selected which gives the lowest present value of the expected costs, discounted at a rate of 7 percent.

The periods currently in use are approximately as follows: In the case of open-wire pole lines, poles are usually erected of sufficient size to carry the expected number of crossarms and wires 20 to 25 years in the future, and then the crossarms and wires are added to keep up with current demand. Underground conduit is also normally placed to provide capacity adequate for 20 to 25 years. In long toll cables, a sufficient number of conductors is usually provided to handle the expected traffic 15 to 20 years in the future, and then the carrier systems which are needed to convert these conductors into usable circuits are provided only 1 to 2 years in advance. Central office equipment is normally installed with a capacity adequate for 1 to 3 years; central office buildings are normally erected with sufficient floor space to house the expected expansion of equipment during the next 4 to 8 years; and when a new building site is acquired, land

may be purchased for the anticipated building needs 20 or more years ahead.

This practice of building ahead of demand suggests that the concept of the spare-capacity coefficient adopted in the capital-requirements theory is reasonably applicable to the telephone industry. It should be remembered that the spare-capacity coefficient is defined as a marginal coefficient, relating changes in capacity to changes in expected output, and not as an average coefficient, relating total capacity and total expected output. New investment in a particular type of equipment is undertaken whenever demand in the near future, making allowance for the construction period, is expected to exceed current total capacity. This capacity was installed at some time in the past on the basis of demand estimates made then, rather than on the basis of demand estimates in the immediately preceding period, as indicated in the capital-requirements theory. When new investment is undertaken, a margin of spare capacity, measured by the period of building ahead of demand, is provided. With a fixed number of years of building in advance, the amount of additional capacity provided is proportional to the expected annual increase in output, and hence its determination can be represented by a fixed marginal spare-capacity coefficient. The total amount of spare capacity in this type of equipment then gradually diminishes as the expected future demand materializes, and the next new investment is required only when demand is again expected to exceed total capacity in the near future.

Once the desired increase in capacity has been determined, the amount of additional capital equipment required to provide this increase in capacity must be determined. The procedure varies according to the type of equipment under consideration.

The required number of additional telephone instruments, to begin with, can be determined almost directly from the estimated increase in total telephones, the third item in the basic demand estimates. The ratio is somewhat higher than 1:1, however, because the required stock of instruments includes a certain number to absorb variations in the flow of connects and disconnects.

The required number of additional pairs of conductors in subscriber cables and open wires (i.e. those which connect subscribers' telephones to the central office of an exchange) can be determined similarly from the estimated increase in lines, the first item in the basic demand estimates. The ratio here is considerably higher than 1:1, however, because of the impossibility of filling each cable exactly to the 100-percent point. The fill is of course better in heavily populated than in lightly populated areas, but a 75-percent fill is considered a satisfactory objective.

The procedure by which the engineer determines the required number of additional circuits in trunk cables and open wires (i.e. those which connect the central office of one exchange to the central office of another exchange) is more complex. The calculation is further complicated by the fact that cables between two exchanges frequently include circuits which connect still other pairs of exchanges. The following discussion refers, for simplicity, only to circuits required to handle traffic between the two terminal exchanges. In this simple case the engineer uses, in essence, two ratios: (1) The average number of busy-hour calls per main telephone (counting only those from one exchange to the other) is determined from the records of the traffic department, modified by expected changes. Note that capacity is provided to handle the traffic during the busy hours of the average day of the busy month, and therefore that at other times there is necessarily some spare capacity. (2) The average holding time per call, in seconds, is likewise determined from the records of the traffic department, modified by any expected changes. Using these two ratios and the future demand estimates for the two exchanges under consideration, the engineer can compute the traffic which the trunk cables and open wires will have to carry, in terms of hundreds of call-seconds, or CCS, by means of the following formula:

Estimated number of main telephones times average number of busy-hour calls per main telephone times average holding time per call divided by 100 equals traffic in CCS.

TABLE 1.—Trunk capacity tables: Hundred call-seconds and percent; use at various service levels for trunk groups of 1 to 50

[The table number indicates the number of calls per thousand encountering all trunks busy]

Trunks	Table 1		Table 5		Table 10		Table 20		Table 30		Table 40	
	Hundred call-seconds	Percent of usage	Hundred call-seconds	Percent of usage	Hundred call-seconds	Percent of usage	Hundred call-seconds	Percent of usage	Hundred call-seconds	Percent of usage	Hundred call-seconds	Percent of usage
1	0.1	0.1	0.2	0.5	0.4	1.0	0.7	2.0	1.1	3.1	1.5	4.2
2	1.6	2.3	3.7	4.8	5.4	7.5	7.9	10.9	9.7	13.5	11.3	15.7
3	6.9	6.4	12.2	11.3	15.7	14.5	20.4	18.9	24.0	22.2	26.9	24.9
4	15.4	10.7	24.2	16.8	29.6	20.6	36.7	25.5	41.6	28.9	45.7	31.8
5	26.6	14.8	38.9	21.6	46.1	25.6	55.8	31.0	61.1	34.2	66.6	37.0
6	40.0	18.5	55.4	25.7	64.4	29.8	76.0	35.2	82.8	38.3	89.3	41.3
7	54.7	21.7	73.4	29.1	83.9	33.3	96.8	38.4	105.0	41.7	112.0	44.4
8	70.9	24.6	92.5	32.1	105.0	36.5	119.0	41.3	129.0	44.8	137.0	47.6
9	88.2	27.2	113.0	34.9	126.0	38.9	142.0	43.8	153.0	47.2	162.0	50.0
10	107.0	29.7	134.0	37.2	149.0	41.4	166.0	46.1	178.0	49.4	188.0	52.2
11	126.0	31.8	156.0	39.4	172.0	43.4	191.0	48.2	204.0	51.5	214.0	54.0
12	145.0	33.6	178.0	41.2	195.0	45.1	216.0	50.0	230.0	53.3	240.0	55.6
13	166.0	35.5	201.0	42.9	220.0	47.0	241.0	51.5	256.0	54.7	267.0	57.1
14	187.0	37.1	224.0	44.4	244.0	48.4	267.0	53.0	283.0	56.1	295.0	58.5
15	208.0	38.5	248.0	45.9	269.0	49.8	293.0	54.3	310.0	57.4	322.0	59.6
16	231.0	40.0	273.0	47.4	294.0	51.1	320.0	55.6	337.0	58.5	350.0	60.8
17	253.0	41.3	297.0	48.5	320.0	52.3	347.0	56.7	355.0	59.6	378.0	61.8
18	276.0	42.6	322.0	49.7	346.0	53.4	374.0	57.7	392.0	60.5	407.0	62.8
19	299.0	43.7	347.0	50.7	373.0	54.5	401.0	58.6	420.0	61.4	436.0	63.8
20	323.0	44.9	373.0	51.8	399.0	55.4	429.0	59.6	449.0	62.4	465.0	64.6
21	346.0	45.8	399.0	52.8	426.0	56.4	458.0	60.6	478.0	63.2	494.0	65.3
22	370.0	46.7	424.0	53.5	453.0	57.2	486.0	61.4	507.0	64.0	523.0	66.0
23	395.0	47.7	451.0	54.5	480.0	58.0	514.0	62.1	536.0	64.7	552.0	66.7
24	419.0	48.5	477.0	55.2	507.0	58.7	542.0	62.8	564.0	65.3	582.0	67.4
25	444.0	49.3	504.0	56.0	535.0	59.4	571.0	63.4	593.0	65.9	611.0	67.9
26	469.0	50.1	531.0	56.7	562.0	60.1	599.0	64.0	623.0	66.6	641.0	68.5
27	495.0	50.9	558.0	57.4	590.0	60.7	627.0	64.5	652.0	67.1	671.0	68.9
28	520.0	51.6	585.0	58.0	618.0	61.3	656.0	65.1	682.0	67.7	701.0	69.6
29	545.0	52.2	612.0	58.6	647.0	62.0	685.0	65.6	711.0	68.1	731.0	70.0
30	571.0	52.9	640.0	59.3	675.0	62.5	715.0	66.2	741.0	68.6	762.0	70.6
31	597.0	53.5	667.0	59.8	703.0	63.0	744.0	66.7	771.0	69.1	792.0	71.0
32	624.0	54.2	695.0	60.3	732.0	63.6	773.0	67.1	801.0	69.5	822.0	71.4
33	650.0	54.7	723.0	60.8	760.0	64.0	803.0	67.6	831.0	69.9	852.0	71.7
34	676.0	55.2	751.0	61.4	789.0	64.5	832.0	68.0	861.0	70.3	883.0	72.1

TABLE 1.—Trunk capacity tables: Hundred call-seconds and percent; use at various service levels for trunk groups of 1 to 50—Continued

[The table number indicates the number of calls per thousand encountering all trunks busy]

Trunks	Table 1		Table 5		Table 10		Table 20		Table 30		Table 40	
	Hundred call-seconds	Percent of usage	Hundred call-seconds	Percent of usage	Hundred call-seconds	Percent of usage	Hundred call-seconds	Percent of usage	Hundred call-seconds	Percent of usage	Hundred call-seconds	Percent of usage
35	703.0	55.8	779.0	61.8	818.0	64.9	862.0	68.4	891.0	70.7	913.0	72.5
36	729.0	56.3	807.0	62.3	847.0	65.4	892.0	68.8	922.0	71.1	944.0	72.8
37	756.0	56.8	836.0	62.8	876.0	65.8	922.0	69.2	952.0	71.5	975.0	73.2
38	783.0	57.3	864.0	63.2	905.0	66.2	952.0	69.6	982.0	71.8	1,006.0	73.5
39	810.0	57.7	892.0	63.5	935.0	66.6	982.0	69.9	1,013.0	72.1	1,037.0	73.9
40	837.0	58.1	921.0	64.0	964.0	66.9	1,012.0	70.3	1,043.0	72.4	1,069.0	74.2
41	865.0	58.6	950.0	64.4	993.0	67.3	1,042.0	70.6	1,074.0	72.8	1,099.0	74.4
42	892.0	59.0	979.0	64.7	1,023.0	67.7	1,072.0	70.9	1,104.0	73.0	1,130.0	74.7
43	919.0	59.4	1,008.0	65.1	1,052.0	68.0	1,103.0	71.3	1,135.0	73.3	1,161.0	75.0
44	947.0	59.8	1,036.0	65.4	1,082.0	68.3	1,133.0	71.5	1,166.0	73.6	1,192.0	75.3
45	975.0	60.2	1,066.0	65.8	1,112.0	68.6	1,164.0	71.8	1,197.0	73.9	1,223.0	75.5
46	1,003.0	60.6	1,095.0	66.1	1,142.0	69.0	1,194.0	72.1	1,228.0	74.2	1,255.0	75.8
47	1,030.0	60.9	1,124.0	66.4	1,171.0	69.2	1,225.0	72.4	1,259.0	74.4	1,286.0	76.0
48	1,058.0	61.2	1,153.0	66.7	1,201.0	69.5	1,255.0	72.6	1,291.0	74.7	1,317.0	76.2
49	1,086.0	61.6	1,183.0	67.1	1,231.0	69.8	1,286.0	72.9	1,322.0	74.9	1,349.0	76.5
50	1,115.0	61.9	1,212.0	67.3	1,261.0	70.1	1,317.0	73.2	1,353.0	75.2	1,381.0	76.7

The number of circuits required to carry this traffic can then be read off a set of trunk capacity tables, some of which are reproduced in table 1. Each of these tables represents a particular level of availability of circuits, as measured by the number of calls per thousand which can be expected to encounter all circuits busy, on the assumption of random distribution of calls within the busy hours. To illustrate the use of these different tables, the availability of circuits is usually set lower for trunk cables in toll service than for trunk cables in local exchange service, so that the former will be in use a larger percentage of the time. Once the desired availability of circuits is specified, the engineer can read down the appropriate table to the required CCS, and there find the required number of circuits, as well as the percentage of time these circuits can be expected to be in use.

The required increase in central office equipment is determined differently according to whether the central office is equipped with manual switchboards or with automatic switchboards. In determining the required number of operator positions for a central office equipped with manual switchboards, the engineer uses in essence three ratios: (1) The average number of busy-hour calls per main telephone (counting all calls this time) is again determined from the records of the traffic department, modified by expected changes; (2) the number of work-units per call is determined from time studies of the work required to handle calls of different kinds, e.g., toll calls, local exchange calls, uncompleted calls; (3) the number of work units per operator, i.e., the operator load, is determined for each central office on the basis of past experience and expected changes. The Bell System has a theoretical standard operator load, established in 1911, of 230 work-units in the busy hour, the standard being defined as the number of work-units which can be handled by a fully experienced operator of average ability while maintaining a satisfactory grade of service. In particular central offices, however, the actual load differs from the theoretical standard, primarily because of differing experience of the operators. Using these three ratios and the future demand estimate for the particular exchange under consideration, the required number of operator positions is computed by means of the following formula:

Estimated number of main telephones times average number of busy-hour calls per main telephone times number of work-units per call divided by number of work-units per operator equals required number of operator positions.

The determination of the required stock of automatic switchboards in a central office using the dial system is complicated by the fact that there are three main types of auto-

matic switchboards, according to the type of switching mechanism employed—step-by-step, panel, and crossbar. Each of these types consists of a group of more or less separate components—for example, in the step-by-step switchboard, linefinders, selectors, and connectors. For each of the components in each of these types, the engineer must determine the number required to meet the estimated demand. In each calculation, two ratios are used: (1) The average number of busy-hour calls per main telephone is determined as in the case of manual switchboards; (2) the average holding-time per call, either from the records of the traffic department, as before, or from engineering data, if the component is in use only part of the total time consumed in a call. Using these two ratios and the future demand estimate for the particular exchange under consideration, the traffic which the component will have to carry is estimated, in CCS, by the same formula used for trunk cables. Then the number of units of the component required to carry this traffic, with a specified availability of circuits can be read off a trunk capacity table.

Through all these complexities, there exist certain fixed ratios between the increase in capacity desired in each particular type of capital equipment, and the number of additional units required to provide that increase. These ratios depend variously on spares for temporary replacements, on practicable cable fills, on the timing and duration of calls, on operators' experience, on random distribution of calls within the busy hour, and on the planned availability of circuits. They could in principle be calculated directly from the rather complicated engineering procedures, although because of lack of sufficiently complete data I have not been able to do this in the quantitative analysis below. In other words, the concept of the capital coefficient adopted in the capital-requirements theory is a close approximation to reality in the telephone industry.

The possibility of varying the number of CCS handled by a given stock of capital equipment by permitting the availability of circuits to vary should be noted. This possibility arises because the product of the telephone industry has more than one dimension, and these dimensions are to some extent substitutable for each other. The consequence of attempting to produce beyond capacity is not a rise in the marginal cost of an unchanged product, as in most manufacturing industries, but rather a change in one of the dimensions of the product. Specifically, if an automatic switchboard is made to handle a larger number of CCS in the busy hour than it was designed to handle, this is accomplished by keeping customers waiting a few moments until circuits are open, thus keeping the circuits in use more continuously. In the trunk capacity tables, this appears as a movement to the right, along

the row for the existing number of trunks, to a table with a higher percentage of use, but also a higher number of calls per thousand encountering all trunks busy.

How consistent has been the practice in the Bell System of maintaining the planned level of availability of circuits? In time of war, clearly, it has been permitted to fall where necessary to the maximum practicable extent. Yet even in these circumstances the fall is limited technologically; in World War II maximum wartime capability in central office equipment was only 5 percent greater than peacetime capacity. The excess wartime demand has appeared to a large extent in a backlog of unfilled order for service; the backlog has then been eliminated, and the availability of circuits raised again, in the course of postwar construction. This sequence of events can be traced during and after both World Wars I and II.⁴

To sum up, then, the engineering stage in the investment process in the Bell System approximates closely the second basic hypothesis of the capital-requirements theory—that the firm's net investment depends via fixed capital and spare-capacity coefficients upon its demand estimates. Given the demand estimates, and making allowance for the construction period, the engineer determines the desired increase in capacity by referring to the appropriate period of building ahead of demand; this calculation can be represented by the spare-capacity coefficients. Given the desired increase in capacity, and a specified level of availability of circuits, the engineer determines the necessary net investment by referring to a complex of technological considerations; this calculation can be represented by the capital coefficients.

D. Financing investment in the Bell System

In the third stage of the investment process in the Bell System funds must be raised to finance the investment expenditures. The American company has the main responsibility for carrying out this function, because of an arrangement by which the associated companies and the long-lines department obtained a large part of their funds in the first instance as advances from the American company, while the American company provides these advances by raising funds from the public. The associated companies later liquidate the advances from the proceeds of new stock or bond issues.

⁴ American Telephone & Telegraph Co., "Annual Reports," 1916, pp. 7-9; 1917, pp. 7-8; 1919, pp. 16-17, 1920, pp. 27-28; 1923, pp. 22-23; 1924, pp. 11-15; 1925, p. 11; 1941, p. 3; 1942, pp. 3-8; 1943, pp. 2-8; 1944, p. 13; 1945, pp. 1-6; 1946, pp. 1-7; 1947, pp. 1-6; 1948, pp. 2-6.

The critical question here is: how important is the availability of funds in determining the final investment decision? The answer is not clear. The question must be considered at least implicitly before the boards of directors can approve a suggested investment program, derived from the demand estimates and the engineering calculations. Yet there have apparently been no instances in which an investment program has been drawn up and then cut back because of lack of funds, or expanded because of the ease of obtaining funds. The fundamental reason why the availability of funds is not more explicitly considered, however, is probably that the Bell System has not experienced serious difficulty in financing whatever investment expenditures have been suggested by the demand estimates and the engineering calculations. On the basis of these considerations, no serious error seems to be involved in neglecting the influence of the availability of funds upon the final investment decisions, as suggested in the capital-requirements theory.

A more important consideration in the investment process of the Bell System seems to be that of deciding how the necessary funds for the investment program can best be raised. The historical pattern of Bell System financing can be seen in the following calculation. During the period from 1913 to 1935 the total financial requirements of the system⁵ were supplied from various sources in the following percentages: depreciation—21 percent; undistributed profits—7 percent; other internal sources—4 percent; associated company stock issues—4 percent; associated company bond issues—12 percent; other associated company sources—3 percent; American company stock issues (including premiums obtained in the conversion of convertible bonds into stocks)—28 percent; American company bond issues (including the principal of convertible bonds later converted into stocks)—19 percent; other American company sources—6 percent. The figures add up to more than 100 percent because the definition of funds raised exceeded the definition of financial requirements in this calculation by about 4 percent.⁶

E. The influence of technological progress and of price changes

The capital-requirements theory recognizes only one important source of change in the relationship between expected increases in demand and the firm's net investment—technological progress. What then have been the principal technological developments in the history of the telephone industry, and how important have they been in affecting investment in the Bell System?

A major technological change has been the development of the three existing types of automatic switchboards. The panel type, which uses selectors operating from a continuous power drive, was introduced in 1917, primarily for large metropolitan exchanges. During the twenties, after a delay due to the war, manual switchboards in these exchanges were generally replaced. About the same time the step-by-step type, which uses electromagnetic switches, was installed in various small cities where cost studies showed that replacement of the manual switchboards would be economical. This trend in the smaller exchanges has continued up to the present time. Then in 1938 the crossbar type, which uses all relays, was developed

for use in the large metropolitan exchanges. While the existing panel type has not been generally replaced, the crossbar type has since been used for expansion of capacity in these exchanges. The latest development in this field permits toll operators to make long distance connections by dialing, and requires supplementary automatic switching apparatus which makes connection to the proper exchange.

The cost calculations made in deciding whether to convert from manual to dial operation have been quite detailed. A comparison was made between the present value of the expected annual costs of operation, maintenance, and taxes for the existing manual switchboards; and the present value of the expected total annual costs, including amortization (after allowance for salvage of the manuals), for the automatic switchboards—all costs being calculated over the engineering life of the equipment, and discounted at a rate of 7 percent. Many of the cost calculations for the smaller exchanges revealed that it would be economical to continue to add operator positions to the existing manual switchboard until the cost of further additions rose significantly, e.g., because of the necessity of increasing the size of the building to house the additional positions. Hence replacement of the existing manual switchboards in these exchanges has been a gradual process, depending in each location upon the time when a major expansion of capacity became necessary.

A second technological change obvious to the customers has occurred in the design of telephone instruments. In 1927, a hand set with separate bell box was distributed among the associated companies as an alternative to the existing desk sets. Technical improvements followed, and in 1934 another hand set, with the bell in the base and with a new antisidetone circuit, was authorized. In both cases replacement of existing telephone sets was gradual. This technological change has repercussions on other types of equipment as well. The strength of the signal from the new instruments was greatly increased, and this made it practicable to reduce the diameter of the conductors in the connecting wires and cables. The increased strength of signal from the instruments more than compensated for the increased attenuation in the smaller conductors.

Third, a number of gradual improvements in the design and utilization of cables have occurred. The design of cables has been improved by decreasing the size of the wires, altering their insulation, increasing the number of wires in the sheath, and altering the sheath. The utilization of cables has been intensified by the development of suitable loading techniques, which consist essentially in placing coils of the proper inductance at regular intervals along each conductor. Originally the attenuation of the signal in 1 mile of cable was as great as the attenuation in 50 to 100 miles of open wires, but successive improvements in loading and cable design gradually extended the distance over which it was economical to transmit by cables. In the late twenties in particular, open wires in toll service were widely replaced by cables.

A fourth major technological improvement was the development of the carrier system of transmission. By the use of this system a large number of messages can be transmitted simultaneously over a single circuit, and hence its introduction means that a smaller amount of outside plant is subsequently required to handle a given traffic load. The carrier system was developed in 1918, but at first could only be applied to circuits in open wires. In 1938, however, the K-type carrier system was applied on a commercial basis to toll cables. This system requires twin voice cables for transmission in both directions,

but each pair of wires in the two cables provided 12 channels of voice communication ranging in 4-kilocycle steps from 16 to 60 kilocycles. A few years later, coaxial cables were put into commercial use. These cables contain eight coaxial conductors, each pair of which, because of their wide frequency response, is capable of providing 600 channels of voice communications. Both the K-type carrier system and the coaxial cables, however, are most economical over long distances, and cost studies have therefore been made to determine their proving-in points. The latest development in this field has been the use of microwave radio channels, beamed along a line of towers spaced at approximately 25-mile intervals, thus dispensing with cables entirely. New types of carriers are still being developed, and Bell System engineers expect that within another year or two a system suitable for operation over the existing single voice cables will be available. In general these new systems will be installed to handle expansion of demand rather than to replace older types.

Thus it is clear that technological progress has exerted an important influence upon investment in the Bell System. It should be remembered that a technological change is defined in the capital-requirements theory as an abrupt alteration of the marginal capital and spare-capacity coefficients for the affected type of capital equipment. Therefore these four major technological developments should be reflected in the statistical coefficients calculated in the next section from the historical course of telephone investment. The chronology of these developments is used there as a standard for evaluating the statistical results. Moreover, it should be noted that technological changes have been introduced in the Bell System in the course of expanding capacity, and that replacement of the obsolescent equipment has been gradual. This is in accord with the emphasis upon marginal rather than average coefficients in the capital-requirements theory.

The capital-requirements theory, as pointed out before, neglects the influence of changes in prices upon the firm's investment. Does the investment practice in the Bell System throw any light upon the validity of this simplification?

The detailed calculations of the present values of expected costs for alternative periods of building ahead of demand indicate that changes in the prices of elements in installation costs may alter the spare-capacity coefficients. Indeed, since World War II the period of building ahead of demand in cable installations has been extended somewhat because of increases in labor costs. The periods of building ahead of demand in use today, however, are essentially the same as those in use in the early thirties, and hence in general price changes must have been either infrequent and small, or of minor importance in the investment process. It may be noted in passing that the market rate of interest is not relevant here, since a conventional 7-percent rate of discount is used.

The detailed calculations of the present values of expected costs for alternative types of switchboards also suggest that changes in the relative prices of capital equipment and of other inputs may alter the capital coefficients. In the history of the Bell System, however, it is difficult to isolate instances in which relative price changes have had this effect. Possible instances are the shift from open wire to cable and the shift from manual switchboards to automatic switchboards, but both of these instances are so closely associated with technological developments that the influence of the relative price change by itself appears small.

In general the influence of price changes seems to have been of minor importance in the investment process in the Bell System,

⁵ Defined as the funds for capital expansion (75 percent of the total), omitting the funds used for replacement of retired capital equipment; plus the funds used to retire maturing obligations, omitting retirements of convertible bonds by the issue of new stocks.

⁶ Federal Communications Commission, "Investigation," pp. 423-428.

compared to the influence of technological changes. It is probably a reasonably close approximation to reality to assume, as in the capital-requirements theory, that all major changes in spare-capacity coefficients and capital coefficients are due to technological developments.

F. Retirement in the Bell System

According to the capital-requirements theory, retirement is a fixed fraction of the firm's stock of capital equipment. The retirement practice in the Bell System casts some light on the usefulness of this third basic hypothesis.

To begin with, although there seems to be no type of capital equipment which is retired when it reaches the end of a specified service life, there is some tendency for retirement to be fairly regular for other reasons. Outside plant, such as telephone poles, is tested periodically for physical soundness, and a fairly stable number of units tends to be retired every year because of wear and tear discovered in these tests. Inside plant, such as switchboards, is retired primarily when new technological developments are introduced, but the policy of introducing technological developments gradually tends to make retirement of inside plant fairly regular.

On the other hand, almost every type of capital equipment is quite durable, which weakens the tendency toward regular retirement. In 1935 the estimated service lives used for depreciation accounting by the long-lines department were as follows: Central office equipment, 13 years; buildings, 36 years; pole lines, 20 years; aerial cable, 25 years; underground cable, 30 years; underground conduit, 75 years.⁷ The durability of capital equipment also makes it difficult to contract the existing stock when demand falls, which is in keeping with the asymmetry of the capital-requirements theory.

There is also some indication that once a unit of capital equipment has been retired, its replacement is in most cases automatic. Inside plant is usually replaced automatically because the reason for its retirement is to substitute new equipment of improved design. Many types of outside plant are replaced automatically because they are links in a chain of capital equipment, and failure to replace the individual links would involve abandoning the capacity of the entire chain. Individual poles in pole lines and individual sections of cable have this characteristic, while individual open wires do not. Finally, the automatic replacement of both inside and outside plant may be based on the fact that demand has grown steadily for many years, and even when its growth has been interrupted, the expectation of future growth has justified maintaining the existing stock of capital equipment. The consequence of this tendency toward automatic replacement of retired capital equipment is that net investment has never become significantly negative in the Bell System. In terms of the capital-requirements theory, this means that the asymmetry between the effects of a rise and of a fall in expected demand has occurred at the point where net investment is approximately zero, rather than at the point where it is negative and equal to retirement.

IV. A QUANTITATIVE ANALYSIS OF TELEPHONE INVESTMENT

A. The method

The capital-requirements theory is tested quantitatively in this section by calculating its coefficients from statistical data for the entire industry, and then examining the

statistical coefficients for stability and for consistency with the known technological history of the industry. This quantitative analysis uses the investment procedures in the Bell System as a guide for certain details of the calculations; more important, it relies upon the chronology of major technological developments in the Bell System as a standard for evaluating the statistical coefficients.

The method adopted for calculating the coefficients depends upon available statistical series for output of telephone service, stocks of various types of capital equipment, and retirement of various types of capital equipment. Because of lack of more complete data, I have not been able to calculate the coefficients directly from the investment procedures of the Bell System. In principle this could be done, and should give more precise results, but the quantitative analysis presented here is limited to a cruder method.

The method uses aggregate statistical series except in one instance. This has been done both because most of the available data are for the industry as a whole, and because the desired results, if obtainable, are aggregate coefficients. One of the distinctive characteristics of the telephone industry, however, is that both demand and capital equipment are geographically localized. The theoretical relation between net investment and expected increases in demand applies strictly only to each individual telephone exchange, and can be applied to the industry as a whole only as a statistical approximation. In particular, the stability of the statistical coefficients depends partly on a regular geographical distribution of increases in demand among the individual exchanges—a regularity which has not always prevailed in fact.

This is an instance of a general problem in statistical analysis—the problem of aggregation.⁸ Only under special conditions has it been found possible to deduce valid relationships among macro-economic variables from theoretical relationships among micro-economic variables. Consequently, most aggregate relationships suitable for statistical analysis are derived by analogy rather than deduction, and should be conceived simply as approximations to the more fundamental micro-economic relationships. Specifically, the industrywide coefficients calculated in this section are so conceived.

On the other hand, the use of data for a single industry largely avoids another general problem in statistical analysis—the problem of identification. The essence of this problem is how to isolate a single causal relationship from a system of mutually interdependent causal relationships, when the available statistical time series reflect the entire system rather than the single desired relationship. If analysis is limited to a single industry, however, the reflex effect of that industry upon itself, by way of the system of mutually interdependent relationships outside that industry, is small and can be neglected without serious error. In other words, the analysis reverts from general equilibrium to partial equilibrium analysis. The use of data for a single industry also makes the analogy between aggregate and micro-economic relationships more plausible.

The principal justification in the past for statistical studies at the level of the entire economy has been that they describe the structure of the economy in terms of a comparatively small number of relationships, and hence reduce the analysis to manageable proportions. The development of the interindustry input-output scheme, however, which describes the structure of the economy in terms of a much larger number of relationships among its various industries,

offers some hope that statistical studies can be shifted to the level of single industries, thus simplifying the problem of aggregation and largely avoiding the problem of identification. The results of these industry studies can then be tied together manageably in the input-output analysis.

Another feature of the statistical method is that it uses a one-dimensional measure of output and capacity. As indicated in the last section, however, one of the distinctive characteristics of the telephone industry is that its product is multidimensional, and in particular that the number of CCS handled by a given stock of capital equipment can be altered by permitting the availability of circuits to vary. Unfortunately the data needed to compensate for the other dimensions are not available. Using a one-dimensional measure of output and capacity, of course, implies that the other dimensions are held fairly stable—an implication which has not always been valid in the short run.

B. Calculation and evaluation of demand estimates

The first part of the quantitative analysis should preferably consist in calculating a historical series of expectations coefficients from statistical data, and then examining their stability. Unfortunately, however, information about actual demand estimates in the telephone industry is not available except for one small sample. Therefore it has been necessary simply to assume a value for the expectations coefficient, and then to check this assumption against the one small sample.

The expectations coefficient is assumed to be +1, i.e., the recent proportional trend in output is expected to continue without diminution. This is compatible with the importance of trend extrapolation in the investment procedures of the Bell System, and with the fact that the growth in number of telephones in the United States actually has approximated an exponential trend. In addition, when the recent trend is either negative or unusually small, the trend which is extrapolated is assumed to be that of the last normal year, set on the base of the current subnormal year. This is compatible with the optimism regarding future growth which seems to prevail in the Bell System.

In algebraic terms, the first basic hypothesis of the capital-requirements theory is

$$(7, 6)$$

$$O_{t+1} = O_t [1 + \epsilon (O_t - O_{t-1} / O_{t-1})]$$

With the expectations coefficient assumed to be +1, and with the modification for optimism, this hypothesis becomes

$$(7, 14)$$

$$O_{t+1} = O_t (O_t / O_{t-1})$$

in which

O_t / O_{t-1} in a "subnormal" year is replaced by the same ratio in the last "normal" year.

The one small sample of actual demand estimates in the telephone industry which is available for checking the assumed expectations coefficient consists of the estimates of toll messages made in the Bell System in the 4 years 1927-30. The actual number of toll messages is also available, and hence it is possible to calculate demand estimates in these years, using equation (7, 14), and to compare them with the actual demand estimates. This comparison is shown in table 2 and chart 1 [chart not printed in RECORD]. It is clear that the calculated demand estimates, based on the assumed expectations coefficient of +1, approximate the actual demand estimates closely. Note in particular that the calculated demand estimates for 1930, based on the "normal" trend of 1929, forecast a rising trend comparable to that of the actual demand estimates, even though the number of toll messages showed a "subnormal" increase in 1930. Thus insofar as

⁷ Federal Communications Commission, "Docket," exhibit No. 135, "Long-time Department, Financial and Operating Summary," p. 85.

⁸ The regional aspects of this problem are discussed in chs. 4 and 5.

such a short series of actual demand estimates is significant, it lends support to the assumed value of the expectations coefficient and to equation (7, 14). More generally, it lends support to the first basic hypothesis

of the capital-requirements theory—that demand estimates depend, via a fixed expectations coefficient, upon the recent trend of output.

Three steps may now be taken in prepara-

tion for the calculation of capital and spare-capacity coefficients in the next part of the quantitative analysis. These steps are set forth in table 3 and chart 2 [chart not printed in RECORD].

TABLE 2.—Comparison of actual and calculated demand estimates

Year	Number of toll messages	Relative increase in toll messages	Actual 1927 estimates	Calculated 1927 estimates ¹	Actual 1928 estimates	Calculated 1928 estimates ²	Actual 1929 estimates	Calculated 1929 estimates ³	Actual 1930 estimates	Calculated 1930 estimates ⁴
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
	Millions		Millions	Millions	Millions	Millions	Millions	Millions	Millions	Millions
(1) 1923.....	22.3									
(2) 1924.....	24.0									
(3) 1925.....	27.7									
(4) 1926.....	31.9									
(5) 1927.....	35.2	0.103								
(6) 1928.....	41.7	.185	38.8	38.8						
(7) 1929.....	49.3	.192	42.7	42.8	47.8	49.4				
(8) 1930.....	50.5	.025	47.4	47.2	55.4	58.5	59.0	58.3		
(9) 1931.....	48.4		52.2	52.1	63.4	69.3	69.0	68.9	58.8	59.7
(10) 1932.....	38.0		57.4	57.5	71.0	82.1	80.0	81.4	68.2	71.6
(11) 1933.....	35.5				80.0	97.2	92.0	96.2	76.8	84.6
(12) 1934.....	37.5						105.0	113.7		

¹ Calculated from formula, $35.2 \times (1 + 0.103)^n$, in which n is number of years in future.

² Calculated from formula, $41.7 \times (1 + 0.185)^n$.

³ Calculated from formula, $49.3 \times (1 + 0.182)^n$.

⁴ Calculated from formula, $50.5 \times (1 + 0.182)^n$.

Source: Col. 1, Federal Communications Commission, docket, exhibit No. 135, p. 36; data are for long-lines department of Bell System; cols. 3, 5, 7, 9, Federal Communications Commission, docket, exhibit No. 580, p. 12; data are for long-lines department of Bell System.

TABLE 3.—Calculation of demand estimates

Year	Number of telephones in Bell System	Number of telephones in United States	Ratio of U.S. telephones this year to last year	Calculated telephones next year ¹	Calculated present capacity	Calculated increase in telephones over capacity ²	Year	Number of telephones in Bell System	Number of telephones in United States	Ratio of U.S. telephones this year to last year	Calculated telephones next year ¹	Calculated present capacity	Calculated increase in telephones over capacity ²
	(1)	(2)	(3)	(4)	(5)	(6)		(1)	(2)	(3)	(4)	(5)	(6)
	Millions	Millions		Millions	Millions	Millions		Millions	Millions		Millions	Millions	Millions
(1) 1912.....	4.76	8.73					(20) 1931.....	14.91	19.71	.9757	20.62	21.16	0
(2) 1913.....	5.11	9.54	1.0928	10.43	9.54	0.89	(21) 1932.....	13.31	17.42	.8838		21.16	0
(3) 1914.....	5.44	10.05	1.0635	10.59	10.05	.54	(22) 1933.....	12.82	16.71	.9592		21.16	0
(4) 1915.....	5.80	10.52	1.0468	11.01	10.52	.49	(23) 1934.....	13.12	16.97	1.0156		21.16	0
(5) 1916.....	6.37	11.24	1.0684	12.01	11.24	.77	(24) 1935.....	13.57	17.42	1.0265		21.16	0
(6) 1917.....	6.83	11.72	1.0427		11.72		(25) 1936.....	14.45	18.43	1.0580	19.50	21.16	0
(7) 1918.....	7.05	12.08	1.0307		12.08		(26) 1937.....	15.33	19.45	1.0553	20.53	21.16	0
(8) 1919.....	7.59	12.67	1.0488	13.21	12.67	.54	(27) 1938.....	15.76	19.95	1.0257	21.05	21.16	0
(9) 1920.....	8.13	13.41	1.0584	14.19	13.41	.78	(28) 1939.....	16.54	20.83	1.0441	21.75	21.16	.59
(10) 1921.....	8.72	13.88	1.0350	14.69	13.88	.81	(29) 1940.....	17.48	21.93	1.0528	23.09	21.93	1.16
(11) 1922.....	9.32	14.35	1.0339	15.19	14.35	.84	(30) 1941.....	18.84	23.52	1.0725		23.52	
(12) 1923.....	10.20	15.37	1.0711	16.46	15.37	1.09	(31) 1942.....	20.01	24.92	1.0545		24.92	
(13) 1924.....	11.17	16.21	1.0547	17.10	16.21	.89	(32) 1943.....	21.25	26.38	1.0586		26.38	
(14) 1925.....	11.91	16.94	1.0450	17.70	16.94	.76	(33) 1944.....	21.58	26.86	1.0182		26.86	
(15) 1926.....	12.67	17.75	1.0478	18.60	17.75	.85	(34) 1945.....	22.45	27.87	1.0376	29.89	27.87	2.02
(16) 1927.....	13.41	18.52	1.0434	19.32	18.52	.80	(35) 1946.....	25.71	31.61	1.1342	35.85	31.61	4.24
(17) 1928.....	14.18	19.34	1.0443	20.20	19.34	.86	(36) 1947.....	28.51	34.87	1.1031	38.47	34.87	3.60
(18) 1929.....	15.04	20.23	1.0460	21.16	20.23	.93	(37) 1948.....	31.36	38.35	1.0998	42.18	38.35	3.83
(19) 1930.....	15.19	20.20	.9985	21.13	21.16	0							

¹ Calculated from formula (col. 2) × (col. 3); 1919 calculation uses 1917 ratio; 1921 and 1922 calculations use 1920 ratio; 1930 and 1931 calculations use 1929 ratio; 1938 calculation uses 1937 ratio; 1945 calculation uses 1941 ratio.

² Entered from col. 2, 1913-29 and 1940-48; from 1929 entry in col. 4, 1930-39.

³ Calculated from formula (col. 4) - (col. 5).

First, equation (7, 14) is used to compute a series of demand estimates for the entire telephone industry over the period 1913-48. There is, of course, no possibility of checking these estimates directly, because of lack of information on actual demand estimates. The measure of industrywide output used in deriving the recent trend for these calculations is the total number of telephones in the United States. This is compatible with the practice in the Bell System of estimating demand in terms of number of lines, main telephones, and total telephones. The "subnormal" years for the purpose of the modification for optimism in equation (7, 14) are 1921-22, 1930-31, and 1938. It is not reasonable to expect such optimism in the depth of the depression, 1932-35, but since the demand estimates in those years, whether optimistic or pessimistic, were far below capacity, they can be neglected. No demand estimates are calculated for the years of war of Government seizure, 1918-19 and 1942-45, and the immediate postwar or postseizure estimates made in 1919 and 1945 are calculated from the trends of the last essentially peacetime years, 1917 and 1941, respectively.

Second, a series is obtained to represent effective industrywide capacity over the same period 1913-48. According to the investment procedures of the Bell System, it should be remembered, new investment in each individual exchange is undertaken whenever expected demand exceeds current total capacity, but because of the policy of building ahead of demand, the next new investment is required only after several years in which the growth of demand gradually uses up the spare capacity. This means that at any one time in the industry as a whole there exists a distribution of spare capacity in the individual exchanges. Unfortunately, however, there are no published figures for this distribution of spare capacity. Statistically, therefore, it seems desirable to represent effective industrywide capacity by the current industrywide output, as measured by the actual number of telephones in the United States. The theoretical justification for this is that an expected increase in industrywide demand over current industrywide output provided it is distributed in some regular way among the individual exchanges, requires new in-

vestment in those particular exchanges, at one end of the distribution, which have used up their spare capacity. It would also be possible to represent effective industrywide capacity by the calculated-demand estimate made in the previous year, but since this is a derived figure, it seems less desirable in most years. The only exception to this rule is in 1930, when the actual industrywide output did not increase over 1929, yet a large net investment program was carried through; capacity in 1930, is therefore measured by the calculated-demand estimate. The statistical series for effective industrywide capacity is continued at its maximum previous level, even when expected demand subsequently falls. In other words, the telephone industry is assumed to make replacement investment equal to its retirement. This is compatible with the tendency to automatic replacement noted in the Bell System procedures.

Third, a series of differences is computed between the calculated demand estimates 1 year in the future and the calculated effective capacity in the current year. A 1-year projection is used here because it is the

closest approximation using annual data to the construction periods indicated in the last section. This series of differences—the calculated increases in expected demand over capacity—is one of the two main elements needed for computing the statistical capital and spare-capacity coefficients.

C. Calculation and evaluation of capital and spare-capacity coefficients

The second part of the quantitative analysis consists in calculating a historical series of capital and spare-capacity coefficients for each type of telephone capital equipment. Then the statistical coefficients are examined to see if they vary in the proper direction and in the proper years as indicated by the known history of technological developments in the industry, but are stable from one technological change to the next. This is a key part of the quantitative analysis. It tests directly the second basic hypothesis of the capital-requirements theory—that net investment depends, via fixed capital and spare-capacity coefficients, upon changes in expected demand—and indirectly the first basic hypothesis, since the calculated demand estimates are used in computing the coefficients.

The evaluation of the stability of the statistical coefficients and their consistency with the technological history of the industry requires a subjective judgment. Here it is meaningful to think in terms of a scale of closeness of approximation of the hypothesis to the data, rather than in terms of the dichotomy of proof or disproof. This will be brought out in the evaluation below.

One of the two main elements needed for computing the statistical coefficients has already been obtained—the series of calculated increases in expected demand over capacity. The other is a series of deflated net investment for each of the various types of capital equipment used in the telephone industry. It is obtained as follows:

Data are available stating the value of six types of capital equipment in the Bell System at the end of each year 1912-48. These series have been corrected for changes in the number of companies included in the consolidated accounts; some important changes in accounting definitions occurred between 1932 and 1933, however. The six types are central-office equipment (mainly switchboards), land and buildings (mainly central-office buildings), exchange lines (outside plant used mainly for local service), toll lines (outside plant used mainly for toll service), station equipment (mainly telephone instruments and installations), and other plant (mainly vehicles and office furniture).

These six series are first blown up to the level of the entire industry by the use of a series of ratios between the total value of capital equipment in the industry and the total value in the Bell System. The ratios are computed directly for every fifth year from 1912 to 1937 (years of the Census of Electrical Industries), and by interpolation for the intervening years. Annual net investment in current prices in each type of equipment is then calculated by taking the annual increments of these six series. Finally, separate price indexes on a 1926 base are derived for each type of equipment, and the six series of annual increments are deflated with these indexes. It would have been preferable to use these indexes to deflate gross investment, to use another index to deflate retirement, and to take the difference between the two deflated series, but this was not possible because of lack of data. The data and procedure for calculating deflated net investment in central-office equipment are presented for illustrative purposes in table 4.

Now that both of the main elements needed for computing the statistical capital

and spare-capacity coefficients have been obtained, it is revealing to plot the two series for comparison of the timing of their variations. According to the capital-requirements theory, their timing should be synchronous. This comparison is shown in

charts 3 through 5 [not printed in RECORD]. Note that the expected demand increases are plotted in the charts 1 year later than in table 3 to refer to the year in which the increase is expected to occur rather than the year in which the estimate is made.

TABLE 4.—Central office equipment: Calculation of capital and spare-capacity coefficients

Year	Central office equipment in Bell System (millions of dollars)	Ratio of industry to Bell System ¹	Central office equipment in telephone industry ² (millions of dollars)	Increase in central office equipment (millions of dollars)	Price index for central office equipment ³	Deflated increase in central office equipment ⁴ (millions of 1926 dollars)	Calculated capital and spare capacity coefficient ⁵ (1926 dollars per telephone)
	(1)	(2)	(3)	(4)	(5)	(6)	(7)
(1) 1912	99	1.46	145				
(2) 1913	108	1.440	156	11	69	16	
(3) 1914	119	1.420	169	13	69	19	21.35
(4) 1915	125	1.400	175	6	69	9	16.67
(5) 1916	136	1.380	188	13	69	19	38.78
(6) 1917	157	1.36	214	26	69	38	49.35
(7) 1918	175	1.340	235	21	98	21	
(8) 1919	191	1.320	252	17	98	17	
(9) 1920	224	1.300	291	39	115	34	62.96
(10) 1921	273	1.280	349	58	127	46	58.97
(11) 1922	343	1.26	432	83	126	66	81.48
(12) 1923	436	1.242	542	110	112	98	116.67
(13) 1924	565	1.224	692	150	110	136	124.77
(14) 1925	652	1.206	786	94	103	91	102.25
(15) 1926	735	1.888	873	87	100	87	114.47
(16) 1927	795	1.17	930	57	97	59	69.41
(17) 1928	858	1.166	1,000	70	90	78	97.50
(18) 1929	946	1.162	1,099	99	84	118	137.21
(19) 1930	1,041	1.158	1,205	106	79	134	144.09
(20) 1931	1,101	1.154	1,271	66	89	74	
(21) 1932	1,099	1.15	1,264	-7	89	-8	
(22) 1933	1,067	1.148	1,225	(⁶)	90	(⁶)	
(23) 1934	1,067	1.146	1,223	-2	103	-2	
(24) 1935	1,067	1.144	1,221	-2	109	-2	
(25) 1936	1,082	1.142	1,236	15	110	14	
(26) 1937	1,122	1.14	1,279	43	109	39	
(27) 1938	1,162	1.140	1,325	46	95	48	
(28) 1939	1,194	1.140	1,361	36	96	38	
(29) 1940	1,245	1.140	1,419	58	101	57	96.61
(30) 1941	1,360	1.140	1,550	131	100	131	112.93
(31) 1942	1,463	1.140	1,668	118	100	118	
(32) 1943	1,499	1.140	1,709	41	100	41	
(33) 1944	1,542	1.140	1,758	49	100	49	
(34) 1945	1,611	1.140	1,837	79	100	79	
(35) 1946	1,816	1.140	2,070	233	100	233	115.35
(36) 1947	2,246	1.140	2,560	490	122	402	94.81
(37) 1948	2,718	1.140	3,099	539	137	393	109.17

¹ Calculated from total capital equipment in Bell System and total capital equipment in telephone industry, at the 5-year intervals of the census of electrical industries, 1912-37, and by interpolation in the intervening years.

² Calculated from formula (col. 1) × (col. 2).

³ Calculated from data supplied by American Telephone & Telegraph Co.

⁴ Calculated from formula (col. 4) - (col. 5).

⁵ Calculated from formula (col. 6) - (col. 6, table 2, previous year).

⁶ Omitted because affected by accounting change between 1932 and 1933.

Source: col. 1: American Telephone & Telegraph Co.

Turning to the individual comparisons, the timing of variations in net investment in central office equipment, as shown in chart 3 [not printed in the RECORD], is quite similar to the timing of variations in the expected demand increases, in particular at the peaks in 1914, 1917, 1924, 1930, 1941, and 1947. This correspondence indicates that net investment in central office equipment, which is the largest component of total telephone investment, is timed in accordance with the capital-requirements theory.

One discrepancy which recurs in the comparisons for the other types of equipment should be pointed out, however. According to the capital-requirements theory, during the thirties no positive net investment should have been required, since actual demand remained below the 1929 peak until 1939 and expected demand remained below capacity until 1940. During the early thirties, in fact, net investment remained approximately zero, indicating both that no expansion was required and that retirement was almost entirely replaced. During the late thirties, on the other hand, some positive net investment was undertaken. This investment apparently was not due to lack of capacity in the industry as a whole; rather it was due in part to increases in demand in particular geographical areas, not

typical of the entire country, and in part to the introduction of technological improvements even though existing capacity was adequate. Although this positive net investment began earlier than the capital-requirements theory indicates, it is significant that net investment rose sharply in 1940 and 1941, when expected demand definitely exceeded existing capacity.

The timing comparisons for the other kinds of capital equipment reveal a successively diminishing correspondence between net investment and expected demand increases, more or less in the following ranking: Exchange lines, as shown in chart 4 [not printed in RECORD], rank second in correspondence, and are also the second largest component of total telephone investment. Land and buildings, as shown in chart 4 [not printed in RECORD], rank third, partly because buildings have a longer construction period, and hence annual investment is more regular. Station equipment, as shown in chart 5 [not printed in RECORD], ranks fourth in correspondence, with exceptionally large discrepancies over the depression years. Two distinctive characteristics of station equipment may account for these discrepancies: its construction period is short, so that investment can be rapidly adjusted to actual rather than expected changes in de-

mand; and its retirement is large, so that disinvestment can be significant when demand falls, and excess capacity does not persist to bar investment when demand rises again. Toll lines, as shown in chart 5 [not printed in RECORD], are fifth, primarily because they are "lumpy" inputs. Each major new line is a comparatively large part of the total stock of toll lines, and includes a large margin of spare capacity. Finally other plant, as shown in chart 3 [not printed in RECORD], ranks last in correspondence, because it simply does not have a definite technological relationship to demand. It is also the smallest component of total telephone investment.

To sum up, these comparisons indicate that the extent to which net investment is timed in accordance with the capital-requirements theory differs from one type of capital equipment to the next. The correspondence between net investment and expected demand increases is quite close, however, for the most important types—central office equipment and exchange lines.

The statistical capital and spare-capacity coefficients are now computed by dividing the series of deflated net investment in each type of capital equipment by the series of calculated increases in expected demand over capacity, i.e., by finding the ratios between the two main elements plotted in charts 3 through 5 [not printed in RECORD]. This calculation is illustrated for central office equipment in table 4. It should be noted that the statistical results are combined capital and spare-capacity coefficients, rather than the two kinds of coefficients taken separately. The reason for this has already been pointed out—that data for the distribution of spare capacity in the industry are not available. The coefficients are marginal coefficients, stating the amount of capital equipment (in 1926 dollars) required for each additional telephone, rather than average coefficients, stating the amount of capital equipment required for each existing telephone. No coefficients have been calculated for other plant, since it seems clear that net investment in other plant is not explained by the capital-requirements theory.

In algebraic terms, the second basic hypothesis of the capital-requirements theory is

$$(7, 12)$$

$$\Delta K^{a_{t+1}} = \beta^a \gamma^a (O^{a_{t+1}} - 1/\gamma^a C^{a_{t+1}}), \quad \Delta K^{a_{t+1}} \geq -R^{a_{t+1}}$$

For statistical analysis, using (a) the assumed value for the expectations coefficient and equation (7, 14) above, (b) the statistical measure for effective industrywide capacity and the assumption of automatic replacement, and (c) the deflated value of increments in capital stock for a measure of net investment, the combined capital and spare-capacity coefficients are computed from

$$(7, 15)$$

$$\Delta V^{a_{t+1}}/P^{a_{t+1}} = \beta^a \gamma^a (O^{a_{t+1}} - C^{a_{t+1}}), \quad \Delta V^{a_{t+1}}/P^{a_{t+1}} \geq 0$$

in which

ΔV = the increment in value of capital stock,

P = the price index, and,

C' = effective industrywide capacity.

The historical course of the statistical capital and spare-capacity coefficients can be seen in charts 6 to 8 [not printed in RECORD]. How may these statistical results be evaluated? In general the calculated coefficients have two notable characteristics: they fluctuate significantly from year to year, and they trace out underlying patterns of variation over the entire period.

The annual fluctuations are, of course, at variance with the capital-requirements theory, which assumes that the coefficients are stable except when altered by technological change. These fluctuations do not seem to be sufficiently extreme, however—at least for the more important types of capital

equipment—to warrant rejection of the theory. The year-to-year fluctuations seem to arise from a combination of three sources. In part they are due to chance variations in the number of local exchanges requiring expansions of capacity as a result of a given industrywide increase in expected demand, i.e., they stem from the aggregation problem discussed earlier. In part they result from variations in the availability of circuits, i.e., they stem from using a one-dimensional measure of output and capacity. And in part they arise from considerations affecting net investment which are abstracted from in the capital-requirements theory—in particular, from policy decisions to vary the rate of introduction of technological improvements. Such year-to-year fluctuations must be expected in view of the approximations of the statistical technique and the simplicity of the theory.

The underlying patterns of variation over the entire period, on the other hand, appear to reflect the fundamental influence of the capital coefficients and spare-capacity coefficients of the capital-requirements theory. These patterns can in general be explained in the light of the technological developments known to have taken place in the various types of capital equipment in the period 1913-48. In the charts, therefore, simple freehand lines have been drawn to represent these underlying patterns, consistent with the dates and directions of the known technological changes.

The statistical coefficients for the individual types of capital equipment reveal a successively diminishing stability and consistency with the technological history, more or less in the same ranking noted earlier in the timing comparison.

As shown in chart 6 [not printed in RECORD], the coefficients for central office equipment trace out an underlying pattern of variation which reflects clearly the technological change from manual to automatic switchboards. The coefficients rose sharply from 1920 to 1923, when the automatics, which have higher capital costs than the manuals (but lower operating costs), were first introduced; and then remained in the neighborhood of this higher level throughout the twenties, in 1940-41, and in 1946-48, when the automatics continued to be used for expansion and gradual replacement. Certain of the year-to-year fluctuations around this pattern are also understandable. The peak in 1923 and 1924 was due to the process of eliminating backlog demand and restoring the normal availability of circuits after wartime shortages, and the fall in 1925 followed the completion of this process. The peak in 1929 and 1930 was due to temporary acceleration of the technological shift from manual to automatic switchboards.

Chart 7 [not printed in RECORD] indicates that the coefficient for exchange lines trace out a steadily rising pattern from 1914 through 1930, and then a falling pattern through 1941 to the years after World War II. The earlier upward trend reflects the technological shifts which took place in those years from open wire to cable, and from wire and cable above ground to cable underground, each of which require larger amounts of capital equipment per telephone. It also reflects the extension of telephone service to less heavily populated areas. The later falling trend stems from the technological changes in station equipment in those years, raising the strength of the signal from the telephone instruments and thus permitting a reduction in the size of the conductors in cables, i.e., a reduction in capital requirements in exchange lines.

In the third rank, as shown in chart 6 [not printed in RECORD], the coefficients for land and buildings trace out an underlying pattern which was high in the twenties, low

in 1914-17 and 1940-41, and rising after World War II. This pattern arose from policy decisions as well as technological developments. The high level of the coefficients in the prosperous twenties (especially 1929 and 1930), and the low level in the post-depression years, were due partly to a program of constructing large administration buildings and making general improvements in architectural design, which was carried through in the twenties but later curtailed. The low level of coefficients in later years was also partly a result of the technological trend to smaller and more compact central office equipment, reducing capital requirements in land and buildings.

The coefficients for station equipment, chart 7 [not printed in RECORD], trace out an underlying pattern in variation which reflects the technological change from desk sets to hand sets, starting in 1927 and continuing through the thirties. The coefficients rose somewhat in the late twenties and continued at this level in 1940-41. The lower level prevailing after World War II is more difficult to explain, however. Perhaps it is due to the fact that the actual transition from desk sets to hand sets had been virtually completed.

The coefficients for toll lines shown in chart 8 [not printed in RECORD], have been less stable from year to year than those for any other type of capital equipment. This reflects the lumpy character of investment in toll lines. Insofar as an underlying pattern of variation can be discerned, however, it is in accord with the known changes in technology. The rise of the coefficients in the late twenties was due fundamentally to the technological solution of the problem of long-distance transmission over cables; although, more immediately, to a policy decision to undertake general replacement of open wire by aerial and underground cable at this time, and to provide a complete cable network in the northeastern part of the country. The technological change raised the underlying pattern of the coefficients, since cable requires more investment than open wire; while the concentrated replacement program raised the annual coefficients to the extraordinary peak of 1929 and 1930. The subsequent lower level of the coefficients before and after World War II reflects a second technological change, the development of carrier systems of transmission, which markedly reduced the amount of outside plant required for each toll circuit.

TABLE 5.—Central office equipment: Calculation of retirement coefficients

Year	Retirement	Stock of central office equipment	Retirement coefficient ¹
	(1)	(2)	(3)
	Thousands	Millions	
(1) 1915.....	\$758	\$25.65	-----
(2) 1916.....	675	27.00	0.02632
(3) 1917.....	272	29.76	.01007
(4) 1918.....	715	32.95	.02403
(5) 1919.....	663	36.91	.02012
(6) 1920.....	710	43.16	.01924
(7) 1921.....	1,464	51.86	.03392
(8) 1922.....	757	72.87	.01460
(9) 1923.....	892	100.47	.01224
(10) 1924.....	1,768	154.05	.01760
(11) 1925.....	2,721	178.34	.01766
(12) 1926.....	3,639	190.61	.02040
(13) 1927.....	30,712	178.81	(2)
(14) 1928.....	7,461	186.39	.04173
(15) 1929.....	5,811	204.91	.03118
(16) 1930.....	7,822	220.39	.03817
(17) 1931.....	14,298	230.68	.06488
(18) 1932.....	20,345	230.50	.08820
(19) 1933.....	13,306	231.29	(3)
(20) 1934.....	4,949	230.49	.02140
(21) 1935.....	6,756	227.42	.02931
(22) 1936.....	2,779	227.63	.01222
(23) 1937.....	5,093	231.34	.02237
(24) 1938.....	7,016	237.74	.03033
(25) 1939.....	10,952	235.88	.04607
(26) 1940.....	8,434	238.51	.03576

Footnotes at end of table.

TABLE 5.—Central office equipment: Calculation of retirement coefficients—Continued

Year	Retirement	Stock of central office equipment	Retirement coefficient ¹
	(1)	(2)	(3)
	Thousands	Millions	
(27) 1941.....	\$4,621	\$244.50	.01937
(28) 1942.....	3,457	249.98	.01414
(29) 1943.....	1,084	252.52	.00434
(30) 1944.....	858	254.30	.00340
(31) 1945.....	1,179	258.02	.00464
(32) 1946.....	1,433	275.06	.00555
(33) 1947.....	2,590	340.50	.00942
(34) 1948.....	3,365	243.84	.00988

¹ Calculated from formula (col. 1) ÷ (col. 2 previous year × 1,000).

² Omitted because affected by change in area of operations in 1927.

³ Omitted because affected by accounting change between 1932 and 1933.

Source: Cols. (1), and (2), Federal Communications Commission, unpublished reports of New York Telephone Co.

To sum up, the statistical capital and spare-capacity coefficients for the various types of capital equipment reveal both year-to-year fluctuations and underlying patterns of variation over the entire period. The annual fluctuations are at variance with the capital-requirements theory, but do not seem to be sufficient to reject the theory for the more important types of capital equipment. The underlying patterns of variation, on the other hand, are in general consistent with the known timing and direction of technological developments. All in all, this statistical analysis seems to lend considerable support to the second basic hypothesis of the capital-requirements theory—that net investment depends, via fixed capital and spare-capacity coefficients, upon changes in expected demand.

D. Calculation and evaluation of retirement coefficients

In the third part of the quantitative analysis, annual retirement coefficients for the various types of capital equipment are derived, and the stability of the historical course of the statistical coefficients is examined. The capital-requirements theory assumes that retirement is a fixed fraction of the stock of capital equipment; therefore these coefficients should be essentially stable over the period studied, though perhaps modified by technological changes.

The essence of the statistical procedure is to take ratios between the retirement in each year and the stock of capital equipment in use at the end of the previous year; thus the coefficients are stated in pure numbers. Several aspects of the detailed procedure should be pointed out, however. Since statistical series for retirement by types of capital equipment are not available for the Bell System or for the industry as a whole, series have been compiled for the New York Telephone Co., the largest unit in the Bell System, from unpublished reports made to the Interstate Commerce Commission and the Federal Communications Commission. The classification of capital equipment is somewhat different from that used previously. Four types are essentially the same—central office equipment, land and buildings, station equipment, and other plant.

Outside plant, however, which previously was divided between exchange lines and toll lines, is divided here among aerial wire, aerial cable, underground cable, pole lines, and underground conduit. The series are all stated in value terms. The value of the stock of capital equipment is essentially the sum of the original values, at the time they

were first installed, of the various units still in service; no adjustment is made for depreciation. The value of retirement is essentially the original value of the units retired. Unfortunately these value series cannot be deflated, because information regarding the dates at which the retired units were originally purchased is lacking. The year 1927 has been omitted because in that year the New York Co. transferred its properties in northern New Jersey, containing 10 to 30 percent of the various types of capital equipment, to a wholly owned subsidiary, which later became the New Jersey Bell Telephone Co. The years 1933, in some cases 1937, and in other cases 1933–37, have been omitted because of changes in accounting definitions in those years. The entire procedure is illustrated in table 5 for central office equipment.

In algebraic terms, the third basic hypothesis of the capital-requirements theory is

$$(7, 13)$$

$$-R_{t+1} = -\rho^a K_t$$

Using undeflated value series for a single telephone company, the statistical retirement coefficients are calculated from

$$(7, 16)$$

$$-U_{t+1} = -\rho^a V_t$$

in which

U = the value of retirement, and

V = the value of the stock of capital equipment.

The historical course of the resulting statistical coefficients can be seen in charts 9 through 13 [not printed in RECORD]. In general the retirement coefficients fluctuate quite widely from year to year, indicating that annual retirement is subject to considerably more managerial discretion than the capital requirements theory suggests. All of the calculated coefficients, for example, fell very low during World War II, when new equipment was difficult to get for replacement; and most remained low in the postwar period, when new equipment was used mainly for expansion. These year-to-year fluctuations are associated with the fact that the coefficients for most types of equipment are very small, indicating that the equipment is quite durable, and hence that there is scope for discretionary variation of retirement. Some of the fluctuations are also associated with the technological changes which are known to have occurred in this period. On the other hand, there appears to be some tendency for the year-to-year fluctuations to center around certain normal levels, even though the stocks of capital equipment increased manyfold over the entire period. This suggests that there may be a longrun tendency for retirement to be a certain fraction of the capital stock.

Turning to the individual types of capital equipment, the two types which have the most stable retirement coefficients from year to year and are most consistent with the capital-requirements theory are station equipment and other plant. It is significant that these two types also have the largest retirement coefficients. This supports the generalization that the less durable a type of equipment, the less scope there is for varying its retirement. Moreover, because large fractions of station equipment and other plant are retired in each year, replacement investment for these two types is more important than net investment. The statistical coefficients for station equipment are shown in chart 9 [not printed in RECORD]. The normal level of these coefficients seems to have varied, rising to a higher level beginning in 1928 and continuing through 1940. This reflects the technological transition from desk sets to hand sets in these years. The statistical coefficients for other plant are plotted in chart 9 [not printed in RECORD].

The normal level of these coefficients seems to have fallen from about 15 percent in the twenties to about 11 percent in the thirties.

The retirement coefficients for central office equipment, chart 10 [not printed in RECORD], are among the most variable from year to year, and the least consistent with the capital-requirements theory. This may be explained by the fact that retirement of central office equipment is due largely to obsolescence, and is primarily affected by policy decisions regarding the rate of introduction of technological improvements. Thus retirement was increased from 1928 to 1932 as a result of an accelerated program of replacing manual with automatic switchboards; whereas in the 8 years 1921–27 dial service had been introduced in 46 central offices, in the 4 years 1928–31 dial service was installed in 70 central offices.⁹ An additional reason for increasing retirement in 1931 and 1932 was to reduce maintenance and operating expense by abandoning manual equipment no longer needed in view of the fall in demand. Over the entire period from 1915 to 1948, however, in which the value of central office equipment increased about 16 times, the statistical coefficients appear to have some tendency to center around a normal level of about 2½ percent. The retirement coefficients for land and buildings, as shown in chart 10 [not printed in RECORD], trace out a pattern of annual fluctuations similar to that of the coefficients for central office equipment, since this type of telephone plant consists mainly of buildings to house the central office equipment. The peak of retirement in 1929, however, was due to the transfer of many administrative and operating functions to a single new building in that year, and the normal level of the coefficients seems to have been about 1 percent.

The retirement coefficients for aerial wire, aerial cable, and underground cable reflect an interesting way the technological change which took place in this period from open wire to cable, both aerial and underground, and from aerial conductors, both wire and cable, to underground cable. These coefficients are plotted in charts 11 and 12 [not printed in the RECORD]. In 1929 and 1930 the coefficients for both aerial wire and aerial cable rose well above normal, while the coefficients for underground cable did not. Then in 1931 and 1932 the coefficients for aerial wire remained high, while the coefficients for both aerial and underground cable fell. Over the entire period the coefficients for aerial wire were in the order of 8 percent, and in contradiction to the capital-requirements theory, fluctuated markedly from year to year. The coefficients for both aerial cable and underground cable were in the order of 2 percent, and were also more stable, particularly after 1938.

Pole lines, aerial wire, and aerial cable are complementary types of capital equipment, and hence the retirement coefficients for pole lines, as shown in chart 12 [not printed in the RECORD], trace out a pattern of annual fluctuations similar to that of the coefficients for aerial wire and aerial cable. Over the entire period from 1915 to 1948 the normal level of the coefficients appears to have been about 5 percent, and except for 1921 the annual fluctuations are reasonably compatible with the capital-requirements theory. Underground conduit and underground cable have a similar complementary technological relationship, but annual retirement in these 2 types is not so closely related because the conduit is about 10 times as durable as the cable. As set forth in chart 13 [not printed in the RECORD] (note the change in

⁹ New York Telephone Co., annual reports, 1928, p. 5; 1929, p. 5; 1930, p. 6; 1931, p. 8.

scale), the retirement coefficients for conduit were in the order of 0.2 percent in most years. Moreover, because of this durability the coefficients were more erratic from year to year than the coefficients for any other type of equipment, and hence less consistent with the capital-requirements theory.

In sum, the statistical retirement coefficients for the various types of capital equipment exhibit varying degrees of year-to-year fluctuations in the period studied. Station equipment and other plant are most stable; underground conduit, aerial wire, central office equipment, and land and buildings are least stable; and pole lines, aerial cable, and underground cable are intermediate. These fluctuations reflect the managerial discretion which enters retirement decisions, but which is abstracted from in the capital-requirements theory. Such discretion is inversely related to durability, and hence it is important that all types but station equipment and other plant are quite durable. On the other hand, over the period as a whole, while large increases in stocks of capital equipment were taking place, normal levels of the coefficients can in general be discerned. Thus there may be a long-run tendency toward normal retirement. All in all, however, this calculation of statistical retirement coefficients lends only limited support to the third basic hypothesis of the capital-requirements theory—that retirement depends, via a fixed coefficient, upon the existing stock of capital equipment.

V. CONCLUSION

This study points to one main conclusion—that the capital-requirements theory is a useful explanation of certain fundamental features of the investment process in the telephone industry. The hypothesis that demand estimates depend upon a fixed expectations coefficient is supported by the importance of trend extrapolation in the Bell System procedures, and also by the one short series of actual demand estimates. The hypothesis that net investment depends upon fixed capital and space-capacity coefficients is supported by the policy of building ahead of demand and the essentially rigid engineering relationships in the Bell System procedures, and also by the consistency of the statistical capital and space-capacity coefficients with the known technological developments in the period studied. The hypothesis that retirement depends upon fixed retirement coefficients, on the other hand, is supported to only a limited degree, largely because of the durability of most of the capital equipment in the industry.

An important question is the extent to which the capital-requirements theory can be extended to other industries. It should be recognized that the telephone industry has three important characteristics which are favorable to the theory. First, its productive process is heavily capital-intensive, with little scope of substitution of other inputs, and its product cannot be produced for inventory. This means that investment decisions are dominated by essentially rigid technological relationships. Second, the demand for telephone service has risen steadily and rapidly throughout the history of the industry, so that investment designed to expand capacity has bulked large in the investment program, technological improvements have been introduced primarily as alternative techniques for expansion, and it has been economical to build ahead of demand. Third, the telephone industry is essentially a monopoly, and is subject to public utility regulation. Its investment is little affected by the reactions of oligopolistic rivals, and must be adequate to meet demand at commission-determined prices.

These favorable characteristics, however, are clearly not limited to the telephone industry. The other public utilities, which

together provide a significant fraction of total investment in our economy,¹⁰ are similar in most of these respects. Many manufacturing industries as well as characterized by capital-intensive productive processes, historically rising demand, and nonaggressive market structures. Therefore, although each industry should be examined individually, it seems probable that the capital-requirements theory can be extended to a considerable number of other industries.¹¹

Moreover, insofar as this study of telephone investment can be generalized, it indicates that the capital-requirements theory can justifiably be used in integrating investment and disinvestment in capital equipment into the interindustry input-output scheme. The study has two implications for the resulting dynamic analysis, however. First, the theoretical coefficients were found to be more stable over periods of several years than in any single year, in which managerial discretion may affect investment. Therefore the dynamic input-output analysis itself will be more useful in determining what is required to accomplish a specified increase in total outputs over periods of several years than over a single year. Second, the coefficients were significantly altered by technological developments, which indicates, particularly when analysis is focused on periods of several years, that the most up-to-date engineering advice should be sought in calculating the coefficients, in order to make allowance for technological changes which are on the verge of being introduced. If these implications are recognized, however, this study of telephone investment offers a basis for hope that the capital-requirements theory can be successfully used in developing a dynamic input-output analysis.

¹⁰ See ch. 6, sec. 4, table 9.

¹¹ Throughout this chapter I have referred to the capital-requirements theory, meaning the particular theory tested here against the investment practice in the telephone industry. By modifications of particular assumptions, of course, it is possible to develop other variants within the general family of capital-requirements theories; and in extending the theory to other industries, such modifications may be desirable. The particular assumptions which I consider central to any capital-requirements theory are that investment depends upon expected output relative to capacity, that there are fixed technological coefficients relating changes in capacity to changes in stocks of capital equipment, and that negative net investment is limited by the durability of capital equipment to feasible retirement. On the other hand, modified assumptions can readily be introduced regarding the formation of demand expectations, the variability of margins of spare capacity, and the determination of retirement. For an example of another formulation within the family of capital-requirements theories, applied to a number of industries, see Hollis Chenery, "Overcapacity and the Acceleration Principle," *Econometrica*, January 1952. The principal difference between his capacity principle and the capital-requirements theory developed here is that in his formulation net investment depends upon a certain fraction of the difference between output and normal utilization of capacity, so that the margin of spare capacity varies from year to year, approaching the normal margin as a goal; while in my formulation net investment depends upon the entire difference between output and normal utilization of capacity, so that the margin of spare capacity is constant from year to year. The choice between the two versions for particular industries probably depends primarily on whether demand has fluctuated seriously or has risen steadily in the past.

COURTS WOULD NOT PERMIT INVESTMENT CREDIT TO INCREASE PROFIT INCENTIVE

Mr. PROXMIRE. Mr. President, as I have said, utilities as regulated monopolies are afforded opportunities to earn a just and reasonable rate of return. The rate of return is set to assure a return on capital and to attract whatever capital is needed to serve public convenience and necessity. The rate of return is arranged to obtain the necessary capital at whatever cost is required. So that it is very difficult to see how an investment credit under any circumstances could provide an incentive. In fact, the opinions of courts in several cases with respect to regulating utilities make clear that they do not intend to permit the utility to get the benefit of any such provision as the investment credit.

I call attention particularly to the opinion by the Pennsylvania Superior Court in the case of city of Pittsburgh against Pennsylvania Public Utilities Commission:

Counsel asserts that, since utilities are an important segment of the national economy, they must likewise benefit. The weakness in this assertion is in failing to recognize the distinct nature of a utility as a regulated quasi-monopoly. As such it may obtain funds for modernization and expansion at the current reasonable cost, and it is allowed to pass this cost on to its customers in an annual depreciation allowance and its annual allowable net return as well. In fixing the rate of return the commission takes cognizance of the cost of capital to the utility. It appears therefore that this general desire of Congress to provide working capital and funds for modernization and expansion is, and has been for many years, adequately met for public utilities through rate proceedings.

This, of course, referred to the accelerated depreciation provision in the Revenue Code, which was put into effect in 1954.

Similarly, the Supreme Court of Illinois said in the case of city of Alton against Commerce Commission:

Under the policy of this State, utilities are allowed a rate of return calculated to attract the capital required for necessary expansion. Since in this respect utilities differ from other corporations, the purpose of section 167 would not be thwarted nor would discrimination be introduced into the Federal tax law by requiring utilities to pass the savings of accelerated depreciation on to their customers. Utilities are at least partial monopolies, and no competition exists to induce them to pass savings on to the public.

Therefore it is clear that regulatory bodies, public utilities commissions, treat the corporation income tax of utilities as a cost of operation. If the investment credit is given to utilities, why then should public utilities accelerate their investment in equipment?

The major utility companies recognize the fact that they cannot increase their return by increasing investment as long as public utility commissions are sufficiently alert to see that they get only a specified rate of return.

The utilities and their investors do not bear the burden of the corporation income tax.

The utilities will not raise investment significantly in response to this invest-

ment credit because, in the first place, they are a captive monopoly market; second, they have a guaranteed rate of return; third, they have a ready access to capital funds; fourth, they can raise money whenever they need to expand.

Finally, the need for new investment is determined by consumer demand.

EXPERIENCE WITH QUICKIE WRITEOFFS FOR UTILITIES SHOWS INVESTMENT CREDIT WOULD NOT INCREASE INVESTMENT

Mr. President, fortunately, in this case, we have the experience of the accelerated amortization provision in the tax law, which Congress provided in 1954. That experience showed that it did not work to stimulate the utility industry. As a matter of fact, a critical review was made by the Finance Committee in 1957, on the basis of the experience with the accelerated depreciation in the electric utility field. At that time the chairman of the Committee on Finance, the Senator from Virginia [Mr. BYRD] concluded that the effect had not been to stimulate investment. This is what he said, on page 9 of the hearings before the Committee on Finance on S. 1795:

It seems to me there is no justification whatever for a power utility to get a rapid tax depreciation. They are guaranteed profits.

REGULATION WOULD BE DISCRIMINATORY, CONFUSING AND CONTRADICTORY WITH INVESTMENT CREDIT

It is argued that in some cases utilities may have an incentive, because regulatory bodies may be disinclined to require the utilities to reduce their rate to reflect their increased return flowing from the investment credit. Should utilities be allowed to keep the investment credit in addition to a fair return? I believe that undoubtedly some regulatory bodies may say "Yes." I believe, however, that many, as indicated by the decision in Pennsylvania and the decision in Illinois, and I am sure in other States, would say "No." The result of this would be discriminatory, uncertain, confusing, and would not be in the interest of the country or of the public utility interest.

Certainly any flow-through of this advantage to consumers which is called for by existing law means no incentive. Obviously, if the advantage in increasing income is not permitted by the regulatory body, then there would be no real incentive for the utility to increase its purchases of equipment or machinery.

TREASURY FORESEES WINDFALL FOR UTILITIES FROM INVESTMENT CREDIT

The conclusion of the Treasury is that substantially no benefit to consumers or investors would result from this investment credit to utilities but that there would be an addition to dividends.

This is because there is such a variation and it would be very difficult for regulatory bodies to handle the situation fairly. Under those circumstances it is felt that the utility would not pass through or permit a flowthrough of the investment credit advantage to the consumers. However, there would be a dividend windfall.

I should like to point out the variation in the effect on the consumers in various States and on various utilities.

The rate regulating agency would have to monitor each utility's investment in every year to assure that the company did not earn an excessive return through the investment credit.

I have before me a table which indicates the varying effect on many companies during the period 1958, assuming a 3-percent tax credit. It shows, for example, in the case of the Consolidated Edison of New York, in 1958, the customer benefit would be 83 cents, and the stockholder benefit would be an increase of 1.04 percent on equity. There would be an increase in 1960 of \$1.99 by way of a customer benefit, or 2.17 percent increase return to stockholders.

Detroit Edison, Northern States Power Co., and Pacific Gas and Electric Co., are also listed. In the case of Detroit Edison the variation would be the sharpest. In 1958, the consumer benefit would be \$1.37. In 1960, it would be only 45 cents. In 1958 investors would have gotten an increased return of 1 percent, while in 1960, only two-thirds of 1 percent.

This is typical of all the other utilities on the basis of the table which the Treasury has made available. I ask unanimous consent that the table, shown on page 136 of the hearings be printed in the RECORD at this point.

There being no objection, the material was ordered to be printed in the RECORD, as follows:

Estimated effect of 3-percent-tax credit customer benefit versus stockholder benefit, selected utilities, 1958-60 data

Company	Results whether customer or stockholder gets benefits	
	Customer benefit per year ¹	Stockholder benefit extra return on equity ²
Consolidated Edison Co. of New York:		Percent
1958.....	\$0.83	1.04
1959.....	1.11	1.33
1960.....	1.99	2.17
Northern States Power Co. (Minn.):		
1958.....	.61	.66
1959.....	1.18	1.13
1960.....	1.35	1.32
The Detroit Edison Co.:		
1958.....	1.37	1.00
1959.....	1.14	.84
1960.....	.45	.33
Pacific Gas & Electric Co.:		
1958.....	1.36	1.20
1959.....	.85	.78
1960.....	.81	.76
Appalachian Power Co.:		
1958.....	2.88	2.78
1959.....	.57	.55
1960.....	.57	.54

¹ Average reduction in residential electric bills consequent to rate reductions on residential sales made possible by the investment credit.

² Average percentage point increase in rate of return to equity made possible by passing the investment credit through to stockholders.

Source: Office of the Secretary of the Treasury, Office of Tax Analysis, Apr. 2, 1962.

PASSTHROUGH TO CONSUMERS NEGLIGIBLE AT BEST

Mr. PROXMIRE. Mr. President, it could be argued, I presume, that if this investment credit were passed on to the consumers, what is wrong with that? The consumers would get a cut in their rate bill. Of course, first, this would not be the purpose of the reduction. Second, the cut in the rate bill would be very slight indeed.

Some might argue a cut in the rate would be sufficient to persuade consumers to buy more electricity and to expand our output of electricity or the output of utilities generally. The facts are, on the basis of the Treasury study, that the result of a 3-percent credit would be a 1-percent cut in consumer costs. For example, a monthly residential bill of \$7.20 would be cut by 7 cents. That is a typical average bill. In the case of the average industrial bill, which is approximately \$73, the cut would be only 69 cents.

On the basis of the studies made by Fisher & Kaysen, the demand is relatively inelastic. On this basis it is clear that the increase in demand, the result of any passthrough or flowthrough of this investment credit would be virtually nil.

Would the investment stimulate increasing capacity? The fact is that the level of excess capacity in the utility industry is now higher than at any time since 1940. I call attention to a table on page 137 of the hearings. This table shows that there was a real burden on capacity in the period right after World War II. At that time, in 1947, the indicated reserves—that is, the excess over the December peakload as a percentage of the peak—was only 1.2 percent. Since then, in every year, the capacity in proportion to demand has increased, until in 1960 the percentage of excess was 28.6 percent in December. This is, of course, the month in which there are heavy demands on utilities. So the most recent figures show a 28.6 percent and increasing excess capacity. Under those circumstances, it is obvious that the level of excess capacity is so high that any investment credit would be unlikely to stimulate capacity significantly.

While I disapprove of investment credit generally, I think it is possible it may have some stimulation of investment in equipment in competitive manufacturing industry. I think that the exclusion of buildings was wise and a good provision. It saved revenue and eliminated providing overproduction through an investment credit tax cut for buildings, which obviously would not have stimulated our growth significantly.

I ask unanimous consent to insert at this point in the RECORD a table entitled "System Capacity and Peakloads."

There being no objection, the table was ordered to be printed in the RECORD, as follows:

System capacity and peak loads, 1940-60,
U.S. totals for major systems

End of year	Dependable (adverse water year)	December peak loads	Indicated reserves (excess of depend- able over December peak load as percent of peak)
	Kilowatts	Kilowatts	
1940	34,403,434	27,948,071	23.1
1941	37,353,709	31,531,206	18.3
1942	39,665,335	32,942,464	20.4
1943	42,416,767	37,060,061	14.5
1944	43,760,322	37,853,847	15.6
1945	45,373,031	37,368,925	19.8
1946	45,701,894	43,173,803	5.9
1947	48,146,326	47,554,537	1.2
1948	52,689,808	51,611,873	2.1
1949	59,285,449	54,238,069	9.3
1950	65,574,230	61,719,096	6.2
1951	72,687,954	67,869,836	7.1
1952	80,035,407	73,055,403	9.6
1953	89,802,220	78,592,567	14.3
1954	102,055,254	85,580,848	19.3
1955	114,612,107	98,291,077	16.5
1956	120,453,230	102,723,432	17.3
1957	128,325,252	107,388,343	19.5
1958	141,827,422	113,679,341	24.8
1959	154,537,818	121,561,163	27.1
1960	165,536,249	128,713,483	28.6

Source: June 1961 issue of FPC "Electric Power Statistics."

Mr. PROXMIRE. In the same way, it seems to me, if we exclude utilities, as my amendments advocates, we follow the same course as we did in excluding buildings.

INVESTMENT CREDIT FOR UTILITIES COULD NOT IMPROVE COMPETITIVE POSITION WITH OTHER NATIONS

The principal purpose of investment credit, as argued by the Secretary of the Treasury and the proponents of the measure on the floor, was that it would improve our competitive position with foreign countries. Is this principle applicable to utilities? Are Detroit Edison Co., or the big utilities in my State of Wisconsin, or the utilities in Oklahoma or New York, competitive with utilities in Europe or in any other part of the world? Obviously, they are not. No persuasive argument can be made, particularly in view of the fact that there is likely to be little, if any, flowthrough to the consumer, that such an investment credit will help us compete abroad. Industry buying power would not benefit because the record shows no flow through.

Would industry construct its own utilities to take advantage of the credit? That is a legitimate fear on the part of the utility industry. The utility industry believes that if it cannot get investment credit for constructing generators and such facilities, perhaps industry would step in to take advantage of its own tax position to increase its utility capacity. An excellent study by the Treasury Department, which is on page 139 of the hearings, shows that the trend in utilities has been in exactly the opposite direction.

I ask unanimous consent that this table be printed at this point in the RECORD.

There being no objection, the table was ordered to be printed in the RECORD, as follows:

Generating capacity, privately owned electric utilities and industrial establishments, 1939-60

[In thousands of kilowatts]				
Year	Com- bined capacity	Privately owned utilities capacity	Industrial estab- lishments	
			Capacity	Percent of com- bined capacity
1939	44,483	33,908	10,575	24
1940	45,433	34,398	11,035	24
1941	47,631	36,041	11,590	24
1942	49,626	37,442	12,184	25
1943	51,717	39,128	12,589	24
1944	52,610	39,733	12,877	24
1945	53,064	40,307	12,757	24
1946	53,104	40,355	12,749	24
1947	54,816	41,987	12,829	23
1948	58,436	45,381	13,055	22
1949	63,954	50,484	13,470	21
1950	69,106	55,175	13,931	20
1951	74,544	60,192	14,352	19
1952	79,435	64,349	15,086	19
1953	87,063	71,201	15,862	18
1954	95,413	79,127	16,286	17
1955	103,311	86,887	16,424	16
1956	107,790	91,145	16,645	15
1957	114,474	97,376	17,098	15
1958	126,256	108,202	18,054	14
1959	136,510	118,999	17,511	13
1960	145,793	128,000	17,793	12

Source: FPC.

Mr. PROXMIRE. Mr. President, beginning in 1939, the industrial establishment had a percentage of capacity of 24 percent of the combined capacity of the utility production. That percentage has declined steadily and relentlessly year after year, until in 1960 industrial establishments had only 12 percent of such capacity, while privately owned utility capacity was 88 percent. There is a reason for this decline in industrial investment in utility production. The reason is the increasing size of generating facilities and their expense, which puts the activity far beyond the desires of most corporations, even the very big corporations, to engage in it.

Second, the life of a facility is 30 years, and the need for the manufacture for utility service and power is highly variable, if not unpredictable.

Furthermore, as the Treasury calculates, the flow of credit is far less for a 30-year life than for a 10-year life or a 15-year life. So the current trend, as I have pointed out, is in exactly the opposite direction. Many firms now lease production facilities in order to minimize the capital investment required.

The argument is made—and I am sure it will be made in opposition to my amendment—that utility investment credit would help the smaller utilities. Would it? The Treasury shows that there is no support for this contention at all.

GIANT UTILITIES GET 80 PERCENT OF INVESTMENT CREDIT BENEFITS

First, 80 percent of the investment by utilities is made by the giants, by the big utilities, by those which have assets of more than \$250 million—more than a quarter of a billion dollars. Those are the firms which would get the lion's share of the benefit from a tax credit. Let us consider the smaller utilities, which are very small in relation to the

giants, and have assets of from \$5 to \$50 million. The fact is that they now enjoy a substantially higher return. The Treasury points out that there is no support for the argument that the small utilities because they earn less would get the principal benefit. The utilities having assets of from \$5 to \$50 million enjoy a rate of return of from 10 to 20 percent higher, on the average; so it is clear that the smaller utilities do not need such an advantage.

Mr. GORE. Mr. President, will the Senator from Wisconsin yield?

Mr. PROXMIRE. I am glad to yield to the Senator from Tennessee.

Mr. GORE. Does the Senator's amendment cover all utilities? Does it cover not only electric utilities, but oil and gas pipelines, as well?

Mr. PROXMIRE. My amendment covers utilities as defined in the bill at the present time; for that reason it does not cover gas pipelines. The reason why it does not include gas pipelines is that gas pipelines are now given a 7-percent credit.

Mr. GORE. In the bill?

Mr. PROXMIRE. That is correct. I think that the granting of such a benefit is wrong. I believe gas pipelines should be treated as are all other utilities.

My first amendment is directed to the elimination of the 3-percent provision as it applies to utilities. Following that, as soon as I can get the floor, I shall offer an amendment to give the same treatment to gas pipelines as all other utilities receive. If my amendment is agreed to, I shall move to withdraw investment credit entirely for pipelines. If my first amendment fails, I shall move to treat gas pipelines on the same basis with other regulated utilities.

Mr. GORE. I am sure the Senator has good reasons for a division of the question, one reason being that a utility is by definition under the bill confined to electric and similar utilities.

Mr. PROXMIRE. Including a telephone utility.

Mr. GORE. Yes. To put it another way, by definition the term "public utility" does not include gas and oil pipelines.

Mr. PROXMIRE. That is correct.

Mr. GORE. Would the Senator consider possibly combining his two amendments, so that by this vote the Senate would have an opportunity to strike from the bill investment credit for all public utilities?

Mr. PROXMIRE. I should prefer to treat it as I am proposing. I think the case is overwhelming for removing the tax credit from both industries; but I cannot imagine an argument for giving gas pipelines special treatment as distinguished from other utilities. The Secretary of the Treasury made a statement which I should like to use when I call up my other amendment, a statement which is irrefutable, in which he points out that the case for gas pipelines getting credit is the weakest of all. I should

prefer to make that argument later, because I feel that if there is any chance of this amendment being adopted, there will be very little trouble adopting a similar amendment with respect to gas pipelines. On the other hand, I think I may have trouble in having this amendment agreed to, since the committee rejected it. So if it should fail, I feel that I would have a chance to have an amendment adopted to reduce the investment credit for pipelines, and thus reduce the revenue loss to the Treasury by some \$30 million.

Mr. GORE. Does not the Senator find interesting the argument which the proponents advanced for giving an investment credit benefit to regulated utilities, to the effect that the benefits would be passed on to consumers? If, indeed, the benefits were passed on to consumers, where would be the alleged incentive for expansion?

Mr. PROXMIRE. The Senator from Tennessee could not be more correct. In the first place, the pass-on, on the basis of this careful analysis, which no one refutes would certainly be less than 1 percent of the cost to consumers; and there is no evidence that a pass-on of 1 percent of cost to consumers would increase consumers' demand. In fact, studies show exactly the contrary—namely, that there would be no significant increase in consumers' demand if their costs were cut by 1 percent.

Mr. GORE. Has not the trend in utility rates been constantly upward?

Mr. PROXMIRE. There is no question about that. The distinguished Senator from Montana [Mr. METCALF] put in the RECORD the other day a perfectly shocking exhibit, from the Federal Power Commission, showing that in some parts of the country utilities are allowed to earn, as a fair return, as much as 8 or 9 percent on their capital—on their riskless investment—although they can borrow money for a fraction of that. As a matter of fact, the Senator from Montana pointed out, in his excellent statement, that some utilities are now considered growth stocks—those which are regulated by public utility commissions which are so feeble in their regulation that the utilities are allowed to earn in excess of a fair return. Of course, on the principle of leverage, it is then possible for the common stockholder to get a return of 15 to 20 percent on his investment.

Mr. GORE. Then the Senator from Wisconsin thinks that in practical effect the benefits of this investment credit to utilities will flow, not to the consumers, but into the coffers and the improvement of the cash position of the utilities themselves, and thus to the stockholders?

Mr. PROXMIRE. I think that will be exactly the situation. As the Treasury points out, the reason why this kind of advantage for the stockholders will not be reflected in additional investments is, the uncertainty as to whether the regulatory body will act. In many cases they will not act and the investment credit will be a windfall.

Actually, the reason why this investment credit should not, in principle, af-

fect the utility's incentive to make further investments is very simple; it is because the investment credit can only provide an incentive by acting to reduce the corporation income tax. But under the law in every State in the Union the corporation income tax is considered a cost of business to the utility, and it is allowed to earn a fair return after the corporation income tax is deducted. So if the corporation income tax is reduced through the investment credit, and therefore the utility's costs are reduced, its prices should be reduced, at least, and its return is reduced, and it gets no benefit, and has no incentive.

Mr. GORE. Mr. President, will the Senator from Wisconsin yield again to me?

Mr. PROXMIRE. I yield.

Mr. GORE. I wonder whether the American people—the overwhelming majority of whom are busy in their daily walks of life—have stopped to realize that Congress has been cutting away at taxes since 1954, and I wonder whether they realize just who has been getting these tax cuts. In view of the myriad of problems with which Congress is faced, sometimes I wonder whether all Members of the Senate have stopped to take stock and to consider to which particular group the benefits of the tax cuts have been flowing.

If the Senator from Wisconsin will be willing to have me intrude for just a moment upon his time—

Mr. PROXMIRE. Mr. President, I am delighted to yield for that purpose to the Senator from Tennessee.

Mr. GORE. As I said, I doubt that many have realized the extent to which taxes have been cut since 1954. This is true because the tax cuts are often disguised, and therefore generally are not recognized.

In 1954, accelerated depreciation was allowed by Congress. It resulted in an initial loss of revenue to the Government of about \$2 billion a year. That benefit accrued largely, of course, to corporations. About \$4 billion was shifted from the profit side of the ledger—and therefore taxable—to the depreciation side. That benefit accrued indirectly to the owners of corporate stock.

Also in 1954, the \$50 dividend exclusion and the 4-percent dividend credit were enacted. They gave about \$400 million a year directly to the owners of corporation stock.

Just this summer the Treasury Department finally issued its long-awaited revision of Bulletin F, permitting shorter lives and other changes in depreciation procedures. It has been estimated that this will reduce the taxes of business—largely corporations, and largely the large corporations—by about \$1.5 billion a year.

These changes, instituted since 1954, have reduced the Government's revenues by about \$4 billion a year. This amount of tax reduction has gone largely, directly or indirectly, to the owners of the stock of the country's corporations.

If the Senate were now to approve the proposed investment credit, it would give the same beneficiaries another \$1.3

billion. This would run up the ante to more than \$5 billion a year—and I emphasize "a year"—in tax reduction for this special group.

Who are these people? One answer might be that they are the 15 million people in the United States—7½ million families—who own some amount of common stock. But such an answer would be somewhat misleading, because most of them own very little stock. Stockownership is concentrated in the high income groups. Only 2 percent of the Nation's families with incomes of less than \$7,500 a year own as much as \$5,000 worth of stock, which could be expected to return to them about \$20 a month in dividends.

Any tax "breaks," then, associated with corporations must eventually be of the most benefit to those in the upper income groups. The ordinary consumer profits little. The benefits to the whole economy are minimal, because demand is not enhanced appreciably in this way.

This is the old, wolfish, "trickle down" theory dressed up in a sheep's coat.

I thought the distinguished Senator from Wisconsin would like to have this summation of the tax-cutting movement in which the Congress and two administrations have been involved for 8 years now, and bring it into focus, showing that more than \$5 billion in tax reduction per year has already been given, or by this bill will be given, to a very small percentage of the people.

Mr. PROXMIRE. What the Senator has said just could not be more timely. It is exactly the point I am trying to make. The Senator has documented the historical situation so well. Is it true that the \$5 billion tax cut—

Mr. GORE. Per year.

Mr. PROXMIRE. Per year. Is it true that none of it goes to the ordinary taxpayer or ordinary citizen? In other words, the man who is getting \$600 a year exemption for his child still gets no more. Prices are higher. Taxes for other people are lower. But he still gets only a \$600 exemption.

Mr. GORE. I point out that this is a \$5 billion tax cut per year.

Mr. PROXMIRE. Five billion dollars, and none of it goes to the benefit of the ordinary taxpayer, as I have said.

Mr. GORE. I point out one other thing. Very little of such tax cut is the kind of tax cut that we generally regard as stimulative of consumer demand.

Mr. PROXMIRE. That is correct. My proposal, which would eliminate the investment credit for utilities, in the judgment of outstanding economists, the experts in the Treasury Department, the Secretary of the Treasury, the President of the United States, all of whom approve my amendment on the basis of their testimony, would not reduce investments at all, but would save \$225 million for the Treasury.

Mr. GORE. Mr. President, will the Senator yield for a question?

Mr. PROXMIRE. I yield for a question.

Mr. GORE. Does the Senator find it disturbing that the same group of people who with glee propose, endorse, accept,

and vote for this enormous annual tax reduction for the benefit of a minuscule percentage of our people who own corporation stock hold up their hands in horror and shout "fiscal irresponsibility" when someone proposes to bring within some reasonable proximity of the cost of rearing and educating a child, a personal exemption which is now held down to \$600 despite the increase in the cost of living and education?

Mr. PROXMIRE. The Senator is so right. There is no question about it. Who can educate a child on \$600 a year?

The investment credit for utilities is almost certain to result in a windfall to the stockholders, according to the Treasury. This is the Treasury itself saying this; it is not the argument of the Senator from Wisconsin, but the argument made before the Finance Committee. The utilities already have access to capital, and therefore there is no real backlog of investment which they can increase if they can get access to more funds. They have all the funds available that they need.

Temporarily, at least—in the long run they may be required to do so—I doubt that many public utility commissions are going to change their concept of what is a fair return. This is why some of the outstanding utilities oppose investment credit. They, themselves, oppose it.

INVESTMENT CREDIT NOT NECESSARY FOR COMPETITIVE PROTECTION TO UTILITIES

Will the competitive position of utilities suffer in relation to other energy suppliers? This is another argument the Treasury considered very carefully, and found that the answer was "No." In the first place, conversion costs are prohibitive. In the second place, the utility is independent of other energy suppliers. Competition is very peripheral or nonexistent. The Treasury argues that this investment credit for utilities is not appropriate, because they are guaranteed a return. They are insulated, in effect, from the corporation income tax. The corporation income tax can have no real effect on its return, by law.

Mr. GORE. Mr. President, will the Senator yield?

Mr. PROXMIRE. I yield to the Senator from Tennessee.

Mr. GORE. Some persons seem to be of the impression that a 3-percent investment credit is, after all, "small potatoes" and does not mean very much. I call to the Senator's attention the fact that a 3-percent investment credit for Consolidated Edison, based upon its 1962 spending estimate, which is public information, considering plans underway, plans already executed, construction already being achieved, would amount to a tax reduction of 21.9 percent of that corporation's 1961 income tax. It seems to me that this fact should serve to open some eyes as to the amount of tax reduction for utilities which the 3-percent investment credit would give.

I direct the Senator's attention to another company. Alabama Power Co. would have a tax reduction of 13.3 percent by this 3-percent investment credit.

Going near the Senator's part of the country, the Montana-Dakota Utilities would receive a tax reduction of 16.9 percent by this 3-percent investment credit.

Mr. PROXMIRE. If the Senator will yield at that point, because the distinguished junior Senator from Montana [Mr. METCALF] is here, the Senator to whom I referred a few moments ago, on the basis of the brilliant statement he made the other day to the effect that Montana Power Co. was getting 9 percent on its investment capital—

Mr. METCALF. Nine and three-tenths percent.

Mr. PROXMIRE. Nine and three-tenths percent. In this case if we have public utility commissions which seem to be so lax in terms of arriving at a fair return, there will be no passthrough to consumers of the investment credit, then that 9.3 percent will become 10 or 11 or 14 percent, and with the principle of leverage, since they can borrow at 5 or 6 percent, the common stock return will be almost astronomical.

Mr. GORE. Just before the distinguished junior Senator from Montana entered the Chamber, I had pointed out that the 3-percent investment credit would mean a 16.9-percent reduction in taxes for the Montana-Dakota Utilities.

Mr. METCALF. Does the Senator from Tennessee have figures for the Montana Power Co.?

Mr. GORE. I am not sure that I have.

Mr. METCALF. The Montana Power Co.'s reduction would be even higher because of the special situation it has in Montana, where it has the highest rate of return, where it is now attempting to build a low run of river dam on the Columbia, instead of the Knowles Dam which would have a full, multipurpose development. Under the tax credit, it could borrow money and get a tax credit benefit as well as these other benefits, and the taxpayer would be paying for underdevelopment.

Mr. GORE. The table from which I

am reading contains a list of some dozen selected utilities. It does not include the Montana Power Co. I am not at all surprised, however, to learn that the Montana Power Co. would receive a tax reduction greater than does the Montana-Dakota Utilities. In fact, the percentages of reduction vary a great deal among companies. Union Electric would receive a 17.2-percent reduction, whereas Virginia Electric and Power would receive a 10-percent reduction in taxes.

Mr. PROXMIRE. I wish to call to the attention of the Senator from Tennessee that my amendment proposes simply the elimination of the investment credit for utilities. This has been recommended by the Secretary of the Treasury, by the Kennedy administration. It would not touch the remainder of the investment credit. It would put the provision much closer to the form in which the administration recommended it. And it would save \$225 million.

Mr. GORE. Mr. President, will the Senator yield further?

Mr. PROXMIRE. I yield to the Senator from Tennessee.

Mr. GORE. I wish to emphasize that the pending legislation is not to be temporary legislation. It is proposed to give this kind of a tax reduction on a permanent basis. In some years the percentage might be much greater than has been stated. If the utilities stepped up their programs, as this country grows, the tax reduction would be even greater, yet some people wish to dispute the proposition that the investment credit is a tax reduction gimmick. I say that unmistakably it is.

I wonder if the Senator would be willing to have this table inserted in the RECORD at this point in his remarks.

Mr. PROXMIRE. That will be perfectly satisfactory. I ask unanimous consent that the table may be printed in the RECORD at this point.

There being no objection, the table was ordered to be printed in the RECORD, as follows:

Investment tax credit—What it will mean in new tax cut subsidies to selected¹ private power companies

	1962 capital spending estimate	Tax cut under 3-percent tax credit	1961 Federal income taxes	3-percent tax credit as percent of 1961 Federal income tax
Alabama Power.....	\$52,000,000	\$1,560,000	\$11,712,267	13.3
Consolidated Edison.....	270,000,000	8,100,000	36,600,000	21.9
Consumers Power.....	80,000,000	2,400,000	32,965,048	7.3
Delaware Power & Light.....	18,000,000	540,000	4,466,974	12.1
Florida Power & Light.....	70,000,000	2,100,000	34,089,342	6.2
Louisiana Power & Light.....	16,500,000	495,000	6,446,257	7.7
Long Island Lighting.....	² 57,000,000	1,710,000	16,060,000	10.6
Montana-Dakota Utilities.....	18,000,000	540,000	3,190,000	16.9
Northern Indiana Public Service.....	³ 39,500,000	1,185,000	13,600,000	8.7
Ohio Power.....	34,500,000	1,035,000	9,549,000	10.8
Oklahoma Gas & Electric.....	19,000,000	570,000	8,130,000	7.0
Potomac Electric Power.....	53,000,000	1,590,000	9,550,074	16.7
Public Service of Colorado.....	76,000,000	2,280,000	13,653,000	16.7
Public Service Electric & Gas, New Jersey.....	120,000,000	3,600,000	36,821,386	9.8
South Carolina Electric & Gas.....	16,900,000	507,000	3,667,000	13.8
Union Electric.....	62,000,000	1,860,000	10,787,536	17.2
Virginia Electric & Power.....	82,500,000	2,475,000	24,872,167	10.0

¹ "Selected" only because of availability of company estimates of capital spending in 1962.

² One-half of company's estimate of \$114,000,000 for 1962 and 1963.

³ One-half of company's estimate of \$79,000,000 for 1962 and 1963.

Sources: For figures in col. 1, daily and trade publications; for figures in col. 4, company annual report to stockholders or Federal Power Commission.

Mr. METCALF. Mr. President, will the Senator yield?

Mr. PROXMIRE. I yield to the Senator from Montana.

Mr. METCALF. I think this is very important at the present time, because tomorrow the Committee on Public Works will start hearings on the question of whether or not Knowles Dam should be built on the Clark's Fork of the Columbia River, or whether, in places of Knowles Dam, Buffalo Rapids 2 and 4, two run-of-the-river dams, should be built by the Montana company and used as alternates.

I am very grateful that the Senator has pointed out that if the Montana Power Co. alternate dams, which are purely run-of-the-river and would not provide for complete development of that great resource, are built, and if the 3 percent tax credit is given to utilities, Uncle Sam will help pay for that underdevelopment.

We have heard a lot of criticism about the fact that if Knowles Dam should be authorized it would be built with funds from the Federal Treasury. The Senator from Wisconsin has pointed out that no matter which is authorized, the project would be built with funds from the Federal Treasury, except that in one instance there would be only a partial development while in the other there would be full development, since Knowles Dam would provide multipurpose development, complete and comprehensive development.

Mr. PROXMIRE. The irony of the situation is that the investment credit has been claimed, by those who propose the across-the-board credit, to be a growth stimulant, which would permit the economy to grow, to expand, and to compete more rapidly.

As the Senator from Montana has pointed out, this investment credit, as it would work out, might well enable a private concern to grow less rapidly or less comprehensively than would be the case otherwise.

Mr. METCALF. And the utility, in the process, could make more money for the stockholders, as the Montana Power Co. has done in Montana.

Mr. PROXMIRE. Exactly.

Mr. METCALF. I am very grateful to the Senator from Wisconsin for pointing that out.

Mr. PROXMIRE. I thank the Senator from Montana.

Mr. President, I wish to invite attention of the Senator from Tennessee further to the point that the Appalachian Power Co., for example, on the basis of the Treasury Department calculation, for 1958 would have enjoyed an increase in the return on equity, under the 3 percent investment credit, of 2.78 percent. In other words, if the utility had an 8-percent return, this would mean an increase to nearly 11 percent, to 10.78 percent. This would have been an increase of something like 30 or 35 percent in the return on capital, if the investment credit had been applicable.

Talk about a windfall. I think this reinforces the position so brilliantly established by the Senator from Tennessee.

Mr. President, the Treasury Department is opposed to this provision in the bill, and I think they are absolutely correct. While it is conceivable that there might be, under some isolated circumstances, which are hard for me to envision, some benefits—

Mr. GORE. Mr. President, will the Senator yield for a question?

Mr. PROXMIRE. I yield to the Senator from Tennessee for a question.

Mr. GORE. Will the Senator make plain what it is the administration opposes? The Senator does not mean, does he, that the Treasury Department opposes the amendment which the junior Senator from Wisconsin has offered?

Mr. PROXMIRE. No, indeed.

Mr. GORE. In other words, the administration has opposed the inclusion of public utilities as beneficiaries of the tax credit.

Mr. PROXMIRE. It has, indeed.

Mr. GORE. I refer to the investment credit.

Mr. PROXMIRE. And the administration has done so because, as I point out, there would be a revenue loss of \$225 million, with very little, if any, investment encouraged. Far less growth could be achieved in this manner than could be achieved in almost any other way the Government could spend \$225 million.

As the administration points out, there would be less recoupment of the revenue loss. The argument for the investment credit has been that there might not be a gross tax loss, to the full extent of the credit, because growth would be so increased, revenues generally would expand, and even though there were a loss the effective date in regard to taxes might show an increase.

But, in this case, because it would not stimulate growth, the \$225 million loss would be a total loss.

The Treasury Department has also argued that the utilities' investment credit is almost certain to result in a windfall to the stockholders, as I have said.

A.T. & T., BIGGEST BENEFICIARY, DOESN'T WANT TAX CREDIT

Before I conclude, I wish to refer to another argument. I point out that whereas the proposal would result in a reduction of \$225 million in revenues, one-third of all this sum of money would go to one firm. The American Telephone & Telegraph Co. would get a reduction in its tax burden of \$75 million.

The travesty, Mr. President, is that A.T. & T. does not want it. The representatives of A.T. & T. came before the committee and testified against the investment credit provision; said they did not want it, would not use it, and that it would not increase their investment at all.

Whatever criticism may be made of that company, A.T. & T. knows what it is doing and knows what it is saying. They have based their position on a very careful and thorough study.

I wish to read from the statement made by the vice president and controller of American Telephone & Telegraph Co. Certainly, if this is chal-

lenged, he does speak for A.T. & T. I refer to Mr. Alexander L. Stott.

Mr. Stott said, in his appearance:

This statement is made on behalf of the Bell System companies to give our views on the proposal in the pending legislation for an incentive tax credit and other matters. Because the Bell System is a heavy user of capital equipment, it has always had a keen interest in construction and depreciation matters. In recent years the construction program of the Bell System companies has been running in the neighborhood of \$2.5 billion a year.

Mr. Stott further said:

The Bell System's construction program for 1962 is approximately \$2.8 billion and will probably remain in this general area in the immediate future. This construction is designed to meet the needs of the public for telephone service and we have an obligation to construct adequate facilities to meet this need.

Obviously, the company will construct the facilities whether given a tax gimmick or a tax advantage or not.

Mr. Stott also said:

Clearly it would not be economically desirable to build excess plant merely to obtain a tax credit. We have been able, under sound regulation, to obtain from investors the additional amount of new capital required to carry on our construction of new facilities. Therefore, we can see no justification for using tax moneys to help finance our expansion.

Mr. President, I wish to repeat that:

We have been able, under sound regulation, to obtain from investors the additional amount of new capital required to carry on our construction of new facilities. Therefore, we can see no justification for using tax moneys to help finance our expansion. As the proposed incentive credit now stands, our business would obtain substantial benefits whether its construction were increased or not. For example, under a 3-percent rate we estimate that our credit would be in the range of \$75 million for 1962.

This has been confirmed by the Treasury Department. One-third of the benefit of the investment credit to utilities—and this is all my amendment would knock out, since it would only affect utilities—would go to one firm, which, to its credit, has appeared before the Finance Committee to protest the investment credit. The firm says it does not want it, will not use it, and that it will not increase its growth at all.

Mr. President, it would seem to this Senator that on the basis of the testimony of the responsible official of the A.T. & T., the vice president and controller of the American Telephone & Telegraph Company, certainly as to that particular industry we should follow their advice. Their advice is based upon very great competence and success—a success which is not rivaled by another telephone service anywhere in the world. They have said the provision would not work. They do not want it, and it should not pass.

I ask unanimous consent that the statement by Mr. Stott to which I referred be printed at this point in the RECORD.

There being no objection, the statement was ordered to be printed in the RECORD, as follows:

This statement is made on behalf of the Bell System companies to give our views on the proposal in the pending legislation for an incentive tax credit and other matters. Because the Bell System is a heavy user of capital equipment, it has always had a keen interest in construction and depreciation matters. In recent years the construction program of the Bell System companies has been running in the neighborhood of \$2.5 billion a year.

There can be no disagreement with the objective of stimulating modernization and expansion of the Nation's productive facilities. If our Nation is to create the jobs needed for its expanding work force and improve our competitive position in world markets, our productive facilities must be rapidly modernized.

Since the purpose of the incentive tax credit to promote construction and growth, the question is whether it would have that result. As far as the Bell System companies are concerned it will not. Apparently this is also true of many other companies. On February 8, 1962, the Wall Street Journal published the results of a survey it had made on the plans of 68 large corporations. All except 1 stated that their construction programs would not be significantly affected if the proposal should be enacted, and 29 stated that the credit would not change their capital spending plans at all.

The Bell System's construction program for 1962 is approximately \$2.8 billion and will probably remain in this general area in the immediate future. This construction is designed to meet the needs of the public for telephone service and we have no obligation to construct adequate facilities to meet this need. Clearly it would not be economically desirable to build excess plant merely to obtain a tax credit. We have been able, under sound regulation, to obtain from investors the additional amount of new capital required to carry on our construction of new facilities. Therefore, we can see no justification for using tax moneys to help finance our expansion. As the proposed incentive credit now stands, our business would obtain substantial benefits whether its construction were increased or not. For example, under a 3-percent rate we estimate that our credit would be in the range of \$75 million for 1962. At a 4-percent rate it would be about \$100 million, and at an 8-percent rate it would be about \$200 million. If we received this credit we would be taking money from the Government which we should obtain from investors and not the taxpayers.

The investment credit is not a step toward needed tax reform. Rather, it is a subsidy to spur new construction by reducing the cost of acquiring new equipment. We do not think that business needs a subsidy to expand—it needs basic tax reform. In any case we are convinced that it would not be sound tax policy to offer a subsidy until faults in the present tax structure have been remedied. The credit may prove to be a windfall to many rapidly growing companies which would expand in any event. But it would be of little help to those companies whose plant and equipment is in the most need of modernization. Since one taxpayer's subsidy is another taxpayer's penalty, the credit would introduce an undesirable area of discrimination as among taxpayers. Furthermore, if the private enterprise system as we have known it is to remain strong and healthy, we believe it would be a mistake to take a step which may tend to cause business to look more and more to the Government to solve its problems.

It has been stated that the incentive credit is only part of the proposed program for spurring economic growth and that the other component would be a downward revision of depreciable lives set forth as guidelines in bulletin F. On January 18, 1962, the Secre-

tary of the Treasury said, "I consider our program of depreciation reform [bulletin F]—including the investment credit—a central part of our economic policy." If the proposed incentive credit becomes law, there is a distinct possibility that it will be regarded as providing tax depreciation reform, and true reform will be long deferred.

Revision of bulletin F may be useful in some areas. It should be kept in mind, however that bulletin F is only an administrative guide, specifying average service lives for property by industry groups. Actual depreciation allowed for tax purposes is seldom derived solely by reference to these guidelines. This situation would not be changed simply by having the Treasury Department issue a new bulletin listing shorter lives. Such action would certainly be of no value to us and we suspect the same would be true for many other businesses. In our case, depreciation rates are established on the basis of our own detailed engineering studies. As a matter of actual practice, the depreciation which we claim for tax purposes is based on rates prescribed for our companies by regulatory authorities for accounting purposes.

In my opinion it is important to understand why the Nation has fallen behind in modernization and expansion of productive facilities. High tax rates, and inflation in the postwar years are clearly at the root of our trouble. Depreciation allowances for tax purposes have failed to recover the purchasing power of the investment in plant being used up in providing goods and services, taxable income has been overstated, and capital has been taxed under the label of income. To maintain the purchasing power of its investment in plant and equipment, business must replace the capital eroded through taxation, either by undertaking outside financing or by retaining more earnings in the business. Many businesses have not been in a position to replenish their capital by these methods and so have not been able to keep their plant and equipment up to date. Furthermore, even when businesses have been able to obtain the capital needed to offset this erosion, they have put a burden on the savings of the country and have reduced the amount of capital that otherwise would have been available for expansion of the economy.

We believe that the first and most important step to stimulate modernization and expansion should be basic tax reform to permit depreciation allowances adequate to preserve the purchasing power of the investment in the productive facilities of the Nation. Such depreciation allowances could be calculated by adjusting the depreciation determined on the basis of the number of dollars originally invested in plant by the changes in the price level between the year of investment and the current year. The purpose of price-level adjustment of depreciation is to allow for changes in the general purchasing power of the dollar and not for changes in the price of particular assets.

We realize that many methods have been advocated for improving tax depreciation allowances and on the basis of studies we have made, we are convinced that price-level depreciation would be the fairest method for all concerned; that is, the public, business, investors, and the Treasury. But, whatever depreciation methods are adopted, effective control of tax depreciation can be achieved through a requirement in the tax law that the taxpayer may not use for tax purposes any depreciation method that is more liberal than the method used in his books of account. Since generally accepted accounting principles require realistic depreciation methods for financial reporting and accounting purposes, this requirement would protect the Government's tax revenues by preventing the use of fast depreciation methods for tax purposes where such

methods cannot be justified for financial reporting purposes.

By recognizing changes in purchasing power in the computation of depreciation allowances for tax purposes and requiring that no more liberal tax depreciation methods may be used than are used for accounting purposes, substantial amounts of new funds would become available for modernization and expansion to businesses with an appreciable investment in productive facilities. All businesses would obtain relief on an equitable basis, and businesses with the greatest need for modernization would share in the relief. Furthermore, whereas the expected cost of the proposed incentive credit is currently estimated at about \$1.4 billion, without including any changes in depreciation tax treatment, the cost of recognizing realistic depreciation deductions based on purchasing power, with appropriate safeguards, would be about \$2 billion. We are convinced, too, that inadequate depreciation allowances for tax purposes have been holding back growth and that realistic tax depreciation allowances which reflect the change in the purchasing power of the dollar are a necessary condition for a dynamically growing economy.

I should like to comment briefly on two other subjects which were mentioned during the appearance of the Secretary of the Treasury before your committee earlier this week. These are, first, the suggestion to change the restricted stock option provisions presently contained in section 421 of the Internal Revenue Code and, second, a proposal to eliminate the \$50 dividend exclusion and 4-percent dividend credit presently available to individuals. Any major changes in these provisions would seriously impair our ability to continue to obtain the amounts of new capital needed in our business.

RESTRICTED STOCK OPTIONS

Concerning changes in the restricted stock option provisions, our position in this matter was set forth in a statement appearing at page 180 in the record of the hearings held by your committee last year on S. 1625. Briefly, our position is that if there should be any legislation which would change the existing law in this field it should be carefully drafted so as not to cripple the operation of the capital-raising type of employee stock purchase plan which is being used to great advantage by American Telephone & Telegraph Co. and many other companies.

Reference to our company's stock purchase plan will illustrate how very different such a plan is from the incentive-type stock option ordinarily offered only to executives. Under our plan, shares are offered to all employees meeting minimum length-of-service requirements, on a voluntary and nondiscriminatory basis, at a price set at 15 percent below market value. Payment for shares is made by employees on an installment basis over a 24-month period, with no right of prepayment. The essential corporate purpose of the plan is to raise new capital. Important, too, is the opportunity provided for employees to save systematically while at the same time acquiring a proprietary interest in the business. Sales of stock under our plan in the years since World War II have produced about \$1.7 billion, or about one-fifth of the total new equity capital raised by the Bell System in this period. Almost 400,000 employees of American Telephone & Telegraph Co. and its subsidiaries are now participating in the plan. It is currently providing about \$300 million in equity capital annually as compared to our current new money requirements of about \$1 billion a year.

Many other companies have used and are now using stock purchase plans of this kind. A survey which we undertook recently of other companies indicated that, in the 1957-61 period, some \$500 million of stock was approved for offering by 33 separate corpora-

tions under this kind of employee stock purchase plan.

The primary purpose of the broadly based employee stock purchase plan, that of raising needed equity capital, is far different from the purpose of incentive stock option arrangements for top management. It is generally agreed that compensation is the basic business reason behind the granting of stock options to executives. There are strong reasons advanced for the position that the granting of such options serves a legitimate purpose. What I want to emphasize is that the purpose served by executive options is completely unrelated to any need of the business for additional capital, whereas the raising of needed capital is the essence of the employee stock-purchase plan. I might add that our companies have never offered incentive-type stock options to their executives.

The two types of plans are therefore quite different in scope and purpose. Nevertheless, our capital-raising employee stock-purchase plan is treated for tax purposes under the identical rules which apply to options. We believe that this is fundamentally unsound. The small discount available to an employee in connection with his purchase of stock under an employee stock plan such as that of our company is merely normal underpricing—no more of a price differential than is necessary to sell the large number of shares required for any successful capital-raising endeavor. But under the complicated provisions of section 421, which was devised initially to deal with executive stock options, the discount is subject to tax as ordinary income despite the fact that, from the corporate employer's standpoint, no compensation is intended and none is paid.

Section 421 does give our employees a modest tax benefit in that they do not have to pay income tax on the differential between the purchase price and the market value of the stock at the time of acquisition but can defer this tax until disposition of the stock. Without the protection provided in section 421, even this slight benefit would presumably disappear. This would certainly have an adverse effect on the capital-raising type of employee stock-purchase plan.

I therefore urge that any legislation directed toward changing the present provisions of the code in this area expressly recognize the distinction between capital-raising employee stock-purchase plans and executive stock options. It seems to us that if any changes are to be made, the tax status of the employee stock-purchase plan should be improved so as to give greater encouragement to the use of this type of plan, which has made such a valuable contribution to the Nation's economy by providing new capital to industry. Certainly this type of plan should not be stripped of the limited tax benefit it now has.

PROPOSED REPEAL OF \$50 DIVIDEND EXCLUSION AND 4-PERCENT DIVIDEND CREDIT

The proposed repeal of the \$50 dividend exclusion and 4-percent dividend credit will probably fall with greater impact on the Bell System than on most other corporate enterprises. Many investors, especially small investors, are financially interested in our enterprise and the Bell System is more dependent than most other businesses on the securities markets to secure the necessary funds for expansion to meet the public's demand for service.

The American Telephone & Telegraph Co., the parent company of the Bell System, has more than 2 million shareowners accounts, representing more than 2.5 million individual shareowners. Since the passage of these dividend provisions in 1954, almost 1 million shareowners have been added, the great majority being small investors. About 40 percent of A.T. & T.'s shareowners accounts

hold less than 28 shares of stock and receive less than \$100 in dividends per year.

To meet the public's demand for service the Bell System has had to raise about \$15.5 billion in new capital from investors since the end of world War II. More than \$9 billion was equity capital, obtained through the issuance of some 175 million additional shares of stock and representing over 20 percent of all new equity capital raised by corporations. It is clear that no other U.S. corporation has depended on the investing public and its willingness to place its savings in risk capital as heavily as has the Bell System.

In 1954 both the House and Senate committees were explicit in their reports as to the reasons for enacting the dividend exclusion and dividend credit. It was stated that the double taxation of distributed corporate earnings had contributed to the impairment of investment incentives, and had driven investment capital away from equities into safer forms of investment. Thus, the ability of companies to raise equity capital was restricted and they were forced to rely too heavily on debt.

Dividends received from corporations by individual shareowners were not subject to the normal tax prior to the Revenue Act of 1936. At that time, our economy had very little demand for new equity capital. Hence, the effect of imposing a double tax burden on distributed corporate earnings was then of little significance. But in retrospect the long-range effect on investment incentives and capital formation was serious.

It was quite clear in 1954 that remedial action was required to remove the obstacles from risk capital formation for the good of the economy.

Advocates of repeal of the \$50 dividend exclusion and the 4 percent dividend credit have advanced two principal arguments supporting their position.

The first is that the existing provisions are not efficient in that the tax effects are spread over outstanding shares rather than over new shares alone. Thus, it is asserted the stimulating effects are diluted with little increase in the supply of equity funds and a minor reduction in the cost of equity financing.

The second is that the existing provisions deal inadequately with the problem of tax relief and double taxation and are wholly inequitable as between taxpayers in different income brackets.

These arguments in no way negate the existence in 1954, or today, of the factors which motivated the action taken by Congress in 1954. No one has contended that conditions have so changed since 1954 that a return to the older tax basis is desirable. Instead, it is argued that the 1954 act does not go far enough to be fully effective and so should be repealed until something better is devised.

It is inconsistent to offer tax incentives to corporate business to increase its spending for plant and equipment and, at the same time, enact legislation that will substantially reduce the supply of capital available for that purpose. In short, all the tax inducements in the world for business to expand its plant and equipment will be worthless unless investors willingly risk their savings to finance that expansion.

Investment capital in the United States is not an unlimited reservoir that can be tapped at will. The supply of investment capital can be great or small depending on what investors think of the outlook. If investors have confidence that they will receive fair treatment they will have an incentive to commit their capital—otherwise they will not. Clearly the 1954 legislation was to relieve the punitive effects of double taxation, which contributed to the impairment of investment incentives.

It is argued that the dividend provisions give taxpayers in higher income brackets proportionately greater relief. It is obvious that the inclusion or exclusion in taxable income of any kind of income subjects taxpayers in different tax brackets to different tax effects so long as personal incomes are taxed at progressive rates. Even the \$600 exemption for dependents provides proportionately greater tax reduction to taxpayers subject to the higher tax brackets. But this fact has been recognized by the Congress time and again in legislation where the effects on public policy were more important than the relative impact on taxpayers of different means.

While the remedy granted by the act of 1954 was admittedly only partial, the upsurge of investors in equities since that time has been remarkable. In 1954 only 7 million individuals owned shares in American corporations. Today there are around 15 million, an increase of more than 100 percent in only 8 years.

The majority of these new share owners are in the middle and lower income brackets. A 1960 survey of stock ownership among American families made by the University of Michigan Survey Research Center shows that 58 percent of the value of all publicly traded stocks in private possession is owned by families with less than \$15,000 annual income; 36 percent is owned by families with less than \$10,000 annual income; and 10 percent is owned by families with less than \$5,000 annual income. The median income of share owners as reported by the latest New York Stock Exchange survey was \$7,000. In other words, one-half the share owners in America have an annual income below the \$7,000 mark and are in the income level of most schoolteachers and retired individuals. In these groups the incentive to save must be encouraged, not stifled, if the Nation is to obtain the capital needed for dynamic growth.

Since the passage of the 1954 act, the amount of capital, both debt and equity, provided by investors to corporate enterprises has increased substantially. Government data in the attached table show that the average annual amount of external equity financing by all U.S. corporations in the 8 years ending with 1961 was \$3.2 billion, as compared with an annual average of \$1.9 billion in the preceding 8 postwar years, or a 68-percent increase. In the same period, the average annual amount of all external financing increased from \$7.6 billion to \$11.1 billion, or about 46 percent. These amounts represent new investment capital actually supplied to business by investors for the expansion of plant and equipment, and do not include funds placed by investors in outstanding securities through market purchases.

It is argued that corporate profits and stock prices have been more important than the dividend credit provisions in stimulating stockownership. However, corporate profits today are lower than when the provision was passed by the Congress in 1954. The well-known series published by First National City Bank shows that net income of leading manufacturing companies as a percentage of net worth has declined from 12.4 percent in 1954 and 15.0 percent in 1955 to 10.5 percent in 1960 and 10.1 percent in 1961.

U.S. Department of Labor data show there are today more than 4.5 million unemployed persons, considerably above the normal level. The Department estimates that 13.5 million new workers will join the labor force during the 1960 decade. Business must provide jobs for these millions of workers and to do so will require great expansion running into many billions of dollars. Studies indicate it requires an average investment of around \$12,000 to provide one new job in American

industry today. Further, a greater share of available savings will be needed to advance the greatly expanded programs for schools, highways, and adequate housing.

The administration has an expressed goal for the Nation's economic rate of growth of 5 percent per annum, about twice that experienced in recent years. If business is to achieve this rate it will require much more rapid capital expansion than the present rate and much greater incentive for investors to place their savings in free enterprise. For this reason, it is extremely important to avoid any expedient that might throttle the creation of new capital required for the expansion of our economy. A complete return to double taxation of corporate dividends as a means for raising more tax revenues, or to simplify the administration of dividend withholding, without regard to the possible damage it might cause to the economy, should be rejected.

Mr. PROXMIRE. I conclude by pointing out, first, that the amendment is one which the Treasury, the outstanding champion of investment credit, supports the investment credit provision, contending that we need it for growth. It seems to me the Department of the Treasury must inevitably support the Proxmire amendment. Representatives of the Treasury Department have also said that utilities should be excluded from the investment credit.

Second, the Senate has a great responsibility for raising revenue as well as for spending money. This year we have passed the largest appropriation measures in the peacetime history of our country. We have greatly increased spending by the Federal Government. Some of that increase in spending has been absolutely essential. Some of it perhaps has not been. But it seems to this Senator that under circumstances like the present we should do our level best to provide a revenue system that is adequate to meet our spending needs. The amendment, which would conserve \$225 million as effectively as if we had eliminated \$225 million of unnecessary spending, is highly merited, in view of the overwhelming testimony. The clear evidence of impartial and expert economists is that the investment credit for utilities could not possibly provide a significant increase in investment. My amendment would wipe out about one-half of the present revenue loss in the bill as it is presently drafted. As I understand, the bill would provide for a revenue loss of something less than \$500 million. My amendment would increase revenues and reduce the loss by \$225 million. Therefore it would cut the loss in half. It seems to me to be well merited.

Mr. MANSFIELD. Mr. President, I am about to make a unanimous-consent request, which has been cleared with the minority leader, the Senator from Wisconsin [Mr. PROXMIRE], and the Senator from Oklahoma [Mr. KERR]. I ask unanimous consent that at the conclusion of some brief remarks to be made by the Senator from Oklahoma, there be a quorum call, and that at the conclusion of the quorum call there be a time limitation for debate on the Proxmire amendment of 10 minutes, 5 minutes to be controlled by the Senator from Okla-

homa and 5 minutes by the Senator from Wisconsin.

Mr. PROXMIRE. I wish to make a comment in connection with that agreement. I hope that the majority leader and the minority leader will help me get the yeas and nays.

Mr. MANSFIELD. Certainly.

The PRESIDING OFFICER. Is there objection? The Chair hears none, and it is so ordered.

Mr. KERR. I rise to oppose the amendment of the Senator from Wisconsin. The Senator in the main quoted a great deal from a study made by a Mr. Clark. I did not understand exactly who Mr. Clark was. He referred to Mr. Clark as having made a study prior to 1953, and that Mr. Clark found that such a provision as is in the bill, of providing an investment credit of 3 percent on new construction other than depreciable expansion, materials, and facilities, by regulated utilities would not stimulate investment for modernization and expansion.

This Mr. Clark, in 1953, found that such investment credit would not be a stimulant to investment and modernization by telephone companies.

As I say, I do not know who Mr. Clark is. I do not know the basis of his study in 1953 or before.

I remind the Senator from Wisconsin that a more recent and current study was made by the Ways and Means Committee of the House of Representatives, and that study was made in 1961. They found that the investment credit would be a stimulant to regulated utilities, including telephone companies, and would encourage investment for modernization and expansion.

The Finance Committee of the Senate made a study of this subject in 1962. I wish to say to the able Senator from Wisconsin that the Finance Committee went into this matter for many months. They found that the measure would stimulate investment for modernization and expansion by regulated utilities, including telephone companies.

As I said a while ago, I do not know who Mr. Clark is. I do know who the Ways and Means Committee members are. I do know who the members of the Finance Committee are. I must say that I have more respect for their judgment, on the basis of my acquaintance with them and knowledge of them, than I do of someone who is identified only as being referred to as a Mr. Clark. I will say, of course, that Mr. Clark has not had the benefit of serving in the Senate; neither was he hindered nor impaired by having done so. Of course, the members of the Ways and Means Committee and the members of the Finance Committee have the responsibility of studying taxation, actual and proposed, and the relation of it to our economy and to the fiscal position of the Government. In the judgment of the Senator from Oklahoma, they are more entitled to the confidence of this body than someone about whom the only thing we know is his name.

The distinguished Senator from Wisconsin said that the argument was made

for the investment credit as a stimulant and encouragement to domestic industry in their competition with foreign industry.

Then he wonders who would be so foolish as to think that domestic regulated utilities were in competition with foreign-regulated utilities. They are not; but their customers are; and anything which affects the efficiency and economy of the service of an American-regulated utility affects the efficiency and economy of its customers.

The Senator from Wisconsin said that even if the benefit of the tax credit or investment credit were passed on by utilities to their customers, it would amount to only about 1 percent—as if that were nothing. In the sixth or seventh grade, in the arithmetic I studied, I learned that three times nothing is nothing. So if a 1-percent savings to the consumer of a utility is nothing, then three times nothing, to the utility would, I presume, be nothing. If the Senator from Wisconsin is complaining that the pass-on to the consumer would be so little, I see no basis for his complaint about giving the utility three times nothing, since that would be nothing also.

But the pass-on of 1 percent to the consumer is significant, because industry is also in the category of customers of utilities; and any benefit that industry receives, competitive, even though in the form of a pass-on in the cost of that electric power or other utility service, is substantially an economic benefit to those industrial consumers with reference to whom the House Committee on Ways and Means and the Senate Committee on Finance have expressed a deep concern as to the improvement of the competitive position of all American industry with foreign industry.

The distinguished Senator from Wisconsin said that the private regulated utilities have a guaranteed return. That is a fallacy long since exploded. I know of no regulatory body that can guarantee a return to a utility company subject to its jurisdiction. The regulatory body can adjust the utility's rates so as to permit a return; but I know of no greater fallacy than the conclusion often expressed that a regulatory body guarantees a return on the investment of utilities subject to the regulation of the regulatory body.

The Senator from Wisconsin then said that there would be no benefit to the utility, that there would be no stimulant to the utility, if the utility gave its customers the benefit of the savings enjoyed by the utility in the construction or modernization of its equipment and facilities by reason of the proposed investment credit. I do not know how much experience the Senator from Wisconsin has had in the handling of the business of a utility. I do not know how many of them he has operated. Therefore, I am not in a position accurately to evaluate his judgment in that regard. I remind him that the president of the largest regulated utility in this Nation was before our committee for many hours, and he made the positive state-

ment, first, that the 3 percent investment credit would be a stimulant to his company; that it would result in a greater modernization and an accelerated modernization and improvement of its generating equipment; that it would result in an expansion at a faster rate than would be effective or possible without the proposed investment credit.

The president of that regulated electric utility said, in addition, that it would be their purpose to pass on to their customers every dollar of saving realized by reason of the proposed investment credit.

Mr. President, the Senator from Wisconsin can doubt the gentleman's word if he wishes to; but I say in behalf of the witness that he is well known to Members of this body. His name is Donald C. Cook, and he is president of American Electric Power Co. He has been an official in the Government for many years and enjoys as fine a reputation as any man I know. The members of the committee had no basis to doubt his word. He does have the advantage of some experience in the operation of a regulated public utility. He made the positive statement that the proposed investment credit would cause his company to accelerate the modernization and expansion of its facilities and enable it to be of greater service to its present consumers and extend its service to other customers. He said that the proposed investment credit would enable his company to reduce the cost of its service both to present and future customers, and that would be what they would do.

Therefore, Senators can understand why the Committee on Finance acted as it did. It accepted the judgment of the president of a great utility company as to the value of the proposed investment credit to his company and his company's customers. The committee accepted as valid his assurance that the saving would be passed on to the company's customers.

Then the distinguished junior Senator from Tennessee [Mr. GORE], in a colloquy with the distinguished Senator from Wisconsin, indicated that he likewise opposed the proposed credit to regulated electric utilities. The Senator from Tennessee comes from an area which is served by the Tennessee Valley Authority. There are those who feel that the Tennessee Valley Authority and its customers have some advantage over other utilities in this country and their customers. There are some who believe that regulated utilities in the areas around them and in the rest of the country pay a higher rate of taxes, are subject to different regulations, and operate, both with reference to their own operations and their relations with their customers, at some disadvantage as compared with the Tennessee Valley Authority.

I am sure that the fact that this modest investment credit to regulated electric utilities who are competitive with the Tennessee Valley Authority might slightly improve their competitive position with reference to the Tennessee Valley Authority would not be the basis

of the opposition to this investment credit by the Senator from Tennessee. Yet such a conclusion might possibly be drawn, Mr. President, by other Senators—that it would be the purpose of the Senator from Tennessee not only to preserve the TVA in its operations, for the benefit of his area. I remind him that no Member of this body has worked harder to enable the TVA to be of complete service to the customers in its area than has the Senator from Oklahoma. It so happens that the Senator from Oklahoma come from a State which has public power and private power. Two great private utilities operate in Oklahoma. The Senator from Oklahoma is interested in securing electric power to the domestic consumers and the industrial consumers in Oklahoma at the lowest possible cost consistent with an adequate return to the private electric utilities serving the State of Oklahoma.

He is frank to admit that the domestic consumers and the industrial consumers in Oklahoma do not have the benefit of as low-cost electricity as that which is available in the Tennessee Valley. But that fact has not in any way hindered the support of the Senator from Oklahoma of the Tennessee Valley Authority and the adequacy of its service within its service area. So he is a little disappointed that the Senator from Tennessee would now oppose a measure which, in the judgment of the Senator from Oklahoma, would result in making it possible for the utilities in Oklahoma to give a little better service and a little cheaper service to the domestic consumers and the industrial consumers in Oklahoma; and the same situation would prevail in every other State in the Union, even in Wisconsin.

The result of this investment credit for the regulated utilities can be nothing other than encouragement of more modernization and expansion of those regulated utilities and better service and cheaper service to the domestic consumers and the industrial consumers in their service areas; and the Senator from Oklahoma feels that this is an appropriate manner in which to give encouragement to and to be of benefit to the regulated electric utilities in his State. The Senator from Oklahoma believes that by reason of this, the favorable differential to the Tennessee Valley Authority, now existing, as compared to any other area in the Nation, save the Pacific Northwest alone, might be eliminated or might be reduced just a little, to the benefit of the domestic consumers and the industrial consumers in Oklahoma; and he is disappointed that his good friend, the Senator from Tennessee, who always has had the benefit of the help of the Senator from Oklahoma in connection with matters related to electric service in his area, would now be opposing something which, insofar as the electric service and its cost in his area are concerned, can have no effect whatever except to result in some reduction of cost to the domestic consumers and the industrial consumers in Oklahoma. So the Senator from Oklahoma is disappointed that his great and good friend, the Senator from Tennessee,

would now be opposing it; and the Senator from Oklahoma hopes that, upon due and deliberate consideration, the Senator from Tennessee may consider withdrawing that opposition.

Mr. GORE. Mr. President, will the Senator from Oklahoma yield?

Mr. KERR. I yield.

Mr. GORE. The able and distinguished Senator from Oklahoma has drawn an interesting analogy, but I respectfully submit that it is not a valid one.

From the profits which the private power companies reap from the utility bills American consumers pay, a portion is paid to the U.S. Government in the form of taxes. The benefits which the people of the Tennessee Valley receive from the TVA result from the quality of the service they receive and the rates they pay for it. The profits which the TVA earns in supplying that service, for which the people of the Tennessee Valley pay, go to the U.S. Treasury—not in part, but 100 percent. The tax rate on the TVA profits is not 52 percent; it is 100 percent. I do not complain about that, because this is a publicly owned utility—owned by the Federal Government; and, therefore, all the proceeds properly belong to the Federal Government. Therefore, I suggest to the distinguished and able Senator from Oklahoma that the analogy he draws is not a valid one.

Before closing, I should like to say that both I and other Senators from the Tennessee Valley area and the people of that area are very grateful for the leadership which the distinguished senior Senator from Oklahoma provided as chairman of the subcommittee in bringing about the enactment of the self-financing bill for the TVA. But let us not misunderstand that. It operates in this way: The Tennessee Valley Authority sells its own bonds to raise the money with which to build hydroelectric dams or steamplants. The people of the Tennessee Valley pay for those steamplants and those hydroelectric dams through the payment of their utility bills. Yet when they are paid for, they belong to the Federal Government, not to the people of the Tennessee Valley.

When the same thing occurs in the case of a private utility company which sells its bonds in order to raise the money with which to build additional facilities, or when it borrows, by other means, the money with which to do so, and when its customers amortize those plants through the payment of their utility bills, those facilities, too, belong, not to the people who pay the utility bills, but to the corporation which borrowed the money in the first place.

It happens that the Tennessee Valley Authority is a corporation, a corporation wholly Government owned, all the profits and all the net proceeds of which—not 52 percent, and not subject to the benefit of the investment credit, but, I repeat, 100 percent—belong to the Federal Government.

In view of all of this, the people of the Tennessee Valley are grateful for the leadership the distinguished senior Senator from Oklahoma has accorded

on this subject. The people of the Tennessee Valley, I believe—and I am privileged, I think, to speak for them—are proud of the TVA, because it is the most efficient and the largest integrated utility in the world. It has led the way and pointed the way toward the use of larger generators and toward more economic generation of power, and it has blazed the trail for mass distribution of electric energy—many kilowatts at a small profit, rather than a few kilowatts at a large profit per kilowatt.

The Tennessee Valley Authority has served the Nation well, including the privately owned utilities; but again I repeat, all of its proceeds, not 52 percent thereof, become the property of the U.S. Government.

Mr. KERR. I appreciate the kind remarks by the Senator from Tennessee about the Senator from Oklahoma. He knows of our mutual affection and regard. I am in a little disturbed state of mind about what the Senator from Tennessee said I did. He said I drew an analogy. I do not know just what goes on when one draws an analogy. I think I know what an analogy is, but I do not know what happens to it when one draws it. But the Senator from Tennessee then addressed himself to the difference between TVA and a private utility and what it pays to the Federal Government.

The Senator from Oklahoma did not say anything about that. It may be that if a comparison between the TVA and a private utility constitutes an analogy, the Senator from Oklahoma had something to do with it. But if the Senator from Tennessee wants to relate that comparison of the taxes paid by private utilities to the Federal Government and the taxes paid by the TVA to the Government and call that a drawing of an analogy, I remind him that is something he did. The Senator from Oklahoma did not do it. The Senator from Oklahoma compared the situation of consumers in the two areas, not the relationship of either to the Federal Government in the matter of taxes they paid.

The Senator from Tennessee went on to talk about the low cost electricity available in his area. That is what the Senator from Oklahoma was talking about. He is glad they have it. He helped make it possible, and was glad to do so, and shall continue to do so.

What the Senator from Oklahoma said was that he was trying to make it possible for the electric utilities in Oklahoma to provide lower cost electrical power to the domestic and industrial consumers in Oklahoma. There is no hope of making it possible to have the utilities supply electricity to the domestic and industrial consumers in Oklahoma at as low a rate as is available to the domestic and industrial consumers in the Tennessee Valley. The Senator from Oklahoma said he thought the investment credit would bring about a slight narrowing of the margin. There is no possibility of eliminating it. That is what the Senator from Oklahoma was talking about, not about how much taxes either had paid to the Federal Government.

The Senator from Oklahoma is glad that the Senator from Tennessee advised him that the TVA paid taxes to the Federal Government. The Senator from Oklahoma did not know that. Some day, when the Senator from Tennessee has a little time, the Senator from Oklahoma would appreciate having placed in the RECORD a little statement which shows what the Tennessee Valley Authority has paid to the Federal Government in taxes from the day of its creation to the present time. It would be an interesting piece of information to the Senator from Oklahoma and other Senators. I will say to the Senator from Tennessee that if the taxes which have been paid to the Federal Government have been exorbitant and the Senator from Tennessee thinks they ought to be adjusted, the Senator from Oklahoma will be glad to take under consideration with him a joint effort to bring about a more equitable rate on the taxes the Tennessee Valley Authority pays to the Federal Government.

I repeat, I am in opposition to the amendment of the Senator from Wisconsin.

I suggest the absence of a quorum in accordance with the unanimous-consent agreement.

The PRESIDING OFFICER (Mr. CANNON in the chair). The clerk will call the roll.

The legislative clerk called the roll, and the following Senators answered to their names:

[No. 235 Leg.]

Alken	Hart	Metcalf
Allott	Hartke	Miller
Bartlett	Hayden	Monroney
Boggs	Hickenlooper	Morse
Bush	Hill	Mundt
Byrd, Va.	Holland	Pastore
Byrd, W. Va.	Hruska	Pearson
Cannon	Jackson	Pell
Carlson	Javits	Prouty
Carroll	Johnston	Proxmire
Case	Jordan, N.C.	Randolph
Chavez	Keating	Russell
Church	Kefauver	Smith, Maine
Cooper	Kerr	Sparkman
Curtis	Lausche	Stennis
Dirksen	Long, Mo.	Thurmond
Dodd	Long, Hawaii	Tower
Douglas	Long, La.	Wiley
Ellender	Mansfield	Williams, N.J.
Ervin	McCarthy	Young, N. Dak.
Fong	McGee	Young, Ohio
Gore	McNamara	

The PRESIDING OFFICER. A quorum is present.

Mr. MANSFIELD. Mr. President, I ask for the yeas and nays on the Proxmire amendment.

The yeas and nays were ordered.

Mr. MANSFIELD. Mr. President, for the information of the Senate, a unanimous-consent agreement has been arrived at for a yea-and-nay vote within the next 10 minutes.

The PRESIDING OFFICER. Under the agreement the Senator from Oklahoma [Mr. KERR] has 5 minutes and the Senator from Wisconsin [Mr. PROXMIRE] has 5 minutes.

Mr. DIRKSEN. Mr. President, a parliamentary inquiry.

The PRESIDING OFFICER. The Senator will state it.

Mr. DIRKSEN. What is the amendment now pending before the Senate?

The PRESIDING OFFICER. The pending amendment is the amendment

of the Senator from Wisconsin [Mr. PROXMIRE] designated "8-30-62-C."

Mr. DIRKSEN. Mr. President, is it an appropriate inquiry to ask whether the amendment would delete the 3-percent investment credit provision in the pending bill with respect to utilities?

The PRESIDING OFFICER. The Chair states that is not a proper parliamentary inquiry.

Mr. DIRKSEN. I withdraw the inquiry.

Mr. KERR. Mr. President, I yield myself 2 minutes.

The PRESIDING OFFICER. The Senator from Oklahoma is recognized for 2 minutes.

Mr. KERR. The amendment of the Senator from Wisconsin would deny a 3-percent investment credit to regulated utilities while leaving a 7-percent investment credit available to other industry. The Senator from Oklahoma, in accordance with the action of the Finance Committee, is very much opposed to the denial of the investment credit to regulated utilities. The Senator from Wisconsin has said that it would not bring about any expansion and would not bring about cheaper rates.

I refer Senators to the statement of Donald C. Cook, president of the American Electric Power Co., found at pages 935 through 937 in the hearings. Mr. Cook, who is president of the American Electric Power Co., the largest in the Nation, said:

I think it clear—and I intend to show—that, in the case of electric utilities, the tax credit will do more to increase construction and, therefore, to bring about the desired growth in the economy, than in the case of nonutilities.

Further on Mr. Cook made the very positive statement:

While we are among those companies having the lowest rates for power in the United States, we are nonetheless even now studying still further rate reductions which we believe will become possible if the tax credit is made available to us.

Favorable action of this committee and of the Congress on this bill will either make possible or prevent these rate decreases.

What Mr. Cook said was that the companies would respond to the stimulus for greater growth and modernization, and that they would be able to reduce correspondingly both domestic and industrial rates to their consumers.

The PRESIDING OFFICER. The Senator's 2 minutes have expired.

Mr. PASTORE. Mr. President, will the Senator yield for a question?

Mr. KERR. I yield myself 1 minute in order to answer the question of the Senator from Rhode Island. I yield to the Senator.

Mr. PASTORE. In the New England section of the country there are privately owned public utilities serving telephone, electricity, and gas users. I think the rates are the highest in any area in the country. Would the bill assist consumers of electricity and gas, and telephone users in our region of the country if the amendment were agreed to?

Mr. KERR. The Senator from Oklahoma is of the positive conviction that

the present provision of the bill would enable utilities in the section of the country from which the Senator comes to bring the area better service at lower cost, and that such would be the result.

Mr. AIKEN. Mr. President, will the Senator yield for another question?

Mr. KERR. I yield.

Mr. AIKEN. I should like to ask the Senator from Oklahoma if the 3-percent reduction would apply to rural electrification lines and municipal lines as well?

Mr. KERR. If they are taxpayers to the Federal Government it would.

The PRESIDING OFFICER. The Senator's additional 1 minute has expired.

Mr. AIKEN. If they make a profit it would?

Mr. KERR. Definitely it would.

Mr. PROXMIRE. Mr. President, I yield myself 5 minutes. The amendment follows the recommendation of the Kennedy administration and of the Treasury Department. That recommendation originally was that utilities be excluded, not included. The Treasury Department correctly points out that this provision in the bill would cost the Treasury \$225 million in revenue. It was also argued very emphatically by the Treasury that this amount would not be passed on generally to the consumers and that it will not increase investment; on the other hand, it will generally result in a windfall for stockholders.

The Treasury argues that the principal purpose of the investment credit was not to cut people's electric light bills, but to stimulate investment. They say this cannot be done in the utility industry because under the law, at least as it exists now, the public utilities are regulated and their investors under the regulations of the regulatory body receive a fair rate of return. Obviously, if the corporation income tax is to be cut in this way, utilities income should be cut in the same way. So where is the incentive?

It is argued that the consumers will benefit. However, the Treasury has shown that the consumer benefit would be no more than 1 percent.

Mr. President, furthermore, we have had experience with this kind of cut under the 1954 act, when there was a similar reduction made in taxes on utilities through a speedup of amortization. In the report by the Subcommittee on Antitrust and Monopoly of the Judiciary Committee, it was found that the accelerated amortization had no real tendency to encourage construction of emergency facilities. The report stated:

"* * * Under the policies then (i.e., April 1955) in force, no clear relation to defense needs was required for approval of certificates for electric power generation as they were granted on the basis of total demand, including civilian as well as military needs. The lack of incentive was indicated by the fact that in the few instances where proposed facilities were held ineligible—because of location in target areas—the utility companies constructed them despite the rejection. * * *

"Of the applications considered by the Department of the Interior and the Office of Defense Mobilization, approval was given to facilities scheduled to bring in 13,013,450 kilowatts. Applications which were denied

because of their target area location totaled 5,298,000. All of the projects so denied still are scheduled for completion in 1958, despite the withholding of the tax-amortization inducement.

In other words, the experience shows clearly that although in some cases tax benefits were not given, the utilities nevertheless went ahead and made their investment.

Furthermore, one firm would get one-third of the benefit. That is the American Telephone & Telegraph Co. It would get \$75 million of the \$225 million that we are talking about. However, to their credit, the comptroller and vice president of A.T. & T. appeared before the committee and said in behalf of A.T. & T., "We do not want it." We should not have it." He said:

The Bell System's construction program for 1962 is approximately \$2.8 billion and will probably remain in this general area in the immediate future. This construction is designed to meet the needs of the public for telephone service and we have an obligation to construct adequate facilities to meet this need. Clearly it would not be economically desirable to build excess plants merely to obtain a tax credit. We have been able, under sound regulation, to obtain from investors the additional amount of new capital required to carry on our construction of new facilities. Therefore, we can see no justification for using tax moneys to help finance our expansion. As the proposed incentive credit now stands, our business would obtain substantial benefits whether its construction were increased or not. For example, under a 3-percent rate we estimate that our credit would be in the range of \$75 million for 1962. At a 4-percent rate it would be about \$100 million, and at an 8-percent rate it would be about \$200 million. If we received this credit we would be taking money from the Government which we should obtain from investors and not the taxpayers.

That position of this very capable management makes sense and adds up.

To summarize, this provision will not increase investment—and that is the only justification for it that was given—on the basis of the testimony of the one firm that would get the principal benefit from it. It may reduce rates in some cases, but, the Treasury says, that is very erratic and will be rare.

It is their conclusion—and I have documented it by the many tables I have put in the RECORD—that this will primarily result in a windfall for stockholders of the public utilities, which is not merited.

The PRESIDING OFFICER. The time of the Senator has expired.

Mr. KERR. Mr. President, I yield back the remainder of my time.

The PRESIDING OFFICER. All time for debate has expired.

The question is on agreeing to the amendment offered by the Senator from Wisconsin. The yeas and nays have been ordered, and the clerk will call the roll.

The legislative clerk called the roll.

Mr. MANSFIELD. I announce that the Senator from Nevada [Mr. BIBLE], the Senator from North Dakota [Mr. BURDICK], the Senator from Pennsylvania [Mr. CLARK], the Senator from Mississippi [Mr. EASTLAND], the Senator from California [Mr. ENGLE], the Sena-

tor from Arkansas [Mr. FULBRIGHT], the Senator from Minnesota [Mr. HUMPHREY], the Senator from Washington [Mr. MAGNUSON], the Senator from Arkansas [Mr. McCLELLAN], the Senator from Utah [Mr. MOSS], the Senator from Maine [Mr. MUSKIE], the Senator from Oregon [Mr. NEUBERGER], the Senator from Virginia [Mr. ROBERTSON], the Senator from Florida [Mr. SMATHERS], the Senator from Massachusetts [Mr. SMITH], the Senator from Georgia [Mr. TALMADGE], and the Senator from Texas [Mr. YARBOROUGH] are absent on official business.

I further announce that, if present and voting, the Senator from California [Mr. ENGLE], the Senator from Wyoming [Mr. HICKEY], and the Senator from Virginia [Mr. ROBERTSON] would each vote "nay."

I further announce that the Senator from New Mexico [Mr. ANDERSON], the Senator from Alaska [Mr. GRUENING], the Senator from Wyoming [Mr. HICKEY], and the Senator from Missouri [Mr. SYMINGTON] are necessarily absent.

On this vote, the Senator from Nevada [Mr. BIBLE] is paired with the Senator from Pennsylvania [Mr. CLARK]. If present and voting, the Senator from Nevada would vote "nay," and the Senator from Pennsylvania would vote "yea."

On this vote, the Senator from Mississippi [Mr. EASTLAND] is paired with the Senator from Texas [Mr. YARBOROUGH]. If present and voting, the Senator from Mississippi would vote "nay," and the Senator from Texas would vote "yea."

On this vote, the Senator from Arkansas [Mr. FULBRIGHT] is paired with the Senator from Utah [Mr. MOSS]. If present and voting, the Senator from Arkansas would vote "nay," and the Senator from Utah would vote "yea."

On this vote, the Senator from Missouri [Mr. SYMINGTON] is paired with the Senator from Alaska [Mr. GRUENING]. If present and voting, the Senator from Missouri would vote "nay," and the Senator from Alaska would vote "yea."

On this vote, the Senator from Arkansas [Mr. McCLELLAN] is paired with the Senator from Washington [Mr. MAGNUSON]. If present and voting, the Senator from Arkansas would vote "nay," and the Senator from Washington would vote "yea."

On this vote, the Senator from Georgia [Mr. TALMADGE] is paired with the Senator from Oregon [Mr. NEUBERGER]. If present and voting, the Senator from Georgia would vote "nay," and the Senator from Oregon would vote "yea."

On this vote, the Senator from Florida [Mr. SMATHERS] is paired with the Senator from Massachusetts [Mr. SMITH]. If present and voting, the Senator from Florida would vote "nay," and the Senator from Massachusetts would vote "yea."

Mr. DIRKSEN. I announce that the Senator from Maryland [Mr. BEALL], the Senator from Utah [Mr. BENNETT], the Senator from South Dakota [Mr. BOTHE], the Senator from Indiana [Mr. CAPEHART], the Senators from New Hampshire [Mr. COTTON and Mr.

MURPHY], the Senator from Arizona [Mr. GOLDWATER], the Senator from Idaho [Mr. JORDAN], the Senator from California [Mr. KUCHEL], the Senator from Kentucky [Mr. MORTON], the Senator from Massachusetts [Mr. SALTONSTALL], the Senator from Pennsylvania [Mr. SCOTT], and the Senator from Delaware [Mr. WILLIAMS] are necessarily absent.

The Senator from Maryland [Mr. BUTLER] is detained on official business, and if present and voting, would vote "nay."

If present and voting, the Senator from Maryland [Mr. BEALL], the Senator from Utah [Mr. BENNETT], the Senator from South Dakota [Mr. BOTTUM], the Senator from Indiana [Mr. CAPEHART], the Senator from Idaho [Mr. JORDAN], the Senator from California [Mr. KUCHEL], the Senator from Kentucky [Mr. MORTON], the Senator from Massachusetts [Mr. SALTONSTALL], and the Senator from Pennsylvania [Mr. SCOTT] would vote "nay."

The result was announced—yeas 16, nays 49, as follows:

[No. 236 Leg.]

YEAS 16

Bartlett	Jackson	Proxmire
Byrd, Va.	Kefauver	Russell
Douglas	Lausche	Thurmond
Gore	McNamara	Young, Ohio
Hart	Metcalf	
Hartke	Morse	

NAYS—49

Aiken	Fong	Miller
Allott	Hayden	Monroney
Boggs	Hickenlooper	Mundt
Bush	Hill	Pastore
Byrd, W. Va.	Holland	Pearson
Cannon	Hruska	Pell
Carlson	Javits	Prouty
Carroll	Johnston	Randolph
Case	Jordan, N.C.	Smith, Maine
Chavez	Keating	Sparkman
Church	Kerr	Stennis
Cooper	Long, Mo.	Tower
Curtis	Long, Hawaii	Wiley
Dirksen	Long, La.	Williams, N.J.
Dodd	Mansfield	Young, N. Dak.
Ellender	McCarthy	
Ervin	McGee	

NOT VOTING—35

Anderson	Fulbright	Muskie
Beall	Goldwater	Neuberger
Bennett	Gruening	Robertson
Bible	Hickey	Saltonstall
Bottum	Humphrey	Scott
Burdick	Jordan, Idaho	Smathers
Butler	Kuchel	Smith, Mass.
Capehart	Magnuson	Symington
Clark	McClellan	Talmadge
Cotton	Morton	Williams, Del.
Eastland	Moss	Yarborough
Engle	Murphy	

So Mr. PROXMIRE's amendment was rejected.

Mr. KERR. Mr. President, I move that the action whereby the amendment was rejected be reconsidered.

Mr. DIRKSEN. I move to lay that motion on the table.

The motion to lay on the table was agreed to.

Mr. DIRKSEN. Mr. President, I submit an amendment, which I have discussed with the members of the committee. I shall take but a minute or two to inform the Senate about it. I ask that the reading of the amendment be dispensed with, but that the amendment be printed in the RECORD.

The PRESIDING OFFICER (Mr. McCARTHY in the chair). Without objec-

tion, the reading of the amendment will be dispensed with; and the amendment will be printed in the RECORD.

The amendment is as follows:

At the end of the bill insert the following new section:

"Sec. 128. Deduction for income tax purposes of contributions to certain organizations for judicial reform

"For purposes of section 170 of the Internal Revenue Code of 1954 (relating to deduction for charitable, etc., contributions and gifts), a contribution or gift made after December 31, 1961, with respect to a referendum occurring during the calendar year 1962 to or for the use of any nonprofit organization created and operated exclusively—

"(1) to consider proposals for the reorganization of the judicial branch of the government of any State of the United States or political subdivision of such State, and

"(2) to provide information; make recommendations, and seek public support or opposition as to such proposals,

"shall be treated as a charitable contribution if no part of the net earnings of such organization inures to the benefit of any private shareholder or individual. The provisions of the preceding sentence shall not apply to any organization which participates in, or intervenes in, any political campaign on behalf of any candidate for public office."

Mr. DIRKSEN. Mr. President, the basis for the amendment is simply that the Illinois constitution dates back to 1870; and so far as its judicial article is concerned, it dates back to 1848. There has been no revision in the court system of our State since that time, notwithstanding a number of efforts that have been made.

One of the difficulties is in getting information to the people. That is so necessary, because before an amendment can be adopted, it requires either a two-thirds vote by the people in a referendum or a majority of all the votes cast in that particular election for elective State offices.

Over a period of time, the Illinois constitution has been subjected to 26 amendments. Some have carried; others have failed. But the problem of stirring public interest in a modernization of our court system is a difficult one, unless sufficient funds can be obtained in order to make manifest to the people what the issue is. That requires the use of television, radio, newspaper space, and every other means of propaganda and publicity in order to bring the proposal to the attention of the people. This amendment, then, would make it possible for anyone who makes a contribution to this cause, which is nonprofit and is carried on by a nonpartisan group, to deduct that contribution for tax purposes only for the year 1962.

That is the substance of the amendment, and I sincerely hope it will be adopted. I have submitted it to the chairman, and I think it is agreeable to the committee.

Mr. KEATING. Mr. President, will the Senator from Illinois yield?

Mr. DIRKSEN. I yield.

Mr. KEATING. In New York a similar situation exists; for years a distinguished and important nonprofit organization has been seeking reform of our courts. In fact, a constitutional amend-

ment to reorganize the court system has now been adopted. But many improvements remain to be made. This organization and others throughout the Nation must be able to continue the fine work which is being done in this field. Certainly, no one is engaging in it for any purpose except to improve the courts and facilitate and modernize our judicial machinery.

I support the Senator from Illinois and I commend him for offering this amendment. I hope his amendment will be adopted.

Mr. DIRKSEN. I thank the Senator from New York.

I only add, Mr. President, that these referendums always appear on a separate ballot; and there is great difficulty in getting people to mark them, rather than throw them away or turn them in and have them deposited without having made any mark whatever on them. Of course that requires something of a campaign, and funds are required for it.

Since it is in the public interest, and not for the benefit of any group, I think the amendment should commend itself to the Senate.

Mr. KERR. Mr. President, I understand that this amendment is identical with House bill 10080, as amended, which has been reported unanimously by the House Ways and Means Committee. In view of the fact that no contribution treated by this amendment could possibly inure to the benefit of any private individual, and in view of the further fact that the organization must not participate in any political campaign in behalf of any candidate for public office, and in view of the further fact that the nonprofit organizations involved must be created and must operate exclusively for the purpose of considering proposals for the reorganization of the judicial branch of the State government, and to provide recommendations or to seek support for such proposals, and in view of the further fact that the amendment is limited to 1962, I feel that the amendment is worthy, and I urge its adoption.

The PRESIDING OFFICER. The question is on agreeing to the amendment of the Senator from Illinois.

The amendment was agreed to.

Mr. DIRKSEN. Mr. President, I move that the vote by which the amendment was agreed to be reconsidered.

Mr. KERR. Mr. President, I move that the motion to reconsider be laid on the table.

The motion to lay on the table was agreed to.

Mr. PROXMIRE. Mr. President, I call up my amendments identified as "8-29-62-G," and ask unanimous consent that the reading of the amendments be dispensed with. I am perfectly willing to have a unanimous-consent agreement entered in connection with the amendments.

The PRESIDING OFFICER. Without objection, the reading of the amendments will be dispensed with, and they will be printed in the RECORD.

Mr. PROXMIRE's amendments are as follows:

On page 15, line 20, after "electrical energy," insert "gas."

On page 16, strike out lines 1 and 2 and insert the following:

"(ii) transportation of gas by pipeline."
On page 16, line 15, after the period insert the following: "The term 'public utility property' does not include property used predominantly in the production or gathering of gas."

Mr. MANSFIELD. Mr. President, I ask unanimous consent that 20 minutes be allotted for the consideration of the amendments; 10 minutes to be controlled by the Senator from Wisconsin [Mr. PROXMIRE] and 10 minutes to be controlled by the Senator from Oklahoma [Mr. KERR].

The PRESIDING OFFICER. Is there objection? Without objection, it is so ordered.

Mr. PROXMIRE. Mr. President, on the question of agreeing to the amendments; I ask for the yeas and nays.

The PRESIDING OFFICER. Is there a sufficient second?

The yeas and nays were ordered.

Mr. PROXMIRE. Mr. President, these amendments would include gas pipelines as a utility under the bill, and would provide a 3-percent investment credit, instead of the 7-percent credit permitted by the bill.

On page 155 of the committee report, gas pipelines are specifically singled out as examples of property qualifying for the full 7-percent investment credit. This is done in spite of the statement of Secretary Dillon on page 130 of the hearings, as follows:

B. The investment credit is especially inappropriate for gas pipelines.

The natural gas pipeline industry has expanded at a very rapid rate without the investment credit. As of the end of 1960, the index of plant investment was around 350 as compared to 100 at the end of 1950.

In other words, in 10 years an expansion of three and one-half times.

Secretary Dillon also testified:

So far as is known, no desirable expansion or modernization has been prevented by lack of readily available funds.

Expansion of interstate natural gas pipelines can be effectuated only with a certificate of convenience and necessity issued by the FPC. The Commission requires an affirmative showing of the adequacy of reserves before any such certificate will be granted. Certification procedures are designed to assure orderly growth in the industry and will limit the extent to which investment credit can stimulate growth.

On the basis of that clear statement by Secretary Dillon, I cannot imagine that there will be any increased investment because of the investment credit for gas pipe lines; but I am perfectly willing to have them treated in the same way that other utilities are treated.

Mr. PASTORE. In other words, the amendments would cause gas pipelines to be treated in the same way other utilities are treated—by receiving a 3-percent investment credit, instead of a 7-percent investment credit?

Mr. PROXMIRE. That is correct; that is all the amendments will do.

This amendment is a moderate amendment. It would not prevent the gas pipelines from receiving an investment credit. It would simply put them in the same category with every other utility under the bill.

Gas pipelines have all the attributes of other utilities. They are classified as utilities by every authoritative industrial and investment survey—whether Moody's or any other.

Furthermore, according to the Joint Committee on Reduction of Nonessential Federal Expenditures, this amendment would reduce the revenue loss of the bill by \$31.6 million. Mr. President, at a time when there is a deficit and when the deficit is increasing, it seems to me that such an amendment, which would, in effect, provide some additional revenue, should be supported.

Mr. LAUSCHE. Mr. President, will the Senator from Wisconsin yield?

Mr. PROXMIRE. I yield 2 minutes to the Senator from Ohio.

The PRESIDING OFFICER. The Senator from Ohio is recognized for 2 minutes.

Mr. LAUSCHE. Mr. President, I desire to support the amendments offered by the Senator from Wisconsin.

In his recommendation for a tax bill, the President omitted public utilities; he did not include them among the proposed recipients of the bounty that has been labeled a capital-investment incentive.

First, we included public utilities, and granted them a 3-percent tax credit as an inducement, although the representatives of the Government, occupying a position of impartiality, urged against including public utilities as beneficiaries.

Now we find that the gas pipelines are to receive, not the 3-percent credit, but the 7-percent credit. I cannot understand why that should be, in view of the testimony given by the Secretary of the Treasury, who said there is no need for this incentive, first, for the public utilities in general, and, second, much less for the gas pipelines. To one group, a 3-percent credit is to be given; to the other group, a 7-percent credit. What is the difference between them? Why is one given preferential treatment over the others? I cannot understand it.

I think there is logic in the argument which has been made by the Senator from Wisconsin that there should be equality of treatment for all of them.

The PRESIDING OFFICER. The time yielded to the Senator from Ohio has expired.

Mr. KERR. Mr. President, I yield myself 5 minutes.

The PRESIDING OFFICER. The Senator from Oklahoma is recognized for 5 minutes.

Mr. KERR. Mr. President, I rise to oppose the amendments.

These amendments did not originate in the Finance Committee. They originated in the House Ways and Means Committee, and they were adopted by the House.

Under the House version of the bill, all expenditures in connection with the transportation of commodities or humans are eligible for the 7-percent investment credit. Under this bill, the railroads, the trucks, the buses, the automobiles, the airlines, the ships, and the gas pipelines are to receive the 7-percent investment credit; all are to be treated alike.

Actually, I would think that the consumers of Wisconsin were more interested in the 7 percent given to interstate pipelines than in the 7 percent given to any other system of transportation, because interstate carriers of gas are utilities regulated by the Federal Power Commission. There may be State regulatory bodies that will fail to require a regulated private utility to pass on the 3-percent credit to the customers or consumers. I do not know of any. I am not saying there are, but I am saying there may be. But there is not a Member of the Senate who does not know that the Federal Power Commission will require the regulated interstate pipeline companies or transporters to pass on to the consumers the benefit of the 7-percent tax credit available to interstate gas pipelines.

The amendment of the Senator from Wisconsin is a little difficult for the Senator from Oklahoma to understand from the standpoint of the motivation back of it. Under the bill, a local gas distribution system gets only a 3-percent investment credit.

Since the interstate gas transporters are in the bill under the general classification of all transportation, they are treated alike and given 7 percent. But under the Senator's amendment, he would reduce the credit to interstate gas transportation companies from 7 percent to a 3 percent credit. He would increase the credit to a local gas distribution company from a 3-percent basis to a 7-percent basis.

There may be a reason for it and a justification for it. I do not know what they could possibly be. What the Senator would do would be to fix it so that the only transportation facility that would have its tax credit reduced from 7 to 3 percent would be the interstate gas pipeline company, which, above others, is strictly regulated to give the benefit in saving to the consumer. Yet the Senator from Wisconsin would fix it so that the only local utility in the Nation which is regulated that would be moved up from a 3- to 7-percent basis would be the local gas distribution company.

There may be a reason for that kind of amendment. The Senator from Oklahoma cannot comprehend it, and therefore, he must oppose it.

Mr. PROXMIRE. Mr. President, I had the amendment drafted carefully by the legislative counsel staff, and I checked it over and doublechecked it. I think they are competent personnel. There is nothing in my amendment that would increase the investment credit allowable to a gas distribution company from 3 to 7 percent. Both would receive a tax credit of 3 percent. It seems to me every argument made by the Senator from Oklahoma to the effect that transportation of gas by pipelines is done by utilities regulated by the Federal Power Commission would tend to support my position that they ought to be treated just like every other regulated utility.

It is interesting that the Senator from Oklahoma, who is a man of great ability, did not even discuss the argument made by the Secretary of the Treasury to the

effect that expansion of natural gas pipelines can be effectuated only by certificates of convenience and necessity by the Federal Power Commission, and that the Federal Power Commission issues those certificates only to sustain growth of the industry, and that a tax cut should be granted only to the extent that it will stimulate growth. The purpose of investment credit is to stimulate the industry to expand.

The Secretary of the Treasury, it seems to me, has established clearly that the investment credit will not stimulate expansion, cannot stimulate expansion, and it is no way to stimulate expansion of natural gas pipelines.

However, in equity, in view of the fact that other utilities are treated with a 3-percent tax credit, it makes sense to me that they should also be so treated.

MESSAGE FROM THE HOUSE

A message from the House of Representatives, by Mr. Maurer, one of its reading clerks, announced that the House had passed, without amendment, the following bills of the Senate:

S. 1108. An act authorizing the conveyance of certain property in the city of San Diego to the regents of the University of California;

S. 1878. An act to add certain lands to the Wasatch National Forest, Utah, and for other purposes;

S. 2421. An act to provide for retrocession of legislative jurisdiction over U.S. Naval Supply Depot Clearfield, Ogden, Utah;

S. 3071. An act for the relief of Hidayet Danish Nakashidze;

S. 3221. An act to provide for the exchange of certain lands in Puerto Rico; and

S. 3628. An act to amend title 10, United States Code, to authorize the appointment of citizens or nationals of the United States from American Samoa, Guam, or the Virgin Islands to the U.S. Military Academy, the U.S. Naval Academy, and the U.S. Air Force Academy.

The message also announced that the House had agreed to the report of the committee of conference on the disagreeing votes of the two Houses on the amendments of the House to the bill (S. 167) to authorize the Attorney General to compel the production of documentary evidence required in civil investigations for the enforcement of the antitrust laws, and for other purposes.

The message further announced that the House had agreed to the amendments of the Senate to each of the following bills of the House:

H.R. 852. An act to amend chapter 3 of title 38, United States Code, to authorize the Administrator of Veterans' Affairs to establish medical advisory panels to resolve conflicts of evidence in questions involving service connection of disabilities or deaths; and

H.R. 857. An act to amend section 4005 of title 38, United States Code, to provide that cases appealed to the Board of Veterans' Appeals shall contain a brief statement of the facts of the case appealed, with a citation and application of the law, together with the recommendations of the office appealed from, and for other purposes.

The message also announced that the House had agreed to the amendment of the Senate to each of the following bills of the House:

H.R. 860. An act to repeal certain obsolete provisions of title 38, United States Code, relating to unemployment compensation for Korean conflict veterans; and

H.R. 5234. An act to amend title 38, United States Code, to provide for the restoration of certain widows and children to the rolls upon annulment of their marriages or remarriages, and for other purposes.

The message further announced that the House had agreed to following concurrent resolutions, in which it requested the concurrence of the Senate:

H. Con. Res. 518. Concurrent resolution expressing sympathy for the victims of the recent earthquake in Iran; and

H. Con. Res. 519. Concurrent resolution requesting the President to return to the House the bill (H.R. 10062) extending the application of certain laws to American Samoa.

ENROLLED BILL SIGNED

The message also announced that the Speaker had affixed his signature to the enrolled bill (S. 476) to establish the Point Reyes National Seashore in the State of California, and for other purposes, and it was signed by the President pro tempore.

REVENUE ACT OF 1962

The Senate resumed the consideration of the bill (H.R. 10650) to amend the Internal Revenue Code of 1954 to provide a credit for investment in certain depreciable property, to eliminate certain defects and inequities, and for other purposes.

Mr. PROXMIRE. Mr. President, the Senator from Oklahoma has said we should treat pipelines not as utilities, but as transportation companies, which they are. The fact is that the comparison with oil pipelines, truck lines, and other forms of transportation is very imperfect indeed, because it is clear that the latter are not regulated utilities. While railroads might have some of that attribution, the fact is that railroads do not come close to earning a fair rate of return, unlike gas pipelines. So the comparison is not good. It seems to me that is where the gas pipelines belong. That is where my amendment puts them.

Mr. CARROLL. Mr. President, will the Senator yield for a question?

Mr. PROXMIRE. I yield to the Senator from Colorado.

Mr. CARROLL. Will the Senator inform me to what other interstate industry the 3-percent tax credit is applicable? I would fully agree with the argument of the Senator from Wisconsin about natural gas, but I would like to have him point out another interstate utility which is regulated and which comes in the same category. Railroads are not in the same category, so far as I know.

Mr. PROXMIRE. I said that. The argument of the Senator from Wisconsin is that in other interstate transportation the basis for limiting the tax credit to 3 percent—to wit, that there is a guaranteed fair return—does not apply, because many railroads do not come close to earning anything like a fair return on capital investment. All the railroads in my State are in that position.

Mr. CARROLL. I was thinking of private utilities. What other ones are in the interstate category?

Mr. PROXMIRE. There may be some power companies.

Mr. CARROLL. Is there any other industry that comes within the 3-percent category?

Mr. PROXMIRE. I am sure that many power companies sell power across State lines and they come, of course, under the 3-percent provision. I think the Senator makes an excellent point.

Mr. CARROLL. I was not sure whether they would be included.

Mr. PROXMIRE. The colloquy supports my position that there are many utilities that are in interstate commerce because they sell across State lines and they are in the 3-percent category.

Mr. CARROLL. Gas pipelines are under the supervision provided for in the Natural Gas Act. There is no question about it. It does not quite answer the argument of the Senator from Oklahoma. Is there anything in the record to show the other interstate utilities which are not going to get the 7-percent tax credit? I have not been advised on that question. I would like to have the Senator from Wisconsin advise us.

Mr. PROXMIRE. I think my position is clear. I think the comparison made with gas pipelines is imperfect. I think it should be with other utilities, not with other transportation methods or vehicles or institutions, because they are not vested with the same very excellent position which the gas pipelines enjoy—that of being in fact, in practice guaranteed a fair return—and the argument of the Secretary of the Treasury is very clear on it.

Mr. CARROLL. Will the Senator yield further?

Mr. PROXMIRE. My time is almost up.

Mr. CARROLL. The Senator from Oklahoma says there are none.

Mr. PROXMIRE. The decision for the Senate is very clear. It is whether the Senate feels gas pipelines should be classified as a public utility or as a means of transportation, and whether, therefore, they fall primarily within the category of utility rather than transportation.

Mr. KERR. Mr. President, I yield 1 more minute to the Senator from Wisconsin, if he needs time.

Mr. PROXMIRE. No; I am through.

Mr. KERR. Mr. President, I was interested in the question of the Senator from Colorado, as to whether there are no regulated interstate utilities which would get the 7 percent tax credit. The railroads will get it. They are regulated by the Interstate Commerce Commission. The airlines will get it. They are regulated by the Federal Aviation Agency. The Intercoastal shipping lines will get it. They are regulated on their rates. Interstate bus lines will get it, as will interstate truck lines, and they are all regulated by some regulatory body here in Washington. They would get the 7 percent, as is provided in the bill for the interstate gas pipeline.

The Senator said I was mistaken about the effect of the proposal. I ask Senators to turn to page 15 of the bill. Un-

der the amendment the Senator would take the interstate gas pipelines alone out of the transportation facilities. He would deny them the 7 percent which all other interstate transportation facilities would get, and would reduce it to 3 percent.

On line 11 of page 15 Senators will see the language:

(3) PUBLIC UTILITY PROPERTY.—

(A) In the case of section 38 property which is public utility property, the amount of the qualified investment shall be 3/7 of the amount determined under paragraph (1).

Mr. PROXMIRE. Mr. President, will the Senator yield?

Mr. KERR. No, I do not have time. This is the provision under which the utilities would go from 7 to 3 percent.

Mr. PROXMIRE. Will the Senator please let me explain that?

Mr. KERR. I ask for order, Mr. President.

Mr. PROXMIRE. Mr. President, will the Senator yield?

Mr. KERR. I do not yield.

The PRESIDING OFFICER. The Senator will be in order.

Mr. PROXMIRE. Mr. President, will the Senator yield?

The PRESIDING OFFICER. The Senator from Oklahoma has the floor.

Mr. KERR. The language further reads:

(B) For purposes of subparagraph (A), the term "public utility property" means property used predominantly in the trade or business of the furnishing or sale of—

(i) electrical energy, water, or sewage disposal services,

I continue to read, from the top of page 16:

(ii) gas through a local distribution system,

The pending amendment provides, in part:

On page 16, strike out lines 1 and 2—

Mr. PROXMIRE. I ask the Senator to read lines 1 and 2, and the language of my amendment. That is the answer.

Mr. KERR. The amendment states further:

and insert the following:

"(ii) transportation of gas by pipeline,"

Certainly. The Senator would bring it back to the transportation system after having eliminated the distribution system. Every Senator knows that if we should eliminate the distribution system from the three-sevenths basis we would put it back to the 7 percent basis. It is that simple.

The Senator from Oklahoma has no corner on the ability to read the amendment.

Mr. PROXMIRE. Mr. President, will the Senator yield, and permit me to have 30 seconds to explain?

Mr. KERR. I yield the Senator 30 seconds from my time. I have finished my presentation.

Mr. PROXMIRE. The amendment provides for striking out lines 1 and 2 on page 16 and inserting "transportation of gas by pipeline."

If the Senator will read the bill, he will find that the language is:

For purposes of subparagraph (A), the term "public utility property" means property used predominantly in the trade or business of the furnishing or sale of—

electrical energy, water, or sewage disposal services,

I submit that what that means is that gas would be treated as would an electrical energy distribution system, a water distribution system, or a sewage disposal distribution system.

I have been assured by the legislative counsel that this is so. That is adequate to answer the Senator's position.

There is simply no question as any Senator who can read can see that gas distribution under my amendment would get 3 percent, not 7 percent, investment credit.

Mr. KERR. I do not ask any Senator to go to legislative counsel. I merely ask Senators to read the amendment.

Mr. PROXMIRE. I ask them to do the same.

Mr. MANSFIELD rose.

Mr. KERR. Mr. President, I yield to the Senator from Montana.

EXPRESSION OF SYMPATHY FOR VICTIMS OF RECENT EARTHQUAKE IN IRAN

Mr. MANSFIELD. Mr. President, I ask unanimous consent that the Senate may proceed to the immediate consideration of House Concurrent Resolution 518.

The PRESIDING OFFICER. The resolution will be stated for the information of the Senate.

The legislative clerk read as follows:

Resolved by the House of Representatives (the Senate concurring), That the Congress of the United States has learned with shock and sorrow of the devastation caused by the recent earthquake in Iran, which resulted in the death of thousands of its people and injuries and loss of homes to many tens of thousands. The Congress, on behalf of the people of the United States, hereby expresses its deepest sympathy for the people of Iran.

The PRESIDING OFFICER. Is there objection to the request by the Senator from Montana?

There being no objection, the Senate proceeded to consider the concurrent resolution.

The PRESIDING OFFICER. The question is on agreeing to the concurrent resolution.

The resolution (H. Con. Res. 518) expressing sympathy for the victims of the recent earthquake in Iran, was agreed to.

EXTENSION OF CERTAIN LAWS TO AMERICAN SAMOA—REQUEST TO PRESIDENT TO RETURN BILL TO HOUSE OF REPRESENTATIVES

Mr. MANSFIELD. Mr. President, I ask unanimous consent that the Senate may proceed to the immediate consideration of House Concurrent Resolution 519.

The PRESIDING OFFICER. The resolution will be stated for the information of the Senate.

The legislative clerk read as follows:

Resolved by the House of Representatives (the Senate concurring), That the President of the United States is requested to return to the House of Representatives the enrolled bill (H.R. 10062) to extend the application of certain laws to American Samoa. If and when said bill is returned by the President, the action of the Presiding Officers of the two Houses in signing said bill shall be deemed rescinded; and the Clerk of the House is authorized and directed to reenroll said bill in accordance with the conference report thereon adopted by the two Houses.

The PRESIDING OFFICER. Is there objection to the request by the Senator from Montana?

There being no objection, the Senate proceeded to consider the concurrent resolution.

The PRESIDING OFFICER. The question is on agreeing to the concurrent resolution.

The resolution (H. Con. Res. 519) requesting the President to return to the House the bill (H.R. 10062) extending the application of certain laws to American Samoa, was agreed to.

COMMITTEE MEETING DURING SESSION OF THE SENATE TOMORROW

Mr. ELLENDER. Mr. President, I ask unanimous consent that the Committee on Agriculture and Forestry be authorized to meet during the session of the Senate tomorrow. I have consulted with both the majority and minority leaders, and there is no objection.

The PRESIDING OFFICER. Is there objection? The Chair hears none, and it is so ordered.

REVENUE ACT OF 1962

The Senate resumed the consideration of the bill (H.R. 10650) to amend the Internal Revenue Code of 1954 to provide a credit for investment in certain depreciable property, to eliminate certain defects and inequities, and for other purposes.

Mr. KERR. Mr. President, I yield back the remainder of my time.

The PRESIDING OFFICER. All time for debate has expired. The question is on agreeing to the amendments offered by the Senator from Wisconsin [Mr. PROXMIRE]. On this question the yeas and nays have been ordered, and the clerk will call the roll.

The Chief Clerk called the roll.

Mr. MANSFIELD. I announce that the Senator from Alaska [Mr. BARTLETT], the Senator from Nevada [Mr. BIBLE], the Senator from North Dakota [Mr. BURDICK], the Senator from Pennsylvania [Mr. CLARK], the Senator from Mississippi [Mr. EASTLAND], the Senator from Arkansas [Mr. FULBRIGHT], the Senator from Arizona [Mr. HAYDEN], the Senator from Minnesota [Mr. HUMPHREY], the Senator from Washington [Mr. MAGNUSON], the Senator from Montana [Mr. METCALF], the Senator from Utah [Mr. MOSS], the Senator from Maine [Mr. MUSKIE], the Senator from Oregon [Mrs. NEUBERGER], the Senator from Florida [Mr. SMATHERS], the Sena-

tor from Massachusetts [Mr. SMITH], the Senator from Georgia [Mr. TALMADGE], and the Senator from Texas [Mr. YARBOROUGH] are absent on official business.

I further announce that, if present and voting, the Senator from Nevada [Mr. BIBLE], the Senator from Wyoming [Mr. HICKEY], and the Senator from Alaska [Mr. BARTLETT] would each vote "nay."

I further announce that the Senator from New Mexico [Mr. ANDERSON], the Senator from Alaska [Mr. GRUENING], the Senator from Wyoming [Mr. HICKEY], and the Senator from Missouri [Mr. SYMINGTON], are necessarily absent.

On this vote, the Senator from Pennsylvania [Mr. CLARK] is paired with the Senator from Mississippi [Mr. EASTLAND]. If present and voting, the Senator from Pennsylvania would vote "yea," and the Senator from Mississippi would vote "nay."

On this vote, the Senator from Washington [Mr. MAGNUSON] is paired with the Senator from Missouri [Mr. SYMINGTON]. If present and voting the Senator from Washington would vote "yea," and the Senator from Missouri would vote "nay."

On this vote, the Senator from Oregon [Mrs. NEUBERGER] is paired with the Senator from Georgia [Mr. TALMADGE]. If present and voting, the Senator from Oregon would vote "yea," and the Senator from Georgia would vote "nay."

On this vote, the Senator from Florida [Mr. SMATHERS] is paired with the Senator from Massachusetts [Mr. SMITH]. If present and voting, the Senator from Florida would vote "nay," and the Senator from Massachusetts would vote "yea."

Mr. DIRKSEN. I announce that the Senator from Maryland [Mr. BEALL], the Senator from Utah [Mr. BENNETT], the Senator from South Dakota [Mr. BOTTUM], the Senator from Indiana [Mr. CAPEHART], the Senators from New Hampshire [Mr. COTTON and Mr. MURPHY], the Senator from Arizona [Mr. GOLDWATER], the Senator from Idaho [Mr. JORDAN], the Senator from California [Mr. KUCHEL], the Senator from Kentucky [Mr. MORTON], the Senator from Massachusetts [Mr. SALTONSTALL], the Senator from Pennsylvania [Mr. SCOTT], and the Senator from Delaware [Mr. WILLIAMS] are necessarily absent.

The Senator from New York [Mr. JAVITS] is detained on official business.

If present and voting, the Senator from Maryland [Mr. BEALL], the Senator from Utah [Mr. BENNETT], the Senator from South Dakota [Mr. BOTTUM], the Senator from Idaho [Mr. JORDAN], the Senator from California [Mr. KUCHEL], and the Senator from Massachusetts [Mr. SALTONSTALL] would each vote "nay."

On this vote, the Senator from New York [Mr. JAVITS] is paired with the Senator from Indiana [Mr. CAPEHART]. If present and voting, the Senator from New York would vote "yea," and the Senator from Indiana would vote "nay."

The result was announced—yeas 27, nays 38, as follows:

[No. 237 Leg.]

YEAS—27

Aiken
Byrd, Va.
Cannon
Case
Church
Cooper
Dodd
Douglas
Gore

Hart
Hartke
Jackson
Keating
Kefauver
Lausche
Long, Hawaii
McNamara
Morse

Pastore
Pell
Proxmire
Robertson
Russell
Stennis
Thurmond
Williams, N.J.
Young, Ohio

NAYS—38

Allott
Boggs
Bush
Butler
Byrd, W. Va.
Carlson
Carroll
Chavez
Curtis
Dirksen
Ellender
Engle
Ervin

Fong
Hickenlooper
Hill
Holland
Hruska
Johnston
Jordan, N.C.
Kerr
Long, Mo.
Long, La.
Mansfield
McCarthy
McClellan

McGee
Miller
Monroney
Mundt
Pearson
Prouty
Randolph
Smith, Maine
Sparkman
Tower
Wiley
Young, N. Dak.

NOT VOTING—35

Anderson
Bartlett
Beall
Bennett
Bible
Bottum
Burdick
Capehart
Clark
Cotton
Eastland
Fulbright

Goldwater
Gruening
Hayden
Hickey
Humphrey
Javits
Jordan, Idaho
Kuchel
Magnuson
Metcalf
Morton
Moss

Murphy
Muskie
Neuberger
Saltonstall
Scott
Smathers
Smith, Mass.
Symington
Talmadge
Williams, Del.
Yarborough

So Mr. PROXMIRE'S amendments G were rejected.

Mr. LONG of Louisiana. Mr. President, I move to reconsider the vote by which the amendment was rejected.

Mr. MANSFIELD. Mr. President, I move to lay that motion on the table.

The motion to lay on the table was agreed to.

Mr. GORE. Mr. President, I offer my amendment 8-31-62—A, and ask that it be stated.

The PRESIDING OFFICER. The amendment of the Senator from Tennessee will be stated.

The CHIEF CLERK. On page 41, line 18, it is proposed to strike out "or associated with" and insert "and directly connected with".

On page 42, line 4, it is proposed to strike out "or associated with" and insert "and directly connected with".

On page 42, line 7, it is proposed to strike out "or associated with" and insert "and directly connected with".

The PRESIDING OFFICER. The question is on agreeing to the amendment of the Senator from Tennessee.

Mr. GORE. Mr. President, I shall detain the Senate but a few moments on the amendment, having debated perhaps at greater length than I should have the liberality of the bill with respect to expense accounts.

If Senators will be so kind as to pick up a copy of the bill and turn to page 41, I can explain my amendment very quickly. The amendment would strike out, in line 18, page 41, the three words "or associated with," and insert in lieu thereof the words "and directly connected with."

The same amendment would be repeated twice on page 42.

On page 41 is found a general rule for expense account deductions. If the Senate wishes to confine tax deductions for entertainment, recreation, and amusement to functions which are directly connected with and related to a business function, the pending amendment is necessary. On the other hand, if Senators wish to permit deductions for entertainment, amusement, and recreation for vague good will, so long as it is indirectly associated with some business purpose or prospective business purpose, they should vote against my amendment.

I emphasize that on page 41 of the bill, is the general rule for deduction of expenditures for entertainment, amusement, or recreation.

My amendment would make the general rule tight, as the House bill did. My amendment would strike out the three little words "or associated with," which blow the lid off.

I invite the attention of Senators to the exceptions to the general rule on page 45 of the bill.

Subsection (a) on page 41 states the general rule. It begins in line 10. If Senators will follow me by turning to page 45, line 8, they will find the specific exceptions to the application of subsection (a), which is the general rule. There are about four pages of exceptions.

If Senators will read the exceptions—nine of them—they will see that they are not covered by the general rule. It has been my view that the nine exceptions permit deductions for entertainment, amusement, and recreation and other expenses which are more generous than Congress and the Government should permit.

I would prefer the original recommendation of the President, but that is not now before the Senate. What I am talking about now is the pending bill. If Senators wish to see how broad these exceptions are, I ask them to look at the report of the committee, which is on the desk of each Senator. I ask Senators to turn to page 36. There they will find the exceptions spelled out in detail. I should like to read brief excerpts from the report:

Expenses for food and beverages furnished under circumstances which are of a type generally considered to be conducive to a business discussion.

The language makes it plain that this is a deductible expense. The report continues:

Under this exception, the general custom of entertaining business guests at meals in restaurants and hotels would not be disallowed if they meet the ordinary and necessary test of existing law.

Some of my colleagues seem to be disturbed for fear that expenses in connection with attending conventions might not be deductible, and that expenses of entertainment in a hotel or restaurant which are related to business might not be permitted. The bill makes it perfectly plain, and the committee report makes

it perfectly plain, that if these expenses are directly related to a business function, the tax deduction is permitted.

What I am trying to strike out is the amendment of the committee which blows the lid off, which allows almost anything to be tax deductible. I have challenged Senators to name something for which a tax deduction could not be claimed which is now permissible. Of course Senators have been able to cite a few things for which tax deductions would not be permitted, but the tax deduction is not permissible for this item now in almost every instance that has been cited.

I should like to read from the bill the nine exceptions. I will read the titles:

Business meals.

The committee report makes it perfectly plain that these would be allowed. Subsection (1) reads:

(1) **BUSINESS MEALS.**—Expenses for food and beverages furnished to any individual under circumstances which (taking into account the surroundings in which furnished, the taxpayer's trade, business, or income-producing activity and the relationship to such trade, business, or activity of the persons to whom the food and beverages are furnished) are of a type generally considered to be conducive to a business discussion.

Suppose this is at a convention, and a businessman attending that convention gives a luncheon to which guests are invited—guests who in some way offer an opportunity for further business. I have just read the provision of the bill which I do not seek now to change. That provision makes this expense tax deductible. There is no question about it. Let me read the next items:

2. Food and beverages for employees.
3. Expenses treated as compensation.
4. Reimbursed expenses.
5. Recreation, etc., expenses for employees.
6. Employee, stockholder, etc., business meetings.
7. Meetings of business leagues, etc.

I should like to read what the bill and the committee report say of No. 7.

I read from page 47 of the bill, subsection (7):

Meetings of business leagues, etc.—Expenses directly related and necessary to attendance at a business meeting or convention of any organization described in section 501(c)(6) (relating to business leagues, chambers of commerce, real estate boards, and boards of trade) and exempt from taxation under section 501(a).

Now I shall read what the committee report says on that subject:

Expenses directly related and necessary to attendance at a business meeting of an organization, such as a trade association, chamber of commerce, real estate board, etc., described in section 501(c)(6) of the Code.

I now read subparagraph (8), on page 47 of the bill:

Items available to public.—Expenses for goods, services, and facilities made available by the taxpayer to the general public.

(9) Entertainment sold to customers.—Expenses for goods or services (including the use of facilities) which are sold by the taxpayer in a bona fide transaction for an adequate and full consideration in money or money's worth.

When we consider that on pages 41 and 42 of the bill is set forth the general rule, I submit that the general rule should be strict, particularly when more than three pages of exceptions are provided, citing specific instances in which legitimate expenditures for purposes which are directly related to or connected with the business, will be tax deductible. What Senator wishes to go further than that? We want to give a tax deduction for every legitimate expenditure that is spelled out in these exceptions for business functions that are directly related to business. That is provided in the bill. But when we add, in the general rule, the words "or associated with," together with the interpretation of the legislative intent of those three words, the sky is the limit, and the exceptions come to have no meaning at all, and no reason for being.

Therefore, I offered an amendment to strike out the words which were added by the Senate committee amendment, "or associated with," and substitute therefor the words "and directly connected with."

I shall not detain the Senate further. The issue is simple. I have done my best in a brief time to explain the provisions of the bill. I hope Senators do not wish to go further than to allow a tax deduction for legitimate business expenses. But I say in all candor and sincerity that if we go further than that, I do not think it will be right. That is why I am so wrought up about the three little words that make the sky the limit.

Mr. BUSH. Mr. President, will the Senator from Tennessee yield?

Mr. GORE. I yield.

Mr. BUSH. It seems to me that we went all through this discussion about a week ago. I voted for an amendment similar to this. I cannot quite see the difference between what the Senator from Tennessee is now proposing and what he proposed last week.

Mr. GORE. The Senator from Connecticut makes a valid point. I opposed, and the Senator from Connecticut opposed, the committee amendment which wrote into the bill the words "or associated with."

Mr. BUSH. That is correct.

Mr. GORE. But under the parliamentary rule, after the committee amendments had been acted upon, the bill became original text. Therefore, although my amendment would accomplish the same purpose as if the Senate had defeated the committee amendment, I do have the parliamentary right to offer it again.

Mr. BUSH. And that is what the Senator is doing?

Mr. GORE. That is what I am doing. I hope—perhaps I am hoping against hope—that upon careful reconsideration the Senate will not persist in a deliberate desire to give a tax deduction for something which is not a legitimate business expense, that is, connected with the business. Therefore, I shall not insist further. So far as I am concerned, the Senate can vote viva voce.

Mr. ELLENDER. Mr. President, will the Senator yield for a question?

Mr. GORE. I yield.

Mr. ELLENDER. I have been trying to follow the argument of the distinguished Senator from Tennessee. I cannot see much difference between the words "associated" and "connected." The Senator's amendment does not in any way affect the exemptions to which he referred a moment ago, does it?

Mr. GORE. No; my amendment would not modify the exceptions at all.

Mr. ELLENDER. What the Senator is attempting to do is to use the word "connected" so that it will more or less be in accord with the interpretations placed in the report?

Mr. GORE. The Senator will note that I use the conjunction "and" instead of "or." As the bill is now written, a deduction would be allowed on an "or" basis; but when one reads the committee report interpretation of the words "or associated with," he sees that the sky is the limit. According to the committee report, these three words were placed in the bill to eliminate the strict general rule as interpreted in the report of the Ways and Means Committee. Do I make myself clear?

Mr. ELLENDER. That is what I suggested.

Mr. GORE. The point I am trying to make is that my amendment would not modify the specific exceptions. There are 9 of them, and they are generous, indeed. My amendment would prevent the general rule from being so loose, so indefinite, as to permit almost anything as a so-called deductible expenditure associated with business.

Mr. ELLENDER. The language used by the Senator would be more in accord with the House report.

Mr. GORE. I agree.

The PRESIDING OFFICER. The question is on agreeing to the amendment of the Senator from Tennessee. [Putting the question.]

Mr. LONG of Louisiana. Mr. President, on this question, I ask for a division.

On a division, the amendment was rejected.

Mr. KERR. Mr. President, I move that the action whereby the amendment was rejected be reconsidered.

Mr. BUSH. Mr. President, I move to lay that motion on the table.

The motion to lay on the table was agreed to.

DELETE LOBBYING AMENDMENT

Mr. DOUGLAS. Mr. President, I call up my amendment designated "8-25-62—G" and ask that it be read.

The PRESIDING OFFICER. The amendment will be stated.

The CHIEF CLERK. On page 38, beginning with line 17, it is proposed to strike out all through line 21 on page 40—section 3 of the bill, relating to appearances, and so forth, with respect to legislation.

Mr. DOUGLAS. Mr. President, it is with a sense of deep discouragement that I rise to propose this amendment. During the past weeks we have seen included in the bill provision after provision unjustly designed to favor large corporations, and we have seen defeated amend-

ment after amendment intended to introduce a greater degree of tax reform into our laws. These votes have been overwhelming. The leadership on both sides of the aisle have tried to protect the wealthy and powerful, have opposed the administration in connection with many crucial features, and have opposed provisions designed to protect the general taxpayers and the Treasury.

So, Mr. President, in the light of past performance, I have little expectation that my amendment will be adopted.

Nevertheless, it is one's duty to remain at one's post and discharge what one conceives to be one's obligation, even though the odds against one are heavy. The first general order to which a soldier must be faithful is not to leave his post unless he is properly relieved. So long as one serves in the Senate, he has the obligation, even though he stands with a very small group, to try to make legislation as good as possible.

WHAT THE HOUSE DID

My amendment deals with lobbying. It aims at striking out two provisions which were not in the original bill submitted by the President, and to which, indeed, the administration says it is opposed. One of these amendments was inserted by the House Ways and Means Committee at the last minute—no one knows quite why. The bill then went to the House under a closed rule which prohibited amendments, and which only permitted the body of the House to vote either for the bill as a whole or against the bill as a whole. It is the amendment which permitted tax deductions for expenses incurred in direct appearances by business groups and corporations before legislative bodies—not only the traveling expenses, but also all other expenses incurred by a trade or business in connection with such appearances.

This would apply whether the appearances were before local bodies, such as city councils, or whether they were before State legislatures or the Congress; and it would include the cost of preparing testimony and the cost of all the research and developmental work in that connection. It would also permit deductions of the expenses of mass appearances, not only individual appearances and dues by organizations which lobbied for their divers business interests. That was the House provision; and it is to be found on page 39, between line 5 and line 23.

WHAT THE FINANCE COMMITTEE DID

Then the Senate Finance Committee went one better—or one worse—than that; it voted to permit deductions for lobbying costs connected with communications between a business firm and their employees or stockholders, with respect to legislation or proposed legislation of direct monetary interest to the taxpayer. That amendment was approved by a very large majority in the Senate Finance Committee, with the Senator from Tennessee, the Senator from Illinois, and perhaps one or two other Senators voting in the negative.

If these two amendments are enacted, we shall legitimize very large amounts of expenditures by special interests, for the purpose of effecting legislation, while

denying any comparable right to those who seek to defend the general interest, whether they comprise consumers, small taxpayers, or general citizens. I think it is worthwhile for us to know what the existing law on this subject really is.

EXISTING LAW—LOBBYING NOT DEDUCTIBLE

Following the Cammarano decision, there was affirmed the principle that the tax laws should be neutral insofar as lobbying is concerned, and that expenditures by business groups before legislative bodies for the purpose of furthering their own financial interests, are not tax deductible. There can be no question of their right to appear before legislative groups or regulatory bodies; that is a part of their right as citizens. There is no intent to deprive them of their right of petition. But up until now, at least, the law has been that they should pay for such appearances themselves; that Uncle Sam should not pay 52 percent of the cost of such appearances, by exempting those amounts from the corporate income tax.

On the other hand, those who appear because of a general interest as consumers or as small taxpayers are expected to pay these costs themselves. If they feel that a given tax measure, such as the present one, is against the public interest, and if they wish to testify against it, and if they go to the expense of appearing and testifying, they must pay the costs themselves; they may not be charged off as expenses, and the taxpayer may not obtain a tax deduction for them. That is the law—namely, that the tax system shall be neutral insofar as lobbying costs are concerned.

But we well know that, in practice, business concerns frequently are able to evade or avoid the meaning of the law, by disguising lobbying expenses and putting them in other categories. Instead of hiring "lobbyists," they will hire "attorneys" or "economists" or "research specialists"; and these men will appear, not as "lobbyists," but as "legal representatives." They will put lawyers on retainer—ostensibly to be called upon for legal services, but in reality held in reserve to influence legislation.

PRESENT LAW RESTRAINS BAD PRACTICE EVEN IF NOT PERFECT

In practice, a great deal of the lobbying expenses of the corporations and the big industries of the country are charged off as business expenses and escape taxation; but the law holds these expenditures in some degree of restraint. It is not a perfect protection, by any means, but it operates to some degree as a restraint.

If anyone looks at the political scene, and the pressures operating on city councils, and on State legislatures, and on the Congress of the United States, I think he would have to say that the large companies of this country are not unduly handicapped. Quite the contrary, they are very powerful. They spend large sums of money. They are able to shape and influence legislation. They are very powerful.

GENERAL INTEREST WEAK

The general interest, however, is already extremely weak. Any particular measure, such as the gas bill, which our

good friend from Oklahoma got through the Senate in 1950, and helped to get through in 1956, may mean a gain of \$600 million a year to the producers, but it will only cost, let us say, \$20 a year to each of the 30 million consumers who use gas for household purposes. And the consumer has so many things on his or her mind that it is hard to get excited over \$20 a year, or 5 or 6 cents a day. And so the great mass of consumers tend not to be interested in this measure, or, if they are interested in it, they hardly feel it is worth their while to go to the labor and expense of running up against these powerful lobbies when their own interests are so infinitesimal.

So, as I said on the floor of the Senate last week, the struggle all too often is one in which the concentrated power of the producing interests conquers over the diffused general interest.

LOBBYING FOR TAX PRIVILEGES

And it is so in tax measures, too. Those who seek special favors in getting a particular measure which will mean millions, tens of millions, and hundreds of millions of dollars to them, can carry on quite a campaign. The individual taxpayer among the 60 million who pay income taxes will not be greatly affected. But, of course, what happens is that, special privilege, after special privilege, after special privilege is able to write these measures into the laws and administrative rulings of the Nation, the general interest, the general taxpayer, the general consumer, becomes burdened with a multitude of exactions which, taken in their totality, are extreme and great.

This, I think, is one of the great weaknesses of modern democracy.

BILL MAKES MATTERS WORSE

These two amendments would make the situation much worse, because now, instead of the corporations meeting these costs, the Government will instead meet 52 percent of the costs, and the small taxpayers themselves will have to underwrite the lobbying campaigns, which, in a large percentage of the cases, are directed against them. The small taxpayers not only have to pay for any efforts they make on behalf of the public interest but they do not get any tax exemptions for them. In addition, they have to pay half the cost of the lobbying expenses of these selfish special interests which want to get special favors for themselves. I think this section of the bill adds insult to injury.

DOUBLE STANDARD DEVISED

Now let us take up a few of the measures which have come before the Senate. Suppose we take the matter of drug safety or drug pricing. The costs of presenting the views of the drug manufacturers or distributors would be deductible. The general taxpayer would meet half of those costs. But the cost of presenting evidence on behalf of the consumers or of disinterested professional or technical advisers would not be tax deductible.

Suppose, on the State level, that a State legislature is debating a measure designed to decrease stream pollution. Manufacturers who dump industrial wastes into the rivers, who would be ad-

versely affected by the enactment of such a law, could deduct the cost of their opposition. Members of the public interested in pure water for drinking or for recreational uses would have to finance their support of the measure entirely from their own pockets.

Or, at the local level, a business owner of a piece of real estate could file an advantageous amendment of a local zoning ordinance and deduct the cost of his presentation and appearance before the local city council; but owners of nearby residences would not receive this help from the Federal Treasury in the preparation of exhibits and briefs necessary for effective opposition.

LOBBYING CAMPAIGNS DEDUCTIBLE

In the great struggle in which some of us went down to overwhelming defeat last week, that of withholding of the basic income tax on interest and dividends, the building and loan associations and the banks and mutual savings banks, which launched one of the greatest lobbies and letter campaigns ever seen in the history of the United States or of this body, could deduct not merely the cost of their direct appearances, but also the cost of the letterwriting campaign. For they circularized not merely their employees, but also their members and their stockholders. As a result many Senators, and I assume each Senator, received scores of thousands of letters. I have stated before that I received 75,000. Another Senator has said that he received over 50,000. I know of other cases where the number was almost as great.

This amendment, once passed, will permit these building and loan associations and banks to deduct the cost of their circularizing their members and stockholders, and Uncle Sam will pay 52 percent of the bill.

Mr. BUSH. Mr. President, will the Senator yield at that point?

Mr. DOUGLAS. I yield.

Mr. BUSH. My recollection is that I received thousands of letters on that subject, too, but they were all paid for by the individual citizens themselves, who were protesting against that provision of the bill.

May I say to the Senator it seems to me that what the building and loan associations and the savings banks may have done was, in sending out their normal monthly statements, or whatever they send out, to enclose a statement which alerted the saver to the issue before the Senate. I would say the great bulk of the expense incurred by that corporation was incurred by the savers themselves, the citizens themselves.

Mr. DOUGLAS. First let me say that these members and depositors in the building and loan associations and in the savings banks did not write to us in an unsolicited fashion. They were solicited by the institutions. In some cases, as the Senator says, slips were sent out with the ordinary dividend statements.

At least in those cases the cost of printing of the slips would be tax deductible under the committee amendment. In a very large proportion of the cases however the people were circular-

ized by individual letter. Many savings institutions mailed a letter to each one of their depositors or members, asking them to write to their Senators protesting against the measure.

At present this type of communication is legally not tax deductible, although I grant that frequently it is very hard for the Internal Revenue Service agents to go through the books and to detect precisely the postage and printing and expense involved on these particular letters.

In this case the Finance Committee amendment would permit these types of costs to be tax deductible, and 52 percent of the cost would be borne by the general public.

POWERFUL GROUPS STRENGTHENED

Mr. President, one of the weaknesses of modern democracy, as I have said, is the extraordinary disparity between the great and concentrated power of special and powerful interests and the diffused weakness of the general interest. The committee and House amendments would still further intensify and accentuate this lack of balance.

I fear that what the Senate is about to do, with the cooperation of the leadership on both sides of the aisle—if it is about to do what I fear it will do—will help to drive another nail in the coffin of effective political democracy.

I am not going to speak more on this subject although I will answer questions.

Mr. PROXMIRE. Mr. President, will the Senator yield?

Mr. DOUGLAS. Yes, I am glad to yield.

Mr. PROXMIRE. Under the provision in the bill, if a gambling syndicate, a group of liquor dealers, or others wished to support or to oppose proposed legislation, which involved their particular interests, and they hired an expert to do all of the research they wished to have done, so that they could make a strong case, how much of the expense would the general taxpayer be required to pay, assuming a large corporation were involved?

Mr. DOUGLAS. Fifty-two percent.

Mr. PROXMIRE. Assuming that the action on the part of the liquor lobby or on the part of the gambling lobby was opposed by a group of clergymen or a group of people who felt very strongly that the action might adversely affect the morals of the people of the community, or the moral fiber of the community, how much of their expense would that group be allowed to subtract from taxes?

Mr. DOUGLAS. Not 1 cent.

Mr. PROXMIRE. Suppose one of these big financial corporations wished to send not 1 or 2 or even 3, but a very large number of skilled lobbyists to Washington, so that there could be assigned 1 man to each 10 Senators and Representatives in Congress, at a big expense, how much of that expense would the general taxpayer have to bear?

Mr. DOUGLAS. Fifty-two percent.

Mr. PROXMIRE. Would it be possible under the Senate version of the bill for a very large corporation, such as Du Pont or American Telephone & Telegraph Co., which might have an in-

terest in legislation pending before the Congress, to send out literature, or to send out men, for that matter—to send out communications in almost any manner—to stimulate the stockholders or the employees to support the position of the company? If they did so, how much of the expense would the general taxpayer have to bear?

Mr. DOUGLAS. Under the bill as it comes to us, the corporation would be able to avoid the payment of the corporate income tax on these expenditures, and the general taxpayer would pay 52 percent of the expenditures.

Mr. PROXMIRE. The Senator from Illinois has served in this body since 1949. He also served on the Chicago City Council some years before that.

Mr. DOUGLAS. The Senator is correct.

Mr. PROXMIRE. The Senator has had great experience. Has the Senator ever felt lonely, in the sense that he was ignored by special interest groups which had an interest in advancing themselves? Has the Senator ever felt he did not have a sufficient number of lobbyists writing to him, coming to see him, or contacting him? Does the Senator feel he needs these "pen pals," only more so?

Mr. DOUGLAS. I believe in the right of petition, and I believe that business concerns have a right to have lobbyists. I try to see them and to listen to their arguments. Very frequently they are able to present information which I did not previously have. Very frequently they are able to present arguments of which I was not previously aware. I think they carry out, properly, a very valuable function.

Mr. PROXMIRE. I share that viewpoint.

Mr. DOUGLAS. What I object to is the granting to the big corporations, which have a direct business and financial interest, of a tax deduction of 52 percent, whereas the people who are trying to defend the general interest have to pay all of their expenses from their own pockets, though they already suffer from the disadvantage that their interest in a particular measure may be slight, although the concentrated interest of the producing or business group is tremendous.

Mr. PROXMIRE. The question asked by the Senator from Wisconsin went to a different point. I heard a Member of the House of Representatives protest this provision in the law quite vigorously. He argued that he is now swamped with special interest group proposals.

What the Senator has said is true. These people often perform very valuable service. They ought to have a right to present their viewpoint.

Is it not very likely, however, that if the bill shall pass, the staffs of all Senators will be deluged with even more correspondence? My staff must spend some 70 percent of its time, or more, answering mail. I have to spend a great deal of my time talking to people who have a special interest in proposed legislation.

Along with the Senator from Illinois, I am happy to do that, but I must say that if this provision in the bill is made

law, the burden may likely become nearly intolerable. There will be an incentive for corporations to send representatives to the Congress, with the general taxpayer forced to pay 52 percent of the cost. It seems to me this would greatly increase the burden on Members of Congress. Is that not a correct assumption?

Mr. DOUGLAS. I think the Senator from Wisconsin is completely correct.

In the old days, after the Civil War, when Sam Ward was the king of the lobby, he used to entertain Members of Congress with champagne suppers, and there would be shares of stock to be distributed and cash as well.

EXAMPLES OF MAIL CAMPAIGNS

I think the modern lobbyist operates in a more wholesale fashion. He is increasingly trying to muster mail campaigns from constituents. This bill would open the gates for tremendous mail campaigns.

The doctors loosed one on health care for the aged. I am sure they will now seek to deduct the costs of that campaign from their personal incomes.

The savings institutions loosed a tremendous campaign with respect to withholding. The various interests seeking to get protective tariffs or to prevent the trade bill from going through in any effective form will be able to make deductions.

We are all acquainted with the historic struggle between the truckers and the railroads on piggybacks which swamped our offices with mail. I received, I think, 10,000 letters from the truckers, and then I received about 15,000 from the railways. A Senator has to answer all that mail.

The Senator from Wisconsin is quite correct. A large proportion of our time is now devoted to attempting to respond to the pressures which come upon us. One can stand up under it and would welcome it, but to have the general taxpayer called upon to finance special interests is more than I can personally understand.

Mr. PROXMIRE. I should like to ask the Senator to answer arguments raised by those who favor this provision in the bill reported by the committee. I refer the Senator to page 22 of the committee report, in which the majority, which favors this position, says:

The difficulty in allowing trade or business expenses generally, but isolating expenses relating to legislative matters and denying deductions for them, stems in part from the difficulty in segregating and classifying such expenses. This is a form of detailed record-keeping to which taxpayers are not accustomed. Moreover, in the case of many expenses which may primarily be incurred to inform the business itself as to the application of certain proposed legislation, when such information is also made available to legislators it is difficult to determine how an allocation of the expense should be made between legislation and mere planning of the company.

It has been the experience of the Senator from Wisconsin that that would involve no difficulty.

Mr. DOUGLAS. None at all. These costs could be segregated.

Mr. PROXMIRE. And that has been the law until now.

Mr. DOUGLAS. That is correct. It is a law which has been imperfectly executed, but one which has had some restraining influence.

Mr. PROXMIRE. Why would it not be perfectly possible for a business firm to keep track of the cost of hiring its lobbyists and exclude the cost from its expenses in computing its taxes?

Mr. DOUGLAS. And also the cost of correspondence designed to influence legislation. Those costs could be segregated. We must do so in our own offices in segregating our personal mail from our official mail.

Mr. PROXMIRE. The next point about which the Senator from Wisconsin wishes to ask the Senator from Illinois is the provision in the argument in the committee report a little further down, as follows:

It appears anomalous, for example, that expenses incurred in appearing before legislative bodies or before legislators are not deductible while appearances before executive or administrative officials with respect to administrative matters, or before the courts with respect to judicial matters, are deductible where the expenses otherwise qualify as trade or business expenses.

Does it not occur to the Senator from Illinois that legislation should be and must be a matter of general interest and cover the whole generality of the body politic?

Mr. DOUGLAS. That is correct.

Mr. PROXMIRE. All 180 million Americans without discrimination?

Mr. DOUGLAS. That is correct.

Mr. PROXMIRE. To design legislation for a specific industry or individual would be the worst thing that could happen in respect to legislation. In other words, legislation should be designed to apply equally to all people. It should not be designed, as regulations sometimes must be, or as decisions by the administration under the law must be, in accordance with a particular special interest involved.

Mr. DOUGLAS. The Senator from Wisconsin has made an admirable reply to his own question. Proceedings before a regulatory body are necessarily narrow and refer to special and particular interests; and it is legitimate for such special and particular interests to deduct their expenses connected with appearing to defend their interests. But as the Senator has said, it is an entirely different thing when we deal with legislation supposedly affecting all people as equally as possible.

Mr. PROXMIRE. At the bottom of page 23 of the committee report it is stated—

The bill also provides that where a taxpayer is a member of an organization and the organization pays or incurs the expenses of the types referred to above on behalf of its members, the dues which the taxpayer pays to the organization in carrying on his trade or business are to be deductible to the extent they are used for such purposes.

As I understand, what that language means in the way the bill is drafted and is interpreted at other places, too, in the

committee report, is an organization—whether it be the National Association of Manufacturers, the chamber of commerce, or other group—which is representing the particular pecuniary interest of the member.

Mr. DOUGLAS. That is correct.

Mr. PROXMIRE. Under those circumstances dues could be subtracted.

Mr. DOUGLAS. That is correct.

Mr. PROXMIRE. On the other hand, if one wishes to contribute to a church group, the League of Women Voters, the Civil Liberties Union, or the Americans for Constitutional Government, the contribution could not be subtracted because the expense is not directly related to one's making a living. Is that correct?

Mr. DOUGLAS. That is correct.

Mr. PROXMIRE. Such interpretation would particularly discriminate against groups which fight for the public interest as they see it, whether they are conservatives, liberals, or whatever they are.

Mr. MILLER. Mr. President, will the Senator yield at that point for a clarification of the RECORD?

Mr. DOUGLAS. I yield.

Mr. MILLER. Referring to the dues to which the Senator from Wisconsin alluded—for example, in connection with the Chamber of Commerce—would not that interpretation be applicable to the portion of the dues of the union member paying union dues?

Mr. DOUGLAS. It might be; but off-hand I am not certain.

Mr. MILLER. Insofar as such dues might be used by the union organization in connection with its legislative activities?

Mr. DOUGLAS. It might be held that the interest in question was a general interest and not a direct pecuniary interest.

Mr. PROXMIRE. It is the understanding of the Senator from Wisconsin that union dues are deductible in computing income taxes. Is that true?

Mr. DOUGLAS. Most union members do not take the deduction.

Mr. PROXMIRE. They do not itemize their returns.

Mr. DOUGLAS. That is correct.

Mr. PROXMIRE. So they do not get the benefit either way.

I should like to ask the Senator from Illinois two additional questions on the point, because I think it is important. The majority argues that in the provisions of the bill there are exceptions to safeguard public interest. They say:

It is not intended by your committee that any deduction be allowed for an amount paid or incurred for participation or intervention in any political campaign for any candidate.

That is in the second paragraph on page 24. While that may be correct, is it not perfectly possible that in case after case there may be an overwhelming issue between candidates for public office? In those circumstances, under the terms of the bill a large corporation could circularize all its employees in many towns—that could mean most of the people who live in the town.

Mr. DOUGLAS. That is correct.

Mr. PROXMIRE. In many States they may be the dominant force in the State.

Mr. DOUGLAS. That is correct.

Mr. PROXMIRE. Without mentioning names all the stockholders could be circularized to take a position in effect in favor of candidate A as against candidate B.

Mr. DOUGLAS. The material distributed would not mention the candidates but would mention the issues which everyone would know divided candidate A and candidate B; and the company could take a stand on the issues with its stockholders and employees, charge off the expense, and get a tax deduction.

Mr. PROXMIRE. So one-half of that kind of politicking would be paid for by all the taxpayers throughout the country as a result of the company taking a deduction from its income tax.

Mr. DOUGLAS. That is correct.

Mr. BUSH. Mr. President, will the Senator yield for a question?

Mr. DOUGLAS. I yield.

Mr. BUSH. Would not the language on page 40, line 12, outlaw that kind of deduction entirely?

Mr. DOUGLAS. It would not be a direct intervention in a campaign. It might be said to be the marshaling of opinion opposed to a given course of legislation with its employees and stockholders. It might be defended on that ground. Those taking the deduction could piously say, "We are not favoring candidate A as compared to candidate B. We are only opposed to TVA or to health care for the aged."

Mr. BUSH. The language is:

(B) In connection with any attempt to influence the general public, or segment thereof, with respect to legislative matters, elections, or referendums.

Mr. PROXMIRE. "Stockholders" are defined in the committee report in such a way as to exempt them.

Mr. DOUGLAS. The reference is to attempts to influence employees or stockholders. But the appeal could not be made tax deductible if addressed to the general public. If someone tried to appeal to the general public, the expense of such attempt would not be tax deductible. It would only be tax deductible when one could appeal to the direct pecuniary interest or alleged pecuniary interest of one's stockholders and employees. But if he should try to appeal to the general interest, he would be out of luck.

Mr. PROXMIRE. I come to my last question. The first sentence in the third paragraph on page 24 reads:

Your committee's bill further provides that no expense deduction is to be allowed for expenditures to influence the general public, or segments thereof, with respect to legislative matters, elections, or referendums.

The reference is to the general public, but the law is explicit in providing that if an attempt is made to influence employees and stockholders, who, as the Senator from Illinois has pointed out, may be a very large and perhaps decisive part of the general public, in a city or even a State, the cost of the attempt is tax deductible, and the general taxpayer must pay for it.

Mr. MILLER. Mr. President, will the Senator yield?

Mr. DOUGLAS. I yield.

Mr. MILLER. In discussing the question with the Senator from Connecticut, the Senator from Illinois talked about direct intervention in a campaign.

Mr. DOUGLAS. I said it would not be direct intervention.

Mr. MILLER. The Senator used the word "direct." That is the basis for my question. The language of the bill contains nothing about "direct" intervention. In a case such as the one the Senator from Illinois or the Senator from Wisconsin suggested—I do not recall which—when the issues are so clearly defined that a position on an issue would identify a candidate, I think it would be straining the language of the bill considerably if under those circumstances, in the light of what is set forth beginning on line 12, page 40, such expenses would be allowable. The language is:

(a) For participation in, or intervention in, any political campaign on behalf of any candidate for public office—

The timing of the information that is being sent out would be presumptive of the intention to intervene in a political campaign, under the circumstances of the example the Senator from Illinois has used.

Mr. DOUGLAS. That is possible, but I call attention to the clause beginning on line 24, page 39:

In direct connection with communication of information between the taxpayer and employee or stockholder with respect to legislation or proposed legislation of direct interest to the taxpayer.

As I have said, a doctor could certainly claim that health care for the aged was of direct interest to him; or the American Medical Association could claim that it was; or the Du Pont Co., could claim that their bill, which they got through Congress with bipartisan support at the beginning of this session, was of direct interest to them. A savings institution could claim that the withholding provision in the tax bill was of direct interest to them; and so on.

Mr. MILLER. Mr. President, the provision starting on line 12 of page 40 comes after this statement, and I therefore say would be a definite limitation on the expense which the Senator is now talking about. I would suggest that if in the middle of an election, where the line was clearly drawn between candidates, let us say, on a savings and loan issue, if a savings and loan association got out a mailing which clearly identified the candidate through the issue, that would constitute an intervention, because the timing, I believe, in line 12 would be a limitation on the expenses, to which the Senator has referred, on line 24 on page 39, because this material starting on line 12 of page 40 comes later.

Mr. DOUGLAS. The Senator said the intervention on behalf of any candidate must be direct. However, some influences in life are not only direct, but also indirect. Sometimes an indirect influence is more important than a direct influence.

The American Medical Association and doctors have been carrying on a cam-

paign against health care for the aged, and they could indirectly influence the election of Senators and Congressmen. Similarly on every measure they could decide that they were working for no particular candidate, but would say they were trying to educate the stockholders and employees about proposed legislation. It could be said to them, "But this will help John Jones, and not Jack Smith." They could reply, "Oh, we did not know that. What we are trying to do is build up employee and stockholder sentiment about proposed legislation."

Mr. MILLER. I would agree if the language starting on line 12, page 40, contained the word "direct." It does not contain the word "direct." Therefore, we can read the language as being direct or indirect. This intervention can be indirect intervention.

Mr. DOUGLAS. Of course, no one knows what the courts or administrative officials will do. In order to be safe, the Senator from Iowa should vote for my amendment in order to make it certain that it will not be used that way.

Mr. President, I ask unanimous consent that a section of my minority views on lobbying expenses be printed in the RECORD at this point in my remarks.

There being no objection, the excerpt was ordered to be printed in the RECORD, as follows:

THE DEDUCTION FOR CERTAIN LOBBYING EXPENSES OF TAXPAYERS WITH BUSINESS INCOME

Section 3 would permit the deduction of certain lobbying expenses by taxpayers with business income. This would depart from a salutary principle which has been part of the income tax law since World War I. It would provide unwarranted tax reduction where it is least needed for reasons which are specious. It would introduce novel distinctions into the tax law, producing new requirements difficult for the Internal Revenue Service to administer. The specific language in which the deduction is cast contains ambiguities which will create continuing uncertainty as to its exact meaning, and, most important, the relationship of this provision to the whole process by which our citizens seek to influence the enactment of legislation at all levels of government was not adequately considered. Section 3 should be deleted from the bill.

Under existing law the costs of efforts to influence legislation are not deductible, a rule applicable to all taxpayers. Whatever the motive for a citizen's efforts to influence legislation, he now bears the whole cost of that effort himself. No part of the expense can be passed on to the Federal Government through an income tax deduction. In the constant competition for legislative favor and results at National, State, and local levels, the Federal Treasury stands neutral—and properly so.

Section 3 would change all that. It would amend section 162 of the Internal Revenue Code of 1954, the section creating the general authority for deduction of the ordinary and necessary expenses of business operation. Section 3 would add a new subsection specifically authorizing deduction of lobbying expenses in certain categories by taxpayers with business income. Only those taxpayers with business income would receive any benefit. All others would still be subject to the existing rule of no tax benefits for lobbying, a result which follows necessarily from incorporation of the amendment in section 162 and one which is specifically spelled out by the House committee report.

Some specific typical examples will bring this into sharper focus. Suppose a measure is being considered, as many have been, involving a proposed change in the standards or testing procedures for food, drugs, or cosmetics. The costs of presenting the views of drug manufacturers and distributors would be deductible. The cost of presentations on behalf of consumers or of disinterested professional or technical advisers would not be. Or suppose that a State legislature is debating a measure designed to decrease stream pollution. Manufacturers who would be adversely affected by its enactment could deduct the cost of opposition. Members of the public interested in pure water for drinking or for recreational uses would have to finance their support of the measure entirely from their own pockets. Or, at the local level, a business owner of a piece of real estate could seek advantageous amendment of the local zoning ordinance, deducting the cost of his presentation before the local city council. The owners of nearby residences would not receive this help from the Federal Treasury in preparing the exhibits and briefs necessary for effective opposition.

These are discriminations impossible to justify. Can anyone seriously contend that consideration of legislative proposals affecting business taxpayers is seriously handicapped by absence or weakness of expression of business viewpoints? Is there any evidence that business taxpayers, individually or collectively, are now deterred from expressing themselves on these subjects by the present rule of tax neutrality which permits no deduction for lobbying expenses? To ask these questions is to answer them. Of all viewpoints on legislative proposals, those of business are consistently the most ably represented before the Congress and before State and local legislative bodies. Why then should the cost of lobbying activities of taxpayers with business income be singled out for this preferential tax reduction? No adequate reason has been given.

Any discrimination at all among citizens in the exercise of their constitutional right to petition their representatives is patently undesirable. Discrimination by preferential tax deduction is magnified as the amounts spent for these purposes increase. Modern efforts to influence legislation cover a wide range of techniques, some of which are very costly. One can send a letter to his Senator for 4 cents. However, to stimulate tens of thousands to do so requires the expenditure of large amounts running sometimes into the hundreds of thousands, even millions, of dollars. But all this is well known. It has been thoroughly documented many times.

The application of section 3 would not be confined to nominal amounts. It would permit the deduction of some very large sums. In addition to provision for deduction of the costs involved in direct contacts with legislators (personal calls and visits, appearances before committees or statements filed with them), the cost of efforts to influence legislation indirectly are also made deductible in some instances. The costs of communications to organization members and to shareholders and employees have all been blanketed in.

When section 3 is applied to today's scene, we find that it will authorize giant corporations to deduct the cost of communicating the views of management officials to hundreds of thousands, even millions, of shareholders and employees, for the purpose of influencing them with respect to current controversial legislative proposals. To use a painfully familiar example, section 3 would authorize deduction of the cost of campaigns designed to produce a flood of letters opposing withholding on dividend income.

Under existing law these sums are not properly deductible—and never have been. To permit deduction now would shift a very large proportion of these heavy costs to the Federal Treasury, a disguised subsidy for which there would be no justification.

The effects of such subsidized efforts to influence legislation indirectly would not be confined to the recipient members, shareholders, and employees. The views expressed and their source would frequently come to the attention of families and friends of the recipients, thereby broadening the scope of the influence subsidized by the Federal Treasury. Of course, the benefits of section 3 as they would apply to these broadcast efforts to influence legislation can only benefit very large organizations. Small business taxpayers, as well as nonbusiness taxpayers, would have little or no use for it and could well suffer from its use where their interests on legislative matters are opposed to those who could take advantage of it.

True, not all lobbying costs of business taxpayers would be made deductible by section 3. The bill purports to create limitations which will restrict the kind of expenses for which a deduction can be claimed. Thus, to qualify for the deduction, the legislative proposal must be of "direct interest" to the taxpayer. In addition, specific provisions deny deductions for political campaign expenses or for efforts "to influence the general public, or segments thereof." However, a close inspection raises genuine doubt as to the precise meaning and application of these restrictions. They may, in fact, prove largely illusory.

Thus, one might ask, What subjects are not of "direct interest" to a large corporation? Any measure involving a tax or a change in the regulation of business or the marketing of securities or foreign trade or the terms of employment or labor relations or the monetary system will have some impact on every substantial business enterprise. Is it intended that the cost of testimony or statements or communications to shareholders or employees on this entire range of subjects is to be deductible? Similarly, can the prohibition against deductions for political campaign purposes be really effective? Granted that the cost of a folder urging shareholders to vote for Jim Darkwater will not be deductible, what of the cost of a folder urging a position on the principal issue dividing Darkwater from his opponent Bob Cleanriver? Can issues and the candidates be separated so easily? It is doubtful. Section 3 thus could make slightly veiled political contributions deductible. The benefit would not be universal though. To return for a moment to the anti-water-pollution measure used as an example before, suppose Darkwater is against it and Cleanriver is for it. The former's supporters could deduct the cost of their literature discussing the antipollution measure (and thus their support of Darkwater); supporters of Cleanriver could not.

Obviously, congressional memories are very short. For at least a century Senators and Representatives have regularly inveighed, individually and collectively, against lobbyists and their activities. The need for substantial disclosure by lobbyists, particularly in financial respects, has long been recognized. When a person or organization becomes a lobbyist, he is required to register as such and thereafter to report quarterly his expenditures for these purposes. In spite of these safeguards, every few years some lobbyists become so bold and their overreaching so bad that a special inquiry is required. A prime example was the creation in the 84th Congress of the Senate Special Committee to Investigate Political Activities, Lobbying, and Campaign Contributions. Its report states graphically the kinds of abuses which occur and the large sums of

money available to be spent on efforts to influence legislation. Sugar quota bills attract lobbyists like flies and, like flies, their activities are not widely admired. The Senate Foreign Relations Committee is currently beginning an investigation of another group of lobbyists, an inquiry which has grown in large part out of concern for their lucrative financial arrangements. Nor are problems with lobbyists confined to Washington. Their influence on State legislators and their sometimes questionable methods in State capitols is notorious.

When projected against all this experience, section 3's proposed financial bonanza for one group of lobbyists and their employers seems ironic in the extreme, if not downright cynical.

There is no challenge here to lobbying *per se*. It is unquestionably legitimate. A constitutionally protected right of our citizens, it often supplies useful information and reactions on pending legislation. However, it would be foolish to exalt it unduly for those reasons. At best, lobbying is a mixed blessing for it is almost always exclusively concerned with self-interest rather than the broad public interest. Fortunately, section 3 presents only a narrow problem, viz, whether or not the lobbying done by one segment of our society—taxpayers with business income—should be entitled to support from the Federal Treasury.

A number of arguments are made in favor of this measure. Some of them have a surface plausibility, but on close analysis none of them holds water. The issue is actually a simple one. We begin with a longstanding rule that all taxpayers, business and non-business, who seek to influence the work of legislative bodies, National, State, or local, pay their own expenses in full without assistance from the Federal tax system. This neutral posture of the tax law is a healthy one and should be defended and strengthened. Legislation affects all our citizens. It is entirely suitable that all who seek to influence that legislation, directly or indirectly, should be treated alike. The expenses of all should be on the same footing as far as the Treasury of the United States is concerned. The only issue here is whether or not to depart from this principle of neutrality and equality. Plainly, the case for such a change has not been and cannot be proved.

Mr. DOUGLAS. Mr. President, I ask for the yeas and nays on my amendment.

The yeas and nays were ordered.

Mr. BUSH. Mr. President, I wish to oppose the amendment of the Senator from Illinois. It seems to me that this is a very disturbing amendment, one which discriminates very much against small business organizations in this country. The amount which large corporations, the ones the Senator from Illinois is talking about, spend in connection with appearances before committees and Members of Congress and agencies of the Government, is a very small matter for the large corporations, but it may be of great importance to the smaller companies.

It seems to me that the committee amendment is very considerate—as opposed to the Douglas amendment—in that it gives the smaller business companies an opportunity to assert their own self-defense, so-called, when Government has its hand in almost everything, and most small corporations have some business to transact in Washington and must wait upon their Representatives and Senators and some of the agencies, and even appear before committees.

It is a real hardship for them not to be able to charge off as business expenses such appearances in connection with which these expenses are incurred. Such appearances are made by labor organizations and by such groups as the League of Women Voters, and a great many other nonprofit organizations. So I would say, as I read the amendment, having listened carefully to the debate, that the purpose of the committee amendment is to correct an injustice and to give the smaller business organizations a better chance to defend themselves and to state their case before Members of Congress or before committees or before governmental agencies. I very much hope that the amendment of the Senator from Illinois will not prevail.

Mr. PROXMIRE. Mr. President, will the Senator yield?

Mr. BUSH. I yield.

Mr. PROXMIRE. Is it not true that under present law when any businessman comes to Washington and appears before an agency of Government, other than Congress, if the visit relates to his business, the expenses of his trip are deductible at the present time?

Mr. BUSH. I hope so.

Mr. PROXMIRE. That is correct.

Mr. BUSH. That being the case, I see no reason why these people should not be given the same treatment when appearing before the Congress.

Mr. PROXMIRE. Is it not true that the members of other groups to which the Senator has referred, such as the League of Women Voters, cannot subtract their expenses? I am referring to the members of the league who make contributions to the league.

Mr. BUSH. Such organizations do not pay any income tax, because they are nonprofit organizations.

Mr. PROXMIRE. I mean the people who contribute to the league. The contribution they make to the league is not deductible, although it is for members of a trade association, for example.

Mr. BUSH. I assume that if members of the league come here as delegates, their State organization pays their expenses. If that is the case, they should be able to deduct their expenses, if they have a legitimate case.

Mr. PROXMIRE. I agree with the Senator. However, they cannot do it. They are not allowed to do it. The amendment of the Senator from Illinois would do away with a very severe imbalance. The members of the league cannot deduct their contributions from their income taxes.

Mr. BUSH. I would correct that imbalance the other way. I would be liberal in giving them a chance to deduct their expenses, or to have someone assume the expenses, if they have business to transact with the Federal Government in their own interest. I do not believe, because organizations have an interest, that it is necessarily an interest against the public interest. That has been so often said here this afternoon. Many people come to Washington who belong to small organizations. They may consist of 40, 50, or 60 people. Not

long ago a delegation came to see me on the trade bill. One of the organizations employs 60 people, another 200 or 300 people. These are important employers in little towns in my State. What the Senator from Illinois wants to do, as I see it, is to deprive them of the privilege given them under the bill of charging their expenses against their income account.

Mr. PROXMIRE. I agree 100 percent that those business groups often do represent the public interest. But whether they do or not they should in all instances be heard and be given every encouragement to appear. Their appearance is not on the same basis as the appearance of nonprofit groups, because the activities of such groups as the League of Women Voters or the Committee for Constitutional Action, or any other such group, are not related to any financial benefit but to a deep conscientious conviction. So under the present tax laws, unless we violate in some way the principle of permitting only those expenses to be deducted which are related to increasing income or reducing cost, I do not see how we can give the same consideration to other groups. Unless we can equate it in that way, it seems to me it would be much better to carry on with the present law, which treats all groups equally.

Mr. CURTIS. Mr. President, will the Senator from Connecticut yield?

Mr. BUSH. I yield.

Mr. CURTIS. I do not think we can compare a business entity with non-business or nonprofit organizations which are interested in causes. The purpose of a deduction under the income tax law, is to enable a taxpayer to determine his net income, so that the Government may apply and collect the tax. If a small businessman must make an expenditure of any kind, whether it is for a repair or for buying supplies, that expenditure, of course, must be deducted from his gross income to ascertain whether there is enough income from which to pay the tax.

By the same token, in this day of big government, if small business must come to the government and present its case, as an ordinary and necessary step to take in transacting business, that expense cannot be distinguished from any other expense, and it should be deductible.

Mr. BUSH. The Senator is absolutely correct.

Mr. CURTIS. An organization may be a worthwhile organization, but may not be engaged in a trade or a business, so is not taxed. Therefore, there is no necessity for determining its net income, and the principle of the business deduction does not apply at all.

Mr. BUSH. The Senator is absolutely correct.

Mr. CURTIS. I think it might be well to show the legislative intent as to why paragraph (C) was included as a committee amendment. That paragraph reads:

In direct connection with communication of information between the taxpayer and

an employee or stockholder with respect to legislation or proposed legislation of direct interest to the taxpayer.

That provision was adopted by the committee after it had rejected an argument for extending it to the general public. The committee decided that that would not be a proper tax deduction, because such an extension would go quite far. But the committee very appropriately, I think, contended that the language in paragraph (C) was something vital to the business and was a proper business expense.

Mr. BUSH. I think that is absolutely correct.

Mr. President, I again express the hope that the amendment will be rejected.

Mr. KERR. Mr. President, the amendment in the bill which the Senator from Illinois seeks to strike is in reality a very simple amendment and, in my judgment, an equitable and just amendment. The Senator from Illinois made two or three significant remarks. He said there is no way to foretell what the Supreme Court will do. That is true. If the Supreme Court had not done something that was not foreseen, this amendment would not have been necessary, because under the 1954 code, section 162(a), is the provision:

There shall be allowed as a deduction all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, including—

Among other things—

(2) traveling expenses (including the entire amount expended for meals and lodging) while away from home in the pursuit of a trade or business.

That language is specifically in the basic income tax law. It provides that the income tax percentages shall not apply to that part of the expenditures by a taxpayer made in carrying on any trade or business, including traveling expenses, meals, lodging, and so forth, while away from home in the pursuit of a trade or business.

In spite of that plain provision in the law, the Treasury issued regulations which were to the contrary, and said that if they were expenditures to come to Washington to see Members of Congress, such expenditures were not deductible.

The Supreme Court held that in view of these regulations having been promulgated by the Treasury, the act of Congress was ineffective, in view of the fact that it did not specifically repeal them.

Therein, as I said, the Senator from Illinois is right; we cannot tell what the Supreme Court will do.

The Supreme Court handed down two decisions upholding the validity of the regulations.

Mr. DOUGLAS. Mr. President, will the Senator yield?

Mr. KERR. Please let me finish.

In *Cammarano* against United States and *F. Straus and Sons, Inc.*, against United States, the Court held that although the amounts expended for legislative matters were "ordinary and necessary"—in fact, essential to the very survival of the taxpayer's business—never-

theless they were not deductible because the regulations barred the deduction of this particular type of expense.

Congress finally got around to recognizing its duty of establishing the rights of taxpayers.

Mr. DOUGLAS. Mr. President, will the Senator yield?

Mr. KERR. I yield.

Mr. DOUGLAS. Is the Senator quoting from—

Mr. KERR. I am quoting from the committee report.

Mr. DOUGLAS. Is the Senator quoting the opinion of the Court as handed down by Justice Harlan?

Mr. KERR. I would not know.

Mr. DOUGLAS. Or is the Senator quoting the concurring opinion of Justice Douglas?

Mr. KERR. I am reading from the report of the committee with reference to the bill.

Mr. DOUGLAS. The Senator is not going back to the decision itself?

Mr. KERR. I am not reading from the language of the decision.

Mr. DOUGLAS. The Senator said that the Court had held that those expenses were ordinary and necessary. I have the decision before me. I cannot find that anywhere in the Harlan opinion, which was joined in by eight of the nine members of the Court. There is language of a similar nature in the concurring opinion of Justice Douglas. I think the Senator is quoting the exception, not the rule.

Mr. KERR. Mr. President, if the Supreme Court had not handed down the decision holding that the language of the statute did not mean what it said, and was adversely affected by regulations, then this amendment would not be necessary. The reason why the committee amendment is necessary is that the code, in 1954, specifically provided that such expenses were deductible.

Mr. DOUGLAS. No, it did not. It provided for expenses which were ordinary and necessary to the conduct of a business.

Mr. KERR. I liked what the Senator said about the first amendment to the Constitution.

Congress shall make no law respecting an establishment of religion, or prohibiting the free exercise thereof; or abridging the freedom of speech, or of the press; or the right of the people peaceably to assemble, and to petition the Government for a redress of grievances.

Mr. DOUGLAS. There was no violation of that in the Cammarano case.

Mr. KERR. I understand. The Constitution guarantees the people the right to petition the Government, provided it is at their own expense.

Mr. DOUGLAS. But it does not create a business interest and provide that the taxpayers shall pay 52 percent.

Mr. KERR. Oh, the Senator kind of tickles me about that. He talks about consumers. I am a consumer. A consumer has a right to this deduction if he comes here to talk about his trade or business.

Mr. DOUGLAS. No; he does not.

Mr. KERR. Yes, he does, if he comes here in connection with his trade or business.

Mr. DOUGLAS. But not in his function as a consumer; not in his function as a generalized taxpayer.

Mr. KERR. The big corporation cannot get a deduction for its expenses in coming here as a consumer.

Mr. DOUGLAS. But it can get a deduction for its expenses when it appears here in connection with its direct financial interest as a producer.

Mr. KERR. It can get a deduction for its expenses if it comes here in relation to a legislative matter directly connected with its business, and so can a consumer.

Mr. DOUGLAS. But the consumer's interest is not directly related.

Mr. KERR. But every consumer has a trade or business.

Mr. DOUGLAS. But the consumption function is not included.

Mr. KERR. Well, that is subject to another tax; it has not been overlooked, I say to the Senator from Illinois.

Mr. DOUGLAS. I am sure it has not; and the Senator from Oklahoma would heap more onerous sales taxes on the consumers, too.

Mr. KERR. That is not correct, and I defy the Senator to show that I have ever said anything in that regard. I do not impute his motives. I simply say he has made an incorrect statement, and I challenge him to document to the contrary.

Mr. DOUGLAS. The effect of what the Senator from Oklahoma is doing is to make the tax system of the country more regressive.

Mr. KERR. That is a matter of opinion, Mr. President.

Mr. DOUGLAS. No, it is a matter of fact.

Mr. KERR. It is stated as a fact; I know some Senators think their opinions are automatically facts. But I know of no law making it so, nor do I know of any law making their opinions binding on the Congress.

Mr. DOUGLAS. The Senator from Oklahoma is proceeding in his characteristic fashion.

Mr. KERR. That is marvelous. And so is the Senator from Illinois. And I am sure is enjoying it as much as the Senator from Oklahoma is.

Mr. DOUGLAS. It is never a pleasure to debate with the Senator from Oklahoma.

Mr. KERR. Then why waste so much time doing it?

Mr. DOUGLAS. Because I think some matters of principle are involved. I do not take pleasure in insulting fellow Senators.

Mr. KERR. Then why do it? Why make the statement that the Senator from Oklahoma is in favor of sales taxes? That was making an attack by the use of a statement not based on fact. However, I do not regard it as an insult. I do not think the Senator from Illinois could insult me, Mr. President. I love him; I respect him; I am delighted to debate with him; I would not be denied that privilege, or have it denied him, for anything in the world—although it is a great job to try to keep his mind on his business or to try to keep his statements in line with the record. But even that is not a burden, I admit.

Mr. President, this provision in the

Constitution is a very valid one and a very interesting one.

The Senator from Illinois said special privilege after special privilege after special privilege exert pressure and get special legislation against consumers.

You know, Mr. President, all the people who come here constitute all of America. The people who come here to petition their Congress represent the sum total of the population of the United States; and it is our job to represent them. As was said by the Senator from Illinois, every once in a while they bring us information we did not have. It probably happens as often to me as it does to any other Senator. I welcome them, if they are from Oklahoma; I want them to come here.

But I sat here and listened to the Senator from Wisconsin and the Senator from Illinois talk about how unbearable it was for their constituents to come here and press upon them their matters of interest. I wish to say to the people from Oklahoma that it is not unbearable to the Senator from Oklahoma for his people to come here.

Mr. DOUGLAS. May I ask whether the Senator from Oklahoma is speaking for the administration when he speaks now?

Mr. KERR. I am speaking for KERR, of Oklahoma, and I did not know the administration had authorized DOUGLAS to speak for it.

Mr. DOUGLAS. No, it has not. But the Treasury has announced that it is opposed to these provisions; and it is extraordinary to see the Senator from Oklahoma sitting in the seat of the Democratic leadership and opposing amendments which are quite in harmony with the administration.

Mr. KERR. And it is amazing to me to see the Senator from Illinois sitting here and lobbying for the administration and getting a deduction for his expenses. [Laughter.]

Yet that is done under the law:

For purposes of the preceding sentence, the place of residence of a Member of Congress (including any Delegate and Resident Commissioner) within the State, congressional district, territory, or possession which he represents in Congress shall be considered his home, but amounts expended by such Members within each taxable year of living expenses shall not be deductible for income tax purposes in excess of \$3,000.

Why, Mr. President, every Member of Congress has a deductible item of up to \$3,000 for living expenses while attending to his business here, even though his business for the moment is lobbying for the administration. Yet he would deny that right to his constituents.

Mr. President, I wish to say that I am glad to have my constituents come here. I would be worried if they did not come.

Mr. President, all in the world that this provision does is to say that business people or consumers or laborers or truckers or farmers who come here to talk to their Members of Congress about their business can deduct, for income-tax purposes, their expenses of coming here and doing that. Would not it be an empty right to guarantee them the right to petition their Members of Congress, and then say, "You have that

right, but you must pay all the expenses out of your own funds, and they will not constitute a deduction"—although the income tax applies only to the net income after the deductions specifically mentioned in the 1954 code; and the reference to that would not be necessary except for the fact that the Supreme Court disregarded it and held that it was not effective.

Mr. President, I urge that the amendment be rejected.

Mr. COOPER. Mr. President, I should like to ask one or two questions of either the Senator from Oklahoma or the Senator from Illinois. I have listened to the arguments made for the amendment, and I have listened to the arguments made against it.

As I understand it, the argument made by the Senator from Oklahoma is that these expenses are like other expenses; that if they are directly related to or associated with the carrying on of the trade or business, then, so the Senator from Oklahoma argues, they should be deductible, if they are involved in presenting claims for legislation.

Mr. KERR. Yes.

Mr. COOPER. And I also understand that that would apply, as a matter of policy, in connection with the taxpayer's right to petition.

But I ask about provision (1) on page 39, to which the Senator from Nebraska referred. As I understand, there is no connection with the obtaining by the employer or stockholder of information in reference to proposed legislation of direct interest to the taxpayer. If this section remains in, as I see it, such expenses would be deductible if they are for transportation, for travel, or for food or for preparing information or statements, or talks between a taxpayer and the employers or stockholder, with respect to legislation.

Mr. KERR. In connection with his own business.

Mr. COOPER. His own business?

Mr. KERR. Yes.

Mr. COOPER. I must say that in this case I cannot see that the same argument would apply to this section; I refer to the argument supporting the deduction of expenses by a taxpayer who presents his case to this legislative body or to some other legislative body. I should like to know the rationale in favor of arguing that expenses covered by subparagraph (C) should be deductible expenses. Accepting the Senator's argument that a taxpayer should have the right to deduct expenses for presenting his case before a legislative body, whether of the Federal Government, a State, or a local subdivision of government—on what reasoning can the same argument be applied to a taxpayer discussing legislation with his employees or stockholders? Is not that a normal expense of his business which does not bear directly upon his presentation of the businesses' interest—whether corporate or individual—to a legislative body?

Mr. KERR. Mr. President, is the Senator directing a question to me?

Mr. COOPER. Yes.

Mr. KERR. One of the responsibilities of management is to operate its busi-

ness in such a way as to pay a return to the stockholders on their investment. Certainly, management has the responsibility of keeping the stockholders and the employees informed as to legislation which affects their business. Why should a business or trade be denied the right to deduct the expense of informing its owners of matters which could adversely affect it, when they are charged with the responsibility of management? Otherwise, it occurs to the Senator from Oklahoma, they would be derelict in their duty. If an insurance policy is taken out against fire loss, that is a deductible expense. If a lawyer is hired on a retainer basis to protect the company and to handle its business in accordance with the law, that is a deductible expense. If a law is proposed which would have an adverse effect, the cost of opposing that law in Congress is deductible. Should not the managers have a right to deduct the expense of informing the stockholders or employees so they can be protected, just as they are protected against fire, adverse litigation, or other matters affecting the welfare or profitability of the business?

Mr. COOPER. If Congress wants to, it can extend the right to deduct expenses in this or other fields, but I think there is a distinction here.

Mr. KERR. I say to the Senator that while that is a separate item from that of sending someone to Washington, it still has to be directly connected with the trade or business; but the amendment of the Senator from Illinois would strike both provisions out of the bill.

Mr. COOPER. As has been argued, and reported, this entire section is bottomed on the idea that a taxpayer—one carrying on a trade or business—should be able to deduct expenses for appearing, communicating, or preparing to present his case to legislative bodies upon pending or proposed legislation. That is the essence of the section. If it is desired to give the taxpayer such deductions for appearing before legislative bodies, preparing testimony, and for necessary and proper expenses in connection with presenting their petitions—if one wants to use the constitutional phrase—to a legislative body, such a purpose is understandable. But the provision I am talking about is something else. The taxpayer would also be permitted to deduct expenses for communications between the taxpayer and his stockholders or his employees—persons who do not have jurisdiction for the enactment of legislation.

For example, this would cover all kinds of expenses for communications between persons and to persons who are not charged with legislation. Admitting the reasoning upon which the plea for the entire section is based—that of the presentation of a position to a legislative body—it does not apply to carrying on a kind of campaign with stockholders for or against legislation. There is a distinction between these two kinds of expenses.

Mr. KERR. I can understand how one could make a differentiation, but the majority of the Finance Committee felt that this language was consistent with the language of the entire provision.

The Senator from Oklahoma concurred in that feeling. That action certainly is not binding on the Senate.

The proposed amendment would strike out the entire section. After that amendment was disposed of, if the Senator from Kentucky wanted to offer an amendment to strike out the particular portion to which he is addressing himself, it would be in order. I would not agree with him, but it would be in order.

Mr. CURTIS. Mr. President, will the Senator yield?

Mr. COOPER. I yield.

Mr. CURTIS. I am opposed to the amendment that is offered.

Mr. COOPER. Is the Senator responding to the question I raised?

Mr. CURTIS. Yes. I believe that paragraph (C) should be the law, anyway, but I also think it is well to keep it in the bill. Certainly, it is a duty of management to keep the stockholders and owners informed, if it is a necessary expense of doing business, and without the doing of business, no employees could be kept employed.

May I also point out that in lines 6 and 7 of page 39 of the bill are the words "ordinary and necessary." This section is not an invitation to businessmen to come to Washington on anything which might be interesting. It has to be an ordinary and necessary expense. The business must be threatened or it must be proposed that burdensome government regulations are to be put on the business which might result in loss of operations or loss of jobs. To defend against that kind of legislation, as the Senator from Oklahoma has pointed out, is just the same as defending the business against fire or any other business hazard.

Mr. COOPER. I understand and agree with the Senator on the paragraphs dealing with the presentation of position to legislative bodies. I understand that legitimate expenses are incurred in presenting views on legislation at Washington, or Frankfort, Kentucky, or Omaha, Nebraska, on legislation which may be critical to the business. But the Senate version extends the House version and permits deductions for functions which the business performs anyway, and which are not communications, appearances, with legislative bodies or officials.

Mr. CURTIS. The business would perform it anyway, but there should be a deduction for it.

Mr. COOPER. With respect to expenses incurred in connection with taxpayers appearing before Congress or other legislative bodies, it would be reasonably easy to ascertain whether the expenses were necessary for a legislative purpose, because the legislation or proposed legislation could be identified, as well as the committees or members. But I do not know how it could practically be determined whether expenses covered by subparagraph (C) were necessary in the case of legislation which was proposed or pending before a legislative body.

My question is, Why was it added? What is the rationale?

Mr. CURTIS. I have stated my reason.

Mr. COOPER. For the purpose of informing the stockholders or employees about legislation?

Mr. CURTIS. No; because it is a necessity of doing business.

Let us consider a hypothetical case of an industry threatened by a trade agreement or a tariff change. If the industry were threatened with injury, that would be a threat to the employees. Suppose that this caused an explanation to be made to the employees, as to what the industry believed about the situation. Suppose it caused a petition to be printed, so that employees might sign their names. There would be a communication to them. I think that would be the same necessary expense of doing business as a fire insurance policy would be.

Mr. MILLER. Mr. President, would the Senator yield?

Mr. COOPER. I yield.

Mr. MILLER. Perhaps I can be helpful.

I wish to say that I agree with the Senator from Nebraska that, generally speaking, such expenses are deductible expenses now. There is no point, even, in having the provision enacted for those, since that is already a part of the law and is already contained in the concept of what is ordinary and necessary.

I can visualize a situation which might develop in which a different aspect might arise. For example, let us consider the case mentioned by the Senator from Nebraska, in which a mailing might be made to employees and to stockholders, calling their attention to the fact that a certain bill was pending in the Congress and that, if enacted, it might cause considerable hardship to the company. That would be all that would be said, and I think that would be a deductible expense under the present law. That would be a matter of information. Usually that information would be contained in some kind of a weekly or monthly letter of information to the people involved, anyway.

Let us assume, however, that coupled with the information there would be a statement, "We urge upon you to contact your Members of Congress. This is the list of the Members of Congress. Write to them along this line. Here is a sample letter you might use."

I would suggest that then they would be getting into an area prohibited under present tax law, which would be the effort to influence legislation. It would be almost a direct invitation to people to participate in a mass movement to affect legislation.

I think this type of activity probably would not be allowable as a deduction under the present state of the law, but under the proposed provision it would be deductible.

I think each Senator must reach a judgment as to whether that latter type of activity is a kind of activity to be encouraged, to be put in about the same category as the first activity. So far as I am concerned, I wish to say that the junior Senator from Iowa believes it is a good idea for people to be educated on these things, and I think it is all right. But there would be a question, in the present state of the law.

Mr. PROXMIRE. Mr. President, will the Senator yield for a question?

Mr. COOPER. I yield.

Mr. PROXMIRE. The Senator from Kentucky has raised a question to which there has been no answer. What the proponents of the amendment argue is that this expense should be allowed as a deduction as a necessary business expense. The Senator from Kentucky raised the question as to why it would be a necessary expense to tell the stockholders about proposed legislation or to tell employees about proposed legislation unless there were a desire for them to take some kind of action to bring pressure on the Congress, on a State legislative body, or on a city council, or to take a particular action which the business might wish them to take.

So far as that being a necessary business expense is concerned, in the sense of reducing cost or of increasing income, it is perfectly obvious and apparent it would not be. I think the question raised by the Senator from Kentucky has not been answered at all.

The Senator from Nebraska made a noble attempt to give an example, under the Trade Agreement Act, of a company which might be injured. In that particular case, he said, the employees should be told the situation, for they might wish to sign a petition. Certainly that would be fair, but it would have nothing to do with reducing cost or increasing income, unless there were a desire to bring pressure upon a legislative body.

Mr. MILLER. Mr. President, will the Senator yield at that point, so that I may develop the idea about increasing income or reducing cost? It is not merely a question as to whether it will increase income or reduce cost. It also involves the question of maintaining income. That would involve ordinary and necessary expense. If the business volume of a taxpayer were threatened by proposed legislation, it would be an ordinary and necessary business expense to seek to maintain volume by fighting the proposed legislation.

Mr. PROXMIRE. That might be. The Senator from Kentucky very wisely divided his question. He said that appearances before a legislative body might involve a necessary expense, but that the carrying on of a campaign among stockholders would have nothing to do with it. The stockholders could do nothing about that.

Mr. COOPER. Mr. President, I believe I still have the floor.

Mr. MILLER. Mr. President, if the Senator will permit, the Senator from Iowa wished to make the point that this would be only one step removed from having a lawyer go to the city of Washington, D.C., to say something about a bill being considered, of importance to a company. What would be the difference between that case and notifying the stockholders, so that they, in turn, could write to their representatives in Congress? It seems to me the same objective would be involved.

If someone is opposed to sending a lawyer to Washington, D.C., and allowing the taxpayer to take that expense as a deduction, naturally the same person

would be opposed to allowing a business deduction based on stockholders contacting Members of Congress.

Mr. PROXMIRE. Mr. President, if the Senator will permit. I should be glad to answer that.

Mr. MILLER. If the Senator believes in the first, I think he will believe in the second.

Mr. COOPER. Mr. President, I offer an amendment, which I send to the desk and ask to have stated.

The PRESIDING OFFICER (Mr. HART in the chair). The amendment will be stated for the information of the Senate.

The LEGISLATIVE CLERK. Beginning on line 24, page 34, it is proposed to strike out all through line 2 on page 40.

Mr. COOPER. Mr. President, this puts the question before the Senate.

Mr. PROXMIRE. Mr. President, will the Senator yield for a question?

Mr. COOPER. I yield.

Mr. PROXMIRE. I say to the Senator from Iowa that if employees were to go to the city of Washington, D.C.—

The PRESIDING OFFICER. The Senator will suspend.

The Chair is advised that the proposed amendment does not bear on the Douglas amendment.

Mr. KERR. Mr. President, I should like to remind the distinguished Senator from Kentucky that after the pending amendment is voted upon, his amendment then would be in order.

Mr. COOPER. I wrote the amendment hurriedly in pencil, and I will perfect it.

Mr. KERR. Mr. President—

The PRESIDING OFFICER. The Chair assumes that the Senator from Kentucky temporarily is withholding his amendment.

Mr. KERR. It could not be before the Senate, because it has not been completed.

Mr. COOPER. The amendment is completed now. I ask that it be stated.

The PRESIDING OFFICER. The Chair is now advised that the amendment offered by the Senator from Kentucky is in order, and the amendment will be stated for the information of the Senate.

The LEGISLATIVE CLERK. Beginning on line 24, page 39, it is proposed to strike out through line 2 on page 40.

Mr. KERR. Mr. President, a parliamentary inquiry.

The PRESIDING OFFICER. The Senator will state it.

Mr. KERR. Is the parliamentary situation one in which the amendment offered by the Senator from Kentucky is to be considered a substitute for the amendment offered by the Senator from Illinois?

The PRESIDING OFFICER. The Chair is advised that it will be regarded as a perfecting amendment.

Mr. KERR. I would say to the Presiding Officer in that relationship, as I understand the situation, the Senator from Illinois offered an amendment to strike out a very great deal of language.

The PRESIDING OFFICER. The Senator is correct.

Mr. KERR. Now the Senator from Kentucky has offered an amendment to

strike out only a limited part of that same language.

The PRESIDING OFFICER. The Chair is advised that this is in order as a perfecting amendment.

Mr. KERR. I understand.

Mr. COOPER. Mr. President, may I ask the status of my amendment?

The PRESIDING OFFICER. The amendment has been stated. The question is on agreeing to the amendment offered by the Senator from Kentucky.

Mr. McCARTHY. Mr. President, as I understand the amendment offered by the Senator from Kentucky, it would leave in section 3, the deductions which are to be allowed, to include all necessary and ordinary expenses paid or incurred in the taxable year in direct connection with appearances before committees of Congress or legislative bodies. It would also leave intact section (B) on page 39, providing for communications between the taxpayer and the organization of which he is a member.

However, the effect would be to strike from the bill section (C), beginning on page 39, which would allow deductions "in direct connection with communication of information between the taxpayer and an employee or stockholder with respect to legislation or proposed legislation of direct interest to the taxpayer."

This section was added in the Finance Committee, and I think it would open the way to real abuse.

I was in favor of allowing deductions for the ordinary expenses of lobbying. But I do think that the proposed deduction which would permit deductions in connection with communications of information between the taxpayer and his employer or stockholders would open the way to the use of the deduction for political purposes. If such a deduction were to be allowed, it should be part of a general change in the law, so that individual voters or individual citizens could have the same advantages. I hope that the amendment offered by the Senator from Kentucky will be agreed to.

Mr. COOPER. Mr. President, I ask that my amendment be perfected by adding on line 23 the word "or." I make the request because of the reference to "C)." The last word in line 23 would be "or."

Mr. JAVITS. Mr. President, will the Senator yield?

Mr. COOPER. I yield.

Mr. JAVITS. I wish to express my agreement with the Senator from Kentucky and the Senator from Minnesota. I think we are approaching or apparently getting into a field which needs some charting. The proposal is a fair way to begin. I am somewhat acquainted with the legal problems of corporations. I think there should be some analogy with the authority of trade unions. If the amendment is trimmed in the way my colleagues have now designed it, it will get started upon that path without going beyond it.

The reason is that almost any general piece of legislation, no matter how broad, will affect a major company. Therefore we would open quite a door in the proposal with relation to stockholders and employees. It may be justified, but

I think we are well advised to start in a limited way with what the Senators have outlined. I support them in their amendment.

The PRESIDING OFFICER. The question is on agreeing to the amendment of the Senator from Kentucky.

Mr. JAVITS. Mr. President, I ask for the yeas and nays.

The PRESIDING OFFICER. Is there a sufficient second?

The yeas and nays were not ordered.

Mr. COOPER. Mr. President, I suggest the absence of a quorum.

The PRESIDING OFFICER. The clerk will call the roll.

The legislative clerk proceeded to call the roll.

Mr. KERR. Mr. President, I ask unanimous consent that the order for the quorum call be rescinded.

The PRESIDING OFFICER. Is there objection? The Chair hears none, and it is so ordered.

Mr. KERR. Mr. President, I ask for the yeas and nays.

The PRESIDING OFFICER. Is there a sufficient second?

The yeas and nays were ordered.

The PRESIDING OFFICER. The question is on agreeing to the amendment of the Senator from Kentucky.

Mr. COOPER. Mr. President, as the Senator from New York has said, when testimony is adduced, on this particular section, necessity for it may be demonstrated. But the committee report deals only with the question of taxpayers appearing before and communicating with legislative bodies. There has been opposition even to these deductions. So far as I am concerned, I have felt that taxpayers have the right to present their cases before legislative bodies. But it seems to me that this particular provision would add a new element, which is not connected with the problem of taxpayers presenting their cases before legislative bodies.

Taxpayers would have the right to deduct for their communications to employees or stockholders, upon matters which, it seems to me, are wholly the concern of their business considered in the context of the entire section which is dealing with the presentation of issues before legislative bodies. It seems to me that this provision is an extension beyond the purpose of the entire section.

The PRESIDING OFFICER. The question is on agreeing to the amendment of the Senator from Kentucky. The yeas and nays have been ordered, and the clerk will call the roll.

The legislative clerk proceeded to call the roll.

Mr. DOUGLAS. Mr. President, a parliamentary inquiry.

The PRESIDING OFFICER. The Senator will state it.

Mr. DOUGLAS. Is the amendment of the Senator from Kentucky an amendment to the bill or an amendment to my amendment?

The PRESIDING OFFICER. The amendment would amend the language of the bill which the amendment of the Senator from Illinois proposes to strike.

Mr. KERR. Mr. President, a parliamentary inquiry.

The PRESIDING OFFICER. The Senator will state it.

Mr. KERR. If the Cooper amendment is agreed to, then the Senate will vote on the Douglas amendment, which would strike the remainder of the language of the section.

The PRESIDING OFFICER. The Senator is correct.

Mr. KERR. It is kind of like cutting a dog's tail off an inch at a time so it would not hurt so badly.

Mr. GORE. Mr. President, a parliamentary inquiry.

The PRESIDING OFFICER. The Senator will state it.

Mr. GORE. How is it possible that while one amendment to a section of the bill is pending, an amendment in the second degree to the same section to which the pending amendment applies, may be considered?

The PRESIDING OFFICER. The Chair is advised that the amendment is a perfecting amendment, intended for the purpose of perfecting a portion of the bill proposed to be stricken.

Mr. MILLER. Mr. President, a parliamentary inquiry.

The PRESIDING OFFICER. The Senator will state it.

Mr. MILLER. I regret that the Senator from Iowa is still not clear on the question. Do I correctly understand that the Cooper amendment would amend the Douglas amendment in such a way that the only portion that would affect the bill would be on page 39 to strike the language starting on line 23 with the word "or" and going over to line 2 on page 40?

The PRESIDING OFFICER. The Chair is advised that it would not affect the Douglas amendment. The action on the Cooper amendment would not affect the motion by the Senator from Illinois to strike out what may thereafter be left.

Mr. DOUGLAS. Mr. President, a parliamentary inquiry.

The PRESIDING OFFICER. The Senator will state it.

Mr. DOUGLAS. If the amendment does not affect my amendment, how can it be a perfecting amendment to my amendment?

The PRESIDING OFFICER. The Chair is advised that, in the parliamentary sense, it is not a perfecting of the language in the Senator's amendment at all.

Mr. McCARTHY. Mr. President, a parliamentary inquiry.

The PRESIDING OFFICER. The Senator will state it.

Mr. McCARTHY. If the amendment is agreed to, then the bill would be without section (C). The Douglas amendment would then strike out sections (A) and (B), because (C) would be gone. So the practical effect would be the same, it seems to me, in any case.

If the amendment is agreed to, the Douglas amendment would run only to (A) and (B) because only those two sections would be left in the bill.

The PRESIDING OFFICER. The Parliamentarian points out that the

Senate could change any section that remains in the bill thereafter.

Mr. McCARTHY. The Douglas amendment now runs to sections (A), (B), and (C). If the Cooper amendment is agreed to, no section (C) would remain.

The PRESIDING OFFICER. The motion of the Senator from Illinois would have the effect of striking out all that remains in the bill after action on the Cooper amendment.

Mr. HOLLAND. Mr. President, to simplify the question, I ask for a division of the three elements in the Douglas amendment.

The PRESIDING OFFICER. The Chair is advised that the yeas and nays having been ordered on the Cooper amendment, the request for a division on the other parts, not included in the Cooper amendment, is not in order at this time.

Mr. PASTORE. Mr. President, a parliamentary inquiry.

The PRESIDENT. The Senator will state it.

Mr. PASTORE. If the Cooper amendment were rejected, would not the Douglas amendment have to be modified? Otherwise, we would have to vote on part C a second time. Is that not correct?

The PRESIDING OFFICER. The question would then come on the amendment of the Senator from Illinois to strike out all of that section, whereas the amendment of the Senator from Kentucky is to strike out only one section.

Mr. PROXMIRE. Mr. President, a parliamentary inquiry.

The PRESIDING OFFICER. The Senator will state it.

Mr. PROXMIRE. Is it not true that the amendment of the Senator from Illinois was pending, and therefore the Cooper amendment would be in order only as an amendment to the amendment of the Senator from Illinois?

The PRESIDING OFFICER. The Chair is advised that the Senator's statement is not correct.

Mr. HICKENLOOPER. Mr. President, I ask for the regular order.

The PRESIDING OFFICER. The question is on agreeing to the amendment offered by the Senator from Kentucky [Mr. COOPER].

The yeas and nays have been ordered, and the clerk will call the roll.

The legislative clerk proceeded to call the roll.

Mr. METCALF (when his name was called). On this vote I have a pair with the Senator from Texas [Mr. YARBOROUGH]. If he were present and voting he would vote "yea." If I were at liberty to vote, I would vote "nay." I therefore withhold my vote.

The rollcall was concluded.

Mr. MANSFIELD. I announce that the Senator from Nevada [Mr. BIBLE], the Senator from North Dakota [Mr. BURDICK], the Senator from Mississippi [Mr. EASTLAND], the Senator from Louisiana [Mr. ELLENDER], the Senator from Arkansas [Mr. FULBRIGHT], the Senator from Minnesota [Mr. HUMPHREY], the

Senator from Washington [Mr. MAGNUSON], the Senator from Utah [Mr. MOSS], the Senator from Maine [Mr. MUSKIE], the Senator from Florida [Mr. SMATHERS], the Senator from Massachusetts [Mr. SMITH], and the Senator from Texas [Mr. YARBOROUGH] are absent on official business.

I further announce that the Senator from New Mexico [Mr. ANDERSON], the Senator from Alaska [Mr. GRUENING], the Senator from Wyoming [Mr. HICKEY], and the Senator from Missouri [Mr. SYMINGTON] are necessarily absent.

I further announce that, if present and voting, the Senator from North Dakota [Mr. BURDICK], the Senator from Louisiana [Mr. ELLENDER], the Senator from Alaska [Mr. GRUENING], the Senator from Minnesota [Mr. HUMPHREY], the Senator from Washington [Mr. MAGNUSON], the Senator from Utah [Mr. MOSS], the Senator from Maine [Mr. MUSKIE], and the Senator from Massachusetts [Mr. SMITH] would each vote "yea."

On this vote, the Senator from Florida [Mr. SMATHERS] is paired with the Senator from Missouri [Mr. SYMINGTON]. If present and voting, the Senator from Florida would vote "nay," and the Senator from Missouri would vote "yea."

Mr. DIRKSEN. I announced that the Senators from Maryland [Mr. BUTLER and Mr. BEALL], the Senator from Utah [Mr. BENNETT], the Senator from South Dakota [Mr. BOTTUM], the Senator from Indiana [Mr. CAPEHART], the Senators from New Hampshire [Mr. COTTON and Mr. MURPHY], the Senator from Arizona [Mr. GOLDWATER], the Senator from Idaho [Mr. JORDAN], the Senator from California [Mr. KUCHEL], the Senator from Kentucky [Mr. MORTON], the Senator from Massachusetts [Mr. SALTONSTALL], and the Senator from Delaware [Mr. WILLIAMS] are necessarily absent.

The Senator from Wisconsin [Mr. WILEY] is detained on official business.

If present and voting, the Senator from Maryland [Mr. BEALL], the Senator from Indiana [Mr. CAPEHART], and the Senator from Idaho [Mr. JORDAN] would each vote "nay."

The result was announced—yeas 40, nays 29, as follows:

[No. 238 Leg.]

YEAS 40

Aiken	Hill	Pastore
Bartlett	Jackson	Pell
Byrd, W. Va.	Javits	Prouty
Carroll	Keating	Proxmire
Case	Kefauver	Randolph
Church	Long, Mo.	Russell
Clark	Long, Hawaii	Scott
Cooper	Long, La.	Sparkman
Dodd	McCarthy	Stennis
Douglas	McGee	Talmadge
Engle	McNamara	Williams, N.J.
Gore	Monroney	Young, Ohio
Hart	Morse	
Hayden	Neuberger	

NAYS 29

Allott	Fong	McClellan
Boggs	Hartke	Metcalf
Bush	Hickenlooper	Miller
Byrd, Va.	Holland	Mundt
Cannon	Hruska	Robertson
Carlson	Johnston	Smith, Maine
Chavez	Jordan, N.C.	Thurmond
Curtis	Kerr	Tower
Dirksen	Lausche	Young, N. Dak.
Ervin	Mansfield	

NOT VOTING—31

Anderson	Fulbright	Muskie
Beall	Goldwater	Pearson
Bennett	Gruening	Saltonstall
Bible	Hickey	Smathers
Bottum	Humphrey	Smith, Mass.
Burdick	Jordan, Idaho	Symington
Butler	Kuchel	Wiley
Capehart	Magnuson	Williams, Del.
Cotton	Morton	Yarborough
Eastland	Moss	
Ellender	Murphy	

So Mr. COOPER's amendment was agreed to.

Mr. COOPER. Mr. President, I move that the vote by which the amendment was agreed to be reconsidered.

Mr. KEATING. I move to lay that motion on the table.

The motion to lay on the table was agreed to.

The PRESIDING OFFICER. The question now recurs on the amendment of the Senator from Illinois [Mr. DOUGLAS], as amended.

Mr. GORE. Mr. President, a number of Senators have indicated that they have engagements. I understand that the Arkansas Choir is about to present a program. I will make an offer. If Senators will give me their attention for 5 minutes, I will finish in 5 minutes.

I think the philosophical basis for support of or opposition to the amendment was amply delineated by comments of the distinguished and able senior Senator from Oklahoma [Mr. KERR], who said a few moments ago that the people who come to Washington "to petition their Congress represent the sum total of the population of the United States; and it is our job to represent them." He also stated that "all the people who come here constitute ail of America."

I fear there is a tendency to feel that this is so; but I deny that it is or ought to be a fact. True, we are now tending to become a government by organization and for organization. This is contrary to the fundamental concept of our system which is based upon individual citizenship and the concept that Members of Congress represent the whole people and must give the interests of the whole people more weight than is given private interests, no matter how organized.

The question involved in this amendment is not the constitutional right of petition. That is not at issue in the bill at all. No right is impinged by the pending amendment. The right of petition is clear; indeed, Congress could not deny it if it desired to do so. What is involved? I think there is here a basic question of public policy in the ends which can properly be promoted by tax law—the policy of giving legislative endorsement by way of tax deduction to lobbying on a national scale; tax deduction for lobbying not only with respect to contacts with Members of Congress, but appearances before congressional committees. It is activity at the congressional level that we hear most about.

But if we read the bill, starting at the bottom of the section, instead of the first sentence of the section, we find that a tax deduction is provided for lobbying all the way down to the grass roots—with respect to legislative bodies of the counties; the city council of the smallest

incorporated town in every State; and State legislatures.

Dues are made tax deductible. What kind of dues? In what amount? How assessed? No definition is provided. I believe the records show that last year the American Medical Association spent more money for lobbying than any other organization in the United States. Suppose next year the AMA spent twice that much, or ten times that amount; and at the end of the year, each individual member of the AMA received a notice saying, "Your dues are thus and so"—perhaps 10 times or 25 times what they were last year. No limits are placed by the bill; there is no definition in the bill. The word used is "dues". For what purpose? For the purpose of buying \$100 a plate dinners? For the purpose of ringing doorbells in an attempt to manufacture sentiment?

The real question before the Senate is a simple one: Do we want to preserve the traditional concept of our democratic way of life that Members of Congress represent individual citizens, or do we want to give legislative endorsement and encouragement to government by organization and for organization? The question is just that simple, it seems to me.

Perhaps it is old fashioned, but I prefer to view my job otherwise. I do not wish to see the people of the country misled—as they were, recently, into thinking that a withholding procedure was a new tax.

Mr. President, sometimes I feel that my heaviest responsibility is to represent those who are least aware of their need for representation—to be of assistance to the people who do not belong to special-interest lobbies.

Mr. PASTORE. Mr. President, will the Senator from Tennessee yield?

Mr. GORE. I yield.

Mr. PASTORE. The Senator does make a point; but it has been my experience, in serving on congressional committees, that they invite people to come to Washington and to testify before them, and not all the witnesses are subpoenaed. Many of them are invited to come to testify, in order to help the committee make its record. Does the Senator take the position that they should have to pay their own expenses, out of their own pockets, rather than be able to have them handled as deductible expenses? Such witnesses testify before many committees—in fact, before all the committees, including the Joint Committee on Atomic Energy. When we invite them to come before the committees, as witnesses, to help the committees, how would the Senator from Tennessee have their expenses treated?

Mr. GORE. It seems to me that when Congress wishes to receive testimony from an individual who is knowledgeable in a given area, Congress should be able to provide reimbursement of his expenses.

Mr. PASTORE. But Congress does not do that; that is done only when a witness is subpoenaed. Only when a witness is subpoenaed are his expenses paid. Otherwise, there is absolutely no appropriation for any such purpose.

Many witnesses come here and testify before the congressional committees at their own expense. For instance, witnesses testify for that purpose before the Joint Committee on Atomic Energy. The Senator from Tennessee says they would have to pay their expenses out of their own pockets. That makes no sense at all.

Mr. GORE. But there is no reason why there could not be such an appropriation; and I think public policy might well be served by adopting such a policy.

Mr. PASTORE. But that would have to be done, it seems to me, before this provision is discarded; otherwise there would be a vacuum.

Mr. GORE. On the contrary, if the provisions of this section of the bill are adopted, it seems to me the other course is foredoomed. I think this is quite an unwise provision. The Senator from Rhode Island and the Senator from Tennessee are discussing expenses in connection with appearing and testifying before a congressional committee. But I say to my friend from Rhode Island that will be a minuscule part of the expenses dealt with and encouraged by this provision. Senators should read the section. Let them find in it some definition of "dues" or some definition of "expenditures" or some definition of "research," or some way, by means of this provision, whereby the government could deny a tax deduction for a retainer fee paid to the leading politician in every congressional district or in every county in the country, or to lawyers or public-relations experts. This provision gives legislative sanction to nationwide lobbying organizations, operating from the level of city councils and the magistrates' courts in the counties to the State legislatures and to the Congress. This provision is more serious than some seem to think. I feel that its adoption would be a grave mistake.

Mr. President, I promised to be brief; and I now take my seat.

Mr. HOLLAND. Madam President—
The PRESIDING OFFICER (Mrs. NEUBERGER in the chair). The Senator from Florida is recognized.

Mr. HOLLAND. Madam President, I strongly support the provision of the committee bill which is being attacked by means of this amendment; and I oppose the amendment.

Everyone knows that when a business, large or small, a corporation or an individual, is being sued in court and is being threatened, either in its entirety or in regard to any part—large or small—of its equities, it has a right to employ lawyers or economists or specialists or other professional men in various fields, and the expenses in connection with employing them are deductible as business expenses. Everyone knows that, and it is taken for granted.

Madam President, the greatest Chief Justice our country ever had made one statement for which he will always be remembered—namely, that the power to tax is the power to destroy.

When taxation is proposed or threatened against a business, and when the business believes the tax will be destruc-

tive in whole or in part of its property rights, why is it any less a business expense for that business to employ someone who can properly defend it, and, in that connection, send to Washington someone—whether a lawyer or an economist or an engineer or some other expert—and have the knowledge that that expert will do his best to represent the business, and have the knowledge that the expense of employing that expert will be deductible as a business expense.

It seems to me that is so reasonable and is such a commonsense proposal that no one could for a moment deny it.

Shall we say that anyone who is engaged in business or who has a business, large or small, does not have the right to defend himself when he is confronted with a legislative proposal which he regards as injurious or destructive of his business, and does not have the right to regard the expenses of his defense as expenses which he should be allowed to deduct from his income-tax statement? It seems to me that such a provision is just full of commonsense and reason and equity, and of course I support it.

The only other provision left in the Senate version of the bill against which the amendment is directed is the similar provision allowing such a business to deduct as a business expense its payment to an association or organization of which it is a part—an organization which is conducting the defense or is engaging in the representation of a group of businesses—for example, a railroad which pays dues to the National Association of Railroads for assembling the facts which relate to the entire industry may deduct such dues, and similar cases will occur to all Senators. That is all that is left in this provision of the bill.

The only provision which might have been subjected to reasonable question was the one which was attacked by the Senator from Kentucky. In its wisdom, the Senate has deleted that provision. I did not agree with that act of deletion, but I do agree that that provision was more subject to question than the two portions which are left.

But the provision now under consideration simply cannot be questioned—the provision that any businessman shall have a right to proceed to his own defense and, in that connection, to employ those he may need to represent and defend him—whether it be a lawyer or an economist or an engineer, or whoever in his opinion will properly represent his particular business and regard such employment as a business expense. I think the committee provision should be defended, and that the amendment should be rejected.

Mr. KERR. Madam President, all of us know that the Government is collecting taxes of nearly \$100 billion a year from the American people and from American businesses, both large and small, regardless of the size of their financial activities or interests. Such taxes are collected from corporations, many of them regulated and controlled, and all of them having to do with the life, the health, the vigor, and the vitality of American business.

To say that the expenses should not be deductible when a taxpayer or citizen comes to Washington in connection with a matter directly related to his business is, as the Senator from Florida has just now said, like saying to that taxpayer that if he has a matter which is in court, he can employ a lawyer to help defend him, but he cannot deduct the expense of employing the lawyer—or that if a taxpayer or a businessman has a matter before the Federal Trade Commission or the Federal Power Commission or the Interstate Commerce Commission, he can defend himself, but cannot deduct that expense as a business expense.

I cannot imagine the concept of those who would say that expenses directly connected with the trade or business of a taxpayer should not be deductible—when the taxpayer travels to Washington and testifies before a congressional committee, when the Congress is in the process of increasing taxes, which now total nearly \$100 billion a year, or is in the process of expanding the restrictions or controls, which already are most burdensome.

So I join the Senator from Florida in urging that the amendment be rejected.

The PRESIDING OFFICER. The question is on agreeing to the amendment of the Senator from Illinois [Mr. DOUGLAS] to strike out section 3 on page 38, line 17, through line 2, page 40, as amended by the Senator from Kentucky [Mr. COOPER].

The yeas and nays have been ordered, and the clerk will call the roll.

The Chief Clerk proceeded to call the roll.

Mr. HART (when his name was called). On this vote I have a live pair with the Senator from Nevada [Mr. BIBLE]. If he were present and voting, he would vote "nay." If I were at liberty to vote, I would vote "yea." I therefore withhold my vote.

The rollcall was concluded.

Mr. KERR. I announce that the Senator from Nevada [Mr. BIBLE], the Senator from North Dakota [Mr. BURDICK], the Senator from Mississippi [Mr. EASTLAND], the Senator from Louisiana [Mr. ELLENDER], the Senator from Arkansas [Mr. FULBRIGHT], the Senator from Minnesota [Mr. HUMPHREY], the Senator from Washington [Mr. MAGNUSON], the Senator from Montana [Mr. MANSFIELD], the Senator from Utah [Mr. MOSS], the Senator from Maine [Mr. MUSKIE], the Senator from Georgia [Mr. RUSSELL], the Senator from Florida [Mr. SMATHERS], the Senator from Massachusetts [Mr. SMITH], the Senator from Alabama [Mr. SPARKMAN], and the Senator from Texas [Mr. YARBOROUGH] are absent on official business.

I further announce that the Senator from New Mexico [Mr. ANDERSON], the Senator from Alaska [Mr. GRUENING], the Senator from Wyoming [Mr. HICKLEY], and the Senator from Missouri [Mr. SYMINGTON] are necessarily absent.

I further announce that, if present and voting, the Senator from Mississippi [Mr. EASTLAND], the Senator from Louisiana [Mr. ELLENDER], the Senator from Montana [Mr. MANSFIELD], and the Senator

from Missouri [Mr. SYMINGTON] would each vote "nay."

On this vote, the Senator from Alaska [Mr. GRUENING] is paired with the Senator from Florida [Mr. SMATHERS]. If present and voting, the Senator from Alaska would vote "yea," and the Senator from Florida would vote "nay."

Mr. YOUNG of North Dakota. I announce that the Senators from Maryland [Mr. BUTLER and Mr. BEALL], the Senator from Utah [Mr. BENNETT], the Senator from South Dakota [Mr. BOTTOM], the Senator from Indiana [Mr. CAPEHART], the Senators from New Hampshire [Mr. COTTON and Mr. MURPHY], the Senator from Arizona [Mr. GOLDWATER], the Senator from Idaho [Mr. JORDAN], the Senator from California [Mr. KUCHEL], the Senator from Kentucky [Mr. MORTON], the Senator from Massachusetts [Mr. SALTONSTALL], and the Senator from Delaware [Mr. WILLIAMS] are necessarily absent.

The Senator from Illinois [Mr. DIRKSEN], the Senator from Iowa [Mr. HICKENLOOPER], and the Senator from Wisconsin [Mr. WILEY] are detained on official business.

If present and voting, the Senator from Maryland [Mr. BEALL], the Senator from Utah [Mr. BENNETT], the Senator from South Dakota [Mr. BOTTOM], the Senator from Indiana [Mr. CAPEHART], the Senator from Illinois [Mr. DIRKSEN], the Senator from Idaho [Mr. JORDAN], the Senator from California [Mr. KUCHEL], the Senator from Kentucky [Mr. MORTON], and the Senator from Massachusetts [Mr. SALTONSTALL] would each vote "nay."

The result was announced—yeas 13, nays 51, as follows:

[No. 239 Leg.]

YEAS—13

Bartlett	Gore	Pell
Carroll	Kefauver	Proxmire
Church	McNamara	Young, Ohio
Clark	Morse	
Douglas	Neuberger	

NAYS—51

Alken	Hayden	Metcalf
Allott	Hill	Miller
Boggs	Holland	Monroney
Bush	Hruska	Mundt
Byrd, Va.	Jackson	Pastore
Byrd, W. Va.	Javits	Pearson
Cannon	Johnston	Prouty
Carlson	Jordan, N.C.	Randolph
Case	Keating	Robertson
Chavez	Kerr	Scott
Cooper	Lausche	Smith, Maine
Curtis	Long, Mo.	Stennis
Dodd	Long, Hawaii	Talmadge
Engle	Long, La.	Thurmond
Ervin	McCarthy	Tower
Fong	McClellan	Williams, N.J.
Hartke	McGee	Young, N. Dak.

NOT VOTING—36

Anderson	Fulbright	Moss
Beall	Goldwater	Murphy
Bennett	Gruening	Muskie
Bible	Hart	Russell
Bottom	Hickenlooper	Saltonstall
Burdick	Hickey	Smathers
Butler	Humphrey	Smith, Mass.
Capehart	Jordan, Idaho	Sparkman
Cotton	Kuchel	Symington
Dirksen	Magnuson	Wiley
Eastland	Mansfield	Williams, Del.
Ellender	Morton	Yarborough

So Mr. DOUGLAS' amendment, as amended, was rejected.

Mr. KERR. Madam President, I move that the vote whereby the amendment was rejected be reconsidered.

Mr. CURTIS. Madam President, I move to lay that motion on the table.

The PRESIDING OFFICER. The question is on agreeing to the motion to lay on the table the motion to reconsider.

The motion to lay on the table was agreed to.

Mr. CURTIS. Madam President, I do not wish to call up an amendment, but I wish to discuss an amendment.

It is my understanding that, perhaps tomorrow, the distinguished Senator from Illinois will offer his amendment identified as "8-23-62-K," commonly referred to as H.R. 10. The amendment relates to payments into retirement funds, before taxes, for the self-employed and for unincorporated businesses.

The Senator from Nebraska has an amendment "8-30-62-I," which is intended to be an amendment to the Dirksen amendment. I wish to explain that amendment at this time, briefly.

Under existing law corporations can set up pension plans covering both their employees and their officers. Payments into the pension funds are made before taxes. The pension funds themselves are tax free. The income which comes to the pension funds is not subject to tax.

That is the reason why there will be proposed the Dirksen amendment, known as H.R. 10. An individual doctor, lawyer, operator of a farm, or operator of a grocery store which is unincorporated, when he saves for his retirement, must do so from income upon which he has paid the tax. Then, if the income is put into a fund and it earns interest or dividends or other income, that also is subject to tax annually.

Corporate entities are able to provide pension funds or retirement funds before taxes, and those funds can grow without payment of taxes, while the individual citizen must save for his retirement after taxes, and the income he may receive is taxed annually.

H.R. 10 would provide that the individual, by meeting substantially the same requirements met by a corporation, could save for his retirement before taxes. This would mean that the individual lawyer, in order to qualify a pension plan, would also provide for his employees, other lawyers working for the firm, the stenographers, and so on. The doctor, the grocer, the farmer, or someone else would have to do the same thing. This would tend to equalize the opportunity for the citizens to save for their own retirement before taxes.

However, if H.R. 10 should be passed, there still would be many individuals who would be employed for a concern which would not and perhaps could not set up a pension plan. There would be individual businessmen and individual farmers who, because of advanced years or because of limited income of their businesses, could not set up a plan and take advantage of H.R. 10.

My amendment to H.R. 10 would provide that any individual, in any calendar year in which he was not covered by either a corporate plan or a plan under H.R. 10 could buy a special issue of Government bonds in an amount not to exceed \$300 a year, and that he could

buy such bonds before taxes. Those bonds could be cashed when the person reached 64½ years of age, or was older. When the individual cashed them, he would pay taxes on the entire amount, both the principal and the interest.

The amendment of the Senator from Nebraska to H.R. 10 would equalize the opportunity for our people to provide for their pensions. It would place Government bonds in the hands of individuals, as contrasted to banks and other institutions. It would provide long-term financing for Government bonds. It would promote thrift. It would make it possible for the people who are not so fortunate as to be able to work for a concern which has a retirement plan to save a small amount and to do so before taxes.

As a matter of simple equality, these people should have that opportunity.

A question has been raised as to why the amount should be held down to \$300 a year, or \$25 a month. The people about whom I am talking perhaps cannot have a great deal more than that. That is a reason. When they get greater allowances, they must set up plans for their employees. These people would have to meet other requirements. The modest provision would cover people who could not meet other requirements.

It is my expectation that tomorrow, or whenever the Dirksen amendment is offered, I shall offer this amendment, which would permit the people with modest incomes to save some money for old age and to do so before taxes, exactly as the corporate officers and corporate employees now do, and as it is proposed that or more successful farmers, businessmen and professional men could do if H.R. 10 should pass.

Madam President, I yield the floor.

Mr. McCARTHY. Madam President, I offer the amendment which I send to the desk and ask to have stated.

The PRESIDING OFFICER. The amendment will be stated for the information of the Senate.

The LEGISLATIVE CLERK. On page 98, in line 14, it is proposed to strike out the period and to insert a comma and the following: "and without any deduction for dividends to policyholders provided by section 832(c) (11)".

Mr. McCARTHY. Madam President, the amendment is in the nature of a correcting amendment. It was made necessary because, subsequent to the adoption of a committee amendment in the Finance Committee, another amendment was adopted, and the language of the bill as it now stands would have the effect of giving an unintended benefit to certain insurance companies.

Mr. KERR. Madam President, the Senator from Oklahoma has also submitted a series of amendments, one of which is the amendment that has been offered by the Senator from Minnesota. Therefore I request its adoption.

The PRESIDING OFFICER. The question is on agreeing to the amendment of the Senator from Minnesota. The amendment was agreed to.

THALIDOMIDE AND THE FOOD AND DRUG ADMINISTRATION

Mr. KERR. Madam President, I ask unanimous consent that two very able articles which appear in the current issue of the Saturday Review, namely, an article by Mr. John Lear entitled "The Unfair Story of Thalidomide," and another article tracing the history of the work of Dr. Frances Oldham Kelsey and Dr. Barbara Moulton, be printed at this point in the RECORD.

There being no objection, the articles were ordered to be printed in the RECORD, as follows:

THE UNFINISHED STORY OF THALIDOMIDE

Two years and three months ago—on the 3d day of June 1960—Mr. George P. Larrick, U.S. Commissioner of Food and Drugs, the man responsible for policing abuses in the marketing of drugs in this country, appeared as a witness before the Senate Subcommittee on Antitrust and Monopoly in Washington, D.C. He was there primarily to explain how it was that his professional subordinate and personal friend, Henry Welch, Ph. D., then Chief of the Antibiotics Division of the Food and Drug Administration, had managed to obtain and keep official sanction for an arrangement under which Dr. Welch collected more than a quarter of a million dollars in private fees as editor of antibiotics promotion journals at the same time he was being paid a Government salary for judging the worth of antibiotics to physicians and their patients. Mr. Larrick explained that he had trusted his Antibiotics Division Chief completely, hence had no cause to ask for figures when Dr. Welch assured him that only a few small honoraria were involved in straightforward editorial work free of ethical conflict.

A woman physician recently resigned from the FDA staff—Dr. Barbara Moulton, daughter of a family long distinguished in American science—had testified earlier that questionable relationships like the one existing between Dr. Welch and the drugmakers were constantly invited through repeated visiting and telephoning of FDA officers by drug company agents. But Commissioner Larrick denied "categorically * * * all * * * suggestions and accusations * * * that the review of new drug applications * * * may in some instances * * * have been superficial."

"You will recall * * * the tragedy that led to the enactment [in 1938] of the new drug section of the present law," he testified. "In 1937 a drug manufacturer, believing that a liquid solution of sulfanilamide would be more acceptable to the patient than a tablet, used [as a solvent] an industrial chemical that had heretofore been widely employed as an antifreeze. Animal testing would have exposed the danger from this poisonous elixir. But the manufacturer did not test his liquid. His mixture of sulfanilamide killed over 100 people before we could remove stocks from the market."

"For the past 22 years * * * we have not had a repetition of the type of disaster that brought the new drug section into the law, and will not under the present procedures."

Let us set them aside for consideration later, and proceed with recollection of events as they occurred in 1960.

The Senators accepted Commissioner Larrick's assurances and passed over suggestions that he be requested to retire from his post of authority.

On that same day, however, Commissioner Larrick's official superior, the then U.S. Secretary of Health, Education, and Welfare,

Hon. Arthur S. Flemming, directed that two investigations be opened into FDA's affairs. One of these studies would be scientific, and would be carried out by a special panel of the National Academy of Sciences. The second inquiry would be administrative, and would be assigned to a task force headed by Mr. Charles Kendall. In due time, the National Academy panel recommended that the drug law be changed to require new drugs to be proved effective as well as safe before going onto the market. The Kendall group urged, among other advices, that fraternization between FDA officers and drugmakers' agents be discouraged; and in January 1961 Commissioner Larrick's deputy, John Harvey, circulated a memo to the FDA staff calling for obedience to the Kendall injunction. Why the memo was necessary to exorcise a spirit whose presence Commissioner Larrick refused to admit was not explained.

One year and six months later—on July 15, 1962—the Washington Post published published word that an hypnotic drug called thalidomide (tha-lid'-o-mide)—implicated in the birth during 1961 of thousands of armless, legless, earless and otherwise malformed babies (some mere cocoons of flesh, with heads attached) to women in many foreign countries who took the drug in early pregnancy—had been held off the American market by a stubborn woman doctor in FDA, Dr. Frances Oldham Kelsey, herself mother of two. The writer of this Post news report, Mr. Morton Mintz, said Dr. Kelsey had accomplished her purpose only after months of resistance to a steady stream of telephone calls, letters, personal visits and appeals over her head to her FDA superiors by representatives of the William S. Merrell Company of Cincinnati, which wanted to sell the drug in this country.

U.S. Senator ESTES KEFAUVER, of Tennessee, before whose subcommittee Commissioner Larrick in 1960 had denied the possibility of such tactics by drugmakers, immediately proposed to President Kennedy that Dr. Kelsey be awarded the Distinguished Federal Civilian Service Medal for standing off the promoters of thalidomide.

The Merrell Co. reacted by publishing a statement minimizing and justifying the demands it had made on Dr. Kelsey's time and patience. Senator KEFAUVER replied by reading into the CONGRESSIONAL RECORD on August 8, 1962, a play-by-play account of Dr. Kelsey's experience (see chronology below). Taken from a memo in FDA's files, this document listed 50-odd different approaches including a question of libel and an open hint that Commissioner Larrick himself would be enlisted by the drug house to neutralize Dr. Kelsey if she continued to refuse a permit.

What medical miracle did thalidomide's maker claim deserved such urgency?

Thalidomide would help people to sleep. Very well. The drug house salesman lost their sense of perspective on thalidomide. Such things happen to all of us from time to time. Why emphasize this instance? Dr. Kelsey had some trouble keeping thalidomide off the American market. But she did keep it off. That's history. Can't we treat it as history?

Even after some matters have passed into history, they ought not to be forgotten. But does thalidomide yet belong to history?

The Council on Drugs of the American Medical Association has issued a public statement saying that although thalidomide has never been sold commercially in this country, the drug has been in experimental use since 1956. Since the experimenters are not identified in this document, and since

existing law does not require the drug houses to notify the Government of such experiments, and since physicians taking part in the experiments are not required to tell patients that the patients are being used as experimental subjects, and since physicians are not required by law to report births of abnormal babies, there is no way of knowing how many babies deformed by the drug are now living as helpless and hopeless charges of unwitting parents.

It was only after the epidemic of infant monsterism in Europe became public knowledge in late 1961 and early 1962 that occasional deformed babies were found to have been born of European mothers who took thalidomide as far back as 1957.

There is one armless child in New England, now aged 3 years, who medical authorities are almost certain is a product of thalidomide's experimental use here. But the baby's mother cannot remember what pills she took during her pregnancy. Can you remember what pills you took 4 years ago, or even last year?

Troubled parents all over the country have written letters to Government offices in Washington by the hundreds since Dr. Kelsey got the medal from the President. Among them is a report of an unexplained crop of deformed babies born in the same block of New York City within a short span of time 5 or 6 years ago. All the families in the block patronized the same drug store. Could thalidomide somehow have got into drugstores during its early period of experimental use? Some doctors have sold drugmakers' "samples" of other drugs to druggists, who have got into trouble on resale, sometimes because the labels got mixed up. Or are drugs other than thalidomide, capable of mutilating babies, on the market unknown to physicians?

Appropriate investigation of such questions is a long and tedious process. Without pinpoint documentation of details, firm answers are unlikely. The first set of reliable statistics on infant deformations in the country is only now being compiled in Philadelphia by the Foundation for Medical Research—Perinatal Project. Working on a grant from the American Medical Association, supplemented by other sources interested in drugs, Dr. Sydney Kane, chief of pediatrics at Frankford Hospital, is tabulating, on a high-speed computer, voluntary reports of births in 150 hospitals in 43 of the 50 States, the District of Columbia and Puerto Rico. During the 18 months ending with June 30, 1962, the number of babies born with any type of abnormality averaged 2.7 in 100,000 births.

This figure will in time become a base for comparative studies. Because there is no way to tell how many isolated cases of thalidomide deformation may be dotted through Dr. Kane's record of the last 18 months, it would probably take an epidemic of abnormalities to show up clearly in the data.

What are the prospects of an epidemic of this sort arising from Merrell's experiments with thalidomide?

When Merrell applied for an FDA permit to sell the drug on September 12, 1960, the company said its experimenters had been using the drug on human patients since January 1959. In anticipation of sales arising from the experiments, Merrell had originally imported approximately 2,000 kilograms of thalidomide from Chemie Gruenthal, the West German drug house whose employees (Herbert Keller and Willie Kunz) had synthesized the drug in 1953. Later, Merrell itself had manufactured 3,300 kilograms more in this country. Simple addition gives a total of 5,300 kilograms.

On March 8, 1962, when Merrell withdrew its application for a permit to sell the drug, the company had 3,200 kilograms of the 5,300 total in the company warehouses. The

2,100 kilogram balance had gone out to physicians for experimental use.

A kilogram contains 1,000 grams. A gram contains 1,000 milligrams. Therefore, there are 1 million milligrams in a kilogram. In other words, 2,100 million milligrams of thalidomide had been put into the hands of doctors.

When FDA rounded up what was left of the drug in doctors' offices between July 27, 1962, and August 21, field agents found 79 American physicians with a total of 25,096 unused pills.

The biggest size thalidomide pill that Merrell made contained 200 milligrams. If all the confiscated pills had been that size, the total thus accounted for would have been 5,019,200 milligrams.

What happened to the remaining 2,094,980,800 milligrams that Merrell turned over to the doctors?

Merrell told FDA it was all disposed of by 1,231 physicians who took part in the experiment.

FDA agents turned up 36 additional doctors who were not participating in the experiment but nevertheless had thalidomide in their possession and had prescribed it to patients.

"A few investigators," FDA explained, "gave some of the drug to their partners or to other physicians."

FDA's total of the number of patients using the pill was 19,822.

In order for that many patients to account for that much of a drug, each patient would have to take a 200-milligram pill every day for 528 days—the best part of one and a half years.

Merrell says an undisclosed amount of the drug was destroyed by the doctors. Whatever that amount is would have to be deducted from the immense dosage designated above for the experimental patients. On the other hand, it must be recognized that the average dose of thalidomide is not 200 milligrams but perhaps 100 or even 50 milligrams. Merrell made tablets of the stuff in 200 milligrams, 100 milligrams, 50 milligrams, 25 milligrams, 12½ milligrams, 6¼ milligrams, and 4 milligrams. It was prescribed as a sleep-inducer, a cough suppressor, a bellyache quieter, and an antidote for "morning sickness" in pregnancy.

Therefore, the number of doses of thalidomide distributed over the country was considerably greater than the number calculated on the basis of a 200 milligram average dose.

With such a broad distribution, some questions logically arise:

At what point does medical experimentation end, and when does sample salesmanship begin?

Was thalidomide actually on the American market in every sense except a sale price?

Could FDA possibly be sure that only 19,822 persons took Merrell's thalidomide pills?

Could the physicians to whom Merrell gave the drug be sure?

One thousand pills were found in the medicine cabinet of a single doctor's office in Virginia months after Merrell called off its experiment with thalidomide.

One doctor in New York kept prescribing thalidomide to a patient and was puzzled by her repeated failure to fill the prescription at a drugstore.

FDA says that 3,760 women of childbearing age, 207 known to be pregnant, got the drug as part of the Merrell experiment and that one of these women may have produced a deformed baby.

Dr. Helen Taussig, of Johns Hopkins University, has authorized me to say that she knows of another deformed baby born of a mother who took some of Merrell's pills. This mother had participated in the thalidomide experiment without the mother's

knowledge, her doctor's knowledge, or Merrell's knowledge. She was given the drug by an older person who had received it from a doctor.

"I fear we will learn of others who have taken the drug in the same innocent way," Dr. Taussig told me. Her opinion must be respected not only for the fame of her "blue baby" research but because she is the one physician in this country who knows the German and British experience with thalidomide at firsthand. Within days after learning about the epidemic of infant monsterism abroad from a German doctor who visited her Johns Hopkins clinic, she took off on a tour of European hospitals and clinics last spring. She alerted the American medical community to the danger here as soon as she learned of the Merrell experiment from FDA upon her return home.

Dr. Taussig believes that even if the prospect of an American epidemic of malformed infants is small, the danger should be faced openly. Women who have reason to suspect the abnormality of embryos now in their wombs could seek X-ray confirmation. Where malformation is apparent, therapeutic abortion is as justifiable in Dr. Taussig's opinion as is therapeutic abortion for mothers attacked by German measles. German measles abortions are legal in most States.

Qualified statisticians familiar with pharmacy not only share Dr. Taussig's concern about malformed babies yet to come, but anticipate worse possibilities than she. One who prefers not to be quoted because of his vulnerable position in the Government figures that by Christmas, or by Easter at the latest, between 30 and 40 malformed children may be born in this country of women who took thalidomide.

This chilling estimate may be wrong. The man who made it hopes it will turn out to be so. The gods of chance may in the end be kind. Through an incredible piece of luck American parents may escape any sizeable epidemic of helpless offspring. But during the months of anxious waiting that lie ahead, it will not be reassuring to know that drug experiments on human guinea pigs can be and have been conducted in this country by persons not only inexperienced in any particular discipline of healing art but lacking even a medical degree.

The whole business of drug experimenting (and business is a far more accurate word for it than is science under the law as now worded) is turned over to the drugmakers. They pick the experimenters, decide the number of same, and are free to accept or reject anyone's claim to qualifications and facilities. They may begin using drugs on humans before safety has been established through animal tests, and they have the privilege of keeping the patients in ignorance throughout lest knowledge of the guinea pig status have some undesirable psychological effect on the results of the experiment.

FDA need not be, and normally is not, advised of these experiments until a request comes in for a sales permit for the drug.

Considering this quality of drug experimentation, FDA Commissioner Larrick was hardly in position in June 1960 to say that "under the present procedures . . . we . . . will not . . . have . . . a repetition of the type of disaster that brought the new drug section into the law." For it was faulty procedures, not faulty law, that made it possible for the thalidomide experiment to threaten unborn children. The law specifically authorizes administrative regulations to cover drug experiments. The regulations could have been changed at any time Mr. Larrick chose to recommend change. The climate for change has been favorable ever since SR exposed the conflict of interest in Dr. Henry Welch's affairs in February 1959.

was still incomplete and that in particular she was awaiting receipt of the data on safety, which had been promised at the September 7 meeting.

"September 18, 1961: Mr. Murray telephoned Dr. Kelsey to ask what additional data was required. Dr. Kelsey told him she needed the toxicity data promised at the recent meeting.

"September 26, 1961: Mr. Murray telephoned Dr. Smith to ask whether it was possible to predict when the drug application would become effective. Merrell wanted to put the drug on the market by the middle of November; to do that, printing of the labels should commence early in October. When Dr. Smith offered no prediction, the telephone call was switched to Dr. Kelsey. Mr. Murray tried to get her to set a deadline for marketing the drug. He wondered if he could give labeling changes on the telephone so that the printing could begin in October and the drug could be on the market by Christmas. Dr. Kelsey said no.

"September 29, 1961: Merrell sent new data on use of the drug during the later months of pregnancy.

"October 2, 1961: Merrell sent a letter correcting an accidental omission from its letter of September 29.

"October 19, 1961: Merrell sent further data on nervous side effects of the drug.

"October 23, 1961: A Merrell representative telephoned one of Dr. Kelsey's colleagues in the new drug branch of FDA to ask suggestions on who would be good investigators to study the drug in children.

"November 2, 1961: Merrell sent changes in labeling and promised further data.

"November 7, 1961: Dr. Kelsey advised Merrell by letter that the application was still incomplete and consequently was again being considered as withdrawn and resubmitted.

"November 30, 1961: Mr. Murray called Dr. Kelsey to tell her that the drug had been withdrawn from sale in Germany because of reports of abnormal babies born to women who took the drug in early pregnancy. He expressed hope that the abnormal births would prove to be only coincidental. Dr. Kelsey questioned the safety of the drug in view of the fact that one of its uses was supposed to be in treatment of morning sickness.

"December 27, 1961: Dr. Kelsey advised Merrell by letter that the application was still incomplete in absence of data relative to the drug's role in deformities in newborn babies.

"March 8, 1962: Merrell withdrew its application for sale of the drug in the United States.

"March 14, 1962: Dr. Kelsey acknowledged withdrawal of the drug application.

"April 11, 1962: Dr. Kelsey asked Merrell by letter whether the drug was still undergoing investigational use. If so, she asked to be informed what had been done to warn physicians of the dangers of the drug. She asked what measures the company had taken to inform doctors of the association between the drug and fetal abnormalities at the time the association first became known to the firm. She also asked for a complete and up-to-date list of all physicians who had been supplied with the drug for investigational purposes since the experiment began."

THE FEMININE CONSCIENCE OF FDA: DR. FRANCES OLDHAM KELSEY—SHE FOLLOWED A TRADITION THAT ONLY SEEMS NEW, THAT OF THE REASONING WOMAN

Invitations to the White House are not easily come by. A citizen who unexpectedly finds himself in position to ask a dozen others to go along and meet the President is bound to pick the dozen from those he holds in deepest regard and respect. Therefore, the character of Dr. Frances Oldham Kelsey may be illuminated by examining the

list of guests who accompanied her to the August 7, 1962, ceremony at which President John F. Kennedy clasped about her neck a ribbon dangling the Distinguished Federal Civilian Service Medal.

As everyone who can read or hear surely knows by now, Dr. Kelsey is the Canadian-born medical officer of the U.S. Food and Drug Administration who refused to approve American marketing of thalidomide, the hypnotic drug that somehow makes armless, legless, and otherwise monstrous cripples of babies born to women who take the drug "to get a good night's sleep" during early pregnancy.

Dr. Kelsey did not actually have a full dozen White House invitations to dispense. But she did receive 10 a few days in advance of her bemedalling, and, by special dispensation at the last minute, she got an 11th.

Dr. Kelsey gave the first invitation to her husband, Ellis Kelsey, Ph. D., a pharmacology professor turned public health officer, who, among many other things, had sat up nights with her in September of 1960 trying in vain to understand the chemical analysis which the William S. Merrell Co. had submitted to FDA in support of an application for permission to sell thalidomide.

The next two White House invitations went to the teenage daughters Frances Kelsey had borne to Ellis: Susan and Christine.

The fourth, fifth, and sixth invitations Dr. Kelsey gave to her brothers, John and Stewart Oldham, and to Stewart's daughter, Nancy.

The seventh invitation went to Mrs. Esther McGuire, an old friend of the Kelseys. Recipient of the eighth invitation was Dr. Kelsey's onetime professor at the University of Chicago: Dr. E. M. K. Geiling, a pioneer in pharmacological science in America.

Those eight choices were the sort anyone might be expected to make. The immediate family, an old family friend, and a revered teacher. Who would deserve the remaining three places in such company?

Dr. Kelsey's 9th, 10th, and 11th invitations to the White House went to three physician colleagues in Federal Government service: Dr. Barbara Moulton, Dr. John Nestor, and Dr. Irwin Siegel.

Why those three?

Dr. Moulton is already a familiar figure to readers of SR. Her account of her harassed life as an officer of the U.S. Food and Drug Administration was told in SR Research for July 1960 under the title: "The Drugmakers and the Government—Who Makes the Decisions?" Member of a family long distinguished in American science (her father was founding director of the Brookings Institution, an uncle for many years was operating head of the American Association for the Advancement of Science, and for a period only one other family name appeared more often than the Moulton name in "Who's Who in America"), Dr. Moulton had preceded Dr. Kelsey in the FDA post Dr. Kelsey now occupies. After fighting to keep worthless and dangerous drugs off the American market, sometimes being overruled by her official superiors, and finally acceding to a transfer in jobs before realizing that she had been moved to please a drug house, Dr. Moulton quit FDA in disgust in 1960 and related her experiences from a U.S. Senate witness stand during the Kefauver investigation of drug abuses. Following that she made a special study of drugs for the Kefauver committee, took a scientific evaluation job with the Federal Trade Commission, became a personal friend of Dr. Kelsey, and privately coached Dr. Kelsey on ways and means of avoiding some of the political booby traps Dr. Moulton herself had previously fallen into.

By inviting Dr. Moulton to the White House ceremony, Dr. Kelsey, a modest woman, was plainly saying: "Maybe you are

the one who really should be getting this medal from the President."

Natural enough.

Now the other two Government physicians among Dr. Kelsey's guests—what had they done to win her affection?

Curiously, newspaper, radio and TV commentators have ignored this question. Yet the answer is of considerable importance to a country now in the midst of a desperate struggle to escape the perils of antiquated drug control laws. When one of the newest recruits in FDA's ranks receives from the President of the United States one of the highest honors the President has in his power to bestow—an honor that logically should have gone to her more experienced superiors—it is appropriate to inquire how she managed to make herself felt effectively from so low a level. She could not have done it alone. Who helped her?

Dr. Kelsey was not nominated for the President's Distinguished Federal Civilian Service Medal by her immediate superior, Dr. Ralph Smith, or by Dr. Smith's superior, Dr. William H. Kessenich, or by Dr. Kessenich's superior, FDA Commissioner Larrick. The nomination came originally from Senator ESTES KEFAUVER of Tennessee, immediately seconded by the four other Democratic Senators on the drug investigating committee, and later seconded again by the entire membership—Democrat and Republican alike—of the Senate Government Operations Subcommittee chaired by the Honorable HUBERT HUMPHREY, Democratic party whip. Aside from Dr. Moulton, who helped Dr. Kelsey when she needed help?

The recipient of her tenth invitation to the White House, Dr. John Nestor, works on the same administrative level of FDA as Dr. Kelsey herself. He is a physician in the new drug branch of the medical division of FDA. He, too, is a fighter. To insiders, he and Dr. Kelsey are known as "the young turks of the FDA." "Some people ask whether the name fits me properly," Dr. Kelsey says wistfully. She is 48 years old. "Perhaps I am young in spirit."

The holder of the 11th of Dr. Kelsey's invitations, Dr. Irwin Siegel, is deputy director of the medical division of FDA. Throughout Dr. Kelsey's ordeal, Dr. Siegel stood between her superior, new drug branch chief Dr. Smith, and Dr. Smith's superior, medical division director Dr. Kessenich. When asked about his role in the thalidomide affair, Dr. Siegel temporizes with such remarks as: "I am happy indeed to see Dr. Kelsey's work recognized."

It is interesting that the medical division director, Dr. Kessenich, has chosen this moment in time to resign from FDA in order to take a lesser and more exhausting job in a Veterans' Administration hospital. His friends are puzzled by his explanation that he feared continuance in FDA would overstrain his heart.

It is even more interesting that FDA Commissioner Larrick should choose the new drug branch chief, Dr. Smith, as acting replacement for Dr. Kessenich. For the FDA's own chronology of the thalidomide case shows that Dr. Smith gave the drug company repeated access to Dr. Kelsey 3 months after Commissioner Larrick assured the Senators that such openings for fraternization between FDA officials and agents of the drugmakers did not occur. And in an unchallenged passage of her Senate testimony of 1960, Dr. Moulton said that Dr. Smith had unexpectedly joined a meeting between herself and four drug company delegates and had on the spot released a new drug for sale "without proof of safety for chronic use, and without waiting for completion of pharmacological studies." Dr. Moulton told the Senators she was "reasonably sure" Dr. Smith "had not at that time reviewed the data in the new drug application but was acting solely on instructions from above."

Under the usual rules of internal promotion in Federal Government agencies, Dr. Siegel would have been given an opportunity to fill Dr. Kessenich's place. The announcement that Dr. Siegel had been passed over in favor of Dr. Smith was given to the press by Mr. Larrick's office just 1 day before Dr. Siegel appeared at the White House as a guest of Dr. Kelsey: 1 of the 11 people she most wanted to share her pleasure over an accolade from the President.

Is Dr. Kelsey discouraged by any of this? If so, she is hiding the signs. She professes not to notice that anyone in FDA is out of tune with her own sense of dedication to protection of the drug consumer. The last time she stopped to count, there were upward of 600 letters on the table inside the front door of her home on Brookside Drive in Kenwood, a Maryland suburb of Washington, D.C.; most of them were from women cheering her on, telling her where to look for clues to drug law conundrums she might have missed in her reading of the medical literature. Every one of those letters is going to be answered, either by a personal note, or by referral to FDA and other agencies which have power to inquire and to act. For Dr. Kelsey knows that the female of the species really is more deadly than the male when the female chooses to sting. And she remembers the decisive role that other women played in hanging that medal around her neck.

There was, first of all, the woman reader of SR who asked SR's science editor to compile a census of antibiotics, and so broke the case of Henry Welch. The Welch case brought Dr. Moulton off the family farm in West Virginia to throw her weight behind all-out reform in the drug laws. Following the feminine bent to seek advice from another female, Dr. Moulton went to Congresswoman LEONOR SULLIVAN of Missouri, who had been trying for 10 years to stir interest in a new law that would protect women from the chemical dangers of cosmetics and the mechanical perils of purportedly protective devices as well as from the hazards of unfamiliar drugs. Through Congresswoman SULLIVAN, Dr. Moulton reached the Kefauver committee in the Senate, where she teamed her talents as an outsider with two Government insiders of formidable talent: Dr. Irene Till, an economist noted for her association with the late Franklin D. Roosevelt's New Deal, and Mrs. Lucille Went, a patent attorney, one of the few persons anywhere who knows which chemical names fit the myriad trade names of drugs.

Knowing that Dr. Moulton had resigned the FDA post she now occupied, Dr. Kelsey attended the Kefauver drug hearings to hear her predecessor's testimony. In this way the two women met. They liked each other, and quickly became friends.

Dr. Moulton's formal contact on the Kefauver committee staff was Dr. Eppes Wayles Browne, Jr., who reports to Chief Staff Economist Dr. John Blair. In time, Drs. Moulton and Browne discovered they had other common interests than drugs. But courting was difficult because Dr. Browne was newly divorced and because hardly anyone outside the Kefauver committee was talking to Dr. Moulton at that point in time. Dr. Kelsey solved the problem by inviting the lovestruck pair to the Kelsey house for dinners and evenings of talk.

These evenings were as comforting to Dr. Kelsey as they were to her guests. For Dr. Kelsey had many moments of feeling rather alone after the Merrell application for thalidomide reached her FDA desk in September 1960. She recognized her own experiences as a parallel to the experiences Dr. Moulton had described on the witness stand, and she wondered whether she could escape Dr. Moulton's fate. At one point, when a Merrell representative questioned whether Dr. Kelsey had libeled Merrell, she sought legal advice.

She had her husband's support, of course, and it was much more than a husband usually can give. For as a pharmacologist, Dr. Ellis Kelsey could follow and confirm his wife's reasoning step by step. First the puzzling chemistry of the drug, then the unsatisfying tests on animals—none of which it put to sleep, then the discovery in England that habitual use of the drug brought peripheral paralysis to some people, and finally the awful truth about the malformed babies.

After the struggle was past and Merrell had withdrawn its application for permission to sell the drug commercially, Dr. Kelsey felt she had lived through a fairy tale. It was hard for her to believe that she, Frances Kelsey, had accurately predicted, on theoretical grounds, that because thalidomide caused paralysis of peripheral nerves in those who took the drug habitually, the drug probably would cause greater damage to the developing human embryo. Great scientists did such things. But "Frankie" Kelsey?

Most women who afterward read or heard about what she had done lacked the scientific background to appreciate her accomplishments. They really didn't care about the science of it; what mattered to them was the heartbreak of helpless babies. They were all for Dr. Kelsey. The male politicians of Washington did not at first understand this. They saw an aura of partisan politics around Senator KEFAUVER's proposal for a Presidential medal for Dr. Kelsey. And Dr. Kelsey's name was missing from the original White House list of those who were to receive the Distinguished Federal Civilian Service award.

At that point, a woman who grasped both the human and scientific implications decided to act. The aforementioned Mrs. Lucille Went, having left the Kefauver committee staff for a post on the Federal Trade Commission, risked crossing the party line of a Democratic administration in Washington and took the story to a Republican Senator from her home State, South Dakota: the Honorable KARL E. MUNDT. Mrs. Went pointed out to the Senator that Dr. Frances Kelsey and her family had lived in South Dakota for 8 years prior to moving to Washington, and that the Kelseys still maintained a home in Vermillion, S. Dak., as a voting address.

Senator MUNDT is not one to slight a worthy constituent of either political party. When Dr. Kelsey appeared before Senator HUMPHREY's Government Operations Subcommittee, Mr. MUNDT took over the stage to acknowledge South Dakota's particular debt to her. He lauded her as "friend to over 50,000 South Dakota residents" whom she had served as a family doctor: citizens of "Lemmon, in Perkins County; Faith, in Meade County; Philip, in Haakon County; Martin in Bennett County; Pierre, in Hughes County; Gregory and Burke, in Gregory County; Armour, in Douglas County; and Vermillion, in Clay County, the seat and the home of the University of South Dakota Medical School."

Before that hearing day was over, Dr. Kelsey's symbolic value was plain to the whole membership of Senator HUMPHREY's subcommittee, and Mr. HUMPHREY led the group in seconding Senator KEFAUVER's nomination of her for the Presidential medal.

As the New York Times has noted, Dr. Kelsey's triumph over a powerful drug house "points up the fact that all important Government decisions do not flow from plush offices with wall-to-wall carpeting." She works in a bare-floored room in a rickety barrack that has been temporary quartering for FDA since World War II; the walls are tattered with faded green paint; there are blinds but no curtains at the windows; desk and tables are piled with books and papers, in the manner of a place accustomed to long and intense concentration.

Entirely apart from her demonstration that science can fulfill—and thrill in the fulfilling

of—its social responsibility to a democratic people, many women will love Dr. Kelsey because of her personal candor. She admits she doesn't like housework. She would rather read or play tennis. She isn't a good cook (at least not in her own estimation), yet she cheerfully prepares the meals for the family and finds some pride in a relative lack of complaints of indigestion.

Dr. Kelsey has been a naturalized citizen of the United States since 1955. But she still betrays many signs of her birth on Vancouver Island, where the citizenry is more British than the British. She is altogether reserved, wears her hair short and straight and her heels broad and flat. Her faith in the goodness of people sometimes leads her into moments of naivete. However, like others who share her shyness, she can wreak havoc on those who expect either fear or gullibility.

Mr. DOUGLAS. Madam President, I urge Members of Congress and the people of the country to read those articles. I think they will confirm our opinion of the heroism not only of Dr. Kelsey but also of Dr. Barbara Moulton, who earlier protested against the way in which the drug section of the Food and Drug Administration was being maladministered under the direction of Mr. Larrick, and who was also very helpful in exposing some of the activities of Dr. Welch.

Dr. Moulton comes from a very distinguished family. Her father was Harold G. Moulton, who was for many years professor at the University of Chicago, and then for many years head of the Brookings Institution. Her uncle was the celebrated astronomer Forrest Moulton, who for many years was secretary of the American Association for the Advancement of Science.

Dr. Moulton is one of the unsung heroines in the whole battle because, exposed to heavy pressure from drug manufacturers and with little or no support from her superiors, she stood fast. The two articles indicate the need for a thorough housecleaning in the Food and Drug Administration. I believe the President should seriously consider whether or not Dr. Larrick and his assistants should be reappointed.

REVENUE ACT OF 1962

The Senate resumed the consideration of the bill (H.R. 10650) to amend the Internal Revenue Code of 1954 to provide a credit for investment in certain depreciable property, to eliminate certain defects and inequities, and for other purposes.

Mr. PROXMIRE. Madam President, it is my understanding that the Senate is about to adjourn. Before the Senate adjourns, I wish to say that this is one of the saddest days in the history of the Senate, in my judgment. The failure of the Douglas amendment was a real tragedy. It goes far beyond tax legislation because it relates to all legislation that comes before us. I think we should now be aware that what we have done in the tax bill is to provide special advantages to those persons and corporations that have a financial interest in the legislation. The advantage is perfectly enormous. It means that one-half the cost of lobbying legislation would be borne by the Federal Government if the lobbyists are large corporations. Of course, small

corporations would not have that advantage.

But the public interest and those who advocate the public interest, whether they are the Civil Liberties Union, the League of Women Voters, or Americans for Constitutional Reform, or any group that fights for their ideals would not have an equal opportunity or equal advantage. The administration directly opposed this lobbying provision. The House under a closed rule had no chance to vote on it. The Senate collapsed.

I intended to vote against the bill even before the Douglas amendment failed. Now I feel that it is important that all Senators give the most careful and thoughtful consideration to the action which was taken today especially the 36 Senators who failed to vote on the Doug-

las amendment. This has indeed been a tragic day for the U.S. Senate.

RUMORED INVITATION TO KHRUSHCHEV TO VISIT THE UNITED STATES

Mr. LAUSCHE. Madam President, word has been received that there is a movement in Ohio to invite Khrushchev to the United States, and especially to Ohio. I wish the RECORD to show that I do not approve of any such movement. I am sure that the people of Ohio do not approve it. I am certain that a visit by Khrushchev to the United States could not be of help to our country. It would only give further encouragement and cause trouble to us on all shores and in many spots of the world.

ENROLLED BILL PRESENTED

The Secretary of the Senate reported that on today, September 4, 1962, he presented to the President of the United States the enrolled bill (S. 476) to establish the Point Reyes National Seashore in the State of California, and for other purposes.

ADJOURNMENT UNTIL 10 O'CLOCK TOMORROW MORNING

Mr. KERR. Madam President, I move that the Senate stand in adjournment until 10 o'clock tomorrow morning.

The motion was agreed to; and (at 5 o'clock and 36 minutes p.m.) the Senate adjourned until tomorrow, Wednesday, September 5, 1962, at 10 o'clock a.m.

Digest of CONGRESSIONAL PROCEEDINGS

OF INTEREST TO THE DEPARTMENT OF AGRICULTURE

OFFICE OF
BUDGET AND FINANCE

(For information only;
should not be quoted
or cited)

Issued Sept. 6, 1962
For actions of Sept. 5, 1962
87th-2d, No. 159

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HIGHLIGHTS: Senate committee voted to report bills for revised apportionment of school lunch and extension work funds, expanded forestry research, land development program in Alaska, and cooperation with States in administration of agricultural laws. Senate committee reported roads bill. Sen. Neuberger urged removal of Jones Act restrictions on lumber shipments to Puerto Rico. Sen. Humphrey urged discontinuance of administrative budget.

SENATE

- 1. AGRICULTURE AND FORESTRY COMMITTEE.** The Agriculture and Forestry Committee voted to report (but did not actually report) without amendment S. 2805, to provide for a program of agricultural land development in Alaska; S. 3589, authorizing acquisition of certain lands in Wright County, Minn., for exchange for State-owned lands in Superior National Forest; S. 3475, to provide further cooperation with the States in the administration and enforcement of certain Federal laws; H. R. 9728, authorizing an increase from \$2.5 million to \$5 million in the annual appropriation under the Cooperative Forest Management Act; H. R. 12589, to revise the formula for the distribution of Federal funds for agricultural extension work; with amendment H. R. 12688, authorizing cooperation with and encouragement of the States in carrying out programs of forestry research; and H. R. 11665, to revise the formula for the apportionment among the States of funds under the National School Lunch Act. p. D808
- 2. INTERIOR AND INSULAR AFFAIRS COMMITTEE.** The Interior and Insular Affairs Committee voted to report (but did not actually report) S. 3335, changing the name of Big Hole Battlefield National Monument to Big Hole National Battle-

field, and acquiring additional land therefor (amended); S. 3530, authorizing acquisition of land along the Delaware River for the creation of Tocks Island National Recreation Area (amended); S. 3160, to amend the act concerning homestead entry on land containing coal, oil, and gas so as to extend its provisions to the townsite laws applicable in Alaska (amended); S. J. Res. 136, to determine the susceptibility of minerals to electrometallurgical processes (amended); H. R. 9280, to give the Secretary of the Interior discretionary authority to sell certain mineral and vegetative materials on public lands by negotiation rather than by competitive bid when in the best interest of the Government; H. R. 10540, to make deposits of petrified wood disposable under the Materials Act; and H. R. 11164, to approve an amendatory repayment contract negotiated with the Quincy Columbia Basis Irrigation District. p. D809

3. ROADS. The Public Works Committee reported with amendments H. R. 12135, the proposed Federal-Aid Highway Act of 1962, which includes authorizations for forest highways and forest development roads and trails (S. Rept. 1997). p. 17425
4. FORESTRY. Sen. Neuberger stated that no domestic lumber is now being shipped to Puerto Rico because of certain restrictions of the Jones Act and that she intended to propose an amendment to the foreign trade bill to permit the Secretary of Commerce to waive Jones Act requirements with respect to such lumber shipments to Puerto Rico. p. 17427
5. BUDGET. Sen. Humphrey urged that the present administrative budget be replaced by two budgets, "the current budget covered by current revenues, and the capital budget financed largely by borrowings backed up by capital assets and by earnings from these projects," and stated that "until we scrap the obsolete accounting procedures of the Federal administrative budget, we will be unable to create the dynamism which one has a right to expect from the leader of the free world." pp. 17557-8
6. TAXATION. Continued debate on H. R. 10650, the proposed Revenue Act of 1962 (pp. 17425-5, 17440-556). Agreed to a unanimous-consent agreement that, effective Thurs., Sept. 6, further debate on the bill will be limited to four hours (p. 17516). Sen. McCarthy inserted a statement to clarify the tax status of farmers' cooperatives after Sen. Kerr assured him that "I have a positive conviction that nothing in the bill would lose to a cooperative any tax-exempt status it now has under existing law" (p. 17551).
7. RECLAMATION. The Interior and Insular Affairs Committee reported without amendment H. R. 575, to authorize construction of the upper division of the Baker reclamation project, Ore. (S. Rept. 1996). p. 17425
8. APPROPRIATIONS. The "Daily Digest" states that a subcommittee of the Appropriations Committee "marked up and agreed to report to the Subcommittee on Public Works proposed funds for the Atomic Energy Commission and the Tennessee Valley Authority embodied in H. R. 12900, fiscal 1963 appropriations for public works p. D808
9. FOREIGN TRADE. Sen. Neuberger submitted an amendment intended to be proposed to H. R. 11970, the foreign trade bill. p. 17425
10. FORESTRY; NATURAL RESOURCES. Sen. Morse inserted his speech at the Western States Democratic Conference at Seattle, Wash., on Aug. 5, in which he discusses legislation relating to forestry, natural resource development, and other subjects. pp. 17569-70

EXECUTIVE COMMUNICATIONS, ETC.

The ACTING PRESIDENT pro tempore laid before the Senate the following letters, which were referred as indicated:

REPORTS ON RESERVE COMPONENTS CONSTRUCTION AUTHORIZATION PROGRAM

A letter from the Deputy Assistant Secretary of Defense (Properties and Installations), transmitting, pursuant to law, reports on the location, nature, and estimated cost of facilities projects proposed to be undertaken for the respective Reserve components of the Armed Forces (with accompanying reports); to the Committee on Armed Services.

REPORT ON DEPARTMENT OF DEFENSE PRIME CONTRACT AWARDS TO SMALL AND OTHER BUSINESS FIRMS

A letter from the Acting Assistant Secretary of Defense (Installations and Logistics), transmitting, pursuant to law, a report on Department of Defense prime contract awards to small and other business firms, for the fiscal year 1962 (with an accompanying report); to the Committee on Banking and Currency.

SUSPENSION OF DEPORTATION OF CERTAIN ALIENS

Two letters from the Commissioner, Immigration and Naturalization Service, Department of Justice, transmitting, pursuant to law, copies of orders suspending deportation of certain aliens, together with a statement of the facts and pertinent provisions of law pertaining to each alien, and the reasons for ordering such suspension (with accompanying papers); to the Committee on the Judiciary.

REPORTS OF COMMITTEES

The following reports of committees were submitted:

By Mr. JACKSON, from the Committee on Interior and Insular Affairs, without amendment:

H.R. 575. An act to authorize the Secretary of the Interior to construct, operate, and maintain the upper division of the Baker Federal reclamation project, Oregon, and for other purposes (Rept. No. 1996).

By Mr. CHAVEZ, from the Committee on Public Works, with amendments:

H.R. 12135. An act to authorize appropriations for the fiscal years 1964 and 1965 for the construction of certain highways in accordance with title 23 of the United States Code, and for other purposes (Rept. No. 1997).

Mr. MANSFIELD. Mr. President, I ask unanimous consent that a statement prepared by the Senator from New Mexico [Mr. CHAVEZ] relating to the bill (H.R. 12135), just reported by him, be printed in the RECORD.

There being no objection, the statement was ordered to be printed in the RECORD, as follows:

STATEMENT BY SENATOR CHAVEZ

This bill authorizes a continuation of the Federal-aid highway program for the regular systems for the fiscal years 1964 and 1965. It also authorizes additional amounts for roads on Federal lands for those years, and additional funds for completion of the Inter-American Highway and the Rama Road.

The bill also provides for payment of relocation assistance to families and businesses

displaced by Federal-aid highway construction.

On April 5, 1962, the President sent to Congress his message on the transportation system of the Nation. This message contained several important recommendations as to the role of highways in our transportation system.

On April 6, 1962, the Secretary of Commerce submitted to the Congress a draft of proposed legislation to implement the recommendations of the President concerning Federal-aid highway legislation.

H.R. 12135 follows very closely the recommendations of the Secretary of Commerce on Federal-aid legislation.

The bill authorizes \$950 million for each of fiscal years 1964 and 1965 for the regular A-B-C systems.

It authorizes funds for roads for administration, development, utilization, and protection of our public lands and reservations, at slightly increased amounts over previous years. These amounts are believed necessary for proper development of our natural resources, and to take care of the increased use of our forests, parks, and public lands.

It authorizes the use of secondary highway funds on urban extensions of the secondary system, transportation planning in urban areas, and for highway planning and research.

The committee believes that the provisions of H.R. 12135 will keep our A-B-C highway program in balance with the other highway programs, to meet the needs of present traffic, and will go a long way toward meeting the recommendations of the President on transportation and Federal-aid highways.

BILLS INTRODUCED

Bills were introduced, read the first time, and, by unanimous consent, the second time, and referred as follows:

By Mr. SMITH of Massachusetts:

S. 3693. A bill for the relief of Emilia Suppa; to the Committee on the Judiciary.

By Mr. LONG of Missouri:

S. 3694. A bill for the relief of Dr. Dunet Francois Belancourt; to the Committee on the Judiciary.

By Mr. HUMPHREY:

S. 3695. A bill for the relief of the Standard Spring Co.; to the Committee on the Judiciary.

By Mr. CLARK:

S. 3696. A bill for the relief of Nicolas Louvaris; to the Committee on the Judiciary.

TRADE EXPANSION ACT OF 1962— AMENDMENT

Mrs. NEUBERGER. Mr. President, I submit an amendment, intended to be proposed by me, to the bill (H.R. 11970) to promote the general welfare, foreign policy, and security of the United States through international trade agreements and through adjustment assistance to domestic industry, agriculture, and labor, and for other purposes, and ask that it be printed and appropriately referred. I ask unanimous consent that the amendment be held at the desk for 5 days to receive signatures of additional cosponsors.

The ACTING PRESIDENT pro tempore. The amendment will be received, printed, and referred to the Committee on Finance; and, without objection, the amendment will be held at the desk, as requested by the Senator from Oregon.

NOTICE OF HEARING ON NOMINATION OF WALTER C. SAUER, OF THE DISTRICT OF COLUMBIA, TO BE FIRST VICE PRESIDENT OF THE EXPORT-IMPORT BANK OF WASHINGTON

Mr. ROBERTSON. Mr. President, as chairman of the Committee on Banking and Currency, I wish to give notice that a public hearing has been scheduled for Friday, September 7, at 10 a.m., in room 5302, New Senate Office Building, on the nomination of Walter C. Sauer, of the District of Columbia, to be First Vice President of the Export-Import Bank of Washington, vice Tom Killefer.

All persons who wish to appear and testify on this nomination are requested to notify Mr. Matthew Hale, chief of staff, Senate Committee on Banking and Currency, room 5300, New Senate Office Building, telephone Capitol 4-3121, extension 3921.

ADDRESSES, EDITORIALS, ARTICLES, ETC., PRINTED IN THE APPENDIX

On request, and by unanimous consent, addresses, editorials, articles, etc., were ordered to be printed in the Appendix, as follows:

By Mr. WILEY:

Excerpts from address prepared by him for delivery over Wisconsin radio stations on the weekend of September 1-2, 1962, on the subject of "Major U.S. Economic Goals."

Article by Justin Schmiedeke, public information director, Wisconsin State Historical Society, dealing with the mobile museum traveling throughout the State featuring subjects of major significance to Wisconsin's history.

By Mr. HUMPHREY:

Editorial entitled "Canadian Competition," published in the Minneapolis Morning Tribune of August 15, 1962, dealing with quotas and tariffs on lumber imports from Canada.

By Mrs. NEUBERGER:

Article entitled "A Complicated Maze Puzzles the Consumer," written by David Hamilton and published in the September 1962 issue of Frontier magazine, dealing with various consumer protection proposals.

By Mr. SCOTT:

Sundry newspaper articles dealing with the Berlin situation and the visit of President de Gaulle of France to West Germany.

Mr. MANSFIELD. Mr. President, is there any further morning business?

The ACTING PRESIDENT pro tempore. Is there any further morning business? If not, morning business is closed.

REVENUE ACT OF 1962

Mr. MANSFIELD. Mr. President, I move that the unfinished business be laid before the Senate and be made the pending business.

The motion was agreed to; and the Senate resumed the consideration of the bill (H.R. 10650) to amend the Internal Revenue Code of 1954 to provide a credit for investment in certain depreciable property, to eliminate certain defects and inequities, and for other purposes.

The ACTING PRESIDENT pro tempore. The bill is open to further amendment.

Mr. MANSFIELD. Mr. President, I suggest the absence of a quorum.

The ACTING PRESIDENT pro tempore. The clerk will call the roll.

The Chief Clerk proceeded to call the roll.

Mr. MANSFIELD. Mr. President, I ask unanimous consent that the order for the quorum call be rescinded.

The ACTING PRESIDENT pro tempore. Without objection, it is so ordered.

Mr. DIRKSEN. Mr. President, I submit an amendment, and send it to the desk.

The ACTING PRESIDENT pro tempore. The amendment will be stated.

The LEGISLATIVE CLERK. On page 391, between lines 21 and 22, it is proposed to insert a new section 127.

Mr. DIRKSEN. Mr. President, I ask that the further reading of the amendment be dispensed with.

The ACTING PRESIDENT pro tempore. Without objection, it is so ordered; and the amendment will be printed in the RECORD.

The amendment submitted by Mr. DIRKSEN is as follows:

On page 391, between lines 21 and 22, insert the following new section:

"SEC. 127. AMENDMENT TO TITLE I OF THE SOCIAL SECURITY ACT RELATING TO STATEMENT OF FINANCIAL STATUS OF CLAIMANTS FOR MEDICAL ASSISTANCE FOR THE AGED.

"Paragraph (11) of section 2(a) of the Social Security Act is amended (1) by striking out 'and' at the end of clause (D), (2) by striking out the period at the end of clause (E), and (3) by adding after clause (E) the following new clause:

"(F) prior to October 1, 1963, may, and on and after such date, shall, provide that any statement required of a claimant for medical assistance for the aged, if made in writing and signed by the claimant, shall, insofar as such statement relates to the financial status of such claimant, be presumed by such State agency to be factually correct for purposes of determining his eligibility for such assistance."

On page 391, line 22, strike out "27" and insert in lieu thereof "28".

TAX-REDUCTION VIEWS OF CHAMBER OF COMMERCE OF THE UNITED STATES

Mrs. NEUBERGER. Mr. President, on July 23 I had printed in the CONGRESSIONAL RECORD a statement by the Chamber of Commerce of the United States which set forth in detail the chamber's view that taxes should be reduced promptly. Although the statement was most explicit, I noted one portion lacking substantiation. That statement read:

Another implication of the problem of high tax rates is that every needless public expenditure should be eliminated. As of now, approximately 20 percent of our gross national product is required to keep the Federal Government running. Since we must continue to meet every demand which the cold war imposes, all other types of expenditures must be scrutinized rigorously to meet the highest standard of the public interest.

Of course, I concur with much of what was said in this statement, as do most Senators. I am certain that all Senators feel that "every needless public expenditure should be eliminated." We would be remiss in our duties if we knowingly voted large expenditures which were unneeded. Therefore, I think that Senators who vote for the appropriation of sums which the chamber might call "needless" must only disagree with what can be considered the "highest standard of the public interest."

In seeking to understand what the chamber of commerce might consider the "public interest," I wrote Mr. Ladd Plumley, president of the chamber of commerce, and asked for a specific statement of what expenditures the chamber thought constituted "needless" public expenditures.

The chamber responded with a large notebook crammed with copies of the many letters the chamber has written urging their specific point upon the many chairmen of appropriation subcommittees of both Houses. Included were copies of testimony by the chamber before congressional committees, urging budget reductions.

I noted a summary of recommendations, with small comments on the chamber's position on each. But, after much searching, I came to the sad conclusion that the chamber had failed in many instances to provide any detailed explanation, beyond this small summary, of a recommended reduction. For example, I was immediately struck by the note attached to the recommendation of a \$105 million reduction in the special milk fund which would result in the termination of this program. In explaining the chamber's reasons for urging this reduction, they state:

Federal funds should not be appropriated for this program as it is the responsibility of the States.

This statement constitutes the complete explanation of the chamber's feeling on this program. Yet I would have appreciated a comment which would explain in more detail why the program is considered a waste when it does much to help reduce surpluses in milk and actually provides the Government with a means of insuring our children an inexpensive supplement to their diet. I also would have appreciated a recommendation for the establishment of an equally effective program at the State level.

I was even more dismayed to discover that the chamber would recommend a \$108 million decrease in the amounts appropriated to the school lunch program, a program which provided 2,470,400,000 meals to 13.5 million needy children last year. Their reduction is recommended with this justification:

The portion of this appropriation used for cash payments to the States is opposed as an unnecessary Federal school subsidy.

To further complicate the oft-stated view that \$5 billion can be cut from the fiscal 1963 Federal budget, the chamber has recommended the elimination of more than a half billion dollars in aid

to education funds which have not yet been authorized by the Congress. They recommend the elimination of the \$600 million proposed for general aid to public schools, and the elimination of the \$29 million that will be spent if the conference committee recommends passage of an aid to higher education bill with the provisions of the Federal scholarship program intact. Of course, I and many other Senators find aid to education in the "public interest." We voted for the higher education bill because of our concern that, under existing programs, we may not be meeting the tremendous needs of our exploding school age population.

In further examination of the reductions recommended by the chamber in expenditures of the Department of Health, Education, and Welfare, I noted that the chamber favored a \$5.6 million reduction in the budget request of the Food and Drug Administration. Of course, this request was made in March before the public was informed of FDA's role in preventing the use of thalidomide, but it still did not answer many arguments that are being made for the need to expand the Food and Drug Administration so that it can keep pace with the mounting complexities of food and drug proposals.

I have mentioned many of the smaller programs of the Federal Government which are considered by the chamber to be "needless" in whole or part. I think that other Senators would probably wonder, as I did, what sort of recommendations the chamber of commerce made for reduction of needless expenditures in the Department of Agriculture and the Department of Defense, the two areas where the greatest amount of Federal funds are spent.

When I examined the Department of Agriculture, however, I began to see the pattern of the chamber's budget philosophy. I have already mentioned the special milk program which it opposed, and the school lunch program which the chamber felt should be reduced. These programs represent a proposed expenditure of only \$275 million of the approximately \$6 billion that will be appropriated for the activities of the Department of Agriculture. Yet the reduction of \$213 million in the budget of these two minor but important activities would amount to almost half of the \$505 million reduction proposed by the chamber of commerce.

Further, the chamber would favor the reduction of approximately \$60 million in the program for the removal of surplus agricultural commodities. With the ever-mounting cost of commodity storage that results from our increasing productivity, I would have thought that the chamber would approve of programs designed to reduce the immense agricultural surpluses so that we could lower the cost of the vast price support and crop storage programs.

I must confess that I found the recommendations of the chamber of commerce rather disappointing. It seems that the chamber has been acting a lot like the

ity, and the guarantee of collective bargaining in the Wagner Act.

When Justice Cardozo died in 1938, Frankfurter was widely regarded as his appropriate successor, as Cardozo had been the rightful inheritor of the place left by Holmes in 1932.

Two appointments had already been made to the Court by Roosevelt, that of Hugo Black to succeed Justice Van Devanter in 1937, and of Stanley Reed to succeed Justice Sutherland in 1938. Frankfurter's appointment was urged by the faculties of leading law schools as well as by members of the bar.

A poll conducted in the autumn of 1938 showed that he was the choice of five times as many lawyers as any other individual, although two-thirds of those voting were anti-Roosevelt.

He was nominated on January 5, 1939, confirmed 12 days later, and took his seat on January 30.

While the nomination was pending in the Senate Judiciary Committee, he was invited to appear before the committee and he did so, though expressing regret that the committee was departing from an almost unbroken practice of refraining from summoning a Supreme Court nominee.

"While I believe that a nominee's record should be thoroughly scrutinized by this committee," Frankfurter said, "I hope you will not think it presumptuous on my part to suggest that neither such examination nor the best interests of the Supreme Court will be helped by the personal participation of the nominee himself."

"I should think it improper for a nominee no less than for a member of the Court to express his personal views on controversial issues affecting the Court. My attitude and outlook have been fully expressed over a period of years and are easily accessible."

"I should think it not only bad taste but inconsistent with the duties of the office for which I have been nominated for me to attempt to supplement my past record by present declarations."

Despite these animadversions, the precedent set in the hearings on Frankfurter has been adhered to by the committee in considering more recent nominations to the High Court.

On the Court, Justice Frankfurter sought to avoid extreme positions. In many cases he was in disagreement with Justices Black and Douglas, who were joined in late years by Chief Justice Warren and Justice Brennan.

Critics have argued that Frankfurter weakened in his attachment to the principles of civil liberty. The answer contained in his opinions is that for a judge, the issues are more complex than the critics acknowledge.

On questions of fair procedure, due process of law in the primary sense, Justice Frankfurter remained insistent on the observance of civilized standards by prosecutors and judges.

He did not hesitate, for example, to reverse convictions obtained in the Federal courts through illegal searches and seizures, wire-tapping, or confessions obtained during a period of unlawful detention of the accused.

Over these abuses, he believed, the Supreme Court rightly exercised wide supervisory control. But he was more hesitant about applying the identical standards to the States as a matter of constitutional law, however much he personally deprecated these practices.

Similarly, he refused to apply his own judgments of sound legislative policy to invalidate statutes on constitutional grounds.

Though much of the legislation affecting rights of speech and association in the name of internal security was offensive to him, he insisted that a judicial judgment must

be divorced from such considerations and must consider only whether the law had passed the bounds of reason or had violated a specific prohibition in the Constitution.

This judicial philosophy was poignantly expressed in the Flag-Salute case of 1943.

Members of the sect of Jehovah's Witnesses had been required to join in the traditional flag-salute ceremony in the public schools despite their religious conviction that to do so was an act of profanation.

The Supreme Court ruled that the requirement was unconstitutional.

Frankfurter, however, delivered a dissenting opinion which began with this self-revealing passage:

"One who belongs to the most vilified and persecuted minority in history is not likely to be insensible to the freedoms guaranteed by our Constitution."

"Were my purely personal attitude relevant, I should wholeheartedly associate myself with the general libertarian views in the Court's opinion, representing as they do the thought and action of a lifetime."

"But as judges, we are neither Jew nor Gentile, neither Catholic nor agnostic. * * * As a member of this Court I am not justified in writing my private notions of policy into the Constitution, no matter how deeply I may cherish them or how mischievous I may deem their disregard."

In appreciation of this judicial philosophy, Judge Learned Hand wrote concerning Justice Frankfurter, on the latter's 76th birthday: "I regard him at the moment as the most important single figure in our whole judicial system."

On occasion Justice Frankfurter was prepared to find that State action had passed the limits of tolerance under the Bill of Rights. Thus, he joined in the decision up-setting released-time programs for religious education carried on in the public schools, and he wrote the Court's opinion ruling that Michigan could not prevent all sales of books that might corrupt the minds of children.

In 1957 he wrote a separate concurring opinion in the case of *Sweezy v. New Hampshire* in which the Court held that the State attorney general lacked authority to question a university lecturer about the contents of a classroom lecture.

Justice Frankfurter voiced his concern for academic freedom when threatened by governmental intrusion:

"These pages need not be burdened with proof, based on the testimony of a cloud of impressive witnesses, of the dependence of a free society on free universities. This means the exclusion of governmental intervention in the intellectual life of a university."

"It matters little whether such intervention occurs avowedly or through action that inevitably tends to check the ardor and fearlessness of scholars, qualities at once so fragile and so indispensable for fruitful academic labor."

Justice Frankfurter was able to differentiate the *Sweezy* case when he was faced in 1959 with the conviction of Lloyd Barenblatt, a college instructor, for contempt of the House Un-American Activities Committee in refusing to answer questions concerning his membership in the Communist Party.

Justice Frankfurter allied himself with a five-man majority to uphold the conviction, believing that actual Communist membership was a subject into which government might inquire, even in the case of a teacher.

Frequently delivering a separate concurring opinion to sharpen the meaning of a decision, Justice Frankfurter regretted that the pressure of the Court's docket did not permit the writing of individual opinions in every case, as is the practice in the British House of Lords.

Highly articulate and sensitive to the

shadings of language, he took great pains in the composition of his opinions. Of his literary style, Archibald MacLeish, writing in 1939, said:

"Few scholars and fewer scholars of the law, have written a more natural, more lucid or more readable English than Mr. Frankfurter writes at his best."

Justice Frankfurter is fond of saying that his best literary critic is his wife, the former Marian A. Denman, whom he married in 1919.

A warm admirer of English justice and English literature, Justice Frankfurter has maintained close ties with judges, scholars, and journalists in that country.

More than any other member of the Court, he has embellished his opinions with references to the law of England and the British Commonwealth. He is a regular reader of English newspapers and learned periodicals; the air edition of the London Times is supplied to him each day by the Library of Congress before it is filed.

He spent the academic year 1933-34 as Eastman visiting professor at Oxford, and in 1939 received an honorary doctorate of laws from that university.

The range of Justice Frankfurter's friendships reflected the catholicity of his interests and the warmth of his nature.

A volume of essays by the justice, published in 1956 under the title "Of Law and Men," contains such diverse figures as Alfred E. Smith and Alfred North Whitehead, Harold J. Laski and Lord Lothian, John Dewey and Thomas Mann.

When Justice Brandeis was asked on his retirement whether he planned to write his memoirs, he replied, "I think you will find that my memoirs have already been written."

In a sense the same could be said of Justice Frankfurter, but those who know the liveliness and richness of his mind will be looking forward to some new and exciting chapters.

[From the Washington Post, Aug. 31, 1962]

FRANKFURTER'S GIFT TO LAW

Justice Felix Frankfurter's contribution to American life and law cannot be adequately measured in these columns. Like his great predecessor, Justice Oliver Wendell Holmes, Mr. Frankfurter and his philosophy and judicial decisions will be a fruitful subject for judges, authors, and commentators for many years to come. Out of this intellectual churning of his ideas will emerge a clearer view of his standing among the great jurists of our history. It is possible, however, as he goes into retirement, to appraise some of the qualities of his mind and thus to give a better understanding of the void that his departure leaves on the bench.

Probably the most significant thing about him is the breadth of his intellectual interests. It has not been possible to fit Mr. Frankfurter into a narrow groove or to identify him with any "ism," "interest," cult or predilection. On one occasion he expressed the view that a judge "should be compounded of the historian and the philosopher and the prophet," and this has been the aim of his own endeavor.

He has recognized that judges are men, "not disembodied spirits." But this does not mean that all men are fit to be judges—far from it. Recognizing that the judge needs something of the creative artist in him, he has cultivated acquaintance, as Judge Learned Hand advised, with Acton and Maitland, with Thucydides, Gibbon and Carlyle, with Homer, Dante, Shakespeare, Milton and many others. Knowing that decisions on the bench will reflect "the totality of a man's nature and experience," he has insisted on

enriching the resources on which his judgment could draw.

Despite his generous measure of self-confidence, Justice Frankfurter has never supposed that he was elevated to the Supreme Bench to weave his own superior wisdom into the law of the land. Rather, he has sought to make his conclusions reflect understanding of, and due regard for, law as the expression of the views and feelings that may fairly be deemed representative of the community as a continuing society." He has recognized a duty to emancipate his conclusions as a judge from his personal prejudices and desires.

It would be foolish, of course, to assume that Mr. Frankfurter or any other judge has attained complete objectivity. But he must be credited with a mighty struggle in that direction. As one who deeply loves the Supreme Court and who deeply believes in its function as the balance wheel of our democratic system, he has sought to emulate the best judicial tradition of the Court. "A judge worth his salt," he has often said, "is in the grip of his function." As a dedicated instrument of justice on a national scale, he naturally gravitated toward soul searching and disinterestedness.

The retiring Justice has also been keenly aware of the complicated nature of the problems that are laid before the Supreme Court. Most of the cases reaching the Court of last resort are highly controversial and some of them involve more than one basic constitutional principle. In situations of this kind Justice Frankfurter has insisted on looking at the whole complex and not at merely an oversimplified part of it. One may quarrel with some of his conclusions in specific cases, but it is difficult to take exception to his insistence that the judicial process requires reconciliation of these conflicting claims in the light of the whole Constitution, the nature of our system, the experience of nearly two centuries and previous decisions of the Court.

When the work of Justice Frankfurter can be seen in greater perspective, his sense of historic continuity is likely to command greater appreciation than it does today. Some of his critics accused him of shifting, with the advance of the years, from liberalism to conservatism. In part this seeming evolution is attributable to changes in the orientation of the Court as a whole. In part it is also due to changes in the concept of liberalism on the Bench. What used to be called liberalism was the disposition of Holmes, Brandeis, Stone and others to give Congress a free hand in legislating so long as it did not patently overstep its powers. Now liberalism is often equated with the policy of restricting congressional power for the attainment of greater individual liberty.

Actually Justice Frankfurter has followed the Holmes tradition with a large measure of consistency. When unwilling to go as far as some of his brethren in upholding claimed rights, it was because he saw the long-range necessity of preserving governmental power to serve the public welfare. The interests of both stability and adaptation to new conditions must be served. The Justice is fond of quoting Alfred North Whitehead to the effect that "those societies which cannot combine reverence to their symbols with freedom of revision, must ultimately decay either from anarchy, or from the slow atrophy of a life stifled by useless shadows."

Justice Frankfurter's service has been dedicated to the idea that the United States can use the principles that have proved trustworthy in the past as a guide to changes that need to be effected in the present and future. With all his emphasis on judicial restraint, he has never had a static approach to the momentous business of judging. Now that he will be seeking well-earned rest the

country will be keenly aware of its need for new jurists of his stature, of his historic perspective and of his largeness of spirit.

Mr. MANSFIELD. Mr. President, I suggest the absence of a quorum.

The ACTING PRESIDENT pro tempore. The clerk will call the roll.

The legislative clerk called the roll, and the following Senators answered to their names:

[No. 240 Leg.]

Aiken	Hickenlooper	Scott
Bartlett	Hill	Smith, Maine
Bush	Hruska	Sparkman
Byrd, Va.	Keating	Stennis
Cannon	Kerr	Thurmond
Carlson	Lausche	Tower
Dirksen	Mansfield	Wiley
Ervin	Monroney	Williams, Del.
Fulbright	Morse	Young, N. Dak.
Gore	Neuberger	Young, Ohio
Hartke	Pearson	
Hayden	Saltonstall	

Mr. MANSFIELD. I announce that the Senator from Mississippi [Mr. EASTLAND], the Senator from Alaska [Mr. GRUENING], the Senator from Minnesota [Mr. HUMPHREY], and the Senator from Washington [Mr. MAGNUSON] are absent on official business.

I further announce that the Senator from New Mexico [Mr. ANDERSON], the Senator from Nevada [Mr. BIBLE], the Senator from Wyoming [Mr. HICKEY], and the Senator from Missouri [Mr. SYMINGTON] are necessarily absent.

Mr. KUCHEL. I announce that the Senator from Utah [Mr. BENNETT], the Senator from South Dakota [Mr. BORUM], the Senator from Indiana [Mr. CAPEHART], the Senator from Arizona [Mr. GOLDWATER], the Senator from Kentucky [Mr. MORTON], and the Senator from New Hampshire [Mr. MURPHY] are necessarily absent.

The ACTING PRESIDENT pro tempore. A quorum is not present.

Mr. MANSFIELD. Mr. President, I move that the Sergeant at Arms be directed to request the presence of absent Senators.

The ACTING PRESIDENT pro tempore. The question is on agreeing to the motion of the Senator from Montana.

The motion was agreed to.

The ACTING PRESIDENT pro tempore. The Sergeant at Arms will carry out the order of the Senate.

After a little delay Mr. ALLOTT, Mr. BEALL, Mr. BOGGS, Mr. BURDICK, Mr. BUTLER, Mr. BYRD of West Virginia, Mr. CARROLL, Mr. CASE, Mr. CHAVEZ, Mr. CHURCH, Mr. CLARK, Mr. COOPER, Mr. COTTON, Mr. CURTIS, Mr. DODD, Mr. DOUGLAS, Mr. ELLENDER, Mr. ENGLE, Mr. FONG, Mr. HART, Mr. HOLLAND, Mr. JACKSON, Mr. JAVITS, Mr. JOHNSTON, Mr. JORDAN of North Carolina, Mr. JORDAN of Idaho, Mr. KEFAUVER, Mr. KUCHEL, Mr. LONG of Missouri, Mr. LONG of Hawaii, Mr. LONG of Louisiana, Mr. MCCARTHY, Mr. McCLELLAN, Mr. McGEE, Mr. McNAMARA, Mr. METCALF, Mr. MILLER, Mr. MOSS, Mr. MUNDT, Mr. MUSKIE, Mr. PASTORE, Mr. PELL, Mr. PROUTY, Mr. PROXMIER, Mr. RANDOLPH, Mr. ROBERTSON, Mr. RUSSELL, Mr. SMATHERS, Mr. SMITH of Massachusetts, Mr. TALMADGE, Mr. WILLIAMS of New Jersey, and Mr. YARBOROUGH entered the Chamber and answered to their names.

The PRESIDING OFFICER (Mr. PELL in the chair). A quorum is present.

REVENUE ACT OF 1962

The Senate resumed the consideration of the bill (H.R. 10650) to amend the Internal Revenue Code of 1954 to provide a credit for investment in certain depreciable property, to eliminate certain defects and inequities, and for other purposes.

Mr. DIRKSEN. Mr. President, when the Senate had under consideration the so-called social security amendments, to which there was offered the Anderson-Javits proposal, copious tears were shed in this Chamber over the alleged fact that our senior citizens were compelled to take a so-called pauper's oath to secure benefits under the Kerr-Mills Act.

I made mention at that time that no Senator stood in his place in the Senate and offered a proposal to amend existing law in order to cure that difficulty if it actually was a difficulty. I saw no one stand in his place and offer an amendment to the Kerr-Mills Act with respect to what was called the pauper's oath.

Mr. KERR. Mr. President, will the Senator yield?

Mr. DIRKSEN. I yield.

Mr. KERR. I ask unanimous consent that Mr. Fred Arner, of the Legislative Reference Service, a technician on social security legislation, be permitted to sit with me in the consideration of this amendment.

The PRESIDING OFFICER. Without objection, it is so ordered.

Mr. DIRKSEN. I determined then that before the end of the session I was going to offer some language that would wholly or in part cure what was the alleged difficulty. It is never easy to contrive language which will retain the spirit of the Kerr-Mills Act and still effectuate what one has in mind.

However, I have submitted an amendment this morning, which is permissive in character. It amends the Social Security Act in the proper place to this effect, in adding another criterion that is spelled out in the law. It says:

On page 391, between lines 21 and 22, it is proposed to insert the following new section:

"SEC. 127. AMENDMENT TO TITLE I OF THE SOCIAL SECURITY ACT RELATING TO STATEMENT OF FINANCIAL STATUS OF CLAIMANTS FOR MEDICAL ASSISTANCE FOR THE AGED.

"Paragraph (11) of section 2(a) of the Social Security Act is amended (1) by striking out 'and' and at the end of clause (D), (2) by striking out the period at the end of clause (E), and (3) by adding after clause (E) the following new clause:

"(F) provide that any statement required of a claimant for medical assistance for the aged, if made in writing and signed by the claimant, shall, insofar as such statement relates to the financial status of such claimant, be presumed by such State agency to be factually correct for purposes of determining his eligibility for such assistance."

On page 391, line 22, strike out "27" and insert in lieu thereof "28".

Mr. President, as the amendment was originally drawn, it included the word "shall," which would have made the provision mandatory. But after conferring

on the amendment, and in order to preserve the Federal-State spirit of the Kerr-Mills Act, I have modified the amendment to make it permissive. So it would be up to the States to do exactly what I have in mind; and if anyone should quarrel about what his State does with respect to the requirement of an oath that in effect must affirm the indigence of the claimant in question, that is a question for the State to determine. Certainly the State will still qualify under the Federal act to make it permissive.

In connection with this whole subject, I recall that not only was the pauper's oath so generously ventilated on the floor, but so many other things in connection with medicare were advanced, that I made the statement then that, in my judgment, neither the Federal nor the State authorities had undertaken any real effort or had diligently set themselves to the business of selling to the people what was available to them under the Kerr-Mills Act. Since that time, I have caused to be prepared a pamphlet on the subject.

Mr. President, I ask unanimous consent that in the form in which it is printed be made a part of the RECORD.

There being no objection, the pamphlet was ordered to be printed in the RECORD, as follows:

**ARE YOU OVER 65?—ILLINOIS HAS MEDICARE—
YOU ARE ENTITLED TO MEDICAL CARE**

You are eligible for medicare in Illinois if you (1) are 65 or over, (2) a permanent resident, (3) have yearly income not over \$1,800—if an individual or \$2,400—if married couple, (4) own assets under \$2,400 (not counting home), (5) need major medical care.

Apply: Illinois Public Aid Commission, at your county seat.

FIRST 11 MONTHS ILLINOIS MEDICARE

The following report on Illinois medicare is from its beginning, August 1, 1961, through June 1962:

Applications approved.....	3,329
Applications pending.....	660
Applications denied or withdrawn ¹	2,277
Cases billed and payment made.....	1,183
Paid out on these bills.....	\$634,000
Average expenditure made on paid bills.....	\$536
Cases approved during last 2 months (May, June 1962).....	961

¹ Some applications were for information only. Others were withdrawn before completion but the 10 main reasons for rejection were: (1) relatives able to meet costs; (2) income or assets exceeded limits; (3) applied for services not offered; (4) refused to comply with IPAC policy; (5) failed appointment; (6) death of applicant; (7) applicant not yet 65; (8) applicant not hospitalized; (9) medical needs met by insurance; (10) eligible for another State program.

HOW MEDICARE CAME ABOUT

1960: Congress approved the Kerr-Mills law. The Kerr-Mills law provides for a Federal-State medical program on behalf of people 65 or over.

July 1961: The Illinois General Assembly passed the Arrington-Kaplan Act authorizing the Illinois medicare program; \$18,300,000 for the first 2 years of the program was approved in the Arrington-Kaplan Act.

Half the cost of services are paid by the Federal Government and half by the State of Illinois.

August 1, 1961: Services became available to Illinois residents.

BENEFITS OFFERED

1. Unlimited hospital care.
2. Doctors' care in hospital (except in Cook County by IPAC decision).
3. Thirty days' physician care after hospitalization.

WHAT IS AUTHORIZED

The Illinois Public Aid Commission has been given power to decide what will be provided through the program, but the basic Illinois law authorizes the following services: Drugs, nursing home,¹ diagnostic, physician, hospital, dental, laboratory and X-ray, outpatient clinic, physical therapy, home health care, private nursing.

Mr. DIRKSEN. Mr. President, on the first page of the pamphlet, in sufficiently large type, I raise the question:

I read from the pamphlet:

Are you over 65?

Beneath that:

Illinois has medicare. You are entitled to medical care.

On the next two pages, in large type:

You are eligible for medicare in Illinois if you (1) are 65 or over, (2) a permanent resident, (3) have yearly income not over \$1,800—if an individual or \$2,400—if married couple, (4) own assets under \$2,400 (not counting home), (5) need major medical care.

Apply: Illinois Public Aid Commission, at your county seat.

Then I have set forth the experience in Illinois:

First 11 months Illinois medicare:

The following report on Illinois medicare is from its beginning, August 1, 1961, through June 1962: 3,329 applications were approved; 660 applications were pending; 2,277 applications were denied or withdrawn; 1,183 cases had been billed and payment made; \$634,000 had been paid out on these bills; \$536 average expenditure was made on paid bills; 961 cases were approved during last 2 months (May, June 1962).

Then I set forth in the pamphlet some of the reasons why applications were denied.

Some applications were for information only, others were withdrawn before completion, but the 10 main reasons for rejection were: (1) relatives able to meet costs; (2) income or assets exceeded limits; (3) applied for services not offered; (4) refused to comply with IPAC policy; (5) failed appointment; (6) death of applicant; (7) applicant not yet 65; (8) applicant not hospitalized; (9) medical needs met by insurance; (10) eligible for another State program.

Then I set forth on page 5, under the title "How Medicare Came About," this language:

Year 1960: Congress approved the Kerr-Mills law. The Kerr-Mills law provides for a Federal-State medical program on behalf of people 65 or over.

July 1961: The Illinois General Assembly passed the Arrington-Kaplan Act authorizing the Illinois medicare program—\$18,300,000 for the first 2 years of the program was approved in the Arrington-Kaplan Act.

Half the cost of services are paid by the Federal Government and half by the State of Illinois.

August 1, 1961: Services became available to Illinois residents.

Finally, on page 6, I have set forth the following information:

¹ Persons needing nursing home care for which they are unable to pay can obtain such services through another State program through the IPAC offices.

Benefits offered:

1. Unlimited hospital care.
2. Doctor's care in hospital (except in Cook County by IPAC decision).
3. Thirty days' physician care after hospitalization.

Then the pamphlet states:

What is authorized:

The Illinois Public Aid Commission has been given power to decide what will be provided through the program, but the basic Illinois law authorizes the following services:

Drugs, nursing home,¹ diagnostic, physician, hospital, dental, laboratory, and X-ray, outpatient clinic, physical therapy, home health care, private nursing.

Mr. President, I desired that the contents of this pamphlet be a part of my remarks to indicate that 28 States have now passed enabling legislation whereby the benefits of the Kerr-Mills Act become available.

So we come to the question whether a person in need of medical care is required to take a so-called pauper's oath. As I read the language of the existing law, I doubt whether that is a valid interpretation; but in order to clear any doubts on the subject and to make certain that there is no requirement upon the State to require an oath or affirmation of that kind, it would be made clear in the Federal law itself, by the language of this amendment, that any statement required of the claimant for medical assistance for the aged, if made in writing and signed by the claimant, shall, so far as the last statement relates to the financial status of such claimant, be presumed by such agency to be factually correct for the purposes of determining his eligibility for such assistance.

Mr. President, I know, of course, that the amendment amends the Social Security Act and not a tax or revenue act as such; but after all the discussion and after the surcharged atmosphere of the Senate Chamber when the Senate was considering the Anderson-Javits proposal, I did not feel at that time that it was appropriate to complicate the matters before the Senate by submitting this amendment. But I was dutybound, and I was bound in my own conscience, to offer it before this session of Congress adjourned. As a result, this language will make it permissive and will leave it to the States whether or not they will require that kind of oath. In doing so, the amendment preserves the essential and basic spirit of the Kerr-Mills Act, which is essentially a Federal-State system.

After all the tears that were shed, Mr. President, here is an opportunity to redeem those tears, if some still feel that Federal law requires that the recipient take some sort of oath declaring the impoverishment of the claimant who may be in need of medical care.

Mr. McNAMARA. Mr. President, will the Senator from Illinois yield for several questions?

Mr. DIRKSEN. I yield.

Mr. McNAMARA. Is it not true that the States generally already do what is

¹ Persons needing nursing-home care for which they are unable to pay can obtain such services through another State program through the IPAC offices.

proposed by this amendment? In my experience, the States follow this procedure; they pay the bill when the claim is made, and later determine whether there is justification for the payment. Under the Senator's amendment, what is happening now would continue to happen. So it seems to me the amendment would not change a thing.

Mr. DIRKSEN. In the first place, Mr. President, I am not familiar with the provisions of the laws of all the States. But here on the floor of the Senate it was averred that there was a requirement to take a pauper's oath. I wish to make sure that the Federal law makes no such requirement of the States. Then those who made the statements about a pauper's oath will be free to return home and question their aid commissions, their Governor, and anyone else concerned, and say to them, "The Federal law does not require it; so now let us take it out of our State law, if it is included in the enabling act."

Mr. McNAMARA. Mr. President, will the Senator from Illinois yield again?

Mr. DIRKSEN. I yield.

Mr. McNAMARA. I repeat that this is what is happening now: The claimant is paid, generally, on the basis of statements he makes in his application, and later it is checked. Logically this follows, because the Kerr-Mills Act is based on need; and if there is need, proof is required. Whether it is called a pauper's oath or whether it is called something else, the facts are the same. Does not the Senator from Illinois agree that the amendment does not change anything from the present procedure?

I repeat that when there is a law based on need—as is true of the Kerr-Mills Act—there is a requirement to show the need. It can be called a pauper's oath or anything else.

Mr. DIRKSEN. If the Senator from Michigan is correct, then all the throbbing statements made on this floor when the Anderson-Javits proposal was before us would have no validity whatever.

Mr. McNAMARA. I do not agree. The Kerr-Mills Act is based on need, and the applicant is required to prove the need. The proof of need may take the form of a pauper's oath or some other form, but the effect is the same.

Mr. DIRKSEN. The Senator forgets that need is expressed in terms of the ownership or lack of ownership of assets or of a home, and so forth; and those things are set forth in the State law. In Illinois one can have an income of \$1,800, if he is single, or a couple can have an income of \$2,400, and can own a home and, in addition, can own \$2,400 in assets, and still can be eligible to receive medical care—under our law.

Mr. McNAMARA. In some States.

Mr. DIRKSEN. I am talking about my State.

Mr. McNAMARA. I have no doubt that is true in Illinois. But it is not the general rule. In some States one who is to receive such aid can own little or nothing—not even enough funds to make possible a decent burial. But this amendment would not change that situation.

Mr. DIRKSEN. But I feel a responsibility to the people of my State. If it was not properly done—although I think it was properly done—I would return home and would render my suplications and apologies to the people of my State. So I wish to be sure that no one interprets the Kerr-Mills Act as requiring something which could be called a pauper's oath.

Mr. McNAMARA. I merely wish to say that any law based on need requires a showing of the need. It can be called a pauper's oath or it can be given some other name, but the facts are the same.

I thank the Senator from Illinois.

Mr. DIRKSEN. I wish to say that when we started with the Kerr-Mills Act, we made plain that need should be shown. Of course in that respect it differed from the Anderson-Javits proposal, under which everyone—regardless of his assets or estate or income—could qualify; it made no difference whether the person involved was Everett Dirksen or Bob Kerr or Mike Mansfield or Nelson Rockefeller or the richest man in the Nation; all would still be eligible, under the Anderson-Javits proposal, for medical care.

So we just recite some income limitations, and say, "Below this amount, you are entitled to receive this aid." And I think those are very generous proposals, to say the least.

Mr. McNAMARA. But this is not the general rule throughout the States. It might be the rule in Illinois, but it does not prevail in other States.

Mr. DIRKSEN. Well, it is in Illinois; and nearly every program of which I have any knowledge which provides a State-Federal basis tries to make the aid available, and then permits the State to assume its share of the responsibility. If Michigan is behind the parade, the Senator should go to Lansing and should importune his legislature.

Mr. McNAMARA. Then we would just go up the hill and come down again.

The trouble was that the States were not handling this matter in the manner in which the framers of the law thought it should be handled. So we would go up the hill and would come down again, and would still say it should be left to the States. So we would have accomplished nothing.

Mr. DIRKSEN. I simply remind my friend that since we are in the month of September, in a few days we shall observe the 175th anniversary of the Constitution of the United States; and if it does anything in addition to protecting the freedoms of the people, it sets up a framework of government beautifully checked and balanced, to which we refer as a State-Federal system; and the powers we enjoy here in the Senate are those which have been expressly delegated to the Central Government by the Constitution. All other powers are reserved. I try to see to it that that balance of State-Federal responsibility is carefully safeguarded. I think we did so very well in the Kerr-Mills Act; we made it a State-Federal system. And the people of Michigan ought to exercise their responsibility, even as we in the State of Illinois have done.

Mr. McNAMARA. It is not a question of the law to be applied to the State of Illinois or to the State of Michigan. I think perhaps the only justification for this law, if applied at the Federal level, will be that it applies to all the States. I know there are certain things that were not specifically delegated to the Federal Government; but there have been many changes since then. If we carry the original concept to a logical conclusion, we could not today have a Federal income-tax law. And if we leave everything to the States, we would have trouble with a conscription act in time of war.

So we have progressed very far from the time when that was the accepted theory of government.

In order to make this meaningful, I think there might be a further amendment. I hold one in my hand, and I suggest that the Senator from Illinois consider accepting it. The purpose is to strike out, at the end of paragraph (f), the period and the quotation marks, and to add:

Such statement shall be conclusive as to claimant's eligibility, and no action at law or equity shall be brought for the recovery of payments made after the filing and acceptance of such statement.

This goes a little further; but if anything is to be accomplished, I think this route must be followed.

I repeat that I think the Senator's amendment accomplishes nothing; I think it deals with the way this is operating now, for any law based on need will require a means test, or whatever else it may be called.

Mr. DIRKSEN. Mr. President, that is only a personal opinion.

However, I do not wish to have the next to the last statement the Senator from Michigan made stand—that we have departed from our basic concept of government. I do not agree, because in the Constitution there is a mandatory provision; and whenever either the Congress or the States initiate the action under that mandatory clause, then it is up to the people to decide whether the Constitution shall be amended—but always within the concept as laid down 175 years ago.

Mr. McNAMARA. I ask the Senator, What brought this up? The Senator from Illinois injected this question into the debate.

Mr. DIRKSEN. I think, if we looked at the reporter's notes, they would show that the Senator from Michigan indicated that, somehow, we had mysteriously departed from the sound Federal-State system; and we have not at any time in the history of the Republic.

When we speak about recovery, that would have to involve a suit in equity or law. It would have to be one of the two. I want to be sure no one will rise in his place and say that under the Kerr-Mills Act a pauper's oath is required, but leave it to the State as to what it will propose to do about it.

Mr. McNAMARA. Mr. President, if the Senator will yield, I will rise in my place and say that I construe it in just that way. It is a pauper's oath. One may call it something else; it is a requirement based on need, and the Sen-

ator does not change it with his amendment.

Mr. DIRKSEN. Mr. President, it is so wonderful that, under our Constitution, my friend can cherish that opinion to his heart's content.

Mr. SMATHERS. Mr. President, will the Senator yield?

Mr. DIRKSEN. I yield.

Mr. SMATHERS. I wish to congratulate the able Senator from Illinois for offering this amendment. I believe it is both desirable and needed.

I think it should be very clear that, so far as the Federal Government is concerned, and as the Senator from Illinois has so well stated, there should be no requirement of a pauper's oath insofar as Federal participation is concerned. I think it should be left to the States as to how generous or ungenerous they wish to be in applying their funds under the Kerr-Mills law to take care of elderly people who might be in need of medical attention.

The State Legislature of Florida has not seen fit so far to implement the Kerr-Mills Act, but I am very hopeful that in the forthcoming session in 1963 it will implement it, and that it will follow the same pattern which the State of Illinois is following, which I think is quite fair, and certainly generous in most respects. I think this is the kind of medical program we ought to have—a program that provides total medical care for those in need.

I cannot see any earthly reason why the richest man in my State or in my community, who probably does not want it to start with, should have other citizens pay for his medical bills. On the other hand, I do not like the idea of requiring elderly persons to take an oath and state they are completely without funds, that they are destitute, in order to get such medical aid. This amendment, which would leave it to the States to decide how generous they want to be, is very desirable. The State of Illinois has set standards which are eminently generous. One can own his own home and have an income with, of course, limitation and still be eligible for benefits under the Kerr-Mills Act.

We should make it abundantly clear, and I am hopeful all States will do likewise, that none of our senior citizens be required to take a pauper's oath to avail themselves of needed medical care when it is obvious from their financial position that a need exists. These people should not be deprived of living in honor and decency or be required to dispose of their property to obtain such medical care under this law.

I wish to associate myself with the remarks made by the Senator from Illinois, and approve everything he said, including the statement that we must not destroy the Federal-State relationship. This system has over the past proved to be the best way to take care of problems which in essence, and basically, are local problems, it is desirable to get the county, State, and Federal governments in cooperation with each other to provide medical care for elderly people in need, without requiring them to take a humiliating pauper's oath, or to indicate a

complete lack of funds, which they do not want to do, and should not be required to do.

The pending amendment, which would allow the States to set the standards, is eminently desirable; and I hope the committee and the Senate will accept the amendment of the Senator from Illinois.

Mr. KERR. Mr. President, I am aware of every word the distinguished Senator from Illinois has said. I am aware that this is an insistence, but not a social security insistence, for a medical care amendment to the tax bill. I must say, however, that the Senator from Oklahoma is in entire accord with what the Senator from Illinois has said and with the language of the amendment, and therefore finds himself unable to offer any opposition to its adoption.

The PRESIDING OFFICER. The question is on agreeing to the amendment of the Senator from Illinois.

The amendment was agreed to.

Mr. DIRKSEN. Mr. President, I move to reconsider the vote by which the amendment was agreed to.

Mr. HRUSKA. Mr. President, I move to lay that motion on the table.

The motion to lay on the table was agreed to.

Mr. KERR. Mr. President, I call up my amendments 9-4-62—C.

The PRESIDING OFFICER. The amendments offered by the Senator from Oklahoma will be stated.

The legislative clerk proceeded to read the amendments.

Mr. KERR. Mr. President, I ask unanimous consent that the amendments be printed in the RECORD, without their being read.

There being no objection, the amendments were ordered to be printed in the RECORD, as follows:

On page 131, line 11, strike out "or".

On page 131, line 14, strike out "stock." and insert "stock, or".

On page 131, after line 14, insert the following:

"(D) received on obligations acquired as a result of the disposition of a trade or business actively conducted by the taxpayer in a foreign country or possession of the United States or as a result of the disposition of stock or obligations of a corporation in which the taxpayer owned at least 10 percent of the voting stock."

On page 140, beginning with line 16, strike out all through line 3 on page 141 and insert the following:

"(c) EFFECTIVE DATES.—

"(1) AMENDMENT TO SECTION 911.—The amendment made by subsection (a) shall apply to taxable years ending after December 31, 1962, but only with respect to amounts—

"(A) received after March 12, 1962, which are attributable to services performed after December 31, 1962, or

"(B) received after December 31, 1962, which are attributable to services performed on or before December 31, 1962, unless on March 12, 1962, there existed a right (whether forfeitable or nonforfeitable) to receive such amounts.

"(2) AMENDMENT TO SECTION 72(f).—The amendment made by subsection (b) shall apply to taxable years ending after December 31, 1962."

On page 196, line 20, strike out "5 years" and insert "one year".

On page 197, strike out lines 9 through 18 and insert the following:

"(3) SPECIAL RULE.—For purposes of this subpart, a United States shareholder of a controlled foreign corporation may, under regulations prescribed by the Secretary or his delegate, make the determinations under subsection (a)(2) of this section and under subsection (f) of section 954 as of the close of the years following the years referred to in such subsections, or as of the close of such longer period of time as such regulations may permit, in lieu of on the last day of such years. Any election under this paragraph made with respect to any taxable year shall apply to such year and to all succeeding taxable years unless the Secretary or his delegate consents to the revocation of such election.

"(4) EXCEPTION.—For purposes of this subpart, property shall not constitute qualified investments in less developed countries if such property is disposed of within 6 months after the date of its acquisition."

On page 197, line 19, strike out "(4)" and insert "(5)".

On page 198, lines 2 and 3, strike out "which is created or organized under the laws of a less developed country and".

On page 198, lines 17 and 18, strike out "5 years" and insert "one year".

On page 238, line 16, strike out "An election" and insert the following: "A United States shareholder of an export trade corporation may, under regulations prescribed by the Secretary or his delegate, make the determinations under paragraphs (2) and (3) with respect to export trade assets described in section 971(e)(3) as of the close of the years following the years referred to in such paragraphs, or as of the close of such longer period of time as such regulations may permit, in lieu of on the last day of such years and in lieu of on the day prescribed in the preceding sentence. Any election".

On page 280, after line 10, insert the following:

"(c) DETERMINATION OF EARNINGS AND PROFITS.—

"(1) IN GENERAL.—For purposes of this section, the earnings and profits of any foreign corporation for any taxable year shall be determined according to rules substantially similar to those applicable to domestic corporations, under regulations prescribed by the Secretary or his delegate.

"(2) EARNINGS AND PROFITS OF SUBSIDIARIES OF FOREIGN CORPORATIONS.—If—

"(A) subsection (a) applies to a sale or exchange by a United States person of stock of a foreign corporation and, by reason of the ownership of the stock sold or exchanged, such person owned within the meaning of section 958(a)(2) stock of any other foreign corporation; and

(B) such person owned, within the meaning of section 958(a), or was considered as owning by applying the rules of ownership of section 958(b), 10 percent or more of the total combined voting power of all classes of stock entitled to vote of such other foreign corporation at any time during the 5-year period ending on the date of the sale or exchange when such other foreign corporation was a controlled foreign corporation (as defined in section 957),

then, for purposes of this section, the earnings and profits of the foreign corporation the stock of which is sold or exchanged which are attributable to the stock sold or exchanged shall be deemed to include the earnings and profits of such other foreign corporation which—

"(C) are attributable (under regulations prescribed by the Secretary or his delegate) to the stock of such other foreign corporation which such person owned within the meaning of section 958(a)(2) (by reason of his ownership within the meaning of section 958(a)(1) (A) of the stock sold or exchanged) on the date of such sale or exchange; and

"(D) were accumulated in taxable years of such other corporation beginning after December 31, 1962, and during the period or periods—

"(i) such other corporation was a controlled foreign corporation, and

"(ii) such person owned within the meaning of section 958(a)(2) the stock of such other foreign corporation."

On page 280, line 11, strike out "(c) SPECIAL RULES" and insert "(d) EXCLUSIONS FROM EARNINGS AND PROFITS".

On page 281, beginning with line 12, strike out all through line 3 on page 282 and insert the following: "corporation (as defined in section 902(d)), if the stock sold or exchanged was owned for a continuous period of at least 10 years, ending with the date of the sale or exchange, by the United States person who sold or exchanged such stock."

On page 283, after line 17, insert the following:

"(e) SALES OR EXCHANGES OF STOCK IN CERTAIN DOMESTIC CORPORATIONS.—Under regulations prescribed by the Secretary or his delegate, if—

"(1) a United States person sells or exchanges stock of a domestic corporation, or receives a distribution from a domestic corporation which, under section 302 or 331, is treated as an exchange of stock, and

"(2) such domestic corporation was formed or availed of principally for the holding, directly or indirectly, of stock of one or more foreign corporations,

such sale or exchange shall, for purposes of this section, be treated as a sale or exchange of the stock of the foreign corporation or corporations held by the domestic corporation."

On page 283, line 18, strike out "(d)" and "(f)".

On page 284, line 8, strike out "(e)" and insert "(g)".

Mr. KERR. Mr. President, this is a series of amendments, a number of which are purely technical, a number of which are clarifying, some of which are corrective.

I ask unanimous consent that they may be adopted en bloc, and become a part of the text of the bill and subject to amendment by any Senator who desires to offer amendments with reference thereto.

The PRESIDING OFFICER. Is there objection? Without objection, the amendments will be considered en bloc. Without objection, they are agreed to en bloc.

The bill is open to further amendment.

Mr. DIRKSEN. Mr. President, I propose at this time to submit as an amendment H.R. 70, but before doing so, I think we ought to have a quorum call.

Mr. MANSFIELD. I suggest that the Senator have the amendment laid before the Senate.

Mr. DIRKSEN. Mr. President, am I recognized?

The PRESIDING OFFICER. The Senator from Illinois is recognized.

Mr. DIRKSEN. Before having the amendment laid before the Senate, I would like to talk to the distinguished Senator from Tennessee [Mr. GORE], and then I shall lay down H.R. 10 as an amendment to the bill. I know that a motion to table will be in order immediately after someone gets the floor for that purpose, and I wonder if we could have some understanding as to whether or not a given amount of time can be allotted to it before a motion to table,

if any is contemplated, is made. I think there are Senators on this side who want to be heard.

Mr. MANSFIELD. Mr. President, to remove any doubt in the Senator's mind—and I am sure there is no doubt in his mind—a motion to table will be made.

How much time would the Senator like to have in a limitation of debate?

Mr. DIRKSEN. Speaking for myself, I would want to have 15 minutes. The distinguished Senator from Florida, who is the actual author of this proposal, will doubtless want to speak on it.

Mr. MANSFIELD. Would the Senator agree to an hour's limitation, 40 minutes on his side and 20 minutes on the other side?

Mr. DIRKSEN. I think that would be fair.

Mr. MANSFIELD. Mr. President, I ask unanimous consent that 1½ hours be allocated to the consideration of the amendment involving H.R. 10, 1 hour to be allocated to the minority leader, and one-half hour to the majority leader. I feel certain that some of the time I would be allotted could be allocated to Senators who wish to speak.

Mr. GORE. Mr. President, reserving the right to object, as I understand the Senator's request, it relates only to the amount of debate before the motion to lay the amendment on the table.

Mr. MANSFIELD. That is correct.

Mr. GORE. In the perhaps unlikely event that the motion is not agreed to, then the limitation of time would not be effective?

Mr. MANSFIELD. That is correct. Is that agreeable?

Mr. DIRKSEN. Yes.

Mr. GORE. Reserving the right to object, Mr. President—and I shall not object—in view of the fact that there is to be a limitation of time before the motion to table, I wonder if the distinguished majority leader and distinguished minority leader would consider it advisable to have a brief quorum call, to alert other Senators that such a proposal is being made. It is a little out of the ordinary.

Mr. MANSFIELD. If the Senator wishes to do so, that is all right; but the procedure is not out of the ordinary. I think we have cleared it with the proponents and the opponents. I think nobody's mind would be changed. I am merely trying to make it possible for us to get out sometime and to get home.

Mr. GORE. I shall not assume any responsibility for other Senators. So far as I am concerned, I have no objection. I was merely making the suggestion that it was a little unusual.

Mr. DIRKSEN. I think it is quite appropriate that there be a short quorum call and that the staff notify Senators that the amendments embodying the provisions of H.R. 10 will be before the Senate.

Mr. MANSFIELD. Mr. President, I wish to say—and I hope this will be taken in the right way, and I hope all Senators will understand—that, so far as I am concerned, I do not intend to spend all day on these amendments, be-

cause there are other amendments which must be considered, also.

Mr. GORE. Yes.

Mr. MANSFIELD. As Senators know, a motion to table is in order at any time that a Senator who so desires can obtain the floor.

Mr. GORE. I do not object.

The PRESIDING OFFICER. Is there objection to the request by the Senator from Montana?

Mr. MANSFIELD. Mr. President, I suggest the absence of a quorum.

The PRESIDING OFFICER. The clerk will call the roll.

The legislative clerk proceeded to call the roll.

Mr. MANSFIELD. Mr. President, I ask unanimous consent that further proceedings under the quorum call may be dispensed with.

The PRESIDING OFFICER. Without objection, it is so ordered.

Mr. DIRKSEN. Mr. President, I offer my amendments identified as "8-23-62—K."

The PRESIDING OFFICER. The amendments will be identified for the information of the Senate.

The LEGISLATIVE CLERK. On page 391, after line 21, it is proposed to insert a new section 27, "Self-Employed Individuals Voluntary Pension Plans."

The amendments are as follows:

On page 391, after line 21, insert the following new section:

"SEC. 27. SELF-EMPLOYED INDIVIDUALS VOLUNTARY PENSION PLANS.

"Section 401 of the Internal Revenue Code of 1954 (relating to qualified pension, profit-sharing, and stock bonus plans) is amended—

"(1) by adding at the end of paragraph (5) of subsection (a) the following new sentence: 'For purposes of this paragraph and paragraph (10), the total compensation of an individual who is an employee within the meaning of subsection (c)(1) means such individual's earned income (as defined in subsection (c)(2)), and the basic or regular rate of compensation of such an individual shall be determined, under regulations prescribed by the Secretary or his delegate, with respect to that portion of his earned income which bears the same ratio to his earned income on the basic or regular compensation of the employees under the plan bears to the total compensation of such employees.';

"(2) by adding at the end of subsection (a) the following new paragraphs:

"(7) A trust shall not constitute a qualified trust under this section unless the plan of which such trust is a part provides that, upon its termination or upon complete discontinuance of contributions under the plan, the rights of all employees to benefits secured to the date of such termination or discontinuance, to the extent then funded, or the amounts credited to the employees' accounts, are nonforfeitable. This paragraph shall not apply to benefits or contributions which, under provisions of the plan adopted pursuant to regulations prescribed by the Secretary or his delegate to preclude the discrimination prohibited by paragraph (4), may not be used for designated employees in the event of early termination of the plan.

"(8) A trust forming part of a pension plan shall not constitute a qualified trust under this section unless the plan provides that forfeitures must not be applied to increase the benefits any employee would otherwise receive under the plan.

"(9) In the case of a plan which provides contributions or benefits for employees some or all of whom are employees within the meaning of subsection (c) (1), a trust forming part of such plan shall not constitute a qualified trust under this section unless, under the plan, the entire interest of each employee—

"(A) either will be distributed to him not later than his taxable year in which he attains the age of 70½ years, or, in the case of an employee other than an owner-employee (as defined in subsection (c) (3)), in which he retires, whichever is the later, or

"(B) will be distributed, commencing not later than such taxable year, (i) in accordance with regulations prescribed by the Secretary or his delegate, over the life of such employee or over the lives of such employee and his spouse, or (ii) in accordance with such regulations, over a period not extending beyond the life expectancy of such employee or the life expectancy of such employee and his spouse.

"(10) In the case of a plan which provides contributions or benefits for employees some or all of whom are owner-employees (as defined in subsection (c) (3))—

"(A) paragraph (3) and the first and second sentences of paragraph (5) shall not apply, but—

"(i) such plan shall not be considered discriminatory within the meaning of paragraph (4) merely because the contributions or benefits of or on behalf of employees under the plan bear a uniform relationship to the total compensation, or the basic or regular rate of compensation, of such employees, and

"(ii) such plan shall not be considered discriminatory within the meaning of paragraph (4) solely because under the plan contributions described in subsection (e) (3) (A) which are in excess of the amounts which may be deducted under section 404 (determined without regard to section 404 (a) (10)) for the taxable year may be made on behalf of any owner-employee; and

"(B) a trust forming a part of such plan shall constitute a qualified trust under this section only if the requirements in subsection (d) are also met; and

"(3) by redesignating subsection (c) as subsection (h) and inserting after subsection (b) the following new subsections:

"(c) DEFINITIONS AND RULES RELATING TO SELF-EMPLOYED INDIVIDUALS AND OWNER-EMPLOYEES.—For purposes of this section—

"(1) EMPLOYEE.—The term "employee" includes, for any taxable year, an individual who has earned income (as defined in paragraph (2)) for the taxable year. To the extent provided in regulations prescribed by the Secretary or his delegate, such term also includes, for any taxable year—

"(A) an individual who would be an employee within the meaning of the preceding sentence but for the fact that the trade or business carried on by such individual did not have net profits for the taxable year, and

"(B) an individual who has been an employee within the meaning of the preceding sentence for any prior taxable year.

"(2) EARNED INCOME.—

"(A) IN GENERAL.—The term "earned income" means the net earnings from self-employment (as defined in section 1402 (a)) to the extent that such net earnings constitute earned income (as defined in section 911(b) but determined with the application of subparagraph (B)), but such net earnings shall be determined—

"(i) without regard to paragraphs (4) and (5) of section 1402(c),

"(ii) in the case of any individual who is treated as an employee under sections 3121 (d) (2) (A), (C), or (D), without regard to paragraph (2) of section 1402(c), and

"(iii) without regard to items which are not included in gross income for purposes of this chapter, and the deductions properly allocable to or chargeable against such items.

For purposes of subparagraph (A), sections 911(b) and 1402, as in effect for a taxable year ending on December 31, 1961, and subparagraph (B), as in effect for a taxable year beginning on January 1, 1962, shall be treated as having been in effect for all taxable years ending before such date.

"(B) EARNED INCOME WHEN BOTH PERSONAL SERVICES AND CAPITAL ARE MATERIAL INCOME-PRODUCING FACTORS.—In applying section 911(b) for purposes of subparagraph (A), in the case of an individual who is an employee within the meaning of paragraph (1) and who is engaged in a trade or business in which both personal services and capital are material income-producing factors and with respect to which the individual actually renders personal services on a full-time, or substantially full-time, basis, so much of his share of the net profits of such trade or business as does not exceed \$2,500 shall be considered as earned income. In the case of any such individual who is engaged in more than one trade or business with respect to which he actually renders substantial personal services, if with respect to all such trades or businesses he actually renders personal services on a full-time, or substantially full-time, basis, there shall be considered as earned income with respect to the trades or businesses in which both personal services and capital are material income-producing factors—

"(i) so much of his share of the net profits of such trades or businesses as does not exceed \$2,500, reduced by

"(ii) his share of the net profits of any trade or business in which only personal services is a material income-producing factor.

The preceding sentences shall not be construed to reduce the share of net profits of any trade or business which under the second sentence of section 911(b) would be considered as earned income of any such individual.

"(3) OWNER-EMPLOYEE.—The term "owner employee" means an employee who—

"(A) owns the entire interest in an unincorporated trade or business, or

"(B) in the case of a partnership, is a partner who owns more than 10 percent of either the capital interest or the profits interest in such partnership.

To the extent provided in regulations prescribed by the Secretary or his delegate, such term also means an individual who has been an owner-employee within the meaning of the preceding sentence.

"(4) EMPLOYER.—An individual who owns the entire interest in an unincorporated trade or business shall be treated as his own employer. A partnership shall be treated as the employer of each partner who is an employee within the meaning of paragraph (1).

"(5) CONSTRUCTIVE OWNERSHIP.—An individual shall be treated as owning any interest in an unincorporated trade or business which is owned, directly or indirectly, by his spouse or minor children. An individual who owns any interest in an unincorporated trade or business or is an employee of such trade or business shall be treated as owning any interest in such unincorporated trade or business which is owned, directly or indirectly, by his ancestors or lineal descendants. Any interest treated as owned by any individual by reason of the application of the preceding sentences shall not be treated as owned by him for the purpose of applying such sentences in order to make any other individual the constructive owner of such interest. For purposes of this paragraph, a legally adopted child of an individual shall be treated as a child of such individual by blood.

"(6) CONTRIBUTIONS ON BEHALF OF OWNER-EMPLOYEES.—The term "contribution on behalf of an owner-employee" includes, except as the context otherwise requires, a contribution under a plan—

"(A) by the employer for an owner-employee, and

"(B) by an owner-employee as an employee."

"(d) ADDITIONAL REQUIREMENTS FOR QUALIFICATION OF TRUSTS AND PLANS BENEFITING OWNER-EMPLOYEES.—A trust forming part of a pension or profit-sharing plan which provides contributions or benefits for employees some or all of whom are owner-employees shall constitute a qualified trust under this section only if, in addition to meeting the requirements of subsection (a), the following requirements of this subsection are met by the trust and by the plan of which such trust is a part:

"(1) In the case of a trust which is created on or after the date of the enactment of this subsection, or which was created before such date but is not exempt from tax under section 501(a) as an organization described in subsection (a) on the day before such date, the trustee is a bank, but a person (including the employer) other than a bank may be granted, under the trust instrument, the power to control the investment of the trust funds either by directing investments (including reinvestments, disposals, and exchanges) or by disapproving proposed investments (including reinvestments, disposals, and exchanges). This paragraph shall not apply to a trust created or organized outside the United States before the date of the enactment of this subsection if, under section 402(c), it is treated as exempt from tax under section 501(a) on the day before such date. For purposes of this paragraph, the term "bank" means a bank as defined in section 581, a corporation which under the laws of the State of its incorporation is subject to supervision and examination by the commissioner of banking or other officer of such State in charge of the administration of the banking laws of such State, and, in the case of a trust created or organized outside the United States, a bank or trust company, wherever incorporated, exercising fiduciary powers and subject to supervision and examination by governmental authority.

"(2) Under the plan—

"(A) the employees' rights to or derived from the contributions under the plan are nonforfeitable at the time the contributions are paid to or under the plan; and

"(B) in the case of a profit-sharing plan, there is a definite formula for determining the contributions to be made by the employer on behalf of employees (other than owner-employees).

Subparagraph (A) shall not apply to contributions which, under provisions of the plan adopted pursuant to regulations prescribed by the Secretary or his delegate to preclude the discrimination prohibited by subsection (a) (4), may not be used to provide benefits for designated employees in the event of early termination of the plan.

"(3) The plan benefits each employee having a period of employment of 3 years or more. For purposes of the preceding sentence, the term "employee" does not include any employee whose customary employment is for not more than 20 hours in any one week or is for not more than 5 months in any calendar year.

"(4) Under the plan—

"(A) contributions or benefits are not provided for any owner-employee unless such owner-employee has consented to being included under the plan; and

"(B) no benefits may be paid to any owner-employee, except in the case of his becoming disabled (within the meaning of section 213(g) (3)), prior to his attaining the age of 59½ years.

"(5) The plan does not permit—

"(A) contributions to be made by the employer on behalf of any owner-employee in excess of the amounts which may be deducted under section 404 (determined with-

out regard to section 404(a)(10)) for the taxable year;

“(B) in the case of a plan which provides contributions or benefits only for owner-employees, contributions to be made on behalf of any owner-employee in excess of the amounts which may be deducted under section 404 (determined without regard to section 404(a)(10)) for the taxable year; and

“(C) if a distribution under the plan is made to any employee and if any portion of such distribution is an amount described in section 72(m)(5)(A)(i), contributions to be made on behalf of such employee for the 5 taxable years succeeding the taxable year in which such distribution is made.

Subparagraphs (A) and (B) shall not apply to any contribution which is not considered to be an excess contribution (as defined in subsection (e)(1)) by reason of the application of subsection (e)(3).

“(6) Except as provided in this paragraph, the plan meets the requirements of subsection (a)(4) without taking into account for any purpose contributions or benefits under chapter 2 (relating to tax on self-employment income), chapter 21 (relating to Federal Insurance Contributions Act), title II of the Social Security Act, as amended, or any other Federal or State law. If—

“(A) of the contributions deductible under section 404 (determined without regard to section 404(a)(10)), not more than one-third is deductible by reason of contributions by the employer on behalf of owner-employees, and

“(B) taxes paid by the owner-employees under chapter 2 (relating to tax on self-employment income), and the taxes which would be payable under such chapter 2 by the owner-employees but for paragraphs (4) and (5) of section 1402(c), are taken into account as contributions by the employer on behalf of such owner-employees.

then taxes paid under section 3111 (relating to tax on employers) with respect to an employee may, for purposes of subsection (a)(4), be taken into account as contributions by the employer for such employee under the plan.

“(7) Under the plan, if an owner-employee dies before his entire interest has been distributed to him, or if distribution has been commenced in accordance with subsection (a)(9)(B) to his surviving spouse and such surviving spouse dies before his entire interest has been distributed to such surviving spouse, his entire interest (or the remaining part of such interest if distribution thereof has commenced) will, within 5 years after his death (or the death of his surviving spouse), be distributed, or applied to the purchase of an immediate annuity for his beneficiary or beneficiaries (or the beneficiary or beneficiaries of his surviving spouse) which will be payable for the life of such beneficiary or beneficiaries (or for a term certain not extending beyond the life expectancy of such beneficiary or beneficiaries) and which will be immediately distributed to such beneficiary or beneficiaries. The preceding sentence shall not apply if distribution of the interest of an owner-employee has commenced and such distribution is for a term certain over a period permitted under subsection (a)(9)(B)(ii).

“(8) Under the plan—

“(A) any contribution which is an excess contribution, together with the income attributable to such excess contribution, is (unless subsection (e)(2)(E) applies) to be repaid to the owner-employee on whose behalf such excess contribution is made;

“(B) if for any taxable year the plan does not, by reason of subsection (e)(2)(A), meet (for purposes of section 404) the requirements of this subsection with respect to an owner-employee, the income for the taxable year attributable to the interest of such

owner-employee under the plan is to be paid to such owner-employee; and

“(C) the entire interest of an owner-employee is to be repaid to him when required by the provisions of subsection (e)(2)(E).

“(9)(A) If the plan provides contributions or benefits for an owner-employee who controls, or for two or more owner-employees who together control, the trade or business with respect to which the plan is established, and who also control as an owner-employee or as owner-employees one or more other trades or businesses, such plan and the plans established with respect to such other trades or businesses, when coalesced, constitute a single plan which meets the requirements of subsection (a) (including paragraph (10) thereof) and of this subsection with respect to the employees of all such trades or businesses (including the trade or business with respect to which the plan intended to qualify under this section is established).

“(B) For purposes of subparagraph (A), an owner-employee, or two or more owner-employees, shall be considered to control a trade or business if such owner-employee, or such two or more owner-employees together—

“(i) own the entire interest in an unincorporated trade or business, or

“(ii) in the case of a partnership, own more than 50 percent of either the capital interest or the profits interest in such partnership.

For purposes of the preceding sentence, an owner-employee, or two or more owner-employees, shall be treated as owning any interest in a partnership which is owned, directly or indirectly, by a partnership which such owner-employee, or such two or more owner-employees, are considered to control within the meaning of the preceding sentence.

“(10) The plan does not provide contributions or benefits for any owner-employee who controls (within the meaning of paragraph (9)(B)), or for two or more owner-employees who together control, as an owner-employee or as owner-employees, any other trade or business, unless the employees of each trade or business which such owner-employee or such owner-employees control are included under a plan which meets the requirements of subsection (a) (including paragraph (10) thereof) and of this subsection, and provides contributions and benefits for employees which are not less favorable than contributions and benefits provided for owner-employees under the plan.

“(11) Under the plan, contributions on behalf of any owner-employee may be made only with respect to the earned income of such owner-employee which is derived from the trade or business with respect to which such plan is established.

“(e) EXCESS CONTRIBUTIONS ON BEHALF OF OWNER-EMPLOYEES.—

“(1) EXCESS CONTRIBUTION DEFINED.—For purposes of this section, the term “excess contribution” means, except as provided in paragraph (3)—

“(A) if, in the taxable year, contributions are made under the plan only on behalf of owner-employees, the amount of any contribution made on behalf of any owner-employee which (without regard to this subsection) is not deductible under section 404 (determined without regard to section 404(a)(10)) for the taxable year; or

“(B) if, in the taxable year, contributions are made under the plan on behalf of employees other than owner-employees—

“(i) the amount of any contribution made by the employer on behalf of any owner-employee which (without regard to this subsection) is not deductible under section 404 (determined without regard to section 404(a)(10)) for the taxable year;

“(ii) the amount of any contribution made by any owner-employee (as an em-

ployee) at a rate which exceeds the rate of contributions permitted to be made by employees other than owner-employees;

“(iii) the amount of any contribution made by any owner-employee (as an employee) which exceeds the lesser of \$2,500 or 10 percent of the earned income for such taxable year derived by such owner-employee from the trade or business with respect to which the plan is established; and

“(iv) in the case of any individual on whose behalf contributions are made under more than one plan as an owner-employee, the amount of any contribution made by such owner-employee (as an employee) under all such plans which exceeds \$2,500; and

“(C) the amount of any contribution made on behalf of an owner-employee in any taxable year for which, under paragraph (2)(A) or (E), the plan does not (for purposes of section 404) meet the requirements of subsection (d) with respect to such owner-employee.

For purposes of this subsection, the amount of any contribution which is allocable (determined in accordance with regulations prescribed by the Secretary or his delegate) to the purchase of life, accident, health, or other insurance shall not be taken into account.

“(2) EFFECT OF EXCESS CONTRIBUTION.—

“(A) IN GENERAL.—If an excess contribution (other than an excess contribution to which subparagraph (E) applies) is made on behalf of an owner-employee in any taxable year, the plan with respect to which such excess contribution is made shall, except as provided in subparagraphs (C) and (D), be considered, for purposes of section 404, as not meeting the requirements of subsection (d) with respect to such owner-employee for the taxable year and for all succeeding taxable years.

“(B) INCLUSION OF AMOUNTS IN GROSS INCOME OF OWNER-EMPLOYEES.—For any taxable year for which any plan does not meet the requirements of subsection (d) with respect to an owner-employee by reason of subparagraph (A), the gross income of such owner-employee shall, for purposes of this chapter, include the amount of income for such taxable year attributable to the interest of such owner-employee under such plan.

“(C) REPAYMENT WITHIN PRESCRIBED PERIOD.—Subparagraph (A) shall not apply to an excess contribution with respect to any taxable year, if, on or before the close of the 6-month period beginning on the day on which the Secretary or his delegate sends notice (by certified or registered mail) to the person to whom such excess contribution, the amount of such excess contribution, and the income attributable thereto, is repaid to the owner-employee on whose behalf such excess contribution was made. If the excess contribution is an excess contribution as defined in paragraph (1)(A) or (B)(i), or is an excess contribution as defined in paragraph (1)(C) with respect to which a deduction has been claimed under section 404, the notice required by the preceding sentence shall not be mailed prior to the time that the amount of the tax under this chapter of such owner-employee for the taxable year in which such excess contribution was made has been finally determined.

“(D) REPAYMENT AFTER PRESCRIBED PERIOD.—If an excess contribution, together with the income attributable thereto, is not repaid within the 6-month period referred to in subparagraph (C), subparagraph (A) shall not apply to an excess contribution with respect to any taxable year beginning with the taxable year in which the person to whom such excess contribution was paid repays the amount of such excess contribution to the owner-employee on whose behalf such excess contribution was made, and pays to such owner-employee the amount of income attributable to the interest of such

owner-employee which, under subparagraph (B), has been included in the gross income of such owner-employee for any prior taxable year.

“(E) SPECIAL RULE IF EXCESS CONTRIBUTION WAS WILLFULLY MADE.—If an excess contribution made on behalf of an owner-employee is determined to have been willfully made, then—

“(1) subparagraphs (A), (B), (C), and (D) shall not apply with respect to such excess contribution;

“(ii) there shall be distributed to the owner-employee on whose behalf such excess contribution was willfully made his entire interest in all plans with respect to which he is an owner-employee; and

“(iii) no plan shall, for purposes of section 404, be considered as meeting the requirements of subsection (d) with respect to such owner-employee for the taxable year in which it is determined that such excess contribution was willfully made and for the 5 taxable years following such taxable year.

“(F) STATUTE OF LIMITATIONS.—In any case in which subparagraph (A) applies, the period for assessing any deficiency arising by reason of—

“(1) the disallowance of any deduction under section 404 on account of a plan not meeting the requirements of subsection (d) with respect to the owner-employee on whose behalf an excess contribution was made, or

“(ii) the inclusion, under subparagraph (B), in gross income of such owner-employee of income attributable to the interest of such owner-employee under a plan,

for the taxable year in which such excess contribution was made or for any succeeding taxable year shall not expire prior to 1 year after the close of the 6-month period referred to in subparagraph (C).

“(3) CONTRIBUTIONS FOR PREMIUMS ON ANNUITY, ETC., CONTRACTS.—A contribution by the employer on behalf of an owner-employee shall not be considered to be an excess contribution within the meaning of paragraph (1), if—

“(A) under the plan such contribution is required to be applied (directly or through a trustee) to pay premiums or other consideration for one or more annuity, endowment, or life insurance contracts on the life of such owner-employee issued under the plan,

“(B) the amount of such contribution exceeds the amount deductible under section 404 (determined without regard to section 404(a)(10)) with respect to contributions made by the employer on behalf of such owner-employee under the plan, and

“(C) the amount of such contribution does not exceed the average of the amounts which were deductible under section 404 (determined without regard to section 404(a)(10)) with respect to contributions made by the employer on behalf of such owner-employee under the plan (or which would have been deductible under such section if such section had been in effect) for the first 3 taxable years (1) preceding the year in which the last such annuity, endowment, or life insurance contract was issued under the plan and (ii) in which such owner-employee derived earned income from the trade or business with respect to which the plan is established, or for so many of such taxable years as such owner-employee was engaged in such trade or business and derived earned income therefrom.

In the case of any individual on whose behalf contributions described in subparagraph (A) are made under more than one plan as an owner-employee during any taxable year, the preceding sentence shall not apply if the amount of such contributions under all such plans for such taxable year exceeds \$2,500. Any contribution which is not con-

sidered to be an excess contribution by reason of the application of this paragraph shall, for purposes of subparagraphs (B) (ii), (iii), and (iv) of paragraph (1), be taken into account as a contribution made by such owner-employee as an employee to the extent that the amount of such contribution is not deductible under section 404 (determined without regard to section 404(a)(10)) for the taxable year, but only for the purpose of applying such subparagraphs to other contribution made by such owner-employee as an employee.

“(f) CERTAIN CUSTODIAL ACCOUNTS.—

“(1) TREATMENT AS QUALIFIED TRUST.—For purposes of this title, a custodial account shall be treated as a qualified trust under this section, if—

“(A) such custodial account would, except for the fact that it is not a trust, constitute a qualified trust under this section;

“(B) the custodian is a bank (as defined in subsection (d)(1));

“(C) the investment of the funds in such account (including all earnings) is to be made—

“(i) solely in regulated investment company stock with respect to which an employee is the beneficial owner, or

“(ii) solely in annuity, endowment, or life insurance contracts issued by an insurance company;

“(D) the shareholder of record of any such stock described in subparagraph (C) (i) is the custodian or its nominee; and

“(E) the contracts described in subparagraph (C)(ii) are held by the custodian until distributed under the plan.

For purposes of this title, in the case of a custodial account treated as a qualified trust under this section by reason of the preceding sentence, the custodian of such account shall be treated as the trustee thereof.

“(2) DEFINITION.—For purposes of paragraph (1), the term “regulated investment company” means a domestic corporation which—

“(A) is a regulated investment company within the meaning of section 851(a), and

“(B) issues only redeemable stock.

“(g) ANNUITY DEFINED.—For purposes of this section and sections 402, 403, and 404, the term “annuity” includes a face-amount certificate, as defined in section 2(a)(15) of the Investment Company Act of 1940 (15 U.S.C. sec. 80a-2); but does not include any contract or certificate issued after December 31, 1961, which is transferable, if any person other than the trustee of a trust described in section 401(a) which is exempt from tax under section 501(a) is the owner of such contract or certificate.

“SEC. 28. DEDUCTIBILITY OF CONTRIBUTIONS TO PLANS.

“(a) INCLUSION OF SELF-EMPLOYED INDIVIDUALS.—Section 404(a) of the Internal Revenue Code of 1954 (relating to the deductibility of contributions to pension, annuity, profit-sharing, or stock bonus plans or plans of deferred compensation) is amended—

“(1) by striking out in paragraph (2) ‘and (6),’ and inserting in lieu thereof ‘(6), (7), and (8), and, if applicable, (9) and, in the case of a plan described in paragraph (9) of this subsection, which meets the requirements of section 401(a)(10) and of section 401(d) (other than paragraph (1)),’; and

“(2) by adding after paragraph (7) the following new paragraphs:

“(8) SELF-EMPLOYED INDIVIDUALS.—In the case of a plan included in paragraph (1), (2), or (3) which provides contributions or benefits for employees some or all of whom are employees within the meaning of section 401(c)(1), for purposes of this section—

“(A) the term “employee” includes an individual who is an employee within the

meaning of section 401(c)(1), and the employer of such individual is the person treated as his employer under section 401(c)(4);

“(B) the term “earned income” has the meaning assigned to it by section 401(c)(2);

“(C) the contributions to such plan on behalf of an individual who is an employee within the meaning of section 401(c)(1) shall be considered to satisfy the conditions of section 162 or 212 to the extent that such contributions do not exceed the earned income of such individual derived from the trade or business with respect to which such plan is established, and to the extent that such contributions are not allocable (determined in accordance with regulations prescribed by the Secretary or his delegate) to the purchase of life, accident, health, or other insurance; and

“(D) any reference to compensation shall, in the case of an individual who is an employee within the meaning of section 401(c)(1), be considered to be a reference to the earned income of such individual derived from the trade or business with respect to which the plan is established.

“(9) PLANS BENEFITTING OWNER-EMPLOYEE.—In the case of a plan included in paragraph (1), (2), or (3) which provides contributions or benefits for employees some or all of whom are owner-employees—

“(A) the limitations provided by paragraphs (1), (2), (3), and (7) on the amounts deductible for any taxable year shall be computed, with respect to contributions on behalf of employees (other than owner-employees), as if such employees were the only employees for whom contributions and benefits are provided under the plan;

“(B) the limitations provided by paragraphs (1), (2), (3), and (7) on the amounts deductible for any taxable year shall be computed, with respect to contributions on behalf of owner-employees—

“(i) as if such owner-employees were the only employees for whom contributions and benefits are provided under the plan, and

“(ii) without regard to paragraph (1) (D), the second and third sentences of paragraph (3), and the second sentence of paragraph (7); and

“(C) the amounts deductible under paragraphs (1), (2), (3), and (7), with respect to contributions on behalf of any owner-employee, shall not exceed the applicable limitation provided in subsection (e).

For purposes of this paragraph and subsections (e) and (f), the term “owner-employee” has the meaning assigned to it by section 401(c)(3) (determined with the application of section 401(c)(5)).

“(10) SPECIAL LIMITATION ON AMOUNT ALLOWED AS DEDUCTION FOR SELF-EMPLOYED INDIVIDUALS.—Notwithstanding any other provision of this section, the amount allowable as a deduction under paragraphs (1), (2), (3), and (7) in any taxable year with respect to contributions made on behalf of an individual who is an employee within the meaning of section 401(c)(1) shall be an amount equal to—

“(A) so much of the contributions made on behalf of such individual in such taxable year which are deductible under such paragraphs (determined with the application of paragraph (9) and of subsection (e) but without regard to this paragraph) as does not exceed \$1,000, plus

“(B) one-half of the contributions made on behalf of such individual in such taxable year which are deductible under such paragraphs (as so determined) as exceeds \$1,000. For purposes of section 401, the amount which may be deleted, or the amount deductible, under this section with respect to contributions made on behalf of such

individual shall be determined without regard to the preceding sentence."

"(b) LIMITATIONS ON DEDUCTIBLE CONTRIBUTIONS ON BEHALF OF OWNER-EMPLOYEES.—Section 404 of the Internal Revenue Code of 1954 (relating to the deductibility of contributions to pension, annuity, profit-sharing, or stock bonus plans or plans of deferred compensation) is amended by adding after subsection (d) the following new subsections:

"(e) SPECIAL LIMITATIONS FOR OWNER-EMPLOYEES.—

"(1) IN GENERAL.—In the case of a plan included in subsection (a) (1), (2), or (3), which provides contributions or benefits for employees some or all of whom are owner-employees, the amounts deductible under subsection (a) (determined without regard to paragraph (10) thereof) in any taxable year with respect to contributions on behalf of any owner-employee shall, subject to the provisions of paragraph (2), not exceed \$2,500, or 100 percent of the earned income derived by such owner-employee from the trade or business with respect to which the plan is established, whichever is the lesser.

"(2) CONTRIBUTIONS MADE UNDER MORE THAN ONE PLAN.—

"(A) OVERALL LIMITATION.—In any taxable year in which amounts are deductible with respect to contributions under two or more plans on behalf of an individual who is an owner-employee with respect to such plans, the aggregate amount deductible for such taxable year under all such plans with respect to contributions on behalf of such owner-employee (determined without regard to subsection (a)(10)) shall not exceed \$2,500.

"(B) ALLOCATION OF AMOUNTS DEDUCTIBLE.—In any case in which the amounts deductible under subsection (a) (within the application of the limitations of this subsection) with respect to contributions made on behalf of an owner-employee under two or more plans are, by reason of subparagraph (A), less than the amounts deductible under such subsection determined without regard to such subparagraph, the amount deductible under subsection (a) (determined without regard to paragraph (10) thereof) with respect to such contributions under each such plan shall be determined in accordance with regulations prescribed by the Secretary or his delegate.

"(B) CONTRIBUTIONS ALLOCABLE TO INSURANCE PROTECTION.—For purposes of this subsection, contributions which are allocable (determined under regulations prescribed by the Secretary or his delegate) to the purchase of life, accident, health, or other insurance shall not be taken into account.

"(f) CERTAIN LOAN REPAYMENTS CONSIDERED AS CONTRIBUTIONS.—For purposes of this section, any amount paid, directly or indirectly, by an owner-employee in repayment of any loan which under section 72(m) (4) (B) was treated as an amount received under a contract purchased by a trust described in section 401(a) which is exempt from tax under section 501(a) or purchased as a part of a plan described in section 403(a) shall be treated as a contribution to which this section applies on behalf of such owner-employee to such trust or to or under such plan."

"SEC. 29. TAXABILITY OF DISTRIBUTIONS.

"(a) EMPLOYEES' ANNUITIES.—Section 72 (d) (2) of the Internal Revenue Code of 1954 (relating to employees' annuities) is amended to read as follows:

"(2) SPECIAL RULES FOR APPLICATION OF PARAGRAPH (1).—For purposes of paragraph (1)—

"(A) if the employee died before any amount was received as an annuity under the contract, the words "receivable by the employee" shall be read as "receivable by a beneficiary of the employee"; and

"(B) any contribution made with respect to the contract while the employee is an employee within the meaning of section 401(c) (1) which is not allowed as a deduction under section 404 shall be treated as consideration for the contract contributed by the employee."

"(b) SPECIAL RULES RELATING TO SELF-EMPLOYED INDIVIDUALS AND OWNER-EMPLOYEES.—Section 72 of the Internal Revenue Code of 1954 (relating to annuities, etc.) is amended by redesignating subsection (m) as subsection (o) and by inserting after subsection (l) the following new subsections:

"(m) SPECIAL RULES APPLICABLE TO EMPLOYEE ANNUITIES AND DISTRIBUTIONS UNDER EMPLOYEE PLANS.—

"(1) CERTAIN AMOUNTS RECEIVED BEFORE ANNUITY STARTING DATE.—Any amounts received under an annuity, endowment, or life insurance contract before the annuity starting date which are not received as an annuity (within the meaning of subsection (e) (2)) shall be included in the recipient's gross income for the taxable year in which received to the extent that—

"(A) such amounts, plus all amounts theretofore received under the contract and includible in gross income under this paragraph, do not exceed

"(B) the aggregate premiums or other consideration paid for the contract while the employee was an owner-employee which were allowed as deductions under section 404 for the taxable year and all prior taxable years. Any such amounts so received which are not includible in gross income under this paragraph shall be subject to the provisions of subsection (e).

"(2) COMPUTATION OF CONSIDERATION PAID BY THE EMPLOYEE.—In computing—

"(A) the aggregate amount of premiums or other consideration paid for the contract for purposes of subsection (c) (1) (A) (relating to the investment in the contract),

"(B) the consideration for the contract contributed by the employee for purposes of subsection (d) (1) (relating to employee's contributions recoverable in 3 years), and

"(C) the aggregate premiums or other consideration paid for purposes of subsection (e) (1) (B) (relating to certain amounts not received as an annuity),

any amount allowed as a deduction with respect to the contract under section 404 which was paid while the employee was an employee within the meaning of section 401(c) (1) shall be treated as consideration contributed by the employer, and there shall not be taken into account any portion of the premiums or other consideration for the contract paid while the employee was an owner-employee which is properly allocable (as determined under regulations prescribed by the Secretary or his delegate) to the cost of life, accident, health, or other insurance.

"(3) LIFE INSURANCE CONTRACTS.—

"(A) This paragraph shall apply to any life insurance contract—

"(i) purchased as a part of a plan described in section 403(a), or

"(ii) purchased by a trust described in section 401(a) which is exempt from tax under section 501(a) if the proceeds of such contract are payable directly or indirectly to a participant in such trust or to a beneficiary of such participant.

"(B) Any contribution to a plan described in subparagraph (A) (i) or a trust described in subparagraph (A) (ii) which is allowed as a deduction under section 404, and any income of a trust described in subparagraph (A) (ii), which is determined in accordance with regulations prescribed by the Secretary or his delegate to have been applied to purchase the life insurance protection under a contract described in subparagraph (A), is includible in the gross in-

come of the participant for the taxable year when so applied.

"(C) In the case of the death of an individual insured under a contract described in subparagraph (A), an amount equal to the cash surrender value of the contract immediately before the death of the insured shall be treated as a payment under such plan or a distribution by such trust, and the excess of the amount payable by reason of the death of the insured over such cash surrender value shall not be includible in gross income under this section and shall be treated as provided in section 101.

"(4) AMOUNTS CONSTRUCTIVELY RECEIVED.—

"(A) ASSIGNMENTS OR PLEDGES.—If during any taxable year an owner-employee assigns (or agrees to assign) or pledges (or agrees to pledge) any portion of his interest in a trust described in section 401(a) which is exempt from tax under section 501(a) or any portion of the value of a contract purchased as part of a plan described in section 403(a), such portion shall be treated as having been received by such owner-employee as a distribution from such trust or as an amount received under the contract.

"(B) LOANS ON CONTRACTS.—If during any taxable year, an owner-employee receives, directly or indirectly, any amount from any insurance company as a loan under a contract purchased by a trust described in section 401(a) which is exempt from tax under section 501(a) or purchased as part of a plan described in section 403(a), and issued by such insurance company, such amount shall be treated as an amount received under the contract.

"(5) PENALTIES APPLICABLE TO CERTAIN AMOUNTS RECEIVED BY OWNER-EMPLOYEES.—

"(A) This paragraph shall apply—

"(i) to amounts (other than any amount received by an individual in his capacity as a policyholder of an annuity, endowment, or life insurance contract which is in the nature of a dividend or similar distribution) which are received from a qualified trust described in section 401(a) or under a plan described in section 403(a) and which are received by an individual, who is, or has been, an owner-employee, before such individual attains the age of 59½ years, for any reason other than the individual's becoming disabled (within the meaning of section 213(g) (3)), but only to the extent that such amounts are attributable to contributions paid on behalf of such individual (whether or not paid by him) while he was an owner-employee,

"(ii) to amounts which are received from a qualified trust described in section 401(a) or under a plan described in section 403(a) at any time by an individual who is, or has been, an owner-employee, or by the successor of such individual, but only to the extent that such amounts are determined, under regulations prescribed by the Secretary or his delegate, to exceed the benefits provided for such individual under the plan formula, and

"(iii) to amounts which are received, by an individual who is, or has been, an owner-employee, by reason of the distribution under the provisions of section 401(e) (2) (E) of his entire interest in all qualified trusts described in section 401(a) and in all plans described in section 403(a).

"(B) (i) If the aggregate of the amounts to which this paragraph applies received by any person in his taxable year equals or exceeds \$2,500, the increase in his tax for the taxable year in which such amounts are received and attributable to such amounts shall not be less than 110 percent of the aggregate increase in taxes, for the taxable year and the 4 immediately preceding taxable years, which would have resulted if such amounts had been included in such person's gross income ratably over such taxable years.

"(ii) If deductions have been allowed under section 404 for contributions paid on behalf of the individual while he is an owner-employee for a number of prior taxable years less than 4, clause (i) shall be applied by taking into account a number of taxable years immediately preceding the taxable year in which the amount was so received equal to such lesser number.

"(C) If subparagraph (B) does not apply to a person for the taxable year, the increase in tax of such person for the taxable year attributable to the amounts to which this paragraph applies shall be 110 percent of such increase (computed without regard to this subparagraph).

"(D) Subparagraph (A) (ii) of this paragraph shall not apply to any amount to which section 402(a)(2) or 403(a)(2) applies.

"(E) For special rules for computation of taxable income for taxable years to which this paragraph applies, see subsection (n) (3).

"(6) OWNER-EMPLOYEE DEFINED.—For purposes of this subsection, the term "owner-employee" has the meaning assigned to it by section 401(c)(3) (determined with the application of section 401(c)(5)).

"(n) TREATMENT OF CERTAIN DISTRIBUTIONS WITH RESPECT TO CONTRIBUTIONS BY SELF-EMPLOYED INDIVIDUALS.—

"(1) APPLICATION OF SUBSECTION.—

"(A) DISTRIBUTIONS BY EMPLOYEES' TRUST.—Subject to the provisions of subparagraph (C), this subsection shall apply to amounts distributed to a distributee, in the case of an employees' trust described in section 401(a) which is exempt from tax under section 501(a), if the total distributions payable to the distributee with respect to an employee are paid to the distributee within one taxable year of the distributee—

"(i) on account of the employee's death,

"(ii) after the employee has attained the age of 59½ years, or

"(iii) after the employee has become disabled (within the meaning of section 213 (g)(3)).

"(B) ANNUITY PLANS.—Subject to the provisions of subparagraph (C), this subsection shall apply to amounts paid to a payee, in the case of an annuity plan described in section 403(a), if the total amounts payable to the payee with respect to an employee are paid to the payee within one taxable year of the payee—

"(i) on account of the employee's death,

"(ii) after the employee has attained the age of 59½ years, or

"(iii) after the employee has become disabled (within the meaning of section 213 (g)(3)).

"(C) LIMITATIONS AND EXCEPTIONS.—This subsection shall apply—

"(i) only with respect to so much of any distribution or payment to which (without regard to this subparagraph) subparagraph (A) or (B) applies as is attributable to contributions made on behalf of an employee while he was an employee within the meaning of section 401(c)(1), and

"(ii) if the recipient is the employee on whose behalf such contributions were made, only if contributions which were allowed as a deduction under section 404 have been made on behalf of such employee while he was an employee within the meaning of section 401(c)(1) for 5 or more taxable years prior to the taxable year in which the total distributions payable or total amounts payable, as the case may be, are paid.

This subsection shall not apply to amounts described in clauses (ii) and (iii) of subparagraph (A) of subsection (m)(5) (but, in the case of amounts described in clause (ii) of such subparagraph, only to the extent that subsection (m)(5) applies to such amounts).

"(2) LIMITATION OF TAX.—In any case to which this subsection applies, the tax attributable to the amounts to which this subsection applies for the taxable year in which such amounts are received shall not exceed whichever of the following is the greater:

"(A) 5 times the increase in tax which would result from the inclusion in gross income of the recipient of 20 percent of so much of the amount so received as is includible in gross income, or

"(B) 5 times the increase in tax which would result if the taxable income of the recipient for such taxable year equaled 20 percent of the amount of the taxable income of the recipient for such taxable year determined under paragraph (3) (A).

"(3) DETERMINATION OF TAXABLE INCOME.—Notwithstanding section 63 (relating to definition of taxable income), for purposes only of computing the tax under this chapter attributable to amounts to which this subsection or subsection (m)(5) applies and which are includible in gross income—

"(A) the taxable income of the recipient for the taxable year of receipt shall be treated as being not less than the amount by which (i) the aggregate of such amounts so includible in gross income exceeds (ii) the amount of the deductions allowed for such taxable year under section 151 (relating to deductions for personal exemptions); and

"(B) in making ratable inclusion computations under paragraph (5) (B) of subsection (m), the taxable income of the recipient for each taxable year involved in such ratable inclusion shall be treated as being not less than the amount required by such paragraph (5) (B) to be treated as includible in gross income for such taxable year.

In any case in which the preceding sentence results in an increase in taxable income for any taxable year, the resulting increase in the taxes imposed by section 1 or 3 for such taxable year shall not be reduced by any credit under part IV of subchapter A (other than section 31 thereof) which, but for this sentence, would be allowable.

"(c) CAPITAL GAINS TREATMENT OF CERTAIN EMPLOYEES' TRUSTS DISTRIBUTIONS.—Section 402(a)(2) of the Internal Revenue Code of 1954 (relating to capital gains treatment for certain distributions) is amended by adding at the end thereof the following new sentence: "This paragraph shall not apply to distributions paid to any distributee to the extent such distributions are attributable to contributions made on behalf of the employee while he was an employee within the meaning of section 401(c)(1)."

"(d) CAPITAL GAINS TREATMENT OF CERTAIN EMPLOYEES' ANNUITY PAYMENTS.—Section 403(a) of the Internal Revenue Code of 1954 (relating to taxability of a beneficiary under a qualified annuity plan) is amended—

"(1) by striking out in paragraph (2) (A) (i) "which meets the requirements of section 401(a)(3), (4), (5), and (6)" and inserting in lieu thereof "described in paragraph (1)";

"(2) by adding at the end of paragraph (2) (A) the following new sentence: "This subparagraph shall not apply to amounts paid to any payee to the extent such amounts are attributable to contributions made on behalf of the employee while he was an employee within the meaning of section 401(c)(1)."; and

"(3) by adding after paragraph (2) the following new paragraph:

"(3) SELF-EMPLOYED INDIVIDUALS.—For purposes of this subsection, the term "employee" includes an individual who is an employee within the meaning of section 401(c)(1), and the employer of such individual is the person treated as his employer under section 401(c)(4)."

"SEC. 30. PLANS FOR PURCHASE OF UNITED STATES BONDS.

"(a) QUALIFIED BOND PURCHASE PLANS.—Part I of subchapter D of chapter 1 of the Internal Revenue Code of 1954 (relating to deferred compensation, etc.) is amended by adding at the end thereof the following new section:

"SEC. 405 QUALIFIED BOND PURCHASE PLANS.

"(a) REQUIREMENTS FOR QUALIFICATION.—A plan of an employer for the purchase for and distribution to his employees or their beneficiaries of United States bonds described in subsection (b) shall constitute a qualified bond purchase plan under this section if—

"(1) the plan meets the requirements of section 401(a)(3), (4), (5), (6), (7), and (8) and, if applicable, the requirements of section 401(a)(9) and (10) and of section 401(d) (other than paragraphs (1), (5)(B), and (8)); and

"(2) contributions under the plan are used solely to purchase for employees or their beneficiaries United States bonds described in subsection (b).

"(b) BONDS TO WHICH APPLICABLE.—

"(1) CHARACTERISTICS OF BONDS.—This section shall apply only to a bond issued under the Second Liberty Bond Act, as amended, which by its terms, or by regulations prescribed by the Secretary under such Act—

"(A) provides for payment of interest, or investment yield, only upon redemption;

"(B) may be purchased only in the name of an individual;

"(C) ceases to bear interest, or provide investment yield, not later than 5 years after the death of the individual in whose name it is purchased;

"(D) may be redeemed before the death of the individual in whose name it is purchased only if such individual—

"(i) has attained the age of 59½ years, or

"(ii) has become disabled (within the meaning of section 213(g)(3)); and

"(E) is nontransferable.

"(2) MUST BE PURCHASED IN NAME OF EMPLOYEE.—This section shall apply to a bond described in paragraph (1) only if it is purchased in the name of the employee.

"(c) DEDUCTION FOR CONTRIBUTIONS TO BOND PURCHASE PLANS.—Contributions paid by an employer to or under a qualified bond purchase plan shall be allowed as a deduction in an amount determined under section 404 in the same manner and to the same extent as if such contributions were made to a trust described in section 401(a) which is exempt from tax under section 501(a).

"(d) TAXABILITY OF BENEFICIARY OF QUALIFIED BOND PURCHASE PLAN.—

"(1) GROSS INCOME NOT TO INCLUDE BONDS AT TIME OF DISTRIBUTION.—For purposes of this chapter, in the case of a distributee of a bond described in subsection (b) under a qualified bond purchase plan, or from a trust described in section 401(a) which is exempt from tax under section 501(a), gross income does not include any amount attributable to the receipt of such bond. Upon redemption of such bond, the proceeds shall be subject to taxation under this chapter, but the provisions of section 72 (relating to annuities, etc.) and section 1232 (relating to bonds and other evidences of indebtedness) shall not apply.

"(2) BASIS.—The basis of any bond received by a distributee under a qualified bond purchase plan—

"(A) if such bond is distributed to an employee, or with respect to an employee, who at the time of purchase of the bond, was an employee other than an employee within the meaning of section 401(c)(1), shall be the amount of the contributions by the employee which were used to purchase the bond, and

"(B) if such bond is distributed to an employee, or with respect to an employee, who, at the time of purchase of the bond, was an employee within the meaning of section 401(c)(1), shall be the amount of the contributions used to purchase the bond which were made on behalf of such employee and were not allowed as a deduction under subsection (c).

The basis of any bond described in subsection (b) received by a distributee from a trust described in section 401(a) which is exempt from tax under section 501(a) shall be determined under regulations prescribed by the Secretary or his delegate.

"(e) CAPITAL GAINS TREATMENT NOT TO APPLY TO BONDS DISTRIBUTED BY TRUSTS.—Section 402(a)(2) shall not apply to any bond described in subsection (b) distributed to any distributee and, for purposes of applying such section, any such bond distributed to any distributee and any such bond to the credit of any employee shall not be taken into account.

"(f) EMPLOYEE DEFINED.—For purposes of this section, the term "employee" includes an individual who is an employee within the meaning of section 401(c)(1), and the employer of such individual shall be the person treated as his employer under section 401(c)(4).

"(g) PROOF OF PURCHASE.—At the time of purchase of any bond to which this section applies, proof of such purchase shall be furnished in such form as will enable the purchaser, and the employee in whose name such bond is purchased, to comply with the provisions of this section.

"(h) REGULATIONS.—The Secretary or his delegate shall prescribe such regulations as may be necessary to carry out the provisions of this section."

"(b) CLERICAL AMENDMENT.—The table of sections for such part is amended by adding at the end thereof the following new item:

"Sec. 405. Qualified bond purchase plans."

"SEC. 31. PROHIBITED TRANSACTIONS.

"Section 503 of the Internal Revenue Code of 1954 (relating to prohibited transactions) is amended by adding at the end thereof the following new subsection:

"(j) TRUSTS BENEFITING CERTAIN OWNER-EMPLOYEES.—

"(1) PROHIBITED TRANSACTIONS.—In the case of a trust described in section 401(a) which is part of a plan providing contributions or benefits for employees some or all of whom are owner-employees (as defined in section 401(c)(3)) who control (within the meaning of section 401(d)(9)(B), determined with the application of section 401(c)(5)) the trade or business with respect to which the plan is established, the term "prohibited transaction" also means any transaction in which such trust, directly or indirectly—

"(A) lends any part of the corpus or income of the trust to;

"(B) pays any compensation for personal services rendered to the trust to;

"(C) makes any part of its services available on a preferential basis to; or

"(D) acquires for the trust any property from, or sells any property to;

any person described in subsection (c) or to any such owner-employee, a member of the family (as defined in section 267(c)(4)) of any such owner-employee, or a corporation controlled by any such owner-employee through the ownership, directly or indirectly, of 50 percent or more of the total combined voting power of all classes of stock entitled to vote or 50 percent or more of the total value of shares of all classes of stock of the corporation.

"(2) SPECIAL RULE FOR LOANS.—For purposes of the application of paragraph (1) (A), the following rules shall apply with respect to a loan made before the date of the enactment of this subsection which would

be a prohibited transaction if made in a taxable year beginning after December 31, 1961:

"(A) If any part of the loan is repayable prior to December 31, 1964, the renewal of such part of the loan for a period not extending beyond December 31, 1964, on the same terms, shall not be considered a prohibited transaction.

"(B) If the loan is repayable on demand, the continuation of the loan beyond December 31, 1964, shall be considered a prohibited transaction."

"SEC. 32. OTHER SPECIAL RULES, TECHNICAL CHANGES, AND ADMINISTRATIVE PROVISIONS

"(a) RETIREMENT INCOME CREDIT.—Section 37(c)(1) of the Internal Revenue Code of 1954 (relating to definition of retirement income) is amended—

"(1) by striking out subparagraph (A) and inserting in lieu thereof the following:

"(A) pensions and annuities (including, in the case of an individual who is, or has been, an employee within the meaning of section 401(c)(1), distributions by a trust described in section 401(a) which is exempt from tax under section 501(a)); and

"(2) by striking out 'and' at the end of subparagraph (C), by striking out 'or' at the end of subparagraph (D) and inserting in lieu thereof 'and', and by adding after subparagraph (D) the following new subparagraph:

"(E) bonds described in section 405(b)(1) which are received under a qualified bond purchase plan described in section 405(a) or in a distribution from a trust described in section 401(a) which is exempt from tax under section 501(a), or."

"(b) ADJUSTED GROSS INCOME.—Section 62 of the Internal Revenue Code of 1954 (relating to the definition of adjusted gross income) is amended by inserting after paragraph (6) the following new paragraph:

"(7) PENSION, PROFIT-SHARING, ANNUITY, AND BOND PURCHASE PLANS OF SELF-EMPLOYED INDIVIDUALS.—In the case of an individual who is an employee within the meaning of section 401(c)(1), the deductions allowed by section 404 and section 405(c) to the extent attributable to contributions made on behalf of such individual."

"(c) DEATH BENEFITS.—Section 101(b) of the Internal Revenue Code of 1954 (relating to employees' death benefits) is amended—

"(1) by striking out clause (ii) of paragraph (2)(B) and inserting in lieu thereof the following:

"(ii) under an annuity contract under a plan described in section 403(a), or; and

"(2) by adding at the end thereof the following new paragraph:

"(3) SELF-EMPLOYED INDIVIDUAL NOT CONSIDERED AN EMPLOYEE.—For purposes of this subsection, the term "employee" does not include an individual who is an employee within the meaning of section 401(c)(1) (relating to self-employed individuals)."

"(d) AMOUNTS RECEIVED THROUGH ACCIDENT OR HEALTH INSURANCE.—Section 104(a) of the Internal Revenue Code of 1954 (relating to compensation for injuries or sickness) is amended by adding at the end thereof the following new sentence: 'For purposes of paragraph (3), in the case of an individual who is, or has been, an employee within the meaning of section 401(c)(1) (relating to self-employed individuals), contributions made on behalf of such individual while he was such an employee to a trust described in section 401(a) which is exempt from tax under section 501(a), or under a plan described in section 403(a), shall, to the extent allowed as deductions under section 404, be treated as contributions by the employer which were not includible in the gross income of the employee.'

"(e) AMOUNTS RECEIVED UNDER ACCIDENT AND HEALTH PLANS.—Section 105 of the In-

ternal Revenue Code of 1954 (relating to amounts received under accident and health plans) is amended by adding at the end thereof the following new subsection:

"(g) SELF-EMPLOYED INDIVIDUAL NOT CONSIDERED AN EMPLOYEE.—For purposes of this section, the term "employee" does not include an individual who is an employee within the meaning of section 401(c)(1) (relating to self-employed individuals)."

"(f) NET OPERATING LOSS DEDUCTION.—Section 172(d)(4) of the Internal Revenue Code of 1954 (relating to nonbusiness deductions of taxpayers other than corporations) is amended—

"(1) by striking out 'and' at the end of subparagraph (B);

"(2) by striking out the period at the end of subparagraph (C) and inserting '; and'; and

"(3) by adding after subparagraph (C) the following new subparagraph:

"(D) any deduction allowed under section 404 or section 405(c) to the extent attributable to contributions which are made on behalf of an individual who is an employee within the meaning of section 401(c)(1) shall not be treated as attributable to the trade or business of such individual."

"(g) CERTAIN LIFE INSURANCE RESERVES.—Section 805(d)(1) of the Internal Revenue Code of 1954 (relating to pension plan reserves) is amended—

"(1) by striking out in subparagraph (B) 'meeting the requirements of section 401(a)(3), (4), (5), and (6) or' and inserting in lieu thereof 'described in section 403(a), or plans meeting'; and

"(2) by striking out in subparagraph (C) 'and (6)' and inserting in lieu thereof '(6), (7), and (8)'. "

"(h) UNINCORPORATED BUSINESSES ELECTING TO BE TAXED AS CORPORATIONS.—Section 1361(d) of the Internal Revenue Code of 1954 (relating to unincorporated business enterprises electing to be taxed as domestic corporations) is amended by inserting before the period at the end thereof the following: 'other than an employee within the meaning of section 401(c)(1) (relating to self-employed individuals), or for purposes of section 405 (relating to qualified bond purchase plans) other than an employee described in section 405(f)'. "

"(i) ESTATE TAX EXEMPTION OF EMPLOYEES' ANNUITIES.—Section 2039 of the Internal Revenue Code of 1954 (relating to exemption from the gross estate of annuities under certain trusts and plans) is amended—

"(1) by striking out in subsections (e)(2) 'met the requirements of section 401(a)(3), (4), (5), and (6)' and inserting 'was a plan described in section 403(a)'; and

"(2) by adding at the end of subsection (c) the following new sentence: 'For purposes of this subsection, contributions or payments on behalf of the decedent while he was an employee within the meaning of section 401(c)(1) made under a trust or plan described in paragraph (1) or (2) shall be considered to be contributions or payments made by the decedent.' "

"(j) GIFT TAX EXEMPTION OF EMPLOYEES' ANNUITIES.—Section 2517 of the Internal Revenue Code of 1954 (relating to exclusion from gift tax in case of certain annuities under qualified plans) is amended—

"(1) by striking out in subsection (a)(2) 'met the requirements of section 401(a)(3), (4), (5), and (6)' and inserting in lieu thereof 'was a plan described in section 403(a)'; and

"(2) by adding at the end of subsection (b) the following new sentence: 'For purposes of this subsection, payments or contributions on behalf of an individual while he was an employee within the meaning of section 401(c)(1) made under a trust or plan described in subsection (a)(1) or (2) shall be considered to be payments or contributions made by the employee.'

"(k) FEDERAL UNEMPLOYMENT TAX ACT.—Section 3306(b)(5) of the Internal Revenue Code of 1954 (relating to definition of wages) is amended by striking out subparagraph (B) and inserting in lieu thereof the following new subparagraphs:

"(B) under or to an annuity plan which, at the time of such payment, is a plan described in section 403(a), or

"(C) under or to a bond purchase plan which, at the time of such payment, is a qualified bond purchase plan described in section 405(a)."

"(1) WITHHOLDING OF INCOME TAX.—Section 3401(a)(12) of the Internal Revenue Code of 1954 (relating to definition of wages) is amended by striking out subparagraph (B) and inserting in lieu thereof the following new subparagraphs:

"(B) under or to an annuity plan, which, at the time of such payment, is a plan described in section 403(a); or

"(C) under or to a bond purchase plan which, at the time of such payment, is a qualified bond purchase plan described in section 405(a)."

"(m) INFORMATION REQUIREMENTS.—

"(1) IN GENERAL.—Subpart B of part III of subchapter A of chapter 61 of the Internal Revenue Code of 1954 (relating to information concerning transactions with other persons) is amended by adding at the end thereof the following new section:

"SEC. 6047. INFORMATION RELATING TO CERTAIN TRUSTS AND ANNUITY AND BOND PURCHASE PLANS.

"(a) TRUSTEES AND INSURANCE COMPANIES.—The trustee of a trust described in section 401(a) which is exempt from tax under section 501(a) to which contributions have been paid under a plan on behalf of any owner-employee (as defined in section 401(c)(3)), and each insurance company or other person which is the issuer of a contract purchased by such a trust, or purchased under a plan described in section 403(a), contributions for which have been paid on behalf of any owner-employee, shall file such returns (in such form and at such times), keep such records, make such identification of contracts and funds (and accounts within such funds), and supply such information, as the Secretary or his delegate shall by forms or regulations prescribe.

"(b) OWNER-EMPLOYEES.—Every individual on whose behalf contributions have been paid as an owner-employee (as defined in section 401(c)(3))—

"(1) to a trust described in section 401(a) which is exempt from tax under section 501(a), or

"(2) to an insurance company or other person under a plan described in section 403(a),

shall furnish the trustee, insurance company, or other person, as the case may be, such information at such times and in such form and manner as the Secretary or his delegate shall prescribe by forms or regulations.

"(c) EMPLOYEES UNDER QUALIFIED BOND PURCHASE PLANS.—Every individual in whose name a bond described in section 405(b)(1) is purchased by his employer under a qualified bond purchase plan described in section 405(a), or by a trust described in section 401(a) which is exempt from tax under section 501(a), shall furnish—

"(1) to his employer or to such trust, and

"(2) to the Secretary (or to such person as the Secretary may by regulations prescribe),

such information as the Secretary or his delegate shall by forms or regulations prescribe.

"(d) CROSS REFERENCE.—

"For criminal penalty for furnishing fraudulent information, see section 7207."

"(2) CLERICAL AMENDMENT.—The table of sections for such subpart B is amended by adding at the end thereof the following:

"Sec. 6047. Information relating to certain trusts and annuity and bond purchase plans."

"(3) PENALTY.—Section 7207 of the Internal Revenue Code of 1954 (relating to fraudulent returns, statements, or other documents) is amended by adding at the end thereof the following new sentence: 'Any person required pursuant to section 6047 (b) or (c) to furnish any information to the Secretary or any other person who willfully furnishes to the Secretary or such other person any information known by him to be fraudulent or to be false as to any material matter shall be fined not more than \$1,000, or imprisoned not more than 1 year, or both.'

"SEC. 33. EFFECTIVE DATE.

"The amendments made by this Act shall apply to taxable years beginning after July 31, 1963."

On page 391, line 22, strike out "27" and insert in lieu thereof "28".

Mr. DIRKSEN. Mr. President, the amendments have been modified from the printed form in one respect. As first submitted, the effective date was to be December 31, 1961. That has been modified to July 1, 1963.

Mr. MANSFIELD. Mr. President, I should like to renew the unanimous-consent request to the effect that there be 1½ hours allocated to the consideration of the amendments, 1 hour to be under the control of the distinguished minority leader and one-half hour to be under the control of the Senator from Montana.

Mr. CURTIS. Mr. President, reserving the right to object, the Senator from Nebraska will offer an amendment to the amendments offered by the distinguished minority leader, the Senator from Illinois [Mr. DIRKSEN]. What was the intent in reference to that?

Mr. MANSFIELD. I meant to limit debate on the amendment and amendments thereto.

We are trying to be reasonable as to the amount of time, because, as I have indicated, I will make a motion to table, and that is in order at any time.

Mr. CURTIS. Not a great deal of time would be desired, but I would want an assurance of having a short time to state the amendment. Whether it is voted on before the motion to table or after does not matter.

Mr. MANSFIELD. I am sure we could arrange that.

Mr. DIRKSEN. Yes. Time can be granted from the 1 hour.

Mr. CURTIS. Ten minutes would be satisfactory.

Mr. DIRKSEN. I have only one other request, for 15 minutes.

Mr. CURTIS. Ten minutes would be satisfactory.

Mr. DIRKSEN. I will take about 10 minutes.

Mr. CURTIS. I have no objection.

The PRESIDING OFFICER. Is there objection to the request by the Senator from Montana? The Chair hears none, and it is so ordered.

Mr. MANSFIELD. Mr. President, the agreement is on the motion to table only.

Mr. DIRKSEN. Mr. President, there is no occasion for me to labor the proposal very long. I think merely to recite the history pretty well states the case. Actually, bills substantially like H.R. 10

have been before the House and Senate for the past 11 years.

Mr. MANSFIELD. Mr. President, with the concurrence of the distinguished minority leader, I should like to change the time of the agreement entered into by the Senate from "an hour and a half" to "not exceeding an hour and a half."

The PRESIDING OFFICER. Without objection, it is so ordered.

Mr. MANSFIELD. I thank the Senator from Illinois.

Mr. DIRKSEN. Mr. President, as I indicated, this is not a new question before the Congress. The first bill on this subject was introduced in 1951, and there have been at least six or more measures comparable and similar to H.R. 10 which have been considered at one time or another either by the House or the Senate, or by the Senate Finance Committee or the House Committee on Ways and Means.

I believe the first bill passed the House on July 29, 1958, but there was no action taken in the Senate. The bill passed the House again in the 87th Congress.

In the first instance, when the first bill was passed by the House, in 1958, in the 85th Congress, it was approved by the Senate Finance Committee by a vote of 12 to 5.

The measure now before the Senate was approved by the Finance Committee August 25, 1961, by a vote of 14 to 3, and the bill has been on the Senate Calendar since September of last year. That means the bill has been on the calendar for nearly a year.

At this point I wish to pay my respects to, and to salute the distinguished Senator from Florida [Mr. SMATHERS], who has labored so long and earnestly with the measure. He is entitled to full credit, because what is before the Senate is really the so-called Keogh-Smathers bill, named after Representative KEOGH, of New York, and the distinguished Senator from Florida.

The purpose of the measure and the reason therefor are thoroughly set out in the report on the bill.

In 1942 legislation to encourage the establishment of pension funds was first enacted by the Congress for the benefit of people who operate in business and industry. I understand that 66,000 pension plans have been filed and are now in effect, covering approximately 20 million people, and that nearly a million people are added to those plans every year. If one adds to the private pension plans the plans for State officials and employees of local governments, for the Army, for the civil service, for railroad retirement, and so forth, an estimated 30 million people now receive benefits under a private plan or a public plan of some kind.

In addition, of course, there is social security.

But it seems that there has been one group in the country which has been forgotten. Those are the self-employed, which includes professional people—doctors, lawyers, small businessmen, farmers, and a great many others.

I could read a statement with respect to what the measure contains. The

principle is very simple. In the case of the self-employed, they have the dual character of employer and employee, in order to carry out a principle that has been established in law. As the bill now recites, the entire amount of the first \$1,000 that would be trusted could be deducted and would be deductible for tax purposes. Of the remaining \$1,500—since \$2,500 is the limit—50 percent could be deducted, so the top would be \$1,700, and \$50 a year, which could be actually trusted. It would become available at a given retirement date. When it would become available then, of course, it would become taxable.

I set out a statement in the RECORD on September 27, 1961, which contains an analysis of the bill. It is brief but sufficiently complete. Mr. President, I ask unanimous consent that the statement be printed at this point in my remarks.

There being no objection, the statement was ordered to be printed in the RECORD, as follows:

STATEMENT BY SENATOR DIRKSEN

ESTABLISHMENT OF VOLUNTARY PENSION PLANS
BY SELF-EMPLOYED INDIVIDUALS

For the past 10 years I have followed with considerable interest H.R. 10, a bill to encourage the establishment of voluntary pension plans by self-employed individuals. I have long been in favor of the principle of this legislation, but on several occasions during the course of this 10-year period I found it necessary to differ with the proponents as to the method of achieving their goal. Today I am pleased to say that I wholeheartedly endorse H.R. 10 as reported by the Senate Finance Committee. The features which I found objectionable in the past have either been eliminated or changed to the point where I can, in all good conscience, embrace this legislation.

Practically everyone who is acquainted with this subject will agree that the principle of this legislation as now proposed is sound. Certainly the Members of the House recognized this in the 85th and 86th Congresses and again in this session when they passed H.R. 10 by a practically unanimous vote. Certainly the members of the Senate Finance Committee in the 86th Congress recognized this when, after extensive hearings, they approved H.R. 10 by a 12 to 5 vote. On August 25 of this year, this committee ordered H.R. 10 favorably reported 14 to 3.

It was apparent to me, after reading the minority views in the Senate Finance Committee report, that a number of misconceptions still exist in the minds of two of my distinguished colleagues. Their proposals were heard and voted down by the committee in the 86th Congress and again this year. I am confident that the proponents of this legislation will, on the floor of this Congress, meet these arguments again and in such a way as to gain the overwhelming support of this body. Rather than criticize, I wish to commend the spokesmen for the various national self-employed groups because, to the best of my knowledge, at no time have they said, "If you won't give us these benefits, then we wish to have them taken away from the corporate employees."

This is a good bill and for a number of reasons, one of which is the fact that it encourages people to help themselves. It encourages initiative, self-reliance, and the other quantities which helped to make this country great, but qualities, which I regret to say, are disappearing rapidly from the American scene. This Congress has an opportunity to resurrect these attributes which

are so desperately needed by our country at this time by enacting H.R. 10 into law.

This remedial legislation is designed to correct an inequity in our tax structure which prevents this Nation's 10 million small business, farm, and professional people from receiving treatment comparable to that which is accorded corporate employees.

The impetus for the steady growth in corporate coverage was supplied in 1942 by the 77th Congress when it wisely enacted legislation which encouraged corporations to promote the economic well-being and future security of their employees. One has only to look at the increase which has occurred since 1940 to appreciate the soundness of this legislation. In that year 4.1 million were covered; in 1950, 9.8 million; and in 1960 the figure rose to 20 million. Approximately 1 million people are being added each year to private pension plans.

When we add to the 1960 total the approximately 8 million covered by State and local government plans, civil service, armed services, railroad retirement systems, etc., the total number of Americans covered by pension plans is approximately 30 million people.

H.R. 10 does not, as its few opponents would have you believe; broaden a tax loophole, and open a Pandora's box, but rather extends what has been proven over the past 19 years to be sound legislation to the point where it includes a dedicated, courageous group of Americans, the self-employed.

To accomplish this, self-employed persons are treated for retirement plan purposes as the employers of themselves. This was the fundamental concept of the House bill and it is retained in the Senate Finance Committee's substitute. As employers, self-employed individuals are permitted, like other employers, to deduct contributions (within specified limits) made to pension or profit-sharing plans for the benefit of themselves and such other employees as may be covered under the plan. Under the committee bill, a self-employed person would be permitted to contribute to a retirement plan 10 percent of his earned income or \$2,500, whichever is the lesser. He would be permitted to deduct 100 percent of the first \$1,000 contributed and 50 percent of the remaining \$1,500, which may be contributed. The maximum deductible amount would be \$1,750.

As employees, as with other employees, they are not taxed on such contributions made for their benefit, or the income thereon, until they receive the funds upon retirement or otherwise.

The committee changes have drastically reduced the size of the revenue deferral, in fact to a point where this can no longer be used as a major argument against this measure. Oh, I am not deluding myself, because there will be some who will cry economy, who will use the international situation as an excuse for opposing this bill; but these few, time and time again have, and will continue, to support domestic programs with high price tags and questionable dollar value.

The estimates for H.R. 10 range from less than \$100 million to \$200 million. In view of the actual experience in other countries, Great Britain, Canada, and New Zealand; and the fact that the Treasury Department generally overestimates, I am inclined to accept the lower figure.

Regardless of the exact amount, I wish to remind you that the potential revenue deferral is already made possible in the present tax law since the establishment of tax-deferred pension plans is available to any self-employed person who incorporates his business or occupation.

If we fail to act in this Congress, we will, I am certain, force a great many of this

Nation's self-employed to incorporate and in most cases solely for the purpose of gaining tax treatment relative to their retirement savings similar to that which is offered their corporate brethren. Passage of H.R. 10 will encourage these fine, hard-working Americans to retain their self-employed status, defeat will be a major blow to them and an invitation to incorporate for tax advantage because of their national desire to protect themselves in their later years. Now I don't believe we can afford the loss of too many more self-employed without jeopardizing the position of this country both on the domestic and international fronts.

H.R. 10 is a good bill, it is a just bill. I urge my colleagues on both sides of the aisle to join with me in working for the early enactment of H.R. 10 in the 2d session of the 87th Congress.

Mr. DIRKSEN. I think there are only two other things I care to say.

First, since we have pending a tax bill, the amendment obviously is completely germane to the subject matter of the bill under consideration. The so-called H.R. 10 is a tax measure. Therefore it is rightly before the Senate at the present time.

I should like to read into the record a statement made by the President of the United States when he was a Member of the Senate. This statement was made in January of 1960, and came in an answer to an inquiry as to his position on what was then known as the Simpson-Keogh bill, named after Representative Simpson of Pennsylvania and Representative Keogh of New York. The statement appears in volume 107, No. 67, April 20, 1961, of the CONGRESSIONAL RECORD. At that time the President said:

I am myself disposed to support the type of provisions which are contained in the Simpson-Keogh bill. I personally feel that there has been ample testimony from many sources over a long period of time in both Houses and that it is time to take floor action on this legislation. * * * I hope that it will be acted upon favorably during this Congress.

I now read into the record one other statement of the President, which was made prior to November 1960. The distinguished President wired the following message to the American Thrift Assembly:

Thank you for providing me with an opportunity to comment upon the proposal to amend the Revenue Act to permit small businessmen, farmers and self-employed people to make provisions for their retirement with the same tax advantages now possessed by corporate employees. As you know, this proposal has been before the Congress for 9 years. During that time extensive hearings have been held. Committee reports have been filed and the original proposal has undergone considerable modification to meet objections against it. These objections now seem to have been overcome, for the Treasury reports there will be little loss of tax revenues. The objectives of encouraging thrift and independence in retirement have my wholehearted support. I am particularly pleased that it is planned to eliminate the discrimination against employees and permit them to participate in pension plans.

Mr. President, I know of nothing else that I need add to the cause, for in the past 11 years the subject has insinuated

itself into the mind of every Senator. Senators know what it is about. I am now prepared to yield the floor. I think my distinguished friend from Florida [Mr. SMATHERS], who deserves all the credit for the work done on the bill, and who was the coauthor along with Representative KEOGH, may now wish to address himself to the Senate.

Mr. SMATHERS. Mr. President, will the Senator yield me 2 minutes?

Mr. KERR. Mr. President, I yield 5 minutes to the Senator from Florida.

Mr. SMATHERS. Mr. President, I am grateful to the able Senator from Illinois [Mr. DIRKSEN], the minority leader, for his very kind references to me. I know of his great interest in the proposal. I, like him and many others, feel that it is a most meritorious, worthwhile, and long overdue piece of proposed legislation.

I understand that the majority leader, the distinguished Senator from Montana [Mr. MANSFIELD], will later today make a motion to table the amendment. At that time I shall have several questions to put to the majority leader and I will elaborate a bit further on my feelings with respect to H.R. 10. I am grateful to the very able minority leader and congratulate him for having made the move. I had a similar amendment prepared which I also intended to propose to the pending bill. Had he not brought his amendment up, I would have brought mine up. His offer of the amendment at the present time brings the subject to a head and, as a result of his having offered the amendment, I now feel completely confident that there will be an opportunity to discuss rather fully the merits of H.R. 10 as reported by the Senate Finance Committee. But most important of all, I am satisfied that we shall now be able to get a vote on the measure. I commend the Senator, and I thank him. I will have more to say a little later.

Mr. PASTORE. Mr. President, will the Senator give us a brief explanation of what the amendment would do?

Mr. SMATHERS. A brief explanation of the amendment is as follows: It would provide for self-employed people, such as doctors, lawyers, accountants, real estate people, barbers, farmers, and small businessmen, the opportunity to set aside certain sums of money not to exceed \$2,500, or 10 percent of their income, whichever is the lesser, in an approved retirement program to take care of themselves in their retirement years. Benefits under such program may not begin before age 59½, except in case of disability or death, nor later than age 70½.

They are not permitted to deduct the entire amount contributed under the plan. The first \$1,000 contributed and 50 percent of the contribution in excess of this amount is deductible. This means that an owner-employee who makes the maximum annual contribution of \$2,500 may only deduct \$1,750 of that amount.

We say this proposal is long overdue, because since 1941, under laws passed by Congress, we have authorized the setting up of retirement and pension programs for large corporations. Today there are

perhaps 60 million people who are covered by these pension programs which are much more generous than the self-employed provisions which we are proposing. Many of the corporations set up programs theoretically for all of their employees, and all of that money contributed by the corporation is deductible. The self-employed under the proposed amendment have only a tax deferral. They will be taxed when they derive their benefits under the approved plan.

Mr. PASTORE. Mr. President, will the Senator yield?

Mr. SMATHERS. I yield.

Mr. PASTORE. Must the individual retire?

The PRESIDING OFFICER. The time of the Senator has expired.

Mr. KERR. I yield 3 additional minutes to the Senator from Florida.

Mr. SMATHERS. Not necessarily. If he is to avail himself of the retirement program he must begin to draw benefits sometime between the ages of 59½ and 70½.

Mr. PASTORE. He must retire, under the law?

Mr. SMATHERS. Ordinarily he will retire. The proposal does not permit him to defer receipt of this money indefinitely. No retirement test is provided by the bill because of the difficulty of determining when a self-employed person has retired. In any event, the retirement program does go into effect at age 70½. It is not merely left to his estate as a tax-free amount of money to be passed on to his heirs.

Mr. PASTORE. What if he does not retire?

Mr. SMATHERS. Then he just continues to work and the program continues and just stays in effect. He is eventually taxed on what he receives under the plan at ordinary income tax rates.

Mr. PASTORE. As it would have been in the beginning?

Mr. SMATHERS. As it would be at the moment. That is the big advantage, I might say. There is no question that there is an advantage in a person doing it, because usually he is in a lower income bracket when he is 65 or 67 and retires than he is when he is earning the money. There is no question that that gives him some advantage. However, we say there are already 60 million people who are enjoying the privilege today. The self-employed have not thus far been able to take advantage of the corporate pension programs. We are attempting to bring equity to these 7½ million people who have not been able to set up a retirement program for themselves.

Mr. PASTORE. I should like to clear up one point. The Senator said that a person must retire in order to receive this money. Then the Senator has said that if the person continues to work he can still get the money.

Mr. SMATHERS. He is not required to retire. What I meant was that he cannot have it both ways. We say if he continues to work he must begin to draw benefits before he is age 70½.

Mr. PASTORE. At the prevailing rate of interest?

Mr. SMATHERS. Yes.

Mr. CURTIS. Mr. President, will the Senator yield?

Mr. SMATHERS. I yield.

Mr. CURTIS. I believe the distinguished Senator from Rhode Island will be interested in this fact. Under the amendment the self-employed person must set up a program for his employees. He cannot merely qualify himself. The self-employed person—the operator of an unincorporated business or a professional man—must substantially meet the same requirements that the corporate pension plan requires. There they must cover every employee, and the officers cannot be covered alone.

The PRESIDING OFFICER. The time of the Senator has again expired.

Mr. KERR. I yield 3 additional minutes to the Senator from Florida.

Mr. PASTORE. Will the Senator from Nebraska be a little more specific? If a doctor has three nurses, he cannot set up a plan for himself without setting up the plan for his three nurses as well. Is that correct?

Mr. CURTIS. That is correct. Just as our great corporations cannot set up retirement plans to cover the officers only. There are provisions, however, that they can classify employees and cover their regular employees as contrasted with the casual employees.

Mr. PASTORE. How does that work? Let us assume that a doctor has three nurses. Do we say he can deduct up to a thousand dollars and then take one-half of the remaining \$1,500? What does he do about the other employees, in other words?

Mr. CURTIS. He has to pay. First of all, he has to have a plan that is approved.

Mr. PASTORE. Approved by whom?

Mr. SMATHERS. I appreciate the Senator from Nebraska making that clear. Each one of these plans must be approved by the Treasury of the United States.

Mr. PASTORE. In other words, if a lawyer has a stenographer or secretary, he must provide for her as well. Is that correct?

Mr. SMATHERS. He must. He must provide for her on what we call a non-discriminatory basis. He cannot set up a generous proposal for himself and a less generous proposal for his employees. There must be the same ratio.

Mr. PASTORE. Where does the money come from to set up the fund for the benefits that are made available?

Mr. SMATHERS. From the employer.

Mr. PASTORE. From his own personal income?

Mr. CURTIS. From his business income.

Mr. SMATHERS. He is permitted to deduct it.

Mr. CURTIS. The employer pays it.

Mr. SMATHERS. When the employer puts the money into the fund for his employees from his business, he is permitted to deduct the amount of money to take care of his employees. There are large corporations which are permitted to deduct the amount of money which they put into a fund to take care of all

their employees. The same thing would be true in this case.

Mr. PASTORE. It would be a business expense?

Mr. SMATHERS. It would be a business expense, Mr. President, I will have more to say about this matter later in the coming days—and I hope there will not be too many of them—and this measure will be rather well explored.

I now yield the floor.

Mr. DIRKSEN. Mr. President, I yield 5 minutes to the distinguished Senator from Nebraska.

Mr. CURTIS. Mr. President, I thank the distinguished Senator from Illinois. If I may have the attention of the proponents of the amendment, I wish to say that I have long favored the principle involved in it. Many years ago, as a member of the Ways and Means Committee, I made the motion that we hold what were the first hearings on the principle involved here.

A great inequity exists throughout the country. The corporate entities can set up pension plans for their officers and for their employees. The money which goes into these pension plans goes into them before taxes. The income that the pension fund earns is not taxed. An individual who is in some kind of business—be he a grocer, or doctor, or dentist, or farmer, or lawyer—pays taxes and must save for his old age after taxes. Then when he puts his savings aside, if it earns income, he is taxed again. So we have one group that sets aside money before taxes, and the tax is paid when the benefits are paid later. Another group has two handicaps. We cannot go on like that. The corporate plans are increasing rapidly. No one is suggesting that they be abolished or that the tax benefits that may be applicable to them should be repealed. The answer is that we must equalize it and extend it to others. The requirement of putting 10 percent of income aside—or up to \$2,500, or \$1,750, as now—is quite rigid.

There is the trustee plan, for example, which projects itself for some distance into the future; or an insurance contract must be entered into; and all employees must be covered in both instances. In a trustee plan it is permissible to use Government bonds.

But if we adopt the Dirksen amendment, there will still be millions of people throughout the country who will not be covered by a corporate plan and will never be able to set up a plan under H.R. 10. Legally, they are permitted to do so, but practically they cannot. Some of them may be 57 or 58 years old now. Some of them have a business which is uncertain, and they cannot enter into an insurance contract to provide themselves and their employees with any degree of certainty. Their business is so small that they cannot go to the expense of having a plan drafted and submitted to the Internal Revenue Service and approved and carried out. Yet those people, if they save anything for their old age, will have to do so after taxes, and their savings will be taxed.

My amendment to the Dirksen amendment would not in any sense take away any of the rights and privileges of the

self-employed that the amendment would give, but it would take care of the other group which would still be outside these plans, should the amendment be adopted.

I refer to the small employer, who cannot set up a plan. I refer to the employee who has worked all his life and will continue to work all his life for an establishment for which there will not be a pension plan.

So we say that any individual, in any calendar year in which he is not covered by a pension plan, either a corporate plan or under H.R. 10 or a Government plan—

The PRESIDING OFFICER. The time of the Senator from Nebraska has expired.

Mr. CURTIS. I yield myself 5 additional minutes.

We say that in any such year he may buy a special issue of Government bonds up to a total limit of \$300. In other words, he may save \$25 a month, and on that saving he will not be taxed. Then in his old age, when he cashes the bond, just as in the case of the other plans, he will pay a tax on the full amount. The plan would be very simple to operate.

Suppose there is a bond for the base amount of \$100. The person could go to the bank or post office where the bonds were sold. He would give his age. The teller or clerk could look at a table and determine that the bond could be bought for X dollars. Just as in the case of an E-bond, if the purchaser did not cash the bond at age 65, it would draw interest beyond that time.

This proposal would enable people having modest incomes, people who are some of the hardest working and most worthy in our country, to have an opportunity to save for their old age before taxes.

I say to the proponents of H.R. 10, who are concerned with whether or not such a bill might be vetoed, if this amendment be adopted—and perhaps it will not have such universal application—the chances of the bill being vetoed will be very much less.

Mr. HRUSKA. Mr. President, will the Senator from Nebraska yield?

Mr. CURTIS. I yield.

Mr. HRUSKA. Through his fine presentation and constructive contribution, my colleague has again demonstrated why he is considered to be one of the valuable members of the Committee on Finance.

I should like to ask the Senator a question concerning his proposal: Assume a person who invests in such a bond does not wait until he is 64½ years of age, but rather sells the bond prior to that time. What would happen in that event?

Mr. CURTIS. The bonds would be nontransferable. The only occasion on which the holder of such a bond could cash it—and it would be in a lesser amount—and have it nontaxable, would be if he were found to be totally disabled under the same section under which he must prove disability for social security. Then he could cash the bond.

Mr. HRUSKA. Otherwise, the bond would not be cashable until the holder reached the age of 64½?

Mr. CURTIS. It would not be transferable. Let me state what it will mean. It will mean the sale of bonds to individuals instead of to banks and finance companies. The program would be anti-inflationary. Many of these bonds would be for long terms. One of the Treasury's problems arises from the sale of bonds for a term of less than 5 years. The problem of financing our enormous debt is made difficult when the sale of bonds is on such a short turnover basis. What is needed is long-term financing. This proposal will contribute to long-term financing. The income would not escape taxation; taxation would merely be deferred until the holder of the bond used the income.

Mr. HRUSKA. I thank my colleague.

Mr. CURTIS. I thank the Senator from Nebraska.

Mr. PASTORE. Mr. President, will the Senator yield?

Mr. CURTIS. I yield.

Mr. PASTORE. I am very much interested in the Senator's proposal. Was his amendment advanced in the committee?

Mr. CURTIS. It was, and it failed, as I recall, by one vote.

Mr. PASTORE. Did the Treasury Department make any comment on the amendment?

Mr. CURTIS. Those hearings were not held this year. I am reaching back in memory. It is my understanding that the Treasury was opposed to all such legislation—including both H.R. 10 and my proposal. I hope I am not doing the Treasury an injustice, but that is my recollection.

Mr. PASTORE. Did I correctly understand the Senator to say that when one of these bonds was purchased, it would not be redeemable until its maturity?

Mr. CURTIS. That is correct; except that if the holder became disabled before that time, he could cash it.

Mr. PASTORE. What if he should die in the meantime?

Mr. CURTIS. The bond would become a part of the estate.

Mr. PASTORE. It would become a part of the estate?

Mr. CURTIS. Yes. An individual who came under the \$300 limit and could buy nothing but Government bonds would not be required to cover employees or other persons. I dare say that the more successful business and professional men who are advocating H.R. 10 would prefer trustee plans under which they could get growth investment.

The PRESIDING OFFICER. The time of the Senator from Nebraska has expired.

Mr. DIRKSEN. I yield 5 additional minutes to the Senator from Nebraska.

Mr. PASTORE. Those who would be eligible under the Senator's plan would be only the self-employed who did not employ other persons?

Mr. CURTIS. Employees could avail themselves of this plan. A person who worked for a small business which did not have a pension plan, and perhaps

could never come under such a plan, could use any of his earned income to buy Government bonds for his old age and pay taxes when he cashed them.

Mr. PASTORE. Suppose later such a person joined a pension plan.

Mr. CURTIS. His limit would be fixed yearly. In any year in which he was not covered by a pension plan, he could buy the bonds.

Mr. PASTORE. So all the safeguards are provided?

Mr. CURTIS. I believe so.

Mr. President, I yield back the remainder of my time.

Mr. KERR. Mr. President, I yield 5 minutes to the junior Senator from Tennessee.

Mr. GORE. Mr. President, H.R. 10 goes in the opposite direction from tax reform. While apparently throughout the country there is a feeling that there is a dire need of thoroughgoing tax reform, H.R. 10 is seriously proposed in the opposite direction. Instead of closing loopholes of tax favoritism, the enactment of H.R. 10 would create one of the biggest and one of the worst, another big and another bad, loophole of tax favoritism.

For the moment, I shall not discuss the details of the bill. Suffice it to say that this special benefit would accrue largely to those who least need tax relief. Let me cite the estimate of the Treasury Department, made during the administration of President Eisenhower, as to the use which would be made of the provisions of H.R. 10. In estimating revenue losses under terms of the bill, the Treasury assumed that only 15 percent of the people in the low income brackets who would be eligible to receive this benefit would be in financial circumstances to take advantage of it, but two-thirds of those in the upper income brackets who would be eligible for this special benefit or favor would not only be able to take advantage of it, but would do so.

I should like to observe, briefly, that every statement made today in the Senate in support of H.R. 10 has attempted to justify it on the basis of abuses of corporate pension provisions of our tax law. Thus, we see a continuation of the trend to justify a proposed new tax gimmick on the basis of abuse of provisions already in the law. But what is the duty of representatives of the people, with respect to loopholes of tax favoritism? Is it to remove the offending provisions from the law; or is it to leave them in the law, and to enact other loopholes, using the existing ones as an excuse? I think the proper course is to enact tax reform which will be fair and equitable, and to strike down the existing loopholes and favoritism gimmicks, instead of creating more.

When H.R. 10 is before the Senate, I shall attempt to have it amended. I shall have two objectives. The first will be to make the benefits of the bill available to all taxpayers. Mr. President, what is the justice of providing that a well-to-do doctor can receive tax deduction for the purchase of an insurance policy for his own benefit, whereas a

newspaper reporter or a bank clerk cannot have that privilege? I have been imbued with the notion that Congress represents all the people. I shall undertake so to do with respect to H.R. 10.

Second, I shall undertake, by means of amendments—since the Senate is determined to enter upon consideration of pension plans—

The PRESIDING OFFICER. The time yielded to the Senator from Tennessee has expired.

Mr. GORE. May I have 2 additional minutes?

Mr. MANSFIELD. Mr. President, I yield 2 additional minutes to the Senator from Tennessee.

The PRESIDING OFFICER. The Senator from Tennessee is recognized for 2 more minutes.

Mr. GORE. I thank the Senator from Montana.

Mr. President, by means of amendments, I shall undertake to correct some of the more flagrant abuses of the corporate pension plans, particularly the owner-manager type corporation, to which the junior Senator from Florida referred, and by which he sought to justify H.R. 10.

Mr. President, I believe in tax reform. But I believe that if we continue to load down this bill with one example of favoritism after another, tax reform will be aborted.

I have given assurances to the distinguished majority leader that if this bill is brought up by motion as a separate bill, I shall undertake to have it defeated, and shall do so with all the strength and power of persuasion that I may have; and if it is not defeated, I shall undertake to amend it in the ways I have suggested. But I have also assured him that I would not engage in dilatory tactics with respect to H.R. 10 as a separate bill, any more than I have been with respect to the pending bill.

The PRESIDING OFFICER. The additional time yielded to the Senator from Tennessee has expired.

Mr. GORE. May I have 1 more minute?

Mr. MANSFIELD. I yield 1 more minute to the Senator from Tennessee.

The PRESIDING OFFICER. The Senator from Tennessee is recognized for 1 more minute.

Mr. GORE. Mr. President, I shall neither organize nor participate in a dilatory movement with respect to H.R. 10, to prevent it from coming to a vote.

Mr. KERR. Mr. President, I ask for 1 minute.

Mr. MANSFIELD. Mr. President, I yield 1 minute to the Senator from Oklahoma.

The PRESIDING OFFICER. The Senator from Oklahoma is recognized for 1 minute.

Mr. KERR. Mr. President, yesterday, as I stated, I submitted a series of amendments on page 140, line 16. One of them was to make the effective date September 4, 1962. I find that as set forth on page 2 of the amendments, in line 8, instead of that date, there has inadvertently been set forth there the date December 31, 1962.

I ask unanimous consent that the date December 31, 1962, be stricken, and that there be inserted in lieu thereof the date of the submission of the amendments, which was September 4, 1962.

The PRESIDING OFFICER. Without objection, it is so ordered.

Mr. KEATING. Mr. President—

Mr. DIRKSEN. Mr. President, I yield 5 minutes to the Senator from New York [Mr. KEATING].

The PRESIDING OFFICER. The Senator from New York is recognized for 5 minutes.

Mr. KEATING. Mr. President, I sincerely hope that the amendment offered by the distinguished minority leader will not be tabled.

When I was in the other body, I introduced a bill which went considerably farther than this bill does, in giving people an opportunity to lay funds aside for their future years and to have the amounts laid aside declared tax deductible. My recollection is that the amount permitted to be so treated in my bill was less than \$2,500, but the bill extended to a much wider group of taxpayers. I therefore think there is considerable merit in the argument earlier presented by the distinguished Senator from Tennessee to the effect that more people should be included in coverage of H.R. 10 but, we shall not have an opportunity to deal with this proposition unless we defeat the proposed motion to lay on the table. I hope the Senator from Tennessee will vote accordingly.

This amendment by the distinguished minority leader gives self-employed persons an opportunity to plan their retirement on a basis similar to that very generally and widely afforded corporate employees. Adoption of the amendment would do away with an unfortunate discrimination in existing law, under which both employees and persons defined as owner-managers are permitted to participate in tax-exempt retirement plans; yet self-employed individuals have no opportunity to do so.

When we speak of the self-employed, we are not just referring to a small minority, but to a group estimated at between 7 million and 9 million persons engaged in a wide group of activities. Included in the group would be lawyers, doctors, and journalists earning fees of as much as \$40,000 or \$50,000 or \$100,000. However, these are by no means the only people covered.

It must be remembered that there would also be included gasoline station attendants and persons running small grocery stores—persons with incomes of perhaps \$2,000 or \$3,000, and—and I speak from personal experience—in many years running their businesses at a loss. Also included would be employees of the self-employed persons—which means that under this bill, pension plans would become available to an estimated 9 million or 10 million Americans who are not self-employed and do not presently have pension rights. This is a very significant change in the original version of H.R. 10.

Every year this idea, which I believe is eminently sound and just, has gained

increased momentum. In the 82d and 83d Congresses, the bill was submitted, but it never got out of committee. In the 84th Congress it was reported to the floor of the House, but no action was taken on it. Finally, in the 85th Congress, a bill similar to the amendment now pending, was passed by the House. In each of the two succeeding Congresses legislation was passed in the other body, but in no instance has it received Senate consideration.

The present H.R. 10, as it is designated, was passed on June 3, 1961. The Senate Finance Committee reported the bill in September of last year. Since that time it has remained on the calendar, collecting new supporters all the time, but not receiving any attention in the Senate.

The principal argument that has been used against this legislation is the loss of revenue involved. Of course, that is a matter which we must always consider most seriously. Every time the bill has come up, the Executive has indicated that the revenue that would be lost would be some enormous sum of money.

In the first place, I have serious doubt about the size of the figures that are given. Of course, it will result in some revenue loss—

The PRESIDING OFFICER. The time of the Senator has expired.

Mr. KEATING. I yield myself 2 more minutes.

But offset against this loss is the inherent fairness of the plan, plus the fact that it will be a significant spur to our economy, because many of the persons who will benefit under H.R. 10 will feel that, if they are providing for their later years, they can more liberally spend now and enjoy life as they go along. It will thereby be an impetus to our economy, which certainly needs it.

Mr. President, the tabling of H.R. 10 will be the death knell not only of these hopes and aspirations, but any effort which may be made to improve H.R. 10 as worded. I sincerely hope that the effort to table this amendment, will be defeated.

Mr. DIRKSEN. Mr. President, I yield 3 minutes to the Senator from Nebraska [Mr. HRUSKA].

Mr. HRUSKA. Mr. President, I rise in support of the amendment of the Senator from Illinois and join in the thoughts and conclusions just expressed by our colleague the Senator from New York.

The amendment, after all, has for its objective the correction of an inequity which has existed ever since the present provisions for pension plans were devised for officers and employees of corporations. It is a substantial inequity because it affects somewhere between 7 and 10 million self-employed individuals.

The Dirksen amendment would place these small businessmen, farmers, and professional people on a parity with officers and employees of corporations.

By treating self-employed individuals as their own employers for the purposes of establishing voluntary pension plans, this amendment would give these individuals substantially the same opportunities they would otherwise have were

they carrying on their business or profession as a corporation. Limited amounts which are set aside for retirement plans for the benefit of themselves would be made deductible. As in the case of other employees, self-employed persons would not be taxed on these contributions or the income which accrues thereon until such time as these funds are distributed to them during their retirement.

Thus, this amendment looks beyond the mere form in which an individual may be doing business. It brings us to the substance of this whole question, that people should be encouraged to help themselves regardless of the particular form or style of business organization under which they may be operating.

This concept has been advanced for several years. Similar legislation for providing equal treatment for the self-employed was passed by the House during the 85th and 86th Congresses and again during the first session of this Congress. The Senate Finance Committee held extended hearings on H.R. 10 during the 86th Congress and approved the bill. The committee reaffirmed its approval of the bill almost a year ago, and it has been pending on the Senate Calendar since that time.

Therefore, the Dirksen amendment which embodies the provisions of H.R. 10 is a seasoned piece of legislation. It has been developed and refined to its present form after a great deal of consideration, debate, and study.

Under the amendment, a self-employed person would be permitted to contribute 10 percent of his earned income or \$2,500, whichever is smaller, to a qualified retirement plan. Like other employers, he could claim a deduction for this contribution in the year that it is made. However, this deduction would be limited to 100 percent of the first \$1,000 and 50 percent of the remaining contribution. Hence, the maximum deduction in any year would be \$1,750.

Like other employees, the self-employed person would not be taxed on these contributions until such time as the benefits are payed out during his retirement.

The amendment also insures equality of treatment as between the self-employed individual and his own employees. In order to qualify, a pension plan must cover all full-time employees with 3 years of service. Further, contributions on behalf of these employees must vest at the time they are made so that they are nonforfeitable.

The PRESIDING OFFICER. The time of the Senator has expired.

Mr. DIRKSEN. Mr. President, I yield 2 more minutes to the Senator from Nebraska.

Mr. HRUSKA. An objection frequently raised to H.R. 10 is that its enactment would result in a substantial loss of tax revenue. The loss under the House passed version was estimated to be somewhere between \$325 and \$358 million a year. The Treasury Department cited this as one of its principal objections to the measure.

However, the amendments recommended by the Senate Finance Commit-

tee would reduce this potential loss in revenue to an estimated \$180 million for a full year's operation. Therefore the objection voiced is largely overcome. And in view of the gross inequities overcome by the present bill, which have already been discussed, this cannot be the sole consideration.

Mr. President, I hope that our many self-employed citizens will at last be extended the relief provided by H.R. 10 as it now stands on the Senate Calendar. This bill should have been called up for full debate and action by the Senate a long time ago. Unfortunately, it was not. We now have the opportunity to act upon it.

It is my hope that the motion to table will be defeated and the amendment will be approved.

I yield back the remainder of my time.

Mr. DIRKSEN. Mr. President, I thought it might be well for the RECORD to read just a few excerpts from the report of the Senate Finance Committee on H.R. 10. I read from page 8 of the report, in which are assigned the reasons for the bill:

The primary reason for the House bill (as amended by your committee) is to give self-employed persons access to retirement plans on a reasonably similar basis to that accorded corporate stockholder employees. It thus tends to correct a discrimination in present law under which self-employed individuals—sole proprietors and partners—are prevented from participating in retirement plans established for the benefit of their employees although owner-managers of corporations may do so.

The second reason assigned for the bill is, as follows:

The bill allows contributions to retirement plans to be a deduction for income tax purposes at the time these contributions are made, but requires that retirement benefits when received be subject to taxation.

The third reason assigned:

Your committee, like the Committee on Ways and Means of the House, is of the opinion that extending the coverage of individuals under voluntary retirement plans is in the public interest. The bill will make self-employment somewhat more attractive than at present compared to employment with a corporation, and will thus help to keep small business strong and independent professional practice thriving.

As a part of my remarks, Mr. President, I may say that there have been statements to the effect that this is a lawyers' bill and a doctors' bill. I heard a statement on the floor a moment ago with respect to teachers, reporters, and others. I know of no teachers who are under no private pension plan. I presume that statement would apply to reporters, and other newspaper employees as well, who would be under corporate pension plans.

In addition, Mr. President, there have been many endorsements of H.R. 10. I shall ask to have some of the endorsements printed, but I recite at this point that the list I am submitting includes the American Association of Small Business, the American Farm Bureau Federation, the American Authors League of America, Inc., the Contracting Plasterers' and Lathers' International Association, the National Association of Plumb-

ing Contractors, the National Association of Real Estate Boards, the National Farmers Union, the National Federation of Independent Business, the National Milk Producers Federation, the Painting and Decorating Contractors of America, and the National Wholesale Furniture Salesmen's Association.

I am sure others could be added, because I noted in the RECORD that Representative KEOGH, of New York, included a very large number of associations and groups which wholeheartily endorse H.R. 10.

I ask unanimous consent that these endorsements may be printed in the RECORD.

There being no objection, the endorsements were ordered to be printed in the RECORD, as follows:

I urgently request you again to do your utmost to see that H.R. 10, the Self-Employed Individuals' Retirement Act, is approved by your committee promptly, so that it may be acted upon by the entire Senate.

The inequality of opportunity experienced by the self-employed, as compared with the pension provisions furnished the employee by the many segments of industry, has long created a hardship for the self-employed.—American Association of Small Business.

The American Farm Bureau Federation has supported the general principles of this type of legislation for several years, within limits adequate to prevent abuse.—Statement of the American Farm Bureau Federation.

Like many other organizations speaking for self-employed craftsmen, businessmen and professional people, the Authors League has previously had the opportunity—I might add ruefully and regretfully—several opportunities—to express its support for H.R. 10 and the retirement program for self-employed taxpayers, which it would make possible.—American Authors League of America, Inc.

The Contracting Plasterers' & Lathers' International Association is an organization of lathing and plastering contractors with members in the United States and Canada, but with the great bulk of its membership in the United States.

The members of this association are all small businessmen. A good number of the members are in unincorporated firms, and have no means of setting up a retirement fund of their own through which they may prepare for the day when they are no longer able to carry on their business.

H.R. 10 would meet the need of the good majority of the members of this association, and indeed, would meet the needs of a majority of the small businessmen in America today.—Contracting Plasterers' & Lathers' International Association.

The National Association of Plumbing Contractors is composed of approximately 10,000 members who do about 80 percent of the total volume of plumbing contracting in the United States. * * * The vast majority of these contractors are small shops and as such qualify as small businessmen. Our association has 46 State associations and approximately 390 local affiliated groups.

The National Association of Plumbing Contractors feel that a measure like H.R. 10 would help keep many people from incorporating to reduce their taxes. There are a number of plumbing and heating contractors who could have saved considerable money during the past few years on their income tax by incorporating their business.—National Association of Plumbing Contractors.

I am testifying on behalf of the more than 69,000 members of the National Association of Real Estate Boards, the large majority of

whom would be directly affected by enactment of this bill. It is consistent with the professional nature of their work that they do business in a noncorporate form, and most of them, therefore, are self-employed. Because of this, the present tax inequity which exists relative to pension plans for the self-employed affects them adversely just as it does doctors, lawyers, and others. There is, therefore, overwhelming support in our association for passage of H.R. 10.—National Association of Real Estate Boards by Realtors' Washington Committee.

Delegates to the convention of National Farmers Union, meeting in Washington, D.C., in March of this year, adopted a resolution in favor of a retirement program for self-employed persons. Their approval was expressed as follows:

"Deductions for farmers and other self-employed to establish retirement funds should be permitted on the same basis currently afforded to corporations to provide such benefits for their employees."

I respectfully request your support of H.R. 10 * * * when it comes before the Senate Finance Committee for action.—National Farmers Union.

Speaking for the more than 170,000 individual independent business and professional people from all 50 States of this country, individuals who are active, current members of this federation, we urge that you act favorably on bill H.R. 10, a bill that rights an injustice in our laws which permit corporations to take tax deductions for payments into private retirement funds for their officers and employees, yet prohibits self-employed business and professional people from enjoying the same opportunities.

Please understand, we are not telling you what we or any small self-appointed group think our members want. We are only repeating to you what our members themselves have told their Congressmen and told us in repeated soundings in federation nationwide membership mandate polls in which each of our members has had one and only one vote and in the course of which members have sent their voted, signed and thereby authenticated, opinions to their Congressmen.—National Federation of Independent Business.

We shall greatly appreciate it if you will include in the hearing record of H.R. 10 this statement supporting the bill.

The National Milk Producers Federation is a national farm organization. It represents approximately half a million dairy farmers and some 800 dairy cooperative associations.

The lack of adequate provisions for the retirement income of dairy farmers is a matter about which we are deeply concerned.

We have given a great deal of thought to what might be done for dairy farmers in this field. The more we work on it, the more convinced we are that the first step should be legislation such as H.R. 10.

We hope you will bear in mind, in your deliberations on this bill, the need of dairy farmers for a base on which they can build more adequately for their own retirement.—National Milk Producers Federation.

The Painting & Decorating Contractors of America is the spokesman for some 8,500 active painting contractors from every section of this great Nation. I do not believe that a better example of the American small businessman can be found than today's painting and decorating contractor. The large majority of these men employ less than 10 workmen. They willingly contribute to welfare and pension funds for their workmen but are denied the right to set aside any amount for their own retirement on any tax deferred basis. As a national association we strongly feel that this is working a hardship on these self-employed persons who help make up the backbone of this Nation. We strongly urge that the Senate Finance Com-

mittee favorably report H.R. 10 for consideration of the U.S. Senate.—Painting & Decorating Contractors of America.

I hope that the members of this committee will consider the effect on the morale of the self-employed who comprise a very important part of this country's citizenry. It is our feeling that passage of H.R. 10 will show an act of faith on the part of Members of the Congress in the well-being of their constituents who are self-employed and an integral part of the backbone of America.—National Wholesale Furniture Salesmen's Association.

Mr. MANSFIELD. Mr. President, it is my understanding that the proponents of the amendments have completed their presentation on their time. I do not anticipate using the 11 minutes remaining on this side, but I wish to state that one of the reasons why I shall make the motion to table the pending amendments is because of a fear on my part that if the amendments are agreed to it is possible—and I say this only in a personal sense—that the tax bill may well be vetoed. I make that statement because of the fact that in my opinion there are enough opponents of H.R. 10 and of the tax bill, perhaps, to be able to sustain a Presidential veto.

I do not know what the President will do if the motion to table is successful and H.R. 10 then becomes the pending business at the conclusion of consideration of the tax bill, as it will if the motion to table is successful, but I would anticipate the chances for its passage would be much better than they are at the present time.

Mr. HARTKE rose.

Mr. MANSFIELD. I yield at this time to the Senator from Indiana [Mr. HARTKE].

Mr. HARTKE. Mr. President, as I understand the remarks made by the majority leader, one difficulty with respect to the bill is that the President has an understanding that it would cause an increase in the deficit, so far as overall revenues are concerned. Is that correct?

Mr. MANSFIELD. I am certain that is the feeling both of the present President and was of the previous President, Mr. Eisenhower.

Mr. HARTKE. Is it not true also that the withholding provision which was recommended could have been helpful in regard to the deficit, and that the difficulty would not have been presented, at least in the same scope, under the bill with the withholding provision as it is presented under the bill as it is today?

Mr. MANSFIELD. The Senator is correct. It is unfortunate that the withholding provisions were not retained in the bill. That was a good proposal. It is a fact that the law now, and the law for 20 years, has provided for payment of taxes on such income, but the withholding provision involves the question of enforcement.

Mr. HARTKE. If the motion to table is sustained, is my understanding correct that it is the intention of the majority leader to make H.R. 10 the next order of business?

Mr. MANSFIELD. That is correct. Immediately after the disposition of the

pending tax revenue measure it is the intention of the Senator from Montana to lay before the Senate H.R. 10 and to make it the pending business, and to stay with it until a vote is taken one way or another.

Mr. HARTKE. That is the measure which at the present time is on the calendar?

Mr. MANSFIELD. The Senator is correct.

Mr. SMATHERS. Mr. President, will the Senator yield for a question?

Mr. MANSFIELD. I yield to the Senator from Florida.

Mr. SMATHERS. I had intended to ask very much the same questions the Senator from Indiana has asked. As I gathered, the majority leader has said it is his impression that if H.R. 10 is attached to the pending tax bill there is some likelihood the bill will be vetoed.

Mr. MANSFIELD. Yes. I can see some people in effect laughing up their sleeves after such a statement, but I would urge caution. In my personal opinion, if the bill were vetoed there would be sufficient votes on the part of those who are opposed to H.R. 10 and those opposed to the tax bill itself to uphold a Presidential veto.

Mr. SMATHERS. I wish to say to the able majority leader that, while there was not a very specific statement, nonetheless the impression I gathered was that if H.R. 10 were attached to the tax bill there was a great likelihood the whole tax bill, including H.R. 10, would be vetoed. As I say, there was nothing specific said in that respect, but that was the definite impression I had.

Another question I had related to an assurance by the majority leader that there will be a vote on the merits of H.R. 10 prior to the Senate considering the trade bill.

Mr. MANSFIELD. Yes. Immediately following the disposition of the tax bill, it will be considered. I had notified certain Senators that at an appropriate time H.R. 10 would be considered this session. That appropriate time has been moved up considerably, due to circumstances over which I had no control.

Mr. SMATHERS. Mr. President, will the Senator yield to me so that I may make a brief statement, with the understanding that he will not lose his right to the floor?

Mr. MANSFIELD. I yield.

Mr. SMATHERS. In the light of what the majority leader has said, I wish to state that the impression I gathered, after talking to people at the White House, was the same impression gathered by the able majority leader.

It would seem to me that the wisest course to be followed by those who genuinely wish to see H.R. 10 pass would be to support the majority leader in his motion to table. This I say for the very simple reason that later, down the road, after we pass H.R. 10—and I am confident we have enough votes in the Senate to pass it as amended by the Senate Finance Committee, which would reduce the cost to the Government from \$380 million a year to \$180 million a year, and perhaps less than that—the

question then would arise as to whether H.R. 10, standing by itself, might run into a Presidential veto.

I have heard no expression about that. Anticipating the worst, and with no great reason to do so, other than to be forewarned, it would occur to me that H.R. 10, standing by itself, could be passed over a Presidential veto.

I do not believe, however, that we could override a veto of the tax bill and H.R. 10 combined, because there are certain Senators opposed to H.R. 10 and other Senators opposed to certain features of the tax bill. There are a number of Senators who would like to see the tax bill defeated.

After all, since the bill would collect from the savings and loan associations and mutual banks \$200 million, it is in a way to their interest not to have the tax bill passed.

Since the bill would tighten up on expense accounts bringing in an additional \$85 million in tax revenue, many people would like to see the tax bill not passed, for that reason.

Since the bill would provide for collecting some \$105 million from the sale of certain depreciable property, there are some people who would not like to see it pass for this reason.

Since the bill would provide for collecting \$25 million from mutual, fire and casualty insurance companies, there are certain companies which would not like to see it pass.

Since the bill would provide for collecting \$30 million from cooperatives, there are some others who would not like to see it pass.

Since there would be \$90 million coming in from a tax on foreign subsidiaries, there are even others who would not like to see the measure pass.

When we note all of the people who are opposed to the tax bill, or to certain provisions in it, combined with those who are opposed to H.R. 10, it is my considered opinion we would have a very difficult time overriding a veto of a tax bill including H.R. 10. If we should pass H.R. 10, standing on its own feet, with the knowledge which Senators and Representatives in Congress have about it, considering the many expressions which have been made by Senators as to their belief in the equitableness and righteousness of it, and their willingness to support it, I am of the firm conviction that we could override a presidential veto if one should occur. I certainly hope there will not be a Presidential veto.

I should like to say, so far as the junior Senator from Florida is concerned, I have long been interested in this proposed legislation. I think its passage is overdue. I think it is an equitable proposal. I think it is a just proposal. I think the Senate ought to pass it. I think the way to pass it is to support the motion by the majority leader to table the pending amendment.

Mr. PASTORE. Mr. President, will the Senator yield?

Mr. MANSFIELD. I yield to the Senator from Rhode Island.

Mr. PASTORE. One of the things which has impressed the Senator from

Rhode Island in the past has been the fine cooperation between the majority and minority floor leadership. In view of the assurance by the majority leader that he will make H.R. 10 the pending business following action on the tax bill, and the fact that he is determined to have it come to a vote, I wonder why, in his good judgment, the minority leader does not withdraw his amendments.

Mr. MANSFIELD. That is something for the minority leader to decide for himself.

Mr. PASTORE. I was looking at the minority leader when I said that.

Mr. MANSFIELD. I can well understand his point of view. As a matter of fact, I can sympathize with it.

We have the issue now before us.

Mr. DIRKSEN. Mr. President, if an egg is good, it is good whether it is served up alone or served up with a dozen other eggs.

The measure is a good egg and it is in a bill. We can take our choice as to whether the President would veto the measure or not. I leave the question to Senators on the basis of the President's statement in January 1960, which Senators will find in volume 107 of the CONGRESSIONAL RECORD. I shall read it once more into the RECORD.

Senator Kennedy, now President Kennedy, said:

I am myself disposed to support the type of provisions which are contained in the Simpson-Keogh bill. I personally feel that there has been ample testimony from many sources over a long period of time in both Houses, and that it is time to take floor action on this legislation. * * * I hope that it will be acted upon favorably during this Congress.

That was John Fitzgerald Kennedy speaking.

I for the life of me cannot understand why the President should veto a tax bill containing H.R. 10, in view of that statement made in January of 1960.

Mr. PASTORE. Mr. President, will the Senator yield?

Mr. DIRKSEN. I yield.

Mr. PASTORE. The senior Senator from Rhode Island is impressed with the logic stated, and certainly supports it. But I doubt very much that that is the real reason. After all, it is important proposed legislation. The House bill has been modified by the Senate. We have not had a thorough explanation. The question has not been fully debated, and I think it is worthy of such debate.

Cursory examination on my part makes me feel that I would support the proposed legislation. But there has not been sufficient opportunity to debate it. I think it should be debated for the benefit of the country and all the taxpayers. For that reason I think the amendment should be withdrawn.

Mr. HRUSKA. Mr. President, will the Senator yield?

Mr. DIRKSEN. I yield.

Mr. HRUSKA. The Senator from Nebraska might suggest to the Senator from Rhode Island that one way to get a debate on the question is to defeat the

motion to table the amendment. There will then be ample time to debate all the merits, all the history, and all the fine features embodied in the bill.

Mr. MANSFIELD. There would be more than ample time if the motion to table were defeated.

Mr. PASTORE. That is correct. The measure is not completely germane to the issue before the Senate. The Senator knows that.

Mr. DIRKSEN. Mr. President, I have only one further statement to make. I have before me the Senate committee report on H.R. 10. It is dated September 13, 1961. We are now in the month of September. Within a week the measure will have been on the Senate Calendar for 1 whole year. By that time everybody should have developed a reasonable familiarity with the provisions of the bill. But I am content now to let the Senate vote.

Mr. HARTKE. Mr. President, will the Senator yield for a question?

Mr. MANSFIELD. Mr. President, how much time have I remaining?

The PRESIDING OFFICER. The Senator from Montana has 2 minutes remaining.

Mr. HARTKE. Mr. President, will the Senator yield 1 minute to me?

Mr. MANSFIELD. I yield.

Mr. HARTKE. I should like to ask whether the Senator from Illinois did not make a statement some time ago—about 1959—that the measure was a budget-busting measure?

Mr. DIRKSEN. Mr. President, I should like to refresh the memory of my friend. When the bill was first reported under the Eisenhower administration, the Treasury Department indicated that the cost would be \$400 million or more. The Senator from Illinois picked up the cudgels for the then President of the United States on the measure and said that in its then form he was opposed to it. I remind my friend, who happens to be a member of the Senate Finance Committee, that the measure has been put in such form that even the objections of the Treasury Department have been withdrawn. Even liberals who filed minority views on the measure have indicated that it would probably cost not in excess of \$185 million. I think the amount would be less. Though I am not a member of the Finance Committee, I am happy to refresh the memory of the Senator from Indiana as to the facts.

Mr. HARTKE. Mr. President, will the Senator yield 1 additional half minute?

Mr. MANSFIELD. I yield.

Mr. HARTKE. In response to that statement, if the minority leader is willing to follow the recommendations of the Treasury Department, I shall give him an opportunity again to vote on the proposed withholding of taxes on dividends and interest before the debate is over, and we shall see whether we can have consistency of cooperation with the Treasury Department, and we will see whether the Senator has had a change of heart on the subject.

Mr. DIRKSEN. I shall be delighted, and I shall tell the Senator now how I shall vote.

Mr. MANSFIELD. Mr. President, before I make the motion to table the amendment, I wish to say that when the distinguished minority leader acted as he has described under the previous administration, the Senator from Illinois was the leader of the President's party in the Senate.

While the Senator said that he would cook only one egg at this time, I hope this egg will be laid at this time.

Mr. HOLLAND. Mr. President, will the Senator yield?

Mr. MANSFIELD. Mr. President, how much time have I remaining?

The PRESIDING OFFICER. The Senator from Montana has 1 minute remaining.

Mr. MANSFIELD. Mr. President, I yield to the Senator from Florida.

Mr. HOLLAND. Mr. President, I think I heard the distinguished majority leader say that he would move to consider H.R. 10 immediately after the disposition of the pending business and that H.R. 10 would remain the pending business until it was disposed of. Am I correct?

Mr. MANSFIELD. The Senator is correct.

Mr. HOLLAND. I thank the Senator.

Mr. WILLIAMS of Delaware. Mr. President, will the Senator yield for a question?

Mr. MANSFIELD. I yield.

Mr. WILLIAMS of Delaware. Does that statement mean that consideration of the trade bill will be postponed until after the Senate completes consideration of H.R. 10?

Mr. MANSFIELD. I do not think so.

Mr. President, I move to table the amendment of the Senator from Illinois, and ask for the yeas and nays on the question.

The yeas and nays were ordered.

Mr. MANSFIELD. Mr. President, I suggest the absence of a quorum.

The PRESIDING OFFICER. The clerk will call the roll.

The legislative clerk proceeded to call the roll.

Mr. MANSFIELD. Mr. President, I ask unanimous consent that the order for the quorum call be rescinded.

The PRESIDING OFFICER. Without objection, it is so ordered.

The question is on agreeing to the motion of the Senator from Montana to lay on the table the amendments of the Senator from Illinois. On this question the yeas and nays have been ordered, and the clerk will call the roll.

The legislative clerk called the roll.

Mr. MANSFIELD. I announce that the Senator from Mississippi [Mr. EASTLAND], the Senator from Washington [Mr. MAGNUSON], the Senator from Alaska [Mr. GRUENING], and the Senator from Minnesota [Mr. HUMPHREY] are absent on official business.

I also announce that the Senator from Missouri [Mr. SYMINGTON], the Senator from New Mexico [Mr. ANDERSON], the Senator from Nevada [Mr. BIBLE], and the Senator from Wyoming [Mr. HICKEY] are necessarily absent.

I further announce that, if present and voting, the Senator from Mississippi [Mr. EASTLAND] would vote "nay."

On this vote, the Senator from Alaska [Mr. GRUENING] is paired with the Senator from Wyoming [Mr. HICKEY]. If present and voting, the Senator from Alaska would vote "yea," and the Senator from Wyoming would vote "nay."

On this vote, the Senator from Minnesota [Mr. HUMPHREY] is paired with the Senator from Nevada [Mr. BIBLE]. If present and voting, the Senator from Minnesota would vote "yea," and the Senator from Nevada would vote "nay."

Mr. KUCHEL. I announce that the Senator from Utah [Mr. BENNETT], the Senator from South Dakota [Mr. BOTTUM], the Senator from Indiana [Mr. CAPEHART], the Senator from Arizona [Mr. GOLDWATER], the Senator from Kentucky [Mr. MORTON], and the Senator from New Hampshire [Mr. MURPHY] are necessarily absent.

If present and voting, the Senator from Utah [Mr. BENNETT], the Senator from South Dakota [Mr. BOTTUM], the Senator from Arizona [Mr. GOLDWATER], the Senator from Kentucky [Mr. MORTON], and the Senator from New Hampshire [Mr. MURPHY] would each vote "nay."

On this vote, the Senator from Indiana [Mr. CAPEHART] is paired with the Senator from Minnesota [Mr. HUMPHREY]. If present and voting, the Senator from Indiana would vote "nay," and the Senator from Minnesota would vote "yea."

The result was announced—yeas 45, nays 41, as follows:

[No. 241 Leg.]

YEAS—45

Bartlett	Jackson	Miller
Byrd, Va.	Johnston	Monroney
Byrd, W. Va.	Jordan, N.C.	Moss
Carroll	Kefauver	Muskie
Church	Kerr	Neuberger
Clark	Lausche	Pastore
Dodd	Long, Mo.	Pell
Ellender	Long, Hawaii	Randolph
Engle	Long, La.	Russell
Ervin	Mansfield	Smathers
Gore	McCarthy	Smith, Mass.
Hart	McClellan	Sparkman
Hayden	McGee	Talmadge
Hill	McNamara	Williams, N.J.
Holland	Metcalf	Young, Ohio

NAYS—41

Aiken	Dirksen	Prouty
Allott	Douglas	Proxmire
Beall	Fong	Robertson
Boggs	Fulbright	Saltonstall
Burdick	Hartke	Scott
Bush	Hickenlooper	Smith, Maine
Butler	Hruska	Stennis
Cannon	Javits	Thurmond
Carlson	Jordan, Idaho	Tower
Case	Keating	Wiley
Chavez	Kuchel	Williams, Del.
Cooper	Morse	Yarborough
Cotton	Mundt	Young, N. Dak.
Curtis	Pearson	

NOT VOTING—14

Anderson	Eastland	Magnuson
Bennett	Goldwater	Morton
Bible	Gruening	Murphy
Bottem	Hickey	Symington
Capehart	Humphrey	

So Mr. MANSFIELD's motion to lay on the table Mr. DIRKSEN's amendment was agreed to.

Mr. MANSFIELD. Mr. President, I move that the Senate reconsider the vote by which the motion to lay on the table was agreed to.

Mr. KERR. I move to lay that motion on the table.

The motion to lay on the table was agreed to.

Mr. DIRKSEN. Mr. President, I should like to make a parliamentary inquiry—if it can be considered a parliamentary inquiry. I believe the majority leader stated immediately before the vote on the motion to table that once the Senate had completed action on the tax bill, H.R. 10 would be laid before the Senate as the pending business.

Mr. MANSFIELD. That is correct. If the Senate will agree to my doing so, it is my intention to call up H.R. 10 and to make it the pending business immediately following the disposal of the tax bill.

Mr. DIRKSEN. I thank the distinguished majority leader.

Mr. KEFAUVER. Mr. President, until the very last moment, I had intended to vote against the majority leader's motion to table. The amendment, which was the same as H.R. 10, was certainly germane to the tax bill in that it would remove a great inequity in our present tax structure. Executives and employees of corporations can have part of their earnings paid into a pension fund without paying taxes on this portion of their earnings at the time. It is only fair that a lawyer, doctor, farmer, or small businessman who is not incorporated should also be able to set aside part of his income before taxes in order to provide retirement income. H.R. 10 would put the self-employed individual on substantially the same basis as the employee of a corporation with respect to saving for retirement.

This proposal has been pending before the Congress for 11 years and the House has passed it several times but the Senate has never even voted on it. While we are concerned with a broad bill correcting inequities in our tax structure, we should also face up to this problem.

I was impressed though with the statement of the distinguished majority leader that he feared the inclusion of H.R. 10 in the tax bill might result in a veto, and that a bill this broad could not then be passed over the President's veto. I was also impressed with the supporting argument by the Senator from Florida [Mr. SMATHERS], who has always been one of the most dedicated supporters of this bill and who reported H.R. 10 from the Finance Committee, when he said that he felt confident that there were sufficient votes to pass H.R. 10, and if necessary override a Presidential veto, if it were vetoed separately.

These remarks, coupled by the majority leader's promise to take up H.R. 10 and pursue it to a final vote immediately upon completion of the tax bill, led me to support the motion to table. I expect to vote for H.R. 10 on final passage and I make this statement now so that my vote in favor of the motion to table will not be misconstrued.

Mr. GORE. Mr. President, I call up my amendment designated "8-27-62—A," and ask that it be identified.

The PRESIDING OFFICER. The amendment will be identified.

The legislative clerk identified the amendment designated "8-27-62—A."

The PRESIDING OFFICER. Without objection, the amendment will be printed in the RECORD.

The amendment is as follows:

On page 175, beginning with line 9, strike out all through line 18, on page 245 (section 12 of the bill), and in lieu thereof insert the following:

"SEC. 12. CONTROLLED FOREIGN CORPORATIONS.

"(a) IN GENERAL.—Part III of subchapter N of chapter 1 (relating to income from sources without the United States) is amended by adding at the end thereof the following new subpart:

"SUBPART F—CONTROLLED FOREIGN CORPORATIONS

"Sec. 951. Amounts included in gross income of United States shareholders.

"Sec. 952. Limitations on amounts included in gross income of United States shareholders.

"Sec. 953. Less developed country corporations defined.

"Sec. 954. Withdrawal of previously excluded foreign base company income from qualified investment.

"Sec. 955. Investment of earnings in United States property.

"Sec. 956. Controlled foreign corporations.

"Sec. 957. Rules for determining stock ownership.

"Sec. 958. Exclusion from gross income of previously taxed earnings and profits.

"Sec. 959. Special rules for foreign tax credit.

"Sec. 960. Adjustments to basis of stock in controlled foreign corporations and of other property.

"Sec. 961. Miscellaneous provisions.

"Sec. 962. Inclusion on a consolidated basis of earnings and profits.

"SEC. 951. AMOUNTS INCLUDED IN GROSS INCOME OF UNITED STATES SHAREHOLDERS.

"(a) AMOUNTS INCLUDED.—

"(1) IN GENERAL.—If a foreign corporation is a controlled corporation on any day of a taxable year beginning after December 31, 1962, every person who is a United States shareholder (as defined in subsection (b)) of such corporation and who owns (within the meaning of section 957(a)) stock in such corporation on the last day, in such year, on which such corporation is a controlled foreign corporation shall include in his gross income, for his taxable year in which or with which such taxable year of the corporation ends—

"(A) in case of a controlled foreign corporation which is not a less developed country corporation (as defined in section 953(a)), his pro rata share (determined under paragraph (2)) of the corporation's earnings and profits for such year; and

"(B) his pro rata share (determined under section 955(a)(2)) of the corporation's increase in earnings invested in United States property for such year (but only to the extent not excluded from gross income under section 958(a)(2)).

"(2) PRO RATA SHARE OF EARNINGS AND PROFITS.—The pro rata share referred to in paragraph (1)(A) in the case of any United States shareholder is the amount—

"(A) which would have been distributed with respect to the stock which such shareholder owns (within the meaning of section 957(a)) in such corporation if on the last day, in its taxable year, on which the corporation is a controlled foreign corporation it had distributed pro rata to its shareholders an amount (1) which bears the same ratio to its earnings and profits for the taxable year, as (11) the part of such year during which the corporation is a controlled foreign corporation bears to the entire year, reduced by

"(B) the amount of any distribution received by any other United States person

during such year as a dividend with respect to such stock.

"(3) LIMITATION ON PRO RATA SHARE OF INVESTMENT IN UNITED STATES PROPERTY.—For purposes of paragraph (1)(B), the pro rata share of any United States shareholder in the increase of the earnings of a controlled foreign corporation invested in United States property shall not exceed an amount (A) which bears the same ratio to his pro rata share of such increase (as determined under section 955(a)(2)) for the taxable year, as (B) the part of such year during which the corporation is a controlled foreign corporation bears to the entire year.

"(b) UNITED STATES SHAREHOLDER DEFINED.—For purposes of this subpart, the term "United States shareholder" means, with respect to any foreign corporation, a United States person (as defined in section 7701(a)(30)) who owns (within the meaning of section 957(a)), or is considered as owning by applying the rules of ownership of section 957(b), 10 percent or more of the total combined voting power of all classes of stock, or of the total value of shares of all classes of stock, of such foreign corporation.

"(c) COORDINATION WITH ELECTION OF A FOREIGN INVESTMENT COMPANY TO DISTRIBUTE INCOME.—A United States shareholder who, for his taxable year, is a qualified shareholder (within the meaning of section 1247 (c)) of a foreign investment company with respect to which an election under section 1247 is in effect shall not be required to include in gross income, for such taxable year, any amount under subsection (a) with respect to such company.

"SEC. 952. LIMITATIONS ON AMOUNT INCLUDED IN GROSS INCOME OF UNITED STATES SHAREHOLDERS.

"(a) IN GENERAL.—For purposes of section 951(a) the term "earnings and profits for the taxable year" means, in the case of any controlled foreign corporation, the earnings and profits as defined in section 316(a)(2) for the taxable year subject to the provisions of subsections (b) and (c).

"(b) EXCLUSION OF UNITED STATES INCOME.—Earnings and profits do not include any item includible in gross income under this chapter (other than this subpart) as income derived from sources within the United States of a foreign corporation engaged in trade or business in the United States.

"(c) LIMITATION.—For purposes of subsection (a), the earnings and profits of any controlled foreign corporation for any taxable year shall not exceed the earnings and profits of such corporation for such year reduced by the amount (if any) by which—

"(1) the sum of the deficits in earnings and profits for prior taxable years beginning after December 31, 1962, exceeds

"(2) an amount equal to the earnings and profits described in section 958(c)(3) accumulated for taxable years beginning after December 31, 1962 (determined as of the close of the taxable year).

For purposes of the preceding sentence, any deficit in earnings and profits for any prior taxable year shall be taken into account under paragraph (1) for any taxable year only to the extent it has not been taken into account under such paragraph for any preceding taxable year to reduce earnings and profits of such preceding year.

"(d) SPECIAL RULE IN CASE OF INDIRECT OWNERSHIP.—For purposes of subsection (c), if—

"(1) a United States shareholder owns (within the meaning of section 957(a)) stock of a foreign corporation, and by reason of such ownership owns (within the meaning of such section) stock of any other foreign corporation, and

"(2) any of such foreign corporations has a deficit in earnings and profits for the taxable year,

then the earnings and profits for the taxable year of each such foreign corporation which is a controlled foreign corporation shall, with respect to such United States shareholder, be properly reduced to take into account any deficit described in paragraph (2) in such manner as the Secretary or his delegate shall prescribe by regulations.

"SEC. 953. LESS DEVELOPED COUNTRY CORPORATIONS DEFINED.

"(a) LESS DEVELOPED COUNTRY CORPORATIONS.—

"(1) IN GENERAL.—For purposes of this subpart, the term "less developed country corporation" means a foreign corporation which during the taxable year is engaged in the active conduct of one or more trades or businesses and—

"(A) 80 percent or more of the gross income of which for the taxable year is derived from sources within less developed countries other than as foreign base company income or as previously excluded foreign base company income withdrawn from qualified investment in less developed country corporations,

"(B) 80 percent or more in value of the assets of which on each day of the taxable year consists of—

"(i) property used in such trades or businesses and located in less developed countries,

"(ii) money, and deposits with persons carrying on the banking business, located in less developed countries,

"(iii) stock, and obligations which, at the time of their acquisition, have a maturity of 5 years or more, of any other less developed country corporation,

"(iv) obligations of the government of a less developed country,

"(v) an investment which is required because of restrictions imposed by a less developed country, and

"(vi) property described in section 955(b)(2); and

"(C) is created or organized under the laws of one of the less developed countries in which property described in subparagraph (B) (1) is located.

For purposes of subparagraph (A), the determination as to whether income is derived from sources within less developed countries shall be made under regulations prescribed by the Secretary or his delegate and, for purposes of subparagraph (A) only, amounts previously excluded from foreign base company income withdrawn from qualified investment in less developed country corporations shall be treated as included in gross income.

"(2) LESS DEVELOPED COUNTRY DEFINED.—For purposes of this subpart, the term "less developed country" means (in respect of any foreign corporation) any foreign country (other than an area within the Sino-Soviet bloc) or any possession of the United States, with respect to which on the first day of the taxable year, there is in effect an Executive order by the President of the United States designating such country or possession as an economically less developed country for purposes of this subpart. For purposes of the preceding sentence, an overseas territory, department, province, or possession may be treated as a separate country. No designation shall be made under this paragraph with respect to Australia, Austria, Belgium, Canada, Denmark, France, Germany (Federal Republic), Hong Kong, Italy, Japan, Liechtenstein, Luxembourg, Monaco, Netherlands, New Zealand, Norway, San Marino, Sweden, Switzerland, Union of South Africa, United Kingdom.

"(b) FOREIGN BASE COMPANY INCOME.—For purposes of section 952(a)(2), the term "foreign base company income" means for any taxable year the sum of—

"(1) the foreign personal holding company income for the taxable year (determined under subsection (d)),

"(2) the foreign base company sales income for the taxable year (determined under subsection (e)), and

"(3) the foreign base company services income for the taxable year (determined under subsection (f)).

"(c) EXCLUSIONS AND SPECIAL RULES.—

"(1) CERTAIN DIVIDENDS AND INTEREST FROM LESS DEVELOPED COUNTRY CORPORATIONS EXCLUDED.—For purposes of subsection (b), foreign base company income does not include dividends and interest received during the taxable year by a controlled foreign corporation from qualified investments in less developed country corporations (as defined in section 954(d)), to the extent that such dividends and interest do not exceed the increase for the taxable year in qualified investments in less developed country corporations of the controlled foreign corporation (as determined under subsection (g)).

"EXCEPTION FOR FOREIGN CORPORATIONS NOT AVAILABLE OF TO REDUCE TAXES.—For purposes of subsection (b), foreign base company income does not include any item of income received by a controlled foreign corporation if it is established to the satisfaction of the Secretary or his delegate with respect to such item that the creation or organization of the controlled foreign corporation receiving such item under the laws of the foreign country in which it is incorporated does not have the effect of substantial reduction of income, war profits, excess profits, or similar taxes.

"(3) ITEMS OF INCOME TO BE INCLUDED ONLY ONCE.—If an item of income would, but for the provisions of this paragraph, be includible as an item of income under more than one paragraph of subsection (b), such item shall be included under the paragraph specified by regulations prescribed by the Secretary or his delegate.

"(d) FOREIGN PERSONAL HOLDING COMPANY INCOME.—

"(1) IN GENERAL.—For purposes of subsection (b)(1), the term "foreign personal holding company income" means the foreign personal holding company income (as defined in section 553), modified and adjusted as provided in paragraphs (2), (3), and (4).

"(2) RENTS INCLUDED WITHOUT REGARD TO 50 PERCENT LIMITATION.—For purposes of paragraph (1), all rents shall be included in foreign personal holding company income without regard to whether or not such rents constitute more than 50 percent of gross income.

"(3) CERTAIN INCOME DERIVED IN ACTIVE CONDUCT OF TRADE OR BUSINESS.—For purposes of paragraph (1), foreign personal holding company income does not include dividends, interest, rents, and royalties which—

"(A) are derived in the active conduct of a trade or business; and

"(B) are received from a person other than a related person (within the meaning of subsection (e)(3)).

"(4) CERTAIN INCOME RECEIVED FROM RELATED PERSONS.—For purposes of paragraph (1), foreign personal holding company income does not include—

"(A) dividends and interest received from a related person which (i) is organized under the laws of the same foreign country under the laws of which the controlled foreign corporation is created or organized, and (ii) has a substantial part of its assets used in its trade, or business located in such same foreign country; or

"(B) rents, royalties, and similar amounts received from a related person for the use of, or the privilege of using, property within the country under the laws of which the controlled foreign corporation is created or organized.

"(e) FOREIGN BASE COMPANY SALES INCOME.—

"(1) IN GENERAL.—For purposes of subsection (b)(2), the term "foreign base com-

pany sales income" means income (whether in the form of profits, commissions, fees, or otherwise) derived in connection with the purchase of personal property from a related person and its sale to any person, the sale of personal property to any person on behalf of a related person, the purchase of personal property from any person and its sale to a related person, or the purchase of personal property from any person on behalf of a related person, where—

"(A) the property which is purchased (or in the case of property sold on behalf of a related person, the property which is sold) is manufactured, produced, grown, or extracted outside the country under the laws of which the controlled foreign corporation is created or organized, and

"(B) the property is sold for use, consumption, or disposition outside such foreign country, or, in the case of property purchased on behalf of a related person, is purchased for use, consumption, or disposition outside such foreign country.

"(2) CERTAIN BRANCH INCOME.—For purposes of determining foreign base company sales income (within the terms of paragraph (1)), in situations in which the carrying on of activities by a controlled foreign corporation through a branch or similar establishment outside the country of incorporation of the controlled foreign corporation has substantially the same effect as if such branch or similar establishment were a wholly owned subsidiary corporation deriving such income, then, under regulations prescribed by the Secretary or his delegate, the income attributable to the carrying on of such activities of such branch or similar establishment shall be treated as income derived by a wholly owned subsidiary of the controlled foreign corporation and shall constitute foreign base company sales income of the controlled foreign corporation.

"(3) RELATED PERSON DEFINED.—For purposes of this section, a person is a related person with respect to a controlled foreign corporation, if—

"(A) such person is an individual, partnership, trust, or estate which controls the controlled foreign corporation;

"(B) such person is a corporation which controls, or is controlled by, the controlled foreign corporation; or

"(C) such person is a corporation which is controlled by the same person or persons which control the controlled foreign corporation.

For purposes of the preceding sentence, control means the ownership, directly or indirectly, of stock possessing more than 50 percent of the total combined voting power of all classes of stock entitled to vote. For purposes of this paragraph, the rules for determining ownership of stock prescribed by section 957 shall apply.

"(f) FOREIGN BASE COMPANY SERVICES INCOME.—For purposes of subsection (b)(3), the term "foreign base company services income" means income (whether in the form of compensation, commissions, fees, or otherwise) derived in connection with the performance or furnishing of technical, managerial, engineering, architectural, scientific, skilled, industrial, commercial, or like services which are—

"(1) performed or furnished for or on behalf of any related person (within the meaning of subsection (e)(3)), and

"(2) are performed or furnished for or in connection with business activities carried on by such related person outside the country under the laws of which the controlled foreign corporation is created or organized.

"(g) INCREASE IN QUALIFIED INVESTMENTS IN LESS DEVELOPED COUNTRY CORPORATIONS.—For purposes of subsection (c)(1), the increase for any taxable year in qualified investments in less developed country corporations of any controlled foreign corporation is the amount by which—

"(1) the qualified investments in less developed country corporations (as defined in section 954(b)) of the controlled foreign corporation at the close of the taxable year, exceeds

"(2) the qualified investments in less developed country corporations (as so defined) of the controlled foreign corporation at the close of the preceding taxable year.

"SEC. 954. WITHDRAWAL OF PREVIOUSLY EXCLUDED FOREIGN BASE COMPANY INCOME FROM QUALIFIED INVESTMENT.

"(a) GENERAL RULES.—

"(1) **AMOUNT WITHDRAWN.**—For purposes of this subpart, the amount of previously excluded foreign base company income of any controlled corporation withdrawn from investment in less developed country corporations for any taxable year is an amount equal to the decrease in the amount of qualified investments in less developed country corporations of the controlled foreign corporation for such year, but only to the extent that the amount of such decrease does not exceed an amount equal to—

"(A) the sum of the amounts excluded under section 953(b)(1) from the foreign base company income of such corporation for all prior taxable years, reduced by

"(B) the sum of the amounts previously excluded from foreign base company income withdrawn from investment in less developed country corporations of such corporation determined under this subsection for all prior taxable years.

"(2) **DECREASE IN QUALIFIED INVESTMENTS.**—For purposes of paragraph (1), the amount of the decrease in qualified investments in less developed country corporations of any controlled foreign corporation for any taxable year is the amount by which—

"(A) the amount of qualified investments in less developed country corporations of the controlled foreign corporation at the close of the preceding taxable year, exceeds

"(B) the amount of qualified investments in less developed country corporations of the controlled foreign corporation at the close of the taxable year, to the extent the amount of such decrease does not exceed the sum of the earnings and profits for the taxable year and the earnings and profits accumulated for prior taxable years beginning after December 31, 1962. For purposes of this paragraph, if qualified investments in less developed country corporations are disposed of by the controlled foreign corporation during the taxable year, the amount of the decrease in qualified investments in less developed country corporations of such controlled foreign corporation for such year shall be reduced by an amount equal to the amount (if any) by which the losses on such dispositions during such year exceed the gains on such dispositions during such year.

"(3) **PRO RATA SHARE OF AMOUNT WITHDRAWN.**—In the case of any United States shareholder the pro rata share of the amount of previously excluded foreign base company income of any controlled foreign corporation withdrawn from investment in less developed country corporations for any taxable year is his pro rata share of the amount determined under paragraph (1).

"(b) QUALIFIED INVESTMENTS IN LESS DEVELOPED COUNTRY CORPORATIONS.—

"(1) **IN GENERAL.**—For purposes of this subpart, the term "qualified investments in less developed country corporations" means property acquired after December 31, 1962, which is—

"(A) stock of a less developed country corporation held by the controlled foreign corporation, but only if the controlled foreign corporation owns 10 percent or more of the total combined voting power of all classes of stock, or of the total value of shares of all classes of stock, of such less developed country corporation; or

"(B) an obligation of a less developed country corporation held by the controlled foreign corporation, which, at the time of its acquisition by the controlled foreign corporation, has a maturity of 5 years or more, but only if the controlled foreign corporation owns 10 percent or more of the total combined voting power of all classes of stock, or of the total value of shares of all classes of stock, of such less developed country corporation.

"(2) **COUNTRY CEASES TO BE LESS DEVELOPED COUNTRY.**—For purposes of this subpart, property which would be a qualified investment in less developed country corporations, but for the fact that a foreign country has, after the acquisition of such property by the controlled foreign corporation, ceased to be a less developed country, shall be treated as a qualified investment in less developed country corporations.

"(3) **INVESTMENTS AFTER CLOSE OF YEAR.**—For purposes of this subpart, a controlled foreign corporation may, under regulations prescribed by the Secretary or his delegate, elect to treat property described in paragraph (1) or (2) which was acquired after the close of a taxable year and on or before the close of the following taxable year, or on or before such day after the close of the following taxable year as such regulations may prescribe, as having been acquired on the last day of such year.

"(4) **AMOUNT ATTRIBUTABLE TO PROPERTY.**—The amount taken into account under this subpart with respect to any property described in paragraph (1) or (2) shall be its adjusted basis, reduced by any liability to which such property is subject.

"SEC. 955. INVESTMENT OF EARNINGS IN UNITED STATES PROPERTY.

"(a) **GENERAL RULES.**—For purposes of this subpart—

"(1) **AMOUNT OF INVESTMENT.**—The amount of earnings of a controlled foreign corporation invested in United States property at the close of any taxable year is the aggregate amount of such property held, directly or indirectly, by the controlled foreign corporation at the close of the taxable year, to the extent such amount would have constituted a dividend (determined after the application of section 954(a)) if it had been distributed.

"(2) **PRO RATA SHARE OF INCREASE FOR YEAR.**—In the case of any United States shareholder, the pro rata share of the increase for any taxable year in the earnings of a controlled foreign corporation invested in United States property is the amount determined by subtracting—

"(A) his pro rata share of the amount determined under paragraph (1) for the close of the preceding taxable year, reduced by amounts paid during the taxable year to which section 958(c)(1) applies, from

"(B) his pro rata share of the amount determined under paragraph (1) for the close of the taxable year.

"(3) **AMOUNT ATTRIBUTABLE TO PROPERTY.**—The amount taken into account under paragraph (1) or (2) with respect to any property shall be its adjusted basis, reduced by any liability to which the property is subject.

"(b) UNITED STATES PROPERTY DEFINED.—

"(1) **IN GENERAL.**—For purposes of subsection (a), the term "United States property" means any property acquired after December 31, 1962, which is—

"(A) tangible property located in the United States;

"(B) stock of a domestic corporation; or

"(C) an obligation of a United States person.

"(2) **EXCEPTIONS.**—For purposes of subsection (a), the term "United States property" does not include—

"(A) money, or deposits with persons carrying on the banking business, located in the United States;

"(B) property located in the United States which is purchased in the United States for export to, or use in, foreign countries;

"(C) any obligation of a United States person arising in connection with the sale of property if the amount of such obligation outstanding at no time during the taxable year exceeds the amount which would be ordinary and necessary to carry on the trade or business of both the other party to the sale transaction and the United States person had the sale been made between unrelated persons;

"(D) any aircraft, railroad rolling stock, vessel, motor vehicle, or container used in the transportation of persons or property in foreign commerce and used predominantly outside the United States; or

"(E) the amount of assets of an insurance company equivalent to the unearned premiums on outstanding business with respect to reinsurance contracts or insurance or annuity contracts—

"(i) in connection with property or liability arising out of activity in, or in connection with the lives or health of residents of, the United States, or

"(ii) in connection with property not included in subdivision (i) as the result of any arrangement whereby another corporation receives a substantially equal amount of premiums or other consideration in respect of any reinsurance or the issuing of any insurance or annuity contract in connection with property or liability arising out of activity in, or in connection with the lives or health of residents of, the United States.

"(c) **PLEDGES AND GUARANTEES.**—For purposes of subsection (a), a controlled foreign corporation shall, under regulations prescribed by the Secretary or his delegate, be considered as holding an obligation of a United States person if it is a pledgor or guarantor of such obligation.

"SEC. 956. CONTROLLED FOREIGN CORPORATIONS.

"(a) **GENERAL RULE.**—For purposes of this subpart, the term "controlled foreign corporation" means any foreign corporation of which more than 50 percent of the total combined voting power of all classes of stock entitled to vote is owned (within the meaning of section 957(a)), or is considered as owned by applying the rules of ownership of section 957(b), by United States shareholders on any day during the taxable year of such foreign corporation.

"(b) **CORPORATIONS ORGANIZED IN UNITED STATES POSSESSIONS.**—For purposes of this subpart, the term "controlled foreign corporation" does not include any corporation created or organized in the Commonwealth of Puerto Rico or a possession of the United States or under the law of the Commonwealth of Puerto Rico or a possession of the United States if—

"(1) 80 percent or more of the gross income of such corporation (computed without regard to section 931) for the 3-year period immediately preceding the close of the taxable year (or for such part of such period immediately preceding the close of such taxable year as may be applicable) was derived from sources within the Commonwealth of Puerto Rico or a possession of the United States; and

"(2) 50 percent or more of the gross income of such corporation (computed without regard to section 931) for such period, or for such part thereof, was derived from the active conduct within the Commonwealth of Puerto Rico or a possession of the United States of any trades or businesses constituting the manufacture or processing of goods, wares, merchandise, or other tangible personal property; the processing of agricultural or horticultural products or commodities (including but not limited to

livestock, poultry or fur-bearing animals); the catching or taking of any kind of fish or mining or extraction of natural resources, or any other manufacturing or processing of any products or commodities obtained from such activities; or the ownership or operation of hotels.

For purposes of paragraphs (1) and (2), the determination as to whether income was derived from sources within the Commonwealth of Puerto Rico or a possession of the United States and was derived from the active conduct of a described trade or business within the Commonwealth of Puerto Rico or a possession of the United States shall be made under regulations prescribed by the Secretary or his delegate.

“SEC. 957. RULES FOR DETERMINING STOCK OWNERSHIP.

“(a) DIRECT AND INDIRECT OWNERSHIP.—

“(1) GENERAL RULE.—For purposes of this subpart (other than sections 954 (b) (1) (A) and (B)), stock owned means—

“(A) stock owned directly, and

“(B) stock owned with the application of paragraph (2).

“(2) STOCK OWNERSHIP THROUGH FOREIGN ENTITIES.—For purposes of subparagraph (B) of paragraph (1), stock owned, directly or indirectly, by or for a foreign corporation, foreign partnership, or foreign trust or foreign estate (within the meaning of section 7701(a) (31)) shall be considered as being owned proportionately by its shareholders, partners, or beneficiaries. Stock considered to be owned by a person by reason of the application of the preceding sentence shall, for purposes of applying such sentence, be treated as actually owned by such person.

“(3) SPECIAL RULE FOR MUTUAL INSURANCE COMPANIES.—For purposes of applying paragraph (1) in the case of a foreign mutual insurance company, the term “stock” shall include any certificate entitling the holder to voting power in the corporation.

“(b) CONSTRUCTIVE OWNERSHIP.—For purposes of section 951(b), 953(e) (3), and 956, section 318(a) (relating to constructive ownership of stock) shall apply to the extent that the effect is to treat any United States person as a United States shareholder within the meaning of section 953(e) (3), or to treat a foreign corporation as a controlled foreign corporation under section 956, except—

“(1) In applying paragraph (1) (A) of section 318(a), stock owned by a nonresident alien individual (other than a foreign trust or foreign estate) shall not be considered as owned by a citizen or by a resident alien individual.

“(2) In applying the first sentence of subparagraphs (A) and (B), and in applying clause (i) of subparagraph (C), of section 318(a) (2)—

“(A) if a partnership, estate, trust, or corporation owns, directly or indirectly, more than 50 percent of the total combined voting power of all classes of stock entitled to vote of a corporation, it shall be considered as owning all the stock entitled to vote, and

“(B) if a partnership, estate, trust, or corporation owns, directly or indirectly, more than 50 percent of the total value of shares of all classes of stock of a corporation, it shall be considered as owning the total value of all of the outstanding stock of such corporation. The application of this subparagraph shall not have the effect of increasing voting power of a partner, beneficiary, or shareholder, for purposes of subparagraph (A).

“(3) Stock owned by a partnership, estate, trust, or corporation, by reason of the application of the second sentence of subparagraphs (A) and (B), and the application of clause (ii) of subparagraph (C), of section 318(a) (2), shall not be considered as owned by such partnership, estate, trust, or

corporation, for the purposes of applying the first sentence of subparagraphs (A) and (B), and in applying clause (i) of subparagraph (C), of section 318(a) (2).

“(4) In applying clause (1) of subparagraph (C) of section 318(a) (2), the phrase “10 percent” shall be substituted for the phrase “50 percent” used in subparagraph (C).

“SEC. 958. EXCLUSION FROM GROSS INCOME OF PREVIOUSLY TAXED EARNINGS AND PROFITS.

“(a) EXCLUSION FROM GROSS INCOME OF UNITED STATES PERSONS.—For purposes of this chapter, the earnings and profits for a taxable year of a foreign corporation attributable to amounts which are, or have been, included in the gross income of a United States shareholder under section 951(a) shall not, when—

“(1) such amounts are distributed to, or

“(2) such amounts would, but for this subsection, be included under section 951 (a) (1) (B) in the gross income of,

such shareholder (or any other United States person who acquires from any person any portion of the interest of such United States shareholder in such foreign corporation, but only to the extent of such portion, and subject to such proof of the identity of such interest as the Secretary or his delegate may by regulations prescribe) directly, or indirectly through a chain of ownership described under section 957(a), be again included in the gross income of such United States shareholder (or of such other United States person).

“(b) EXCLUSION FROM GROSS INCOME OF CERTAIN FOREIGN SUBSIDIARIES.—For purposes of section 951(a), the earnings and profits for a taxable year of a controlled foreign corporation attributable to amounts which are, or have been, included in the gross income of a United States shareholder under section 951(a), shall not, when distributed through a chain of ownership described under section 957(a), be also included in the gross income of another controlled foreign corporation in such chain for purposes of the application of section 951(a) to such other controlled foreign corporation with respect to such United States shareholder (or to any other United States shareholder who acquires from any person any portion of the interest of such United States shareholder in the controlled foreign corporation, but only to the extent of such portion, and subject to such proof of identity of such interest as the Secretary or his delegate may prescribe by regulations).

“(c) ALLOCATION OF DISTRIBUTIONS.—For purposes of subsections (a) and (b), section 316(a) shall be applied by applying paragraph (2) thereof, and then paragraph (1) thereof—

“(1) first to earnings and profits attributable to amounts included in gross income under section 951(a) (1) (B) (or which would have been included except for subsection (a) (2)),

“(2) then to earnings and profits attributable to amounts included in gross income under section 951(a) (1) (A) (but reduced by amounts not included under section 951(a) (1) (B) because of the exclusion in subsection (a) (2), and

“(3) then to other earnings and profits.

“(d) DISTRIBUTIONS EXCLUDED FROM GROSS INCOME NOT TO BE TREATED AS DIVIDENDS.—Except as provided in section 959(a) (3), any distribution excluded from gross income under subsection (a) shall be treated, for purposes of this chapter, as a distribution which is not a dividend.

“SEC. 959. SPECIAL RULES FOR FOREIGN TAX CREDIT.

“(a) TAXES PAID BY A FOREIGN CORPORATION.—

“(1) GENERAL RULE.—For purposes of subpart A of this part, if there is included, under section 951(a), in the gross income of a domestic corporation any amount attributable to earnings and profits—

“(A) of a foreign corporation at least 10 percent of the voting stock of which is directly owned by such domestic corporation, or

“(B) of a foreign corporation at least 50 percent of the voting stock of which is directly owned by a foreign corporation at least 10 percent of the voting stock of which is in turn directly owned by such domestic corporation,

then, under regulations prescribed by the Secretary or his delegate, such domestic corporation shall be deemed to have paid the same proportion of the total income, war profits, and excess profits taxes paid (or deemed paid, if paragraph (4) applies) by such foreign corporation to a foreign country or possession of the United States for the taxable year which the amount of earnings and profits of such foreign corporation so included in gross income of the domestic corporation bears to the entire amount of the total earnings and profits of such foreign corporation for such taxable year.

“(2) TAXES PREVIOUSLY DEEMED PAID BY DOMESTIC CORPORATION.—If a domestic corporation receives a distribution from a foreign corporation, any portion of which is excluded from gross income under section 958, the income, war profits, and excess profits taxes paid or deemed paid by such foreign corporation to any foreign country or to any possession of the United States in connection with the earnings and profits of such foreign corporation from which such distribution is made shall not be taken into account for purposes of section 902, to the extent such taxes were deemed paid by such domestic corporation under paragraph (1) for any prior taxable year.

“(3) TAXES PAID BY FOREIGN CORPORATION AND NOT PREVIOUSLY DEEMED PAID BY DOMESTIC CORPORATION.—Any portion of a distribution from a foreign corporation received by a domestic corporation which is excluded from gross income under section 958(a) shall be treated by the domestic corporation as a dividend, solely for purposes of taking into account under section 902 any income, war profits, or excess profits taxes paid to any foreign country or to any possession of the United States, on or with respect to the accumulated profits of such foreign corporation from which such distribution is made, which were not deemed paid by the domestic corporation under paragraph (1) for any prior taxable year.

“(4) TAXES PAID BY A FOREIGN SUBSIDIARY.—If subparagraph (A) of paragraph (1) applies with respect to an amount included in gross income under section 951(a) for a taxable year, then such amount shall be considered a dividend for purpose of the application of section 902(b).

“(5) INCLUSION IN GROSS INCOME.—
“For inclusion in gross income of amount equal to taxes deemed paid under paragraph (1), see section 78.

“(b) SPECIAL RULES FOR FOREIGN TAX CREDIT IN YEAR OF RECEIPT OF PREVIOUSLY TAXED EARNINGS AND PROFITS.—

“(1) INCREASE IN SECTION 904 LIMITATION.—In the case of any taxpayer who—

“(A) either (i) chose to have the benefits of subpart A of this part for a taxable year in which he was required under section 951 (a) to include in his gross income an amount in respect of a controlled foreign corporation, or (ii) did not pay or accrue for such taxable year any income, war profits, or excess profits taxes to any foreign country or to any possession of the United States, and

“(B) chooses to have the benefits of subpart A of this part for the taxable year in which he receives a distribution or amount which is excluded from gross income under section 958(a) and which is attributable to earnings and profits of the controlled foreign corporation which was included in his gross income for the taxable year referred to in subparagraph (A), and

“(C) for the taxable year in which such distribution or amount is received, pays, or is deemed to have paid, or accrues income, war profits, or excess profits taxes to a foreign country or to any possession of the United States with respect to such distribution or amount,

the applicable limitation under section 904 for the taxable year in which such distribution or amount is received shall be increased as provided in paragraph (2), but such increase shall not exceed the amount of such taxes paid, or deemed paid, or accrued with respect to such distribution or amount.

“(2) AMOUNT OF INCREASE.—The amount of increase of the applicable limitation under section 904(a) for the taxable year in which the distribution or amount referred to in paragraph (1) (B) is received shall be an amount equal to—

“(A) the amount by which the applicable limitation under section 904(a) for the taxable year referred to in paragraph (1) (A) was increased by reason of the inclusion in gross income under section 951(a) of the amount in respect of the controlled foreign corporation, reduced by

“(B) the amount of any income, war profits, and excess profits taxes paid, or deemed paid, or accrued to any foreign country or possession of the United States which were allowable as a credit under section 901 for the taxable year referred to in paragraph (1) (A) and which would not have been allowable but for the inclusion in gross income of the amount described in subparagraph (A).

“(3) CASES IN WHICH TAXES NOT TO BE ALLOWED AS DEDUCTION.—In the case of any taxpayer who—

“(A) chose to have the benefits of subpart A of this part for a taxable year in which he was required under section 951(a) to include in his gross income an amount in respect of a controlled foreign corporation, and

“(B) does not choose to have the benefits of subpart A of this part for the taxable year in which he receives a distribution or amount which is excluded from gross income under section 958(a) and which is attributable to earnings and profits of the controlled foreign corporation which was included in his gross income for the taxable year referred to in subparagraph (A),

no deduction shall be allowed under section 164 for the taxable year in which such distribution or amount is received for any income, war profits, or excess profits taxes paid or accrued to any foreign country or to any possession of the United States on or with respect to such distribution or amount.

“(4) INSUFFICIENT TAXABLE INCOME.—If an increase in the limitation under this subsection exceeds the tax imposed by this chapter for such year, the amount of such excess shall be deemed an overpayment of tax for such year.

“SEC. 960. ADJUSTMENTS TO BASIS OF STOCK IN CONTROLLED FOREIGN CORPORATION AND OF OTHER PROPERTY.

“(a) INCREASE IN BASIS.—Under regulations prescribed by the Secretary or his delegate, the basis of a United States shareholder's stock in a controlled foreign corporation, and the basis of property of a United States shareholder by reason of which he is considered under section 957(a)(2) as owning stock of a controlled foreign corporation,

shall be increased by the amount required to be included in his gross income under section 951(a) with respect to such stock or with respect to such property, as the case may be, but only to the extent to which such amount was included in the gross income of such United States shareholder.

“(b) REDUCTION IN BASIS.—

“(1) IN GENERAL.—Under regulations prescribed by the Secretary or his delegate, the adjusted basis of stock or other property with respect to which a United States shareholder or a United States person receives an amount which is excluded from gross income under section 958(a) shall be reduced by the amount so excluded.

“(2) AMOUNT IN EXCESS OF BASIS.—To the extent that an amount excluded from gross income under section 958(a) exceeds the adjusted basis of the stock or other property with respect to which it is received, the amount shall be treated as gain from the sale or exchange of property.

“SEC. 961. MISCELLANEOUS PROVISIONS.

“(a) EARNINGS AND PROFITS.—For purposes of this subpart, the earnings and profits of any foreign corporation, and the deficit in earnings and profits of any foreign corporation, for any taxable year shall be determined according to rules substantially similar to those applicable to domestic corporations, under regulations prescribed by the Secretary or his delegate.

“(b) BLOCKED FOREIGN INCOME.—Under regulations prescribed by the Secretary or his delegate, no part of the earnings and profits of a controlled foreign corporation for any taxable year shall be included in earnings and profits for purposes of sections 952, 954, and 955, if it is established to the satisfaction of the Secretary or his delegate that such part could not have been distributed by the controlled foreign corporation to United States shareholders who own (within the meaning of section 957(a)) stock of such controlled foreign corporation because of currency or other restrictions or limitations imposed under the laws of any foreign country.

“(c) RECORDS AND ACCOUNTS OF UNITED STATES SHAREHOLDERS.—The Secretary or his delegate may by regulations require each person who is, or has been, a United States shareholder of a controlled foreign corporation to maintain such records and accounts as may be prescribed by such regulations as necessary to carry out the provisions of this subpart.

“SEC. 962. INCLUSION IN GROSS INCOME ON CONSOLIDATED BASIS OF EARNINGS AND PROFITS.

“(a) GENERAL RULE.—A United States shareholder may elect to include in gross income under section 951 on a consolidated basis the earnings and profits (less his pro rata share of deficits) of controlled foreign corporations.

“(b) REGULATIONS.—The Secretary or his delegate shall prescribe such regulations as he may deem necessary in order that the tax liability with respect to the earnings and profits (less deficits) of controlled foreign corporations for which the election provided for under subsection (a) is exercised and of each separate corporation, both during and after the period of such consolidation, may be returned, determined, computed, assessed, collected, and adjusted, in such manner as clearly to reflect the income tax liability and the various factors necessary for determination of such liability, and in order to prevent avoidance of such tax liability.

“(b) TECHNICAL AND CLERICAL AMENDMENTS.—

“(1) Section 551(b) (relating to foreign personal holding company income included in gross income of United States shareholders) is amended by adding at the end thereof the following new sentence: ‘The amount

included in the gross income of any United States shareholder for any taxable year under the preceding sentence shall be reduced by such shareholder's proportionate share of the undistributed personal holding company income which is included in his gross income under section 951(a)(1)(A) (relating to amounts included in gross income of United States shareholders) for such taxable year as his pro rata share of the earnings and profits of the company.’

“(2) Section 901 (relating to foreign tax credit) is amended by striking out ‘section 902’ and inserting in lieu thereof ‘sections 902 and 960’.

“(3) Section 902(e) is amended to read as follows:

“(e) CROSS REFERENCES.—

“(1) For application of subsections (a) and (b) with respect to taxes deemed paid in a prior taxable year by United States shareholder with respect to a controlled foreign corporation, see section 960.

“(2) For reduction of credit with respect to dividends paid out of accumulated profits for years for which certain information is not furnished, see section 6038.’

“Section 904(f) is amended to read as follows:

“(f) CROSS REFERENCES.—

“(1) For increase of applicable limitation under subsection (a) for taxes paid with respect to amounts received which were included in the gross income of the taxpayer for a prior taxable year as a United States shareholder with respect to a controlled foreign corporation, see section 960(b).

“(2) For special rule relating to the application of the credit providing by section 901 in the case of affiliated groups which include Western Hemisphere trade corporations for years in which the limitation provided by subsection (a)(2) applies, see section 1503(d).’

“(5) The table of subparts for part III of subchapter N of chapter 1 is amended by adding at the end thereof the following:

“SUBPART F. CONTROLLED FOREIGN CORPORATIONS.’

“(6) Section 1016(a) (relating to adjustments to basis) is amended—

“(A) by striking out the period at the end of paragraph (18) and inserting in lieu thereof a semicolon; and

“(B) by adding after paragraph (18) the following new paragraph:

“(19) to the extent provided in section 961 in the case of stock in controlled foreign corporations (or foreign corporations which were controlled foreign corporations) and of property by reason of which a person is considered as owning such stock.’

“(c) EFFECTIVE DATE.—The amendments made by this section shall apply with respect to taxable years of foreign corporations beginning after December 31, 1962, and to taxable years of United States shareholders within which or with which such taxable years of such foreign corporations end.”

Page 164, after line 18, insert the following new section:

“SEC. . SALES AND EXCHANGES OF PATENTS, ETC., TO CERTAIN FOREIGN CORPORATIONS.

“(a) TREATMENT OF GAIN AS ORDINARY INCOME.—Part IV of subchapter P of chapter 1 (relating to special rules for determining capital gains and losses) is amended by adding after section 1248 (as added by section 16 of this Act) the following new section:

“SEC. 1249. GAIN FROM CERTAIN SALES OR EXCHANGES OF PATENTS, ETC., TO FOREIGN CORPORATIONS.

“(a) GENERAL RULES.—Gain from the sale or exchange after December 31, 1962, of a patent, an invention, model, or design (whether or not patented), a copyright, a secret formula or process, or any other similar

property right to any foreign corporation by any United States person (as defined in section 7701(a) (30)) which controls such foreign corporation shall, if such gain would (but for the provisions of this subsection) be gain from the sale or exchange of a capital asset or of property described in section 1231, be considered as gain from the sale or exchange of property which is neither a capital asset nor property described in section 1231.

"(b) CONTROL.—For purposes of subsection (a), control means, with respect to any foreign corporation, the ownership, directly or indirectly, of stock possessing more than 50 percent of the total combined voting power of all classes of stock entitled to vote. For purposes of this subsection, the rules for determining ownership of stock prescribed by section 957 shall apply.

"(c) OTHER TRANSFERS OF PATENT RIGHTS, ETC., TO FOREIGN CORPORATIONS.—

"For allocation, etc., of income by the Secretary or his delegate, in case of corporations owned or controlled directly or indirectly by the same interests, see section 482(a)."

"(b) CLERICAL AMENDMENT.—The table of sections for such part IV is amended by adding at the end thereof the following:

"SEC. 1249. Gain from certain sales or exchanges of patents, etc., to foreign corporations."

"(c) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 1962."

Mr. GORE. Mr. President, this amendment is the identical text presented to the Committee on Finance by the Secretary of the Treasury. It proposes to require the annual payment of taxes by U.S. taxpayers on profits earned in foreign countries through foreign corporations controlled by U.S. taxpayers or foreign subsidiaries of U.S. corporations.

I have already spoken at considerable length on this subject in the debate on the pending bill. Earlier this year I made a series of four major addresses on this subject. Therefore, my views are well known to the Senate and are clearly a matter of record. It seems to me that this makes it unnecessary to debate the amendment at great length, unless Senators have questions or unless statements are made which require refutation or answer.

Existing tax law gives many advantages to business operations in foreign countries.

One of the factors now at work to draw economic activities abroad and keep them there is the tax magnet, the tax advantage, the tax subsidy existing in present U.S. law which favors operations in countries other than our own. This is not the only force at work, of course; but it is one about which Congress can do something effective at this session and in this bill. The pending bill contains many provisions affecting the taxation of income and profits earned abroad. Many of these provisions are meritorious and deserve support. The major deficiency in the bill in this respect is that it does not go far enough to do the job effectively.

The pending amendment is a substitute for section 12. As I have said, it is identical to the provision which the Treasury Department drafted. It follows the recommendation of President Kennedy. It was submitted to the Fi-

nance Committee by Secretary Dillon; and I introduced the amendment as a bill, after it had been presented to the Senate Finance Committee.

Section 12 is the principal section dealing with the taxation of foreign operations. As now drafted and included in the bill, it is a purely tax-haven approach to the problem. It is good as far as it goes, and would do about half the job which needs to be done. I wish to express gratitude that Congress is, on this subject, at least going in the right direction, finally. Only 2 years ago a bill, identified as H.R. 5, was nearing enactment; and it would have created a greater tax subsidy and would have provided greater incentive for the movement of American industry and the making of investments by American interests abroad. However, now that the Congress is proceeding in the right direction, we must do an effective job. Half a loaf is not enough, when the full loaf is attainable.

My amendment strikes directly at the heart of the entire question of the deferral of payment of U.S. income taxes. As the law now stands, U.S. income taxes on profits earned abroad through foreign corporations may be indefinitely or even permanently postponed. In the case of a foreign subsidiary corporation organized in a tax-haven country, this may amount to virtual forgiveness of all income taxes, both United States and foreign. Even in non-tax-haven countries, tax favors such as those now being given in southern Italy and elsewhere may eliminate all income taxes for several years, until the operation concerned has grown and matured through reinvestment of tax-free earnings. As I have said, the tax-haven approach embodied in the bill, while accomplishing something, is far from sufficient. We should, and I think we must, do more. What we must do if we are to make progress toward a real solution of this problem is to strike directly at the deferral privilege in our own tax law, so that U.S. taxpayers are taxed annually on the profits they realize through their foreign investments in technically foreign corporations which they control.

The Secretary of the Treasury has agreed that anything short of this would be but "piddling" with the job. I call the testimony of Secretary Dillon on this point to the attention of the Senate.

The President of the United States, in his message to Congress on April 20, 1961, said:

I, therefore, recommend that legislation be adopted which would, after a two-step transitional period, tax each year American corporations on their current share of the undistributed profits realized in that year by subsidiary corporations organized in economically advanced countries. This current taxation would also apply to individual shareholders of closely held corporations in those countries.

So, Mr. President, we have the request and the recommendation of President Kennedy, and we have the testimony of the Secretary of the Treasury, Douglas Dillon; and the Senate has before it an

amendment—drafted by the Treasury Department—to implement the recommendations of the President and the Secretary of the Treasury.

I ask the Senate to adopt it. I think it is a good provision. It will eliminate the tax subsidy for the movement of business and industry and jobs abroad.

As I have said, the pending amendment does exactly what President Kennedy sought and requested. The bill as it has come to the Senate from the Senate Finance Committee falls far short of this desirable end. The concern of American citizens with the flight abroad of business and jobs and capital is a deep one, and this is a serious problem. The outflow of capital adversely affects the national interest. It creates a severe balance-of-payments problem; and it is one of the big factors creating widespread unemployment in our country.

To illustrate the concern of working men and women, I wish to read to the Senate a telegram which I received today from Mr. George Meany, president of AFL-CIO. I believe other Members of the Senate received an identical telegram.

Senator GORE: AFL-CIO firmly believes that Gore amendment on foreign income is essential to tax equity and to prevent export of jobs of American workers. Finance Committee bill continues practice of subsidizing overseas investment through tax incentives. Therefore our tax laws are subsidizing manufacture of products abroad instead of in the United States, cutting exports and eliminating American jobs. Gore amendment would not prevent foreign investment. It would merely remove the tax incentive to such investment. I therefore urge you to vote for the Gore foreign income amendment.

GEORGE MEANY,
President, AFL-CIO.

The amendment to which this telegram refers is now pending at the desk, and upon this amendment we shall soon have a vote. The amendment provides that those U.S. taxpayers who own as much as 10 percent of the stock of a foreign corporation which is controlled by these American taxpayers will be taxed each year on their share of the profits made by these foreign corporations.

As President Kennedy has recommended, this amendment provides for an exception in the case of a corporation doing business in an underdeveloped country unless most of the income of that corporation is of a tax haven type.

For the benefit of those who have not had an opportunity to study the provisions of this amendment, let me give a few additional details. Under this amendment, deferral of taxes of U.S. taxpayers based on the income of controlled foreign corporations, as defined in the amendment, would be eliminated except, as I have noted, with regard to certain corporations operating legitimately in underdeveloped countries.

This approach to the problem is, of course, a more direct and all-inclusive approach than that contained in section 12 of the pending bill, which is aimed, as I have said, merely at tax-haven operations.

I submit that the tax-haven-operation approach will do only about 50 percent

of the job which needs to be done if we are going to put our tax laws in a position of neutrality with respect to domestic and foreign operations of U.S. interests.

This amendment would affect only foreign operations which are in fact controlled by American interests. A "controlled foreign corporation" is defined as one which is more than 50 percent owned by U.S. taxpayers each of whom owns at least 10 percent of the stock of the foreign corporation. As I have stated, an exception is made for legitimate operations in underdeveloped countries, and in this respect the amendment pretty well follows section 12 of the bill.

The tax-haven operations, even in underdeveloped countries, however, are included in operations to be taxed currently by providing that a "less-developed-country corporation" must not receive a sizable amount of its income from the typical tax-haven activities—that is, base-company income.

The amendment has been carefully drafted by technicians in the Treasury Department in consultation with our own experts here on the Hill. It has been reworked several times since it was first drafted at my request more than a year ago. So it comes, I believe, as a carefully drawn measure, with the recommendation and endorsement of President Kennedy and Secretary Dillon.

As Mr. Meany's telegram points out, my amendment in no way seeks to prevent U.S. citizens from investing their capital abroad, in whatever amounts they please. Perhaps the Congress should consider placing the export of capital under some reasonable regulation, but that question is not now before the Senate. My amendment does not propose that.

All that my amendment would do would be to require the U.S. owners of foreign corporate subsidiaries and foreign corporations controlled by American taxpayers to be amenable, on an annual basis, to the tax laws of the United States. In other words, the income from such corporations to the U.S. taxpayer who owns and controls such foreign corporations would be taxable on an annual basis.

Annual payment of taxes is not an innovation, Madam President, and every American taxpayer whose income is earned in the United States must pay such taxes annually. Why should we permit a corporation that builds up industry abroad through a technically foreign subsidiary and earns a profit in doing so to defer the payment of its taxes until such time as it may suit the purposes and desires of such corporation?

I do not know why we should discriminate against an American citizen or corporation who invests in economic and industrial development in the United States. Conversely, I do not see either the sense or justice in rewarding one with a tax favor who builds an industry and makes jobs in other countries.

Let me repeat and make perfectly plain that my amendment would not prevent any American taxpayer from investing to his heart's content in a foreign coun-

try, but I do respectfully submit that I do not think we should continue to reward him for doing so by means of favored tax treatment.

There may have been a time when our national interest was served by encouraging the investment of American capital abroad. I refer particularly to Western Europe, in its wartorn condition during the period following World War II. But that period has passed. Now business activity in Western Europe is growing at 2½ times the rate of economic growth of the United States. It is to Western Europe that much of our migrating capital is flowing, and most of this flow to Europe goes into manufacturing establishments.

We are now beginning to get the backwash of imports into the United States of goods manufactured abroad by corporations financed by American capital, employing American know-how, using well-known and well-established American trade names and brands.

The most difficult competition which an American businessman faces comes from imports of goods manufactured by American capital with American know-how abroad, bearing a trade name which has long been established in our country.

Mr. MORSE. Madam President, will the Senator yield?

The PRESIDING OFFICER. (Mrs. NEUBERGER in the chair). Does the Senator yield?

Mr. GORE. I yield.

Mr. MORSE. I am glad the Senator from Tennessee is emphasizing this point again, because it needs to be emphasized over and over. I should like to have my Democratic Party know that there is a growing resentment against Democratic Party policy in regard to this matter, as manifested in this bill and as illustrated by the Senator from Tennessee in the point he is now making.

What we are doing, in effect, is exporting American jobs abroad, to the great detriment and economic hardship of American labor, American farmers, and of American consumers generally.

I wish to cite two industries in which this is particularly notorious at the present time. The first is the movie industry. This has brought a great depression to the movie industry of this country, as American investors go abroad filming movies and bringing them to the United States, further depressing our movie industry. The other is the music industry, in regard to musical productions and the development of records, as a result of which a great many musicians in this country are out of work.

I am one Democrat who leaves the party on this issue. That does not mean I leave the party—I leave it on this issue, because the Democratic Party, in my judgment, is dead wrong. I do not know why we should play the Republicans' game for them.

Mr. GORE. I wish to point out to my distinguished friend that the amendment I have offered, which is now pending, was recommended by President Kennedy. It was drafted by the Treasury Department. It was submitted to the Senate Finance Committee. This is what

the administration requested, recommended, and desired.

I take it that the Senator's remark with respect to the Democratic Party applies not to the original recommendation by President Kennedy, but to the bill recommended by the Finance Committee, which is now before the Senate.

Mr. MORSE. And to the President's support of the bill now before the Senate.

Mr. GORE. I was hoping that before the vote the President might again request the Congress to do an effective job with respect to removing the preferential tax treatment of income earned abroad. I must say that I know of no official record which shows that either the President or the Secretary of the Treasury supports the provisions of section 12 of the pending bill.

Mr. MORSE. Madam President, will the Senator yield?

Mr. GORE. I will yield in a moment.

I read in the newspapers that the terms of the pending bill have the tacit support of the administration, whatever that means. But I am going by the record. We have seen the President's recommendations. We have heard the testimony by the Secretary of the Treasury in support of those recommendations. We have before us the text of the amendment presented by the administration.

Now I yield to the Senator.

Mr. MORSE. Is the Senator from Tennessee laboring under any mistaken notion that the President of the United States does not know the Senate is about to have a third reading of this bill?

Mr. GORE. I am sure the President is perfectly aware of the progress of this proposed legislation.

Mr. MORSE. The bill has been under debate in the Senate for a good many days, has it not?

Mr. GORE. Yes, indeed.

Mr. MORSE. The Secretary of the Treasury and the President of the United States have been in Washington, D.C., most of that time, have they not?

Mr. GORE. Yes.

Mr. MORSE. Does the Senator have any indication of any message which has been brought to us, directly or indirectly, officially or unofficially, of any disapproval by the President or by the Secretary of the Treasury of this bill?

Mr. GORE. No. On the other hand, I know of no record indicating any disapproval of the amendment which I have offered.

Mr. MORSE. I shall vote for the Senator's amendment, but I wish to state that I have recently returned from my State. I want the President of the United States to know that, in my judgment, the overwhelming majority of the people of my State will have none of this bill, as they will have none of the satellite bill and as they will have none of a whole series of mistakes being made in recent weeks in regard to legislation before the Senate.

Mr. GORE. Madam President, the senior Senator from Oregon referred to the movie industry. I recently read an advertisement of a movie in a Washington, D.C. newspaper. A statement

was made in the advertisement that this was the first major movie which had been made in Hollywood in a long while. I do not remember the exact time, but I believe it was 5 years.

The senior Senator from California on the floor of the Senate only a few days ago referred to Hollywood as a ghost city.

Mr. MORSE. Madam President, will the Senator yield?

Mr. GORE. I yield.

Mr. MORSE. I was about to say that in my part of the country we have some old western ghost towns. Not so long ago I went through the movie sets of Hollywood. I think it is quite appropriate to refer to them as the ghost town part of Hollywood.

Mr. GORE. This result has not occurred because movies are not being made. It is because the industry has moved abroad almost en masse as a result of our faulty tax laws. I propose to correct that.

Madam President, this issue is of far greater importance than the movie industry, important as that is, or than the recording industry, important as that is.

Last year, in the 12-month period, \$4½ billion of American capital was invested abroad, including retained earnings, depreciation allowances, and new money, a large part in manufacturing facilities. Meanwhile, the Senate was considering and passing a bill to help economically distressed areas in the United States. West Virginia was cited as were other States. There are many depressed communities in my own State. That law has not yet been too successful in relieving the stringent economic conditions in many areas of the United States which are in economic distress.

What would the \$4½ billion have accomplished if invested in the United States? The bill contains a provision known as the investment credit. It is estimated that the provision would provide \$1,300 million per year in tax reduction to American business. Investment credit is advocated on the ground that the great incentive of \$1,300 million in tax reduction would stimulate our economy, solve our unemployment problem, and generate economic activity that would swell the tax revenues of the Government. Compare that \$1,300 million with the \$4½ billion of American capital that was invested abroad last year.

The Senate by overwhelming vote has approved the investment credit. I ask it to vote to eliminate the tax incentive for investments abroad. As I have said many times, I know that there are other inducements that entice American capital into other countries. The Congress has no jurisdiction over the actions and the policies of other countries. But we do have jurisdiction over the tax policies and the tax laws of the United States. I am asking that we repeal the provision that grants deferral of taxes on income and profits earned abroad until such income has been repatriated to the United States. I shall not now speak at great length.

I call to the attention of Senators the addresses which I have previously made

on the subject. It is a subject to which I have been devoting concentrated study for almost 3 years. I believe I have learned a good deal about the problem. It is a serious one.

Some people think that the proposal of the President and the junior Senator from Tennessee would lead to economic isolation. Madam President, nothing could be further from the truth. The amendment is on all fours with the reciprocal trade program. The reciprocal trade program proposes to eliminate obstacles and barriers, insofar as practical, to the even flow of commerce between and among nations. The pending amendment which I have offered proposes to remove an incentive for a flow in one direction, a subsidy for the outflow of U.S. capital.

There are many communities in America that would be very happy if some foreign capital were invested in their home communities. It would provide jobs, profits, economic activity, the upbuilding of the State and the locality, and swell the revenues of the U.S. Treasury.

The same thing happens in foreign communities when American investment is made in manufacturing facilities abroad. The Ford Motor Co. has 130,000 employees in other countries. This will indicate the magnitude of the problem.

I hope that the Senate will ponder the issue. It goes to the very heart of the balance-of-payments problem, which is serious. It goes to the heart of the export of business, industry, and jobs. It goes to the heart of America's unemployment problem. I do not claim that the enactment of my amendment would provide a complete solution to any of these problems. But it would help all three. It is within the jurisdiction and the power of the United States to put into execution the provisions of the amendment, which I think would be very helpful.

Later I shall suggest the absence of a quorum. I shall ask for a yea-and-nay vote on the amendment, after debate has been concluded.

Mr. MANSFIELD. Madam President, would the Senator from Tennessee be agreeable to vote on the amendment at a time certain?

Mr. GORE. What time limit would the Senator suggest?

Mr. MANSFIELD. I would suggest that at 2 o'clock there be a quorum call, and immediately afterward, the vote.

Mr. GORE. Not later than 2. Would the Senator reserve for me the last 5 minutes in case I desire it?

Mr. MANSFIELD. If that would be agreeable, I should like to make a unanimous-consent request that there be a quorum call at 2 o'clock, and that immediately after the quorum call, the yeas and nays would be asked for, and that the—

Mr. KERR. Madam President, will the Senator yield?

Mr. MANSFIELD. I yield.

Mr. KERR. And that the time thereafter be divided 5 minutes to a side, and the Senator from Tennessee may have the remaining time.

Mr. MANSFIELD. No, the last 5 minutes before the quorum call.

Mr. GORE. I like the suggestion of the senior Senator from Oklahoma better. After the quorum is present, perhaps the senior Senator from Oklahoma and I could exchange views that might be helpful.

Mr. MANSFIELD. Madam President, I ask unanimous consent that, at the conclusion of a quorum call to be instituted, there be 20 minutes allotted for debate on the amendment, 10 minutes to each side, the time to be equally divided between the Senator from Tennessee [Mr. GORE] and the Senator from Oklahoma [Mr. KERR].

The PRESIDING OFFICER. Is there objection? The Chair hears none, and it is so ordered.

Mr. MANSFIELD. Madam President, I suggest the absence of a quorum.

The PRESIDING OFFICER. The clerk will call the roll.

The Chief Clerk proceeded to call the roll.

Mr. MANSFIELD. Mr. President, I ask unanimous consent that the order for the quorum call be rescinded.

The PRESIDING OFFICER (Mr. BURDICK in the chair). Without objection, it is so ordered.

Mr. MANSFIELD. Mr. President, in view of the unusual circumstances—and not to set a precedent—I ask unanimous consent that the yeas and nays may be ordered on the Gore amendment.

The PRESIDING OFFICER. Is there objection? The Chair hears none, and it is so ordered.

Mr. MANSFIELD. I wish to state again to the Senate that this is not to be considered a precedent.

The PRESIDING OFFICER. The time for debate is under control, with 10 minutes allotted to each side.

Mr. KERR. Do the 10 minutes on each side prior to the vote start now?

The PRESIDING OFFICER. The Senator is correct.

Mr. KERR. I yield myself 5 minutes.

I hope the amendment offered by the Senator from Tennessee [Mr. GORE] and the Senator from Illinois [Mr. DOUGLAS] may be resoundingly defeated. I really wish that every Member of the Senate could hear the Senator from Tennessee relate in complete detail what is contained in the amendment. Could he do so, no remarks would be necessary in opposition to it.

The amendment seeks to go completely contrary to the basic concept of the income tax law, which has long been the foundation pillar in our tax structure. Under our income tax law, income is taxed when received by the individual receiving it. The Senator from Tennessee made a statement that I was surprised to hear him make. He said every taxpayer of the United States must pay such taxes annually as earned as the Senator seeks to reach in this amendment.

If I know anything about the income tax law, and if I know anything about what is in the amendment of the Senator from Tennessee and the Senator from Illinois, that statement cannot be supported by the provisions of either.

Certainly it cannot be supported by the provisions of the income tax law, because under the income tax law a stockholder pays taxes on his dividends when he receives them. He does not pay taxes as the corporation in which he owns stock earns money. He does not pay his taxes until that corporation has passed those earnings on to its stockholders.

The Senator from Tennessee is of the opinion—I know he is because he said so—his amendment would stop the exporting of jobs; that his amendment would stop investment by Americans in foreign manufacturing corporations.

In my judgment, the Senator from Tennessee could not be in greater error. In my considered judgment, all that his amendment would do would be to change the investment by Americans, so far as they sought and desired to make investments in corporations doing business abroad, from corporations controlled by American stockholders to corporations controlled by foreign stockholders.

Drastic as his amendment is, it does not reach earnings in foreign corporations which are controlled by foreign stockholders, even to the extent of the earnings of those corporations and the beneficial effect of those earnings on Americans owning stock in those corporations. His amendment would tax earnings in American-controlled foreign corporations. His amendment would export jobs with reference to the corporations doing the manufacturing and with reference to the export of American industry selling its output for export to foreign corporations.

Any Senator knows that if an American group controlled a foreign corporation, there would be far more likelihood that they would buy the output of American factories and American industry and export it from this country for use by that foreign-controlled corporation, than would be the case of foreign corporations controlled by foreign management and foreign owners.

The PRESIDING OFFICER. The time of the Senator from Oklahoma has expired.

Mr. KERR. I yield myself 3 additional minutes.

The tendency would be for those corporations to buy their industrial products abroad. So the Senator from Tennessee would defeat the very purpose which he states that he seeks to accomplish.

His amendment would make it impossible for American investors abroad to compete with foreign competitors who do not have to pay the taxes with reference to manufacturing efforts which would be collected under the amendment of the Senator from Tennessee and the Senator from Illinois.

This proposal was before the House Committee on Ways and Means, and was rejected by that committee. The amendment was before the Committee on Finance, and was rejected by it. The Senators now offering the amendment are in the same posture as an automobile dealer would be who came forth this fall, when all others were presenting their 1963 models, and offered a model T or a

1925 model, seeking to compete with other automobile manufacturers who were in the field with their 1963 models.

This amendment would destroy the opportunity for Americans to do business abroad, compete in foreign markets, be customers for the American industrial production, and be in the posture of bringing back their money to this country as it was paid out, as it was earned and declared as dividends.

The bill before the Senate cures the tax haven provisions which now exist and stops the tax haven abuses now in being, but does not destroy the opportunity for Americans owning manufacturing companies to compete in foreign countries with domestic industry in those foreign countries.

I submit that the amendment should be rejected.

Mr. GORE. Mr. President, the distinguished senior Senator from Oklahoma seems to be laboring under the impression that the defeat of an amendment by the Committee on Finance in some way condemns it to outer darkness. I respectfully submit that, in the opinion of some, rejection of an amendment by the Committee on Finance may sometimes add luster to it. The 1963 model public interest amendments to the pending bill are more likely to be identified with those defeated by the committee than with those adopted by the committee.

I did not say that the amendment which I, along with the senior Senator from Illinois [Mr. DOUGLAS], have offered, would stop the export of jobs. I did not say that the amendment would stop the outflow of U.S. capital. I did not say the amendment would cure our balance-of-payments problem. I did not say it would solve our unemployment problem. I said it would remove the tax subsidy, the tax incentive, for the export of capital, industry, and jobs; that it would help to solve our balance-of-payments problem.

Let us consider the balance-of-payments problem. The Treasury Department estimated that this amendment would help the balance-of-payments problem by about \$400 million a year. That is a very sizable amount, indeed. I should like to read what the Secretary of the Treasury said about the pending bill and the subject matter of the pending amendment. His statement appears on page 455 of part 1 of the hearings:

Senator GORE. Unless the tax deferral problem is treated effectively, then we but piddle with the problem of preferential treatment of foreign income; would you agree with that?

Secretary DELON. I think that is it. We do hit the tax haven thing fairly well here, but the basic problem is in deferral, and that has not been touched at all.

Mr. President, that problem is not touched at all in the committee bill. It is this lodestone, this magnet, that may be the decisive factor, next year and the year after and the year after that, in the establishment of factories abroad, bringing unemployment to our own people, worsening our balance-of-payments problem, and increasing the import competition that comes most severely from goods manufactured abroad by Ameri-

can capital and American know-how, imported into the United States, sold by well-established distribution chains, under well-established and well-known American labels and brand names.

Mr. President, how much time have I left?

The PRESIDING OFFICER. Five and one-half minutes.

Mr. GORE. Mr. President, I should like to cite some statistics from a study and survey reported in the U.S. News & World Report for January 1, 1962. The report concerned 75 firms with substantial foreign sales. In 1950 these firms manufactured abroad 36 percent of the products they sold abroad. The same U.S. corporations in 1955 manufactured abroad 56 percent of their foreign sales. In 1960 the figure had increased to 68 percent. The trend is continuing.

So we find that American manufacturing abroad is displacing exports from U.S. factories; and then there is the backwash, which we are now beginning to get in large volume—the importation into the United States of those products manufactured abroad by these subsidiaries of U.S. corporations. Today, Mr. President, if only a little over 1 percent of the \$9 billion of sales by U.S.-owned European subsidiaries displaces sales from the United States or if 8 percent of the sales outside the country of production displace U.S. sales, the net export effect of U.S. subsidiary investment would be lost. As for creating domestic jobs, a dollar invested in Europe has the effect, through increased exports, of only 10 cents invested at home. But a dollar invested at home generates 40 cents worth of continuing production.

Foreign profits are becoming more important and inducing additional outflows of capital. The 1960 profits of foreign subsidiaries and branches of U.S.-controlled corporations totaled \$3,500 million after foreign taxes.

Mr. President, I wish to point out how much this means, and what an enticement it is to the movement abroad of American industry. A study by the American Management Association, conducted in 1960, and reported in Business Week for December 31, 1960, shows that:

Because of tax differentials, the reinvestment of foreign earnings over a 3-year period can provide roughly double the rate of profit accumulation for reinvestment that is possible under domestic tax schedules.

Think of that, Mr. President. I ask Senators who have engaged in our free-enterprise system to contemplate a situation in which in 3 years' time one can double his rate of profit accumulation for reinvestment abroad over what one could do here at home.

Again I ask, why do we provide a tax subsidy for this flight of capital? Why do we provide a tax incentive for the outflow of jobs and industry? What is the sense of it?

Mr. President, I am not proposing to stop the outflow of capital. Frankly, I feel that the time may be just around the corner when direct regulation may be considered by Congress. But I am not proposing that now. I am only propos-

ing to strike down the tax incentive for such export of capital.

I know that it is argued that the United States will receive a return on foreign investments. Perhaps it will; but we do not know just when that will happen. It may be 12 to 16 years before current investments pay off. The United Kingdom insists on a 2-year pay-back, before authorities there will authorize investment capital outflow.

The PRESIDING OFFICER. The time of the Senator from Tennessee has expired.

Mr. GORE. Mr. President, I see that my time has terminated.

Mr. MANSFIELD. Mr. President, how much time remains available to the Senator from Oklahoma?

The PRESIDING OFFICER. Two minutes.

Mr. MANSFIELD. I yield that time to the Senator from Tennessee.

Mr. GORE. I thank the distinguished majority leader.

The PRESIDING OFFICER. The Senator from Tennessee is recognized for 2 additional minutes.

Mr. GORE. Mr. President, I say now is the time to deal with this tax problem. The bill contains mild, timid, half-way effective treatment of the subject. I have offered an amendment which, in my opinion, will deal effectively with the subject; and in the opinion of the Secretary of the Treasury, the amendment will deal effectively with the subject.

I repeat that I have submitted an amendment which was drafted by the Treasury Department, was submitted to the Senate Finance Committee, was recommended by the Secretary of the Treasury, and was recommended by the President of the United States. It is true that the amendment does not bear the endorsement of the Senate Finance Committee; but I have every right to appeal that decision to the Senate.

The PRESIDING OFFICER. The additional time yielded to the Senator from Tennessee has expired.

Mr. GORE. Mr. President, I am ready for the vote to be taken.

The PRESIDING OFFICER. The question is on agreeing to the amendment of the Senator from Tennessee. On this question, the yeas and nays have been ordered; and the clerk will call the roll.

The legislative clerk called the roll.

Mr. HUMPHREY. I announce that the Senator from Mississippi [Mr. EASTLAND], the Senator from Washington [Mr. MAGNUSON], and the Senator from Virginia [Mr. BYRD] are absent on official business.

I further announce that the Senator from New Mexico [Mr. ANDERSON], the Senator from Nevada [Mr. BIBLE], the Senator from Wyoming [Mr. HICKEY], and the Senator from Missouri [Mr. SYMINGTON] are necessarily absent.

I further announce that, if present and voting, the Senator from Wyoming [Mr. HICKEY] and the Senator from Mississippi [Mr. EASTLAND] would each vote "nay."

Mr. KUCHEL. I announce that the Senator from Utah [Mr. BENNETT], the

Senator from South Dakota [Mr. BOTTUM], the Senator from Arizona [Mr. GOLDWATER], the Senator from Kentucky [Mr. MORTON] and the Senator from New Hampshire [Mr. MURPHY] are necessarily absent.

If present and voting, the Senator from Utah [Mr. BENNETT], the Senator from South Dakota [Mr. BOTTUM], the Senator from Kentucky [Mr. MORTON] and the Senator from New Hampshire [Mr. MURPHY] would each vote "nay."

The result was announced—yeas 30, nays 58, as follows:

[No. 242 Leg.]

YEAS—30

Bartlett	Hart	Morse
Burdick	Hill	Moss
Byrd, W. Va.	Jackson	Muskie
Carroll	Kefauver	Neuberger
Church	Lausche	Pastore
Clark	Long, Hawaii	Proxmire
Douglas	Mansfield	Randolph
Ervin	McGee	Sparkman
Gore	McNamara	Yarborough
Gruening	Metcalfe	Young, Ohio

NAYS—58

Alken	Hartke	Pearson
Allott	Hayden	Pell
Beall	Hickenlooper	Prouty
Boggs	Holland	Robertson
Bush	Hruska	Russell
Butler	Humphrey	Saltonstall
Cannon	Javits	Scott
Capehart	Johnston	Smathers
Carlson	Jordan, N.C.	Smith, Mass.
Case	Jordan, Idaho	Smith, Maine
Chavez	Keating	Stennis
Cooper	Kerr	Talmadge
Cotton	Kuchel	Thurmond
Curtis	Long, Mo.	Tower
Dirksen	Long, La.	Wiley
Dodd	McCarthy	Williams, N.J.
Ellender	McClellan	Williams, Del.
Engle	Miller	Young, N. Dak.
Fong	Monroney	
Fulbright	Mundt	

NOT VOTING—12

Anderson	Byrd, Va.	Magnuson
Bennett	Eastland	Morton
Bible	Goldwater	Murphy
Bottum	Hickey	Symington

So Mr. GORE's amendment was rejected.

Mr. KERR. Mr. President, I move to reconsider the action whereby the amendment was rejected.

Mr. DIRKSEN. Mr. President, I move to lay that motion on the table.

The PRESIDING OFFICER. The question is on agreeing to the motion to lay on the table the motion to reconsider.

The motion to lay on the table was agreed to.

Mr. HARTKE. Mr. President, I offer my amendment 8-29-62—A, and I ask for the yeas and nays on the amendment.

The yeas and nays were ordered.

The PRESIDING OFFICER. Without objection, the amendment will be printed in the RECORD without being read.

The amendment is as follows:

On page 354, beginning with line 4, strike out all through line 19 on page 369 and insert the following:

"SEC. 19. WITHHOLDING OF INCOME TAX AT SOURCE ON INTEREST, DIVIDENDS, AND PATRONAGE DIVIDENDS.

"(a) IN GENERAL.—

"(1) AMENDMENT OF SUBTITLE C.—Subtitle C (relating to employment taxes and collection of income tax at source) is amended by redesignating chapter 25 as chapter 26 and by inserting after chapter 24 the following new chapter:

"CHAPTER 25—COLLECTION OF INCOME TAX AT SOURCE ON INTEREST, DIVIDENDS, AND PATRONAGE DIVIDENDS

"SUBCHAPTER A. Interest.

"SUBCHAPTER B. Dividends.

"SUBCHAPTER C. Patronage dividends.

"SUBCHAPTER D. General provisions.

"Subchapter A—Interest

"Sec. 3451. Income tax collected at source on interest.

"Sec. 3452. Interest defined.

"SEC. 3451. INCOME TAX COLLECTED AT SOURCE ON INTEREST.

"(a) REQUIREMENT OF WITHHOLDING.—Except as otherwise provided in this chapter, every person who pays interest shall deduct and withhold on such interest a tax equal to 20 percent of the amount thereof.

"(b) PAYEE UNKNOWN.—If the withholding agent is unable to determine the person to whom the interest is payable, the tax under this section shall be deducted and withheld at the time payment of the interest would be made if such person were known.

"(c) CROSS REFERENCES.—

"(1) For credit, against income tax of the recipient of the income, of amounts deducted and withheld under this section, see section 39.

"(2) For special rules as to credit or refund of such amounts, see sections 3484, 3485, 3486, 3487, and 3505.

"(3) For exemption from requirement of deducting and withholding on certain interest paid to certain persons, see section 3483.

"SEC. 3452. INTEREST DEFINED.

"(a) GENERAL RULE.—For purposes of this chapter, the term "interest" means—

"(1) interest on evidences of indebtedness (including bonds, debentures, notes, and certificates) issued by a corporation with interest coupons or in registered form, and, to the extent provided in regulations prescribed by the Secretary or his delegate, interest on other evidences of indebtedness issued by a corporation of a type offered by corporations to the public;

"(2) interest on amounts held by an insurance company under an agreement to pay interest thereon;

"(3) interest on deposits with stockbrokers;

"(4) interest on obligations of the United States; and

"(5) in the case of a non-interest-bearing obligation of the United States—

"(A) issued on a discount basis, and

"(B) having a maturity date more than one year from the date of issue,

the amount by which the amount paid on surrender or redemption exceeds the issue price.

"(b) EXCEPTIONS.—For purposes of this chapter, the term "interest" does not include—

"(1) interest on obligations described in section 103(a) (1) or (3) (relating to interest on certain governmental obligations);

"(2) any amount paid by—

"(A) a foreign government or international organization,

"(B) a foreign corporation not engaged in trade or business within the United States,

"(C) a nonresident alien individual not engaged in trade or business within the United States, or

"(D) a partnership not engaged in trade or business within the United States and composed in whole or in part of nonresident aliens;

"(3) any amount paid by one corporation to another corporation, if both corporations are members of the same affiliated group which filed a consolidated return for the preceding taxable year of the affiliated group;

"(4) interest subject to withholding under subchapter A of chapter 3 (sec. 1441 and following, relating to withholding of tax on nonresident aliens and foreign corporations) by the person paying such interest, or which would be so subject to withholding by such person, but for the fact that it is not treated as income from sources within the United States;

"(5) any amount on which the withholding agent is required to deduct and withhold a tax under section 1451 (relating to tax-free covenant bonds), or would be so required but for section 1451(d) (relating to benefit of personal exemptions);

"(6) any amount described in subsection (a) (5) paid to a State or a foreign government or international organization.

"(c) EXEMPTION FOR UNITED STATES.—The Secretary may authorize exemption from the tax imposed by section 3451 for any amount paid by the United States or any wholly owned agency or instrumentality thereof to the United States or any wholly owned agency or instrumentality thereof if the Secretary determines that the imposition of the tax with respect to such amount will cause a burden or expense which can be avoided by granting the tax exemption.

"Subchapter B—Dividends

"Sec. 3461. Income tax collected at source on dividends.

"Sec. 3462. Dividend defined.

"SEC. 3461. INCOME TAX COLLECTED AT SOURCE ON DIVIDENDS.

"(a) REQUIREMENT OF WITHHOLDING.—Except as otherwise provided in this chapter, every person who pays a dividend shall deduct and withhold on such dividend a tax equal to 20 percent of the amount thereof.

"(b) PAYEE UNKNOWN.—If the withholding agent is unable to determine the person to whom the dividend is payable, the tax under this section shall be deducted and withheld at the time payment of the dividend would be made if such person were known.

"(c) AMOUNT OF DIVIDEND UNKNOWN.—If the withholding agent is unable to determine the portion of a distribution which is a dividend, the tax under this section shall be computed on the entire amount of the distribution.

"(d) CROSS REFERENCES.—

"(1) For credit, against income tax of the recipient of the income, of amounts deducted and withheld under this section, see section 39.

"(2) For special rules as to credit or refund of such amounts, see sections 3484, 3485, 3486, 3487, and 3505.

"(3) For exemption from requirement of deducting and withholding on dividends paid to certain individuals, see section 3483.

"Sec. 3462. DIVIDEND DEFINED.

"(a) GENERAL RULE.—For purposes of this chapter, the term "dividend" means—

"(1) any distribution by a corporation which is a dividend (as defined in section 316); and

"(2) any payment made by a stockholder to any person as a substitute for a dividend (as so defined).

"(b) EXCEPTIONS.—For purposes of this chapter, the term "dividend" does not include—

"(1) any amount paid in the stock, or rights to acquire the stock, of the distributing corporation if the distribution is not includible in gross income of the recipient under the provisions of section 305 (relating to distributions of stock and stock rights);

"(2) any distribution to the extent that, under chapter 1—

"(A) the amount thereof is treated by the recipient as an amount received on the sale or exchange of property, or

"(B) gain or loss to the recipient is not recognized;

"(3) any amount which is includible in gross income as a taxable dividend by reason of the provisions of section 302 (relating to redemptions of stock), 306 (relating to dispositions of certain stock), 356 (relating to receipt of additional consideration in connection with certain reorganizations), or 1081(e)(2) (relating to certain distributions pursuant to order of the Securities and Exchange Commission);

"(4) any amount paid by one corporation to another corporation, if both corporations are members of the same affiliated group which filed a consolidated return for the preceding taxable year of the affiliated group;

"(5) an amount which—

"(A) is subject to withholding under subchapter A of chapter 3 (sec. 1441 and following, relating to withholding of tax on nonresident aliens and foreign corporations) by the person paying such amount, or

"(B) would be subject to withholding under such subchapter A by the person paying such amount but for—

"(i) the fact that it is attributable to income from sources outside the United States, or

"(ii) the fact that the payor thereof is excepted from the application of section 1441(a) by the provisions of section 1441(c);

"(6) any amount paid by a foreign corporation not engaged in trade or business within the United States;

"(7) any amount described in section 1373 (relating to undistributed taxable income of electing small business corporations);

"(8) amounts paid pursuant to the terms of a lease entered into before January 1, 1954, if under such lease the shareholders of the lessor corporation are entitled to such amounts without deduction for any tax which any law of the United States might require to be deducted and withheld on the payment of dividends.

"Subchapter C—Patronage dividends

"Sec. 3471. Income tax collected at source on patronage dividends.

"Sec. 3472. Amounts subject to withholding.

"SEC. 3471. INCOME TAX COLLECTED AT SOURCE ON PATRONAGE DIVIDENDS.

"(a) REQUIREMENT OF WITHHOLDING.—Except as otherwise provided in this chapter, every cooperative to which part I of subchapter T of chapter 1 applies which pays an amount described in section 3472 shall deduct and withhold on such amount a tax equal to 20 percent of such amount.

"(b) PAYEE UNKNOWN.—If the withholding agent is unable to determine the person to whom the amount is payable, the tax under this section shall be deducted and withheld at the time payment of the amount would be made if such person were known.

"(c) CROSS REFERENCES.—

"(1) For credit, against income tax of the recipient of the income, of amounts deducted and withheld under this section, see section 39.

"(2) For special rules as to credit or refund of such amounts, see sections 3484, 3485, 3486, 3487, and 3505.

"(3) For exemption from requirement of deducting and withholding on amounts paid to certain individuals, see section 3483.

"SEC. 3472. AMOUNTS SUBJECT TO WITHHOLDING.

"(a) GENERAL RULE.—Except as otherwise provided in this section or section 3483, the amounts subject to deduction and withholding under section 3471 are—

"(1) the amount of any patronage dividend (as defined in section 1388(a)) which is paid in money, qualified written notices of allocation (as defined in section 1388(c)),

or other property (except nonqualified written notices of allocation as defined in section 1388(d)), and

"(2) any amount, described in section 1382(c)(2)(A) (relating to certain nonpatronage distributions), which is paid in money, qualified written notices of allocation, or other property (except nonqualified written notices of allocation) by an organization exempt from tax under section 521 (relating to exemption of farmers' cooperatives from tax).

"(b) EXCEPTIONS.—The provisions of section 3471 shall not apply to—

"(1) any amount paid by one corporation to another corporation, if both corporations are members of the same affiliated group which filed a consolidated return for the preceding taxable year of the affiliated group;

"(2) an amount which—

"(A) is subject to withholding under subchapter A of chapter 3 (sec. 1441 and following, relating to withholding of tax on nonresident aliens and foreign corporations) by the person paying such amount, or

"(B) would be subject to withholding under such subchapter A by the person paying such amount but for the fact that it is attributable to income from sources outside the United States; and

"(3) any amount paid by a foreign corporation not engaged in trade or business within the United States.

"(c) EXEMPTION FOR CERTAIN CONSUMER COOPERATIVES.—A cooperative which the Secretary or his delegate determines is primarily engaged in selling at retail goods or services of a type that are generally for personal, living, or family use shall, upon application to the Secretary or his delegate, be granted exemption from the tax imposed by section 3471. Application for exemption under this subsection shall be made in accordance with regulations prescribed by the Secretary or his delegate.

"(d) DETERMINATION OF AMOUNT PAID.—For purposes of this subchapter, in determining amounts paid—

"(1) property (other than a written notice of allocation) shall be taken into account as its fair market value, and

"(2) a qualified written notice of allocation shall be taken into account as its stated dollar amount.

"Subchapter D—General Provisions

"Sec. 3481. Liability for return and payment of withheld tax.

"Sec. 3482. Return and payment by United States.

"Sec. 3483. Exemption certificates.

"Sec. 3484. Refund of tax to individuals.

"Sec. 3485. Refund of tax to States, tax-exempt organizations, etc.

"Sec. 3486. Refund of tax to corporation.

"Sec. 3487. Credit for tax withheld on corporation.

"Sec. 3488. Obligation sold between interest-payment dates.

"Sec. 3489. Presumption.

"Sec. 3490. Definitions.

"SEC. 3481. LIABILITY FOR RETURN AND PAYMENT OF WITHHELD TAX.

"(a) GENERAL RULE.—Every person required to deduct and withhold any tax under this chapter shall, on or before the last day of the first month following the close of each quarter of his taxable year, make a return of the tax required to be deducted and withheld during such quarter and pay the tax to the officer designated in section 6151. The withholding agent shall be liable for the payment of the taxes required to be deducted and withheld under this chapter, and shall not otherwise be liable to any person for the amount of any such payment.

"(b) TAX PAID BY RECIPIENT.—If the withholding agent, in violation of the provisions of this chapter, fails to deduct and withhold any tax under this chapter, and thereafter

the tax against which such tax may be credited is paid, the tax so required to be deducted and withheld shall not be collected from the withholding agent; but this subsection shall in no case relieve the withholding agent from liability for any penalties or additions to the tax otherwise applicable in respect of such failure to deduct and withhold.

“(c) CROSS REFERENCE.—

“For limitation on the use of Government depositaries in the collection of taxes deducted and withheld under this chapter, see the last sentence of section 6302(c).

“SEC. 3482. RETURN AND PAYMENT BY UNITED STATES.

“If the withholding agent is the United States the return of the tax deducted and withheld under this chapter may be made by an officer or employee of the United States having control of the payment of the amount subject to withholding, or appropriately designated for that purpose.

“SEC. 3483. EXEMPTION CERTIFICATES.

“(a) GENERAL RULES.—

“(1) INDIVIDUALS UNDER AGE 18.—Any individual may file with any withholding agent an exemption certificate on which he certifies the date of his birth. If such a certificate is filed, all amounts payable by such withholding agent to such individual, on and after the effective date for such certificate and before the beginning of the calendar year during which the certificate indicates that he will attain age 18, shall be exempt from the requirement of deducting and withholding under this chapter.

“(2) INDIVIDUALS OVER AGE 17.—Any individual may file with any withholding agent an exemption certificate on which he certifies—

“(A) that he will have attained age 18 before the close of the calendar year for which such certificate is filed, and

“(B) that he reasonably believes that he will not (after the application of the credits against tax provided by part IV of subchapter A of chapter 1, other than the credits under sections 31 and 39) be liable for the payment of any tax under chapter 1 for each of his taxable years any portion of which is included in the period for which such certificate will be in effect.

If such a certificate is filed, all amounts payable by such withholding agent to such individual during the period such certificate is in effect shall be exempt from the requirement of deducting and withholding under this chapter. Except as may otherwise be provided in regulations prescribed by the Secretary or his delegate, an exemption certificate filed by an individual described in this paragraph shall remain in effect only for the period beginning on the effective date of such certificate and ending at the close of the calendar year in which such period begins.

“(3) TAX-EXEMPT ORGANIZATIONS.—

“(A) Any organization (other than a cooperative described in section 521) which is exempt from the tax imposed by chapter 1 may file with any withholding agent who pays amounts described in section 3452(a) (5) an exemption certificate on which it certifies that it is such an organization. If such a certificate is filed, all amounts described in section 3452(a) (5) payable by such withholding agent to such organization on and after the effective date for such certificate shall (except as provided in subparagraph (B)) be exempt from the requirement of deducting and withholding under this chapter.

“(B) An exemption certificate filed by an organization under subparagraph (A) shall cease to be effective on the thirtieth day after the day on which the withholding agent, with whom such certificate was filed,

is notified by either the organization or the Secretary or his delegate that the organization is no longer exempt from the tax imposed by chapter 1. If an organization ceases to be exempt from such tax, it shall, within the time specified in regulations prescribed by the Secretary or his delegate, so notify each withholding agent with whom it has an exemption certificate in effect.

“(b) EXCEPTIONS AND SPECIAL RULES.—

“(1) CERTAIN EXCEPTIONS.—This section shall not apply to any amount—

“(A) described in section 3452(a) (1) (relating to interest on evidences of indebtedness), or

“(B) described in section 3452(a) (4) (relating to interest on obligations of the United States).

“(2) SERIES E BONDS, ETC.—In the case of transactions involving the redemption of one or more obligations described in section 3452(a) (5) (relating to certain obligations of the United States issued on a discount basis), a separate certificate shall be filed with respect to each such transaction.

“(3) NOMINEES, CUSTODIANS, AND JOINT OWNERSHIPS.—Under regulations prescribed by the Secretary or his delegate, the exemption provided by subsection (a) may be extended, in a manner consistent with the other provisions of this section, to—

“(A) amounts (other than amounts described in section 3462(a), relating to dividends) paid through nominees;

“(B) amounts paid to custodians; and

“(C) amounts paid jointly to 2 or more individuals;

“(4) EFFECTIVE DATE OF CERTIFICATE.—Any exemption certificate under this section shall take effect on such day as is specified in accordance with regulations prescribed by the Secretary or his delegate.

“(5) FORM AND CONTENTS OF CERTIFICATE AND NOTICE.—Any exemption certificate under this section, and any notice under subsection (a) (3) (B), shall be in such form and contain such information as the Secretary or his delegate may by regulations prescribe.

“(c) CROSS REFERENCE.—

“For penalty for filing fraudulent certificate, or for failing to provide notice, under this section, see section 7205.

“SEC. 3484. REFUND OF TAX TO INDIVIDUALS.

“(a) GENERAL RULE.—Except as provided in subsection (e), the tax deducted and withheld under this chapter with respect to amounts received by an individual during any quarter (other than the fourth quarter) of his taxable year (together with any tax so deducted and withheld on amounts which were received by him during any prior quarter of such year and with respect to which no allowable claim for refund has been filed under this section) shall, to the extent such tax does not exceed his refund allowance as of the time the claim for refund is filed, be promptly refunded to him as an overpayment of tax. A refund of tax shall be made under this section only if the amount claimed and allowable equals or exceeds \$10.

“(b) REFUND ALLOWANCE.—For purposes of this section, the refund allowance of an individual as of the time the claim for refund is filed is an amount equal to the excess, if any, of—

“(1) an amount equal to 22 percent of—

“(A) the total of the deductions which, on the basis of facts existing at the time the claim for refund is filed, such individual would be allowed for the taxable year under section 151 (relating to deductions for personal exemptions), plus

“(B) in the case of an individual who, at the time the claim for refund is filed, reasonably expects that he will be allowed a credit under section 37 (relating to retirement income) for the taxable year, the amount which, at such time, such individual

reasonably expects to be the amount of his retirement income (as defined in section 37(c) and as limited by section 37(d)) for the taxable year, less

“(C) the amounts (other than amounts on which tax is required to be deducted and withheld under this chapter) which, at the time the claim for refund is filed, such individual reasonably expects to be includible in his gross income for the taxable year; over

“(2) the amounts of tax with respect to which an allowable claim for refund has been previously filed under this section during the taxable year.

For purposes of paragraph (1) (C), an individual who files more than one claim for refund under this section for any taxable year may use the estimate for the preceding claim for such year unless, at the time he files the claim, he reasonably expects the amounts referred to in paragraph (1) (C) to exceed such prior estimate by more than \$100.

“(c) MARRIED INDIVIDUALS.—For purposes of subsections (a), (b), and (d), married individuals shall be treated as an individual if, at the time the claim for refund is filed, they reasonably expect that they will file a joint return for the taxable year in which such claim is filed.

“(d) TIME FOR FILING CLAIM.—Not more than one claim may be filed under this section by any individual during any quarter of his taxable year. A refund of tax deducted and withheld on amounts received during a taxable year shall be made under this section only if claim therefor is filed on or before the last day of such taxable year.

“(e) INDIVIDUALS NOT ELIGIBLE FOR REFUND.—No claim for refund may be filed under this section by—

“(1) any individual (other than an individual referred to in paragraph (2) or (3)) unless, at the time the claim for refund is filed, he reasonably expects that his gross income for the taxable year will not exceed \$5,000;

“(2) any married individual unless, at the time the claim for refund is filed, he reasonably expects that the aggregate gross income of such individual and his spouse for the taxable year will not exceed \$10,000;

“(3) a head of a household (as defined in section 1(b) (2)) or a surviving spouse (as defined in section 2(b)) unless, at the time the claim for refund is filed, he reasonably expects that his gross income for the taxable year will not exceed \$10,000; or

“(4) any child, unless, at the time the claim for refund is filed, he reasonably expects that no deduction would be allowed for him under section 151(e) (1) (B) for the taxable year of his parent (or parents) beginning with or within the calendar year in which the claim for refund is filed.

“(f) CROSS REFERENCE.—

“For credit or refund of amounts not refunded under this section, see section 39.

“SEC. 3485. REFUND OF TAX TO STATES, TAX-EXEMPT ORGANIZATIONS, ETC.

“(a) GENERAL RULE.—In the case of a person which is—

“(1) the United States or a State,

“(2) an organization (other than a cooperative described in section 521) which is exempt from the tax imposed by chapter 1,

“(3) a foreign government or international organization, or

“(4) a foreign central bank of issue, if the tax deducted and withheld under this chapter with respect to amounts received by such person during any calendar quarter exceeds the credit, if any, claimed by and allowable to such person under section 3505 (relating to credit against employment taxes) for such quarter, the excess (together with any such excess for any

prior quarter of the same calendar year with respect to which no refund has been claimed and allowed under this section) shall be promptly refunded or credited to such person as an overpayment of tax. In the case of a person to which paragraph (4) applies, the amount which may be refunded or credited against this section shall not exceed the amount of tax deducted and withheld under section 3451 on interest paid on obligations of the United States which are not held for, or used in connection with, the conduct of commercial banking functions or other commercial activities.

“(b) CROSS REFERENCES.—

“(1) For period of limitation for filing claim under this section, see section 6511.

“(2) For presumed date of payment for purposes of (A) period of limitation, see section 6513(b), and (B) allowance of interest on overpayments, see section 6611(d).

“SEC. 3486. REFUND OF TAX TO CORPORATION.

“(a) GENERAL RULE.—If the tax deducted and withheld under this chapter with respect to amounts received by a corporation (other than a corporation described in section 3485(a)) during any quarter (other than the fourth quarter) of its taxable year exceeds the amount claimed by and allowable to such corporation under section 3487 as a credit against its liability for tax under this chapter for such quarter, the excess (together with any such excess for any prior quarter of the same year with respect to which no refund has been claimed and allowed under this section) shall be promptly refunded or credited to such corporation as an overpayment of tax. A refund of tax shall be made under this section only if claim therefor is filed after the close of the period covered by the claim and on or before the last day of the taxable year.

“(b) CROSS REFERENCE.—

“For credit or refund of amounts not refunded under this section, see section 39.

“SEC. 3487. CREDIT FOR TAX WITHHELD ON CORPORATION.

“(a) GENERAL RULE.—Any tax deducted and withheld under this chapter with respect to amounts received by a corporation (other than a corporation described in section 3485(a)) during a taxable year shall, to the extent not claimed and allowable as a credit or refund to the corporation under section 3486, be allowed, under regulations prescribed by the Secretary or his delegate, as a credit against (but not in excess of) the tax for which such corporation is liable under this chapter in respect of amounts paid by it during such year.

“(b) DIVIDENDS AND PATRONAGE DIVIDENDS PAID DURING TAXABLE YEAR.—For purposes of determining the credit allowable to any corporation under subsection (a), a dividend, or amount subject to withholding under section 3471, paid by it may be considered as having been paid during the taxable year—

“(1) in the case of a personal holding company, if treated as paid during such taxable year under section 563(b),

“(2) in the case of a regulated investment company, if treated as paid during such taxable year under section 855(a),

“(3) in the case of a real estate investment trust, if treated as paid during such taxable year under section 858(a), or

“(4) in the case of a cooperative described in section 1381(a), if paid during the payment period (as defined in section 1382(d)) for such taxable year.

“(c) SPECIAL RULE FOR CORPORATIONS WHICH ARE MEMBERS OF AN AFFILIATED GROUP.—To the extent and subject to such conditions as may be provided in regulations prescribed by the Secretary or his delegate, the tax deducted and withheld under this chapter with respect to amounts re-

ceived by a corporation which is a member of an affiliated group which filed a consolidated return for the preceding taxable year of the affiliated group may, for purposes of this section, be treated as tax deducted and withheld under this chapter from any corporation which is a member of the same affiliated group.

“SEC. 3488. OBLIGATION SOLD BETWEEN INTEREST-PAYMENT DATES.

“For purposes of any credit or refund provided in section 3484, 3485, 3486, or 3487, in the case of an obligation which is sold or exchanged between interest-payment dates the amount required to be deducted and withheld on the interest at the end of the interest-payment period shall be treated in the manner provided in section 39(c).

“SEC. 3489. PRESUMPTION.

“For purposes of establishing that any person is entitled to a credit or refund of any tax required to be deducted and withheld under this chapter with respect to amounts received by such person, the correct amount of such tax shall, in the absence of evidence to the contrary, be presumed to have been so deducted and withheld.

“SEC. 3490. DEFINITIONS.

“For purposes of this chapter—

“(1) PERSON.—The term “person” includes the United States, a State, a foreign government, and an international organization.

“(2) STATE.—The term “State” includes a State, the District of Columbia, a possession of the United States, any political subdivision of any of the foregoing, and any wholly owned agency or instrumentality of any one or more of the foregoing.

“(3) FOREIGN GOVERNMENT.—The term “foreign government” includes a foreign government, a political subdivision of a foreign government, and any wholly owned agency or instrumentality of any one or more of the foregoing.

“(4) NONRESIDENT ALIEN.—The term “nonresident alien individual” includes an alien resident of Puerto Rico.”

“(2) CLERICAL AMENDMENTS, ETC.—

“(A) The heading for subtitle C is amended to read as follows:

“SUBTITLE C—EMPLOYMENT TAXES AND COLLECTION OF INCOME TAX AT SOURCE”

“(B) The table of chapters for subtitle C is amended by striking out the last line and inserting in lieu thereof the following:

“CHAPTER 25. Collection of income tax at source on interest, dividends, and patronage dividends.

“CHAPTER 26. General provisions relating to employment taxes and collection of income taxes at source.”

“(C) The table of subtitles under the heading ‘Internal Revenue Title’ at the beginning of the Internal Revenue Code of 1954 is amended by striking out the third line and inserting in lieu thereof the following:

“SUBTITLE C. Employment taxes and collection of income tax at source.”

“(D) The heading for chapter 26 (as redesignated by paragraph (1) of this subsection) is amended to read as follows:

“CHAPTER 26—GENERAL PROVISIONS RELATING TO EMPLOYMENT TAXES AND COLLECTION OF INCOME TAXES AT SOURCE”

“(b) CREDITS AGAINST INCOME TAX FOR TAX WITHHELD.—

“(1) ALLOWANCE OF CREDIT.—Part IV of subchapter A of Chapter 1 (relating to credits against tax) is amended by inserting after section 38 (added by section 2 of this Act) the following new section:

“SEC. 39. TAX WITHHELD ON INTEREST, DIVIDENDS, AND PATRONAGE DIVIDENDS.

“(a) GENERAL RULE.—Under regulations prescribed by the Secretary or his delegate, the tax deducted and withheld under chapter 25 (relating to withholding at source on interest, dividends, and patronage dividends) shall be allowed, to the recipient of the amount with respect to which such tax was deducted and withheld, as a credit against the tax imposed by this subtitle for the taxable year in which such amount is received.

“(b) SPECIAL RULE FOR DEPENDENT CHILDREN.—If—

“(1) the taxpayer for his taxable year is entitled to a deduction under section 151(e) (1) (B) with respect to a child, and

“(2) such child had, for the calendar year ending with or within the taxpayer's taxable year—

“(A) gross income of less than \$600, and

“(B) no wages (as defined in section 3401(a)) with respect to which withholding was required under chapter 24,

then, under regulations prescribed by the Secretary or his delegate, the taxpayer shall be entitled to the credit provided by subsection (a) with respect to amounts received by such child during such calendar year, but only if such child has not filed any claim for credit or refund of any portion of the tax deducted and withheld with respect to such amounts.

“(c) APPORTIONMENT OF CREDIT.—For purposes of subsection (a), if an obligation is sold or exchanged between interest-payment dates—

“(1) so much of the amount required to be deducted and withheld on the interest at the end of the interest-payment period as is properly allocable to that part of such period which ends on the date of the sale or exchange shall be treated as an amount deducted and withheld from the transferor on the date of the sale or exchange, and

“(2) so much of such amount as is properly allocable to that part of such period which begins on the day after the date of the sale or exchange shall be treated as an amount deducted and withheld from the transferee.

“(d) LIMITATIONS.—The credit provided by subsection (a) shall not be allowed—

“(1) REFUND TO INDIVIDUALS.—To any individual with respect to any amount of tax allowed him as a refund under section 3484.

“(2) CREDIT OR REFUND TO STATES, ETC.—To any person with respect to any amount of tax allowable to such person as a credit or refund under section 3485 or as a credit under section 3505.

“(3) CREDIT OR REFUND TO CORPORATIONS.—To any person with respect to any amount of tax allowed such person as a credit or refund under section 3486 or as a credit under section 3487.

“(4) CERTAIN DEPENDENT CHILDREN.—To any person with respect to any amount of tax which has been claimed and is allowable as a credit to such person's parent by reason of the provisions of subsection (b).

“(5) NOMINEES, ETC.—To any person with respect to any amount of tax allowed such person as a credit under section 1444(b).”

“(2) COMMON TRUST FUNDS.—Section 584 (c) (relating to the income of participants in the fund) is amended by adding at the end thereof the following new paragraph:

“(3) TAX WITHHELD AT SOURCE ON INTEREST, DIVIDENDS, AND PATRONAGE DIVIDENDS.—In any case where tax under chapter 25 is deducted and withheld on any amounts received by a common trust fund, for purposes of any credit or refund provided in section 39 or 3505, or chapter 25, such tax shall, in accordance with regulations prescribed by the Secretary or his delegate, be considered

as having been deducted and withheld proportionately from each participant."

"(3) ESTATES AND TRUSTS.—Section 642(a) (relating to special rules for credits and deductions in the case of estates and trusts) is amended by adding at the end thereof the following new paragraph:

"(4) TAX WITHHELD AT SOURCE ON INTEREST, DIVIDENDS, AND PATRONAGE DIVIDENDS.—In any case where tax under chapter 25 is deducted and withheld on any amounts received by an estate or trust, for purposes of any credit or refund provided in section 39 or 3505, or chapter 25, such tax shall, in accordance with regulations prescribed by the Secretary or his delegate, be considered as having been deducted and withheld from each beneficiary in an amount which, when added to the amounts paid, credited, or required to be distributed to him, equals the amounts which would have been paid, credited, or required to be distributed to him in the absence of chapter 25. Any tax under chapter 25 which is deducted and withheld on amounts received by the estate or trust shall be considered as withheld from such estate or trust to the extent it is not considered as withheld from a beneficiary under the provisions of the preceding sentence."

"(4) TECHNICAL AMENDMENTS.—

"(A) Section 164(b)(1) (relating to deduction denied in the case of certain taxes) is amended by—

"(i) striking out the word "and" at the end of subparagraph (B);

"(ii) striking out the comma at the end of subparagraph (C) and inserting "; and"; and

"(iii) adding after subparagraph (C) the following new subparagraph:

"(D) the tax withheld at source under chapter 25 (relating to collection of income tax at source on interest, dividends, and patronage dividends)."

"(B) Section 874(a) (relating to allowance of deductions and credits to nonresident alien individuals) is amended by striking '31 and 32' and inserting in lieu thereof '31, 32, and 39'.

"(C) Section 1314(e) (relating to inapplicability of part II of subchapter Q of chapter 1 of subtitle A to taxes imposed by subtitle C) is amended by striking 'employment taxes' and inserting in lieu thereof 'employment taxes and collection of income tax at source'.

"(D) Section 6211(b)(1) (relating to rules applicable in determination of deficiency) is amended by striking '31' and inserting in lieu thereof '31 or 39'.

"(E) The table of sections for part IV of subchapter A of chapter 1 is amended by striking out

"Sec. 38. Overpayments of tax."

and inserting in lieu thereof

"Sec. 38. Investment in certain depreciable property.

"Sec. 39. Tax withheld on interest, dividends, and patronage dividends.

"Sec. 40. Overpayments of tax."

"(c) INTEREST AND DIVIDEND PAID TO NON-RESIDENT ALIENS, ETC.—

"(1) WITHHOLDING RATE.—

"(A) Section 1441 (relating to withholding of tax on nonresident aliens) is amended by adding at the end thereof the following new subsection:

"(e) TREATIES.—In the case of amounts described in section 3452(a) (relating to interest), section 3462(a) (relating to dividends), and section 3472(a) (relating to patronage dividends), the tax required to be deducted and withheld under subsection (a) shall not by reason of the provisions of any treaty be less than 20 percent of such amounts."

"(B) Section 1442 (relating to withholding of tax on foreign corporations) is amended by adding at the end thereof the

following new sentence: 'In the case of amounts described in section 3452(a) (relating to interest), section 3462(a) (relating to dividends), and section 3472(a) (relating to patronage dividends), the tax required to be deducted and withheld under the preceding sentence shall not by reason of the provisions of any treaty be less than 20 percent of such amounts.'

"(2) NOMINEES ETC.—Subchapter A of chapter 3 (relating to withholding of tax on nonresident aliens and foreign corporations) is amended by adding at the end thereof the following new section:

"SEC. 1444. INTEREST AND DIVIDENDS PAID TO NOMINEES; CREDITS TO WITHHOLDING AGENTS.

"(a) WITHHOLDING OF TAX BY PAYOR.—Under regulations prescribed by the Secretary or his delegate, every person who pays amounts subject to withholding under chapter 25 and who has been notified by a payee thereof that the payee is a nominee required to deduct and withhold on such amounts under section 1441 or 1442 shall, in lieu of the nominee, deduct and withhold from such amounts paid to the nominee the tax required to be deducted and withheld under section 1441 or 1442, in the same manner as if such amounts were paid by such person directly to the beneficial owner thereof.

"(b) CREDITS TO WITHHOLDING AGENTS.—In the case of any person who is required to deduct and withhold tax under section 1441 or 1442 in respect of amounts received by him during any calendar year on which tax was deducted and withheld (or, in the case of amounts described in section 39(c)(1), was treated as deducted and withheld) under chapter 25, the taxes so deducted and withheld (or treated as deducted and withheld) under chapter 25 shall, under regulations prescribed by the Secretary or his delegate, be allowed as a credit against (but not in excess of) his liability for the year in respect of the taxes imposed by sections 1441 and 1442."

"(3) CLERICAL AMENDMENT.—The table of sections for subchapter A of chapter 3 is amended by adding at the end thereof the following:

"Sec. 1444. Interest and dividends paid to nominees; credits to withholding agents."

"(d) CREDIT FOR STATES AND TAX-EXEMPT ORGANIZATIONS.—

"(1) ALLOWANCE OF CREDIT.—Chapter 26 (general provisions relating to employment taxes and income tax withheld at source) is amended by adding at the end thereof the following new section:

"Sec. 3505. SPECIAL CREDIT IN CASE OF STATES OR TAX-EXEMPT ORGANIZATIONS.

"(a) GENERAL RULE.—In the case of a person which is a State (as defined in section 3490(2)) or which is an organization (other than a cooperative described in section 521) which is exempt from the tax imposed by chapter 1, the tax deducted and withheld under chapter 25 with respect to amounts received by it during any calendar quarter shall be allowed, under regulations prescribed by the Secretary or his delegate, as a credit against (but not in excess of) such person's liability (after the adjustments, if any, provided for in sections 6205(a) and 6413(a) for such quarter in respect of the taxes imposed by chapter 21 (Federal Insurance Contributions Act) and by chapter 24 (collection of income tax at source on wages). Such credit shall be allowed only if claim therefor is made, in accordance with such regulations, at the time of the filing of the return with respect to the taxes under chapter 21 and chapter 24 for such quarter.

"(b) OBLIGATIONS SOLD BETWEEN INTEREST-PAYMENT DATES.—For purposes of this section, in the case of an obligation which is sold or exchanged between interest-payment

dates, the amount required to be deducted and withheld on the interest at the end of the interest-payment period shall be treated in the manner provided in section 39(c).

"(c) CROSS REFERENCE.—

"For refund under chapter 25, see section 3485."

"(2) TECHNICAL AMENDMENTS.—

"(A) Section 3502 (relating to nondeductibility of taxes in computing taxable income) is amended by adding at the end thereof the following new subsection:

"(c) The tax deducted and withheld under chapter 25 shall not be allowed as a deduction in computing taxable income under subtitle A either to the person deducting and withholding the tax or to the recipient of the amounts subject to withholding."

"(B) The table of sections for chapter 26 is amended by adding at the end thereof the following:

"Sec. 3505. Special credit in case of States or tax-exempt organizations."

"(e) OTHER TECHNICAL AMENDMENTS.—

"(1) DECLARATION OF ESTIMATED INCOME TAX BY INDIVIDUALS.—Section 6015(a) (relating to declaration of estimated income tax by individuals) is amended by striking out the period at the end of paragraph (2) and inserting in lieu thereof 'and amounts on which tax is required to be deducted and withheld under chapter 25'.

"(2) ADJUSTMENT OF TAX; UNDERPAYMENT.—

"(A) Subsection (a)(1) of section 6205 (relating to special rules relating to assessment of employment taxes) is amended by striking out 'or 3402 is paid with respect to any payment of wages or compensation,' and inserting in lieu thereof '3402, 3451, 3461, or 3471 is paid with respect to any payment of remuneration, interest, dividends, or other amounts'.

"(B) Subsection (b) of such section is amended by striking out 'or 3402 is paid or deducted with respect to any payment of wages or compensation' and inserting in lieu thereof '3402, 3451, 3461, or 3471 is paid or deducted with respect to any payment of remuneration, interest, dividends, or other amounts'.

"(C) The heading for such section is amended to read as follows:

"Sec. 6205. SPECIAL RULES APPLICABLE TO CERTAIN TAXES UNDER SUBTITLE C."

"(D) The table of sections for subchapter A of chapter 63 is amended by striking out

"Sec. 6205. Special rules applicable to certain employment taxes."

and inserting in lieu thereof

"Sec. 6205. Special rules applicable to certain taxes under subtitle C."

"(3) USE OF GOVERNMENT DEPOSITARIES.—

Section 6302(c) (relating to use of Government depositaries) is amended by adding at the end thereof the following new sentence: 'The Secretary or his delegate shall not require the deposit under this subsection of any tax deducted and withheld under chapter 25 (relating to collection of income tax at source on interest, dividends, and patronage dividends) in a Government depository before the last day prescribed in section 3481 for payment of the tax.'

"(4) EXCESSIVE WITHHOLDING.—Section 6401(b) (relating to excessive withholding) is amended to read as follows:

"(b) EXCESSIVE WITHHOLDING.—If the amounts allowable as credits under section 31 (relating to credit for tax withheld at source under chapter 24) and section 39 (relating to credit for tax withheld on interest, dividends, and patronage dividends under chapter 25) exceed the taxes imposed by chapter 1 against which such credits are allowable, the amount of such excess shall be considered an overpayment."

"(5) ADJUSTMENT OF TAX; OVERPAYMENT.—

"(A) Subsection (a)(1) of section 6413 (relating to special credit and refund rules applicable to certain employment taxes) is amended by striking out 'or 3402 is paid with respect to any payment of remuneration,' and inserting in lieu thereof '3402, 3451, 3461, or 3471 is paid with respect to any payment of remuneration, interest, dividends, or other amounts.'

"(B) Subsection (b) of such section is amended—

"(1) By striking from the heading of such subsection the words 'OF CERTAIN EMPLOYMENT TAXES; and

"(ii) By striking out 'or 3402 is paid or deducted with respect to any payment of remuneration' and inserting in lieu thereof '3402, 3451, 3461, or 3471 is paid or deducted with respect to any payment of remuneration, interest, dividends, or other amounts'.

"(C) The following new subsection is added at the end of such section:

"(e) CROSS REFERENCES.—

"For special refunds or credits of tax withheld on interest, dividends, or patronage dividends under chapter 25, see sections 3484, 3485, 3486, 3487, and 3505.'

"(D) The heading for such section is amended to read as follows:

"SEC. 6413. SPECIAL RULES APPLICABLE TO CERTAIN TAXES UNDER SUBTITLE C.'

"(E) The table of sections for subchapter B of chapter 65 is amended by striking out "Sec. 6413. Special rules applicable to certain employment taxes.'

and inserting in lieu thereof

"Sec. 6413. Special rules applicable to certain taxes under subtitle C.'

"(6) OVERPAYMENT NOT DEDUCTED AND WITHHELD.—Section 6414 (relating to income tax withheld) is amended by striking 'chapter 3' and inserting in lieu thereof 'chapter 3 or 25'.

"(7) TIME TAX CONSIDERED PAID.—Section 6513(b) (relating to time tax considered paid) is amended by adding at the end thereof the following new sentences: 'For purposes of section 6511 or 6512, any tax deducted and withheld under chapter 25 which is allowable under section 39, 3484, 3485, or 3486 as a credit against tax or as a refund of an overpayment (or an amount treated as an overpayment) of the tax imposed by chapter 1 shall, in respect of the person entitled to such credit or refund, be deemed to have been paid by him on the last day prescribed for filing the return (determined without regard to any extension of time for filing such return) of tax under chapter 1 for his taxable year in which the amount subject to withholding under chapter 25 is received by him or, if such person has no taxable year, on the fifteenth day of the fifth calendar month following the close of such person's annual accounting period within which such amount is received by him. In the case of an amount allowable as a credit under section 39(b) to the parent of a child, such amount shall, if claimed by the parent, be deemed to have been paid on the last day for filing his return (determined without regard to any extension of time for filing such return) for his taxable year which begins with or within the calendar year in which amounts subject to withholding under chapter 25 were received by the child.'

"(8) FAILURE TO PAY ESTIMATED INCOME TAX.—

"(A) INDIVIDUALS.—Subsections (e) and (f) of section 6654 (relating to failure by individuals to pay estimated income tax) are amended to read as follows:

"(e) APPLICATION OF SECTION IN CASE OF WITHHELD TAXES.—For purposes of applying this section—

"(1) the estimated tax shall be computed without any reduction for amounts which

the individual estimates as his credits under section 31 (relating to tax withheld at source on wages) and section 39 (relating to tax withheld on interest, dividends, and patronage dividends); and

"(2) the amount of the credits allowed under sections 31 and 39 for the taxable year shall be deemed a payment of estimated tax, and an equal part of such amount shall be deemed paid on each installment date (determined under section 6153) for such taxable year, unless the taxpayer establishes the dates on which all amounts were actually withheld (or in the case of amounts described in section 39(c)(1), were treated as withheld), in which case the amounts so withheld shall be deemed payments of estimated tax on such dates.

"(f) TAX COMPUTED AFTER APPLICATION OF CREDITS AGAINST TAX.—For purposes of subsections (b) and (d), the term "tax" means the tax imposed by chapter 1 reduced by the credits against tax allowed by part IV of subchapter A of chapter 1, other than the credits against tax provided by section 31 (relating to tax withheld on wages) and section 39 (relating to tax withheld on interest, dividends, and patronage dividends).'

"(B) CORPORATIONS.—Section 6655 (relating to failure by corporation to pay estimated income tax) is amended—

"(i) by striking out the period at the end of subsection (e)(2)(B) and inserting in lieu thereof ', other than the credit against tax provided by section 39 (relating to tax withheld on interest, dividends, and patronage dividends).'; and

"(ii) by redesignating subsection (f) as subsection (g) and inserting after subsection (e) the following new subsection:

"(f) APPLICATION OF SECTION IN CASE OF TAX WITHHELD ON INTEREST, DIVIDENDS, AND PATRONAGE DIVIDENDS.—For purposes of applying this section—

"(1) the estimated tax shall be computed without any reduction for the amount which the corporation estimates as its credit under section 39 (relating to tax withheld on interest, dividends, and patronage dividends); and

"(2) the amount of the credit allowed under section 39 for the taxable year shall be deemed a payment of estimated tax, and an equal part of such amount shall be deemed paid on each installment date (determined under section 6154) for such taxable year, unless the corporation establishes the dates on which all amounts were actually withheld (or in the case of amounts described in section 39(c)(1), were treated as withheld), in which case the amounts so withheld shall be deemed payments of estimated tax on such dates.'

"(9) PENALTY FOR FILING FRAUDULENT EXEMPTION CERTIFICATE.—Section 7205 (relating to fraudulent withholding exemption certificate or failure to supply information) is amended by adding the following new sentence at the end thereof: 'Any person who willfully files an exemption certificate with any withholding agent under section 3483, on which the certification is known by him to fraudulent or to be false as to any material matter, or who is required to file a notice under subsection (a)(3)(B) of section 3483 and who willfully fails to provide such notice in the manner, at the time, and showing the information required under such subsection (a)(3)(B), or the regulations prescribed thereunder, shall, in lieu of any penalty otherwise provided, upon conviction thereof, be fined not more than \$500, or imprisoned not more than 1 year, or both.'

"(10) OFFENSES WITH RESPECT TO COLLECTED TAXES.—The last sentence of section 7215(b) (relating to offenses with respect to collected taxes) is amended to read as follows: 'For purposes of paragraph (2), a lack of funds existing immediately after the payment of wages or amounts subject to withholding

under chapter 25 (whether or not created by the payment of such wages or amounts) shall not be considered to be circumstances beyond the control of a person.'

"(1) DEFINITION OF WITHHOLDING AGENT.—Section 7701(a)(16) (defining the term 'withholding agent') is amended by striking out 'or 1461' and inserting in lieu thereof '1461, 3451, 3461, or 3471'.

"(f) EFFECTIVE DATES.—

"(1) GENERAL RULE.—Except as provided in paragraph (2), the provisions of this section shall apply in the case of interest and dividends paid on or after January 1, 1963.

"(2) SPECIAL RULES.—

"(A) In the case of transferable obligations described in paragraph (1) or (6) of section 3452(a) of the Internal Revenue Code of 1954, the provisions of this section shall apply only to interest paid with respect to interest-payment periods commencing on or after January 1, 1963.

"(B) The provisions of this section shall apply to amounts described in section 3472 of such Code paid on or after January 1, 1963, with respect to patronage occurring on or after the first day of the first taxable year of the cooperative beginning on or after January 1, 1963."

Mr. BUSH. Mr. President, may we have the amendment identified?

Mr. HARTKE. Mr. President, it is my amendment 8-29-62—A.

The PRESIDING OFFICER. The clerk will identify the amendment.

The LEGISLATIVE CLERK. The Senator from Indiana [Mr. HARTKE] offers an amendment identified as "8-29-62—A," which is, on page 354, beginning with line 4, to strike out all through line 19 on page 369 and insert a section 19, "Withholding of Income Tax at Source on Interest, Dividends, and Patronage Dividends."

The PRESIDING OFFICER. The question is on agreeing to the amendment offered by the Senator from Indiana [Mr. HARTKE].

Mr. HARTKE. Mr. President, much has been said about the proposal to withhold taxes due on dividends and interest, and many Americans have been led to believe—I think mistakenly—that the original proposal was for new taxation. Of course it was not.

My amendment is designed to eliminate any arguments which might come from the widows, from the children, from the older people, from the thrift associations—the savings and loan associations or the banks—because it would not cover those persons.

When I originally examined the tax bill, as I understood it to come from the President, the bill had two basic purposes. The first basic purpose was to close the tax loopholes; and the second basic purpose was to provide an incentive for business growth. Insofar as revenues were concerned, the cost of providing incentives for business growth was to be recouped by closing the hidden loopholes.

One part of that proposal was not to be a substantive change in the law, but instead a procedural change, which was to apply the same withholding provision to dividends and interest income as was applied to wages and salaries of wage earners. The proposal was to apply withholding to those who earn their living from investments and also from coupon clipping, in the same manner as

it applied to income from wages; in other words, to apply the same principle of withholding to those who receive funds from the working of their dollars as is applied in the case of those who work with their hands and their minds.

My amendment would provide for the Government an estimated revenue recoupment of \$530 million. It was estimated that the original proposed withholding provision would bring in, according to what I have been able to calculate from reliable reports, some \$780 million. As a result Senators are to be given an opportunity to place back into the bill about three-fourths of the loss already occasioned by the failure to adopt the House withholding principle.

Frankly, the withholding provision proposal in the Finance Committee was turned down based upon the arguments made by the thrift institutions, the savings and loan institutions, and the banks. Their opposition to the bill was quite vehement.

There was a problem presented as to minors, which I thought was corrected. There was a problem with respect to the elderly, which I thought was corrected. There was a problem with respect to widows and others, which I thought was corrected.

Some people thought, however, so far as this question is concerned, that the procedure recommended would be too cumbersome. As a result, the Finance Committee proposed that a certain reporting system be adopted.

The Treasury Department has consistently said that the reporting system could not and would not provide for the recoupment of the revenue loss.

I have consistently supported this provision, both in the committee and in the Senate. I understand how Senators could be swayed, either by the large amount of mail or by arguments concerning withholding on savings accounts. Frankly, I disagree with them, but I can understand how they could be swayed by the arguments.

However, I fail to see why the entire principle of withholding should be rejected, especially in respect to those who are receiving their incomes from dividends on stocks, or those who are receiving interest on certain evidences of indebtedness, in particular stocks and corporate investments.

(At this point Mrs. NEUBERGER assumed the chair as Presiding Officer.)

Mr. HARTKE. This list of those types of interest and those types of dividends which would be covered is set forth on page 3 of my proposal, in case any Senator would like to read about that in detail.

The withholding principle in and of itself is a good principle. It has been good because it has provided not alone a means for collection. It has been helpful to the Treasury Department on a certain level. It has provided for payment by all of a fair share of the taxes.

After all, the national debt, to the extent it has been incurred—much of it due to war—is the debt of each individual person who pays taxes. It does not belong to some more than to others, merely

because some have an opportunity to avoid payment of taxes or, in some cases, an opportunity to evade the payment of taxes.

Frankly, I feel that the Finance Committee and the Senate acted in good faith in striking the proposed withholding section from the bill. I assume they did. As I have said, that argument certainly can apply to dividends. It certainly cannot apply to interest on stocks and bonds. Many people are avoiding paying those amounts at the present time.

The tables shown in volume 10 of the hearings, pages 4355 and 4356, show that about 11.8 percent of dividends which are paid are never reported on income tax returns.

I believe in plugging loopholes. I think we should be fair to one group of our society as well as to others. As I have said before, the arguments which apply to widows and children, thrift associations, and banks no longer apply here.

I call attention to the fact that the minority leader and I had a little discussion about a certain statement in which he was speaking about H.R. 10. I did not oppose him on H.R. 10. I opposed my own leadership on that measure. I thought the measure had some merit.

I ask unanimous consent to have printed at this point in the RECORD an article entitled "Dirksen Tells Opposition to Tax Break for Professionals," by Carleton Kent, published in the Chicago Sun-Times on March 4, 1959.

There being no objection, the article was ordered to be printed in the RECORD, as follows:

DIRKSEN TELLS OPPOSITION TO TAX BREAK FOR PROFESSIONALS

(By Carleton Kent)

WASHINGTON.—Senate Republican Leader EVERETT M. DIRKSEN, of Illinois, emerged Tuesday as an opponent of a tax-exemption bill supported by doctors, lawyers, and other professional persons.

Fresh from the regular weekly conference of GOP leaders with President Eisenhower, DIRKSEN told White House reporters the bill would "plow a hole" of as much as \$3,365 million in Federal revenues.

The measure, which the House Ways and Means Committee has reported out favorably, is identical to one the House passed by a voice vote (no rollcall) late in the last session of Congress, and which died in the Senate Finance Committee's files.

Its authors are Representative EUGENE J. KEOUGH, Republican of New York, and Representative RICHARD M. SIMPSON, Republican of Pennsylvania, both of whom rank high on the Ways and Means Committee.

PERSONAL OPPOSITION

Perhaps because Simpson also is chairman of the Republican House campaign committee, DIRKSEN emphasized that his opposition was personal, and that he had not discussed it with other Republican leaders.

Nor had President Eisenhower taken a position on the matter when DIRKSEN brought it up, the Illinois Senator said.

The Keogh-Simpson bill would permit self-employed persons to deduct from their taxable incomes up to \$2,500 a year, and a total of \$50,000, paid into private institutions to create pensions for themselves.

TELLS CHIEF OBJECTION

DIRKSEN claimed this would cost \$365 million annually in Federal revenues, starting

January 1, 1959, but indicated this wasn't the chief reason for his opposition.

"If you do this, teachers, railroad workers, people on social security and others who pay on pension funds could come in with good grace and ask for tax exemptions on their contributions," DIRKSEN said.

And this would open a \$3 billion hole in Federal revenues over a period of years."

The Senate minority leader indicated he might have favored the bill earlier when he added:

"My dedication to a balanced budget is such that I will assert it even if it means rejecting a commitment I had already made."

DOUGLAS HELD DUBIOUS

So far Senator PAUL H. DOUGLAS, Democrat of Illinois, has not announced his position on the bill, which has an excellent chance to be passed by the House again. But his friends said he was dubious, on grounds that the bill would narrow the Federal tax base.

A leading light in pushing the Keough-Simpson measure is Stephen A. Mitchell, Chicago attorney, former Democratic national chairman, and an old political foe. But DIRKSEN's friends said Mitchell's position had not turned DIRKSEN's sympathies against the measure.

LOBBY FORMED IN 1957

The lobby behind the Keough-Simpson bill, formed in 1957, calls itself the American Thrift Assembly, and claims to represent 500,000 persons. Its board of directors represents a broad range of professional and other self-employed groups:

The American Bar Association, American Institute of Accountants, American Institute of Architects, American Dental Association, American Medical Association, American Optometric Association, American Patent Law Association, American Veterinary Medical Association, National Association of Real Estate Boards, National Association of Retail Druggists, National Association of Tax Accountants, National Association of Women Tax Lawyers, National Small Businessmen's Association, and the National Society of Professional Engineers.

Mr. HARTKE. In answer to a question a while ago the Senator from Illinois [Mr. DIRKSEN] stated that the measure would have caused a revenue loss of \$3,365 million. Two amendments to the bill before the Senate have been offered by the minority leader, both of which would cause a revenue loss to the Treasury. The Senator did not seem to feel any qualms about asking the Senate to agree to those measures. There would be a reduction of \$500 million in tax revenue in regard to judicial reform. I am not arguing the merits of the proposal, but it would cost \$500 million. The Senator did not seem to object to asking for a \$50 million annually loss of revenues in respect to the measure which would provide for special tax consideration for people over 65 in the sale of their houses, eliminating the capital gains tax. I asked the Senator at that time how he planned to vote, if given an opportunity, to provide for a closing of some of the loopholes and to provide for a balanced budget.

My amendment would balance the tax bill. Senators who are concerned about balancing the budget should support the measure. As I said before, the amendment would provide a recoupment of \$530 million of the \$800 million which was lost.

Mr. MILLER. Mr. President, will the Senator yield for a question?

Mr. HARTKE. I yield to the Senator from Iowa.

Mr. MILLER. The Senator is talking about recouping revenue which he fears would be lost without the amendment. However, it seems to me that by having the language which is present in the bill, and which was added to the bill in committee by the chairman of the committee, which would require information returns to be sent to the taxpayer—the recipient—and to the Internal Revenue Service alike, would go a long way toward improving the present situation.

I am wondering why the Senator would not be content to try that system to see how it would work. If it did not work—if it did not catch the revenue which is being lost now—then and only then we would resort to something as vast as the Senator's proposal.

Mr. HARTKE. The Secretary of the Treasury told us in committee that, so far as the procedure of reporting is concerned, although it was thought to be a good suggestion, no provision would be made for the necessary checking. The task would be beyond the capabilities of the present staff. Additional staff members would be required to collect the revenue. Although reports would be sent to individuals, still someone would have to check the returns against the reports. I do not object to that type of informational return, but I do not believe it would provide the proper revenue. The Treasury Department does not believe it would provide the revenue necessary to balance the tax bill.

Mr. MILLER. I thank the Senator for his response. I cannot agree with the Secretary of the Treasury in that respect. I think the additional auditing which he envisions as a result of trying to take care of the informational returns would be offset by the additional auditing of millions of claims for refunds, which the amendment of the Senator from Indiana would entail. I recognize that there is a difference of opinion. I appreciate the Senator's response.

Mr. BYRD of Virginia. Mr. President, will the Senator yield?

Mr. HARTKE. I yield.

Mr. BYRD of Virginia. As I understand, the amendment of the Senator from Indiana is similar to an amendment which was previously rejected by the Senate—receiving only 20 votes—with the exception of the fact that under the Senator's amendment there would be no withholding of interest on deposits in savings and loan institutions.

Mr. HARTKE. Savings and loan institutions and bank deposits.

Mr. BYRD of Virginia. With that exception, the amendment is the same as that which was rejected in the Senate Finance Committee twice, once by a vote of 10 to 5 and once by a vote of 11 to 5. When the proposal reached the floor of the Senate, it received only 20 votes.

Mr. HARTKE. The chairman of the committee is exactly correct. I was 1 of the 20.

Mr. BYRD of Virginia. Senators have already voted on the substantive provisions of the amendment, and only 20 Senators voted in favor of it.

Mr. HARTKE. I invite the attention

of my distinguished chairman to the fact that the House of Representatives passed the bill in a form which included withholding of taxes on savings, and the opposition to the withholding provision basically came from the savings and loan institutions. I am not saying whether they were right or wrong. I thought they were wrong. Many Senators probably thought they were right, and that an undue burden would be placed upon those institutions.

It now seems that the burden is relieved. The representatives of most corporations with whom I have talked tell me that there would be no additional burden involved in withholding, as distinguished from reporting on dividends.

Mr. BYRD of Virginia. The amendment of the Senator from Indiana would withhold taxes on every other kind of interest except interest from building and loan institutions. Such institutions were eliminated because of the fact that they made strong objection to the withholding plan. I think if we were to withhold taxes of that kind at all, we ought to withhold with respect to everyone.

Mr. HARTKE. I quite agree with the distinguished chairman.

Mr. BYRD of Virginia. If taxes were to be withheld on all other kinds of interest and on all kinds of dividends, there should be no exemptions.

Mr. HARTKE. The distinguished chairman is exactly correct. I think withholding should apply to everyone. The Senate decided otherwise. I am now giving Senators an opportunity to vote to withhold taxes on payments by some of such institutions.

If the principle of withholding is to be applied to a person who works with his hands and to a person who is on salary, it should apply also to a man who clips coupons, receives dividends, and obtains his income from investments. I grant that the amendment would not cover all savings institutions; but possibly next year we can apply the measure to the remainder of the institutions. I wish the principle to be applied. I think it is good.

Mr. BYRD of Virginia. Mr. President, will the Senator yield?

Mr. HARTKE. I yield.

Mr. BYRD of Virginia. The Senator knows that the Senate Committee on Finance spent many hours considering that provision. The committee heard many witnesses. It remained in executive session. There were two votes on the measure. It was we decided that the reporting system would be adequate. The information would be available in time so that the Secretary of the Treasury could collect the taxes.

It was further concluded that the measure would be a great hardship on millions of people. Fifteen million people would be involved. It was said that those entitled to receive refunds would get them within 4 months. However, there is no assurance that they would get their refunds in 4 months. The Senator from Indiana knows that a taxpayer desiring a refund would have to fill out a four-page complicated application to get a refund of a few dollars.

I hope the Senate will reject the amendment. The proposal has been before the Senate for months. I do not see why we should reverse ourselves and give privileges to the building and loan people, and apply withholding to everyone else. It ought to be all or none.

The PRESIDING OFFICER. The question is on agreeing to the amendment of the Senator from Indiana [Mr. HARTKE]. On this question, the yeas and nays have been ordered, and the clerk will call the roll.

The legislative clerk called the roll.

Mr. HUMPHREY. I announce that the Senator from Mississippi [Mr. EASTLAND] and the Senator from Washington [Mr. MAGNUSON] are absent on official business.

I further announce that the Senator from New Mexico [Mr. ANDERSON], the Senator from Nevada [Mr. BIBLE], the Senator from Wyoming [Mr. HICKEY], and the Senator from Missouri [Mr. SYMINGTON] are necessarily absent.

I further announce that, if present and voting, the Senator from Nevada [Mr. BIBLE], the Senator from Mississippi [Mr. EASTLAND], the Senator from Wyoming [Mr. HICKEY], and the Senator from Washington [Mr. MAGNUSON] would each vote "nay."

Mr. KUCHEL. I announce that the Senator from Utah [Mr. BENNETT], the Senator from South Dakota [Mr. BOTTRUM], the Senator from Arizona [Mr. GOLDWATER], the Senator from Kentucky [Mr. MORTON], and the Senator from New Hampshire [Mr. MURPHY] are necessarily absent.

If present and voting, the Senator from Utah [Mr. BENNETT], the Senator from South Dakota [Mr. BOTTRUM], and the Senator from New Hampshire [Mr. MURPHY] would each vote "nay."

The result was announced—yeas 20, nays 69, as follows:

[No. 243 Leg.]

YEAS—20

Bartlett
Carroll
Clark
Cooper
Dodd
Douglas
Gore

Gruening
Hart
Hartke
Humphrey
Kefauver
Mansfield
McNamara

Morse
Neuberger
Pell
Proxmire
Smith, Mass.
Yarborough

NAYS—69

Alken
Allott
Beall
Boggs
Burdick
Bush
Butler
Byrd, Va.
Byrd, W. Va.
Cannon
Capehart
Carlson
Case
Chavez
Church
Cotton
Curtis
Dirksen
Ellender
Engle
Ervin
Fong
Fulbright

Hayden
Hickenlooper
Hill
Holland
Hruska
Jackson
Javits
Johnston
Jordan, N.C.
Jordan, Idaho
Keating
Kerr
Kuchel
Lausche
Long, Mo.
Long, Hawaii
Long, La.
McCarthy
McClellan
McGee
Metcalf
Miller
Monroney

Moss
Mundt
Muskie
Pastore
Pearson
Prouty
Randolph
Robertson
Russell
Saltonstall
Scott
Smathers
Smith, Maine
Sparkman
Stennis
Talmadge
Thurmond
Tower
Wiley
Williams, N.J.
Williams, Del.
Young, N. Dak.
Young, Ohio

NOT VOTING—11

Anderson
Bennett
Bible
Bottrum

Eastland
Goldwater
Hickey
Magnuson

Morton
Murphy
Symington

So Mr. HARTKE's amendment was rejected.

Mr. BYRD of Virginia. Madam President, I move that the Senate reconsider the vote by which the amendment was rejected.

Mr. ROBERTSON. I move to lay that motion on the table.

The motion to lay on the table was agreed to.

Mr. HARTKE. Madam President, I call up my amendment designated "8-29-62-C" and ask that it be read.

The PRESIDING OFFICER (Mrs. NEUBERGER in the chair). The amendment will be stated.

The LEGISLATIVE CLERK. At the end of the bill it is proposed to insert the following new section:

SEC.—CREDIT FOR POLITICAL CONTRIBUTIONS.

(a) ALLOWANCE OF CREDIT.—Part IV of subchapter A of chapter 1 (relating to credits against tax) is amended by renumbering section 39 (as renumbered by section 2(a) of this Act) as section 40 and by inserting after section 38 (as added by such section) the following new section:

"SEC. 39. CONTRIBUTIONS TO POLITICAL CANDIDATES OR POLITICAL COMMITTEES.

"(a) GENERAL RULE.—In the case of an individual, there shall be allowed, as a credit against the tax imposed by this chapter for the taxable year, an amount equal to one-half of so much of the political contributions (as defined in subsection (c)), payment of which is made by the taxpayer within the taxable year, as does not exceed—

"(1) \$20, or
"(2) \$40, in the case of a husband and wife who file a joint return under section 6013 for the taxable year.

"(b) APPLICATION WITH OTHER CREDITS.—The credit allowed by subsection (a) shall not exceed the amount of the tax imposed by this chapter for the taxable year reduced by the sum of the credits allowable under section 33 (relating to foreign tax credit), section 34 (relating to credit for dividends received by individuals), section 35 (relating to partially tax-exempt interest), and section 37 (relating to retirement income).

"(c) DEFINITIONS.—For purposes of subsection (a), the term 'political contribution' means a contribution or gift to—

"(1) any political candidate, or
"(2) any political committee, but only if such contribution or gift is made to further the candidacy of one or more individuals in a general or special election."

(b) CLERICAL AMENDMENT.—The table of contents for such part IV is amended by striking out

"Sec. 39. Overpayments of tax."

and inserting in lieu thereof
"Sec. 39. Contributions to political candidates or political committees.

"Sec. 40. Overpayments of tax."

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 1962.

Mr. McNAMARA. Madam President, all too seldom do we have an opportunity to vote on major tax legislation.

It seems to be much easier to permit tax inequities to remain locked into the statute books, to permit loopholes to remain wide open, than to attempt the reform so urgently needed in our tax laws.

Thus it is a real disappointment to find what has been billed as a major tax revision—is the sorry specimen now before us.

This measure is a quagmire of inconsistencies.

Rather than plug up gaping tax loopholes, the bill has managed to drill a brandnew one through which more than a billion dollars will escape the Treasury under the guise of an "investment incentive" to business.

Adding insult to that is the apparent fact that not even the business community is particularly enthusiastic about this handout that a willing Congress is about to force upon it at the expense of the Treasury.

And rather than put an end to the shocking abuses of the expense account, the Senate version of the tax bill seems to have found a way to make these abuses a bit more legal.

What about the major revenue-producing item in this so-called "tax revision"—the application of the withhold-tax to dividends and interest?

This would have brought in an estimated \$900 million a year in taxes due the Government but not paid, and might have made the rest of the bill at least palatable, if not exactly savory.

But no. The Senate permitted itself to be snowed under by an avalanche of propaganda, and withholding on dividends and interest was knocked out of the bill.

This is not the first time the tax dodger has hidden behind the skirts of the widows and orphans, and it probably will not be the last.

But the worst of all defects in this tax bill is that it is an empty bag so far as the rank-and-file taxpayer is concerned. It contains nothing to alleviate his unfair tax burden. It does not lower his tax rate—or increase his deductions—or raise personal exemptions from the present \$600 to a more realistic \$700 or \$800.

It does not do away with unfair consumer taxes, such as the 10-percent excise tax on the purchase of his new automobile.

It contains nothing for him except an interesting object lesson of how the lobbyist and the tax lawyer ply his trade in behalf of already well-heeled interests.

To be sure, a ray of hope is held out to the taxpayer. We are told that his turn will come next year, when a major revision of the tax structure will be undertaken.

But I would caution the taxpayer not to get too excited over this prospect. If next year's tax revision displays the same vast gap between proposal and performance as does this year's bill, there will be precious little in it for the average taxpayer.

Madam President, for these reasons, because the bill before us does nothing for those who need help the most, because it will create new tax loopholes costing upward of a billion dollars with no matching income, I shall vote against the pending measure.

Mr. HARTKE obtained the floor.

Mr. SPARKMAN. Madam President, will the Senator from Indiana yield to me?

Mr. HARTKE. Madam President, I yield to the Senator from Alabama without losing my right to the floor.

Mr. SPARKMAN. I ask the attention of the senior Senator from Okla-

homa. I should like to ask a question for clarification. It relates to the language in the report concerning the definition of a domestic building and loan association.

Am I correct in understanding that there is nothing in the bill or the report which would preclude or limit savings and loan associations in the buying of participations in loans to the extent permitted by the regulations of the Federal Savings and Loan Insurance Corporation.

Mr. KERR. The Senator is correct, and on page 186 of the report specific reference is made to the fact that a participation in the loan will be considered in the same manner as a loan made. The program of participation lending has been developed and encouraged by the Federal Home Loan Bank Board and this bill does nothing to impede it.

Mr. SPARKMAN. On page 48 of the report, referring to paragraph (B) in the definition of a domestic building and loan, there is a sentence:

It is not intended, however, that this prevent necessary borrowings from Government agencies such as HOLC.

Am I correct in assuming that this includes loans from Federal Home Loan Banks, the Federal Savings and Loan Corporation, and any other Federal agency from which a savings and loan might legally borrow?

Mr. KERR. The Senator from Alabama is correct; an association could borrow any amount from any Federal agency to the extent otherwise legally permissible. The reference in the report to the HOLC was intended merely as an example.

Mr. SPARKMAN. Also, Madam President, I assume that the word "necessary" means "necessary" for the conduct of business as determined by management.

Mr. KERR. It was not intended that such borrowings would be limited to emergencies. Any borrowing that the management felt was necessary or desirable for the conduct of business would meet this test.

Mr. SPARKMAN. Along this same line, Federal and State associations are also permitted to borrow from commercial banks. Am I correct in understanding that such borrowing is not precluded under this definition?

Mr. KERR. Federal associations are permitted to borrow up to 10 percent of their capital from non-Government sources. I understand State laws are similar. Some may be slightly higher or lower, but borrowing in this range would certainly be acceptable. We do not have the intention of forcing borrowing from Government agencies instead of private banks.

Mr. SPARKMAN. Madam President, I certainly thank the Senator from Oklahoma for clarifying these points. I know the clarification was needed.

I also thank the Senator from Indiana [Mr. HARTKE] for yielding for this purpose.

Mr. KERR. Madam President, I thank the Senator from Alabama, who is a recognized authority on the matters to which his questions were addressed, for

bringing them up, so that these points might be clarified.

Mr. HARTKE. Madam President, my amendment is simple, but is important to the cause of democracy.

The question is whether elections will continue to be run on the basis of contributions by large contributors, or whether the contribution base will be broadened. In 1960 over \$8 million was donated by individuals to groups such as health, welfare, and charitable organizations. Every one of these organizations is very important, but none of them will be of value if the cause of democracy is lost.

This matter is of great concern to many persons. The President has called for a study of this subject, and his Commission on Campaign Costs endorses the approach taken in my amendment.

The amount involved in the amendment is very small. The maximum credit any individual could claim would be \$10. In order to get a \$10 tax credit, he would have to make a political contribution of at least \$20. In other words, he could deduct half of his \$20 contribution and could receive it as a tax credit—but only half. One who contributed \$10 would be able to deduct, as a tax credit, \$5.

In the first place, we know that it costs a great deal to conduct political campaigns. The exact amount perhaps is unknown; but it has been estimated as being between \$165 and \$175 million. At the present time, this cost is spread over an estimated 10 million givers. In my opinion, the base of the political contributions should be broadened. We know that unless something is done, some Government action will have to be taken, although perhaps at a different level.

I talked to the distinguished Senator from Arizona [Mr. GOLDWATER], the chairman of the Senate Republican Campaign Committee, and he indicated that he is receptive to a measure along this line, which will make it possible for people to receive such tax credits for the political contributions they make.

Some persons may feel that such an amendment does not belong in this bill; but I think the time has come to do something constructive about this matter, so long as it will not interfere with the President's recommendations.

Mr. McCARTHY. Madam President, will the Senator from Indiana yield?

Mr. HARTKE. I yield.

Mr. McCARTHY. I support the Senator's amendment. Our State has allowed for some years a deduction of up to about \$100 against the State income tax, for political contributions. That works well, and has been easy to administer; and I think it has had a good effect on politics in Minnesota.

Mr. HARTKE. I thank the distinguished Senator from Minnesota. I may say that Minnesota has taken a lead in this field, and has been pointed to with a great deal of pride by the Political Research Foundation, which has given a great deal of study to this matter and to the subject of tax incentives for this purpose. On page 22 of its report it says that, on balance, such a tax credit for

half of the amount of the contribution, up to a maximum of \$10, appears to have more advantages and to represent greater justice, is easier to claim, and appears to offer more incentive to small contributors.

Mr. CANNON. Madam President, will the Senator from Indiana yield?

Mr. HARTKE. I am glad to yield to the distinguished Senator from Nevada—who, incidentally, has introduced a bill which encompasses this item and other items in connection with the financing of Presidential campaigns. He has done an excellent job, and I commend him for it.

Mr. CANNON. I thank the Senator from Indiana. I wish to say that the Subcommittee on Privileges and Elections considered this matter and heard considerable testimony in support of such a provision. The bill as reported to the floor of the Senate contained such a provision. However, there was a question as to whether the provision might be subject to a point of order. Therefore, the controversial section was withdrawn, and the bill was sent to the House; but I took the opportunity to recommend to the chairman of the House committee that it consider adding the particular provision with which the Senator from Indiana is concerned.

I may say that the evidence presented before our committee supported this type of approach to campaign financing. I believe it is a reasonable and a good one, and I am very happy to support the Senator's amendment.

Mr. HARTKE. I thank the Senator from Nevada.

I wish to say that this amendment will, at least to this extent, be of assistance to individuals who wish to make contributions to the committees or candidates or parties of their personal choice, so long as the contributions are made for the purpose of sponsoring or aiding a person in a particular election to be elected.

Campaign funds and expenses are growing larger and larger. We hear about the great costs of television. In New Jersey the television costs are probably prohibitive, because of the fact there are no television stations in that State. Yet the candidates there would like to have their message brought to the American people.

Madam President, I think the amendment makes good sense. The American Heritage Foundation, various labor organizations, and similar organizations would, in my opinion, feel that this is the type of approach which they could support.

I hope that Senators who are interested in the cause of democracy and in the financing of political campaigns will give this amendment favorable consideration; and I hope the amendment will be adopted.

Mr. YOUNG of Ohio. Madam President, will the Senator from Indiana yield?

Mr. HARTKE. I yield.

Mr. YOUNG of Ohio. I desire to compliment the distinguished Senator from Indiana. I feel that he has offered a meritorious amendment to this tax bill.

He has rendered a real and a needful public service.

I think we should encourage people of moderate circumstances and poor people to aspire to public office; and any legislative proposal of this sort certainly deserves our support. So I hope the amendment will be adopted.

Mr. HARTKE. I thank the distinguished Senator from Ohio for his offer of confidence.

Mr. KERR. Madam President—

The PRESIDING OFFICER. Does the Senator from Indiana yield?

Mr. HARTKE. I am glad to yield to the Senator from Oklahoma.

Mr. KERR. I was seeking the floor.

Mr. HARTKE. I am glad to yield the floor.

Mr. KERR. I would hope my good friend from Indiana would not press this amendment. It is one which would implement a new policy which has, so far as I know, never heretofore been a part of our tax laws. There have been no hearings on it before the committee, either of the House or the Senate. If we were going to recognize the principle of permitting a deduction for a contribution to a political committee, I call the Senator's attention to the fact that, if I understand the amendment, it is not limited to contributions to a political party, but includes contributions to any political committee, and each person can use his imagination as to the scope and extent of the committees which would be eligible to be the beneficiaries of this amendment, and the donor would have a tax credit for making the contribution. It would seem to me that that certainly is going very far afield and implementing a privilege with a wide-open application insofar as the identity of the beneficiary is concerned.

We are going to have tax legislation before the Congress next year, general in nature, and I am sure there will be an abundance of opportunity available to any Member of Congress who seeks to have such an amendment or proposal as this considered.

In view of that fact, I hope the distinguished Senator from Indiana will not press his amendment.

Mr. HARTKE. Madam President, will the Senator yield for a question?

Mr. KERR. I do.

Mr. HARTKE. In the first place, with reference to the Senator's statement about its being wide open, I suppose the Senator is aware of the fact that the maximum a taxpayer could claim would be \$10. He is not going to spread that amount far and wide.

Mr. KERR. I understand he would not spread it far and wide, but he could apply it far and wide.

Mr. HARTKE. He could not spread it very far and wide if he wanted, for example, to contribute \$1 each to several committees.

Mr. KERR. He might want to contribute the full amount to one committee whose identity the Senator from Oklahoma could not imagine.

Mr. HARTKE. It is the right of every American not only to vote as he wants to, but to contribute to a political committee if he wants to contribute to it, so

long as that committee does not subvert the Constitution. The taxpayer should have the right, if he wants to, to contribute \$10 to someone for one vote, and that would not go too far.

Mr. KERR. If the Senator from Oklahoma were going to contemplate favorably such a proposal as this, the first identity he would want to make eligible would be the Democratic Party. The Senator from Oklahoma is aware of the fact that he would not get very far in proposing a deductible privilege for a donor to the Democratic Party without also making that deduction available for a donor to the Republican Party. But the Senator from Oklahoma would feel that, having had an urge to make such a contribution deductible, he would have gone far enough and have satisfied most Members of this body if it were limited to the Democratic or the Republican Party.

I would not, as of today, favor an amendment of that kind, because it is a new principle in the matter of tax deductions, and it should be studied by the committees of Congress before being presented to the Senate or the House for their action. But even though the Senator from Oklahoma would urge making contributions to the Democratic Party and/or the Republican Party deductible, he could not support this amendment, because under its provisions a contribution to other political committees would be deductible.

Mr. HARTKE. The Senator is right. I would point out, however, that there have been hearings on the proposal. As the Senator from Nevada [Mr. CANNON] pointed out, there were hearings held. The President—

Mr. KERR. Before what committees of the Congress?

Mr. HARTKE. The Senate committee of which the distinguished Senator from Nevada [Mr. CANNON] is chairman. The Subcommittee on Privileges and Elections of the Committee on Rules and Administration conducted hearings on this matter, and, if I understood the Senator from Nevada, acted favorably and approved deductions of this kind. If I am in error, I would like to be corrected.

Mr. CANNON. Madam President, if the Senator will yield, the Senator from Indiana is correct. This matter was gone into by our committee on the overall bill, which included various methods of financing, whether by tax credit or deductions or other methods, and this was the method approved by the Subcommittee on Privileges and Elections, and also reported by the full committee.

Mr. KERR. Madam President, I would presume that a matter having to do with tax measures must have been heard by the House Ways and Means Committee or the Senate Finance Committee. It is my understanding that those are the committees which appropriately have jurisdiction over such matters. I did not attempt to speak with reference to which other committees considered it.

Mr. MANSFIELD. Madam President, if the Senator will yield, I believe the chairman of the Subcommittee on

Elections and Privileges will agree that the financial aspect of the bill which his committee reported on was taken out because there was a conflict as to whether or not the Finance Committee should have jurisdiction of the section. Is that correct?

Mr. CANNON. The Senator is correct. I made the statement that there was a good question as to whether the particular provision was subject to a point of order because it should properly be considered by other committees of the Senate. Therefore, the provision that is in question here was deleted from the bill as it was considered in the committee.

Mr. MANSFIELD. Was that deletion considered by the Finance Committee, which has jurisdiction of tax matters?

Mr. KERR. So far as I know, it was not, and I would hope the Senator from Indiana would delete that part of the amendment.

Mr. HARTKE. The bill had basically two purposes. One was an incentive for business growth, and the other was closing tax loopholes. I would like to have offered the amendment, but hearings were had upon tax reform and upon the subject of giving special benefits to people who have capital gains.

Mr. KERR. As I understand, the Senator refers to H.R. 10 in one part of the amendment—

Mr. HARTKE. No; I am talking about the two amendments submitted by the minority leader. One was with relation to a special situation in the State of Illinois, to permit a tax deduction for contributions for tax reform—

Mr. KERR. With reference to that, the measure was considered by the Ways and Means Committee of the House and reported by it unanimously.

Mr. HARTKE. To the Senate Finance Committee?

Mr. KERR. To the House.

Mr. HARTKE. I ask the Senator in charge of the bill if this matter was considered by the Finance Committee.

Mr. KERR. No; my statement to the Senator's question is that it was not considered either by the Ways and Means Committee or the Finance Committee.

Mr. HARTKE. I stand corrected if I am wrong. Really, the first amendment submitted by the minority leader was the amendment which was going to cost \$50 million annually, which the Executive says has basic inequities in it. The Senate accepted the amendment submitted by the minority leader relating to the capital gains tax for people over 65, which had an escalator amendment in it. Was that measure considered by the Finance Committee or the Ways and Means Committee?

Mr. KERR. That particular amendment was not considered. The particular amendment offered by the Senator from Illinois was not adopted.

Mr. HARTKE. It was accepted.

Mr. KERR. It was not accepted. The particular amendment which he offered was not.

The Senator offered an amendment which would have exempted from tax-

ation any gain by a person 60 years of age or older on the sale of a home which the taxpayer had possessed and in which he had resided for 5 years.

The matter of the tax treatment on the sale of homes, as the distinguished Senator knows, is a question which has been before the committees of Congress innumerable times through the years and has been the subject of legislation. I know the Senator is familiar with many of the provisions of law which have to do with the tax treatment of gains on homes sold by taxpayers.

The amendment accepted by the Senate was drastically different from the one originally offered by the Senator from Illinois, as to which I understand the estimate was made with respect to losing \$50 million in revenue.

Mr. HARTKE. I am sorry, but I did not hear the statement by the Senator as to how much revenue was involved.

Mr. KERR. I used the figure given by the Senator from Indiana.

Mr. HARTKE. \$50 million was estimated by the Treasury Department.

Mr. KERR. Yes. As I say, the amendment which was accepted changed the age of eligibility from 60 to 65 and recognized the entire gain with reference to the sale of a residence which sold for not more than \$30,000 and the proportionate gain on the sale of a residence which sold for more than \$30,000, on the basis of the relationship between \$30,000 and the amount of the sale.

I am sure that if the Senator will examine the mathematics, he will find that the cost would be substantially less than would have resulted by adoption of the amendment which the Senator from Illinois originally offered.

Mr. HARTKE. I quite agree with the Senator from Oklahoma. The only point I am making is that the rule with respect to considering only those measures which have been heard by the Finance Committee, in regard to questions of taxation, was broken for the minority leader in this case, because the proposal, in its form as offered or in the form as accepted, as amended by the minority leader, was never heard. The rules were broken at that stage of the game. I am willing to abide by the rules, but since the rules were broken at that stage of the game, I think this proposal deserves much more attention, because it goes to the heart and the spirit of democracy.

People in their old age should have their problems considered. I supported medicare. I am in favor of that. I would have supported this measure. I introduced a bill similar to this.

The point is that the rules were broken at that stage of the game. This is a much more important proposal in respect to the welfare of democracy in its overall total than the proposal with respect to people over the age of 65.

Mr. KERR. The statement by the Senator from Oklahoma is that the principle in this amendment is one which, so far as I know, has never been heard either by the Ways and Means Committee or by the Finance Committee of the Senate. The principle of tax treatment of a gain in connection with the sale of

a home is one which has been before the committees of Congress ever since I have been a Member.

Mr. CARLSON. Madam President, will the Senator yield?

Mr. KERR. I yield to the Senator from Kansas.

Mr. CARLSON. While the amendment offered by the Senator from Indiana might have great merit—I think it does have—certainly it ought to be heard by our committee. It deals with a reduction in revenue income, as well as involving a complete change in the present tax statutes. I hope the Senator will not press for a vote.

Mr. KERR. I thank the Senator from Kansas. Again I urge my friend from Indiana not to press his amendment.

The PRESIDING OFFICER. The question is on agreeing to the amendment offered by the Senator from Indiana.

Mr. KERR. Madam President, I suggest the absence of a quorum.

The PRESIDING OFFICER. The clerk will call the roll.

The legislative clerk proceeded to call the roll.

Mr. KERR. Madam President, I ask unanimous consent that the order for the quorum call be rescinded.

The PRESIDING OFFICER. Without objection, it is so ordered.

Mr. HARTKE. Madam President, I ask for the yeas and nays.

The yeas and nays were not ordered.

The PRESIDING OFFICER. The question is on agreeing to the amendment offered by the Senator from Indiana [Mr. HARTKE].

The amendment was rejected.

Mr. WILLIAMS of Delaware. Madam President, for myself, the Senator from Vermont [Mr. AIKEN], the Senator from Maine [Mrs. SMITH], and the Senator from Wisconsin [Mr. PROXMIER], I call up my amendment identified as 8-17-62—C.

The PRESIDING OFFICER. The amendment will be stated for the information of the Senate.

The LEGISLATIVE CLERK. At the appropriate place in the bill it is proposed to insert a new section, as follows:

SEC. . REDUCTION OF OVERALL LIMITATION ON INDIVIDUAL INCOME TAX.

(a) 1962.—With respect to taxable years beginning after December 31, 1961, and before January 1, 1963, section 1(c) of the Internal Revenue Code of 1954 (relating to overall limitation on individual income tax) is amended by striking out "87 percent" and inserting in lieu thereof "75 percent".

(b) 1963.—With respect to taxable years beginning after December 31, 1962, and before January 1, 1964, such section is amended by striking out "75 percent" and inserting in lieu thereof "65 percent".

(c) 1964 AND SUBSEQUENT YEARS.—With respect to taxable years beginning after December 31, 1963, such section is amended by striking out "65 percent" and inserting in lieu thereof "60 percent".

SEC. . DEDUCTION OF DEPLETION ALLOWANCES WITH RESPECT TO OIL AND GAS WELLS.

(a) 1962.—With respect to taxable years beginning after December 31, 1961, and before January 1, 1963, section 613(b)(1) of the Internal Revenue Code of 1954 (relating to percentage depletion in case of oil

and gas wells) is amended by striking out "27½ percent" and inserting in lieu thereof "25 percent".

(b) 1963.—With respect to taxable years beginning after December 31, 1962, and before January 1, 1964, such section is amended by striking out "25 percent" and inserting in lieu thereof "22½ percent".

(c) 1964 AND SUBSEQUENT YEARS.—With respect to taxable years beginning after December 31, 1963, such section is amended by striking out "22½ percent" and inserting in lieu thereof "20 percent".

Mr. WILLIAMS of Delaware. Madam President, this amendment has a twofold purpose:

First, it would provide for a three-step reduction in the depreciation allowance for oil and gas with a 2½-percent reduction for each year for the next 3 years, bringing it down from its present level of 27½ percent to 20 percent.

The second provision of the amendment would permit a simultaneous three-step reduction in the overall limitation on individual income taxes from its present limitation of 87 percent, bringing it down to 60 percent over the 3-year period.

The combination of these two proposals would effectuate a long overdue correction in our existing tax structure and would make this adjustment with an actual gain of revenue to the U.S. Government.

For example, in the first year the depreciation allowance on oil and gas would be reduced from 27½ percent to 25 percent, and the estimated revenue gained from this action is \$75 million.

At this same time the maximum effective rate limitation on individual income taxes will be reduced from its present 87 percent to 75 percent, which would result in a loss of revenue of \$25 million, thus representing a net gain to the Treasury Department for that year of \$50 million.

The second year the depletion allowance for oil and gas would be reduced from 25 percent to 22½ percent, thus providing additional revenue over present law of \$160 million for that year.

Simultaneously the effective rate on individual income taxes would be further reduced from 75 percent to 65 percent, which action would result in an estimated revenue loss of \$80 million.

Thus as the result of this combined action the Federal Government would gain \$80 million.

Effective the third year and for each year thereafter the percentage depletion rate would be reduced to 20 percent. The estimated revenue gain resulting over present law by bringing the depletion rate on oil and gas down from 27½ percent to the 20-percent level would be \$250 million annually.

At the same time in this third year the maximum effective rate limitation on individual income taxes would be further reduced to 60 percent. The revenue loss by reducing this maximum effective rate limitation on individual income taxes from its present 87 percent to 60 percent is estimated at \$130 million annually.

The combined net effect of the adoption of this twofold amendment would be that at the end of the 3-year period the present 27½-percent depletion al-

lowance on oil and gas would be reduced to 20 percent and the present overall limitation on individual income taxes would be reduced from its present 87 percent to 60 percent with an annual net gain to the U.S. Government of \$120 million.

One of the main arguments in support of the need of the present 27½-percent depletion rate for oil and gas has been that under our existing tax structure, which runs as high as 91 percent—with an overall 87-percent limitation—has been that without some special incentive men of wealth would not venture their capital for the narrow margin of gain of 9 or 13 percent. On that point they have a valid argument, and it is for that reason that we have coupled this proposed reduction in the depletion allowance with the simultaneous reduction in the overall limitation on individual income taxes.

The most important feature of this amendment is that its adoption would provide a more equitable distribution of the tax load in America.

At this point I ask unanimous consent to have incorporated in the RECORD a letter dated January 7, 1961, signed by Colin F. Stam, chief of staff of the Joint Committee on Internal Revenue Taxation, in which the estimates as to the revenue of the different sections of the amendment are outlined.

There being no objection, the letter was ordered to be printed in the RECORD, as follows:

CONGRESS OF THE UNITED STATES, JOINT COMMITTEE OF INTERNAL REVENUE TAXATION,

Washington, June 7, 1961.

HON. JOHN J. WILLIAMS,
U.S. Senate,
Washington, D.C.

DEAR SENATOR WILLIAMS: As you requested the staff has prepared a draft of an amendment (attached) to reduce the overall maximum limitation on individual income tax from 87 percent at present to 60 percent over a 3-year period, and to lower the rate of percentage depletion in the case of oil and gas wells from 27½ percent at present to 20 percent, also over a 3-year period.

With respect to the overall limitation on individual income taxes, the draft provides for a three-step reduction, at 1-year intervals, commencing in 1962. For taxable years beginning in 1962, the rate would be 75 percent; for taxable years beginning in 1963, the rate would be 65 percent; and for taxable years beginning in 1964 and thereafter, the limitation would be 60 percent. The staff estimates that these changes in the overall limitation would cause a reduction in revenues to the Federal Government in the amounts shown in the following table.

Maximum effective rate limitation (percent):	Revenue loss (millions of dollars)
75.....	25
65.....	80
60.....	130

The draft also provides for a three-step reduction in the 27½ percent depletion allowance for oil and gas, at 1-year intervals, commencing in 1962. Under the draft, for taxable years beginning in 1962, the rate would be 25 percent; for taxable years beginning in 1963, the rate would be 22½ percent; and for taxable years beginning in 1964 and thereafter, the rate would be 20 percent.

It is extremely difficult to estimate the effect of small changes in the depletion rate

for oil and gas, because we do not have the data we need concerning the present effect of the 50 percent limitation, and because the data on depletion claimed on individual income tax returns is incomplete. Consequently, our estimates for your proposal are rough.

Tax year	Proposed depletion rate for oil and gas	Estimated revenue gain over present law
	Percent	Million
1962	25	\$75
1963	22½	160
1964	20	250

I hope this will be helpful to you.

Sincerely yours,

COLIN F. STAM,
Chief of Staff.

Mr. WILLIAMS of Delaware. Madam President, this proposal should not be too controversial. Perhaps the committee is ready to accept it.

Mr. MANSFIELD. Madam President, it is my intention to move to table the very worthwhile amendment offered by the Senator from Delaware [Mr. WILLIAMS]. It is something new in the way of amendments. It has a good name. It is being offered by the Senator from Delaware [Mr. WILLIAMS], the Senator from Vermont [Mr. AIKEN], the Senator from Maine [Mrs. SMITH], and the Senator from Wisconsin [Mr. PROXMIRE], which gives to it the name "The WASP amendment."

But I do think that Senators ought to have their say both pro and con. I should like to suggest that the Senate vote on a motion to table the pending proposal at 4:30 p.m.

Mr. WILLIAMS of Delaware. Madam President, so far as I am concerned, I have no intention of prolonging the debate. I do not know how much time other Senators may require.

The amendment has received committee consideration. It was offered as an amendment to the bill which was before our committee.

Notice was served to all interested parties who wished to testify that they had an opportunity to appear before our committee. The amendment was pending at the time hearings were held on H.R. 10650. It was discussed during those hearings and it was offered in the committee. So the measure is not something which has been sprung on the Senate without having received committee consideration.

Mr. MANSFIELD. Madam President, I hope the Senator did not take seriously my facetious remark when I referred to his amendment as a new amendment. It is an old, old amendment. I should like to change my request. I ask unanimous consent that 1 hour be allotted on the amendment, the time to be divided equally, before a motion to table the amendment is made and the vote is taken thereon.

The PRESIDING OFFICER. Is there objection? The Chair hears none, and it is so ordered.

Mr. MANSFIELD. The time will be controlled by the Senator from Delaware [Mr. WILLIAMS] and the Senator from Oklahoma [Mr. KERR].

Mr. MONRONEY. Madam President, has the Senator from Delaware used the time available to him?

Mr. WILLIAMS of Delaware. I understand that a half hour is available to each side. I am willing to have the Senator from Oklahoma proceed. If the Senator from Oklahoma finds that he needs more than one-half hour, I shall yield some of my time to him, I have no intention of using all my time.

Mr. MONRONEY. Madam President, the 27½-percent depletion allowance has given America its vast supplies of oil and gas. It has helped us to victory in two world wars, in Korea, and in the cold war. The amendment is not a new amendment. It has been before the Senate about once a year as long as I have been in the Senate. It has been considered by the Finance Committee almost every year. As the distinguished author of the amendment has said, the only new provision is the method of the proposed reduction.

This amendment proposes the progressive reduction in the depletion allowance with respect to oil and gas wells from its present level of 27½ percent to 25 percent for the current taxable year, 22½ percent for 1963, and 20 percent for 1964 and subsequent years.

It proposes that a substantial part of the additional revenue which its sponsors claim would result from this reduction be used to offset loss of revenues which would result from a related provision reducing the maximum limitation on individual income tax from 87 percent to 60 percent over the same 3-year period.

This reduction in income tax in the highest brackets is estimated by the staff of the Joint Committee on Internal Revenue Taxation to result in a loss of revenue of \$25 million the first year, \$80 million the second year, and \$130 million in the third and subsequent years. While it is very difficult to make an accurate estimate of the number of taxpayers involved, I am advised by the Treasury Department that the \$25 million lost in the first year would probably be divided among some 700 taxpayers; that the \$80 million lost in the second year would be divided among some 2,500 taxpayers; and that the \$130 million loss of revenue in the third and subsequent years would probably benefit no more than 10,000 taxpayers.

The proposal for making a cut only in these upper levels of income tax has not been recommended by the administration, has not been the subject of more than casual attention in the hearings, and is proposed at a time when the administration is engaged in a review of the tax structure looking toward recommendations for general reduction next year.

When this amendment was suggested to the Secretary of the Treasury during the hearings, the following exchange occurred between Secretary Dillon and the Senator from Delaware [Mr. WILLIAMS]:

Secretary DILLON. I do not think we would agree with that, because we do not think it is equitable to just reduce the higher rates and not also make the adjustments up and down in the rate structure.

Senator WILLIAMS. This would be making adjustments with the same class of taxpayers and picking up revenue at the same time.

I think that you have said that you thought the individual rates were too high.

Secretary DILLON. I agree they are, but when we recommend the change, we will recommend one up and down the line, not just for the top rates.

Not only do I agree with the Secretary of the Treasury that it is not equitable just to reduce the higher tax rates without a general adjustment in the rate structure, but I suggest that this amendment in effect proposes to benefit these few thousand taxpayers by means of what would amount to an indirect Federal sales tax on gasoline and other petroleum products, which would be paid by every person who drives a car, operates a truck, or heats his home with fuel oil.

I make this charge because the economic facts of the matter are that the 27½-percent depletion allowance, or an increase in petroleum prices which would yield the same amount of money, is absolutely necessary if the oil and gas industry is to find sufficient new oil and gas to replace that being used, and to meet the growing need for oil products in our expanding industrial economy.

They must get the funds for exploration from somewhere. Either they will come from the 27½-percent allowance for depletion of natural resources or they will have to be added to the price of oil products. There is no other way to get the money.

When any mining industry sells a barrel of oil, or a ton of coal, or a pound of uranium, it has one barrel or ton or pound less left to sell. It exhausts that natural resource. If it is to stay in business, it must replace these resources just as a manufacturing industry must replace its wornout equipment.

A manufacturing industry is allowed to retain a part of its earnings, on which it pays no tax, through a depreciation allowance in order that it may replace wornout equipment. In the same way, all mining industries are allowed to retain a part of their earnings to permit them to find and develop new supplies to replace those which have been used up. The oil industry spends a far greater percentage of its income for this purpose than any other mining industry.

It is not generally recognized that the depletion allowance for the oil industry is limited to 27½ percent of its gross or 50 percent of its net earnings, whichever is less. For the industry as a whole, this results in an average depletion allowance of about 23 percent—the same as provided for sulfur, lead, zinc, uranium, nickel, in fact, for a total of 37 other mining industries. Even the producers of sand and clay have smaller depletion allowances under our laws.

If, when an oil well is exhausted, the owner could just go out and buy another, as he would buy a new truck to replace one that is worn out, the depletion allowance could be set much lower. The allowance is set where it is because the process of finding new supplies of oil and gas entails great risk. Unlike minerals which have outcrops on the surface of the earth, there is no way to be certain

where oil is located until the well is drilled and the money spent. If he has average luck, the man looking for the new well will drill eight dry holes before he hits a producer.

Does the Senator from Texas [Mr. TOWER] wish some time?

Mr. TOWER. Yes.

Mr. MONRONEY. Will the Senator tell me how much time he requires?

Mr. TOWER. I should like to have 5 or 10 minutes, if the Senator will yield to me.

Mr. KERR. Madam President, will the Senator yield?

Mr. MONRONEY. I yield.

Mr. KERR. I remind the distinguished Senator that the Senator from Wyoming [Mr. McGEE] and the Senator from Arkansas [Mr. FULBRIGHT] wish a little time.

Mr. MONRONEY. I shall try to make my remarks brief.

If an oil producer invested \$300,000 in a well, and was allowed to recover tax free from the output of that well this same \$300,000 of his original investment, he could not normally go out and for \$300,000 find another well to replace the one he had depleted by production.

Wildcatting odds are dead against that. On the average, a man drilling rank wildcats—a man going out to find new reserves to replace those being depleted—would have to drill nine exploratory wells to find one that even qualified as a producer. But even at that, his one producing well out of nine would—if typical—turn out to be a financial failure. Under the prevailing odds, only about 3 percent of all the new-field wildcat wells drilled are ultimately successful—producing oil or gas or both in quantities deemed sufficient to turn a profit. Ninety-seven percent of all new-field wildcat wells are commercial failures.

Therefore, based on industry averages over a period of time, an oil producer who was depleting a well that cost him \$300,000 would have to have not his \$300,000 back but, at the very least, 32 times that original investment, or \$9,600,000, to stand a fighting chance of bucking the mathematical odds and finding replacement reserves.

Giving him \$300,000 in tax deductions would be little better than giving him nothing. It would be the same as telling him to go out of business because—unless he had a very sensational and remarkable stroke of luck—he just wouldn't be able to find a new wildcat well if allowed no more of a deduction than his investment in a well that was depleting.

In September of 1958 the Chief Petroleum Engineer of the U.S. Bureau of Mines presented a paper to the World Power Conference in Montreal, Canada, in which he discussed the receipts and expenditures of the U.S. petroleum producing industry—including both independents and major companies—for the years 1951, 1953, and 1955. The study shows that in 1955 the industry expended a total of \$5.1 billion in the search for and development of new petroleum reserves within the United States. This study also shows that for the year 1955, finding and developing costs together

with lifting and other operating costs were in excess of income from petroleum production for the entire producing industry by approximately one-half billion dollars.

The \$5.1 billion expended in 1955 in the exploration for and development of new oil reserves was equivalent to \$2.40 per barrel of net crude oil production in that year. Based on the U.S. Bureau of Mines average wellhead price of crude oil for the year 1955 of \$2.77 per barrel, the theoretical maximum percentage depletion could not have exceeded 76 cents per barrel. This depletion figure, however, for petroleum producers is a theoretical maximum, based on the 27½-percent rate, rather than the actual amount of depletion, since the 50-percent-of-net-income limitation reduces the average effective depletion rate for the petroleum industry to no more than 23 percent.

Thus, the domestic petroleum industry's exploration and development expenditures alone in 1955—not including lifting costs, taxes, and so forth—totaled \$2.40 per barrel or more than three times the maximum percentage depletion of 76 cents. That is, for every dollar from percentage depletion plowed back in the search for new oil reserves, the producing industry put up and spent \$2 from other sources.

This information, detailed in the accompanying table, clearly demonstrates that the petroleum producing industry requires new capital far in excess of the depletion deduction to carry on the constant search for new oil and gas reserves.

Mr. RANDOLPH. Madam President, will the Senator yield?

Mr. MONRONEY. I am glad to yield to the Senator from West Virginia.

Mr. RANDOLPH. West Virginia is not ranked with Texas and Oklahoma and Louisiana and other major States in the production of petroleum. Yet from our hills went the oil people of another era to help explore these vast fields in other sections of the country. In West Virginia, in years gone by, we were a pioneering and important oil and gas producing State.

Our State in its entirety, the western three-fourths of Pennsylvania, much of the southwestern area of the State of New York, the eastern half of Ohio, eastern Kentucky, and a narrow strip of the westernmost part of the Commonwealth of Virginia comprise an area known in the oil geology circles as the Appalachian Basin.

Here was located oil's discovery in the United States in 1859—by Col. Edwin Drake at Titusville, Pa. And this is the region of considerable activity in earlier years.

Four of these pioneer oil States—Pennsylvania, New York, Ohio, and West Virginia—are experiencing a new wave of "oil fever." These four States are oil-hunting territory again for several major searchers for new discoveries. During the last 5 years there has been a sharply stepped-up effort to try to find more sources of oil and gas closer to the vast market which surrounds it, namely, the industrial complex of the Ohio River

Valley with its population of more than 52 million.

Technological advances in exploration, drilling tools, and methods have brought about a significant reworking of this pioneer oil producing Appalachian Basin. But today's driller must reach 1 or 2 miles deeper than Colonel Drake's first 69-footer at Titusville to find a product the colonel would have considered a bothersome pest—gas. But gas, as well as oil, is a frequent drilling objective today.

Madam President, exploratory and drilling expenditures have more than doubled during the past 5 years in the Appalachian Basin. The level of \$6.5 million in 1958 reached \$11.9 million in 1961. Estimates for 1962 exceed \$14 million. By the end of this year, the oil industry's outlay for the 5-year period is expected to represent a risk venture of approximately \$52.7 million in the basin. In addition, farmers and landowners in the basin have been paid \$24.4 million for leases plus annual rental payments of \$8.6 million.

Even though these concerted efforts and huge expenditures so far have not brought significant new discoveries in the Appalachian Basin, the industry is continuing its activities in the hope and belief that they may ultimately lead to the discovery of substantial reserves.

Each drilling prospect and the acreage surrounding it represents the concentrated and coordinated skills of highly trained and experienced exploration specialists. Yet, no one in the group can say oil or gas will be found. They can only locate zones where conditions are right for the accumulation of oil or gas. Whether oil or gas actually is there must be proved by drilling a wildcat well. The chances are 9 to 1 against it—45 to 1 against finding a commercial quantity. To engage in risks of that nature is to require encouragement such as the necessary cushion from the depletion allowance.

Considering the unemployment situation and other economic factors prevailing in West Virginia, we are grateful that there is increased search and discovery activity in our State by the oil and gas industry. We know there is drilling at deeper horizons and that this requires more risk capital.

Drilling permits issued in West Virginia increased from 988 in 1959 to 1,383 in 1960 to 1,647 last year.

Producing gas wells last year numbered 16,485 and produced 194,178,000 thousand cubic feet of gas; 12,699 oil wells in our State produced 2,703,000 barrels in 1961.

Crude oil and natural gas production and distribution—exclusive of refineries and service outlets—provided jobs for 8,547 West Virginia resident employees of independent producers and gas utilities, and provided pension payments for 2,282 annuitants. The independent and utility segment of the industry—again excepting refineries and service outlets—spent approximately \$61 million in West Virginia last year—\$43.6 million of it in payrolls and \$8.4 million for rentals and royalties.

Madam President, I have cited statistics indicating that the oil and gas industry is not an inconsequential segment of the West Virginia economy—that it is happily an expanding segment again—not in contraction. We want it to continue expanding and to discover vitally needed new reserves. Our State needs them and they are vital to the economy and the security of our country. I cannot support a deterrent.

There is another reason why I believe the pending amendment is ill timed. More than 60 Members of the Senate joined me in cosponsoring a resolution which was adopted earlier this year and which empowered the Committee on Interior and Insular Affairs to make a thorough national fuels and energy study. The committee has been making very real progress with this study under the capable direction of its distinguished chairman, the junior Senator from New Mexico [Mr. ANDERSON]. It is anticipated that substantial findings and rec-

ommendations will be reported early next year as the 87th Congress gives away to the 88th. We should await the committee's report and its evaluations before taking the nature of action contemplated by the pending amendment. There should be more assurance than has thus far been demonstrated that this amendment will not destroy more than it will create in revenues and in gross national product.

I believe that the incentive which is now written into the law should be continued. The amount of money spent proportionately in West Virginia equals the averages which were given by the knowledgeable Senator from Oklahoma.

Mr. MONRONEY. I thank the Senator for his contribution. I ask unanimous consent to have printed in the RECORD at this point in my remarks some tables which bear on this subject.

There being no objection, the tables were ordered to be printed in the RECORD, as follows:

Net value of production versus expenditures for finding, developing, and producing oil and gas

[In thousands]

	1951	1953	1955
Industry income:			
Net value oil produced.....	\$4,862,136	\$5,401,018	\$5,884,215
Net value gas produced.....	465,451	660,501	836,324
Total, net value production.....	5,327,587	6,061,519	6,720,539
Industry expenditures-exploration costs:			
Geological, geophysical, and related professional services.....	186,000	243,590	245,440
Lease purchases and rentals.....	637,910	744,630	876,520
Dry holes.....	650,290	795,890	940,210
Overhead.....	126,780	171,270	206,220
Total, exploration costs.....	1,600,980	1,955,380	2,268,390
Development costs:			
Drilling and completion of producing wells.....	1,390,050	1,689,607	2,097,225
Equipment (tubing, tanks, flow value, etc.).....	420,360	483,000	556,210
Overhead.....	135,780	168,378	205,640
Total, development costs.....	1,946,190	2,340,985	2,859,075
Subtotal, exploration and development costs.....	3,547,170	4,296,365	5,127,465
Operating costs:			
Oil:			
Direct costs.....	1,274,149	1,392,576	1,540,092
Overhead.....	242,146	306,326	337,758
Total, oil operating costs.....	1,516,295	1,698,902	1,877,850
Gas:			
Direct costs.....	89,220	134,675	134,097
Overhead.....	7,758	10,920	9,387
Total, gas operating costs.....	96,978	145,595	143,484
Total, operating costs.....	1,613,273	1,844,497	2,021,334
Total, expenditures for finding, developing, and producing ¹	5,160,443	6,140,862	7,148,799
Net annual balance.....	+167,144	-79,343	-428,260

¹ Includes maintenance, supervision, and general overhead but excludes charges for research. The costs do not include income taxes, payment on interest and principal, or return to investors.

Source: "Petroleum and Natural Gas in the United States—Relation of Economics and Technologic Trends," by C. C. Anderson, Chief Petroleum Engineer, U.S. Bureau of Mines, Washington, D.C.

Mr. MONRONEY. In the years since 1955 the cost of finding oil has steadily risen. Not only have drilling costs per foot increased, but the number of feet which must be drilled to find a barrel of oil has gone up each year. Most of the oil located 2,000 to 3,000 feet below the surface of the earth has already been found. A far greater percentage of wells are being drilled at greater depths, and we are now exploring at depths of 15,000 to 25,000, at costs as high as \$1 million per well.

During the same period, the price of crude oil has remained essentially stable,

the average value at wellhead having been \$2.77 in 1955, \$2.79 in 1956, \$3.09 in 1957, \$3.01 in 1958, \$2.90 in 1959, \$2.88 in 1960 and \$2.89 in 1961.

If the oil industry were keeping more money than it needed to replace the oil being used, then it might be argued that the depletion allowance is too high. The fact is that each year the industry continues to spend more finding and developing new supplies of oil than it retains under the depletion allowance.

It stands to reason that the funds available to the industry for exploration and development cannot be significantly

reduced without resulting in a proportionate reduction in exploration and development. I hope that we have not reached the point when the Congress of the United States is ready to adopt a policy that we should not develop our own mineral resources and gain the benefits that such development brings to our economy, but should become completely dependent on imported oil. Our entire economic system is geared to an adequate and dependable supply of petroleum. All our transport, from compact cars to jets, from diesel trucks to diesel locomotives, depends upon a cheap and plentiful supply of petroleum. Our industrial plant depends to a large degree upon petroleum products or electricity generated from them for the sinews of its power.

During World War II petroleum products comprised more than half of the tonnage shipped from the United States to battle fronts all over the globe. The military machines that have been developed since that conflict are even more demanding in their fuel consumption. The Air Force alone consumed nearly 6 billion gallons of aviation fuel in the peacetime fiscal year 1960. And it is no wonder when we realize that a single jet bomber has a fuel tank capacity equal to four railroad tank cars. A *Forrestal*-class aircraft carrier carries 1 million gallons of aircraft fuel plus more than 2 million gallons of fuel for its own engines. Recent model Army tanks consume 600 gallons of gasoline in covering 100 miles, and an armored division must burn up 2,100 gallons of fuel to advance 1 mile.

We cannot afford to depend upon imported oil because of our balance-of-payments situation. Oil imports already contribute a billion dollars a year to our balance-of-payments deficit. We should rather look forward to the time when the dependence on imported oil can be substantially reduced and when the growth of world markets again makes the United States a net exporter of petroleum products.

It is inconceivable that as we enter a trade war with the Soviet Union, with oil as the principal weapon, our Nation should simply relinquish the field to the enemy.

Mr. TOWER. Madam President, will the Senator yield?

Mr. MONRONEY. I yield.

Mr. TOWER. Is the Senator aware of the fact that at the conclusion of World War II the oil reserves of the Soviet bloc were approximately one-third of ours and that today they are almost equal to those of the United States? Does not this point up the vital necessity of staying ahead in this field?

Mr. MONRONEY. Yes. The great threat of the Soviet trade offensive is in oil. That is one field in which they have surpluses. With it they are penetrating the free world markets.

We cannot have it both ways. If the American oil industry is to continue to find adequate supplies to meet the Nation's needs, it must obtain the necessary funds to pay for the cost of exploration. We must either retain the present depletion allowance, or accept a substantial increase in the cost of gasoline and other

petroleum products. There are no other sources of the necessary money. The profits of this industry are consistently lower than the average profits of manufacturing industries in the United States.

Some of those who have been critical of the depletion allowance have frankly recognized that its withdrawal would require an increase in price. Prof. Arnold G. Harberger, of the University of Chicago, has testified that—

More oil can indeed be obtained by tax concessions * * * [but] * * * if the rest of the economy wants more oil, it should be willing to pay for it by way of a higher market price.

This means primarily an increase in the price of gasoline.

It is impossible to estimate the contribution to our economic health which has been made by the availability of low-cost motor fuel. The entire automobile industry and much of our commercial transportation has been built on this tremendous economic advantage.

Excluding excise taxes, a gallon of gasoline costs less today than it did in 1926. Today, it costs 20.2 cents per gallon, in 1926 it cost 20.9 cents. At average wage rates, 1 hour's work bought 2.6 gallons in 1926. Today, it buys 10 gallons, exclusive of tax.

To give a tax benefit to a handful of Americans with taxable income over \$150,000 a year and to make up the difference by levying an indirect tax through immediate higher prices on everyone who owns a car or heats his home with fuel oil—this is a proposition which I am confident the Senate will overwhelmingly reject.

Madam President, I yield 5 minutes to the Senator from Texas.

Mr. TOWER. Madam President, I thank the distinguished Senator from Oklahoma, and I associate myself with his comprehensive report on this subject. The oil business is a very unique business, indeed. Actually, it is a business that has been made by the small entrepreneur, the independent operator. Approximately 80 percent of our oil reserves have been discovered by the independent or marginal operator.

If the depletion allowance is reduced, it will drive the independent operator out of business. As the able Senator from Oklahoma has pointed out, production costs have risen steadily. In 1959 the average cost per well was around \$60,100. In 1961 it was \$62,200.

It has been pointed out that we have to go deeper and deeper for oil, and at present costs, to get down to 10,000 feet it costs \$140,000 to drill a well. And then one does not know whether or not he will get any oil.

In most businesses that is not the situation at all. For example, if a man wishes to open a hardware store, he can take a market survey in the area to determine whether his business will succeed and if there will be a market for his business. Based on that survey he can build his store and buy his stock. Then, if his business does not succeed, he still has his capital assets that have some value, and which he can dispose of. He has not taken a very big risk. That is

not the case when a man drills an oil well. When he does that, he does not know whether he will get any oil. It is somewhat like the roll of the dice or the turn of a card.

Oil is extremely important to the defense of this Nation. It is certainly a very important source of tax revenue for State and local governments throughout the various parts of the land.

Oil provides a great number of jobs. It provides our country with material wealth. For this reason the exploration and production of oil must be encouraged.

If we eliminate the depletion allowance, the oil industry, which is already sick, will be even sicker. We are suffering already from imports of oil, and if we eliminate or reduce the depletion allowance, we will inflict an additional burden on the oil industry. We are producing only 8 allowable days a month in Texas, now. This is well below even marginal requirements.

Therefore, I urge the Senate to reject this very well intentioned amendment by the distinguished Senator from Delaware, with whom I am usually associated on fiscal matters, because its adoption would mean economic disaster to many of our oil-producing States. It would mean a substantial loss of tax revenue. Even more, Madam President, it would mean a reduction in the ability of our Nation to wage war through the industrial power that is fueled by petroleum. I believe, furthermore, that it would mean a considerable loss of jobs and production in related industries, and might very well precipitate a recession in the country.

Mr. MONRONEY. Madam President, I yield 5 minutes to the distinguished Senator from Louisiana.

Mr. LONG of Louisiana. Madam President, during the 14 years that I have served in the Senate I have had some experience with this matter. From time to time a Senator has offered a proposal to reduce the depletion allowance on oil and gas. We have debated the matter many times in the Senate. The subject has been studied in committee on occasion. It has not been sustained in the House and it has not been recommended by the committee. Furthermore, the proposal has been defeated by overwhelming vote in the Senate every time it has been brought before us.

If there is a case for reducing the depletion allowance on oil and gas, it is not nearly so good a case as it was 10 or 12 years ago, when the domestic industry was much more profitable than it is now. Actually, the industry is in not nearly so good a condition as it was 12 years ago. About 17 percent of the market for oil in this industry has already been taken from us by low-cost foreign imports which come in under an extremely low tariff.

In addition, as has been indicated, costs have risen. A study made a few years ago by the Chase National Bank indicates that, all things considered, including the allowance for depletion, the oil and gas production industry is less profitable than the average for all manu-

facturing in America. The industry today is in worse shape than it was at the time that study was made.

So the facts simply do not prove that there is any basis for coming in at this time, without any additional supporting evidence, and saying that the depletion allowance should be reduced below the point where it presently exists.

I have given some thought to a proposal that the top income tax brackets be reduced by taking away the tax advantages which various groups have. If that is to be done, it seems to me it would be much fairer simply to eliminate the dividend credit, as the President has recommended it should be eliminated, and save much more money in that way. Instead of reducing the tax level from 85 to 65 percent, or 60 percent, we could reduce it to 50 percent and still save \$100 million to be applied against the national deficit or national debt, however Senators wish to look upon it.

If a motion to table the amendment does not carry, I intend to offer such a proposal as a substitute for the amendment offered by the Senator from Delaware. Most of the giant corporations are incorporated in his State anyway. Inasmuch as the reduction is to be regarded as a reduction in personal income tax rates, it seems appropriate to me that those who are in the class who, for the most part, do not enjoy the highest personal income tax—that is, who enjoy large incomes from dividends—should be willing to give up something rather than to hope to gain a complete tax advantage at the expense of only one segment of the economy—those who produce oil and gas.

If that approach is to be pursued, I should like to offer an amendment in the nature of a substitute to abolish the dividend credit, a credit which has never been approved affirmatively by the Senate. It was rejected by the Senate. It got into the law only as a part of a conference report, with the administration fully supporting the whole package in the conference report. The Senate has repeatedly voted to reject the dividend credit.

If this approach is to be persisted in—and I shall not insist upon it myself—I shall insist on reducing income taxes from the top level by a proposal to eliminate the dividend credit, because that seems to me to be a way which would fall generally across the whole economy with regard to all those who are privileged to enjoy dividends, both from oil and gas companies and any other kind of industrial companies, so that everyone may share the burden of reducing the top bracket to a rate of 50 percent instead of 60 percent.

Mr. DOUGLAS. Madam President, I ask for the yeas and nays.

Mr. WILLIAMS of Delaware. Madam President, will the Senator from Illinois withhold his request? The motion to table has not yet been made.

Mr. DOUGLAS. I withhold my request.

Mr. CARLSON. Madam President, will the Senator from Oklahoma yield 5 minutes to me?

Mr. MONRONEY. Madam President, I yield 5 minutes to the distinguished Senator from Kansas.

Mr. CARLSON. Madam President, I wish to associate myself with the distinguished Senator from Oklahoma [Mr. MONRONEY], the distinguished Senator from Texas [Mr. TOWER], and the distinguished Senator from Louisiana [Mr. LONG], in their opposition to the pending amendment.

For various reasons, this proposal has received increasing attention in this body over the past several years, as well as in the public press. I shall refer in general to the differential tax treatment Congress has authorized for mineral producers and, more particularly, to the percentage depletion rate for oil and gas production.

As we well know, this tax provision has been the subject of repeated study and review by Congress during the 36 years that it has been a part of the Internal Revenue Code. In spite of repeated votes of approval of this vital tax provision, there still remain some who, for one reason or another, seek to reduce the rate or eliminate this vital tax provision.

Many Senators are well acquainted with the historical growth and merits of percentage depletion; while others, I fear, do not quite understand how this provision has served the national interest for more than 36 years.

Madam President, without going into an extensive discussion of this matter, I believe that when Congress placed this tax provision in the law back in 1926, it intended and expected that its newly enacted tax policy would accomplish two basic things: First, recognize that mineral extraction is the using up of a capital asset and, therefore, should not be taxed as income; second, encourage, through fair tax laws, the continuing and increasing exploration for and development of new mineral reserves to replace those currently being used up. In the case of oil and gas, as well as many, many other minerals, percentage depletion has proven eminently worthwhile in accomplishing these goals. It is no longer an experiment; it is a proven experience. Percentage depletion has proven its worth in helping to make available at reasonable prices adequate supplies of petroleum products to meet the needs of our national security and ever-growing economy.

I do not wish to unduly add to what has been said so many times about percentage depletion and just why it is a part of our tax structure. Nor do I intend to cite to you lengthy statistical data to support the principle and allowable depletion rates for the many, many minerals now subject to percentage depletion. This information is readily available for all to read and consider in the many studies by the Senate Committee on Finance and the House Ways and Means Committee.

I do not believe the Senate floor is the proper place to delve into the detailed operation of this or any other long-standing tax provision. We have a highly competent Committee on Finance, of which I am proud to be a member,

which, if need be, is the proper and logical place for a thorough review of this very much misunderstood tax provision.

However, I firmly believe that in the light of all that has been said in the Senate during the past several years, we in the United States Senate have a duty and a responsibility to place this matter of percentage depletion in its proper perspective. One might ask the question, "Just why do we continue percentage depletion in the law?" The answer is obvious. It has successfully accomplished the task laid down for it when it was first written into the law in 1926. When Congress first established the present depletion rate for oil and gas, it recognized the need for an incentive for men to assume the extreme risks peculiar to petroleum exploration. Congress understood then, which remains a fact today, that geological, geophysical, and other predrilling work can only indicate possible oil and gas structures in the earth's crust. Only the drill can determine the actual existence of petroleum. The well-known odds against finding oil in the exploratory well still are 8 to 1, and the dry holes are just as costly to drill as producing wells. I should also point out that even in proven areas the driller of oil wells finds that one of every four wells drilled is dry.

In spite of the fact that this is a very risky industry and that the cost of finding and producing petroleum have grown in leaps and bounds the oil industry is making available to the consuming public today its products at very reasonable prices. Possibly, without percentage depletion, our Nation today would not have available enough petroleum to meet our current as well as our future needs. However, even the critics of this tax provision agree that without it the price of oil and its products would be far greater than now prevail.

If the price of gasoline had increased since 1926, the year percentage depletion came into the law, in proportion to the increase in the consumer price index, gasoline would cost today 65 percent more than it did in 1926. Instead, gasoline, the principal product from a barrel of crude oil, sells today, excluding State and Federal taxes, for about the same price that the consumer paid for a much lower grade product back in 1926.

In 1926 average hourly wages would buy 2.6 gallons of gasoline excluding taxes. Today an hour's average earnings will buy about 10 gallons of much better gasoline.

Stated simply, for more than 36 years, percentage depletion has helped the petroleum industry to make available to the American people the vital energy required to make more and better things for more people—at very reasonable prices. The consumer has been the chief beneficiary of this wise congressional tax policy, percentage depletion.

Madam President, in my own State of Kansas, which is not only a large producer of petroleum but a large consumer of petroleum, the reduction or elimination of percentage depletion would have a great adverse impact upon the produc-

ing branch of the industry as well as adversely affecting the consumers of petroleum in my State. Recent competent studies have shown that to offset the elimination of percentage depletion, if we are to continue to maintain the necessary levels of exploration for and development of adequate petroleum supplies in this Nation, the service stations' price of gasoline would have to be increased approximately 5 cents per gallon in order to provide to the oil producers, after Federal income taxes, the necessary funds which would be denied him from his earnings if percentage depletion were eliminated. Thus, this would mean to the consumers of the State of Kansas an additional cost of approximately \$54 million per year or approximately \$90 additional cost to the average family in the State of Kansas.

Madam President, in these days when we hear so much about the need for economic growth and increased productivity, it becomes important to take a look at some of the basic ingredients for the strong economic growth of our Nation and its productivity.

Economic growth and productivity of the United States is based squarely on the use of inanimate energy. Today, more than 70 percent of the inanimate energy used in America is supplied by oil and natural gas with coal furnishing 24 percent and water power and atomic energy the balance.

With each barrel of oil or cubic foot of natural gas produced in the United States, there comes into being additional energy for use in meeting the ever-broadening national goal of more and better things for more people. Large consumption of petroleum at prices every citizen can afford has provided this Nation with the highest standard of living in the world.

Without question, one of the essential ingredients for meeting and winning the struggle to preserve our way of life is our Nation's growth. Sound growth is dependent upon abundant supplies of energy. Development of the energy age in America has been swift and dramatic causing phenomenal growth in America during the past quarter of a century.

America has substituted petroleum energy for the work once largely performed by humans and animals because of the availability of this commodity at reasonable prices.

For more than 36 years a prime factor contributing to adequate supplies of petroleum at reasonable prices is the wise congressional tax policy—percentage depletion.

For more than a quarter of a century, the growth in the national income in the United States, as well as most other nations of the world, has paralleled the growth in each nation's energy consumption. If we consider each gallon of energy produced and consumed—expressing total energy in terms of equivalent gallons of oil consumed each year—the national income of the nations of the world varies from country to country in the direct relationship of about \$1 of national income per capita for each gallon of such energy consumption.

For example, according to the report of the Joint Congressional Committee on Atomic Energy, January 1956, in the Netherlands per capita consumption of energy was equal to 448 gallons of oil. National income per capita was \$447. In the case of the United States—the highest energy consuming Nation in the world—per capita consumption of energy amounted to 1,711 gallons, and the national income per capita amounted to \$1,857.

As growth and expansion of a nation is directly tied to growth and expansion of available energy supplies, it is axiomatic that our Nation's policies should be such as to encourage the exploration for and development of new petroleum reserves. For more than 30 years the 27½-percent depletion rate for petroleum has been the keystone of the many governmental policies designed to increase this Nation's petroleum resources. It has done its job well. It should be allowed to continue to do so.

Abundant low-cost energy is the foundation of a growing economy, and percentage depletion is the key to greater and greater supplies of such energy at reasonable costs to the consumer.

Percentage depletion fosters growth.

I could speak at length about how a reduction in the effectiveness in percentage depletion would adversely affect the economy of my State of Kansas. However, in the interest of time, I shall simply state that the oil-producing industry in Kansas is becoming more and more a marginal operation, and any adverse tampering with this would, to say the least, be a crushing blow to the economy and welfare of my State. This would, no doubt, be the case in the majority of the other 30 oil-producing States.

I emphasize that aside from the harm that could result to the consumers and oil producers in my State from any cut in percentage depletion rate, there is another and possibly a bigger issue, and that is how would the tampering with this long-established congressional policy affect our basic national resources policy?

In September 1960 President Kennedy stated aptly the basic consideration involved in the depletion principle when he declared—

The depletion allowances which affect over 100 items should be considered primarily as a matter of resources policy and only secondarily as a tax issue.

President Kennedy stated further that—

Its purpose and its value are first of all to provide a rate of exploration, development and production adequate to our national security and the requirements of our economy. * * * The oil depletion allowance has served us well by this test.

All too often the critics of percentage depletion ignore this sound observation and rather contend that a reduction in percentage depletion is necessary because Government temporarily, at least, might collect more revenue if depletion were eliminated. This understood rationale would, of course, have far reaching and undesirable impact throughout our economy.

One of the most sound analyses of the need for and merits of percentage depletion was contained in an editorial paper in the August 1962 issue of the Independent Petroleum Monthly by Minor S. Jameson, Jr., executive vice president of the Independent Petroleum Association of America. I quote in part from this fine editorial:

Percentage depletion is ingrained in the economic and financial processes of the petroleum industry. It has been for 36 years. Its change or elimination would have repercussions of vast proportion, all detrimental. These adverse results could be factually presented only with great detail, but they can be summarized as follows:

1. A flight of capital from the industry and disruption of investments on an almost panic scale. There would be chaos during an unprecedented adjustment in industry financial processes.

2. Sellouts and mergers among smaller industry units would be greatly accelerated with a resulting increase in corporate concentration in the production and control of petroleum.

3. Contraction of the industry would lead to greatly reduced levels of exploration, drilling and development with an inevitable gradual decline in availability of domestic petroleum.

4. Severe impairment would occur in the economies of the thousands of oil communities throughout 33 producing States.

5. Through shrinking of the largest of the mineral producing industries, there would follow a reduction in the overall base for local, State and Federal tax revenues.

6. Expanding military requirements for petroleum fuels, one of the larger single expense items of the Federal Government, would be filled only at a much greater cost.

7. Reduced industrial activities would be followed by reduced markets for steel, other basic materials, and hundreds of supplying and servicing organizations sustained by petroleum production.

8. Capital expenditures would be diverted in large scale to foreign areas with a compounding of our adverse balance-of-payments situation.

9. With economic growth directly related to energy use, principally low-cost petroleum fuels, economic expansion would be impeded.

10. Unquestionably there would be less crude oil and gas found and developed, or adequate domestic supplies would be maintained by a more concentrated industry at greater cost and much higher prices to consumers. The alternative would be greater dependence on foreign oil. Neither alternative would be in the public or national interest.

These are some of the fundamentals which cannot be ignored in consideration of petroleum tax policy. Some would occur immediately, others if depletion provisions were reduced or eliminated. Certainly, as a matter of national policy, it would be inconsistent to precipitate such an upheaval in so basic an industry at a time when economic progress and growth has such priority and urgency.

Madam President, as I stated in the beginning, this important tax policy is one that should not be subject to emotional and unfounded attacks on the Senate floor; but rather any review of how it works and why we have it in the law should be considered only after a thorough and comprehensive study by the committee of Congress charged with the responsibility of weighing all the factors involved in recommending to this

body changes or additions to our Nation's tax laws.

Madam President, I am convinced that, when thoroughly reviewed and considered in this manner, percentage depletion will once more be overwhelmingly approved by Congress.

Mr. TOWER. Madam President, will the Senator from Kansas yield?

Mr. CARLSON. I yield.

Mr. TOWER. Is the Senator from Kansas aware that sometimes the depletion allowance is referred to as a subsidy, but that under no definition of the term could the depletion allowance be regarded as a subsidy, because actually it is the forgiveness of a tax to a man who is actually selling his capital assets, for once oil is sold, it is gone and is not replaceable? As the distinguished junior Senator from Oklahoma said a while ago, it is not possible to go out and buy a new oil well.

Mr. CARLSON. The depletion allowance is given because a capital asset is being destroyed or being used as it is taken out of the ground.

Madam President, I continue to emphasize the need for a depletion allowance.

Mr. McGEE. Madam President, will the distinguished Senator from Oklahoma yield 5 minutes to me?

Mr. MONRONEY. I yield 5 minutes to the distinguished Senator from Wyoming.

Mr. McGEE. Madam President, in no area of the country is the question of oil depletion allowance of more vital concern than in Wyoming. Because of the particular attributes of the geology in our area, exploration for oil is extremely costly and a much less productive venture. Yet because the industry has been willing to take chances, it has been possible to bring in large reserves of oil to serve the national interest.

I think this is the real point at stake in this particular operation: There is a tendency among some who, I am sure, do not understand the situation, to call the depletion allowance an evasion or a loophole when, in fact, it is only a device that is determined upon to encourage further exploration activities. The oil industry in my State would go out of business very quickly if it did not have this further inducement, because of the cost of exploration for oil.

Madam President, America's position in history has been greatly bolstered by the fact that it is a nation rich in natural resources. We have been abundantly blessed with mineral wealth—iron ore, gold, silver, copper, bauxite, to name a few such treasures, plus the vital energy fuels—oil, coal, natural gas, and, more recently, uranium. But having these minerals in the ground means, in itself, nothing to national progress. Other lands with vast mineral resources have remained backward and poverty-ridden.

Mineral wealth of itself is meaningless until there are people with the initiative, the courage, the means, the vision, and the enterprise to get these raw materials out of the ground and make them available to their fellow citizens.

For example, there are vast pools of oil in this country over and above the nearly 39 billion barrels of proved reserves—known reserves—of crude oil and natural gas liquids. These additional reserves, still to be discovered and to be made available for future generations, are variously estimated to run to hundreds of billions of barrels; the recent National Fuels and Energy Study, prepared by a special staff for the Senate Committee on Interior and Insular Affairs, places the figure at somewhere between 225 and 300 billion barrels.

But this oil that is now in the ground could stay there, and conceivably future generations of Americans could suffer all the deprivations of a fuel famine—unless venturesome people pooled the money and the skill to find these reserves in their hiding places thousands of feet in the earth.

The odds are about 50 to 1 against commercial success in wildcat drilling for crude oil, and are only a bit better in the hunt for oil and gas combined. Furthermore, no one is guaranteed even average luck—that he will make a commercial find if he drills 50 wildcat wells. Many an oilman has drilled his way to the poorhouse with a run of hard luck that went even beyond the severe law of averages in wildcatting.

The purpose of percentage depletion is to make the hunt for new oil possible even in the face of these adverse odds. Without this tax provision, there would be an inevitable slackening in the search for new reserves, with the consequence that consumers would feel the pinch a few years hence—and this country could be faced with a very grave crisis.

There is no such thing as percentage depletion in Russia, because in that country the Government owns all the oil lands and oil-finding equipment. The Government does the wildcatting, and it also makes the decision as to what is to be done with the oil. The Soviet Government has already decided that it is uneconomic for average citizens to own automobiles—and for that reason Soviet policy deliberately prevents mass ownership of automobiles such as we have in the United States. This leaves the Government free to exploit its national oil resources by using oil exports as a weapon in the economic cold war.

Our domestic oil industry is faced with this Russian challenge, and so are the oil industries of other free world nations—many of them operated by or affiliated with American companies. If any amendment that tinkers with the depletion rate is enacted, it will directly impair the ability of our free-enterprise domestic oil industry and its foreign affiliates to compete effectively against the government-controlled Soviet oil enterprise, and we shall be handing Russia a trump card that it is sure to play in the cold war.

If this amendment should be adopted, would its sponsors be content with their victory and would they end their attacks on the percentage depletion provision? It is certain that they would not. One victory like this would only whet their appetites for more. It would spur on

the attack against this provision in the law. And it should be understood by all who are going to vote on this amendment that the real issue is not confined by any means to percentage depletion as it applies to oil and gas.

The real issue being disputed today is percentage depletion as it applies to some 100 or so mineral industries—practically every type of mineral produced in this country today. All these industries are the real targets for this attack, with oil and gas just positioned in the bull's-eye. A Senator who votes for this amendment should keep in mind the extent to which he could be jeopardizing the future of the leading mineral industries of his home State, whether his State produces lead, zinc, copper, iron ore, granite, asbestos, or whatever.

Other segments of the extractive industry affected by the depletion allowance consist of 100 or so other minerals that come under the very same tax provision—though at varying rates—which it is being proposed we reduce for oil and natural gas. Should this amendment succeed, it will be used as a lever to pry loose the depletion rates all these other minerals now receive. The only question is which mineral would be next to suffer a cut in its depletion rate?

Would it be uranium? I ask this question with some anxiety because my State happens to rank second, behind New Mexico, in the production of this vital mineral—which now receives a 23-percent rate. Would the next mineral be fluor spar, also entitled to a 23-percent deduction, or tripoli—with 15 percent? Illinois, for example, happens to lead the Nation in the production of both these minerals, and it is an important producer of bituminous coal as well as a significant contributor to the Nation's supply of oil and gas.

Perhaps zinc would be singled out, and that would be bad news for Tennessee because that State happens to be the leader in producing this mineral, with a 23-percent deduction helping to encourage the development of that important industry there.

Perhaps the people of Vermont should be alerted to the danger threatening their asbestos industry. The 23-percent depletion rate for this mineral would be a sure victim of any massive campaign to eradicate or slash to pieces this provision in the Nation's tax laws.

If the deduction for oil and gas is a loophole, then so are these identically based deductions for other minerals; and if the rate for oil and gas is to be reduced, proportionate reductions would necessarily have to be made for these other minerals to restore the balance. But if percentage depletion is a loophole—in the common meaning of the term—then a 20-percent rate or a 15-percent rate can no more be justified than a 27½ percent or 23 percent. If depletion is wrong in principle, changing the rate cannot possibly make it right.

But, of course, the hard fact is that these provisions are not loopholes—none of them. Loophole has merely become an inaccurate label. To the average per-

son on the street, the term "loophole" suggests an evasion of the law. It implies taking advantage of some opening never intended by the framers of a statute. We know that this is not the case with the percentage depletion provision, as it applies to oil and gas or to uranium or to zinc or gold and silver or any other mineral.

The percentage depletion provision is clearly authorized by law. It was duly enacted by Congress in the case of oil and gas and in the case of every other mineral included under the terms of that provision. There is no question whatsoever of its being a loophole. It is a deliberate, express, and clearly intended provision of the tax code.

Was the purpose of this provision—as its opponents insinuate—to give some special advantage to the few? Not at all. The intent of Congress when it enacted this provision with respect to oil and gas was to remove tax obstacles that might have the effect of hindering the high-risk and costly exploration for and development of these vitally needed energy fuels. Other minerals—coal, uranium, zinc, lead, asbestos, gypsum, to name just a few—are included under this provision for exactly the same reason.

Congress recognized that the person engaged in an extractive industry—whether he happens to be a producer of oil or a producer of zinc or of some other mineral—has peculiar operating conditions not experienced by, let us say, the operator of a dry goods store or an auto laundry. The mineral producer—whether he is producing oil or iron ore—is depleting the resource that constitutes his capital.

Every time the oil producer takes a barrel of oil out of his well, he is one barrel closer to going out of business. Every time the mine owner takes out a ton of ore, he is in the same position. Both have to find replacement reserves, and that is not easy.

In the case of oil and gas, of every 100 exploratory wells drilled in the search for a new field, only 3—on the average—will make a commercially successful discovery.

It would be sheer nonsense to tax a business that is up against these odds on the same basis as the operator of a candy store—who has his own problems, it is true, but not this kind of problem—would be taxed.

Abraham Lincoln used to be fond of quoting a riddle that went: "If you call a tail a leg—how many legs does a cow have?" The answer was "Four," because calling a tail a leg does not make it one.

And no matter how much the opponents of the present depletion law for oil and gas may pretend that there is really no practical difference between the business of wildcatting for oil and gas and the business of operating a barber-shop, there really are fundamental differences; and if our tax laws refuse to take those differences into due account, our tax laws will not make sense.

The opponents of percentage depletion seem to be saying, "We don't agree with this provision. We think it is dead

wrong. But we are not calling for its repeal. We just want to change it a little. We want to cut it down some, for oil and gas."

Suppose they succeeded in what they want. Suppose they were able to get even a few percentage points deducted from the rate of this provision as it applies to oil and gas. Is it not plain that such a change would be bound to affect the petroleum industry—already going through a period of distress.

The oil industry would be faced with a grim choice between two highly undesirable courses of action. One course would be to make substantial increases in the price of its products—which would be difficult in the present supply-demand situation. The other possible course would be for the oil industry to curtail drastically its drilling program for the present and for an indefinite future, depending on proved reserves already in the larder.

Such a decision, which would be the almost inevitable course if this amendment were adopted, would have drastic consequences for my State and for every one of the other 31 States with oil and gas production. Over the long haul, the Nation would be badly hurt; but the economies of these States would suffer the first punishing effects of this unwise and shortsighted decision. A few examples of what the oil industry now means to Wyoming will indicate how important this matter is to us.

The petroleum industry provides employment to some 12,000 residents of Wyoming, which means that 1 of every 8 members of the nonagricultural labor force earns his livelihood in the oil business.

The petroleum industry payroll in Wyoming runs around \$66,500,000 annually, which is important money for us, more than 8 percent of the total personal income of the State.

There is now oil or gas production in 21 of the 23 counties of my State, with nearly half of Wyoming's more than 62 million acres under lease for oil production or exploration. Much of this land is not productive now, but is in line for future testing to determine its potential—if any. It is estimated that there are some 28 million acres in this category—presently unproductive land, under lease for future exploration. The owners of this land are now hopeful; but enactment of this amendment would cruelly dash their hopes, because it would discourage the kind of high-risk ventures that alone can determine whether their land will become oil-producing property.

Wyoming now ranks fifth in oil production, but this does not mean that oil is easy or inexpensive to find there. For many years my State held the national record with a well, completed in 1949, that went down 20,521 feet—and turned out to be a worthless dry hole—which cost nearly \$1.5 million. This record stood until 1953, when it was supplanted by a California well—another dry hole—that went almost a thousand feet deeper. That record, in turn, has since been surpassed; and the current deepest well

titleholder is a 1958 Texas wildcat that went down 25,340 feet—and turned out to be another dry hole.

Taxes are not paid on a dry hole; that is true. But, the driller does not get back his money, either. A very great amount of money can be spent in drilling those holes, too—an average of \$900,000 per well for the deep ones in my State.

Last year, of the 391 wildcat wells drilled in Wyoming, 359 were dry holes. In Laramie County, Wyo., there was a 100-percent dry hole record—one wildcat well drilled, one dry hole resulting from it. But they had to go down more than 7,500 expensive feet before they knew the well was destined to be an unproductive dry hole.

To a man unfamiliar with the problems of oil and gas exploration, this dry-hole problem may seem very remote and academic. But out there in the oilfields it is not remote; it is a fact of life. And a simple fact of economics—not classroom economics, but real life economics—is that people will not invest their money in ventures of this sort unless they stand to get some tax consideration if they succeed in spite of the heavy odds against them. If they take the risks and the tax collectors walk off with all the gravy, they will not take those risks any more—and, I may add, there will not be so much gravy for the tax collector, or, in years to come, enough oil for the American people. The issue is as simple as that.

Since production started there 68 years ago, Wyoming has produced more than 2 billion barrels of crude oil. It still has more than 1½ billion barrels of proved crude reserves. We know that there is much more oil thousands of feet deep in the Wyoming earth, but people have to drill down there to find it, and that means taking big chances. How many people will have either the courage or the means to keep up the hunt if the already discouraging odds against success are further magnified by a slash in the depletion rate?

When Congress enacted this depletion law back in 1926, it was not meant to be any favor to oil producers or investors. It is not any favor to them now. It is a favor to the American people. It has enabled Americans to enjoy an abundance of the energy fuels that have given us the means to become the world's foremost industrial power, with unrivaled living standards and invincible military might.

Reducing the rate of percentage depletion would have the direct effect of discouraging the search for new oil reserves needed to meet future requirements, with the result that our energy resources would soon dwindle and progress would lag. This would be an undesirable development at any time. It could be suicidal when we are admittedly engaged in a desperate race with Russia, and should be intent upon building up our economy, rather than tearing it down—on increasing, rather than undercutting, our resources for defense.

Oratory does not alter facts; and the facts—not name calling or emotional responses—are what should influence us.

The present rate of percentage depletion for oil and gas has served this Nation very well, indeed. So have the rates of this provision applying to other minerals essential to our peacetime economy and national defense—uranium, iron ore, sulfur, copper, nickel, zinc, and lead for some examples. This is not the time to be stamped into action which would lead to later repentance and regrets—and recriminations, too. Any proposal that would impede our Nation's resource development and future productivity by reducing the depletion rate for oil or any other mineral deserves overwhelming rejection as contrary to the public interest.

I would like to commend the junior Senator from Oklahoma [Mr. MONRONEY], who, as a man who for some 24 years has represented one of the greatest oil States in the Union, has a deep understanding of the purposes and the need for the depletion allowance. In July of this year at an oil industrial conference held at Dallas, Tex., Senator MONRONEY gave to that group an outstanding address on the subject of the oil depletion allowance and the great need for its continuance.

The junior Senator from Oklahoma pointed out, as I have attempted to do here today, that in States where oil is not considered a vital ingredient of the economy, the basic reasons for the depletion allowance and the national interest in its continuation are practically unknown. In Senator MONRONEY's words:

To the uninformed, it (meaning depletion) has become a symbol of tax favoritism, rather than an instrument that has guaranteed an unfailing and unlimited petroleum supply in two World Wars and in the great industrial and population expansion that followed them.

I sincerely hope, Madam President, that the Members of this body, who have the responsibility to represent not only their individual States, but the national public interest, as well, will agree with me that the mineral depletion allowance is not only necessary but is absolutely essential to the economic well-being and security of the United States.

Mr. ROBERTSON. Madam President—

Mr. KERR. Madam President, I ask unanimous consent that 2 minutes be allowed for questions by the Senator from Virginia [Mr. ROBERTSON].

The PRESIDING OFFICER. Without objection, it is so ordered.

Mr. ROBERTSON. Madam President, before the final action on the bill is taken, I wish to raise a question in regard to entertainment expenses—namely, whether, in that connection, partnerships are to be treated on the same basis as corporations. Yesterday we discussed this matter generally, but this particular point was not covered in detail.

So I should like to ask the Senator from Oklahoma [Mr. KERR] this question: Is the exception to entertainment expense disallowances in section 4(a) of the act intended to apply to partnership business meetings—meetings of its employees or its partners, or both?

Mr. KERR. The exception in section 274(e)(6) is intended to include expenses incurred by a partnership which are directly related to business meetings of its employees, or its partners, or both. Partners are agents, and agents are specifically mentioned in the language of the bill.

Mr. ROBERTSON. I had assumed that the committee intended that meaning; but inasmuch as the language of the bill itself was not too clear, I am very glad to have this legislative history made in connection with this matter.

Mr. KERR. I thank the Senator from Virginia.

Mr. MONRONEY. Madam President, before I yield back the remainder of my time, may I ask how much time we have remaining.

The PRESIDING OFFICER. Four minutes.

Mr. MONRONEY. I yield that time to the distinguished Senator from Arkansas [Mr. FULBRIGHT].

The PRESIDING OFFICER. The Senator from Arkansas is recognized for 4 minutes.

Mr. FULBRIGHT. Madam President, I regret that this amendment is being offered again.

As the Senate knows, we had no adequate hearings on this proposal. Much that could be said about it cannot be developed here on the floor.

My State is not one of the major producers of oil; it produces only about 100,000 barrels a day. Thus, oil is not as important to Arkansas as it is to the major producing States, such as Oklahoma and Texas.

However, attention should be called to the greater difficulty in obtaining new sources of oil. Certainly, we should not forget the implications of such an amendment. When taken up on the floor, it is impossible to have due consideration given to the long-term ability of our country to supply its own oil needs in case of war or other disruption of the supply of oil.

We recall that not too long ago great difficulties were encountered in Europe, as a result of the closing of the Suez Canal.

We can imagine the revolutions which could easily develop and disrupt foreign supplies of petroleum. Very frequently we hear about the possibility of political upheaval in parts of Latin America from which we now import substantial amounts of oil. It would be very inappropriate and inadvisable, it seems to me, to reduce this depletion allowance under these circumstances, for, in effect, it would stop or would slow down to a very great extent the explorations for new supplies of oil in the United States and leave us totally dependent on foreign sources.

It is no news to this body or to the country that each year now, for a long time, it has become more and more difficult to find new supplies of oil. We are using oil much more rapidly than we are finding new reserves. The great reserves which have been discovered in recent years have not been on the North American continent, and certainly not in the United States. Primarily, they have

been in the Middle East and in North Africa. As a matter of national defense and national security, this matter is much too important to be passed upon rather casually on the floor of the Senate, without having careful consideration, in hearings before the committee, of all of the country's interests which are involved.

It will be said that hearings have been held on this matter in the past. That is true; but conditions have changed very rapidly in recent years, especially in the field of oil. Therefore, I think those hearings are obsolete and the record developed no longer useful.

We read daily that one of the principal weapons of the Russians, in their attempts at economic penetration of the free world, is their use of oil. Of course the production of oil under the circumstances which exist in the Soviet Union is quite different from its production in our country. The Russians can, in effect, use oil as a weapon, regardless of its cost, where as under our democratic, free-enterprise system these companies cannot replenish their supplies without the depletion allowance.

I do not wish to repeat what has already been said by the junior Senator from Oklahoma [Mr. MONRONEY] and other Senators in regard to the expense incurred by the oil industry in its efforts to explore for and to find new reserves. He has already pointed out that every year the industry has spent a great deal more than the depletion allowance on its search for oil.

Another vital consideration, it seems to me, is the stabilizing effect of the depletion allowance. I do not think it is the only reason, but it has certainly contributed to the fact that the price of oil today is virtually the same as it was nearly 40 years ago.

So, Madam President, for all these reasons, I hope the amendment will be rejected.

The PRESIDING OFFICER. The time yielded to the Senator from Arkansas has expired.

Mr. WILLIAMS of Delaware. Madam President, how much time remains available to me?

The PRESIDING OFFICER. Twenty-five minutes.

Mr. WILLIAMS of Delaware. I shall not need all of that time.

I merely wish to make a correction of the RECORD. It was said that the amendment has not received committee consideration. They are wrong. I call attention to the fact that the amendment was submitted in the normal manner as an amendment to the pending bill; and it was before the Finance Committee, of which I am a member; and testimony was taken, insofar as any member of the industry wished to be represented or to be heard and the amendment was offered in committee.

The amendment was offered in executive session in the committee; although the amendment was not approved as part of the bill, I wish to point that out to refute the argument that the amendment was not properly considered or that the industry did not have a proper chance to present its case.

It is argued—

Mr. LONG of Louisiana. Madam President, will the Senator from Delaware tell me whether the Secretary of the Treasury testified for it?

Mr. WILLIAMS of Delaware. No, he did not endorse it.

Mr. LONG of Louisiana. Did anyone testify for the amendment?

Mr. WILLIAMS of Delaware. Yes. Some were in favor of the amendment; some were opposed to it. The Senator is a member of the committee. I would not say that this proposal did not have just a little controversy; nevertheless, the argument that there was no opportunity for hearings on it cannot be supported.

The amendment does not propose to take away the oil depletion allowance in its entirety. I may say, in all fairness, I recognize that there is merit to the principle of depletion allowance. If this were a proposal to take away all the 27½-percent depletion allowance, I would not be in favor of it. On the other hand, there is nothing sacred about the 27½-percent figure. That rate percentage was fixed in 1926, when the corporate tax rate was less than 20 percent, and the top individual tax rate was around 15 percent. The effect of a 27½-percent depletion allowance is far different under those rates than when there is a ceiling of about 90 percent on individual tax rates and a 52-percent tax rate on corporations. The higher the tax rates go, the greater the significance of the 27½-percent depletion allowance.

Let me emphasize again that I am not offering the amendment as a reflection on the oil industry. There is no Member of the Senate who has greater respect for the oil industry than I do. I recognize it as one of the great industries of the country, and one which has made a great contribution. On the other hand, it is no more essential to our national welfare than are other industries. The oil industry would be of no use without the steel industry. Neither of those industries would be of any use without agriculture. One could name almost any industry without which we could not do. So to single out one industry and say America could not survive without it is not a valid argument. One could make make the same argument about many of the other industries.

To argue that the depletion allowance merely means that the man investing his capital is getting back his investment is not valid, because in addition to the depletion allowance, the oil industry gets the normal depreciation rates that all other industries get. In addition to the depreciation allowance, it receives this depletion allowance on gross sales, which has no connection with depreciation. In many cases, a member of the oil industry can recover his investment, not once, twice, or three times, but over and over again, up to as many as 90 or 100 times the original investment. There is no limit as to the number of times a member of the oil industry can recover his original investment. Depletion is not in the same category as depreciation.

I give the industry credit for providing many jobs, but so do other industries

in America provide jobs. My argument is that with the cost of defense amounting to \$50 billion a year, at a time when the total budget for running the Government is around \$90 billion, here is an industry which in my opinion is not paying its proportionate share for the costs of defending and running the Government. The \$50 billion defense effort is to protect property investment as well as the lives of the people of America. Here is an industry which represents a major part of the investment of America. Why should not it pay its proportionate part of the cost of Government, instead of having its tax rate frozen at a rate fixed in 1926.

Under this amendment we are trying to adjust this matter on a basis so the industry can pay its proportionate part of the cost of operating the Government.

I want to emphasize again that this is not punitive legislation, because I respect the oil industry as much as does any Member of this body. But I am not alone in saying that this industry is one which needs attention insofar as the tax laws are concerned. The question has been before the committee time and time again.

I wish now to read from the Democratic platform of 1960. I think it well that we refresh the memory of Members on the other side of the aisle. I find this in the Democratic platform on which President Kennedy was elected:

Third, we shall close the loopholes in the tax laws by which certain privileged groups legally escape their fair share of taxation.

Among the more conspicuous loopholes are depletion allowances which are inequitable.

This puts the whole Democratic Party on record.

Mr. MCGEE. Madam President, will the Senator yield?

Mr. WILLIAMS of Delaware. I will yield in just a minute. I would like to finish my remarks first, because I am on limited time, I have already yielded a substantial part of my time to the opponents. If I may complete my statement, I will yield.

I would like to cite another authority on the need for correction of the depletion allowance. I quote this time a former President of the United States, in a message which he sent to the Congress. This can be found in the permanent CONGRESSIONAL RECORD, volume 96, part I, pages 770 and 771, under date of January 23, 1950. It was a message sent by President Harry Truman, and I read from the President's message:

I know of no loophole in the tax laws so inequitable as the excessive depletion exemptions now enjoyed by oil and mining interests.

Under these exemptions, large percentages of the income from oil and mining properties escape taxation, year after year. Owners of mines and oil wells are permitted, after deducting all costs of doing business, to exclude from taxation on account of depletion as much as half of their net income. In the case of ordinary businesses, investment in physical assets is recovered tax free through depreciation deductions. When the original investment has been recovered, a depreciation deduction is no longer allowed under the tax laws. In the case of oil and mining businesses, however, the de-

pletion exemption goes on and on, year after year, even though the original investment in the property has already been recovered tax free, not once but many times over.

Originally introduced as a moderate measure to stimulate essential production in the First World War, this special treatment has been extended during later years. At the present time these exemptions, together with another preferential provision which permits oil-well investment costs to be immediately deducted from income regardless of source, are allowing individuals to build up vast fortunes, with little more than token contributions to tax revenues.

For example, during the 5 years, 1943-47, during which it was necessary to collect an income tax from people earning less than \$20 a week, one oil operator was able, because of these loopholes, to develop properties yielding nearly \$5 million in a single year without payment of any income tax. In addition to escaping the payment of tax on his large income from oil operations, he was also able through the use of his oil tax exemptions to escape payment of tax on most of his income from other sources. For the 5 years his income taxes totaled less than \$100,000, although his income from nonoil sources alone averaged almost \$1 million each year.

This is a shocking example of how present tax loopholes permit a few to gain enormous wealth without paying their fair share of taxes.

I am well aware that these tax privileges are sometimes defended on the grounds that they encourage the production of strategic minerals. It is true that we wish to encourage such production. But the tax boundaries distributed under present law bear only a haphazard relationship to our real need for proper incentives to encourage the exploration, development, and conservation of our mineral resources. A forward-looking resources program does not require that we give hundreds of millions of dollars annually in tax exemptions to a favored few at the expense of the many.

I have just read from President Truman's message as sent to the Congress under date of January 23, 1950.

This amendment before the Senate, in my opinion, is a very moderate approach, making a long overdue correction in our existing tax laws. Time and time again we have changed the rates at which other taxpayers have to pay taxes. I see nothing sacred about the 27½ percent depletion rate fixed for this particular industry.

I repeat again that this is not an effort to whittle the depletion allowance down to nothing. I recognize the equity in the principle of some depletion, but there is nothing sacred about a 27½ percent rate. I think the time is long overdue when this industry should pay its proper proportion of the operating costs of Government.

Mr. TOWER. Madam President, will the Senator yield me 2 or 3 minutes?

Mr. WILLIAMS of Delaware. Madam President, how much do I have left?

The PRESIDING OFFICER. The Senator from Delaware has 14 minutes remaining.

Mr. WILLIAMS of Delaware. I yield 3 minutes to the Senator from Texas.

Mr. TOWER. Madam President, the distinguished Senator from Delaware has quite properly pointed out that the oil industry should bear its share of the tax burden in supporting our gigantic national defense effort. It should be noted

that without the 27½-percent depletion allowance there would not be the incentive to produce the wealth which results from oil exploration and production. Actually, the 27½-percent depletion allowance, rather than denying to the Government a source of revenue, has stimulated the production of new sources of revenue. I would predict quite freely that if the 27½-percent depletion allowance were reduced substantially it would so discourage a sufficient number of people from engaging in this great and vital defense industry as to result in reducing sources of revenue to the extent that there would be a loss of revenue to the Government of the United States, to say nothing of the loss for many State and local governments throughout the United States.

This is not a tax loophole. It is not a subsidy. It is simply a tax allowance because of the fact that when a man sells a barrel of oil he is selling a capital asset. The average cost or production per barrel of \$2.40 is three times greater than the 76 cents allowed under the depletion allowance per barrel.

Mr. KUCHEL. Madam President, will the Senator yield for a question?

Mr. WILLIAMS of Delaware. I yield to the Senator from California.

Mr. KUCHEL. Will the Senator tell his colleagues the rationale behind that part of the amendment which has to do with reducing the highest surtax rates?

Mr. WILLIAMS of Delaware. Yes. One of the arguments made in connection with the depletion allowance—and it is a very valid argument—is that under present rates, since the Government takes as much as 91 percent of a man's income, with an overall limitation of 87 percent, a man who is already in that tax bracket would not put out his money on a gamble wherein he can keep only 13 percent. Therefore as we reduce the depletion rate we propose to lower the individual rates.

There is a gamble involved in the oil-producing business. I recognize that. A man in the 87-percent tax bracket would not gamble, if he could keep only 13 percent of that which he made. If we reduce the depletion allowance without some correction in other rates, we would hinder the exploration for oil.

That is the reason I have coupled the two proposals together. Let us reduce the depletion allowance and also reduce the overall income tax rates.

If a man could keep 40 percent of that which he made, it would pay him to take the risk. In addition, he would have the remaining 20-percent depletion allowance.

At the same time the Government would pick up an additional \$120 million of revenue, at a time the money is needed. I do not think all of the money should be passed on.

Mr. KUCHEL. Has my colleague, by his amendment, restricted the reduction of surtax rates to the 87-percent rate alone?

Mr. WILLIAMS of Delaware. That is the only way to approach the problem.

Mr. KUCHEL. What happens with respect to the rates now existing in the

tax law, lower than 87 percent? Would they remain the same?

Mr. WILLIAMS of Delaware. They would remain the same, down to 60 percent.

Mr. KUCHEL. They would remain the same, down to 60 percent?

Mr. WILLIAMS of Delaware. Yes.

Mr. KUCHEL. What would happen to those surtax rates under 60 percent, as presently written in the tax law?

Mr. WILLIAMS of Delaware. Nothing.

Mr. KUCHEL. That is all.

Mr. WILLIAMS of Delaware. There was a suggestion made that instead of applying it all to the rates over 60 percent, we should raise the personal exemption from \$1,200 to \$1,500 on those over 65. I should be glad to consider offering the amendment in such a way, if the Senator would support it.

Mr. KUCHEL. I shall have the honor to study anything my able friend from Delaware may bring forth. The only way I know how to participate in the legislative process is on the basis of what is pending and to deal with it, up or down. On that basis, I have the honor to disagree with my friend.

Mr. WILLIAMS of Delaware. I understand. I appreciate the position of my good friend from California.

I think this is a good way to approach the problem.

Madam President, I am ready to yield back the remainder of my time.

Mr. MANSFIELD. Madam President, I move to lay on the table the amendment offered by the Senator from Delaware.

Mr. WILLIAMS of Delaware. Madam President, I ask for the yeas and nays.

The yeas and nays were ordered.

The PRESIDING OFFICER. The question is on agreeing to the motion by the Senator from Montana [Mr. MANSFIELD] to lay on the table the amendment offered by the Senator from Delaware [Mr. WILLIAMS], for himself and other Senators. On this question the yeas and nays have been ordered, and the clerk will call the roll.

The legislative clerk proceeded to call the roll.

Mr. ERVIN (when his name was called). Madam President, on this vote I have a live pair with the senior Senator from Mississippi [Mr. EASTLAND]. If he were present and voting, he would vote "yea." If I were at liberty to vote, I would vote "nay." I therefore withhold my vote.

Mr. SALTONSTALL (when his name was called). Madam President, on this vote I have a pair with the senior Senator from Washington [Mr. MAGNUSON]. If he were present and voting, he would vote "nay." If I were at liberty to vote, I would vote "yea." I therefore withhold my vote.

The rolloall was concluded.

Mr. HUMPHREY. I announce that the Senator from Mississippi [Mr. EASTLAND] and the Senator from Washington [Mr. MAGNUSON] are absent on official business.

I further announce that the Senator from New Mexico [Mr. ANDERSON], the Senator from Nevada [Mr. BIBLE], the Senator from Wyoming [Mr. HICKEY],

and the Senator from Missouri [Mr. SYMINGTON] are necessarily absent.

I further announce that if present and voting, the Senator from New Mexico [Mr. ANDERSON], the Senator from Nevada [Mr. BIBLE], and the Senator from Wyoming [Mr. HICKEY] would each vote "yea."

Mr. KUCHEL. I announce that the Senator from Utah [Mr. BENNETT], the Senator from South Dakota [Mr. BOTTUM], the Senator from Arizona [Mr. GOLDWATER], the Senator from Kentucky [Mr. MORTON], and the Senator from New Hampshire [Mr. MURPHY] are necessarily absent.

If present and voting, the Senator from Utah [Mr. BENNETT], the Senator from South Dakota [Mr. BOTTUM], the Senator from Arizona [Mr. GOLDWATER], the Senator from Kentucky [Mr. MORTON], and the Senator from New Hampshire [Mr. MURPHY] would each vote "yea."

The result was announced—yeas 57, nays 30, as follows:

[No. 244 Leg.]

YEAS—57

Allott	Fulbright	McGee
Bartlett	Gruening	Metcalf
Beall	Hartke	Miller
Burdick	Hayden	Monroney
Bush	Hickenlooper	Moss
Butler	Hill	Mundt
Byrd, W. Va.	Holland	Pearson
Cannon	Hruska	Randolph
Capehart	Johnston	Robertson
Carlson	Jordan, N.C.	Russell
Chavez	Jordan, Idaho	Smathers
Cooper	Kerr	Sparkman
Cotton	Kuchel	Stennis
Curtis	Long, Mo.	Talmadge
Dirksen	Long, Hawaii	Thurmond
Dodd	Long, La.	Tower
Ellender	Mansfield	Williams, N.J.
Engle	McCarthy	Yarborough
Fong	McClellan	Young, N. Dak.

NAYS—30

Aiken	Humphrey	Pastore
Boggs	Jackson	Pell
Byrd, Va.	Javits	Prouty
Carroll	Keating	Proxmire
Case	Kefauver	Scott
Church	Lausche	Smith, Mass.
Clark	McNamara	Smith, Maine
Douglas	Morse	Wiley
Gore	Muskie	Williams, Del.
Hart	Neuberger	Young, Ohio

NOT VOTING—13

Anderson	Ervin	Murphy
Bennett	Goldwater	Saltonstall
Bible	Hickey	Symington
Bottum	Magnuson	
Eastland	Morton	

So Mr. MANSFIELD's motion to lay on the table the amendment offered by Mr. WILLIAMS of Delaware was agreed to.

Mr. KERR. Madam President, I move that the action of the Senate whereby the amendment was tabled be reconsidered.

Mr. LONG of Louisiana. Madam President, I move to lay that motion on the table.

The motion to lay on the table was agreed to.

Mr. KERR. Madam President, one of the provisions on which the Committee on Finance worked the longest and the hardest has to do with the taxation of foreign corporations, domestically owned or controlled. I wish to make a few comments as legislative history to augment the language in the committee report in making the intent of the committee clear.

There has been some comment as to

the workings of the minimum distribution escape valve to section 12 when an election is made on a consolidated basis. The report of your committee on pages 271 and 272 contains two examples—examples 1 and 2—to show how foreign tax credits may have to be allocated on a consolidated basis when only a minimum distribution is made and it is not made pro rata from the foreign subsidiaries being consolidated.

I have discussed this matter with the Treasury Department and they agree with me that it would be desirable to provide some further illustrations and examples of how the minimum distribution escape valve is intended to operate on a consolidated basis. Example 3 below demonstrates that for purposes of computing the available foreign tax credit, a domestic corporation electing the minimum distribution section on a consolidated basis utilizes the regular rules for computing foreign tax credit, with no allocations of its credits, provided that its actual distribution is such that the combined U.S. and foreign taxes which result, produce an overall effective rate which is equal to, or above, the overall effective rate that would be produced if the taxpayer had received a minimum distribution pro rata from all of the foreign subsidiaries included in the consolidation. If no minimum distribution is required because the effective foreign rate is 47 percent or higher, then the normal tax credit rules remain applicable with no allocation of credits.

Where the actual distribution does not result in an overall effective rate equal to or above the overall effective rate that would have been produced by such a pro rata minimum distribution from all of the foreign subsidiaries included in the consolidation, then the domestic taxpayer still continues to use his regular rules for computation of foreign tax credit, except that a portion of the foreign tax credits will here be required to be allocated on a consolidated basis. The allocation that is required is only to the extent needed to bring the overall rate of United States and foreign taxes up to the rate that would have been produced by a minimum distribution on a pro rata basis. See examples 1 and 2 in committee report and example 4 below.

The method of computation when a branch is involved and an election has been made to treat the branch as a foreign subsidiary is provided by example 5 below. This example shows that the taxable income of the branch is utilized in determining the foreign effective rate of taxation. Further, when the branch is entitled to deductions, like that provided Western Hemisphere trade corporations, this is reflected by a reduction from taxable income.

Thus, what the examples in the committee report and the further examples attached to this statement show is that the authority given the Secretary of the Treasury or his delegate in section 963(f) to prescribe regulations for the determination of the amount of foreign tax credit is to allocate the normal available foreign tax credit so as to produce an overall effective rate of taxation equal

to the overall effective rate that would be produced by a pro rata minimum distribution pattern. If the taxpayer chooses some other pattern for distribution, no allocation will be made as long as the overall effective rate, utilizing regular rules for computation of foreign tax credit, equals or exceeds what would have been produced by a pro rata minimum distribution.

I think that with these illustrations the comments that have been made will have been satisfactorily answered. My belief continues as strongly as ever that the minimum distributions escape valve is an effective and valuable device.

EXAMPLE 3

Assume domestic corporation M owns 100 percent of the stock of controlled foreign corporations A and B. All the corporations use the calendar year as the taxable year. In 1963, corporation A had earnings and profits of \$62 after payment of foreign income tax of \$38—a 38-percent rate. Corporation B, for taxable year 1963, had earnings and profits of \$18 after payment of foreign income tax of \$2—a 10-percent rate. The consolidated effective foreign tax rate of corporations A and B was $33\frac{1}{3}$ percent—total tax paid divided by consolidated earnings and profits before deduction of foreign taxes—

$$\frac{38+2}{100+20}$$

The required minimum distribution under section 963 was therefore \$48—60 percent of the consolidated earnings and profits after taxes—60 percent of \$80. An election is made to consolidate A and B for purposes of section 963. Assume the application of "gross up" provisions. Assume no withholding taxes are imposed on distributions.

If corporations A and B had each made a distribution to corporation M equal to 60 percent—the required minimum distribution percentage—of their earnings and profits after taxes, the resulting overall effective United States and foreign tax rate on the earnings and profits of A and B for the year 1963 would be 44.5 percent computed as follows:

	A	B	Total
Amount includible in gross income as a dividend.....	\$37.20	\$10.80	\$48.00
Amount includible in gross income under sec. 78.....	22.80	1.20	24.00
Total amount included in gross income.....	60.00	12.00	72.00
Tentative U.S. tax (at 52-percent rate).....	31.20	6.24	37.44
Foreign tax credit.....	22.80	1.20	24.00
Net U.S. tax.....	8.40	5.04	13.44

The combined foreign and U.S. taxes would equal \$53.44—\$40 plus \$13.44. The resulting overall effective rate would thus be 44.5 percent—\$53.44/\$120.

Assume that in fact the actual distributions from A and B and the resulting U.S. tax liabilities and overall effective tax rate are as follows:

	A	B	Total
Amount included in gross income as a dividend.....	\$55.80	\$7.20	\$63.00
Amount included in gross income under sec. 78.....	34.20	.80	35.00
Total amount included in gross income.....	90.00	8.00	98.00
Tentative U.S. tax (at 52-percent rate).....	46.80	4.16	50.96
Foreign tax credit.....	34.20	.80	35.00
Net U.S. tax.....	12.60	3.36	15.96

The combined U.S. and foreign taxes equal \$55.96—\$40 plus \$15.96. This amount exceeds the \$53.44 total tax which would have resulted had a pro rata minimum distribution been made from each corporation, and the resulting combined effective rate of 46.6 percent exceeds the 44.5 percent that would have been produced by a pro rata minimum distribution. The regular foreign tax credit computations remain applicable and no allocation is to be made.

EXAMPLE 4

Assume the facts are the same as in example 3, except that the actual distributions from A and B and the resulting U.S. tax liabilities and overall effective tax rate are as follows:

	A	B	Total
Amount included in gross income as a dividend.....	\$49.60	0	\$49.60
Amount included in gross income under sec. 78.....	30.40	0	30.40
Total amount included in gross income.....	80.00	0	80.00
Tentative U.S. tax (at 52-percent rate).....	41.60	0	41.60
Foreign tax credit.....	30.40	0	30.40
Net U.S. tax.....	11.20	0	11.20

The combined U.S. and foreign taxes equal \$51.20—\$40 plus \$11.20. Since this amount is less than the \$53.44 total tax which would have resulted had a pro rata minimum distribution been made from each corporation, the resulting combined effective rate, 42.7 percent, is less than 44.5 percent. Therefore, the regulations will require that a sufficient amount of the \$30.40 foreign tax credit, namely \$2.24, must be reallocated on a consolidated basis so that the resulting U.S. tax will equal \$13.44. The combined U.S. and foreign tax would then equal \$53.44, resulting in a combined effective rate of 44.5 percent.

EXAMPLE 5

Assume domestic corporation X, with a foreign branch, wholly owns controlled foreign corporation Y. The foreign branch of X has taxable income of \$100 before payment of foreign taxes of \$38. Y has earnings and profits of \$18 after payment of foreign taxes of \$2. Both corporations use the calendar year as their taxable year. Y distributes \$8 to X. Elections are made to treat the foreign branch of X as a controlled foreign corporation and to consolidate Y with the branch for purposes of section 963.

If only 60 percent—the required minimum distribution percentage—of corporation X's branch income is taken into account and assuming that corporation Y made a distribution to corporation X equal to 60 percent of Y's earnings and profits after taxes, the resulting overall effective U.S. and foreign tax rate on the combined foreign profits of X and Y for the year 1963 would be 44.5 percent computed as follows:

	X	Y	Total
60 percent of branch income.....	\$60	-----	\$60.00
Amount included in gross income of X as a dividend.....	-----	\$10.80	10.80
Amount included in gross income of X under sec. 78.....	-----	1.20	1.20
Total amount included in gross income of X (\$60+\$10.80+\$1.20).....	-----	-----	72.00
Tentative U.S. tax.....	-----	-----	37.44
Foreign tax credit (60 percent of \$38+\$1.20).....	-----	-----	24.00
Net U.S. tax.....	-----	-----	13.44

The combined foreign and U.S. taxes equal \$53.44—\$40 plus \$13.44. The resulting overall effective rate is thus 44.5 percent—\$53.44/\$120.

In fact under section 963, X is considered to have distributed 100 percent of its branch income. Assume that corporation Y distributes a dividend of \$7.20 to X. Under this assumption the resulting U.S. tax liabilities and overall effective tax rate are as follows:

	X	Y	Total
Amount of branch income included in gross income.....	\$100	-----	\$100.00
Amount included in gross income as a dividend.....	-----	\$7.20	7.20
Amount included in gross income under sec. 78.....	-----	.80	.80
Total amount included in gross income.....	-----	-----	108.00
Tentative U.S. tax at 52-percent tax rate.....	-----	-----	56.16
Foreign tax credit (\$38 plus \$0.80).....	-----	-----	38.80
Net U.S. tax.....	-----	-----	17.36

The combined U.S. and foreign taxes thus equal \$57.36—\$40 plus \$17.36. The amount exceeds the \$53.44 total which would have resulted had only 60 percent of the income of X and Y been taken into account and the resulting combined effective rate of 47.8 percent thus exceeds 44.5 percent, which would have resulted had only 60 percent of the incomes been taken into account. The regular foreign tax credit computations remain applicable and no allocation is to be made.

Mr. CARLSON. Madam President, will the Senator yield?

Mr. KERR. I yield.

Mr. CARLSON. I inquire if the Senator from Oklahoma, in reading the clarification or interpretation of sections in the bill, referred to section 963.

Mr. KERR. The Senator is correct.

Mr. CARLSON. As the distinguished Senator from Oklahoma knows, I have

prepared and have at the desk two amendments, one of them identified as "8-30-62-F," and one shown as "8-30-62-E," dealing with some proposed amendments to section 963.

I should like to ask the Senator if he believes that the statement he made would generally take care of the situations I had in mind in the amendments that I had intended to propose.

Mr. KERR. I say, generally, to the distinguished Senator from Kansas, that as I understand his amendment "8-30-62-F," the illustrations that I have given do, in my opinion, take care of what he had in mind in that regard. They go as far as the language of the bill would permit, and implement the language in connection with the Senator's other amendment.

Mr. CARLSON. In view of the statement of the Senator from Oklahoma, I shall not offer these amendments.

Mr. KERR. I thank the Senator from Kansas.

Mr. CANNON. Madam President, I call up my amendment designated "8-27-62." I ask that the amendment not be read but that it be printed in the RECORD.

The PRESIDING OFFICER. Without objection, the amendment will be printed in the RECORD.

The amendment is as follows:

On page 391, between lines 21 and 22, insert the following new section:

"SEC. 27. ALLOWANCE TO TAXPAYER OF ADDITIONAL EXEMPTION WITH RESPECT TO DEPENDENT CHILD WHO IS STUDENT ABOVE SECONDARY LEVEL AT EDUCATIONAL INSTITUTION.

"(a) IN GENERAL.—Section 151 of the Internal Revenue Code of 1954 (relating to deductions for personal exemptions) is amended by adding at the end thereof the following new subsection:

"(f) ADDITIONAL EXEMPTION FOR DEPENDENT CHILDREN ATTENDING SCHOOL ABOVE THE SECONDARY LEVEL.—

"(1) IN GENERAL.—An additional exemption of \$600 for each child of the taxpayer—

"(A) for whom the taxpayer is entitled to an exemption under subsection (e)(1) for the taxable year;

"(B) who has not attained the age of 23 at the close of the calendar year in which the taxable year of the taxpayer begins; and

"(C) who, during at least 4 calendar months during the calendar year in which the taxable year of the taxpayer begins, is a full-time student above the secondary level at an educational institution.

"(2) DEFINITIONS.—For purposes of paragraph (1)—

"(A) CHILD.—The term 'child' means an individual who (within the meaning of section 152) is a son, stepson, daughter, or stepdaughter of the taxpayer.

"(B) EDUCATIONAL INSTITUTION.—The term 'educational institution' has the meaning assigned to it by subsection (e)(4).

"(b) TECHNICAL AMENDMENT.—Section 213(c) of the Internal Revenue Code of 1954 (relating to maximum limitations on deductions for medical, dental, etc., expenses) is amended by striking out 'subsection (c)' or '(d), relating to the additional exemptions for age or blindness' and inserting in lieu thereof 'subsection (c), (d), or (f), relating to certain additional exemptions'.

"(c) CONFORMING AMENDMENT.—Section 3402(f)(1) of the Internal Revenue Code of 1954 (relating to withholding exemptions) is amended—

"(1) by striking out 'and' at the end of subparagraph (D);

"(2) by striking out the period at the end of subparagraph (E) and inserting in lieu thereof '; and'; and

"(3) by adding after subparagraph (E) the following new subparagraph:

"(F) one additional exemption for each child with respect to whom, on the basis of facts existing at the beginning of such day, there may reasonably be expected to be allowable an exemption under section 151(f) (relating to dependent children attending school above the secondary level) for the taxable year under subtitle A in respect of which amounts deducted and withheld under this chapter in the calendar year in which such day falls are allowed as a credit."

"(d) EFFECTIVE DATE.—The amendments made by this section, other than the amendments made by subsection (c), shall apply to taxable years beginning after December 31, 1961. The amendments made by subsection (c) shall apply with respect to wages paid on or after the first day of the first month which begins more than 10 days after the date of the enactment of this Act."

On page 391, line 22, strike out "27" and insert in lieu thereof "28".

Mr. CANNON. Madam President, I ask unanimous consent that the following Senators may be added as cosponsors of the amendment: the Senator from South Carolina [Mr. JOHNSTON], the Senator from Florida [Mr. SMATHERS], the Senator from Indiana [Mr. HARTKE], the senior Senator from West Virginia [Mr. RANDOLPH], the junior Senator from West Virginia [Mr. BYRD], the Senator from Colorado [Mr. ALLOTT], and the Senator from Ohio [Mr. YOUNG], because each of these Senators is himself a sponsor of a bill similar in legislative intent to my amendment. Each has recognized the challenge facing this Nation and the importance of an accelerated program for advanced education in order to meet that challenge.

The PRESIDING OFFICER. Without objection, it is so ordered.

Mr. SCOTT. Madam President, will the Senator from Nevada yield?

Mr. CANNON. I yield.

Mr. SCOTT. I ask that my name also be added as a cosponsor of the amendment. I strongly urge its adoption.

Mr. SMATHERS. Madam President, will the Senator from Nevada yield?

Mr. CANNON. I yield.

Mr. SMATHERS. I thank the Senator from Nevada for having included me as a cosponsor of the amendment. I have had an amendment similar to this one pending in the Finance Committee since January 1961. I cannot help feeling that this is a better way in which to educate the young people of America, or to make it possible for their parents to educate them, rather than to talk about loan or grant programs or other proposals of that type, although I am in favor of loan programs. However, I did not see fit to press my amendment at this particular time in light of the fact that the able Senator from Nevada had ventured forth with his amendment. I still believe that my amendment which also includes an exemption for students who work their way through school as well as individuals in the position of foster parents, is a worthwhile amendment.

I am delighted to know that progress appears to be made in the direction of having the administration look with kindness upon an approach to provide a tax deduction for parents in an amount up to \$600 of the cost of sending each child to a college or university. Parents today have a heavy burden due to the high cost of tuition in sending their children to schools of higher learning. Many of them find it an impossible task and as a result the children are deprived of furthering their education. The loser in the end is the child and the Nation. I congratulate the able Senator from Nevada upon his leadership in this direction. I am happy to join with him in his amendment. With administration help I sincerely trust we will achieve success in the next session of the Congress.

Mr. CANNON. I thank the Senator from Florida for his remarks.

Madam President, I ask unanimous consent that the distinguished junior Senator from Texas [Mr. TOWER] and the distinguished Senator from Rhode Island [Mr. PASTORE] also be added as cosponsors of the amendment.

The PRESIDING OFFICER. Without objection, it is so ordered.

Mr. CANNON. Madam President, many of the Senators whose names have been added at their request as cosponsors of the amendment are themselves the sponsors of bills having a similar legislative intent, each of them recognizing the challenge which faces the Nation and the importance of an accelerated program for advanced education in order to meet that challenge.

On Tuesday, I spoke at length on the floor of the Senate pointing out the urgent need in the Nation for an accelerated program to train additional needed personnel for scientific manpower utilization.

In addition, I have consistently supported programs to provide aid to education at every level. My amendment is intended to make possible the achievement of some of those goals about which I spoke on Tuesday, and for which I have voted with consistency. It would provide an additional tax exemption to the parent of any child under 23 who is a full-time student above the secondary level at an educational institution.

As of October 1961, approximately 2,900,000 students under the age of 23 were attending universities in this country. In a study by the University of Michigan, it was determined that the average annual cost per student was \$1,550. Of this amount, the student had earned and saved \$360; \$130 was provided by scholarships; \$950 came from parents; and \$110 from other sources. The study also showed that 4 in 10 found financing to be extremely difficult, while 2 in 10 found that the financial assistance which they were able to obtain was inadequate.

I believe that all children desire an opportunity to compete as adults on an equal basis with their fellows. I believe that every parent desires to give his child that opportunity. Yet, many of our youth are being denied the right to com-

pete due to a lack of advanced training. A study financed by the Ford Foundation and conducted by Elmo Roper & Associates revealed that 60 percent of the Nation's parents had no savings; and of those who did only an average of \$150 was set aside for college expenses. My amendment would assist in meeting the expenses and thus provide an added avenue and an added incentive for the Nation's youth in the pursuit of higher education. Many additional figures would be presented to show that there is a rather desperate financial justification for this amendment.

Perhaps more important, however, in terms of the Nation's continued progress and security is the benefit which would accrue by making possible the full academic development of our Nation's youth.

Madam President, in the past there has been difficulty in getting from the Treasury Department a statement of its position on such a proposal, because of the cost of this type of legislation. Only today I received from the Secretary of the Treasury a letter which, to me, points up the recognition by the Treasury Department of the need for some type of approach to this problem. I shall ask unanimous consent that the entire letter be printed in the RECORD, but first I wish to emphasize the concluding paragraph of the letter, from Secretary Dillon, which reads, as follows:

In the light of the overall revenue aspects of the pending bill, which on our figures shows a gross loss on a full year basis of \$210 million, the addition of a further \$400 million loss is obviously quite serious. I feel strongly therefore that the amendment should be deferred until next year. This will permit the administration to conduct a full and thorough study of the various approaches to financing higher education. We plan to submit to the Congress early next year a recommended solution to the problem.

Madam President, I ask unanimous consent that the entire letter be printed at this point in my remarks.

There being no objection, the letter was ordered to be printed in the RECORD, as follows:

THE SECRETARY OF THE TREASURY,
Washington, D.C., September 5, 1962.
HON. HOWARD W. CANNON,
U.S. Senate,
Washington, D.C.

DEAR SENATOR CANNON: I am writing to you in regard to the amendment you have proposed to H.R. 10650 to grant taxpayers an extra \$600 dependency deduction for each dependent child under the age of 23 who is a full-time student above the secondary level.

The problem of financing the higher education of students, with which your amendment is concerned, is of course an important one. The President has expressed concern over the number of qualified high school graduates who are unable to attend college because of financial reasons and has proposed a program of scholarships and loans to supplement the private and public scholarship and loan programs now in effect. Other approaches seek to provide financial assistance for higher education by granting various tax concessions. All these approaches merit serious study. A solution to the basic problem of financing the higher education of able students must be found. The administration is pursuing this matter vigorously in order to reach a fair and effective solution.

However, I do not believe that it would be desirable to attempt to deal with such a vital issue as financing higher education by means of an amendment to the 1962 revenue bill. This is particularly true in view of the fact that the proposed amendment to grant taxpayers extra dependency deductions for college students would involve an estimated annual revenue loss of at least \$400 million. This estimate is based upon the following considerations. Approximately 3 million of the more than 3½ million students enrolled in institutions of higher education are estimated to be eligible for the extra dependency allowance. At \$600 per eligible student, and allowing for the fact that some parents of college students do not report taxable income sufficient to absorb the extra deduction, this means a reduction in the individual income tax base of \$1.75 billion.

In 1960 the average tax rate paid on taxable income was 23 percent. Twenty-three percent of \$1.75 billion is approximately \$400 million. This is undoubtedly a conservative estimate because it is to be expected that the income of taxpayers who have children in college are higher than that reported on the average taxable income tax return, and because the extra deduction would reduce income subject to the highest marginal, not the average, bracket rate paid by each affected taxpayer.

In the light of the overall revenue aspects of the pending bill, which on our figures shows a gross loss on a full-year basis of \$210 million, the addition of a further \$400 million loss is obviously quite serious. I feel strongly therefore that the amendment should be deferred until next year. This will permit the administration to conduct a full and thorough study of the various approaches to financing higher education. We plan to submit to the Congress early next year a recommended solution to the problem.

Sincerely yours,

DOUGLAS DILLON.

Mr. CANNON. Madam President, I am happy to state that the Treasury Department now recognizes the seriousness of the problem and proposes to submit to Congress early next year, so that Congress may consider the enactment of legislation in this area, a recommended solution of this very serious problem which confronts approximately 2,900,000 students who are attending school.

It is my understanding that the Secretary of the Treasury believes that if the amendment were adopted at this time, there would be grave doubt, because of the deficit which will be created, whether the bill could be recommended for final approval.

I shall defer to the distinguished manager of the bill for his comments.

Mr. KERR. Madam President, I express deep appreciation to the distinguished Senator from Nevada, first, for the amendment he has discussed; and second, for what I believe to be the constructive approach he has shown.

The proposal has been discussed with officials of the Treasury. It was their opinion that, worthy as the amendment is, if it were added to the bill it would create a deficit which would make the bill very unattractive and possibly warrant failure of its approval.

The principle of the Senator's amendment is highly commendatory. I am glad he has brought it up. I am glad he has secured a commitment from the administration that it is a subject with reference to which the administration

will make an appropriate recommendation for its adequate solution early next year.

The Senator from Nevada has made a distinct contribution by bringing forward a proposal which is of deep interest to the American people, one which will be contributory to a wider spread of educational achievement by the youth of our country. I thank him genuinely for the manner in which he has handled the situation.

Mr. CANNON. I thank the Senator from Oklahoma.

Mr. RANDOLPH. Mr. President, will the Senator from Nevada yield?

The PRESIDING OFFICER (Mr. BURDICK in the chair). Does the Senator yield?

Mr. CANNON. I yield.

Mr. RANDOLPH. I commend the Senator from Nevada for his initiative and industry in presenting for the information of the Members of this forum the considered and valid reasons for the adoption of the amendment. I, too, have introduced proposed legislation relating to this problem. It was presented in January 1961, for myself and my colleague from West Virginia [Mr. BYRD]. I felt then, in presenting S. 391, as I feel now, that there is compelling argument for providing this exemption, this additional \$600 benefit for the taxpayer in consideration of helping to offset spiraling education costs at the institutions of collegiate training.

This school year the cost for education at the college and university level for approximately 4,600,000 young men and young women will total \$9,500 million. Only 5 years ago that cost would have been \$4,200 million for only 3 million of our young people—which indicates that the seriousness of this problem comes with the impact of the greater number of our youth enrolled. It is during this period of special impact on the parents that very careful attention must be given the imperative need for this added exemption.

I have in my files letters from fathers who struggle with the costs which accrue to them when they have two or three children in college. One of these citizens sets down the problem in these words:

I have no objection to paying our Federal income taxes, as I realize that our Government must have money for the multitude of purposes set forth in our budget. I consider it a privilege to pay my small share in helping to keep our country great and good.

However, within the past 2 years, two of my children have been fortunate enough to enter West Virginia institutions of higher education, and I have, under our American way of life, been fortunate enough to have the needed income to pay all of their expenses. For the school year of 1960-61, it will cost me approximately \$4,000, or \$2,000 per student, to keep these two in college. At the same time, under our income tax laws I am allowed an exemption of only \$600 per student or a total of \$1,200. Within the next 3 years, if providence permits, I shall have a third child in college, and my average cost for the three will be \$6,000 per year, and my total exemption will be \$1,800.

I firmly believe that higher education affords one of the best ways of providing better American leadership, and I have always strongly urged every American father to attempt to provide his children with college educations. If this recommendation is fol-

lowed, I believe that America would become a better country in which to live, and that we will thereby make certain that America will always remain the greatest leader among world powers.

Accordingly, I urge that legislation be enacted to increase the personal exemption under our income tax laws to at least \$1,200 for each child that the taxpayer wholly provides with a college education.

I ask unanimous consent to have printed at this point in the RECORD, in connection with my remarks, an article, "College Costs Will Hit Record," published today in the Washington Daily News. It indicates the heavy and increasing expense to the parents of the Nation, because of the mounting cost of the education of their children.

There being no objection, the article was ordered to be printed in the RECORD, as follows:

COLLEGE COSTS WILL HIT RECORD

(By Robert Dietsch)

It will cost American parents almost \$9.5 billion to send 4.6 million offspring to college this year.

Both figures are records.

Five years ago, parents paid about \$4.2 billion to send 3 million youngsters to college. And because spending more than doubled in the period while the number of students increased only 53 percent, it should be no great surprise that:

Since 1957, spending for higher education has gone up faster than spending on any other item in the consumer's budget.

ESTIMATE

The U.S. Office of Education has estimated 2¼ million students will enroll at public-supported colleges and universities this month and 1.84 million at private institutions. In 1950, the total was 2.7 million and in 1957 about 3 million.

Basic charges at the public schools (tuition and fees) have gone up from an average \$155 in 1958 to \$190 today. At private colleges the charges have zoomed from \$526 to \$740.

The differences in the figures indicate why 60 percent of today's college students enroll at public schools and only 40 percent at the private ones.

Five years ago, total costs (tuition, fees, books, room, board, clothes, transportation) were \$1,500 at a public-supported college and \$2,000 at a private school. Educators now put those averages at a minimum of \$1,700 and \$2,500.

Which would bring total outlays at public institutions up to \$4.6 billion and at private institutions up to \$4.7 billion.

In the last 5 years, disposable income of all Americans rose 24 percent (from \$293 billion to current rate of \$382 billion). But spending on higher education more than doubled.

It leads any list showing how consumer spending has increased.

Second on such a list compiled by the investment firm of David L. Babson & Co. is expenditures in stocks and bonds (up 90 percent from 1956 to 1962) and third is private school expenditures, up 85 percent.

Spending on books and maps, which might be related to education, ranked fifth—up 72 percent and only slightly behind the 75 percent spending increase on air travel.

REFLECTS BOOM

In fact, the Babson list reflects the American boom for comforts, conveniences, luxuries, entertainment, and culture. The only durable goods products on the big spending list were eyeglasses, braces, artificial limbs, boats, planes, radios, TV sets, records,

and musical instruments—and all of these are connected with leisure, recreation, or health.

Behind spending increases for books and maps were increased outlays for transportation tolls (up 65 percent), private hospitals (60 percent), barbers and beauticians (56 percent), participant sports, life insurance expenses, and radio and TV repair (all 55 percent) and bank service charges and toilet articles (both 54 percent).

Mr. RANDOLPH. Mr. President, I repeat that if this issue is delayed today, it must be met in the coming Congress.

Mr. CANNON. Mr. President, I thank the distinguished Senator from West Virginia for his remarks.

Mr. SCOTT. Mr. President, I support the amendment offered by the distinguished junior Senator from Nevada [Mr. CANNON].

On January 20, 1959, I introduced proposed legislation which would have increased the amendment on personal income tax exemption allowed a taxpayer for a dependent from \$600 to \$1,000 for any taxable year in which such dependent was a student attending school at the college level or above.

It has long been my feeling that the welfare and the future of our country is closely and intimately tied to the educational accomplishments of our young people. The mental resources and technical skills of our young people have to be developed so that the vast knowledge and mastery of complex scientific principles so vital to the national defense are within their grasp. The full resources for strengthening our national defense are not being utilized because many of our young people, due to the financial limitations of their parents, are unable to continue their educational studies above the secondary school level.

There are programs, both private and Government, which have aided the top qualified students desiring to continue their education beyond high school, but I feel that an additional exemption of \$600 to a taxpayer who has a dependent attending a school of higher education on a full-time basis would greatly increase the educational and technical potential of this country for the future, and would ease the heavy burden on parents in sending their children to college. Thousands of our young people of ability either do not enter college or have to drop out before graduation for financial reasons.

This amendment, if adopted, would go far to alleviate the loss suffered by such dropouts and discontinuances if this amendment is favorably considered here today. If not, I urge that it be presented as an amendment to other legislation or as a separate bill.

Mr. President, I urge the Senate's favorable consideration of the proposal.

Mr. CANNON. Mr. President, in view of the recognition of this problem by the administration, and in view of the fact that the administration intends to conduct a full and thorough study of the various approaches, and plans to submit to the Congress, early next year, a recommended solution, I intend to withdraw my amendment. However, before

I do so, I yield to the Senator from Oregon [Mr. MORSE], who wishes to speak on the amendment.

Mr. MORSE. Mr. President, I rise to address myself briefly to the amendment.

I must completely disagree with the Senator from Oklahoma [Mr. KERR] that this is a desirable amendment from the point of view of public policy. I point out that the amendment is not a desirable one from the point of view of policy, and that it is not, so far as I know, a part of the administration's program. The administration was completely opposed to similar amendments, throughout all of our consideration of the educational program of S. 1021. Amendments of this type were discussed then but not adopted. The amendment, in my judgment, is unwise from the standpoint of educational policy, and I believe it to be unwise from the standpoint of tax policy. It gives no help to the student from the low-income family who needs help most and it gives greatest help to those whose family income is highest.

Taxes should be based upon ability to pay; but this amendment has nothing to do with the general problem of ability to pay. The amendment seeks to transfer to others the burden of paying the cost of education of college students. The amendment would give the proposed benefit to the parents of college students, many of whom are in middle to upper income brackets.

I have virtually fought my heart out on the floor of the Senate, working to obtain Federal aid to education. But Federal aid to education should come directly from the Treasury of the United States by appropriation. It should not be provided in the form of favoritism to the parents of some college students who need it the least.

If such an exemption is begun as a matter of tax policy, where will we end the making of exemptions for one group after another which have enough political power and pressure to be able to obtain such exemptions? Rather, I believe we should end the practice of granting one group exemption after another when such exemptions are based upon the political power of various groups. We should proceed to determine, from the standpoint of public policy, what we ought to spend the tax dollars for. Those expenditures should come from the common pool—the Treasury of the United States. We should not authorize various groups to avoid paying their fair share of taxes which are based upon the sound principle of ability to pay.

I favor aid to colleges, and I favor scholarship and loan aid to students—but not by means of such special legislation as the tax-exemption approach of this amendment.

I should like to have the sponsors of this proposal give to Federal aid-to-education legislation all the support they wish to give to this amendment. We might then get a decent, fair, equalized, across-the-board Federal aid-to-education program for the public elementary

and secondary schools. We could then give all the help we can to our institutions of higher learning, and to their students by way of scholarships and loans. But all such aid should come from the Treasury of the United States directly. It should not issue indirectly from a tax exemption amendment such as that proposed.

Mr. CANNON. Mr. President, I withdraw my amendment.

The PRESIDING OFFICER. The amendment of the Senator from Nevada is withdrawn.

Mr. GORE. Mr. President, perhaps it would be appropriate now to call up my amendment which would reduce the tax exemption—now provided by the bill—of \$35,000 a year for bona fide oversea residents to \$6,000, or exactly 10 times what has just now been under consideration in the case of a parent who has a child in college. So I call up my amendment which is identified as "8-27-62-G," and ask that it be modified, on page 2, in line 7, by making the figure at that point read "\$6,000".

The PRESIDING OFFICER. The amendment will be stated.

The LEGISLATIVE CLERK. On page 134, beginning with line 24, it is proposed to strike out all through line 25 on page 135 and insert the following:

(a) GENERAL RULE.—In the case of an individual citizen of the United States who establishes to the satisfaction of the Secretary or his delegate that he has been a bona fide resident of a foreign country or countries for an uninterrupted period which includes an entire taxable year, amounts received from sources without the United States (except amounts paid by the United States or any agency thereof) which constitute earned income attributable to services performed during such uninterrupted period shall not be included in gross income and shall be exempt from taxation under this chapter. The amount excluded under this subsection for any taxable year shall be computed by applying the special rules contained in subsection (c).

On page 137, strike out lines 4 through 13 and insert the following: "a daily basis at an annual rate of \$6,000."

On page 139, line 2, strike out "subsection (a)(1)" and insert "subsection (a)".

On page 139, strike out lines 3 through 20.

On page 140, beginning with line 16, strike out all through line 3 on page 141 and insert the following:

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 1962.

Mr. GORE. Mr. President, by the terms of the pending bill, a citizen who establishes a so-called permanent residence in Nassau will be given a tax exemption on earned income from foreign sources of \$35,000 a year. Whereas a citizen of the United States begins paying income taxes on his income beyond \$600, a citizen who establishes a residence outside the United States, but retains his citizenship in the United States, will have an exemption, under the bill, of \$35,000 a year. I think that is unreasonable; it is only one of the many provisions of the bill with which I found

myself in sharp disagreement with a majority of the Senate Finance Committee.

I do not know exactly what the exemption should be. Frankly, I think it should be something more than the exemption for citizens who reside in the United States. I would like to see it tied to the kind of oversea allowances that our ambassadors receive in various countries, but it seems to me that \$6,000 a year would be a very generous amount of tax-exempt income. It is 10 times the personal exemption of a resident of the United States.

I shall not detain the Senate. The issue is simple. I ask for a vote.

Mr. KERR. Mr. President, I call the attention of Senators to the fact that the language in the bill is restrictive, not permissive. As of now and up to this time American citizens residing abroad beyond 18 months, who are bona fide residents of another country, pay no tax on their income. The language in the bill imposes a tax upon their income. It exempts for the first 3 years the first \$20,000 of income.

After a noninterrupted period of 3 consecutive years of bona fide residence in a foreign country, the exemption becomes \$35,000.

It was the feeling of the Finance Committee that such a provision is necessary to enable American corporations doing business abroad to induce residents of our country to leave their own shores, leave their environment, take their families with them to foreign countries, and there reside in connection with the operation of an American business located in a foreign country, and that unless foreign corporations are able to offer inducements of this kind, they cannot secure the kind of talent and ability that will enable them to compete successfully in the operation of their businesses in other countries.

I say to the Senate again that the language in the bill does not confer a new tax exemption. It terminates large tax exemptions which are now in the law. It is highly restrictive in comparison with the provisions of existing law.

It was adopted by the House Ways and Means Committee, by the House itself, and by the Senate Finance Committee, after the testimony of representatives of American industries doing business abroad that in no other way could they secure the experienced and able talent required to permit them to handle their foreign operations competitively with industries and companies, either nationals within the country where those American companies are doing business or foreign corporations from other countries in the world located in the affected country and competing with American businesses located there.

Mr. LONG of Louisiana. Mr. President, will the Senator yield?

Mr. KERR. I yield.

Mr. LONG of Louisiana. Are American citizens working in foreign lands subject to the State, local, and Federal taxes of those governments, just as a person working in this country is subject to the taxes of Federal, State, and local governments?

Mr. KERR. They are. They must pay the taxes of the countries where they reside, and in many of those countries the taxes exceed those paid in our country.

Mr. LONG of Louisiana. If the logic is correct that by virtue of being a citizen of the United States residing in a foreign land, a person would owe taxes, perhaps, to the local, State, and Federal governments in that land on income earned, would not the same logic require that the U.S. Federal, State, and local governments—a total of six governments—tax the same income?

Mr. KERR. That would be the case if the amendment of the Senator from Tennessee were adopted.

Mr. LONG of Louisiana. As I understand the situation, a person would have to live overseas for 3 years as a bona fide resident there before the \$35,000 exemption limit would apply? Up to that time he would be limited to an exemption of \$20,000?

Mr. KERR. The Senator is correct.

Mr. LONG of Louisiana. Beyond that point, he would still be subject to the taxes of this Government as well as the governments overseas?

Mr. KERR. Except to the extent that the taxes he owed to this country would be after he had received credit for the taxes he paid overseas.

Mr. LONG of Louisiana. But if the logic is correct that this taxation should be levied, the Senator recognizes that a citizen of this country could be subject to taxes by two governments, and at three different levels by each government, a total of six different types of government?

Mr. KERR. Yes.

Mr. GORE. Mr. President, will the Senator yield?

Mr. KERR. I yield.

Mr. GORE. Is it not true that a citizen living abroad who pays taxes to a foreign government receives a credit for the taxes he pays to that foreign government against whatever tax liability he may have to the U.S. Government?

Mr. KERR. As I stated to the Senator from Illinois, the American taxpayer, in computing his tax liability to this country, arrives at the amount of his liability after having taken credit for taxes paid to the foreign government.

Mr. GORE. I would like to ask the Senator two more questions.

Under present law a person who is temporarily abroad for 17 out of 18 months receives an exemption of \$20,000 a year on his earned income from foreign sources.

Mr. KERR. I believe that is correct.

Mr. GORE. That is unchanged by the bill?

Mr. KERR. I think that is true.

Mr. GORE. Under present law, as the Senator has stated, the sky is the limit on tax exemption on earned income for bona fide nonresidents.

Mr. KERR. I am not familiar with the definition of the language "the sky is the limit," but, as the Senator has said, under present law, if a U.S. citizen is a bona fide resident of a country over-

seas, after 18 months he is not subject to income taxes in this country.

Mr. GORE. Perhaps that is a rather good description of "the sky is the limit."

Mr. KERR. Perhaps.

Mr. GORE. The bill before the Senate would provide for this exemption, in the case of a bona fide resident abroad, in two steps. If I went abroad and became a permanent resident, for the first 3 years I would receive a tax exemption of \$20,000, but after having been a resident abroad for 3 years, I would receive a tax exemption of \$35,000.

Mr. KERR. That is correct, but in that same period of time, as the Senator well knows, and as I have indicated, the Senator would be paying local, State, and Federal taxes in the land where he was residing and receiving an income.

Mr. GORE. That fact has no bearing upon the exemption from taxation by the United States. If he fell in the income bracket of \$600, or \$6,000, or \$60,000, he would still get a credit against U.S. taxes for the amount of taxes he paid the foreign government. That really has no bearing upon the issue.

Mr. KERR. The Senator from Tennessee may not agree with the statement of the Senator from Oklahoma. I respect the Senator. If that is his opinion, he is justified in holding it.

Mr. GORE. Does the Senator disagree?

Mr. KERR. The Senator from Oklahoma has said that, with reference to the \$20,000 exemption and the \$35,000 exemption, the American citizen would be paying taxes in the foreign country in which he resided.

Mr. GORE. I close with an observation.

Mr. KERR. The exemption provided in our law would not exempt the person from paying taxes where he works.

Mr. GORE. This is merely another subsidy, another encouragement for the movement of industry and business and jobs overseas. Why give a tax exemption to a permanent resident abroad of 10 times the tax exemption given to a citizen at home?

Mr. KERR. Mr. President, I cannot agree with the statement by the Senator from Tennessee. The businesses with reference to which the American citizens are employed are businesses operating at the domestic level in the foreign countries. They are engaged in the business of selling products which, in many instances, are manufactured in this country. For instance, Sears, Roebuck & Co. has outlets around the world.

They are not exporting jobs from this country when they send somebody overseas to manage a retail outlet in Argentina, in Brazil, anywhere in Latin America, or any other part of the world. The outlet in the foreign country sells mainly American-produced products.

What these companies attempt to do is to find the most able talent they can to go overseas to effectively manage the local branch or local distribution outlet, exactly as is done in the United States. The men who sell in those markets sell goods produced and manufactured in our factories and sent overseas for sale.

That creates jobs in this country; it does not export jobs.

If we change the law so that the companies cannot employ people with competitive talent, all we shall do is either to impair their business or put them out of business. If we should do that, we would destroy American jobs, because, as of now, countless thousands of Americans are engaged in manufacturing products which are sold in the outlets around the world.

Rather than this being a measure to bring about the export of jobs, it is a measure to bring about the creation and maintenance of jobs in our factories at home, in which men and women produce the products which American companies sell; whether they be sewing machines, washing machines, television sets or anything else.

Mr. LONG of Louisiana. Mr. President, will the Senator yield?

The PRESIDING OFFICER (Mr. McNAMARA in the chair). Does the Senator from Oklahoma yield to the Senator from Louisiana?

Mr. KERR. I yield.

Mr. LONG of Louisiana. Is it not true that in many cases the people of whom we are speaking compete in the same countries against Japanese, Germans, Englishmen, Frenchmen, and Italians, trying to get business which will generate more jobs in our country? Insofar as we put our business people in those countries at a competitive disadvantage with respect to those with whom they are competing, from other countries, we tend to lose jobs in this country, do we not?

Mr. KERR. Not only do we lose jobs in this country, but also we reduce revenues to our Government. As American industry makes money overseas, under the language of the bill before the Senate the profits are brought back home, and the profits are taxed when they get here.

It is very simple, Mr. President. American companies which do business abroad will not hire Americans and send them overseas to operate outlets merely because the businesses love them. If they can employ local nationals to manage their business as well as or better than somebody from this country can do it, or as well for less money, that is what they will do. Only when they find that they do a greater volume of business with correspondingly greater benefits to jobs and revenues back home do they employ the American citizens and give them the inducements to go overseas, to enable them more effectively to compete in the foreign markets, as the Senator from Louisiana has said, with outlets supplied by Japan, Germany, England, Belgium, Luxembourg, and even Russia.

Wherever products are produced, from wherever business organizations have come to these areas seeking to do business, the American companies find themselves in the competition provided thereby.

Mr. LONG of Louisiana. Is it not also true that in some of the less developed countries—I have particularly in mind the Latin American countries—Ameri-

can business concerns, such as Sears, Roebuck & Co., which have gone there and show how American capitalism works by installing American methods, have made it possible for the people to learn how capitalism is supposed to work?

Mr. KERR. That is true.

Senators are as aware as I am of the fact that the publications in the greatest demand in many of the underdeveloped countries and, for that matter, in the Communist countries, are catalogs from American producing and distributing companies, showing all the American gadgets, implements, utilities, and so forth which have been produced and which are available for them to buy.

I remember very well the testimony of a man from southern California who had gone to Mexico. He had taken with him his American organization. They were selling tractors and farm machinery. This man told our committee that his volume was \$5 million a year, as I recall, and every dollar resulted from sales of products manufactured in this country by American workers. Through the development of his organization in Mexico, he was selling in competition with implements and machinery being brought in from many other countries. He took his American organization there because it was effective and successful in the competition.

The companies which go into foreign countries to distribute American products need the best talent they can get.

In order to get it they must offer certain inducements. Certainly we would be penny wise and pound foolish to adopt the amendment offered by the Senator from Tennessee.

Mr. SMATHERS. Mr. President, will the Senator yield?

Mr. KERR. I yield to the Senator from Florida.

Mr. SMATHERS. Is it not a fact that the proposal made by the Finance Committee, which is in the bill, would greatly tighten existing law in this particular respect?

Mr. KERR. The Senator is correct.

Mr. SMATHERS. Is it not a fact that we endeavored to do that in order to get at motion picture stars and others who might make large amounts of money and go overseas to avoid taxes?

Mr. KERR. The Senator is correct. We attempted in the bill to cover the people who were leaving the country to provide havens for themselves, but also to continue to protect American industry competitively situated in the distribution of American products in foreign countries.

Mr. SMATHERS. Is it not a fact that the reason for the \$35,000 limitation is, as the Senator so ably says, to protect the representatives of American business doing business abroad? This provision was in no way designed to permit anybody to seek a tax haven. We took care of that earlier by providing that anybody who had an income above the \$35,000 limitation would have to pay the total tax.

Mr. KERR. The Senator is correct. I am sure the distinguished Senator re-

calls the testimony by those representing large families of Americans who live overseas. The heads of those families send their children back to this country to school, at great expense in regard to transportation to and from this country. They are living far removed from their families and parents.

The opportunity to provide incentive is absolutely necessary if the American companies doing business abroad are to be permitted to remain in a competitive position.

Mr. GORE. Mr. President, to be specific, if I had been a resident of Nassau for 3 years, the bill would give me a personal tax exemption of \$35,000. That means that a tax subsidy in the amount of the tax I would owe on \$35,000 a year would be provided for me to live in Nassau instead of in Miami. It is not very far from Miami to Nassau. I believe the flight is about 30 or 40 minutes, and the fare is low. One can be a so-called permanent resident of Nassau but be a frequent visitor to and do business in Miami, while drawing his salary in Nassau from a technically foreign source.

It is true, as has been said, that under present law, there is no tax on earned income of a so-called permanent resident abroad. The bill would require some taxes on a few of these. I think a \$35,000 exemption is utterly unreasonable.

The reason I made the statement that the measure was another encouragement for the movement of business abroad is that it would be easier to persuade people to go abroad if we give them a tax exemption of \$35,000 a year. I think it is unjustified. The committee has done something, but in this case, it has not done enough. The committee started in the right direction, as was the case in several other instances in the bill.

I should like now to refute another statement that my distinguished friend from Oklahoma made. He seemed to treat the whole subject of the movement of industry, business, and investment abroad as something that would increase jobs in the United States. It would, instead, increase exports.

I should like to cite some figures. The U.S. News & World Report last year published the results of a survey of 75 firms with substantial foreign sales. I wish to state the figures which show how their manufacturing abroad is displacing production from our own factories in this country. In 1950, these companies produced abroad only 36 percent of what they sold abroad. By 1955, they were producing abroad 56 percent of their foreign sales. By 1960, this figure had leaped to 68 percent. That means the displacement of U.S. exports. I will not further belabor the point. I hope the Senate will agree to the amendment. How can we say that someone living in Nassau should be given more than 10 times the tax exemption of a person living in Miami?

The PRESIDING OFFICER. The question is on agreeing to the amendment of the Senator from Tennessee.

Mr. DOUGLAS. Mr. President, I ask for a division.

The Senate proceeded to divide.

Mr. HOLLAND. Mr. President, I suggest the absence of a quorum.

The PRESIDING OFFICER. The clerk will call the roll.

The legislative clerk proceeded to call the roll.

Mr. KERR. Mr. President, I ask unanimous consent that the order for the quorum call be rescinded.

The PRESIDING OFFICER (Mr. BURDICK in the chair). Without objection it is so ordered.

The question is on agreeing to the amendment of the Senator from Tennessee [Mr. GORE]. [Putting the question.]

Mr. DOUGLAS. Mr. President, I ask for a division.

On a division the amendment was rejected.

Mr. DOUGLAS. Mr. President, will the Presiding Officer state the count on the vote?

Mr. CURTIS. I ask for the regular order.

Mr. DOUGLAS. Will the Presiding Officer state the count on the vote? I suggest the absence of a quorum.

Mr. HOLLAND. A point of order. No business has been transacted.

The PRESIDING OFFICER. Ordinarily the result of a standing vote is not announced.

Mr. DOUGLAS. May we have it announced in this case?

Mr. MANSFIELD. I ask unanimous consent that the vote be taken and that the Senator from Illinois be notified of what it was.

Mr. LONG of Louisiana. A parliamentary inquiry.

The PRESIDING OFFICER. The Senator will state it.

Mr. LONG of Louisiana. Is it not the practice that on a standing vote, if there are more yeas than yeas, the clerk stops counting at the time he arrives at the conclusion?

Mr. DOUGLAS. A parliamentary inquiry.

The PRESIDING OFFICER. The Senator will state it.

Mr. DOUGLAS. It may be the practice. However, can the Senate take action unless a quorum is present? Is a Senator to be deprived of the knowledge of how many Senators are present?

Mr. MANSFIELD. I have a unanimous consent request pending. I should like to have it honored.

The PRESIDING OFFICER. Is there objection to the unanimous consent request of the Senator from Montana? The Chair hears none, and it is so ordered.

Mr. CANNON. What is the request?

Mr. MANSFIELD. That a count be taken and that the count be announced to the Senator from Illinois.

Mr. DOUGLAS. That the previous count be announced.

Mr. BUSH. Reserving the right to object—

Mr. MANSFIELD. Is there objection? I believe the request was agreed to.

The PRESIDING OFFICER. It is agreed to. As many as favor the amendment will rise and stand until counted.

[After a pause.] Those who oppose the amendment will rise and stand until counted.

On this vote the yeas are 11 and the nays are 15. The amendment is rejected.

Mr. DOUGLAS. Obviously a quorum is not present. I make the point that a quorum is not present. I suggest the absence of a quorum.

Mr. HOLLAND. May I be heard on that question? A quorum may be suggested after the Chair rules and the Senate transacts business, but not before.

Mr. DOUGLAS. I suggest the absence of a quorum.

The PRESIDING OFFICER. The clerk will call the roll.

Mr. HOLLAND. Has the vote been announced?

The PRESIDING OFFICER. It has been announced.

Mr. KERR. A parliamentary inquiry. The PRESIDING OFFICER. The Senator will state it.

Mr. KERR. Has the vote on the amendment been concluded?

The PRESIDING OFFICER. It has been concluded.

Mr. KERR. Has the amendment been rejected?

The PRESIDING OFFICER. The amendment has been rejected.

Mr. DOUGLAS. How can a motion be defeated when a quorum is not present to pass upon it?

The PRESIDING OFFICER. The absence of a quorum was not suggested until after the vote.

Mr. DOUGLAS. I previously suggested the absence of a quorum.

The PRESIDING OFFICER. There are two ways in which to establish a quorum—either by a yeas and nays vote or by a request for a quorum.

Mr. HICKENLOOPER. Mr. President, I ask for the regular order.

The PRESIDING OFFICER. On a division the count does not affect a quorum.

Mr. DOUGLAS. This is obviously another way in which to whipsaw the Senate to pass measures by a small number of Senators. If the rules permit such a procedure, the rules are foolish.

Mr. MANSFIELD. I ask unanimous consent that the vote previously announced be rescinded and that I may be allowed to suggest the absence of a quorum.

The PRESIDING OFFICER. Is there objection? The Chair hears none, and it is so ordered. The clerk will call the roll.

The Chief Clerk proceeded to call the roll.

Mr. MANSFIELD. Mr. President, I ask unanimous consent that the order for the quorum call be rescinded.

The PRESIDING OFFICER. Without objection, it is so ordered.

Mr. MANSFIELD. Mr. President, on the Gore amendment, I ask for the yeas and nays.

The yeas and nays were ordered.

The PRESIDING OFFICER. The question is on agreeing to the amendment of the Senator from Tennessee [Mr. GORE]. The yeas and nays have

been ordered, and the clerk will call the roll.

The Chief Clerk called the roll.

Mr. HUMPHREY. I announce that the Senator from Mississippi [Mr. EASTLAND] and the Senator from Washington [Mr. MAGNUSON] are absent on official business.

I further announce that the Senator from New Mexico [Mr. ANDERSON], the Senator from Nevada [Mr. BIBLE], the Senator from Wyoming [Mr. HICKEY], and the Senator from Missouri [Mr. SYMINGTON] are necessarily absent.

Mr. KUCHEL. I announce that the Senator from Utah [Mr. BENNETT], the Senator from South Dakota [Mr. BOTTUM], the Senator from Arizona [Mr. GOLDWATER], the Senator from Kentucky [Mr. MORTON], and the Senator from New Hampshire [Mr. MURPHY] are necessarily absent.

If present and voting, the Senator from Utah [Mr. BENNETT], the Senator from South Dakota [Mr. BOTTUM], the Senator from Kentucky [Mr. MORTON], and the Senator from New Hampshire [Mr. MURPHY] would each vote "nay."

The result was announced—yeas 36, nays 53, as follows:

[No. 245 Leg.]

YEAS—36

Allott	Hart	Miller
Bartlett	Humphrey	Morse
Burdick	Jackson	Moss
Cannon	Javits	Muskie
Carroll	Johnston	Neuberger
Case	Keating	Pastore
Church	Kefauver	Pell
Clark	Kuchel	Proxmire
Douglas	Lausche	Scott
Ervin	Long, Hawaii	Thurmond
Gore	McNamara	Yarborough
Gruening	Metcalf	Young, Ohio

NAYS—53

Aiken	Fulbright	Pearson
Beall	Hartke	Prouty
Boggs	Hayden	Randolph
Bush	Hickenlooper	Robertson
Butler	Hill	Russell
Byrd, Va.	Holland	Saltonstall
Byrd, W. Va.	Hruska	Smathers
Capehart	Jordan, N.C.	Smith, Mass.
Carlson	Jordan, Idaho	Smith, Maine
Chavez	Kerr	Sparkman
Cooper	Long, Mo.	Stennis
Cotton	Long, La.	Talmadge
Curtis	Mansfield	Tower
Dirksen	McCarthy	Wiley
Dodd	McClellan	Williams, N.J.
Ellender	McGee	Williams, Del.
Engle	Monroney	Young, N. Dak.
Fong	Mundt	

NOT VOTING—11

Anderson	Eastland	Morton
Bennett	Goldwater	Murphy
Bible	Hickey	Symington
Bottem	Magnuson	

So Mr. GORE's amendment was rejected.

Mr. KERR. Mr. President, I move that the vote by which the amendment was rejected be reconsidered.

Mr. DIRKSEN. Mr. President, I move that the motion to reconsider be laid on the table.

The motion to lay on the table was agreed to.

The PRESIDING OFFICER. The Chair wishes to have inserted in the RECORD precedents from "Senate Procedure," on pages 632 and 633, upholding the practice of the Senate in declaring that it is not necessary for a quorum to be present in order to vote by a division.

Is there objection?

There being no objection, the excerpt from the volume "Senate Procedure," pages 632 and 633, was ordered to be printed in the RECORD, as follows:

The Presiding Officer is not required nor is it a practice of the Senate to announce the number voting on a division;³⁴ and usually the number voting for or against a proposition on a division vote, under the practice of the Senate, is not stated by the Presiding Officer;³⁵ he merely declares the results;³⁶ at times the number voting on a division have been announced.³⁷

There is no question of a quorum involved in a division vote;³⁸ it is not required that a quorum shall vote on a division³⁹ and the vote is not invalidated because of that fact;⁴⁰ the number voting on a division is immaterial, the question being simply whether the larger vote is on the one side or the other.⁴¹

Where, on a division, less than a quorum voted on a question, the Presiding Officer held the vote was valid, and that it was not in order, after a quorum call which had been demanded by a Senator, to ask for another division upon the question.⁴²

An announcement by the Presiding Officer that, on a division, less than a quorum voted does not officially disclose the absence of a quorum; where, in such a case, the Presiding Officer made no declaration of the result, the Senate, on appeal, decided the question had not been determined.⁴³

An amendment, on a division, having received a majority of the votes cast, although not a quorum, was declared to have been adopted; while the number of votes announced by the Presiding Officer was less than a quorum, it does not officially show that a quorum is not present; a quorum is presumed to be present until the contrary is shown,⁴⁴ and any Senator can call for a quorum before the vote is announced.

Mr. DIRKSEN. Mr. President, I should like to ask the majority leader whether it is the intention to complete action on the bill tonight.

Mr. MANSFIELD. I am hopeful that that can be done. I do not know how many more amendments will be offered. So far as I know, the Senator from Minnesota [Mr. MCCARTHY] will have an amendment—if he intends to offer it; and the Senator from Illinois [Mr. DOUGLAS] will have an amendment.

Mr. FULBRIGHT. I intend to offer an amendment on behalf of the Senator from Minnesota.

Mr. MANSFIELD. The Senator from Iowa [Mr. HICKENLOOPER] will have an

amendment, and perhaps other Senators will have amendments. The Senate will remain in session tonight in order to finish the bill, if possible.

Mr. HICKENLOOPER. My remarks on my amendment will be brief.

Mr. DIRKSEN. I think the amendment of the Senator from Minnesota [Mr. MCCARTHY] will be offered by the Senator from Arkansas.

Mr. FULBRIGHT. That is correct.

Mr. DIRKSEN. Mr. President, at least that gives us some idea.

Mr. MORSE. Mr. President, will the Senator from Montana yield?

Mr. MANSFIELD. I yield.

Mr. MORSE. When the majority leader spoke about finishing consideration of the bill tonight, did he mean finishing the amendments or finishing the speeches on the bill, following the third reading?

Mr. MANSFIELD. That all depends on the membership; it is not up to the Senator from Illinois and the Senator from Montana. We are the servants of the Senate. We hope to do the best we can. If that is the decision of the Senate, we shall do the best we can.

Mr. MORSE. But apparently there are four or five or six amendments still to be acted on, and there are still speeches to be made on the bill. I do not know how many speeches will be made on it; but the amendments and the speeches might require that the session continue until a rather late hour.

Mr. MANSFIELD. That might well be.

Mr. MILLER. Mr. President, I call up the amendment which I have at the desk, and ask that it be stated.

Mr. MANSFIELD. Mr. President, will the Senator from Iowa yield?

Mr. MILLER. I yield.

Mr. MANSFIELD. I am about to propound a unanimous-consent request, although I do not know whether it will be agreed to. But in view of the fact that a number of Senators have indicated that they have amendments to offer, I propose that there be a time limitation of 30 minutes on each amendment, or 15 minutes to a side.

The PRESIDING OFFICER. Is there objection?

Mr. DOUGLAS. Mr. President, reserving the right to object, let me state that I have an amendment on the depletion allowance. The amendment strikes at the greatest abuse in the entire tax system. I shall not present the amendment at undue length, but I believe it should be presented in such fashion that it can be properly heard and considered.

Mr. KERR. How much time does the Senator from Illinois think he will need?

Mr. DOUGLAS. I do not intend to speak at undue length; but I wish to have the subject treated in thorough fashion. I should not require more than an hour.

So I object.

Mr. MORSE. Mr. President, a parliamentary inquiry.

The PRESIDING OFFICER. The Senator from Oregon will state it.

³⁴ Aug. 11, 1914, 63-2, RECORD, pp. 13612, 13613; see also Mar. 6, 1940, 76-3, RECORD, p. 2440.

³⁵ Jan. 19, 1944, 78-1, RECORD, p. 398; July 10, 1947, 80-1, RECORD, p. 8610; Mar. 6, 1940, 76-3, RECORD, p. 2440; see also Mar. 28, 1933, 73-1, RECORD, p. 927.

³⁶ Sept. 8, 1922, 67-2, RECORD, p. 12250.

³⁷ Mar. 18, 1940, 76-3, RECORD, p. 2985; Apr. 5, 1940, 76-3, RECORD, p. 4104; May 21, 1940, 76-3, RECORD, p. 6495; June 14, 1940, 76-3, RECORD, p. 8252; Mar. 7, 1940, 76-3, RECORD, pp. 2467-2468; Mar. 19, 1935, 74-1, RECORD, p. 3971; Mar. 15, 1940, 76-3, RECORD, p. 2959; Mar. 21, 1940, 76-3, RECORD, p. 3213.

³⁸ May 4, 1914, 63-2, RECORD, p. 7671.

³⁹ Jan. 18, 1915, 63-3, RECORD, p. 1766.

⁴⁰ See Mar. 10, 1916, 64-1, RECORD, p. 3898.

⁴¹ May 4, 1914, 63-2, RECORD, p. 7671.

⁴² June 15, 1910, 61-2, RECORD, pp. 8162-8167.

⁴³ Aug. 18, 1922, 67-2, Journal, p. 393, RECORD, pp. 11559-11561.

⁴⁴ Mar. 25, 1920, 66-2, RECORD, pp. 4812, 4813.

Mr. MORSE. Was objection made to the proposed unanimous-consent agreement?

The PRESIDING OFFICER. Objection was heard.

Mr. MILLER. Mr. President, I call up my amendment and ask that it be stated.

The PRESIDING OFFICER. The amendment will be stated.

The CHIEF CLERK. It is proposed to add to the bill a new section entitled "Incentive Taxation of Growth Income."

Mr. MILLER. Mr. President, I ask unanimous consent that the reading of the amendment be dispensed with, and that the amendment be printed in full in the RECORD.

The PRESIDING OFFICER. Is there objection?

There being no objection, the amendment submitted by Mr. MILLER was ordered to be printed in the RECORD, as follows:

Add the following new section to the bill:

"SEC. . INCENTIVE TAXATION OF GROWTH INCOME.

"(a) REDUCED RATES ON GROWTH INCOME.—

"(1) Section 1 of the Internal Revenue Code of 1954 is amended by striking subsection '(d)' and inserting in lieu thereof the following:

"(d) TAX ON GROWTH INCOME.—Notwithstanding the rates of tax prescribed above, the tax on growth income shall be reduced by an amount equal to one-half the tax otherwise computed on the basis of such rates: *Provided*, That such reduction shall not exceed the tax for the first immediately preceding full taxable year: *And provided further*, That reductions of less than \$5 shall not be recognized.

"(e) CROSS REFERENCE.—

"For definition of taxable income, see section 63.

"For definition of growth income, see section 64."

"(2) Section 3 of the Internal Revenue Code of 1954 is amended by adding the following at the end thereof: '*Provided*, That the tax on growth income shall be reduced by an amount equal to one-half the tax otherwise computed under the table; but such reduction shall not exceed the tax for the first immediately preceding full taxable year, and reductions of less than \$5 shall not be recognized.'

"(3) Section 11 of the Internal Revenue Code of 1954 is amended by changing subparagraph '(d)' to '(e)' and by adding a new subparagraph '(d)' as follows:

"(d) TAX ON GROWTH INCOME.—Notwithstanding the rates of tax prescribed above, the tax on growth income shall be reduced by an amount equal to one-half the tax otherwise computed on the basis of such rates: *Provided*, That such reduction shall not exceed the tax for the first immediately preceding full taxable year: *Provided further*, That reductions of less than \$15 shall not be recognized."

"(4) Section 12 of the Internal Revenue Code of 1954 is amended by adding the following subsection:

"(g) For definition of growth income, see section 64."

"(b) TAX REDUCTION PAYBACK.—

"(1) The Internal Revenue Code of 1954 is amended by changing section '5' to '6' and by adding a new section '5' as follows:

"SEC. 5. TAX REDUCTION PAYBACK.

"(a) The amount of tax reduction attributable to growth income provided for in sections 1 and 3 shall be voided and the reduction shall become a part of the tax due and payable for the following taxable year

to the extent prescribed in subparagraph (b).

"(b) If a taxpayer's combined income from wages and salaries, rents, ordinary dividends, royalties (other than royalties receiving special tax treatment), interest, and business and farming (with adjustments provided in section 64 applicable to the current taxable year) is less than such combined income (with adjustments provided in section 64 applicable to the first immediately preceding taxable year) for the year of tax reduction due to growth income, the tax reduction shall be voided according to the proportion that the decrease bears to the amount of growth income on the basis of which said tax reduction was computed: *Provided*, That said tax reduction shall not be voided to the extent said decrease is attributable to the retirement or death of a taxpayer (or his spouse) or to losses due to fire, flood, drought, windstorm, theft, or other casualty, not covered by insurance or otherwise: *Provided further*, That if said following taxable year is a short year due to termination of an estate or trust, such combined income (with adjustments provided in section 64 applicable to the current taxable year) shall be annualized for the purpose of computing said decrease, if any."

"(2) The Internal Revenue Code of 1954 is further amended by changing section '12' to '13' and by adding a new section '12' as follows:

"SEC. 12. TAX REDUCTION PAYBACK.

"(a) The amount of tax reduction attributable to growth income provided for in section 11 shall be voided and the reduction shall become a part of the tax due and payable for the following taxable year to the extent prescribed in subparagraph (b).

"(b) If a corporation's combined income from rents, ordinary dividends, royalties (other than royalties receiving special tax treatment), interest, and business and farming (with adjustments provided in section 64 applicable to the current taxable year) is less than such combined income (with adjustments provided in section 64 applicable to the first immediately preceding taxable year) for the year of tax reduction due to growth income, the tax reduction shall be voided according to the proportion that the decrease bears to the amount of growth income on the basis of which said reduction was computed: *Provided*, That said tax reduction shall not be voided to the extent said decrease is attributable to losses due to fire, flood, drought, windstorm, theft, or other casualty, not covered by insurance or otherwise: *Provided further*, That if said following taxable year is a short year due to liquidation, dissolution, or reorganization, such income (with adjustments provided in section 64 applicable to the current taxable year) shall be annualized for the purpose of computing said decrease, if any."

"(c) GROWTH INCOME DEFINED.—

"(1) The Internal Revenue Code of 1954 is amended by adding the following new section:

"SEC. 64. GROWTH INCOME DEFINED.

"(a) For purposes of this subtitle, the term "growth income" means the excess of the combined income from the current taxable year from wages and salaries, rents, ordinary dividends, royalties (other than royalties receiving special tax treatment), interest, and business and farming (with adjustments provided below) over such combined income (not less than zero) for the first immediately preceding full taxable year (with adjustments provided below), hereinafter referred to as the "base year."

"(b) With respect to the current taxable year, strike out the following:

"(1) Gains and losses from the sale or exchange of capital assets or property treated as capital assets, the capital loss

carryover deduction, and net operating loss deduction.

"(2) Recognized income due to recovery of bad debts, prior taxes, and delinquency amounts, and due to improvements by a lessee.

"(3) Net income from illegal activities.

"(4) Lump sum income which the taxpayer may ratably allocate for tax purposes except to the extent of the portion ratably allocable to the current taxable year.

"(5) Losses from fire, flood, windstorm, theft, or other casualty not covered by insurance or otherwise.

"(6) Income resulting from a change in method of valuing inventory, method of accounting, or method of depreciation.

"(7) Dividend income from a corporation in excess of 125 percent of such income received from the corporation in the previous taxable year, or in excess of current earnings of said corporation, whichever excess amount is the greater, where 50 percent or more of the total combined voting power of all classes of stock of said corporation is owned by the taxpayer.

"(8) In the case of a taxpayer other than a corporation, income from a business or a partnership which represents the continuation of the business of a corporation, 50 percent or more of the total combined voting of all classes of stock of which is owned by the taxpayer. (This provision shall not apply after the first full taxable year following cessation of such business by the corporation.)

"(9) In the case of a corporation, income which represents the continuation of the business of another corporation merged or consolidated with the taxpayer or which represents the continuation of the business of another corporation of which 50 percent or more of the total combined voting power of all classes of stock is owned by the corporation. (This provision shall not apply after the first full taxable year following such merger or consolidation or cessation of such business by the other corporation.)

"(10) In the case of a corporation, the decrease in deductions for charitable contributions (under section 170) below such deductions for the first immediately preceding full taxable year.

"(11) In the case of estates and trusts, the decrease in deductions for income paid over to beneficiaries below such deductions for the first immediately preceding full taxable year where such payment is discretionary.

"(c) With respect to the base year, delete the following:

"(1) Gains and losses from the sale or exchange of capital assets or property treated as capital assets, the capital loss carryover deduction, net operating loss deductions, and the additional first-year depreciation deduction authorized by section 179.

"(2) Recognized income due to recovery of bad debts, prior taxes, and delinquency amounts, and due to improvements by a lessee.

"(3) Losses from fire, flood, windstorm, theft, or other casualty not covered by insurance or otherwise.

"(4) Income resulting from a change in method of valuing inventory, method of accounting, or method of depreciation when such change results from action of the Commissioner.

"(d) In the case of corporations, the combined income for the base year shall not be less than such income (with the same adjustments) for the taxpayer's calendar or fiscal year 1962 or (if the taxpayer was not in existence or was inactive during such year) the first full taxable year thereafter: *Provided*, That the taxpayer may elect in lieu of such limitation to use the average of such combined income (with the same adjustments) for calendar or fiscal year 1962 and the two immediately preceding full tax-

able years (or, if the taxpayer was not in existence for such period, the first immediately preceding full taxable year) if active during such period.

"In the case of a reorganization, the limitation on the base year of the continuing corporation shall be computed by using the combined income for calendar or fiscal year 1962 of the corporations which are parties to the reorganization; and if the combined income of fiscal or calendar year 1962 and the two immediately preceding taxable years (or first immediately preceding taxable year, as the case may be) is used in lieu of such limitation, the combined income for such period of the corporations which are parties to the reorganization shall be used.

"(e) Where income or deductions have been arbitrarily shifted from one year to another by a taxpayer for no business purpose other than reduction of taxes arising from the reduced tax rates on growth income, the Commissioner is authorized to make such adjustments as are necessary to protect the revenue.

"(f) In determining ownership of stock for purposes of this section, actual or constructive ownership (under section 318) shall be taken into account.

"(g) Where a joint return is filed for the current taxable year and separate returns were filed (either as married or single individuals) for the base year, the base year's income shall include the income (with adjustments specified above) of both returns unless the income on the joint return represents the actual income of only one spouse."

"(d) **EFFECTIVE DATE.**—The section added by this amendment shall be effective January 1, 1963. In the case of taxable years ending prior to December 31, 1963, the tax reduction provided for herein shall be reduced according to the proportion that the number of months not falling within the calendar year 1963 bears to 12."

Amend the title so as to read: "An Act to amend the Internal Revenue Code of 1954 to encourage economic growth by providing for reduced income tax rates on growth income of individuals, estates, trusts, and corporations, to define 'growth income', to eliminate certain defects and inequities, and for other purposes."

Mr. MILLER. Mr. President, it is my intention to ask that the amendment be withdrawn. Nevertheless, I ask unanimous consent that the usual number of copies of the amendment be printed.

The PRESIDING OFFICER. Without objection, it is so ordered.

Mr. MILLER. Mr. President, today there is a long overdue national concern over the adverse effect our system of income taxation has been having on our capitalistic economic system. As the cost of living moves steadily upward, as the squeeze between prices and costs grows tighter, as competition from foreign lands becomes keener, as our annual rate of economic growth remains stagnant, and as serious unemployment continues to be chronic, the key role of income taxation becomes more evident.

Granted that the basic purpose of this taxation is to raise revenue, it is obvious that some of its features can produce by-products of discouragement or encouragement to economic growth. Unfortunately discouragement, rather than encouragement, prevails under the present system.

The need for increased purchasing power and increased capital formation and utilization has prompted a call for tax cuts from the people and assurances of tax cuts from the President. However, despite the theories of some sophisticated economists, there seems to be an awareness on the part of the people that tax cuts, without a cutback in spending to make room for them, would not be meaningful; that tax cuts which produce increased Federal deficits and add to the national debt will, sooner or later, result in reduced purchasing power of our money, so that any savings or capital resulting from such tax cuts will be diluted, and any increased purchasing power or increased capital formation will be illusory. Worse yet, perhaps, the reduced value of our dollar would add to the seriousness of our declining gold reserves.

Congress in its present makeup is not disposed to cut back spending. The President says there will be no reduction in spending for programs which are essential to the national interest, but interpretation of what is essential to the national interest by the administration indicates that it will not reduce its spending proposals to Congress. With such an impasse, we are on dead center; and the situation poses a deadly threat to the future of our Nation. We are desperately in need of a tax change to encourage economic growth.

REQUIREMENTS OF INCENTIVE TAXATION

The word "incentive" has been rather loosely applied in tax policy. Usually it is associated with tax reduction—either through outright tax rate reduction or through so-called tax reform, or both. It assumes that tax reduction will automatically be followed by economic growth, but there is no guaranty that this will happen. Most of us would probably anticipate an overall growth in our economy if we had tax reduction accompanied by stable purchasing power of our money. However, there would probably be taxpayers who would happily enjoy the tax reduction without seeking to contribute to economic growth. They would accept the reward without earning it.

What is required is a tax change which will be an incentive, which will not give

the reward of tax reduction unless the objective of growth is fulfilled, which will operate without jeopardizing the purchasing power of our money, which contains elements of tax reform and tax rate reduction, and which faces up to the political realities existing in Congress and the administration.

In the current issue of *Fortune* magazine, the editorial entitled "The Right Kind of Tax Cut" points out the dilemma that some tax-cutting proponents are in because of the atmosphere with respect to the refusal to cut spending.

In the Friday, August 31, issue of the *Wall Street Journal* an excellent article by Mr. Robert D. Novak also points out the dilemma that tax-cutting proponents find themselves in when there is a refusal to cut back spending.

I ask unanimous consent that the editorial and the article be printed in the *Record* at the conclusion of my remarks.

The PRESIDING OFFICER. Without objection, it is so ordered.

(See exhibit 1.)

Mr. MILLER. I have a plan for such a change, and I call it incentive taxation of growth income. My amendment incorporates this plan.

INCENTIVE TAXATION OF GROWTH INCOME

In a nutshell, my plan proposes to tax any increase in adjusted gross income—in the case of individuals—or taxable income—in the case of estates, trusts, and corporations—over the adjusted gross income or taxable income for the preceding year at one-half the rates that would otherwise apply. You might call it an excess profits tax in reverse. This increase represents "growth income," and tax reduction would take effect only with respect to it. The reward of tax reduction would have to be merited. Taxpayers would have an incentive to devote extra effort in the use of their skills and responsibilities. People with savings would have an incentive to invest their money as risk capital in the purchase of stock or bonds or the making of loans—all of which are needed to provide the expansion of our private economy needed to provide job opportunities for our unemployed and the millions who will be graduating from our high schools and colleges.

Examples of Miller plan for incentive taxation of growth income (effective Jan. 1, 1963)

Year	Adjusted gross income	Tax at old rate	Increase in tax over prior year at regular rate	Tax reduction (½ increase)	New tax
Individual, married, 4 children, using optional standard deduction, with adjusted gross income from a salary, wages, profession or business:					
1962	\$10,000	\$1,108	(1)	(1)	(1)
1963	15,000	2,304	\$1,196	\$598	\$1,706
1964	20,000	3,740	1,436	718	3,022
Individual, married, 2 children, using optional standard deduction, with adjusted gross income from a salary, wages, profession or business:					
1962	5,000	420	(1)	(1)	(1)
1963	5,500	510	90	45	465
1964	6,000	600	90	45	555
Corporation, taxable income as shown in 2d column (note 1st \$25,000 taxes at 30 percent; all over \$25,000 taxed at 52 percent):					
1962	100,000	46,500	(1)	(1)	(1)
1963	120,000	56,900	10,400	5,200	51,700
1964	140,000	67,300	10,400	5,200	62,100

¹ Change not in effect.

From the Government's standpoint, the Treasury would have reasonable assurance of the same amount of revenue from the same amount of income as the previous year, so that the tax reduction under this plan would not cause a loss of revenue and a consequent loss in purchasing power of our money which characterize other tax-cutting plans. I recognize that Government spending increases in anticipation of increased revenues might have to be curbed, but these should be curbed anyhow—as the administration has learned from the disappearance of its promised balanced budget, which was based on excessive optimism over revenue increases for the current year.

However, I suggest that the prospect of paying tax at only one-half the regular rate on growth income would be a tremendous incentive for taxpayers to increase their productivity. Wasteful or marginal costs, which too often are tolerated because they are tax deductible, would be reduced or eliminated. Tax reform is built into the plan because taxpayers would have an incentive—other than that furnished by a revenue agent—to avoid unnecessary or excessive expenditures. Such expenditures would only reduce their growth income and their tax reduction. We could expect real improvement in our rate of economic growth.

GROWTH INCOME DEFINED

The definition of "growth income" must be precise and realistic. It should certainly include business and farming income. With respect to other items of income, either of two approaches may be used. One approach, which is simpler, would be to specify the items. The other approach would be to include all income except certain items which do not have any particular relevance to growth during the current year due to the taxpayer's labor or capital. For example, pensions and annuities, income in respect of a decedent, income from death benefits, compensation for injuries, income from an estate or trust, alimony and separate maintenance benefits, income from the discharge of indebtedness, and the like. Even with these exclusions, however, we would still be faced with situations under which an incentive would be extended to increase income that would be of marginal or questionable significance insofar as labor or capital are concerned, not to mention illegal income, which is nonetheless taxable.

Accordingly, I would propose that in addition to business and farming income, wages and salaries, rents, ordinary dividends, royalties—other than royalties receiving special tax treatment—and interest be specified as the only other type of income which can be used in computing growth in income. These items constitute the major sources of income of the vast majority of taxpayers and are relatively easy to ascertain; and from the standpoint of administration, it is desirable to keep them at a minimum. Moreover, all of them have a clear connection with the utilization of labor or capital in the production of income. Capital gains, including capital divi-

dends, may happen to be realized during the current taxable year, but they usually include growth which has occurred prior to the current taxable year; moreover, they already receive special incentive tax treatment. I would therefore exclude them from the definition of "growth income."

ADJUSTMENTS TO BUSINESS INCOME

To have a realistic measurement of growth in business income, certain adjustments should be made. For example, a lump sum payment received in the taxable year which reflects services rendered over a period of several years cannot reasonably be attributed, in its entirety, to growth during the taxable year. A ratable allocation to the current year under the option available to the taxpayer should be the limit. Income from a change in method of valuing inventory, from a change in method of accounting, or from a change in method of computing depreciation hardly reflects economic growth. Additional income of a corporation resulting from another corporation being merged with it, to the extent of the other corporation's income, certainly does not represent growth of the first corporation's business. Additional income of an individual resulting from the transfer to him—through dissolution—of the business of his controlled corporation would not represent his growth. These items of taxable income should be eliminated in computing growth income.

To be fair, there are other adjustments that should be made to eliminate deductions which are properly allowable for tax purposes but have no essential relationship to growth. Thus net operating loss carryover deductions or capital loss carryover deductions should not be taken into account in determining growth income. It would seem that a loss deduction attributable to fire, flood, windstorm, theft, or other casualty, not covered by insurance or otherwise, should not be permitted to destroy the growth a taxpayer may otherwise have achieved and should also be eliminated.

Another adjustment appears to be desirable in the case of corporations. Contributions to charitable, educational, religious, scientific, and similar activities are becoming increasingly important and are to be encouraged. If a corporation's growth income could be enhanced merely by cutting back its contributions, a long-standing policy of Congress to encourage corporate giving would be frustrated. Accordingly, it appears desirable to provide that growth income of a corporation may not be so achieved.

Business income from illegal activities should be excluded altogether, for I presume this kind of growth is not to be encouraged.

PRIOR-YEAR ADJUSTMENTS

Adjustments with respect to the current year are not the only ones required to properly measure growth. Income of the immediately preceding taxable year, which ordinarily would serve as the base for measuring growth, also requires some adjustments. First of all, we must decide whether a base year income of less than zero should be permitted. Al-

though I would admit that coming from a loss of \$10,000 in one year to a profit of \$10,000 in the following year represents \$20,000 in growth, I do not believe it wise to permit growth income to be measured from a loss position, particularly since a taxpayer already has the benefit of a net operating loss carryover or carryback deduction.

Next, we should not measure growth income in the current year from a fictitiously low economic income base. Thus, if income during the preceding year has been lowered for tax purposes by taking into account a net operating loss deduction, a capital loss carryover deduction, a loss deduction arising from fire, flood, windstorm, theft, or other casualty, not covered by insurance or otherwise, or a deduction for the extra first-year depreciation allowed by section 179, these adjustments should be added back.

I am dubious over permitting a lowering of the base year's income by eliminating income arising from a change in method of valuing inventory, change in method of accounting, or change in method of depreciation. Such changes are usually voluntary on the taxpayer's part and often are made with a view to improving his tax position. Accordingly, I would propose that a lowering of the base year's income by eliminating such income be permitted only where the change in method has been forced on the taxpayer by the Government.

Where a joint return is filed for the current taxable year, it would be unrealistic to measure the income reported therein against the income of only one of the spouses for the preceding year if separate returns were filed by them—either as married or single persons—unless the income of the joint return represents the actual income of only one of them. I use the word "actual" to make it clear that community property law will not enter into this calculation.

PREVENTION OF WINDFALLS, WHIPSAWING, AND OTHER UNDESIRABLE RESULTS

In order to prevent windfalls, whipsaws, whipsawing—fluctuating income from one year to another to take undue advantage of the reduced rates on growth income—and other undesirable results, certain provisions are necessary.

The question arises whether a taxpayer who becomes a wage earner, salaried person, or business operator for the first time should be permitted to treat any or all of his first year's income as growth income. The answer would seem to be "No." Birth of income is not the same as growth in income. A similar answer should apply in the case of the first year of operation of an estate, trust, or corporation. Accordingly, I would define growth income in such a way as to require it to be measured against the first immediately preceding full taxable year, so that at least one full year's experience will be used as a basis for calculating growth. But that first year's experience may represent only part-time or nominal activity. To prevent a windfall by using the income from such a year as a base, I would provide that tax reduction from the special rates on growth income not be in excess of the amount of tax for the preceding year.

For example, B, a college senior, graduates in midyear and commences full employment, earning \$5,000, with regular tax thereon of \$813. During the preceding year he worked part time, earning \$1,200 and paying tax of \$98. His tax reduction for the current year would be \$98—not \$357.50—one-half the difference between \$813 and \$98. C, a corporation, commenced its activities in June of 1963. Reporting on a calendar-year basis, it had a loss of \$10,000 during the short year 1963, income of \$10,000 for 1964, on which tax of \$3,000 was paid, and income of \$100,000 for 1965, on which tax of \$46,500 would be owing under the present rates. C's tax reduction for 1965 would be \$3,000, not \$21,750—one-half the difference between \$46,500 and \$3,000.

Also, to eliminate administrative costs with respect to minute amounts of growth, my amendment provides that tax reduction of under \$5 in the case of individuals, estates, and trusts and \$15 in the case of corporations not be recognized.

An individual in control of a corporation—or a corporation in control of another corporation—might seek to obtain growth income by arbitrarily having the controlled corporation declare extraordinary dividends. To prevent this type of abuse, it would seem desirable to limit the amount of dividends that could be counted for this purpose—say to 125 percent of those received from the controlled corporation during the preceding taxable year, and, in any event, limit such dividends to the amount of current earnings of the corporation. In ascertaining whether or not a taxpayer is in control of a corporation, constructive ownership of stock under the attribution rules of section 318 should be taken into account.

With the payback provision, which I shall presently discuss, the graduated tax rates applicable to individuals, trusts, and estates do not offer much opportunity for whipsawing. There is, however, some opportunity for whipsawing in the case of corporations. To discourage this, I would propose using as a base year for corporations the immediately preceding full taxable year—as in the case of individuals, estates, and trusts—with the limitation that the taxable income for such base year be not less than the taxable income for fiscal or calendar year 1962, assuming this plan becomes effective January 1, 1962. If the corporation was not in existence or active during fiscal or calendar year 1962, its first full taxable year thereafter would be used for this purpose. However, one can conceive of situations where a corporation's taxable income for fiscal or calendar year 1962 might be abnormally high, leaving little or no incentive to the corporation to seek growth because of the arbitrary selection by Congress of the taxable income of such year as a limitation on the base year. To cover these situations, I would propose that in lieu of fiscal or calendar year 1962, a corporation could elect to

use—as a limitation against the taxable income of the base year—the average taxable income of fiscal or calendar 1962 and the 2 preceding taxable years—or the preceding taxable year, if the corporation was not in existence or active during the 2 years preceding fiscal or calendar 1962.

For example, corporation X had taxable income as follows: 1960, \$75,000; 1961, \$100,000; 1962, \$200,000; 1963, \$100,000; 1964, \$150,000. No adjustments were required to taxable income for 1963 and 1964. Obviously there was no growth income for 1963 and no tax reduction. Growth income for 1964 cannot be measured against taxable income of \$100,000 for 1963, because 1963 taxable income cannot be less than the \$200,000 taxable income for 1962. However, the corporation elects to take the average taxable income for 1960, 1961, and 1962, which is \$125,000, as the limitation below which base income for 1962 cannot go. Growth income for 1964 would be \$25,000.

Deliberate whipsawing by taxpayers may possibly be attempted notwithstanding the precautionary provisions built into this plan. With a view to discouraging such efforts, it would seem proper to provide that where income or deductions have arbitrarily been shifted from one year to another by a taxpayer for no business purpose other than reduction of taxes arising from the reduced rates on growth income, the Commissioner may make such adjustments as are necessary to protect the revenue. The doctrine of business purpose is reasonably well settled by the tax law, regulations, and court decisions, and such a provision should be unwelcome only to those who would seek to frustrate the purpose of this new plan.

TAX REDUCTION PAYBACK

Not only do we wish to encourage growth. We wish to discourage going backward after growth. Such a policy, coupled with a policy against whipsawing, prompts me to recommend what I call a tax reduction payback provision. It would require the voiding of a tax reduction based on growth income if, in the following year, the taxpayer's income decreases. The tax reduction would be voided according to the proportion that the decrease in the following year bears to the amount of growth income on the basis of which the tax reduction was computed.

For example, corporation A has taxable income—adjusted—of \$100,000 for 1962, \$100,000 for 1963, and \$100,000 for 1964. It pays \$46,500 tax for each year. It has no tax reduction for 1963 and 1964 because there is no growth income. On \$200,000 combined income for 1963 and 1964 its combined tax is \$93,000.

Corporation B has taxable income—adjusted—of \$100,000 for 1962, \$150,000 for 1963, and \$50,000 for 1964. Its combined income for 1963 and 1964 is \$200,000, and its combined tax is \$93,000—the same as corporation A, computed as follows:

	1963	1964	Total
Taxable income.....	\$150,000	\$50,000	\$200,000
Tax.....	72,500	20,500	93,000
Tax reduction.....	-13,000		
Tax reduction payback.....		+13,000	

If, instead of a decrease from taxable income—adjusted—of \$150,000 for 1963 to \$50,000 for 1964, corporation B dropped only to \$125,000, the tax reduction payback would be only \$6,500—one-half of \$13,000 tax reduction for 1963 based on the proportion of the decrease of \$25,000 in 1964 to the growth income of \$50,000 for 1963.

The amount of the tax reduction payback would become a part of the tax due and payable for the year of the decrease in income. I do not believe it is necessary to require payment of interest inasmuch as the taxpayer will already have lost the use of tax money paid on the higher tax that would have been due for the growth year—even after allowance of the tax reduction.

My amendment has been drafted to prevent the application of the tax reduction payback under circumstances which have no particular relevance to the policy of encouraging growth; namely, retirement or death of a taxpayer, or losses due to fire, flood, drought, windstorm, theft, or other casualty, not covered by insurance or otherwise. Moreover, if the year following the growth year is a short taxable year due to termination of an estate or trust or due to liquidation, dissolution, or reorganization of a corporation, the income is to be annualized to see whether or not there has been a decrease in income.

I recognize that the tax reduction payback may not be popular, but it would leave a taxpayer in no worse tax position than he is now. Moreover, it might serve as a stimulus to prudent management. For example, a businessman who received a tax reduction of—say \$5,000 in 1 year—would be inclined to use it to reduce his indebtedness, on the chance that his income in the following year might decrease and some or all of it would have to be paid back. Otherwise, he might be inclined to make an untimely or risky move.

The tax reduction payback, as I said before, is also needed to prevent whipsawing. The following example illustrates why this is so in the case of two corporations which, having the same base year income of \$100,000, have \$300,000 in income—without adjustments—over a 3-year period. It should be noted that corporation A has a \$100,000 stable annual income for each of the 3 years; whereas corporation B fluctuates—or whipsaws—its income. Both corporations would have the same total tax to pay for the 3-year period; but this would not be true unless the payback provision applied to corporation B, along with the limitation that the base year income cannot be less than that of fiscal or calendar year 1962:

	Base year 1962	1963	1964	1965	3-year total
Corporation A:					
Income.....	\$100,000	\$100,000	\$100,000	\$100,000	\$300,000
Tax.....	46,500	46,500	46,500	46,500	139,500
Tax reduction.....	(1)	None	None	None	None
Net.....					160,500
Corporation B:					
Income.....	100,000	150,000	50,000	100,000	300,000
Tax.....	46,500	72,500	20,500	46,500	139,500
Tax reduction.....	(1)	-13,000		² None	-13,000
Payback.....			+13,000		+13,000
Net.....					160,500

¹ Not in effect.

² Since income for this year of \$100,000 must be measured against income of \$100,000 for calendar year 1962, rather than against income of \$50,000 for the 1st immediately preceding full taxable year.

I emphasize that with the tax reduction payback and other safeguards written into this plan, the possibility of manipulating income to reduce the cumulative tax burden is eliminated. Attempts to artificially induce an income cycle in which the rising phase exceeds 1 year will meet with failure. I have worked out numerous examples in an effort to beat the plan, but they are frustrated by the various safeguards that are built into the plan.

CONCLUSION

Like any other major plan of tax reform, this one has its minuses as well as its pluses. I recognize that many taxpayers would not receive any benefit from it, although the plan envisages extension of the tax reduction to the maximum number of taxpayers. Some are in a declining income position which is beyond their control. Others, including most Members of Congress, are on a stable earnings basis with little likelihood for improvement—although this plan will provide encouragement to make the most of opportunities for improvement.

Eliminating tax reductions of under \$5 in the case of individuals and under \$15 in the case of corporations will greatly reduce the administration required to implement this plan. Moreover, cost of living wage increases under escalation clauses do not really represent increased productivity, and the \$5 limitation will eliminate most of these.

In those situations where weather conditions can have an important bearing on income—such as in the agricultural or construction industries—growth or decrease in income would naturally be affected regardless of the capital or labor contributed. However, the plan does have the protection against highly abnormal vicissitudes of weather; and where weather has had a severe impact on business or wage conditions, there will still be the incentive to work harder to make up for it.

But similar criticisms can be made of other tax-reduction provisions in the tax law. For example, faster depreciation methods and rates are meaningless to a taxpayer caught in the same tax bracket with or without them. Percentage depletion is meaningless to a taxpayer to the extent that it exceeds 50 percent of net income. The deduction for medical and hospital expenses means nothing to over half the taxpayers under 65, who either use the optional standard deduction or find such expenses exceeded by 3 percent of their adjusted gross income.

Nevertheless these have been enacted because Congress considered that, on balance, they were in the national interest. I might also point out that the investment tax credit which the administration is backing so strongly would result in tax relief to only a comparatively small number of taxpayers.

Incentive taxation of growth income is entirely workable and administratively feasible. It would be simple for most taxpayers to compute their tax reduction because they would have few, if any, adjustments to make. Corporations and individuals operating a business would, in some cases, find it complicated. However, when we recall how complicated the excess profits tax law was, perhaps we should not be too impatient with a far less complicated proposal which will, unlike the excess profits tax law, reduce taxes, and provide an incentive for the business expansion so greatly needed to solve our unemployment problem.

Incentive taxation of growth income would, I am confident, spur capitalism and the free enterprise system on to victory over communism in the economic competition to which Premier Khrushchev has challenged us.

Mr. DIRKSEN. Mr. President, will the Senator yield?

Mr. MILLER. I am very happy to yield to the Senator from Illinois.

Mr. DIRKSEN. Mr. President, the distinguished Senator from Iowa has previously advanced what he is stating to the Senate at the present time, and there is an article on it in the publication the Weekly Bond Buyer, September 4, 1962, under the heading "The Miller Plan." Altogether, it is a laudatory article. At this time I ask unanimous consent to have it printed in the RECORD as a part of my remarks, because it is very incisive. It sets forth the very captivating, effective new tax proposal, and I believe it deserves wide currency insofar as the CONGRESSIONAL RECORD can provide it.

There being no objection, the article was ordered to be printed in the RECORD, as follows:

THE MILLER PLAN

WASHINGTON.—Judging from the rash of publicity that is being given to their current activities, it would be excusable to assume that Messrs. BYRD and MILLS, CURTIS and PROXMIRE, DOUGLAS and PATMAN, and perhaps one or two others, hold a tight monopoly on tax ideas emanating from Congress.

However, this is far from true, as the Republicans, to their sorrow, are belatedly discovering. Within their ranks, but virtually overlooked for the past 2 years, is one

of the brightest, most articulate tax minds in Washington, freshman Senator JACK MILLER, Republican, of Iowa.

Senator MILLER, who staged an upset victory to win his seat in the 1960 elections, was an innocent victim of the Senate's archaic seniority rules when the party chieftains organized the Republican minority membership of committees at the outset of the 87th Congress. Otherwise, today he might be on the Senate Finance Committee—and the Nation, and the Republicans, might be the happier for it.

Last week, at the 17th annual meeting of the Tax Executives Institute, at White Sulphur Springs, W. Va., Senator MILLER uncorked a revolutionary new plan for tax cuts that brought the sophisticates upright in their chairs.

Senator MILLER, previously a private tax consultant in Sioux City and before that an "idea man" for the Treasury's Bureau of Internal Revenue, calls his plan "incentive taxation of growth income."

He claims it would cut taxes by one-half on the amount of increase in income (growth) over the previous year. It could become effective in 1963, and it would apply to individuals, corporations, estates, trusts, and partnerships.

"In its simplest terms," Senator MILLER says, "the plan proposes to tax any increases in adjusted gross income for individuals, or taxable income of estates, trusts or corporations over the adjusted gross income or taxable income for the preceding year at one-half the rates that would otherwise apply."

"This increase represents growth income and the tax cut would take effect only with respect to it. The reward of tax reduction would have to be merited."

Senator MILLER points out that under his scheme the Treasury would be assured of the same amount of revenue from the same amount of income as in the previous year, "so that the tax reduction under this plan would not cause a loss of revenue and a consequent loss in purchasing power of our money."

The Iowan recognizes that Government spending increases in anticipation of increased revenues might have to be curbed. But, these should be curbed anyhow—as the administration learned in the disappearance of its promised balanced budget for fiscal 1963, which was based on excessive optimism over the revenue increases for the current year.

Senator MILLER suggests that "the prospect of paying tax at only one-half the regular rate on growth income would be a tremendous incentive to taxpayers to increase their productivity."

"Wasteful or marginal costs," he says, "which are too often tolerated because they are tax deductible, would be reduced or eliminated."

"Tax reform is built into the plan, because taxpayers would have an incentive other than that furnished by the revenue agent, to avoid unnecessary or excessive expenditures. Such expenditures, if permitted to continue, would only reduce their growth income and their tax reduction. We could expect real improvement in our rate of economic growth."

Another way of viewing Senator MILLER's plan is as a sort of excess profits tax in reverse.

In short, rather than being penalized for sharper management, improved production techniques and more skilled marketing and advertising programs—factors which produce greater profits and hence, growth—industry managers would be rewarded by tax cuts in proportion to their proven skills and entrepreneurial abilities.

Senator MILLER, who has acquired a nice veneer of political savvy to accompany his awaitemess of the tax facts of life in his 2

years in the Senate, says he is totally sympathetic with the proposals made by Representatives A. S. HERLONG, of Florida, and HOWARD BAKER, of Tennessee, for a gradual reduction in individual and corporate rates.

"However," he says, "the Herlong-Baker suggestion presupposes a stable purchasing power of our money—a condition that is virtually impossible so long as Congress will refuse to reduce spending to make room for tax cuts.

"It also assumes a period of growth at still some undetermined annual rate—an assumption that might not materialize and, if it didn't the consequences could be serious."

"What is needed," he continues, "is a tax reduction that will be a realistic incentive, which will not pay out the rewards of tax cuts, unless the objective of growth is fulfilled. Also, a change is required that will operate without jeopardizing the purchasing power of our money, and which acknowledges the political realities existing in Congress and the administration."

What is also needed is some fresh Republican blood on the Senate Finance Committee, whose majority and chairmanship will again be held by the Democrats next year, barring some major political upheaval.

If the GOP policymakers in the Senate see fit to correct the error of 1960 caused by almost blind adherence to the rules of seniority, the Senate Finance Committee could have in Senator MILLER a first-rate teammate for Representative JOHN BYRNES, of Wisconsin, who will be the ranking Republican member of the House Ways and Means Committee next year.

Mr. DIRKSEN. Mr. President, in conjunction with the distinguished Senator from Iowa, I discussed this question with the chairman of the Finance Committee, the Senator from Virginia [Mr. BYRD]. I am not only hopeful, but encouraged by the fact that the distinguished Senator from Virginia will be quite willing to have some staff work done on this matter between now and the next session.

Mr. MILLER. I thank the Senator for his kind remarks. I have the assurance of the senior Senator from Virginia, Chairman of the Finance Committee, that he will turn this matter over to the staff of the Joint Committee on Internal Revenue Taxation for its study this fall. I welcome such a study. I wish it had been possible to have had a study before now. I wish it had been possible for my proposal to have been studied and presented after appropriate hearings so that it could have received the kind of consideration which I believe would have warranted its adoption by the Senate so that tax relief of a constructive form could begin at once. But this is a reasonable assurance, and I appreciate it.

Mr. DIRKSEN. It is a most engaging idea, and since it deals with incentive and with growth, certainly the plan merits real study.

Mr. MILLER. Mr. President, as indicated earlier, the chairman of the Finance Committee, the senior Senator from Virginia, has very graciously agreed to have this proposal referred to the staff of the Joint Committee on Internal Revenue Taxation for study. With that assurance, I withdraw my amendment.

The PRESIDING OFFICER. The amendment of the Senator from Iowa is withdrawn.

EXHIBIT 1

[From Fortune magazine, August 1962]

THE RIGHT KIND OF TAX CUT

On the lawn of any racetrack you can hear after the finish that "he" whipped the horse too much or too little, that "he" made his move too late or too soon, that "he" should have taken the animal inside instead of outside (or vice versa). All of this, though usually spoken in bitterness, is a tribute to the importance of jockeyship. But in many cases the tribute is exaggerated. As Ted Atkinson, speaking for all candid jockeys, once put it, "In racing the chief athlete is the horse."

We have not been spending the summer along the rail—the horsey metaphor was thrust upon us by the vocabulary of this summer's discussion of the financial news. It's amazing how often the word "spur," for instance, turned up, as in "Tax Cut Urged to Spur Economy." And as we go to press the administration is considering whether to present to Congress a tax-reduction bill of just that type.

We'd like to see a tax cut, and the sooner the better. But a quickie tax cut to last for only 1 year, say, a cut designed primarily to spur business during the next few months, isn't going to do any real good. What's needed is a permanent cut that rises out of the realization that the basic condition of the business system—the chief athlete—has been hurt by the size and shape of the present tax structure. A cut will increase this year's expected Federal budget deficit, which is as grave a concern to us as to any Congressman. Some advocates of a cut point out that the stimulation would generate enough business to offset the deficit. We can scarcely believe that it would have that immediate effect. But there is no reason to assume that our only long-range choice is between present tax levels and a succession of Federal deficits. Government expenditures can be reduced to a smaller proportion of national product, and indeed if a permanent tax cut is to make any sense they will have to be reduced. We have to begin cutting taxes sometime, and we can think of no better time than right now.

UNDERNOURISHED INVESTMENT

This summer's financial news, centering on the stock market drop, has been dramatic and suspenseful. But we will not understand the present situation if we isolate it from previous danger signals and disappointments in the economy. In 1960, for instance, when John F. Kennedy promised to "get this country moving again" he was assuming that the economy had bogged down. His proposed remedies involved a more active Government role in guiding and stimulating the economy. But the developments of 1962 suggest that some of the trouble may lie in what the Government is already doing.

The general health and spirit of business are both measured and affected by the level of profits. An article called "U.S. Business in Suspense" discusses how the present profit squeeze deprives business of funds needed for expansion and at the same time weakens the incentives for expansion. Among the main factors in the profit squeeze are the high level of Federal taxes and the way taxes are concentrated upon those parts of the economy that should produce investment funds. The U.S. economy's need for investment has not been adequately understood. We have maintained in the postwar period a level of gross capital formation that is more than 20 percent of gross national product. But most of this goes to offset the consumption of capital in the huge U.S. industrial plant. The significant change is in net capital formation—which represents growth. Until 1929 net capital formation ran above 10 percent of gross national product; in the postwar period it has been only about 6

percent. This change is one of the main reasons why incipient booms abort, why a high rate of unemployment persists, why the national growth rate has slowed down.

THE GREAT DEPRESSANT

When do taxes, which are never welcome, become really excessive? President Kennedy, who says he likes sophisticated economic arguments, can read plenty of them on the theoretical limits of tax capacity. Some economists believe that a tax burden that exceeds 25 percent of net national product will overload any economy. (The present take of Federal, State, and local taxes amounts to about 29 percent of the net national product.) Other theoreticians argue that the distribution of the tax load matters more than its total weight.

But the present U.S. tax structure is sponsored by no economic theory. It just grew out of a combination of crises, wars, emotional economics, and crude efforts to use the taxing power as an instrument of social justice. Long before the New Deal, an idea flourished that the inequalities of wealth could be leveled off somewhat by progressive taxes on incomes. In the depression, very heavy increases in these taxes were voted (contrary to all prevailing economic theories of recovery), partly in a spirit of vengeance against the rich and the business system. World War II acted as a kind of multiplier on these misconceived taxes. A couple of postwar tax cuts, then the Korean war tax boosts, then the modest Eisenhower cut of 1954—and that's the tax structure. Nobody designed it. Nobody takes credit for it. And hardly anybody defends it.

Such a tax setup has to be judged by experience rather than theory. But through most of the period of the present structure's existence its effects have been masked by inflation. In such a period rising values invite equity investment; business planners hasten expansion, believing that the cost will be higher for every year of delay. Experience in those years seemed to contradict those who had warned that the tax level would dry up investment. In 1955, Harvard's Prof. J. Keith Butters told a congressional committee he could find little evidence that the tax system had caused an under-supply of risk capital. But he went on to warn that "conclusions as to the extent to which the tax structure stifles the flow of risk capital during a period of high business activity cannot be applied without modification to a time of declining business activity and investor pessimism. * * * The tax structure would be far more repressive * * * in a declining period."

Indeed, it became far more repressive as soon as the upward price spiral flattened out in 1958. But the United States was slow to recognize that in the new situation the old taxes were having a much more serious impact on business. Federal expenditures continued to rise, and warnings on this point were met by the apparently practical argument that the same tax rates had not prevented prosperous years in the fifties.

Most of the tax-cut discussions of the spring and summer of 1962 have been proceeding on the unspoken assumption that Federal expenditures cannot be cut. But the present level of Federal expenditures is not forced upon us by some inexorable law of nature. True, defense expenditures are forced upon us, but the part of the Federal budget that has been rising most rapidly in the last decade has been the nondefense portion. "Needs" are unlimited. * * * If present Federal tax rates are left unchanged and the economy continues its recent slow rate of growth, the Federal Government in 1970 will be collecting about \$130 billion a year. Will it be able to spend that much? Foolish question. President Kennedy, just in his first months in office, proposed expenditures that, had Congress approved,

might have added an extra \$10 billion to expenditures now running around \$90 billion.

A 5-YEAR PLAN

As animals go, horses are pretty dumb. They don't know that the harder they try and the more they win, the heavier will be the weight the racing secretary puts on them the next time out. Even so, horses seem to get discouraged by high weights. Businessmen, who are less sophisticated than Harvard economists but not so dumb as horses, have been pervaded by the deadening prospect that the tax burden will go on and on. Every investment decision on a corporate agenda in the summer of 1962 must be considered under the depressing knowledge that it must struggle to pay for itself under a future tax burden that will weigh down upon the whole economy. This forbidding long-range prospect will have to be changed.

We don't know what, if anything, Congress will do about taxes before it adjourns this summer. A cut in the corporate income tax would be the most useful part of any immediate tax reduction. A cut from 52 percent to 47 would increase corporate earnings after taxes by 10 percent, encourage business investment, and benefit everybody. This would cost the Treasury about \$2.5 billion. An at least equal reduction in the personal income tax take would presumably be the political price of the corporate cut, and perhaps do the economy some good in the next few months. But neither corporate nor personal income tax cuts will accomplish anything at all if they are presented as momentary Federal largess for a momentarily faltering economy. Tax cuts, whether they come now or next January, must be made in such a way as to show that public policy has established a new level of what is considered a tolerable long-range tax burden. We favor cutting by installments, for example, spreading the cuts over a 5-year period (as in the Baker-Herlong bill). There is a very good chance that businessmen, realizing that they were investing for an economy with a decreasing tax burden, would begin immediately to make expansive decisions.

A lower level of tax rates (and Government expenditures) over a period of years should be accompanied by a thorough revision of the present tax structure. Many reforms are needed, but a change in the present emphasis on income taxes is surely one of them. Very few countries count so heavily on personal income taxes as does the United States—and only Great Britain has as high a corporate profits tax. This emphasis inhibits investment and distorts business decisions. But when tax consequences become a dominant factor in business decisions, the efficiency of the whole machine is impaired. We became so fascinated by the idea of taxes graded to ability to pay that we have reduced the economy's ability to progress.

An era of rapid scientific and technological progress offers opportunity that can be seized only by an abundance of capital, flexibly deployed. International competition in the years ahead may make this opportunity a rather grim necessity.

In April 1958, confronted with another of these chronic discouragements in the business outlook, *Fortune* said: "What the country needs most today is no flash-in-the-pan panaceas, and no panicky rush for purchasing-power hypodermics. What it needs is a restoration of normal incentives, acknowledgment of the basic role of profits in the system, and reassurance that the Government understands the true nature of a profit-and-loss economy."

We say it again.

[From the Wall Street Journal, Aug. 31, 1962]
DOWN ON THE LEVIES—PRESIDENT'S DRIVE FOR
TAX REFORM IS HOBLED BY LAWMAKERS'
CHANGING VIEW OF RATE CUTS

(By Robert D. Novak)

WASHINGTON.—The hoary maxim that Congress will swallow the most bitter tax reform schemes if they are sweetened enough by tax cuts may be ready for consignment to the scrap heap of outworn adages.

This is the long-range conclusion that may be drawn from Congress' remarkable reluctance to nibble at the tax reduction bait dangled this summer by President Kennedy. The summertime events pose this question: If the lawmakers this year disdained a straight tax cut with no strings attached, how can they be expected next year to embrace a tax cut encumbered by onerous revenue-producing reforms drawing fire from powerful lobbies?

And if the "sweetener" theory of tax reform must indeed be discarded, then the outlook for the Treasury's grand design of overhauling the tax structure before Mr. Kennedy faces reelection in 1964 must be changed from doubtful to pretty near impossible.

Not since those heady days when the New Frontier first opened in Washington some 18 months ago, has anybody regarded tax reform as anything but a grim and hazardous chore. The agonizing and still uncompleted task of guiding through Congress what they consider a minimal tax revision bill has been a sobering experience for Mr. Kennedy's bright young men at the Treasury, who once talked hopefully of Congress completing a full rewrite of the tax laws before the 1962 elections. Those old hands on Capitol Hill with previous experience in the jungles of tax legislation never had any illusions about the size of the task.

TOO RESTRICTED, TOO SMALL

But until this summer's abortive try for a quick tax cut, both the new faces at the Treasury and the veterans in Congress attributed much of the difficulty encountered by the 1961-62 tax revision bill to its lack of sweetening tax reduction provisions. The bill's proposed tax credit for businessmen who purchase certain kinds of equipment, it was reasoned, was too restricted, too small and too novel to win any widespread support from business. Far from serving as a sweetener to ease passage of the bill, the investment credit has proved more difficult to pass than most of the revision measure's revenue-producing provisions.

On the basis of this experience, the tax writers came to believe that the revision bill would have traveled a smoother road to passage had it included across-the-board cuts in personal and corporate income tax rates. Because the major reform bill next year will contain just such a tax cut plan, they concluded, its prospects for approval might be fairly good.

Treasury officials insist that this reasoning remains essentially valid. They point out with some accuracy that the possibility of a tax cut was raised so suddenly this summer, after the stock market decline, that public sentiment for it never had a chance to grow. Moreover, there was an understandable prejudice in Congress against a tax reduction presented as an emergency measure to stimulate the economy at a time when most lawmakers did not believe the economy was in such bad shape. Things will be different next year, say the Treasury men, when support for tax reduction has gone through more than 6 months of gestation and the cut will be advanced as part of orderly and permanent tax reform rather than as a temporary expedient.

APPARENT PUBLIC INDIFFERENCE

However, this reasoning tends to ignore some of the most interesting aspects of the recent debate over a quickie tax cut. A surprisingly large number of Congressmen showed they simply do not believe there is much political advantage to be had from cutting taxes in these days of wage withholding. What's more, the apparent public indifference to tax reduction is causing a reexamination of the political facts of life by those lawmakers who cling to the time-honored theory that a drop in income tax rates pays off on election day.

Barring a severe economic slump in the coming months, the mood on Capitol Hill next January, is likely to be mildly receptive to tax reduction—but not at any price. In other words, Congress is not apt to desire tax cuts so much that it will lower its guard against Mr. Kennedy's reform schemes.

The tax legislation dilemma confronting the administration comes into focus more clearly when talk of reform shifts from grand generalities to hard specifics. It's not easy to find anyone today willing to predict that tax reduction would induce Congress to accept any of the major reforms under consideration at the Treasury: Reduction of depletion allowances for oil and gas, limitations of the type of earnings that qualify as capital gains, cuts in tax deductions for interest payments or charitable contributions, reduction of the tax credit for retired persons—or even the pending proposal for tax withholding on dividend and interest income.

Moreover, the validity of the sweetener theory of passing tax reform bills has diminished, not only as a result of unexpected congressional apathy toward tax reduction, but also because of a change in the emphasis of the administration's plans for tax reform.

At the heart of the sweetener theory is the implied threat that the President would veto any tax reduction bill that has been stripped of his major revenue-producing reforms. But the administration has made clear in recent months that it regards across-the-board tax cuts not as merely a sweetener but as the most important ingredient of tax reform and a necessity for accelerated economic growth. Thus, the impression has grown in Congress that Mr. Kennedy gladly would accept a tax cut next year even if it included nary a revenue-producing feature.

THORNY PROBLEMS

The President strengthens this impression when he talks of passing a tax bill early next year with tax cuts retroactive to January 1, 1963. Even with unprecedented luck for the administration, Congress could not complete action on a comprehensive reform measure until sometime in 1964. Consequently, lawmakers seem justified in assuming that Mr. Kennedy really is talking about a simple tax cut for 1963.

But passage of such an unencumbered tax reduction bill poses problems not a great deal less thorny than those facing a comprehensive reform measure. Congressional hostility toward tax reduction this summer, stemmed in large part from fears by rank-and-file Democrats that voters would turn against Congressmen who deliberately voted to expand the Federal budget deficits through tax reduction. More important, this opposition to straight tax cuts in times of deficit spending, is found among the senior Democrats in Congress most influential in the tax legislation field.

Representative MILLS of Arkansas, the enigmatic Ways and Means Committee chairman, intimates in his customary delphic manner that tax reduction must be a part of a general reform measure and should not

result in a net revenue loss unless the Federal budget is balanced. The Senate Finance Committee's two top Democrats, Virginia's Senator BYRD and Oklahoma's Senator KERR, state their positions clearly: No net tax reduction while the Federal Government is running in the red.

KERR'S ROLE

But Senator KERR, whose support is absolutely necessary for any tax bill in the Senate, leaves a loophole. The Oklahoman suggests that he would support a 1963 tax reduction if accompanied by a cutback in Federal spending of around \$3 billion or more. Furthermore, the talk on Capitol Hill of a combined tax cut and spending cut no longer is confined to fiscal conservatives. "I'm afraid it's the only way we can get a tax cut bill," gloomily concedes a prominent liberal Senator.

Yet, Mr. Kennedy would have to perform the most spectacular philosophical somersault of his career to accept the Kerr formula. It would constitute a direct repudiation of the President's top economic counselors, who regard diminished Government spending during slack economic times as the height of folly and deflationary in nature. Even Treasury Secretary Dillon, one of the more conservative New Frontiersmen, has expounded this theory repeatedly in testimony before congressional committees.

Even if the President were tempted to consider the acrobatics, which is unlikely, the problem of just where to cut spending would remain. A slash in nondefense outlays would mean a tacit abandonment of some of the Kennedy administration's most cherished programs and policies. A reduction in defense expenditures would require an assessment by Mr. Kennedy that cold war tensions are easing—an unlikely assessment in view of the present world situation.

In truth, there is not now an obvious way for Mr. Kennedy to get any kind of tax bill—comprehensive or straight rate reduction—out of Congress next year. The forecast may be premature, but there is a growing belief that the mangled tax revision bill now limping along toward passage, may be the only general revenue measure passed by Congress during Mr. Kennedy's first term.

Consequently, Democratic politicians fear that if the President proclaims tax reform as his top legislative goal for 1963-64, he may be in for still another humiliating rebuff at the hands of Congress.

Mr. JAVITS. Mr. President, I send an amendment to the desk, on behalf of myself and the Senator from Minnesota [Mr. McCARTHY], and ask to have it stated.

The PRESIDING OFFICER. The amendment offered by the Senator from New York for himself and the Senator from Minnesota will be stated.

The LEGISLATIVE CLERK. It is proposed, on page 193, after line 22, to insert:

(g) CORPORATIONS INCORPORATED IN COUNTRIES OF THE EUROPEAN ECONOMIC COMMUNITY.—For purposes of subsections (d) and (e) of this section, a foreign corporation which is created or organized under the laws of a country of the European Economic Community shall be treated as being created or organized under the laws of each country of the European Economic Community. For purposes of the preceding sentence, the countries of the European Economic Community as of any date shall be those countries which on such date are agreed to achieve a common external tariff through the European Economic Community.

Mr. JAVITS. Mr. President, I sent the amendment to the desk on behalf of myself and the Senator from Minnesota [Mr. McCARTHY]. This is probably

the last chance which we shall have in respect of this bill to do anything about the new concept of taxation on corporations which have subsidiaries abroad and which are manufacturing and selling abroad. This is by all odds the minimal amount of relief which should be afforded in the interest of America's trade position. I would like to emphasize that.

What the amendment does is to provide that any corporation set up within the common market area is deemed to be a corporation of every country within that area and does not have to be separately incorporated in that country. This involves more than a mere saving of incorporation expense.

It would have tax implications. The scheme of the pending bill is to place a tax on a company when a foreign company sells through sales outlets in any country other than the country in which the product is manufactured. The tax consequences could be avoided, if the amendment were adopted, for a company which manufactured in the Common Market and sold in the Common Market, even though the company might set up sales outlets in the individual countries of the Common Market. That is the purport of the amendment.

There is a valid reason for the amendment. It is clear that one of the things which the Senator from Minnesota [Mr. McCARTHY] and I and other Senators have been pressing in the field of foreign corporate taxation is the competitive angle; that is, the fact that American corporations are now competing with corporations of other countries in an effort to sustain the export position of the United States. To sustain that position it is necessary for them to manufacture abroad. The corporation is taxed abroad. The bill would tax the same operations at home.

We have contended that competition is what makes it so difficult for the American corporation moving into those areas. The competition is nowhere more keen and nowhere more evident than in the European Common Market. If the Common Market treats itself as an economic unity, the proper question which we must ask, before we leave consideration of the pending bill—and that will be the end of the matter, so far as American companies which manufacture and sell abroad are concerned—is, "In order for American companies to compete, should we not treat the European Common Market as an entity?"

That is the opportunity which is afforded to the Senate by the amendment. As I say, it is a minimal amendment on the issue of competition, and should be agreed to.

After conferring with the Senator from Minnesota [Mr. McCARTHY] I have confined the amendment only to those two sections of the bill which relate to sales of articles which are manufactured, produced, grown or extracted—tangible personal property—and services, which are also covered by the bill, again when the services are sold. I have omitted the foreign holding companies, so as to avoid getting into the question of securities transactions, havens, and so on. We are dealing now with Ameri-

can corporations which actually are making goods or rendering services, and the freedom of their operations within the limitations of the new tax approach within the European Common Market.

Mr. President, this is a very serious matter. As I say, this is probably the last opportunity any of us will have to do anything in terms of trying to rationalize the picture of competition between American firms operating abroad and their foreign competitors.

If Senators will refer to page 79 of the committee report they will find how the new concept of taxation is applied. I quote from the second full paragraph on page 79 of the report, referring to U.S. corporations: "for their income from foreign sales subsidiaries which are separately incorporated from their manufacturing operations."

I ask Senators to look at page 84, under the heading, "Foreign Base Company Sales Income." The explanation at the top of the page is as follows:

Foreign base company sales income is income derived from the purchase and sale of personal property if the property is either purchased from a related person or sold to a related person.

That refers to the closeness of the relationship as between the U.S. corporation and its subsidiary. I continue the quotation:

However, this applies only where the property purchased is manufactured, produced, grown, or extracted outside of the country where the controlled foreign corporation is organized and the property also is sold for use, consumption or use outside of that country.

I ask Senators to refer to the language in the paragraph relating to foreign base company services income, in the last full paragraph on page 84:

As in the case of sales income, the purpose here is to deny tax deferral where a service subsidiary is separated from manufacturing or similar activities of a related corporation and organized in another country primarily to obtain a lower rate of tax for the service income.

The amendment would provide that if a service company or a sales company were organized in any one country within the European Common Market area—that is now six countries, but it may be a greater number as we go along—it shall be deemed to be a corporation of the same place as the corporation of manufacture, when that corporation is itself within the European Common Market area.

I emphasize that, because I wish to make it perfectly clear that tax consequences are envisaged by the amendment. It does not merely relate to the relatively slight expense of organizing a corporation. It would treat the whole Common Market area, as it were, as one country for the tax implications of the bill as it relates to foreign corporations, provided one is dealing only with operations which deal with manufacture or with services, and excluding the whole personal holding company concept.

In this connection, I refer to the statement which was introduced by our distinguished colleague who is in charge of the bill [Mr. KERR], which appears in

the CONGRESSIONAL RECORD for August 30, 1962. I refer to the memorandum explaining the view of the Treasury Department on the proposed Trade Expansion Act of 1962, which is now being considered by the Finance Committee. It explains with crystal clarity on the highest level of our Government the reason why I say—which I believe is completely supported by the statement—that the European economic community must be considered as a single market in which American companies must compete with other foreign producers who will be operating in that market.

American companies are going to be seriously disadvantaged by the tax consequences of the pending bill. This is an effort to reduce somewhat the extent of that disadvantage.

I wish to read from the memorandum prepared by the Secretary of the Treasury and sent to the Senate Finance Committee in respect to the proposed Trade Expansion Act of 1962:

As the domestic economy grows, American demand for imports will become greater. Despite our best efforts, outlays abroad for the national defense, aid, and investment will continue to be large. If these payments are to be met, the United States must export more. The necessary expansion of exports can occur only if, through negotiations, the doors to major foreign markets—and especially the new and expanding Common Market of Western Europe—are opened wider for U.S. products.

The six countries which formed the European Economic Community have now established their common external tariff, and are expected to bring it into full effect when their transitional period is over, at the latest by the end of 1969. Also, they are rapidly reducing the tariffs which apply to their trade with one another and are committed to eliminate them altogether by the end of 1969. The common agricultural policy, and the terms of continued association with newly independent countries which were formerly European colonies, are rapidly taking shape. The United Kingdom is expected to join the European Economic Community, and others may well follow. The resulting expanded Common Market will constitute a giant new economic unit within the free world.

I emphasize those words—

will constitute a giant new economic unit within the free world. If U.S. exports are to be expanded to the necessary extent, liberal access to the Common Market is absolutely essential.

Mr. BUSH. Mr. President, will the Senator yield?

Mr. JAVITS. I yield.

Mr. BUSH. I think the Senator makes an excellent case for the contention that we should recognize that the 6 countries—which may grow to 7, 8, 9, 10, or more, if the Outer Seven come in, eventually—are one unit from an economic standpoint, and from a trade standpoint.

I fail so far to grasp what are the tax implications of the Senator's amendment. So far as an American company owning a subsidiary abroad and operating in one of the Common Market countries is concerned, I understand that if it is operated in one, it is to be considered as though operating in all. It would be one for all and all for one,

under the Senator's amendment. What would be the tax effects, as they might affect such a company?

Mr. JAVITS. The tax effects would result if the income realized on sales, according to the bill, were realized from a corporation which was a sales company incorporated in the country other than the country in which the manufacturing of the subsidiary took place. For example, American corporation X might have a subsidiary which did manufacturing in France. It would sell in Italy through a sales corporation. The sales income then comes under the inhibitions of the bill in the sense that it is taxed immediately to the American stockholder, even though it is not actually received. That is the fundamental tax change made by the bill.

On the other hand, as to a sales company in France for an American corporation manufacturing through a subsidiary in France, there is no such tax consequence.

Therefore, the amendment would transform the whole Common Market area into a situation analogous to the one I have stated with respect to a subsidiary manufacturing in France and selling in France. That is the way in which the scheme of taxation in the bill is traced out. I have made the amendment, therefore, to apply both to a sales operation in which tangible goods are involved, and to the business of selling services—as, for example, an accounting firm or a company servicing various types of appliances and machinery, some other management service, or some other tangible operating servicing company. Those are the two types of companies to which I have applied the scheme as it relates to the integrated European Common Market. So the tax consequences would then not flow if the whole operation were conducted with the Common Market, as provided by the bill. The tax consequences, therefore, would be analogous to the situation in which the manufacturing and selling would take place in one country, which, as the bill is drafted, does not come under the particular tax applicability which is now established by the bill. That is the thrust of the amendment. The purpose of it is to do what we can to rectify the competitive situation as between other foreigners operating within the European Common Market and ourselves.

One final fact and I shall be through. I point out that business with the European Common Market is a critically important aspect of the American trade surplus. The same memorandum of Secretary Dillon to which I have referred shows that in 1961 we had a surplus in trade with the Common Market of \$1.3 billion, that is, we exported \$3½ billion; we imported \$2.2 billion. We had a surplus in agricultural goods of \$1.3 billion. Even in nonagricultural goods we had a surplus of \$400 million. That information comes directly from Secretary Dillon's memorandum.

This will grow in importance. The standard of living in the European Common Market is rapidly rising. Many American companies are finding it possible to move into the Common Market

with a part of their operations. The proposal would not result in an export of American jobs, in my opinion. I think that is a very fallacious position, because it has been demonstrated time and again in testimony before the Joint Economic Committee and many other committees that in the export of parts, management skills, and original machinery for the purpose of setting up branch plants abroad, the American economy prospers.

In addition, it is impossible to compete in terms of exports at all. Unless we engage in those operations we will lose material opportunities in the export market which we want.

In short, it is not a question of exporting our jobs or exporting our opportunity to export. It is a question of maintaining our competitive position in the field and improving and expanding that position by new techniques, in view of the fact that old techniques are being invalidated by competition and by such things as the European Common Market.

As I have said, I believe this is the last opportunity for us to do anything in respect to the bill. It is some effort to right the competitive situation which will be faced by more and more American companies abroad, especially as new trade legislation is passed. I am the first to state to Senators that participation by American business in the export field is very poor. It represents about 3,000 firms, about 5 percent of the total. One of our great problems is how to increase materially small business participation in the export field. Of course, it can be materially inhibited by adverse tax laws. One effort is being made in the amendment offered by the Senator from Minnesota [Mr. McCARTHY] and myself to equate and alleviate the risks of the new tax scheme—and it is new; it has not been done before—in dealing with a new entity, a new economic problem of competition in the European Common Market.

Mr. COOPER. Mr. President, will the Senator yield?

Mr. JAVITS. I yield.

Mr. COOPER. Am I correct when I say that the bill as reported by the committee would provide certain advantages in the way of tax consequences to a company which has a manufacturing plant in more than one country in Europe?

Mr. JAVITS. It would. If the company sells in the same place, it would find itself free of the new tax consequences in the bill.

Mr. COOPER. But it must be a manufacturing company, producing in each of the countries, or in more than one country.

Mr. JAVITS. Exactly.

Mr. COOPER. There would be some way of averaging the local taxes which would be charged against the company. Then, as the Senator has said, the thrust of his amendment would be to make that advantage available to a company which, say, had a manufacturing unit in one country and a sales unit in another country in the Common Market area.

Mr. JAVITS. Provided it was within the Common Market area. The Com-

mon Market area is treated as if it were one country.

Mr. COOPER. What is the basis of the Senator's argument that the sales company should be given the same advantage if it is acting for a manufacturing company, that is, a subsidiary of that company or its agent, as would be the situation under the committee bill in which it must be manufacturing in more than one country?

Mr. JAVITS. The argument is that the competitive area—in the present case the European Common Market—is not a single country. It is the whole European Common Market area. Therefore, we would be materially disadvantaged in the European Common Market area if we were to visit the consequences of the new tax scheme upon corporations operating within that area merely because they must engage in selling in the various countries of that area which fall under the new provisions of the bill. That is what my amendment is designed to avoid, if at all possible.

Mr. KERR. Mr. President, I rise to oppose the amendment of the Senator from New York. The Senator has said that the European Common Market is a single economic unit. That is true. But it is certainly not a single tax unit. The committee spent many weeks rewriting the foreign tax provisions, or the tax provisions with reference to foreign corporations domestically owned or controlled. The Senator's amendment would entirely destroy that part of the bill. The Senator's amendment would legalize tax havens to as great an extent as they are now legal under existing law. If the amendment of the Senator from New York were agreed to, the effort that has been made to discourage foreign tax havens would be nullified. His amendment would exempt from taxation under the bill dividends and income from one foreign corporation to another or to others in every country in the European economic union or Common Market, now 6 in number—perhaps soon to be 8, 10, or 12.

Mr. CAPEHART. What about the other countries?

Mr. KERR. Only as they would become members of the European economic union would the Senator's amendment apply.

One of the things the bill attempts to reach is the situation of a Swiss corporation acting as the sales agency perhaps for a corporation which someone in this country owns in Germany. It manufactures something there and makes a little profit on it in Germany. Then it sells its product cheap to a Swiss corporation, which in turn sells it anywhere around the world. The profit accumulates, and it is kept in the Swiss corporation and is not subject to American tax.

In view of the fact that Switzerland may probably become a member of the European Economic Union, or perhaps Liechtenstein or Monaco, which countries have no income tax whatever, under the Senator's amendment, if a corporation were a resident of Switzerland or Monaco or Liechtenstein, it would have the privilege under the amendment

of selling anything manufactured anywhere in the world in the European Economic Union, make its profit, and keep the profit free from taxation under our laws or under the pending bill.

In other words, the choice is between legislation which would correct the present abuses of tax havens and the Senator's amendment, because if we adopt the Senator's amendment we destroy the provisions of the bill calculated to eliminate tax havens.

As the House passed the bill, it did two things, as the Senator from Tennessee has so often said on the floor of the Senate. First, it eliminated tax havens. Second, it taxed deferred income of foreign corporations as it was earned before it was brought back to this country. The committee took that provision out of the bill. The committee acted on the theory that earnings should be taxed when put into the hands of the taxpayer, not while they are still in the hands of the corporation in which the taxpayer owns stock, and which have not yet been declared by the corporation to the stockholders.

We thought that was not a reasonable provision in the House bill, and we took it out of the bill. However, we maintain the provisions of the bill—I will say on a much more liberal basis than the House provision—with reference to the elimination of the tax havens. The Senator's amendment would eliminate all that the committee did to stop tax havens. Since the committee adopted the House provisions with reference to taxing deferred income, if the Senator's amendment is adopted there will be no purpose whatever, as I see it, for the bill.

Mr. McCARTHY. Mr. President, will the Senator yield?

Mr. KERR. I yield.

Mr. McCARTHY. I believe that the Senator from Oklahoma and the Senator from New York have stated the situation correctly. The Senator from New York believes, as I do, that it would be a good thing for us to be within the European Economic Union for the purpose of competing in that area. The committee bill places handicaps in the way of effective competition, as we see it. It is the opinion of the Senator from New York, which is shared by me, that both our balance of payments and the stimulation of the economy, including the increase in employment, would be helped by our being active in that competitive market.

The Senator from Oklahoma is quite correct in saying that the action of the committee does not interfere with or hamper the action of American firms in that area. We could departmentalize the provisions as between the various countries, and thus put ourselves at a great disadvantage, to the extent that the firms over there would be in competition with goods produced in the United States, but such competition means very little; on the other hand, it would put them at a great disadvantage in competition with European producers, who compete with them most strongly and most actively in that area.

Switzerland is not now a part of the European Economic Community. In the years to come it may become a member,

but at the present time it is not. The Swiss subsidiaries are not used primarily for avoiding the payment of taxes. The Swiss corporations are usually used as a device by which American firms doing business in other European countries are able to take the income out of higher tax countries and put them into a low tax country. Instead of paying high taxes, they use Switzerland, where the tax rate is lower. When the money is repatriated, they pay more taxes to the United States than they otherwise would if they had no Swiss subsidiary.

Mr. KERR. The Senate very decisively defeated the unreasonable accumulated tax substitute offered by the Senator from Minnesota with reference to the operation of the Common Market as it is now or as it may become. The amendment of the Senator from New York is far looser, or goes more in the direction of tax havens than did the amendment of the Senator from Minnesota. The adoption of the amendment would create an irresistible magnet in the most highly developed industrial area in the world outside of our own, for American capital to be used in building industrial competitive facilities for trade and commerce over there in competition with the trade and commerce that is sought to be built here.

The Senator's amendment would create an irresistible magnet for the exportation of American capital, American business, and American jobs, because insofar as the European Economic Union is concerned, their operations would be practically free so far as they continued to invest money. If they could have it free from taxation by this Government, they would do so.

The highly developed industrial area of Western Europe is the place where that is needed least of all.

We made provision in the bill for certain exemptions with reference to expansion of American-owned industry in undeveloped areas, because in so doing we bring about a situation in which we encourage the exportation of American products for the development of those economies. We believe it is needed there.

However, the Senator's amendment would make that provision available where it is needed least, where the industrialization practically equals our own.

Therefore, it would carry forward not only the abuses now in the law with reference to tax haven exemptions, which are sought to be corrected by the proposed legislation, but it would also do so in a manner calculated to be most effective in siphoning off American business for investment over there and siphoning off jobs which otherwise would be created or maintained in American industries, to give those jobs to workers abroad and provide an ever-stronger industrial complex there to compete with us in the markets of the world, and with our own domestic industry for the domestic market here.

Mr. JAVITS. Mr. President, I believe the Senator from Oklahoma, who is a very eloquent man, has obviously let his eloquence run away with him, and has completely overlooked the facts. I

should like to make clear what I am talking about in that regard. The Senator says that if my amendment, in which the Senator from Minnesota joins, were adopted, certain corporations would be free from tax. That is not correct. They would not be free from tax. Their tax status would be the same as it is now, not as changed by the bill, but the same as it is now. Whenever they repatriated any capital, they would pay taxes to the United States, just as they are paying them now.

Mr. KERR. Mr. President, will the Senator from New York yield?

Mr. JAVITS. I yield.

Mr. KERR. What does a corporation in Switzerland pay in taxes to this country?

Mr. JAVITS. I said when the capital was repatriated. We are talking only about American companies which have subsidiaries and sales corporations abroad. We are not talking about Swiss companies. We cannot tax such companies unless they have a relationship to American companies. The Senator had argued that under this amendment such corporations would be "free of tax."

Mr. KERR. The Senator from Oklahoma said that if and when Switzerland or Liechtenstein or Monaco came into the Common Market, and one of the sales corporations was located in one of those countries, it would pay practically no tax where it was located; and under the Senator's amendment, as under existing law, would not owe any tax here until and unless it saw fit to take out its capital and bring it here.

Mr. JAVITS. The Senator from Oklahoma did not add that phrase until now: "until and unless they saw fit to take it out and bring it home." Then they would have to pay a tax.

Mr. KERR. That is according to existing law.

Mr. JAVITS. That is what the Senator from New York has been talking about.

Mr. KERR. The Senator is trying to amend the existing law by his amendment.

Mr. JAVITS. As to those corporations which are in the condition that I have described.

One further point: Switzerland and other low-tax countries are not now in the Common Market. So the Common Market is now composed of highly industrialized countries which have rather important tax structures of their own.

But beyond that, I think the fundamental point on which I would differ very sharply—and the whole administration differs with it—is that investments by American corporations which manufacture in the European Common Market represent an export of our jobs. If the Senator from Oklahoma would argue that when the trade bill is before the Senate, the Senator would be dead set against the trade bill, because the whole thrust of the trade bill is designed to encourage precisely this kind of freedom of operation on the part of American corporations.

What my amendment tries to accomplish is to retain competitively this free-

dom of operation for them, which, I would tell the Senator, with just as much vigor as he has just used, will be destroyed—the competitive position of American corporations will be absolutely destroyed—by the disadvantage imposed upon them by the artificial operations of this bill in this very respect toward the European Common Market, as the bill treats the European Common Market, as six separate countries and gives tax status as it relates to six separate countries.

Is there anything in the bill which would impose the kind of tax that the Senator wishes to impose upon these corporations, on American corporations with subsidiaries and sales companies in one country in the European Common Market—France or Germany? Is it not true that this bill expressly excludes such corporation from the tax treatment under the bill?

Mr. KERR. In this bill, at page 189, if Senators wish to turn their attention to it, line 13, the language reads:

(4) CERTAIN INCOME RECEIVED FROM RELATED PERSONS.—For purposes of paragraph (1), foreign personal holding company incomes does not include—

(A) dividends and interest received from a related person which (i) is organized under the laws of the same foreign country under the laws of which the controlled foreign corporation is created or organized, and (ii) has a substantial part of its assets used in its trade or business located in such same foreign country.

That provision is in the bill, subject to certain limitations, to give this privilege to foreign personal holding companies if they are in the same country where the controlled foreign corporations are created or organized. Under the bill, all the European Community would be regarded as one country, so that if the holding company were organized in Italy, which I think has a 30-percent rate, or Switzerland, it could come into the Common Market, which has none. Then the corporation could have companies in everyone of the Common Market countries and get the benefit of this provision, which exempts dividends and interest received from a related person, that is, which is organized under the laws of the same foreign country. For the purposes of the bill, the amendment would make the entire Economic Community, as it now is or may become, one country, thereby establishing this benefit to a holding company in Switzerland, if it were there, or any other countries, with reference to all the companies it operated in the entire Economic Community.

Mr. JAVITS. I gather that the manager of the bill concedes that I am right as to one concept, that I do not include in my amendment foreign personal holding companies. If the Senator will examine the amendment, he will see that it relates to foreign business and foreign business service companies, not to holding companies. That is why I do not believe the aspersions—

Mr. KERR. A foreign service company is what is called a foreign holding company.

Mr. JAVITS. But the Senator from

Oklahoma was reading from a section of the bill which my amendment does not affect.

Mr. KERR. But the section of the amendment which the Senator from Oklahoma read would be applicable if the amendment of the Senator from New York became a part of the bill.

Mr. JAVITS. I am sorry; it would not, because my amendment affects subsections (d) and (e), and then it would include material the Senator read from page 189. I sought to exclude specifically holding companies subject to tax and holding company tax havens. That is precisely what is included.

I understood the argument which would be made on the other side. I do not feel, in all fairness, that it ought to be made with respect to what I was trying to accomplish—the same opportunities for American companies which are going to be operating in this field, in accordance with the enlightened concepts of trying to compete on terms of equality with the British, the French, the Germans, and all others who operate in those markets. The bill would very materially disadvantage such companies. That is the correction which the Senator from Minnesota [Mr. McCARTHY] and I, at the very last stages of the debate on the bill, are still trying to make. If we cannot, we cannot. But we still have the right to try.

With all respect to the Senator from Oklahoma, I still do not believe we should be subjected to the charge that we are trying to maintain tax havens and tax avoiders when we have designed an amendment expressly to exclude the personal holding companies which are referred to on pages 183 and 189 of the bill.

If the amendment included Switzerland, the Senate would be at perfect liberty to repeal this provision. But now we are talking only about the six Common Market countries and about American corporations seeking to operate there in the interests of our own export trade in competition with the companies which are not subjected to that which the bill will subject American companies in terms of their income from those operations. That is the fundamental point and the fundamental reason for our position.

I do not feel, in all honesty and fairness, that our position justifies the general assertion that we are trying to sweep back into the bill tax havens and all the other things which are complained of.

Mr. McCARTHY. I think it is significant—and the Record ought to show it—to note what the foreign rates of income tax are in most countries, and what they are in the European Economic Community.

The committee amendment provides that if foreign holding income taxes are in excess of 47 percent, no repatriation is called for. If they are 52 percent, or approximately that, we collect any taxes in excess.

But these are the foreign income taxes, including State and local taxes, chargeable against U.S. taxes:

Austria, 52 percent; Belgium, 28.5 percent; Denmark, 44 percent; Finland, 50 percent; France, 50 percent; Germany, 38 percent; I understand it is now up to 51 percent; Great Britain, 53.75 percent; Ireland, 40 percent; Italy, 37 percent; the Netherlands, 47 percent; Norway, 59 percent; Spain, 37 percent; Sweden, 48 percent; Switzerland, 33 percent.

The reason why American companies operating overseas establish Swiss subsidiaries is to escape paying high taxes, up to 47 percent or 50 percent, or 48 percent in some other country. They move their subsidiaries into a 33-percent country. Then when they repatriate them from that country, we have an opportunity to collect 52 percent, or at least to impose our tax as opposed to the 33-percent tax paid in Switzerland.

So the amendment, it seems to me, could do nothing but help.

Mr. JAVITS. I thank the Senator from Minnesota. I should like to conclude my remarks on this point, because, notwithstanding the importance of the tax sections, this point is more important than anything we have been discussing in the way of taxes. In connection with the trade bill, the fallacious argument will be made that foreign countries in the establishment of American manufacturing facilities somehow brings about the "exporting of jobs." I predict, that if that is the concept on which the Senate will vote on the trade bill and other policy bills, American economic power and influence will atrophy, and American exports will diminish very materially, and we shall be unable to maintain our position in the world. Such a concept reminds one of a general who, when confronted with an overwhelming force, goes about his defense by keeping all his troops in his castle. In such a situation, a sortie is essential. And a sortie is essential both in economics and in war.

It is most important that there be widespread realization of the importance of the true concept in this connection. But, I say, with all respect, that the President has loosely used the concept of "exporting jobs by means of making American investments abroad."

Mr. President, we shall not be able to maintain our freedom or sustain the American economy unless we learn that if we are to maintain the power which we must maintain if we are to survive and if freedom is to survive, we must move out into the world. That is essential if we are to do the economic job which needs to be done.

Arguments based on statements about "exporting jobs" deal with a subject which cannot be separated from the economic policy of the Nation, and are symptomatic of the general climate of thinking.

Even if this amendment does not succeed, I am very glad we have had this debate, because it is most important to put an end to the idea that if an American-owned factory is established abroad, it cuts down the American economy. On the contrary, that is the only way by which we shall survive and keep our com-

petitive position in the world and expand our economy and make possible the employment of our people and maintain freedom in the world—by manifesting our capabilities everywhere, not merely in the United States.

So, Mr. President, based upon this concept of competition, I hope the Senate will see fit to adopt the amendment.

The PRESIDING OFFICER. The question is on agreeing to the amendment offered by the Senator from New York [Mr. JAVITS], for himself and the Senator from Minnesota [Mr. McCARTHY].

Mr. KERR. Mr. President, I am glad the Senator from New York mentioned the trade bill. If the trade bill has justification, it is as a means of providing the opportunity for American corporations in the United States to compete with corporations in other countries for the domestic market here and for the domestic markets in the other countries and in the world. There would be no purpose in passing a bill to promote trade if we could not expect, as a result, more exports from this country to other countries and more sales by our industries at home to our domestic customers.

What the Senator from New York is seeking to do is to strengthen the competitors in the European Economic Union against American-based and American-located industries. Otherwise, why offer the amendment? Otherwise, why offer an amendment of this sort?

The Senator has reminded me that the amendment applies only to "(d) Foreign Base Company Sales Income," on page 190, and "(e) Foreign Base Company Services Income," on page 192. But that was inked into the amendment after it was written, and I did not know the Senator had thus limited the amendment.

But I call the attention of Senators to "(d)" and "(e)". "(d)" refers to "Foreign Base Company Sales Income," and relates to a foreign-based company and its sales, through a subsidiary, of goods or property; and "(e)" relates to "Foreign Base Company Services Income."

So in the final analysis, whether we call it a foreign holding company or a foreign-based service company or a foreign-based sales company, the net result is the same, and the treatment under the bill is the same. The bill is now limited to a single company; but the amendment of the Senator from New York would make it available to the entire European Economic Union as it now is or as it may become, by reason of the fact that the Senator from New York says it shall be treated as one country.

There can be no purpose for his amendment if it is not to permit American finances and American funds to be used to build American-owned and American-operated industries in the European Economic Community, and provide them—under the provisions of the amendment of the Senator from New York—with a tax haven. If the amendment does not do that, it has no purpose. I submit that is what it does do; and when it does it, it brings about the result of the exporting of American dol-

lars and the exporting of American jobs. Therefore, the amendment should be defeated.

Mr. JAVITS. Mr. President, I think the Senator has now conceded the main point, which is that as long as it is done in one country, it is proper under this bill; and my concept is that if it is done in the European Economic Market, it is done in one country, because the European Economic Community is an economic entity.

But my point is that this amendment is necessary in the interest of American companies which employ millions of persons and have thousands of stockholders and have companies operating in the European economic area. That is the point of the amendment; and it deals with one of the great concerns of American business generally in connection with this entire matter.

Mr. KERR. Mr. President, the provision of the bill with reference to companies in the same country is included because in one country such companies receive the same tax treatment. But if we provide that the European Economic Union is one country, for purposes of this bill, we do so for an American corporation, although it is not done in that country. These countries do not have one tax treatment for all companies. There is separate tax treatment for companies in each of these countries. It is one economic union, yes; but it is not one tax union and it is not a common tax union. But that would be the result of the amendment of the Senator from New York.

Mr. JAVITS. Mr. President, I suggest the absence of a quorum.

The PRESIDING OFFICER (Mr. MILLER in the chair). The clerk will call the roll.

The legislative clerk proceeded to call the roll.

Mr. JAVITS. Mr. President, I ask unanimous consent that the proceedings under the quorum call be suspended.

The PRESIDING OFFICER. Without objection, it is so ordered.

Mr. JAVITS. Mr. President, on the amendment which I offered on behalf of the Senator from Minnesota [Mr. McCARTHY] and myself, I ask for a division.

On a division, the amendment was rejected.

Mr. KERR. Mr. President, I move that the vote by which the amendment was rejected be reconsidered.

Mr. HILL. Mr. President, I move to lay that motion on the table.

The motion to lay on the table was agreed to.

Mr. FULBRIGHT. Mr. President, on behalf of the Senator from Minnesota [Mr. McCARTHY] and myself, I offer amendments identified as "8-28-62-G."

The PRESIDING OFFICER. The amendments offered by the Senator from Arkansas for himself and the Senator from Minnesota, will be stated.

The LEGISLATIVE CLERK. It is proposed on page 208, line 10, insert the following new paragraph:

(d) CORPORATIONS ENGAGED IN PRODUCING OR SELLING BOOKS OR OTHER MEDIA OF COMMUNICATIONS WHICH ARE EDUCATIONAL, SCIENTIFIC, CULTURAL, OR INFORMATIONAL IN NATURE.—For purposes of this subpart, the term "controlled foreign corporation" does not include any corporation with respect to which 80 percent or more of its gross income for the 3-year period immediately preceding the close of the taxable year (or for such part of such period immediately preceding the close of such taxable year as may be applicable) was derived from the production or sale of books, including textbooks, educational and scientific books and journals, and encyclopedias, and other media of communications which, under regulations prescribed by the Secretary or his delegate, are deemed to be educational, scientific, cultural, or informational in nature. For purposes of determining income from the production or sale of such books and such other media of communications, dividends and interest from a corporation which is excluded from the definition of "controlled foreign corporation" solely by reason of this subsection shall be deemed to be income from the production or sale of such books and such other media of communications.

On page 208, line 11, strike out "(d)" and insert in lieu thereof "(e)".

Mr. FULBRIGHT. Mr. President, I ask unanimous consent that my statement explaining the amendments be inserted in the RECORD.

There being no objection, the statement was ordered to be printed in the RECORD, as follows:

STATEMENT BY SENATOR FULBRIGHT

Members of the Senate who have traveled widely in the past several years will know how in every country in the world—in developed as well as underdeveloped countries, in scores of languages, and by the tens of millions—inexpensive copies of Soviet books are for sale everywhere, often on newsstands. These books are subsidized by the Soviet Union and by local Communist parties. In 1961, according to the USIA, more than 150 million copies of subsidized low-priced Soviet books, translated into free world languages, were produced for distribution in non-Communist countries. About 90 percent of these were printed in German, English, French, or Spanish. They are part of what Professor Baarghorn, of Yale, calls the Soviet cultural offensive. They are frontline weapons in the battle for men's minds.

No doubt the Soviets would be glad to give these books away—were it not for the fact that men tend to put more value on things they pay for—even if it is only a token payment. We in the United States, far from subsidizing the sale of our books abroad, are in danger of hamstringing our American publishers who seek to sell their books and their educational materials abroad. Our book publishers have found their markets abroad widening. They have been learning to sell in those markets. Last year they sold \$90 million worth of American books to foreign purchasers. This represents an increase in recent years of 10 percent a year.

The American Book Publishers Council, and the American Textbook Publishers Institute, which represent concerns doing 90 percent of the book business in the United States, have expressed concern that the Treasury's proposals about taxation of foreign subsidiaries will hamper their expansion—and may tie the hands of our publishers as they explore new and better ways to project to foreign peoples the best products of America's brainpower.

These two associations have proposed that books and other educational, scientific, cultural, and informational mediums be ex-

empted from the effect of proposed new statutes governing taxation of controlled foreign corporations. They point out that there are many precedents for giving books a special status. This special status is implicit in the Smith-Mundt Act, creating the U.S. Information program, which is now supported by appropriations of more than \$100 million a year. Because USIA libraries could not possibly secure adequate distribution abroad of U.S. books and periodicals, the Congress 10 years ago created an information medium guarantee program backed by appropriations of as much as \$10 million a year, to help publishers and others with their currency-conversion problems; this program still functions in certain countries in which normal sales are not possible. Under the AID and Alliance for Progress programs, great emphasis is being placed on the development of education as an important requisite for economic progress. Still another example of the special role books and other cultural materials are recognized to play in modern foreign relations is the Florence agreement, a treaty approved by the Senate which exempts such educational materials from tariffs.

I have asked Edward Murrow, Director of the U.S. Information Agency, to comment on the proposed exemption of books and other media of information. Here is his statement:

"We believe that the objectives of the U.S. Information Agency overseas will be aided if the receipts from publication or sale of books or other media of communication of an educational, scientific or cultural nature by American companies overseas which are reinvested for expansion of such activities overseas are excepted from the new provisions proposed to be included in section 957 of the Internal Revenue Code through passage of the pending revenue bill. Wider distribution of such American books and other media of communication overseas is important to the advancement of international understanding, and we are aware that the principal American companies involved are expanding their distribution now and may be expected to continue to do so if taxation does not make the financing of such expanded distribution difficult and unprofitable."

I need not remind the Senate that no question of tax forgiveness is involved in such an exemption. Earnings would be taxable in the United States, as they are now, when they are remitted to the parent company. Indeed, if the hopes and expectations of the publishers are realized, the taxable revenue accruing to the Treasury presently may be substantially larger than this would be in the absence of the exemption. Nor is there a question here of perpetuating tax havens, in the sense of refuges for earnings of American companies abroad which cannot be reached by the Treasury; the earnings are reinvested until they come home, presumably enlarged, to be shared with the Treasury.

One American publisher—his company is one of the biggest publishing houses in the world—says this:

"We are just beginning to learn how to distribute our books and other educational materials abroad. I fear that, if section 12 of the new revenue bill is adopted in its present form, we may have to pull out of some of the so-called developed countries where we have begun to expand, and to abandon other expansion projects abroad."

"Our principal product is sets of books, but we also sell other books and educational programs as well. We are developing new products of great potential importance, for example the so-called teaching machine, which is actually a superior form of textbook. My people tell me it may be possible, through such new techniques, to teach

English to tens of millions abroad for a little as \$3 a student.

"We are learning how to sell these books by American methods abroad (including in countries where English is not the dominant language) and this means we sell sets of books on the installment plan with the purchasers having 2 years or more to pay. This immediately complicates our problem of financing. We deliver the sets of books when they are ordered, and we pay commissions and maintain our offices abroad, but we don't begin to show cash earnings until the sale of a set until after most of the monthly payments have been made—no until the last few payments. This means we are faced with an expensive problem of financing. The only practicable way for us to handle this financing is to use the earnings of an established foreign subsidiary before U.S. taxes, to finance the development of a newer subsidiary."

This publisher's company has been expanding explosively both at home and abroad. Expansion has been financed by borrowings, against accounts receivable, now totaling some \$60 million, of which about one-third is due to foreign expansion. Partly because foreign financial institutions are not accustomed to loaning money secured by installment accounts receivable, interest rates paid by this company and its foreign subsidiaries are in some cases as high as 12 percent—and this, of course, puts a brake on expansion.

For a simple and logical reason this company places major reliance on its wholly owned Canadian subsidiary to help finance new foreign expansion. The American company and its various foreign subsidiaries have been borrowing for expansion up to the prudent limit of their capabilities and logical reason for placing major reliance on the Canadian company is that under Canadian law, the earnings of foreign subsidiaries of Canadian corporations are not subject to Canadian tax. Thus the Canadian subsidiary of this American company can borrow money for the company's foreign expansion and can service this debt with the earnings of the new companies in other foreign countries which are its subsidiaries. The larger this income, the greater the expansion.

Again for logical reasons the Canadian subsidiary of this American company seeks to take advantage of whatever legitimate and legal opportunities exist in foreign tax laws which will maximize its foreign earnings and thus increase its borrowing capacity.

I do not pretend to understand fully the economics of the foreign distribution of American publishing companies. I do not know how many other U.S. publishers have problems similar to those of the company I have cited; and we must, of course, assume that if its formula is successful other companies will follow suit.

I do not know if the Treasury would take such a myopic view of what constitutes a tax haven as to bracket this company's practices within its new rules and regulations—even though what is involved is obviously a network of conduits for American ideas and American influence—and not a sequestered haven or shelter.

I do know that the company I have cited is definite in its statement that it will have to curtail some of its foreign expansion projects, and abandon others, if the present language of the bill is approved without further amendment or exemption.

For myself, I must say that the ability of the United States to do justice to itself in the intellectual cold war that is shaking the world is so central to our security that I would favor outright subsidies for our books and informational media if that became necessary. Fortunately, that is not necessary here. Our American publishers are asking here only for the right to continue expanding their sales abroad under the conditions that

have prevailed up to now. The cost of allowing them to do so—if indeed there is any cost—is tiny measured against the stakes.

The Treasury is properly concerned with achieving good and sound tax practice. I suggest our responsibility here in this Chamber is much broader. We are responsible for the national welfare and the national security. Our security overrides all other considerations. That is why I have risen to offer the amendment proposed by the junior Senator from Minnesota.

Mr. FULBRIGHT. Mr. President, the amendment seeks to overcome a conflict in our overall national policy. On the one hand, there is a tax policy which, under the bill, would discourage the publication in foreign countries of books, and especially of educational material designed to teach English, and, on the other hand, we are subsidizing, or paying to do this very thing, through the USIA and other agencies of government.

The amendment would apply only to book-publishing companies—of which there are two principal ones—which are engaged in private enterprise in an effort to make available facilities for the teaching of English and books in English.

I believe that is entirely in accord with the national interest and policy of the Federal Government in promoting throughout the world the greater use of English, the understanding of the language, the reading of books, and so on, for the purpose of creating better relations between this country and other countries.

I believe that, in a sense, there is an inadvertent conflict of the law that would apply to book-publishing companies. I hope the Senator from Oklahoma will agree to accept the amendment.

Mr. KERR. Mr. President, I cannot agree to accept the amendment, but I understand that the USIA and the State Department favor the proposal.

I have been seeking an expression from the Treasury, and early this afternoon I received from the Treasury this assurance: First, that we could provide in the conference language which would accomplish the purpose the Senator has in mind. The Treasury has further assured me that it will attempt to do just that.

In the opinion of the Senator from Oklahoma, in conference, we can attain, within the purview of the language of the two versions of the bill, the objective the Senator from Arkansas has in mind.

Mr. FULBRIGHT. I thank the Senator very much. I realize that it is difficult to adjust these technical matters on the floor of the Senate.

I assure him that within the statement which I have placed in the RECORD, I quoted Mr. Edward Murrow, Director of the U.S. Information Agency, in support of the amendment.

The Senator from Oklahoma is quite correct in his statement about the attitude of the Department of State and the USIA.

With that assurance, I will not press the amendment, because I realize that the hour is late, and I do not wish to belabor it.

Mr. KERR. The objective will not be accomplished in the language of the amendment. If it were, I would recommend accepting the amendment. Technically, the Treasury thinks this purpose can be achieved in different language, and it will cooperate in doing so.

Mr. FULBRIGHT. I thank the Senator. I understand that in the particular activity of publishing books which we foster in other areas of our Government policy, no inhibition would arise under the present language of the bill; but the technical way to arrive at a conclusion is that the Senator will try to reach an agreement, and the Treasury believes it can be done.

Mr. KERR. The Treasury representatives have said they could, and that they will cooperate in doing so.

Mr. FULBRIGHT. I withdraw the amendment.

Mr. DOUGLAS and Mr. LAUSCHE rose.

The PRESIDING OFFICER. The Senator from Illinois.

Mr. KERR. Mr. President, I wonder if the Senator will yield 5 minutes to the Senator from Colorado [Mr. ALLOTT] to offer an amendment?

Mr. LAUSCHE. Mr. President, I do not know whether I am within the rules, but my name has been on the list at the desk, and it preceded that of the Senator from Arkansas.

Mr. KERR. Mr. President, I withdraw the request.

Mr. LAUSCHE. I do not know how I have been relegated to the position to follow—

Mr. DOUGLAS. Mr. President, I shall be glad to yield the floor to allow other Senators to present their views.

The PRESIDING OFFICER. The Chair is following the designations on the list at the desk.

Mr. LAUSCHE. The designation shows my name preceding that of the Senator from Arkansas. Some numerals were added. I do not know how that was done.

I yield to the Senator from Colorado.

Mr. ALLOTT. Mr. President, I ask unanimous consent that I may have 4 minutes within which to propose certain amendments, without the Senator from Ohio losing the floor.

The PRESIDING OFFICER. Without objection, it is so ordered.

Mr. ALLOTT. Mr. President, I send to the desk amendments, and ask unanimous consent that the reading of the amendments be dispensed with and that the amendments be printed in the RECORD.

The PRESIDING OFFICER. Without objection, it is so ordered.

The amendments offered by Mr. ALLOTT are as follows:

On page 391, between lines 21 and 22, insert the following new section:

"SEC. 127. MEDICAL CARE COVERED BY INSURANCE TO BE DISREGARDED IN DETERMINING WHETHER AN INDIVIDUAL IS A DEPENDENT OF TAXPAYER.

"(a) IN GENERAL.—Section 152 (relating to definition of dependent) is amended by adding at the end thereof the following new subsection:

"(e) MEDICAL CARE COVERED BY INSURANCE TO BE DISREGARDED.—For the purposes of subsection (a), medical care for an individual which is provided, or the expenses of which are paid, under an insurance plan, policy, or program shall not be taken into account in determining whether such individual received more than half of his support from the taxpayer."

"(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to taxable years beginning after December 31, 1959."

On page 391, line 22, strike out "27" and insert in lieu thereof "28".

Mr. ALLOTT. Mr. President, this proposal can be presented very briefly. I think it can best be shown by reading a paragraph from a letter I received from the Internal Revenue Service:

Information furnished this office is that the total cost of Mrs. Tyrrell's support for the year was \$2,479.23. Of this amount, Mr. and Mrs. Swanson furnished \$780.76; Mrs. Ted Hunt, Mrs. Tyrrell's daughter, furnished \$266.67; Mrs. Tyrrell furnished \$50 from her own funds; and the balance of \$1,381.80 was furnished by the Scottish Union & National Island Marine Insurance Co.

The sole question to be resolved is this: Mr. Herbert W. Swanson, who claims the woman as a dependent, supported her for 11 months out of the year. She fell and broke her hip, and because of the money the Scottish Union & National Island Marine Insurance Co. paid in the way of hospitalization and health insurance, the amount it paid amounted to more than that which had been contributed to her support for the year.

The Internal Revenue Service has said that their interpretation of the regulations is that such funds, taxable or otherwise, if used, must be considered in determining whether or not Mr. and Mrs. Swanson furnished more than half the support of the dependent.

This question has been discussed with the senior Senator from Oklahoma, who is in charge of the consideration of the bill, and it has been discussed with those connected with the Internal Revenue Service. I am informed it is believed the problem should be handled administratively. If it is not handled administratively certainly it should be handled by approval of the amendment, because certainly it was never the congressional intent that taxpayers who support dependents for more than half the year, providing normal support, should be deprived of the allowance for a dependent because an accident caused insurance payments to be made in behalf of the dependent.

I should like to ask the senior Senator from Oklahoma for his comments in this regard.

Mr. KERR. Does the Senator have available a copy of his amendment?

Mr. ALLOTT. The amendment is at the desk.

Mr. President, it is my intention later to withdraw the amendment, if we can clear this up administratively, which I think we can.

Mr. KERR. Mr. President, I agree with the Senator from Colorado. In my judgment, this is a matter which can be handled administratively. I have submitted it to a representative of the Treasury Department. While he did

not authorize me to say it would be so handled, he authorized me to say that was his opinion and that he would endeavor to have it done that way.

I hope the Senator will give me an opportunity to attempt to reach an adjustment. If it cannot be done, when another tax bill is before us, I will favor his amendment.

Mr. ALLOTT. I appreciate that expression, Mr. President. Certainly I do not believe the law was ever intended to work in this way. The regulation has been interpreted in an arbitrary manner.

Since I have the assurance from the Senator that he will do all he can, I will do what I can, and I hope the situation can be taken care of. Many other people will find themselves in the same situation.

I am sure the law was never intended to operate in this way.

Mr. KERR. Mr. President, a person in a relationship to a dependent such as the person the Senator has described, under those circumstances certainly is entitled to an exemption, under my interpretation of the law, and I hope to be able to help the Senator to obtain relief administratively.

Mr. ALLOTT. I appreciate that very much. I thank the Senator from Oklahoma.

Mr. President, I ask unanimous consent that a copy of a telegram from Mr. Swanson and a copy of the letter of the Internal Revenue Service may be included in the RECORD at this point.

There being no objection, the telegram and letter were ordered to be printed in the RECORD, as follows:

DENVER, COLO.,
July 24, 1962.

Senator GORDON ALLOTT,
Washington, D.C.:

Internal Revenue here claims that even though taxpayer keeps aged parent 11 months, contributing all support; and parent falls in his house breaking hip in December, if medical expenses exceeding taxpayer's support are paid within same year under liability insurance carried by taxpayer, exemption disallowed on grounds insurance company contributed over 50 percent. Obviously law means normal support and certainly nothing so ridiculous. If it takes specific amendment to remedy, can't you introduce such bill? Please wire reply.

HERBERT W. SWANSON.

U.S. TREASURY DEPARTMENT,
INTERNAL REVENUE SERVICE,
Denver, Colo., August 2, 1962.

The Honorable GORDON ALLOTT,
The U.S. Senate,
Washington, D.C.

DEAR SENATOR ALLOTT: Thank you for your letter of July 24, 1962, relative to the examination presently being made of the 1960 income tax return of Herbert W. and Eldora N. Swanson, 5150 Raleigh Street, Denver, Colo.

The sole issue involved is whether Mr. and Mrs. Swanson are entitled to the dependency exemption for Mrs. Norah Tyrrell, mother of Mrs. Swanson. Section 152(a) of the Internal Revenue Code, in defining a dependent, states in part that, "the term 'dependent' means any of the following individuals over half of whose support for the year was received from the taxpayer: * * * (4) The father or mother of the taxpayer * * *." The regulations under paragraph 1.152-1(a) (2)(i) provide: "For purposes of determining whether or not an individual received,

for a given calendar year, over half of his support from the taxpayer, there shall be taken into account the amount of support received from the taxpayer as compared to the entire amount of support which the individual received from all sources, including support which the individual himself supplied. The term 'support' includes food, shelter, clothing, medical and dental care, education, and the like."

Information furnished this office is that the total cost of Mrs. Tyrrell's support for the year was \$2,479.23. Of this amount, Mr. and Mrs. Swanson furnished \$780.76; Mrs. Ted Hunt, Mrs. Tyrrell's daughter, furnished \$266.67; Mrs. Tyrrell furnished \$50 from her own funds; and the balance of \$1,381.80 was furnished by the Scottish Union and National Island Marine Insurance Co. The amount of \$1,381.80 paid by the insurance company was for Mrs. Tyrrell's medical expenses incurred when she fell and broke her hip in Mr. and Mrs. Swanson's home.

Mr. and Mrs. Swanson contend that funds from the insurance company which were used to pay Mrs. Tyrrell's medical expenses are not part of her support. Our interpretation of the regulations is that such funds, taxable or otherwise, if used, must be considered in determining whether or not Mr. and Mrs. Swanson furnished over half of the dependent's support.

Mr. and Mrs. Swanson have been advised of their rights of appeal, i.e., (1) informal conference, (2) review by the Appellate Division, and (3) hearing before the Tax Court.

If we can be of any further assistance in this matter, please let us know.

Best regards.

Sincerely yours,

L. E. HILL,
Acting District Director.

Mr. ALLOTT. I thank my distinguished friend from Ohio very much for yielding to me.

The PRESIDING OFFICER. Does the Senator from Colorado withdraw his amendment?

Mr. ALLOTT. I withdraw my amendment.

The PRESIDING OFFICER. The Senator from Ohio has the floor.

Mr. HICKENLOOPER. Mr. President, will the Senator from Ohio yield to me for the purpose of my offering an amendment, with the understanding that the Senator from Ohio will not lose his right to the floor?

Mr. LAUSCHE. I yield to the Senator from Iowa.

The PRESIDING OFFICER. Without objection, the Senator from Ohio may yield to the Senator from Iowa with that understanding.

Mr. HICKENLOOPER. Mr. President, on behalf of myself and my colleague [Mr. MILLER] I offer the amendment which I send to the desk and ask to have stated.

The PRESIDING OFFICER. The amendment will be stated for the information of the Senate.

The LEGISLATIVE CLERK. On page 104, line 14, it is proposed to strike out "200" and to insert "500".

Mr. HICKENLOOPER. Mr. President, first I wish to express my appreciation to the Senator from Oklahoma for his consideration in the last couple of days, and that of his staff, in attempting to meet the problem which I face, which is quite important.

The amendment refers to page 104.

Mr. KERR. The Senator is correct.

Mr. HICKENLOOPER. It would give certain consideration to casualty companies engaged in operations relating to hail and windstorm damage. A radius of 200 miles is provided in which the business may be concentrated, in connection with certain reserves for losses. I shall not go into the details at this time.

I have discussed this question with the Senator from Oklahoma and with his staff. They understand the problem thoroughly.

The language, as it is written, seems to be an adequate or satisfactory provision for all the companies in this particular catastrophe category of which I know except one, which happens to be in my home State. It is a very substantial company operating there. A number of the catastrophe insurance companies have offices in my State, but mostly the companies are of limited means.

The particular company involved in this regard has an area of approximately 1,000 miles long and 400 miles wide. It begins with the northwest corner of the State of Nebraska, extends to the southwest corner of the State of Kansas, then eastward across the northern half of Missouri to the center of Ohio, north through most of Michigan for about 200 miles, and then southwest to the northern corner of Nebraska. That is a territory of approximately 1,000 miles long and 200 miles wide in which the company has the catastrophe insurance business, relating to hail and windstorm and those items.

The conviction of the company is that the 200-mile radius will not give them the benefit which other companies will enjoy—that, in fact, it would pose a definite hazard to their reserves, as their records show.

In connection with my remarks, Mr. President, I ask unanimous consent to have printed in the RECORD at this point a copy of a letter to me from Mr. Max D. Rutledge, president of Farmers' Mutual Hail Insurance Co. of Des Moines, Iowa, a copy of which I have already delivered to the Senator from Oklahoma and to his staff.

There being no objection, the letter was ordered to be printed in the RECORD, as follows:

HAIL INSURANCE CO.,

Des Moines, Iowa, August 30, 1962.

Hon. BOURKE B. HICKENLOOPER,
Senator from Iowa,
Senate Office Building,
Washington, D.C.

DEAR SENATOR HICKENLOOPER: In response to the request from your office, I shall attempt to furnish you the answers to the questions arising from your conference with Senator KERR and his office.

The term "pure loss ratio" as used by Mr. Benson in his letter of August 10, is the percentage of losses paid (excluding all expense) in relation to total premiums charged. Underwriting experience, when reduced to percentage, indicates the actual profit or loss when all losses and expenses are added together and compared to the premium.

The underwriting experience, especially in our hail department, was exceptionally favorable in the 4 years following the catastrophe of 1956. This favorable experience provided an increase in policyholders' reserve far greater than any similar period in the history of the company.

Year	Earned premium	Underwriting gain or loss	Change in surplus	Surplus on Dec. 31
1956	\$9,054,079.35	-\$3,548,674.14	-\$3,269,679.86	\$2,751,481
1957	10,958,240.63	735,712.25	651,461.21	3,402,943
1958	11,198,749.35	2,164,056.49	1,984,036.72	5,386,979
1959	10,033,866.54	2,173,054.53	2,113,091.43	7,500,070
1960	10,829,527.47	1,535,357.59	1,335,346.81	8,835,417
1961	11,724,685.78	269,886.43	392,032.44	9,227,449

In the year of 1961, there was an underwriting loss in the catastrophe lines; however, this loss was offset by underwriting gains in reinsurance assumed and by investment income.

Already 1962 has developed an underwriting loss on our total hail premium and an underwriting loss by the individual States of Kansas, Iowa, Nebraska, Minnesota, and Wisconsin.

I understand that there were severe storms yesterday and last night running through Nebraska, Minnesota, Iowa, and Wisconsin which will add to this loss.

Your third question, asking what percent of our catastrophe business would be included in a 300-mile radius and a 400-mile radius, is very difficult to answer because of the shape of our territory in relation to a circle of the same radius. Approximately 40 percent of our catastrophe business (28 percent of the total) is contained within the 200-mile radius. The remaining 50 percent is almost equally divided between the third, fourth, and fifth hundred miles, depending upon crop conditions in Kansas which fluctuate greatly from year to year. I believe if the present 200-mile proposal were increased to either 300 miles or 400 miles, administration of the provision would become very complicated. As we have pointed out before, 90 percent of our catastrophe business would fall within a 500-mile radius. The remaining 10 percent is isolated along the eastern seaboard and could be easily segregated.

I am sure the fact can be established that Farmers Mutual Hail Insurance Co. is the only mutual company writing catastrophe insurance that would be limited under the proposed 200-mile radius. It would receive equal benefit with other mutuals under the 500-mile radius. Our concentration of catastrophe liability extends from southwestern Kansas northeasterly to north-central Ohio, a distance of approximately 1,000 miles, yet the width of this concentration is less than 400 miles at any point and would easily fall within the 200-mile radius. This situation results from the fact that this area is the principal grain-producing area which is affected by severe hailstorm damage. Severe hailstorms occur over practically all of this area during a storm period because the storm is caused by a cold front traveling southeasterly from the northern Rocky Mountain region meeting moist, warm air from the Gulf of Mexico. It seems that the main violence of the storm is expended by the time it has gone through this 400-mile strip indicated on the enclosed map.

Thank you again for your interest in our problem. Please express our appreciation to Senator KERR and his staff for taking time to consider this very important problem which directly affects farmers of the Midwest who are trying to provide for themselves security from their greatest source of financial loss: namely, hailstorms.

Yours very truly,

MAX D. RUTLEDGE,
President.

Mr. HICKENLOOPER. The company believes—and, so far as I know, it is true—that it is the only company in the United States which would be so adversely affected by the language as it now stands. The company feels it could live, with reasonable assurance, if the

radius were extended to 500 miles instead of 200 miles. Therefore, we have offered the amendment.

I have discussed the problem with the Senator from Oklahoma and with his staff. We have arrived at an understanding which I believe the staff has reached, which may afford some basis for relief. It would not cause undue difficulty.

I should be pleased to have the Senator's comments.

Mr. KERR. Mr. President, with reference to the amendment offered by the Senators from Iowa, I advise the Senate that this has to do with losses in concentrated disaster areas. The committee felt, in making certain provisions available to companies operating either in one State or within 200 miles of any fixed point selected by the taxpayer, that adequate provision was being made.

The Senator advises that the mutual company he has in mind operates in a much larger area.

The Senator from Oklahoma believes that if the amendment were adopted as presented, it very likely could open up additional advantages beyond the company which the Senator has in mind. The Senator from Oklahoma would suggest a compromise in language as follows:

On page 103, line 25, strike the period and insert the following: “, or one-half of such amount in the case of a taxpayer who elects to compute the concentrated windstorm, and so forth, premium percentage under paragraph (2) (A) (iii).”

Then, on page 104, at the point referred to by the Senator, to include a third alternative, which would be:

(iii) if the taxpayer so elects, within 400 miles of any fixed point selected by the taxpayer,

In that event, if the taxpayer took advantage of the third option, he would get one-half the benefit that those who operated within a point 200 miles of any fixed point would get, but in return for taking half as much benefit pro rata, the taxpayer could elect an area within 400 miles of a fixed point which would give him far greater than twice what one would have at 200.

Mr. HICKENLOOPER. I think I understand what the Senator is suggesting. We have previously discussed it. As I said, I am grateful to the Senator from Oklahoma, his staff, and the staff of the Treasury Department, who have conferred with us on the question.

Mr. KERR. The Senator is aware of the fact that the Treasury would not put itself in a position favoring the amendment.

Mr. HICKENLOOPER. I understand that.

Mr. KERR. But under a good deal of persuasion by the able Senator from

Iowa, who seems to have a very great ability in that regard, the Treasury Department agreed that if it were amended in the manner suggested, they would not vigorously oppose the measure.

Mr. HICKENLOOPER. When one sits in the presence of the distinguished Senator from Oklahoma for any appreciable length of time, that persuasive ability is bound to rub off to some extent—at least to the extent of a thin veneer—on those who hear him. I am sure that my amendment is a worthy one.

Mr. KERR. I thank the Senator, but I remind him that he was in the Senate when I arrived here, and I have sat at his feet and learned.

Mr. HICKENLOOPER. I did not want to create the idea that the Treasury was pressing the proposal. I wanted to thank the officials of the Treasury for their time and effort in attempting to work out something which may not meet with their approval.

Mr. KERR. Mr. President, I send to the desk an amendment, and ask that it be stated.

The PRESIDING OFFICER. The amendment will be stated.

The LEGISLATIVE CLERK. On page 103, line 25, strike the period and insert the following: “, or one-half of such amount in the case of a taxpayer who elects to compute the concentrated windstorm, etc., premium percentage under paragraph (2) (A) (iii).”

On page 104, strike lines 13 and 14 and insert in their place the following:

arising—

- (i) in any one State;
- (ii) if the taxpayer so elects, within 200 miles of any fixed point selected by the taxpayer; or
- (iii) if the taxpayer so elects, within 400 miles of any fixed point selected by the taxpayer.

The PRESIDING OFFICER. Does the Senator from Iowa accept the amendment, as modified?

Mr. HICKENLOOPER. Mr. President, I accept the modification proposed by the Senator from Oklahoma.

The PRESIDING OFFICER. The question is on agreeing to the amendment of the Senator from Iowa, as modified.

The amendment was agreed to.

Mr. KEATING. Mr. President, will the Senator from Ohio yield to me for a colloquy with the distinguished Senator from Oklahoma?

Mr. LAUSCHE. I yield.

Mr. KEATING. Mr. President, the Savings & Loan Bank of the State of New York operates under article 10B of the banking laws of the State of New York.

Being the only institution of its kind, owned and originally operated entirely for the benefit of member associations, it was taken as the prototype for the establishment of the Federal Home Loan Bank system. At the present time, it continues to function in a manner very similar to that of the Federal Home Loan Bank for the benefit of State chartered savings and loan associations in the State of New York. Basically, it extends credit to its members through

loans financed by the surplus cash it receives from its members in the form of time and demand deposits or by the issuance of debenture notes which it offers on the open market.

My colleague [Mr. JAVITS] and I have been in close touch with Mr. Otto J. Rabstajnek, president of the Savings & Loan Bank of the State of New York.

It is our understanding that the definition of a savings and loan association contained in section 8 of H.R. 10650 would in no way curtail or interfere with the essential activities of financial institutions such as the Savings & Loan Bank of New York State. The debentures floated by this bank would clearly qualify as proper holdings under the 10-percent category contained in the definition of the savings and loan association in section 8. While I believe it would have been preferable to have specifically included the New York State Savings & Loan Bank in the Sparkman amendment, I am advised that the bill as presently written would in no way be injurious to the bank.

All who are familiar with the workings of the bank are aware of the vital contribution which it has made to the economy of New York State over the years of its existence. Would the Senator from Oklahoma agree that the definition in the pending bill would not in any way restrict the activities of this institution as far as the issuance and sale of its debentures is concerned?

Mr. KERR. Mr. President, responding to the question of the distinguished Senator from New York, I believe it is quite clear that the definition of domestic savings and loan associations permits it to hold debentures of a type issued by the Savings & Loan Bank of the State of New York to the extent of the specified 10-percent limit.

Mr. KEATING. I thank the Senator.

Mr. JAVITS. Mr. President, will the Senator yield?

Mr. LAUSCHE. I yield.

Mr. JAVITS. That is, according to the definition as amended by the amendment in which I joined with the Senator from Alabama [Mr. SPARKMAN].

Mr. KERR. That is my understanding.

Mr. JAVITS. I thank the Senator.

Mr. DIRKSEN. Mr. President, will the Senator yield?

Mr. LAUSCHE. I yield.

Mr. DIRKSEN. The distinguished Senator from Kentucky [Mr. MORTON] is unavoidably absent. If he were present, he would offer his amendment, which has been designated "8-29-62-H." I am authorized to submit for him an explanation and an analysis of the amendment. I do so, and ask that the explanation be incorporated as a part of my remarks.

There being no objection, the explanation was ordered to be printed in the RECORD, as follows:

The proposed amendment gives full recognition to the need to encourage the growth of savings and loan institutions in this country. Under the Finance Committee bill there are a number of permissible methods

under which such institutions may compute their allowable bad debt deductions—the deductions which measure the extent to which such institutions can make provision for uncollectible loans. One of such permissible methods would allow savings and loan institutions a bad debt deduction generally equal to 3 percent of their growth in outstanding loans. The proposed amendment would increase the deduction to 5 percent.

This increase in the deductible reserve for bad debts is important and necessary for the following reasons:

1. It would encourage the growth of savings and loan institutions by placing the bad debt deduction on a substantial relationship to savings and loan institution growth.

2. It would be particularly beneficial to small and medium-sized institutions which must continue to grow in order to survive in a competitive business.

3. It would provide a more realistic measure of necessary loss reserves, thus permitting savings and loan institutions to maintain sound financial footing.

4. It would extend to small, although not new, institutions the treatment which the Finance Committee recognized should be extended to small new institutions.

5. It would encourage the construction of new housing by increasing the ability of savings and loan institutions to provide reasonable financing.

In short, the proposed amendment would aid small business, i.e., small savings and loan institutions, by encouraging their growth and aiding them in maintaining a sound financial basis. The nationwide community of savers and homeowners is thereby served.

LEGISLATIVE PROGRAM AND ORDER FOR ADJOURNMENT UNTIL 9 A.M. TOMORROW

Mr. DIRKSEN. Mr. President, will the Senator yield?

Mr. LAUSCHE. I yield.

Mr. DIRKSEN. I should like to ask the majority leader what he contemplates at the present time. I ask whether he knows how many more amendments will be offered, what general speeches may be made, and if we can consummate a third reading of the bill this evening.

Mr. MANSFIELD. Mr. President, to the best of my knowledge, the Senator from Tennessee [Mr. GORE] has two, three, or four amendments which he thinks can be disposed of very shortly. The Senator from Illinois [Mr. DOUGLAS] has an amendment relating to an oil and gas depletion allowance on a graduated basis upon which he would like an hour altogether—

Mr. DOUGLAS. I do not wish to confine myself to any definite time limit. I do not intend to take an excessive amount of time. But I do not wish to be placed within an iron lung, so to speak.

Mr. MANSFIELD. I believe the Senator from Minnesota [Mr. MCCARTHY] has an amendment which he wishes to offer.

It is the hope of the leadership that the third reading of the bill may be reached tonight. With the understanding that a third reading may be reached tonight, I should like to propound a unanimous-consent request that there be no votes after the third reading of the bill tonight, and that the Senate meet at 9 o'clock tomorrow morning.

Mr. President, I ask unanimous consent that when the Senate adjourns tonight, it adjourn to meet at 9 a.m. tomorrow.

The PRESIDING OFFICER. Is there objection? The Chair hears none, and it is so ordered.

Mr. MANSFIELD. Mr. President, I ask unanimous consent that 4 hours of general debate be allotted on the bill before the final vote is taken.

The PRESIDING OFFICER. Is there objection?

Mr. LAUSCHE. Mr. President, reserving the right to object, I have been yielding—

Mr. MANSFIELD. Mr. President, will the Senator yield?

Mr. LAUSCHE. I yield.

Mr. MANSFIELD. Since the Senator from Ohio has been so generous and tolerant, I ask unanimous consent that at the conclusion of the morning hour tomorrow, if there is one, the Senator from Ohio be given first recognition.

The PRESIDING OFFICER. Is there objection? The Chair hears none, and it is so ordered.

Mr. MANSFIELD. Mr. President, I ask the Chair to put my original request to the Senate.

The PRESIDING OFFICER. Is there objection to the previous request of the Senator from Montana? The Chair hears none, and it is so ordered.

The unanimous-consent agreement, subsequently reduced to writing, is as follows:

Ordered, That, effective on Thursday, September 6, 1962, at not later than 9:15 a.m., during the further consideration of the bill (H.R. 10650) to amend the Internal Revenue Code of 1954 to provide a credit for investment in certain depreciable property, to eliminate certain defects and inequities, and for other purposes, all debate shall be limited not to exceed 4 hours, to be equally divided and controlled by the majority and minority leaders, or someone designated by them, to be followed by a vote on final passage of the said bill.

Mr. LAUSCHE. Mr. President, I yield the floor.

Mr. DOUGLAS obtained the floor.

Mr. DIRKSEN. Mr. President, will my colleague yield to me for a moment?

Mr. DOUGLAS. I also have been yielding for some time, but I shall be glad to yield to my colleague.

Mr. DIRKSEN. Mr. President, to clarify the unanimous-consent request, do I correctly understand that consideration of the remaining amendments will be concluded this evening, so far as the Senator knows, and that the third reading of the bill will occur tonight?

Mr. MANSFIELD. That is correct. The third reading could not be had unless all amendments were disposed of.

Mr. DIRKSEN. Exactly.

Mr. MANSFIELD. But once the third reading is reached, Senators may speak on any subject they wish. I understand that several Senators have speeches covering various situations in the world.

Mr. President, I ask unanimous consent that tomorrow morning there be a morning hour of 15 minutes, from 9 a.m. to 9:15 a.m., and that the 4 hours to be

allotted on the bill shall start at 9:15 a.m.

The PRESIDING OFFICER. Is there objection? The Chair hears none, and it is so ordered.

Mr. MANSFIELD. In other words, there will be a 15-minute morning hour. Then the 4 hours will begin to run on the debate on the bill before the vote is taken.

Mr. DIRKSEN. I have a further inquiry. If the Senate finished with the amendments tonight, and the third reading is had tonight, the vote tomorrow probably will come at approximately 1 o'clock.

Mr. MANSFIELD. Between 1:15 and 1:30.

Mr. DIRKSEN. Will my colleague ask for a ye-and-nay vote on his amendment?

Mr. DOUGLAS. Yes.

Mr. MANSFIELD. That is the only ye-and-nay vote that I know of. There may be others, but as of now, that is all I know of.

Mr. DOUGLAS. Mr. President, I call up my amendment identified as "8-30-62—J."

The PRESIDING OFFICER. The amendment will be stated by title.

The legislative clerk proceeded to state the amendment.

Mr. DOUGLAS. I ask unanimous consent that the amendment be not read, but printed in the RECORD at this point.

The PRESIDING OFFICER. Without objection, it is so ordered.

The amendment is as follows:

On page 391, after line 21, insert the following new section:

"SEC. 27. PERCENTAGE DEPLETION FOR OIL AND GAS WELLS.

"(a) GRADUATED RATES.—Section 613 (relating to percentage depletion) is amended—

"(1) by striking out in subsection (a), 'specified in subsection (b)' and inserting in lieu thereof 'specified' in subsections (b) and (d);

"(2) by striking out paragraph (1) of subsection (b) and inserting in lieu thereof the following:

"(1) OIL AND GAS WELLS.—The percentage applicable under subsection (d) (1); and

"(3) by redesignating subsection (d) as (e), and by inserting after subsection (c) the following new subsection:

"(d) OIL AND GAS WELLS.—

"(1) PERCENTAGE DEPLETION RATES.—In the case of oil and gas wells, the percentage referred to in subsection (a) is as follows:

"(A) 27½ percent—to the extent that, for the taxable year, the taxpayer's gross income from the oil and gas well, when added to (i) the taxpayer's gross income from all other oil and gas wells, and (ii) the gross income from oil and gas wells of any taxpayer which controls the taxpayer and of all taxpayers controlled by or under common control with the taxpayer, does not exceed \$1,000,000;

"(B) 21 percent—to the extent that, for the taxable year, the taxpayer's gross income from the oil and gas well, when added to (i) the taxpayer's gross income from all other oil and gas wells, and (ii) the gross income from oil and gas wells of any taxpayer which controls the taxpayer and of all taxpayers controlled by or under common control with the taxpayer, exceeds \$1,000,000 but does not exceed \$5,000,000; and

"(C) 15 percent—to the extent that, for the taxable year, the taxpayer's gross income from the oil and gas well, when added to (i) the taxpayer's gross income from all other

oil and gas wells, and (ii) the gross income from oil and gas wells of any taxpayer which controls the taxpayer and of all taxpayers controlled by or under common control with the taxpayer, exceeds \$5,000,000.

"(2) CONTROL DEFINED.—For purposes of paragraph (1), the term "control" means—

"(A) with respect to any corporation, the ownership, directly or indirectly, of stock possessing more than 50 percent of the total combined voting power of all classes of stock entitled to vote, or the power (from whatever source derived and by whatever means exercised) to elect a majority of the board of directors, and

"(B) with respect to any taxpayer, the power (from whatever source derived and by whatever means exercised) to select the management or determine the business policies of the taxpayer.

"(3) CONSTRUCTIVE OWNERSHIP OF STOCK.—The provisions of section 318(a) (relating to constructive ownership of stock) shall apply in determining the ownership of stock for purposes of paragraph (2).

"(4) APPLICATION UNDER REGULATIONS.—This subsection shall be applied under regulations prescribed by the Secretary or his delegate.

"(b) EFFECTIVE DATE.—The amendments made by subsection (a) shall apply only with respect to taxable years beginning after the date of the enactment of this Act."

On page 391, line 22, strike out "27" and insert "28".

Mr. DOUGLAS. I ask for the yeas and nays on the amendment.

The yeas and nays were ordered.

Mr. KEATING. Mr. President, will the Senator from Illinois yield for a parliamentary inquiry?

Mr. DOUGLAS. I yield for a parliamentary inquiry.

Mr. KEATING. Is the amendment of the Senator from Illinois divisible?

Mr. DOUGLAS. No; it is not divisible.

Mr. KEATING. Perhaps I do not understand the amendment. My understanding—and I may be mistaken—is that it has to do with the oil and gas depletion allowance, and also makes provision for something else. Does it relate merely to the depletion allowance?

Mr. DOUGLAS. Yes.

Mr. KEATING. There was some talk about another amendment.

Mr. DOUGLAS. It differs from the amendment of the Senator from Delaware [Mr. WILLIAMS], which proposed to reduce the rates on the upper brackets of the income tax schedule as well as reducing the depletion allowance. My amendment is confined solely to the percentage depletion allowance on oil and gas.

Mr. KEATING. It does not apply to any other subject?

Mr. DOUGLAS. That is correct.

The PRESIDING OFFICER (Mr. MILLER in the chair). The Chair rules that the amendment is divisible. There are parts of it that are divisible.

Mr. MANSFIELD. I believe what the Senator from New York has in mind is the possibility that the amendment of the Senator from Illinois was comparable to the amendment of the Senator from Delaware. The Senator from Illinois says that his amendment is not in the same category.

The PRESIDING OFFICER. The Chair holds that it is not a parlia-

mentary inquiry as to whether it is the same amendment as the original amendment of the Senator from Delaware.

Mr. DOUGLAS. I suppose technically my amendment is divisible, because parts of an amendment can almost always be divided. However, I believe that if Senators will read the amendment they will see that it is an integral whole, one amendment. It is no more divisible than the child brought before King Solomon was divisible.

SLIDING SCALE REDUCTION

My amendment would reduce the depletion allowance on oil and gas from the present 27½ percent down to 15 percent in cases where the taxpayer's gross income from oil and gas in any year exceeds \$5 million. The allowance would be reduced to 21 percent where the taxpayer's income from oil and gas exceeded \$1 million, but did not exceed \$5 million. It would leave the existing 27½ percent allowance for those whose incomes from oil and gas did not exceed \$1 million gross in a year. It differs, therefore, from the amendment offered earlier today by the Senator from Delaware, which would gradually have reduced the allowance to 20 percent, regardless of the amount of the gross income of the recipient. It leaves out, of course, any provision for a reduction in income taxes, which was included in the amendment of the Senator from Delaware.

To repeat, my amendment would leave the existing 27½ percent allowance intact for those whose incomes from oil and gas do not exceed \$1 million gross a year. It would therefore not affect royalties received by farmers or land owners for the use of their land. It would not affect the allowance granted to small oil producers whose gross income, I repeat, is not in excess of \$1 million a year.

Mr. CARROLL. Mr. President, will the Senator yield?

Mr. DOUGLAS. I yield for a question.

Mr. CARROLL. The State of Colorado has become a very important oil producing State. Denver has become an administrative oil center. Will the Senator from Illinois tell me how his amendment compares with the amendment which he presented 2 or 3 years ago, to which the Senator from Wyoming, Mr. O'Mahoney, had an amendment? Is the O'Mahoney amendment included in the Senator's amendment?

Mr. DOUGLAS. It is the same amendment which I have presented on numerous occasions since 1955, I believe, namely, to maintain the depletion allowance intact with respect to those whose gross income from gas and oil was less than \$1 million a year; to reduce the allowance from 27½ percent to 21 percent for those with gross incomes from gas and oil between \$1 million and \$5 million a year; and to reduce the allowance to 15 percent for those whose gross income from gas and oil is more than \$5 million a year.

Mr. CARROLL. Can the Senator from Illinois draw upon his recollection to inform the junior Senator from Colorado as to the provisions of the O'Mahoney amendment which was included in the vote 2 or 3 years ago? The junior

Senator from Colorado does not recall the provisions.

Mr. DOUGLAS. I regret to say that neither can I recall its provisions.

Mr. CARROLL. It was my impression that at that time the Senate voted on the amendment as modified by the amendment of the former Senator from Wyoming, Mr. O'Mahoney. I was hoping that the Senator from Illinois could inform me in that respect.

There is a growing feeling among certain groups, especially small refiners, that the extensive application of the benefits from the depletion allowance, not within the continental limits of the United States, has given a great economic advantage to some of the great major oil companies of the Nation operating in foreign nations which affects the small refiner's marketing position within this country. If I am not mistaken, the former Senator from Wyoming, Mr. O'Mahoney, and the junior Senator from Colorado at one time had an amendment in which we explored the possibility that perhaps the depletion allowance ought to be confined to the continental limits of the United States.

One of the reasons for that was based upon the hearings of the Subcommittee on Antitrust and Monopoly, namely, that excessively large depletion allowance benefits were given to major oil companies which had extensive holdings in Saudi Arabia.

Mr. DOUGLAS. May I reply to that?

Mr. CARROLL. I shall be happy to have the Senator do so, if I may complete this thought.

The former Senator from Wyoming, Mr. O'Mahoney, and I, after those hearings hoped that there might be some joinder of opinion or some union of action among the independent oil companies in support of our position, because we felt that this situation was contributing the tremendous financial windfall which was influencing the marketing situation in the United States today. I have been told this has been happening, although I am not an expert in this field. This is not a small matter; it involves hundreds of millions of dollars which are being currently used, some small independents and some small refiners feel, to their disadvantage and to that of our domestic economy.

If the Senator from Illinois would like to comment on that thought, I should be happy to have him do so.

Mr. DOUGLAS. The Senator from Colorado makes a very important point. It is notorious that the Arabian-American Oil Co., which in turn is owned by several American oil companies, and which has the concessions in Saudi Arabia, to which the Senator from Colorado refers, pays virtually no taxes—I think absolutely no taxes—to the United States, although it makes enormous profits. It is able to avoid taxes by reason of the fact that the 50 percent royalty payment which it makes to Saudi Arabia is called a tax rather than a royalty; and, as a tax, is therefore offset against the American tax which the Arabian-American Oil Co., or the parent companies, would otherwise pay.

The big oil companies which do business in Latin America and the Western Hemisphere have a 14-point tax reduction; but whether they in turn are able to disguise royalties as taxes, and hence avoid the payment of any taxes on their business overseas, is not a subject on which the Senator from Illinois can speak. But they do obtain a depletion allowance.

The amendment of the Senator from Illinois applies to the companies overseas as well as those at home; and since the companies overseas are huge organizations, their depletion allowance would be reduced from 25 percent to 15 percent.

In this way, the smaller companies in the United States would not be taxed as severely as are the big companies overseas or at home, and therefore would have a relative advantage in comparison with the big companies. This would help the independent, nonintegrated refiners. It would also help independent oil distributors who are finding themselves under heavy pressure by reason of predatory price cutting carried on by gasoline stations really owned by the big integrated companies, even though there may be the disguise of a lease.

Mr. CARROLL. Mr. President, will the Senator from Illinois yield?

Mr. DOUGLAS. I yield.

Mr. CARROLL. In the short time which the junior Senator from Colorado has had to prepare for this discussion, he does not in any way wish to draw from the amendment the strength to which it is entitled, because it is his opinion that the amendment will suffer the fate of other amendments which have been proposed to the bill. Therefore, if I may express my personal opinion, I do not feel that there is any chance for the adoption of the amendment. However, I wish to make the RECORD clear for the people in my State that the able Senator from Illinois has put his finger on a subject which involves many small refiners. They are not so much concerned, if I interpret their viewpoint correctly, about what we call the reduction of the depletion allowance from 27½ percent to 15 percent. What they wish to do is to change the whole concept of the law. Rather than have a depletion-of-capital concept, what they are thinking about is the use of the money that they get for depletion allowance in the foreign countries for exploratory purposes in our own country. That is the proposition as it has been presented to me. In other words, they do not want this great financial windfall to be put into the hands of the giant oil companies which can control the market and the marketing facilities. It is not so much that the big companies undercut the market; it is that they are in a position, with their huge financial resources, to establish marketing systems with which the small refiners and the small independents cannot compete.

Mr. DOUGLAS. My amendment, with its differential rate according to the amount of business done, would naturally help the small producer, the small refiner, and indirectly the small distributor, as compared with the giant oil com-

panies. It would also lessen some of the differential advantage which the big companies get from their operations abroad—notably, the Standard Oil group.

Mr. CARROLL. Mr. President, will the Senator from Illinois yield?

Mr. DOUGLAS. I yield.

Mr. CARROLL. To be completely realistic, I have voted on this issue a number of times. Its effects have been in my mind and my philosophy from the days of Franklin Roosevelt, who advocated such a reduction 20 years ago; and from the days of President Truman, who advocated such a cut in 1948 or 1949. Having seen this concept defeated repeatedly upon the floor of the Senate, I think a realistic view is that even the independent producers today—I believe that is true in my own State—are still influenced by the major oil companies and have not yet seen the handwriting on the wall. But I believe they are beginning to see it more clearly each year. I think they are beginning to see it more clearly year after year, because of the point I make about their great wealth of economic resources enabling them to set up marketing conditions with which they cannot compete.

Mr. DOUGLAS. Mr. President, I wish to supplement what the Senator from Colorado has said. One of the distinguishing features in the early years when we were attacking the depletion allowance was the way in which the small independents would attack the proposal. The big companies were able to hoodwink them and would whip them into line.

The Senator from Illinois has been greatly encouraged by the fact that in the past few months a number of the smaller independent operators have come forward and said, "Now we see that this proposal would be a protection to us, and would decrease the power of the big companies."

As I have said, one very interesting development is the way in which the independent owners of companies and distributing stations are coming around. They say that the big integrated companies—the Standard Oil group, Texaco, Shell, Gulf, and other large companies which have wells, refineries, and stations, are using their profits, made in large part from not paying taxes to the U.S. Government, to expand the distributive end of their businesses in part by predatory local price cutting or by driving the independents out of a given market, and then, when they have been driven out, again raising prices and moving on to another market.

Some of them have come to see that the depletion allowance helps to finance the onward march of the big companies. It has taken them a long time to learn this, and their knowledge may well come too late. But it is dawning on them.

Mr. CARROLL. Mr. President, will the Senator from Illinois yield?

Mr. DOUGLAS. I yield.

Mr. CARROLL. What the Senator from Illinois has just stated is what I have recently learned from a small refiner—in other words, the growing un-

derstanding of the domestic economic consequences and effects of the depletion allowance. But I must qualify that by saying that I refer to the effect of the depletion allowance on the companies abroad, where the big resources are. I recall an annual financial statement that one company which operates in Saudi Arabia has a depletion allowance of \$120 million.

The small domestic refiners begin to see that this great financial wealth and financial strength are having an immediate effect upon refiners and distributors in this country.

But I point out that this is not presently a great popular issue in Colorado, and it is impossible to educate the people in a short period of time.

Mr. DOUGLAS. We have been trying to educate the public for 11 years, since this issue was first raised in 1951.

Mr. CARROLL. I understand that the able Senator from Illinois has rendered a magnificent service.

Mr. DOUGLAS. No; apparently I have done very poorly.

Mr. CARROLL. I was referring to my own State. I can hear some in my State say, "The junior Senator from Colorado is against the depletion allowance, and his position will destroy the oil industry in our State."

The Senator from Illinois seeks to limit the depletion allowance for both the domestic economy and foreign producers; but I would like first to limit the depletion allowance for companies beyond the continental limits of the United States; and then we can consider dealing with the situation at home. The companies beyond the continental limits of the United States have great financial resources.

The Senator from Illinois has been fighting for years for the adoption of this amendment, and I have been fighting for it for a few years. No doubt we shall be defeated. But I point out that I should like to have the depletion allowance confined, as a first step, to the continental limits of the United States.

Mr. DOUGLAS. I hope the Senator from Colorado will prepare such an amendment. But again I point out that since the operations abroad are on a much larger scale than those in the United States, this amendment, when applied both abroad and at home, would affect the big companies abroad more than it would affect the average company at home. That is the point.

Mr. CARROLL. I thought I had stated that Senator O'Mahoney and I had prepared such an amendment, but there was no general support for it.

Although I cannot accept the full implications of the amendment of the Senator from Illinois, I intend to support his position, until we can make a better fight; and I hope some day it will be a winning fight.

Mr. DOUGLAS. I appreciate the support of the Senator from Colorado; it is characteristic of him.

I voted against tabling the amendment of the Senator from Delaware [Mr. WILLIAMS], although I did not think that

amendment was the best way to treat this subject. That amendment would have reduced the allowance to 20 percent, regardless of the size of the operator. It would have cut the royalty allowance of the farmer upon whose land oil is found, and from which oil flows; and the amendment also would have included the income tax provisions, which I think inappropriate.

It was my intention—had not the guillotine fallen on his amendment—to have offered my amendment as a substitute. But since that became impossible, I felt that we should not close the debate after merely 1 hour, and that I should not be foreclosed from offering my amendment as a substitute.

So, although I would have voted against the Williams amendment, if the question of its adoption had been before us, I felt that we should not close the debate at that point.

My amendment is free from the defects which I think the Williams amendment had. In other words, my amendment is graduated according to the size of the operations. Farmers who own land from which oil is taken and whose income is less than \$1 million—and that is true of virtually all of them—would lose absolutely nothing by means of my amendment. The small operator—one with one, two, three, or four wells—would lose nothing by means of my amendment. The fairly large operators, with gross incomes between \$1 million and \$5 million a year, will have their depletion allowance reduced by 5 percent. The very large operators—those with annual incomes of more than \$5 million—would have their depletion allowance reduced 12½ points.

Under my amendment there would be a gain of somewhere between \$350 million and \$500 million a year in revenue.

Mr. CARROLL. Mr. President, will the Senator from Illinois yield?

Mr. DOUGLAS. I am glad to yield.

Mr. CARROLL. For the reasons which the Senator from Illinois has stated far more ably than I could have done, I, too, voted against the motion to lay the Williams amendment on the table, because I think this subject should be fully discussed. It involves a very important issue.

If I had known that this matter was coming up on the floor of the Senate, I might have offered the amendment of Senator O'Mahoney, which increased the gross amount of your amendment. Senator O'Mahoney was one of the great fighters for the independent oil groups of Wyoming—or what we call the Rocky Mountain Oil Association; and when he drew up the amendment, I felt that it was one to which I could subscribe. I voted for it; and if I had had time, I would have offered it today.

Mr. DOUGLAS. Let me say to my friend that it is relatively easy for a Senator to support such amendments if there is no oil production in his State. But it so happens that Illinois is the fourth largest oil-producing State in the Nation. One congressional district in Illinois obtains its major revenue from

oil. The oil operators in my State have consistently been opposed to me. But I go into that district and I explain my position. I go into the various centers of the oil industry—at Carmi, Mount Carmel, and other towns. Incidentally, I carried that district by a very handsome margin, although the oil producers poured a lot of money into it in their attempt to defeat me.

Mr. CARROLL. Mr. President, few Members of the Senate have such persuasive charm as does the Senator from Illinois.

Mr. DOUGLAS. Oh, no; the Senator from Colorado is carrying his compliments much too far.

Mr. CARROLL. The Senator from Illinois also has a great consumer area which can balance that situation.

Mr. DOUGLAS. I point out that I consistently opposed the depletion allowance, and I met the oil people in debate.

Mr. CARROLL. Those of us who come from areas where there is a very sparse population find that the oil groups have great financial and economic strength. Certainly this is not an easy issue for us to carry to the people.

Mr. DOUGLAS. I understand.

Mr. CARROLL. So in such areas we are faced with great difficulty.

Mr. DOUGLAS. I understand. If the Senator could make the independent oil men have any sense, they should realize that this amendment would help them against the pressure of the big, integrated companies that are putting them out of business. If they have brains enough to go into the proposal—and the industry is supposed to be composed of able men—they should have brains enough to understand that.

Mr. CARROLL. Mr. President, the able Senator from Illinois has convinced me. I shall ask him to come out to Colorado and talk to the oil producers there; I think he could convince them.

Mr. DOUGLAS. I shall be very glad to come there, unless my presence would hurt the able Senator from Colorado—which I am afraid it might do.

Mr. CARROLL. Mr. President, I thank the able Senator from Illinois for his customary patience.

Mr. DOUGLAS. Mr. President, this amendment strikes at the greatest abuse among the many abuses in our whole tax system.

PRESENT BILL MAKES THINGS WORSE

The many unjust tax privileges now embodied in the revenue system cost the Government several billion dollars a year in revenue. These privileges, sometimes called loopholes—perhaps better termed truck holes—have increased over the years, so that the tax structure of the country is now seriously eroded. The present will would make the situation worse.

The President thought he was going to close some loopholes, but he did not reckon with the House and the Senate. We end by opening more loopholes than we closed. We wind up opening

up the investment credit abuse to the tune of about \$1,300 million.

A lobbying provision has been added opening the floodgates to the special interests and selfish interests, and putting pressure on all the legislative bodies of the country.

We have not improved the situation with regard to the expense account abuse; and indeed in some respects we may have made it worse.

We backed down on applying the withholding method for the collection of the basic income tax on dividends and interest. We failed to close that loop-hole.

We granted to the utilities a 3-percent investment credit, which is totally unnecessary, and which will be a windfall to them.

We granted a 7-percent credit to gas pipelines, which have many powerful friends on both sides of the aisle.

This bill would make the situation worse, rather than better.

In addition, there is H.R. 10. I assume the understanding is that while that bill is not attached to the pending bill, the bipartisan leadership will put it through shortly after action on this bill is completed.

OIL AND GAS DEPLETION GREATEST ABUSE

Of all the abuses, the depletion allowance on oil and gas is the worst. Unless Congress cures this and other erosions and injustices, these abuses will continue to spread like a cancer through our tax system.

I have said that the 27½-percent depletion allowance on income from oil and gas is the worst of the many tax loopholes. Let me review the situation so far as oil and gas are concerned. Under the present law, the host of costs and special allowances are deductible from gross income even before the depletion allowance applies. I wish to enumerate them.

OPERATING COSTS DEDUCTIBLE

First, of course, there are operating costs. This is a deduction which every industry has, and properly so, but perhaps it is the only deduction every industry has which is not a special deduction for the oil industry.

INTANGIBLE DRILLINGS COSTS

Second, the gas and oil industry is credited with intangible drilling and development costs. These can be written off 1 year, and not spread over a period of years, as is the case in other industries. It has been estimated that between 75 and 90 percent of all costs can be written off in this manner. We have, therefore, accorded to this industry virtually the ultimate in accelerated depreciation and fast writeoffs. This is in addition to and apart from the depletion allowance. Thus, there is the very great advantage of the fast writeoff, which many experts tell me is far more advantageous than even the oil depletion allowance.

I am not proposing in my amendment to alter this situation. It applies abroad as well as at home. Most of the costs can be written off in 1 year.

WRITEOFF OF DRY HOLES

Third. The cost of drilling unsuccessful, or so-called dry holes, can be written off against the income from successful drillings.

FOURTEEN-POINT WESTERN HEMISPHERE DEDUCTION

Fourth. There is a 14-point reduction in the tax itself, or a reduction from 52 to 38 percent on taxable income, for income derived from operations abroad in the Western Hemisphere, notably in the oil centers of Venezuela, but also in Mexico and other countries. I point out that Standard Oil has the big drillings and fields in Venezuela.

ROYALTY PAYMENTS DISGUISED AS TAXES

Fifth. As I mentioned in my colloquy with the Senator from Colorado, royalty payments abroad, particularly in the Near East, are commonly disguised as income tax payments, for which the foreign tax credit is then available. The 50-50 plan was started, I believe, in Latin America, was then applied to the Middle East, and now has been applied to Persia and throughout the Middle East. This is really a royalty, but it is called a tax, and therefore it offsets to that degree the tax which the American company would otherwise pay on its income from abroad.

I think it is well known that the Arabian American Oil Co., which is a subsidiary of three Standard companies, probably does not pay a single dollar in income tax to the American people, although its profits run into the hundreds of millions of dollars. There are also tax havens; and as the Senator from Tennessee has pointed out, oil executives abroad, who declare that they are permanent residents abroad, up to now have paid no personal income tax, and under the present bill would be exempted on \$35,000 of income.

PERCENTAGE DEPLETION ALSO

All these provisions would seem to be extremely generous, but the oil and gas industry is permitted a still further allowance called the percentage depletion allowance. In the case of gas and oil, this amounts to an additional 27½ percent of gross income up to one-half of net income. This allowance is, moreover, permitted in perpetuity as long as there is any flow of oil or gas from the well.

There are wells in the east Texas field which started gushing 40 or 50 years ago, and which are still continuing. I believe there is one in the original Galveston field which is still going. The depletion allowance was put into effect in 1926. The owners of such wells have deducted the depletion allowance every year since 1926, or 36 years ago.

Mr. CLARK. Mr. President, will the Senator yield?

Mr. DOUGLAS. I yield.

Mr. CLARK. I have heard it said—and I wonder if the Senator knows whether it is true—that there are instances in which an oil operator has recovered, through the depletion and other allowances, 19 times the cost of the well.

Mr. DOUGLAS. I can well believe

that. There is no limit to the depletion allowances as compared to the original cost of the well. They are not limited to the original cost, and in the case of rich wells and long-gushing or long-flowing wells, the deduction of the depletion allowance has gone on interminably, without any regard whatsoever to original cost. Nineteen times the cost seems a very modest figure to me.

I emphasize again that this depletion allowance is not limited to recapturing the cost of the well in question. Most of this cost, as we have seen, is recovered for tax purposes in the year the outlay is made, through the intangible drilling and development cost deduction.

I emphasize that the depletion allowance is in addition to all other deductions. It continues through time without relationship to the taxpayer's investment in the venture and whether or not the investment has been recovered for tax purposes.

As I previously said, the beginnings of the allowance go back about 36 years, to 1926, when an effort was made to revise the prevailing discovery depletion provisions.

ONE ABUSE HAS LED TO ANOTHER

From its inception the percentage depletion allowance has been 27½ percent. As the Senator from Delaware [Mr. WILLIAMS] pointed out early in the afternoon, as corporation income taxes have risen from 14 percent to the present 52 percent, the value of this allowance has grown. Not only is this true, but also it has brought in its train a host of similar deductions on virtually everything else extracted from the earth and from the sea—sulfur, coal, uranium, helium and every other mineral. In 1951 former Senator Connally of Texas was able to include oyster shells and clam shells, and other Senators were able to have sand and gravel covered. There would seem to be no danger of dry holes in the cases of oyster shells, clam shells, and sand, and gravel.

The depletion allowance is almost a perfect example of a case in which, instead of closing a loophole in the law, an attempt has been made to make the loophole universal.

In 1956, which is the latest year for which I have been able to obtain official figures, the total deductions for depletion allowances in the extractive industries were approximately \$3 billion. For oil and gas alone, the deductions in that year amounted to more than \$2 billion.

This is the citadel of privilege. This is the greatest waste of the taxpayers' money. This is the truck hole which enables certain special favored groups to get enormous privileges from the Treasury and from the taxpayers.

OIL COMPANIES EFFECTIVE TAX RATES LESS THAN HALF NORMAL RATE

The Joint Economic Committee, of which I was chairman at that time, in 1955 had a compendium made on Federal tax policy. It collected a great deal of very interesting material.

We found that the effective tax rate which was paid by 24 large petroleum companies, upon net income, was only

22.6 percent, whereas all other corporations in that year paid taxes at an effective rate of 48.1 percent. In other words, the fact is that the oil industry pays less than half the taxes, percentage-wise, which other industries pay.

That very fact leads to an overinvestment in the oil industry, as compared to other industries, and an improper use of the resources of labor and capital attracted there by tax favors.

I have made a study of 27 producing companies dealing in oil or gas. I shall introduce that into the RECORD very shortly. It shows that many such companies paid infinitesimal fractions of their profits in taxes.

INDIVIDUAL EXAMPLES

Eleven years ago, when some of us first started fighting this excessive depletion allowance, the Secretary of the Treasury published official statistics on certain unidentified individuals in the oil and gas industry, which showed that one individual who had a net income in the

years 1943 to 1947 of \$14,300,000 paid income taxes of only \$80,000 in the entire period of time. In other words, this man paid \$6 in taxes for every \$1,000 of income. He paid less taxes proportionately than a poor workman getting \$3,000 a year, or \$60 a week.

Mr. President, a table submitted by the Secretary of the Treasury in the House hearings on the Revenue Act of 1950 gives examples of the excessive income tax deductions from the depletion allowance and the allowance for drilling and development costs. I ask unanimous consent that a table showing income, deductions, and tax liabilities of 10 selected individual oil and gas operators for the 5-year period 1943-47 be printed at this point in the RECORD.

The PRESIDING OFFICER (Mr. METCALF in the chair). Is there objection to the request by the Senator from Illinois?

There being no objection, the table was ordered to be printed in the RECORD, as follows:

Income, deductions, and tax liabilities of 10 selected individual oil and gas operators for the 5-year period 1943-47

(Money figures in millions)

Individual operator	Net income			Special deductions		Taxable net income	Income tax liability	
	From oil and gas ¹	From other sources	Total	Percentage depletion ²	Development costs ³		Amount	Percent of total net income
A.....	\$10.5	\$3.8	\$14.3	2.2	\$13.0	⁴ - \$0.9	\$0.08	0.6
H.....	5.0	.8	5.8	3.1	2.1	.6	.5	8.6
C.....	3.9	.5	4.4	3.2	4.4	⁴ - 3.2	.15	3.4
D ⁵	9.3	.3	9.6	2.7	0	6.9	6.1	63.5
E.....	2.7	.8	3.5	1.0	.3	2.2	1.4	40.0
F.....	1.7	1.4	3.1	.8	1.5	.8	.6	19.4
G.....	7.7	-1.3	6.4	3.5	2.1	.8	.5	7.8
H.....	2.1	3.6	5.7	1.0	.6	4.1	2.2	38.6
I.....	1.7	.1	1.8	.5	1.0	.3	.2	11.1
J.....	8.0	-.7	7.3	2.9	1.7	2.7	2.2	30.1
Total.....	52.6	9.3	61.9	20.9	26.7	14.3	13.93	22.5

¹ Income after deductions for operating expenses, depreciation, adjusted-basis depletion, exploration costs and losses on abandonment.

² Excess of percentage depletion over adjusted-basis depletion.

³ Development costs are expenditures for the preparation of mineral properties for production, which are deducted as expenses in the year incurred. Consequently, these expenditures are not included in the tax basis of the property and future cost or adjusted-basis depletion is correspondingly reduced. The treatment of development costs as a current expense, however, does not diminish percentage depletion in subsequent years, since the latter is determined on the basis of income in those years.

⁴ While special deductions more than offset the total net income for the 5 years, some income tax was paid because there were deficits only in some years. A deficit caused by excess percentage depletion cannot be carried over against net taxable income of other years.

⁵ Includes only 4 years, 1943-46.

Source: Bureau of Internal Revenue, special tabulation.

Mr. DOUGLAS. Mr. President, while no such statistics have been published by the Treasury in recent years, there is no reason to suppose that the facts are any different or any better now.

The justification given for such a high deduction is that it is a needed inducement for exploration and drilling. There is something to this contention, but not enough to justify the added allowance of 27½ percent of gross revenue.

In the first place, the other tax features provided for the industry—as we have seen—are extremely liberal and, in addition to this, the capital gains treatment, which I have not gone into, gives even further advantages.

Another factor is involved. It is that despite the big depletion allowance, the average rates of profit in the industry do not seem to be appreciably higher than in other industries, although the oil and gas industry pays less than half

as much percentagewise in taxes as do other industries. This is a very clear indication that the tax favors lead to overinvestment in oil and gas, and that the overinvestment brings the average return down to about the level of other industries—not quite to that level, but to about that level. This brings in inefficient wells and inefficient producers.

Also, in its present form, this helps the big operators in the ways I have indicated.

WHAT THE AMENDMENT DOES

I am, therefore, proposing this amendment which would reduce the depletion allowance of 27½ percent to 15 percent if the taxpayer's gross income from oil and gas wells exceeds \$5 million in any 1 year, but that the allowance be reduced only from 27½ percent to 21 percent for those with a gross income from oil and gas wells of between \$1 million and \$5

million, and that the depletion allowance remain at 27½ percent for those whose gross incomes from oil and gas wells does not exceed \$1 million per year.

If I may be pardoned for saying it for the third or fourth time, it is necessary to drive home the fact that no farmer would lose a dollar from the royalties which he now collects, which normally are one-eighth of the gross income. No small operator would lose a dollar. An operator would have to have a good many wells to lose money. The weight of the reduction in the allowance would be on the big companies, which have enormous profits and which are driving the small producers out of the field.

Mr. President, the amendment is not a punitive one, for first, it would not do away with the depletion allowance altogether; and second, it would not affect at all the small wildcat driller or the small producer, except to his competitive advantage.

PROTECTS SMALL PRODUCER

There is a good reason for this last provision. Drilling for oil and gas involves some risk. It is estimated that only about one in nine wells which are drilled actually produce gas or oil. The small driller, with only a few wells over which to spread this risk, does not have enough wells to assure that he will hit the 1 in 9 and may, in fact, drill 20 or 30 dry holes before hitting oil or gas. Consequently, without a great number of wells over which to spread the risk, he takes a greater risk than the large driller, who will average 1 in 9 successful wells if he drills 100 or 200 wells a year.

Mr. President, it is the practice of the big companies to permit the wildcatters to go out ahead of them, to explore the fields, and to take the risks. When the wildcatters find oil, the big companies move in, take the land, put in multiple wells, and reap the profits.

The Treasury estimated sometime ago that the adoption of this amendment would result in a net revenue increase to the Federal Treasury of \$305 to \$310 million per year. At the present time I believe this amount would be at least \$320 million. Others have estimated that it would bring in as much as \$400 to \$500 million additional revenue a year.

The latter and more substantial estimate is the one made by the experts attached to the Library of Congress.

I point out that in its present form the tax bill would result in a deficit or loss of revenue of somewhere around \$500 to \$600 million a year. That is a very serious financial problem.

Mr. McNAMARA. That is a very conservative estimate, too.

Mr. DOUGLAS. The reduction in the depletion allowance would make good most of the loss and would help us to balance the books in large part, so far as the bill is concerned.

Mr. President, I ask unanimous consent that three tables showing the amount of depletion which corporations took as income tax reductions in the period 1946-58, these same deductions by total

asset classes for the years 1948-58, and a further table showing corporate depletion deductions and net income by total

asset classes for the years 1952-55, and for 1958, be printed in the RECORD at this point in my remarks.

There being no objection, the tables were ordered to be printed in the RECORD, as follows:

Selected corporate business deductions, all corporations, 1946-58

[Dollar amounts in millions]

Deduction	1946	1947	1948	1949	1950	1951	1952	1953	1954	1955	1956	1957	1958
Compensation of officers.....	\$5,143.1	\$6,026.4	\$6,733.3	\$6,743.0	\$7,606.8	\$8,122.0	\$8,430.0	\$8,776.7	\$9,113.2	\$10,480.7	\$11,045.1	\$11,829.6	\$12,395.3
Interest paid.....	2,251.0	2,501.4	2,758.7	3,045.1	3,211.9	3,700.5	5,013.2	5,680.9	6,270.6	7,058.4	8,281.0	10,004.5	11,070.2
Taxes paid.....	5,830.5	6,892.9	7,481.7	8,361.3	9,013.2	11,030.8	11,696.8	12,194.9	12,476.9	14,202.6	15,038.5	16,393.0	16,691.7
Contributions or gifts.....	213.9	241.2	239.3	222.6	252.4	343.0	398.6	494.5	313.8	414.8	418.0	417.3	395.4
Depletion.....	798.9	1,210.3	1,711.3	1,476.2	1,709.3	2,085.1	2,126.5	2,301.8	2,358.6	2,805.5	3,084.3	3,346.8	3,148.4
Depreciation.....	4,201.7	5,220.1	6,298.6	7,190.5	7,858.1	8,829.0	9,604.4	10,510.6	13,691.5	13,418.8	14,952.9	16,968.3	18,677.1
Amortization.....	64.5	58.9	38.9	30.6	43.3	291.9	831.3	1,515.3	2,590.3	2,590.3	2,625.9	2,463.9	1,999.2
Advertising.....	2,408.3	3,032.2	3,466.0	3,772.7	4,097.0	4,552.9	5,026.8	5,480.9	5,770.2	6,601.8	7,061.6	7,666.1	7,875.0
Amounts contributed under pension plans, etc. ¹	834.6	1,038.3	1,153.5	1,216.1	1,660.9	2,326.9	2,551.8	2,936.3	2,840.3	3,296.2	3,645.5	4,043.0	3,998.7
Other ²	5,892.1	7,338.4	8,062.8	7,998.7	8,371.3	9,709.7	10,493.6	11,520.5	11,445.5	12,959.1	14,325.4	15,476.4	15,521.2
Total selected deductions.....	27,638.6	33,560.1	37,944.1	40,056.8	43,824.2	50,991.8	56,803.4	62,273.3	65,191.2	74,975.1	81,781.1	90,235.1	93,499.4
Percentage distribution													
Compensation of officers.....	18.6	18.0	17.7	16.8	17.4	15.9	14.8	14.1	14.0	14.0	13.5	13.1	13.3
Interest paid.....	8.1	7.5	7.3	7.6	7.3	7.3	8.8	9.1	9.0	9.4	10.1	11.1	11.8
Taxes paid.....	21.1	20.5	19.7	20.9	20.6	21.6	20.6	19.6	19.1	18.9	18.4	18.2	17.9
Contributions or gifts.....	.8	.7	.6	.6	.6	.7	.7	.8	.5	.6	.5	.5	.4
Depletion.....	2.9	3.6	4.5	3.7	3.9	4.1	3.7	3.7	3.6	3.7	3.8	3.7	3.4
Depreciation.....	15.2	15.6	16.6	18.0	17.9	17.3	16.9	16.9	21.0	17.9	18.3	18.8	20.0
Amortization.....	.2	.2	.1	.1	.1	.6	1.5	2.4	3.5	3.5	3.2	2.7	2.1
Advertising.....	8.7	9.0	9.1	9.4	9.3	8.9	8.8	8.8	8.9	8.8	8.6	8.5	8.4
Amounts contributed under pension plans, etc. ¹	3.0	3.1	3.0	3.0	3.8	4.6	4.5	4.7	4.4	4.4	4.5	4.5	4.3
Other ²	21.3	21.9	21.2	20.0	19.1	19.0	18.5	18.5	17.6	17.3	17.5	17.1	16.6
Total selected deductions.....	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

¹ Deductions claimed under sec. 23(p) of the Internal Revenue Code for amounts contributed by employers under pension, annuity, stock-bonus, or profit-sharing plans, or other deferred compensation plans.

² Contributions under other employee benefit plans.

³ Comprises bad debts, repairs, and rent paid on business property.

Source: Internal Revenue Service, Statistics of Income, Corporation Income Tax Returns.

Corporate depletion deductions by total assets classes, 1948-58 ¹

[Dollar amounts in millions]

Assets classes	1948	1949	1950	1951	1952	1953	1954	1955	1956	1957	1958
Under \$50,000.....	\$4.9	\$3.7	\$4.0	\$3.5	\$3.1	\$4.7	\$4.2	\$5.7	\$8.6	\$12.5	\$9.2
\$50,000 and under \$100,000.....	5.5	4.0	4.4	3.7	5.2	3.7	4.3	5.2	6.9	6.4	5.9
\$100,000 and under \$250,000.....	16.1	11.9	12.6	12.1	13.5	13.5	15.7	27.2	21.1	22.7	22.3
\$250,000 and under \$500,000.....	21.4	16.1	17.1	21.4	21.2	21.4	22.6	26.0	27.5	33.8	32.1
\$500,000 and under \$1,000,000.....	40.8	31.4	31.5	41.4	35.1	38.6	32.2	45.1	43.1	47.0	42.8
\$1,000,000 and under \$5,000,000.....	126.1	101.0	120.8	160.8	150.3	154.0	147.0	191.5	181.6	174.1	167.0
\$5,000,000 and under \$10,000,000.....	72.5	57.5	68.5	83.8	85.7	83.3	73.7	80.0	96.7	124.6	91.4
\$10,000,000 and under \$50,000,000.....	245.2	213.1	278.9	318.9	297.7	306.1	290.3	351.2	339.9	358.3	333.6
\$50,000,000 and under \$100,000,000.....	89.7	92.8	115.2	120.8	131.2	119.8	134.0	178.1	249.0	241.6	200.2
\$100,000,000 or more.....	1,076.5	895.1	1,038.8	1,299.3	1,370.0	1,539.3	1,517.9	1,869.0	2,082.5	2,308.6	2,232.5
Total.....	1,698.9	1,426.5	1,691.8	2,065.8	2,112.9	2,284.3	2,242.4	2,779.1	3,050.7	3,329.7	3,137.0
Percentage distribution											
Under \$50,000.....	0.3	0.3	0.2	0.2	0.1	0.2	0.2	0.2	0.3	0.4	.03
\$50,000 and under \$100,000.....	.3	.3	.3	.2	.2	.2	.2	.2	.2	.2	.2
\$100,000 and under \$250,000.....	.9	.8	.7	.6	.6	.6	.7	1.0	.7	.7	.7
\$250,000 and under \$500,000.....	1.3	1.1	1.0	1.0	1.0	.9	1.0	.9	.9	1.0	1.0
\$500,000 and under \$1,000,000.....	2.4	2.2	1.9	2.0	1.7	1.7	1.4	1.6	1.4	1.4	1.4
\$1,000,000 and under \$5,000,000.....	7.4	7.1	7.1	7.8	7.1	6.7	6.6	6.9	5.9	5.2	5.3
\$5,000,000 and under \$10,000,000.....	4.3	4.0	4.1	4.1	4.1	3.6	3.3	2.9	3.2	3.7	2.9
\$10,000,000 and under \$50,000,000.....	14.4	14.9	16.5	15.4	14.1	13.4	12.9	12.6	11.1	10.8	10.6
\$50,000,000 and under \$100,000,000.....	5.3	6.5	6.8	6.8	6.2	5.2	6.0	6.4	8.1	7.3	6.4
\$100,000,000 or more.....	63.4	62.7	61.4	62.9	64.8	67.4	67.7	67.3	68.1	69.3	71.2
Total.....	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

¹ All returns with balance sheets.

Source: Internal Revenue Service, Statistics of Income, Corporation Income Tax.

Corporate depletion deductions and net income by total assets classes, 1952¹⁻⁵⁵

[Dollar amounts in millions]

Assets classes	1952			1953			1954			1955		
	Net income ²	Depletion deductions	Depletion deductions as percent of net income	Net income	Depletion deductions	Depletion deductions as percent of net income	Net income	Depletion deductions	Depletion deductions as percent of net income	Net income	Depletion deductions	Depletion deductions as percent of net income
Under \$50,000.....	\$382.5	\$2.6	0.7	\$370.6	\$3.2	0.9	\$354.9	\$3.3	0.9	\$422.6	\$4.7	1.1
\$50,000 and under \$100,000.....	577.0	4.7	.8	539.3	3.1	.6	518.1	2.9	.6	631.3	4.1	.6
\$100,000 and under \$250,000.....	1,364.9	11.2	.8	1,251.1	11.2	.9	1,251.3	13.3	1.0	1,571.8	20.8	1.3
\$250,000 and under \$500,000.....	1,336.0	17.5	1.3	1,223.0	18.0	1.5	1,252.2	17.5	1.4	1,589.6	22.0	1.4
\$500,000 and under \$1,000,000.....	1,044.7	27.4	1.7	1,473.2	28.8	2.0	1,459.3	23.9	1.6	1,871.0	37.0	2.0
\$1,000,000 and under \$5,000,000.....	4,716.4	129.2	2.7	4,331.5	120.1	2.8	4,172.5	120.8	2.9	5,293.6	155.2	2.9
\$5,000,000 and under \$10,000,000.....	2,319.1	64.6	2.8	2,188.6	70.2	3.2	2,025.7	59.5	2.9	2,410.3	65.5	2.7
\$10,000,000 and under \$50,000,000.....	6,105.7	250.9	4.1	6,123.9	263.6	4.3	5,555.0	245.0	4.4	6,736.3	305.1	4.5
\$50,000,000 and under \$100,000,000.....	2,806.5	122.4	4.4	2,854.4	106.5	3.7	4,813.8	113.4	4.0	3,174.9	167.6	5.0
\$100,000,000 or more.....	19,105.5	1,350.5	7.1	21,384.2	1,515.6	7.1	20,085.6	1,489.9	7.4	26,563.5	1,835.9	6.9
Total.....	40,368.3	1,980.9	4.9	41,750.9	2,140.3	5.1	39,518.4	2,089.3	5.3	50,270.9	2,608.1	5.2

¹ Returns with balance sheets and net income.² Compiled receipts less compiled deductions as shown in Statistics of Income.

Source: Internal Revenue Service, Statistics of Income, pt. 2.

Corporate depletion deductions and net income, by total assets classes, 1958¹

[Dollar amounts in millions]

Assets classes	1958			Assets classes	1958		
	Net income ²	Depletion deductions	Depletion deductions as percent of net income		Net income ²	Depletion deductions	Depletion deductions as percent of net income
Under \$50,000.....	\$514.7	\$7.8	1.5	\$5,000,000 and under \$10,000,000.....	\$2,169.1	\$62.9	2.9
\$50,000 and under \$100,000.....	746.2	4.3	.6	\$10,000,000 and under \$50,000,000.....	5,694.5	289.3	5.1
\$100,000 and under \$250,000.....	1,770.7	15.2	.9	\$50,000,000 and under \$100,000,000.....	2,960.8	158.0	5.3
\$250,000 and under \$500,000.....	1,637.7	26.8	1.6	\$100,000,000 and over.....	21,985.2	2,049.3	9.3
\$500,000 and under \$1,000,000.....	1,747.7	30.2	1.7	Total.....	43,716.2	2,775.5	6.3
\$1,000,000 and under \$5,000,000.....	4,489.6	131.8	2.9				

¹ Returns with balance sheets and net income.² Compiled receipts less compiled deductions.

Source: Internal Revenue Service, Statistics of Income, Corporation Income Tax Returns, 1958-59.

TABLE 40.—Corporate depletion deductions and net income, by major industrial group, 1958¹

[Dollar amounts in millions]

Major industrial group	1958			Major industrial group	1958		
	Net income ²	Depletion deductions	Depletion deductions as percent of net income		Net income ²	Depletion deductions	Depletion deductions as percent of net income
All industries.....	\$44,148.2	\$2,783.4	6.3	Transportation, communication, electric, gas and sanitary services.....	\$6,114.7	\$90.4	1.5
Agriculture, forestry, and fisheries.....	231.4	2.2	1.0	Wholesale and retail trade.....	5,440.3	18.5	.3
Mining.....	1,191.6	657.1	55.1	Finance, insurance, and real estate.....	8,809.5	105.8	1.2
Construction.....	939.5	6.3	.7	Lessors of real property except buildings.....	97.4	25.3	26.0
Manufacturing.....	20,314.2	1,901.7	9.4	Services.....	1,054.2	1.5	.1
Chemicals and allied products.....	2,651.0	79.7	3.0	Nature of business not allocable.....	22.9	4.3	18.8
Petroleum refining and related industries.....	1,451.7	1,369.6	94.3				
Stone, clay and glass products.....	1,889.1	153.9	17.3				
Primary metal industries.....	1,763.3	107.8	6.0				

¹ Returns with net income.² Compiled receipts less compiled deductions.

Source: Internal Revenue Service, Statistics of Income, Corporation Income Tax Returns, 1958-59.

Mr. DOUGLAS. Mr. President, the first table shows that in 1958, the total amount of deductions for depletion by all corporations was in the amount of \$3,148,400,000. The second table shows that some \$2,232,500,000 of the corporate depletion deductions in 1958, or some 71.2 percent of them, were taken by corporations with net assets of over \$100 million. Thus, the really big corporations took the giant's share—over two-thirds—of the depletion allowances.

This is not something that goes to the small man. It is something that goes to the giant corporations. My amendment would exempt the small operator.

Mr. PROXMIRE. Mr. President, will the Senator yield?

Mr. DOUGLAS. I am glad to yield.

Mr. PROXMIRE. Is it not true that the amendment of the Senator from

Illinois provides that the large firm, that is, the firm which grosses more than \$5 million a year, would have its depletion allowance reduced to 15 percent, but the small firm, which grosses less than \$1 million, would have no reduction in depletion whatsoever?

Mr. DOUGLAS. That is absolutely correct.

Mr. PROXMIRE. Is it not also correct that the amendment would not eliminate a depletion allowance for larger firms; but would provide an allowance near the highest level which other minerals enjoy?

Mr. DOUGLAS. Operators in the sulfur industry receive 23 percent.

Mr. PROXMIRE. With the exception of sulfur and a few other minerals. For some minerals, as I understand, operators obtain as little as 5 or 6 percent

depletion allowance. Others get 15 percent.

Mr. DOUGLAS. That is true, although the allowance on oyster shells and clam shells is rising, and I believe it is rising on sand and gravel.

Mr. PROXMIRE. So the incidence of the increased revenue the Federal Government would receive on the basis of the amendment of the Senator from Illinois would fall upon the big firms, and to a much lesser extent on firms of moderate size, that is, firms which gross between \$1 and \$5 million.

Mr. DOUGLAS. Yes; and landowners would get exemption.

Mr. PROXMIRE. The fabled and time-honored wildcatter, as long as he operated on a reasonably small scale, would also be exempt?

Mr. DOUGLAS. The Daniel Boones of the oil industry would not have their depletion allowance reduced. They could still go scouting ahead.

Mr. PROXMIRE. The amendment of the Senator from Illinois would primarily provide that the giants of the petroleum industry, that is, those firms with assets over \$100 million a year—

Mr. DOUGLAS. Over \$5 million a year.

Mr. PROXMIRE. I understand that, but the Senator gave statistics showing—

Mr. DOUGLAS. Those that had assets of over \$100 million.

Mr. PROXMIRE. I should say firms that had assets of more than \$100 million. Those firms took what proportion of the total depletion allowance?

Mr. DOUGLAS. They took 71 percent of the total depletion allowance.

Mr. PROXMIRE. More than two-thirds?

Mr. DOUGLAS. The Senator is correct.

Mr. PROXMIRE. Those would be the firms, primarily, which would pay more taxes to the Federal Government under the Senator's amendments.

Mr. DOUGLAS. That is correct.

Mr. PROXMIRE. Is it not also true that the industry is far more lightly taxed than is industry generally?

Mr. DOUGLAS. The figures which I introduced show that the 24 leading oil firms paid approximately 22 percent of their profits in taxes, whereas all corporations paid approximately 48 percent. So based on this study oil firms pay less than half the taxes that business corporations as a whole pay. That has led to overinvestment in the industry.

Mr. PROXMIRE. I thank the Senator.

Mr. DOUGLAS. I thank the Senator from Wisconsin. His views on this, as on so many other points, are cogent and well taken.

Mr. President, back in 1950, Secretary of the Treasury Snyder came before the House Ways and Means Committee and urged that it reduce the depletion allowances. He made a very cogent argument for his position, and he further placed in the record a great many facts and figures which were informative and persuasive. I ask unanimous consent that his testimony and exhibits, which appear in the hearings of the Ways and Means Committee on the Revenue Revision of 1950, volume 1, February 3, 1950, be printed in the RECORD at this point.

There being no objection, the testimony and exhibits were ordered to be printed in the RECORD, as follows:

SECRETARY OF TREASURY SNYDER

[From hearings, Ways and Means Committee, 81st Cong., 2d sess., vol. 1., Feb. 3, 1950]

SPECIAL DEPLETION ALLOWANCE

Depletion in ordinary accounting usage is intended to permit taxpayers to recover the cost of mineral properties over the producing life of the properties. Depletion is the counterpart of depreciation which is intended to permit recovery of the cost of other assets over the period of their useful life. When the original investment has been recovered, no further depreciation is allowed for tax purposes. However, in the

case of depletion, special provisions which allow recovery of more than the cost of mineral properties have been in the law since 1918.

Under present law, special allowances are granted on the basis of specified percentages of gross income for different types of minerals. The percentage of gross income allowed is 27½ percent for oil and gas, 23 percent for sulfur, 15 percent for metals and a large number of nonmetallic minerals, and 5 percent for coal.

Percentage depletion continues for the life of the property and generally results in the tax-free recovery of many times the cost. It is granted to those purchasing properties as well as to those operating properties they have developed. The allowances have become more valuable as tax rates have been increased.

Furthermore, the benefits from percentage depletion are increased by provisions which permit development costs to be deducted as an expense in the year incurred instead of being treated as a capital cost to be recovered later through depletion deductions. This is equivalent to a double deduction for the same costs, once when they are incurred and again under percentage depletion. In the oil industry during 1946 and 1947, for every \$3 million allowed as percentage depletion, another \$2 million was deducted as development costs.

The combination of percentage depletion and the expensing of development costs provides a mechanism for pyramiding extensive holdings in oil assets with payment of little or no income tax.

As the President has indicated, millions of dollars are made annually from operating oil properties on which little or no income tax is paid. The President mentioned one outstanding example. You will find others in the attached material (exhibit 2). In the examples cited, annual incomes, on the average, of over \$1 million were obtained on which an average tax of only 22½ percent was paid. This is the rate now paid by persons with incomes of less than \$25,000.

These illustrations suggest how much additional revenue the Government would gain by limiting some of these special allowances.

You will find from an examination of the materials I am submitting to assist the committee in considering revision of these provisions that:

First, the estimated revenue loss is between 400 and 500 million dollars annually. This is as much as the yield of all the retail excises.

Second, the allowance is especially excessive in the case of oil and gas and exempts a higher proportion of the earnings of this industry which may expense more of its development costs than the other mineral industries.

Third, the provision has been found to be of little benefit to small prospectors on whose behalf it is so frequently supported.

Fourth, these deductions enable high-income individuals to reduce to negligible proportions taxes on income from sources totally unrelated to these industries.

There are a number of ways in which the necessary revision of present allowances can be accomplished. In general, these involve either the limitation of percentage depletion or the termination of the option to expense development costs. The benefits of expensing development costs are confined to the finding of new properties. Percentage depletion on the other hand may be obtained on established as well as new properties, and regardless of whether the recipient contributed to the development of the property. The reduction of percentage depletion would tend to reduce windfalls while protecting incentives for exploration.

A reasonable way to reduce the excessive benefits would be to limit the percentage of gross income which might be deducted as

depletion. A reduction in the present net income limitation would leave the more excessive allowances untouched while reducing the benefits on the small, less profitable properties.

Specifically it is proposed that percentage depletion for oil, gas, and sulfur be reduced to 15 percent of gross income and that percentage depletion for nonmetallic minerals be reduced to 5 percent. The existing 15-percent rate for depletion allowed to the metals would be left unchanged.

It is further proposed that oil and gas operators who elect to expense intangible drilling and development costs be required to reduce income from the property by the amount of such expensed costs in computing their depletion allowance. This requirement will reduce the extent of the double deduction now enjoyed by oil and gas enterprises with respect to certain of their capital costs.

Together these proposals would remove the more obvious inequities of the present system without interfering significantly with production incentives.

EXHIBIT 2

SPECIAL DEPLETION ALLOWANCES FOR MINERAL PROPERTIES

One of the major avenues of escape from income tax is the special depletion allowance now accorded mineral properties. This subject has received consideration by congressional committees on a number of occasions.

Nearly 25 years have passed, however, since the date of the investigation of depletion costs on which present allowances were established. In the intervening years there have been important basic changes in those industries.

This study presents current information on the basic aspects of this problem and discusses the considerations affecting the desirability of the present allowances.

I. PRESENT PROVISIONS

The Federal income tax recognizes depletion of wasting mineral assets as a deductible cost in determining net taxable income. The purpose is to allow the taxpayer to recover tax free the capital he has invested in the mineral property. Special allowances in excess of cost are granted to certain groups of taxpayers. In most cases these special allowances are based on a percentage of gross income. Of less importance are special allowances based on discovery value.

(a) Percentage depletion

Percentage depletion is computed as a specified percentage of gross income, without regard to the capital cost of the property. The rates range as high as 27½ percent of gross income in the case of petroleum, but the deduction is limited to 50 percent of the net income (computed without regard to depletion) from the particular property. The following percentages of gross income are allowed different minerals under present law.

Mineral:	Percentage rate on gross income
Oil and gas.....	27½
Sulfur.....	23
Metals.....	15
Coal.....	5
Bauxite, fluorspar, flake graphite, vermiculite, beryl, feldspar, mica, talc (including pyrophyllite), lepidolite, spodumene, barite, ball, sagger, and china clay, phosphate rock, rock asphalt, trona, bentonite, gilsonite, thenardite, and potash.....	15

Percentage depletion continues to be deductible even after 100 percent of the invested capital has been retrieved tax free. The total tax-free recoveries may be substantially in excess of the cost of the property,

and in a large number of cases amount to many times the capital investment.

(b) *Discovery depletion*

Those minerals which are not eligible for percentage depletion may qualify for discovery depletion, under certain conditions. Owing to the wide range of minerals excluded because they are eligible for percentage depletion, and the special conditions attaching to the use of discovery depletion, it applies only to certain nonmetallic substances and is of limited significance at the present time.

Under discovery depletion, a taxpayer who discovers a mine on an unproven tract, the value of which is materially larger than the cost to the taxpayer, is allowed depletion deductions designed to amortize the appreciated discovery value over the economic life of the mine. As in the case of percentage depletion, the annual deduction for discovery depletion is limited to 50 percent of the net income from the property. However, aggregate tax-free recoveries under this method are limited to the discovery value.

(c) *Cost or adjusted-basis depletion*

Percentage depletion is one of the most complex provisions in the tax law. Depletion allowances are computed with respect to each individual mineral property. Mineral-tax payers commonly own several, and in many cases thousands of properties. Each year for each property the taxpayer takes the largest depletion deduction allowable. Both gross and net income must be determined for each separate property to compute percentage depletion. Moreover, a corporate-tax payer's accounting for each property entitled to percentage depletion must reflect each of the three different depletion concepts: (1) Allowable depletion, including percentage or discovery, (2) adjusted-basis depletion, and (3) strict cost depletion.

In all cases the taxpayer is allowed depletion based on cost as a minimum. The annual cost depletion (usually termed adjusted-basis depletion) is computed by spreading the original cost, less amounts previously recovered tax free, over the estimated remaining life of the property, measured in units of mineral product. Increased deductions for percentage depletion reduce the remaining cost or adjusted basis more rapidly. Therefore, the adjusted-basis depletion, which represents the minimum annual deduction, must be recomputed at a lower figure each year after percentage depletion is taken.¹ When the original cost is exhausted through depletion allowances the adjusted-basis depletion is reduced to zero, although percentage depletion may continue to be deducted.

Corporations also account for annual cost depletion computed without regard to amounts recovered from time to time through percentage depletion, in determining their net profits for reports to stockholders and other purposes. Cost depletion in this sense is also recognized for tax purposes in connection with the treatment of liquidating dividends in the hands of the stockholders.²

¹ In addition to determining the minimum annual allowance, the adjusted-basis depletion is important in computing the net operating loss deduction. Under the present 2-year carryback and 2-year carryforward of net operating losses, the loss to be carried over is reduced by the excess of percentage over cost depletion (and similar tax-exempt items) in the year in which the loss occurs. Similarly, the amount of the loss which is deductible is reduced by the amount of such exempt income in the year to which the loss is carried.

² Under existing law dividends to stockholders are taxable to the extent they are paid out of earnings and profits. For this purpose, earnings and profits are computed on the basis of cost depletion.

For purposes of determining gain or loss upon sale or other disposition of a depletable property, the tax basis is reduced by the total amount of allowable depletion (percentage, discovery, or adjusted-basis depletion) in previous years.³ While percentage depletion may continue even though more than 100 percent of the basis has been recovered tax free, the basis for determining gain or loss is reduced only to zero.

(d) *Expensing of capital costs*

In addition to depletion allowances, certain capital costs of developing mineral properties are treated as expenses incurred in doing business and allowed as deductions in the year incurred. This expensing treatment does not reduce allowable percentage depletion in future years, which is based on the income from the developed property. This results in a double deduction for recovery on the same capital investment.

Owners of oil or gas wells have wide opportunities for expensing capital costs incurred in developing their properties. At their option, they may treat intangible drilling and development costs of wells (including expenditures for labor, supplies, repairs, and hauling) as current expenses deductible from taxable income from any source. For example, 90 percent of an oil operator's capital outlay, exclusive of depreciable items, may be for intangible drilling and development costs. If this is deducted as a current expense, and thus recovered tax free at the outlet, only 10 percent of the investment remains to be recovered through depletion allowances. Hence, depletion allowances based on the entire income in effect overlap the initial deduction of a large portion of the capital outlays.

In the case of mines, development costs can be immediately offset against income only to the extent that there are receipts derived from the mine during the development period. However, if considerable quantities of ore are taken out while developing a mine to full producing status, it is possible for a taxpayer to recoup, tax free, immediately a large part of the capital costs of development.

II. BACKGROUND AND DEVELOPMENT OF SPECIAL DEPLETION ALLOWANCES

The original income-tax legislation provided a "reasonable allowance," not to exceed 5 percent of gross income, for wasting mineral assets. This was later changed to a more specific allowance of depletion based on cost, or 1913 value.

Allowances in excess of cost depletion were first granted in the term of discovery depletion in 1918 as a measure to stimulate mineral exploration for war purposes and to lessen tax burdens on small-scale prospectors who made discoveries after years of fruitless search. Discovery depletion deductions allowed the discoverer of any new mineral deposit to retrieve not only his costs but also the materially larger appreciated value of the property at the time its profitability was established. Since no limit was placed on the discovery depletion deduction, in many cases the deduction was in excess of the income from the discovered property and served to offset income from other sources. To prevent such excessive discovery depletion allowances, the annual deduction was limited in 1921 to 100 percent of the net income from the mineral property. In 1924, the limit was reduced to 50 percent of the net income from the property, in order to provide for the taxation of at least one-half of the income from these properties.

Percentage depletion was substituted for discovery depletion in the case of oil and gas properties in 1926 and extended to metals, sulfur, and coal in 1932. The original

³ For years prior to 1932 the excess of percentage over cost depletion was not applied to reduce the tax basis.

percentage-depletion rates, still embodied in present law, were in general fixed at levels which would permit the respective industries approximately the same total annual depletion they had previously enjoyed under discovery depletion.

Despite the recommendation of the Treasury in 1942 that percentage depletion be eliminated, it was extended in 1942 and 1943 as a temporary measure to certain non-metallic minerals at the 15-percent rate applicable to metals. In 1947 the temporary wartime extensions were made permanent, and in addition some items not previously covered were granted the special allowance. Since 1947 a wide range of nonmetallic producers who have not been granted percentage depletion have sought similar preferential tax treatment.⁴

III. SURVEY OF DEPLETION AND RELATED ALLOWANCES

Information on percentage depletion and other special allowances for mineral producers has been recently developed through a special survey of 350 corporation income-tax returns. These returns accounted for about three-fourths of all corporation income-tax allowances for depletion for the year 1946 (table 1). Although the survey group does not necessarily represent a cross-section of the mineral industries, the high proportion of tax allowances for depletion provides reliable information on the mineral-depletion provisions. The statistical data obtained in the course of this survey are presented in tables 1 to 10.

While the survey covers corporations only, it is estimated that corporations account for more than 80 percent and individuals for less than 20 percent of all depletion deductions.

(a) *Excess depletion and resulting revenue loss*

The allowable depletion deducted by the corporations included in this survey amounted to \$555 million in 1946 and \$839 million in 1947. Of these amounts only 10 to 15 percent represented adjusted-basis depletion which would have been required to recover original investment cost.⁵ The remaining 85 to 90 percent constituted the excess allowance attributable to the special depletion provisions for mineral industries (table 2).

The indicated revenue loss for all corporations in the survey due to excess depletion was about \$180 million in 1946 and \$290 million in 1947 (table 3). On the basis of these findings it is estimated that the total revenue loss for all corporations due to excess depletion was nearly \$250 million in 1946 and \$400 million in 1947.

(b) *Distribution of excess depletion by industry groups*

The excess of percentage depletion over cost or basis depletion was correspondingly high for most industry groups. Relatively low excess depletion for a few industries, such as coal and the stone, clay, and glass group, reflects either a low-percentage depletion rate (5 percent for coal) or ineligibility or important components of the industry for percentage depletion.

A high proportion of the excess depletion shown in table 2 was received by corporations whose major activity was other than mining and quarrying. In 1946, for example, \$345 million or more than 70 percent of the

⁴ Within the past 3 years bills have been introduced in Congress to extend percentage depletion to ambygonite, oil shale, tripoli, marble, pumice, scoria, limestone, crushed stone, perlite, diatomaceous earth, granite, borax, calcium and magnesium carbonates, shell, sand, gravel, stone, and all other non-metallic clays and minerals.

⁵ In most cases the adjusted-basis depletion was approximately equal to cost depletion.

total excess was deducted by manufacturing enterprises (notably in the petroleum field) representing large integrated firms whose predominant industrial activity was not mineral extraction.

(c) *Distribution of special depletion and related allowances by mineral products*

Survey data for 1946 and 1947 showing the distribution of depletion allowances (including deductions for development costs) classified by the principal mineral products are presented in tables 4 and 5. As shown in these tables, the bulk of the benefit of percentage depletion in excess of basis depletion was derived by the oil and gas group. They received almost 85 percent of the excess depletion compared with 55 percent of the gross income for corporations included in the survey.

Total deductions for development costs by the selected corporations were \$394 million in 1946 and \$486 million in 1947. Comparison of the development-cost deductions with the excess of percentage over basis depletion for these 2 years indicates that for every \$3 allowed as percentage depletion another \$2 was deducted as development costs. In addition, substantial deductions were taken for exploration costs and losses on abandonment, amounting to \$204 million in 1946 and \$255 million in 1947.

Nearly all of the development-cost deductions were taken by oil and gas producers, and these producers also claimed most of the allowances for exploration and losses on abandonment.

Substantial variations are also shown by tables 4 and 5 in the relative tax benefits derived from special depletion allowances among different types of mineral producers, due in large part to disparities in the rates of percentage depletion. In 1947, for example, allowable depletion was about equivalent to basis depletion for nonmetallics not entitled to percentage depletion, about 3 times basis depletion for coal, 5 times basis depletion for metals, and 16 times basis depletion for oil.

Sulfur producers were entitled to virtually no basis depletion, yet more than one-third of their aggregate net income was excluded from taxation through excess percentage depletion.

The relative importance of special depletion allowances for different type of mineral producers is presented in table 6. As shown in this table, all the corporations included in the survey had depletion deductions equal to about 40 percent of their net income before depletion in the years 1946-47. By contrast, the amount of basis depletion required to recover remaining cost ratably over the useful economic life was only 6 percent of net income in 1946 and 3.6 percent in 1947. Significant variations are shown among mineral products. Thus, depletion allowances in 1946 amounted to 49 percent of net income in the case of oil and gas compared with 1½ percent for nonmetallic products not entitled to percentage depletion, and 18 percent for all nonmetals.

(d) *Depletion allowances in relation to size of firm*

The distributions of various mineral-depletion allowances in dollar amounts and in relation to income, by size of firm, for 1946 and 1947, are shown in tables 7 and 8.

As shown in table 7, about three-fourths of the total depletion allowances and of the excess of percentage over basis depletion was received by very large corporations, with assets of at least \$100 million. By contrast these firms received slightly less than two-thirds of the total gross income from mining.

The percentage of income excluded from taxation through depletion allowances tends to be greater for larger corporations (table 8). In 1947, for example, firms with assets of \$100 million and over had depletion allowances of 20 percent of their gross and 38 percent of their net income, as against 9 percent of gross income and 34.5 percent of net income for corporations with assets between \$100,000 and \$1 million. The bene-

fits of special depletion allowances, reflected in the ratio of allowable depletion to basis depletion, also tend to increase with the size of the firm. In 1947, for example, the allowable depletion of corporations with assets of \$100 million and over was 13 times their basis depletion as compared with about 8 times for corporations with assets between \$1 million and \$10 million.

IV. ILLUSTRATIVE CASES SHOWING TAX EFFECTS OF SPECIAL ALLOWANCES

In connection with the survey of special depletion and related allowances, the effect of these provisions on the tax liabilities of particular taxpayers was studied.

Substantial reductions in income taxes were obtained by a number of individual oil and gas operators for the 5 years 1943 to 1947. In 10 illustrative cases, summarized in table 9, the effective rate of tax on net economic income (based on cost or basis depletion) varied from 63.5 percent to as low as six-tenths of 1 percent. This represents a striking difference between the effective rates of tax actually paid and the general statutory rates on such income, which ranged as high as 90 percent in these years.

During the 5-year period these 10 individual taxpayers received a total economic net income of \$52.6 million from oil and gas properties. This net income was computed after all deductions for operating expenses, depreciation, basis depletion, exploration costs, and losses on unsuccessful ventures. These taxpayers also received a total of \$9.3 million of net income from other sources. Of their aggregate net income from all sources, totaling \$61.9 million, 77 percent was eliminated for tax purposes through the special deductions.

Similar information for 20 corporations taken from income tax returns for 1947 is shown in table 10.

(NOTE.—In the following tables figures are rounded and will not necessarily add to totals. Percentages were computed on the basis of unrounded figures.)

TABLE 1.—Percentage of allowable mineral depletion included in survey of selected corporations, 1946
[Money figures in millions]

Industry group ¹	Allowable depletion for all corporations ²	Allowable depletion for selected corporations ²		Industry group ¹	Allowable depletion for all corporations ²	Allowable depletion for selected corporations ²	
		Amount	Percent of industry total			Amount	Percent of industry total
Mining and quarrying:				Manufacturing:			
Metal mining.....	\$46.1	\$35.1	76.0	Chemicals and allied products.....	\$14.4	\$9.7	67.1
Coal.....	51.0	17.6	34.4	Petroleum and coal products.....	388.0	350.6	90.3
Crude oil and natural gas.....	124.1	72.7	58.6	Iron, steel, and products.....	21.0	17.3	82.3
Nonmetallic mining.....	15.8	12.8	80.8	Nonferrous metals and products.....	23.5	14.5	61.8
Mining not allocable.....	.3	.1	32.0	Stone, clay, and glass products.....	2.1	.1	7.1
				Other manufacturing.....	3.3	0	0
Total mining and quarrying.....	237.3	138.1	58.2	Total manufacturing.....	452.4	392.2	86.7
				Other groups.....	55.5	24.5	44.2
				Total all groups.....	745.1	554.9	74.5

¹ The industry classification is the business activity reported on the tax return. When multiple businesses are reported, the classification is the business activity which accounts for the largest percentage of total receipts.

² Allowable depletion is the deduction permitted for income tax purposes, and is the larger of either adjusted-basis depletion or percentage depletion.

Source: Statistics of Income for 1946, pt. 2, preliminary, for all corporations; Bureau of Internal Revenue, Statistical Division, special tabulation, for the selected corporations.

TABLE 2.—Mineral depletion allowances for selected corporations, by industry groups, 1946 and 1947
[Money figures in millions]

Industry groups ¹	1946				1947			
	Number	Allowable depletion ²	Excess over basis depletion ³		Number	Allowable depletion ²	Excess over basis depletion ³	
			Amount	Percent of allowable depletion			Amount	Percent of allowable depletion
Mining and quarrying:								
Metal mining.....	68	\$35.1	\$28.7	82.0	66	\$64.0	\$54.9	85.9
Coal.....	53	17.6	10.5	59.9	52	21.6	14.9	69.2
Crude oil and natural gas.....	66	72.7	62.0	85.4	60	110.5	100.2	90.9
Nonmetallic mining.....	18	12.8	12.5	98.1	17	16.0	15.8	98.8
Mining not allocable.....	1	.1	(⁴)	5.0	1	.1	(⁴)	23.3
Total mining and quarrying.....	206	138.1	113.8	82.4	196	212.2	185.8	87.6
Manufacturing:								
Chemicals and allied products.....	14	9.7	7.3	75.5	14	11.7	9.4	80.3
Petroleum and coal products.....	45	350.6	321.9	91.8	44	538.7	509.0	94.4
Iron, steel and products.....	14	17.3	11.0	63.4	16	25.9	17.2	66.3
Nonferrous metals and products.....	8	14.5	5.1	34.8	8	17.5	10.4	59.4
Stone, clay, and glass products.....	5	.2	(⁴)	32.5	5	.2	.1	56.3
Total manufacturing.....	86	392.2	345.3	88.0	87	594.0	546.1	91.9
Other groups.....	60	24.5	20.8	84.9	61	32.6	28.0	86.0
Total all groups.....	352	554.0	479.9	86.5	344	838.7	759.9	90.6

¹ The industry classification is the business activity reported on the tax return. When multiple businesses are reported, the classification is the business activity which accounts for the largest percentage of total receipts.
² Allowable depletion is the deduction permitted for income tax purposes, and is the larger of either adjusted-basis depletion or percentage depletion.
³ Basis depletion is the deduction necessary to recover the unamortized portion of

the taxpayer's depletable property over its estimated remaining useful life. The unamortized portion, or adjusted basis, is reduced each year by the amount of allowable depletion.
⁴ Less than \$50,000.
Source: Bureau of Internal Revenue, Statistical Division, special tabulation.

TABLE 3.—Computed revenue loss resulting from excess mineral depletion deductions, selected corporations, by industry groups, 1946 and 1947 ¹
[In millions]

Industry group ²	1946 (352 returns)	1947 (344 returns)	Industry group ²	1946 (352 returns)	1947 (344 returns)
Mining and quarrying:			Manufacturing—Continued		
Metal mining.....	\$10.9	\$20.9	Petroleum and coal products.....	\$122.3	\$193.4
Coal.....	4.0	5.7	Iron, steel, and products.....	4.2	6.5
Crude oil and natural gas.....	23.6	38.1	Nonferrous metals and products.....	1.9	3.9
Nonmetallic mining.....	4.8	6.0	Stone, clay, and glass products.....	(³)	(³)
Mining not allocable.....	(³)	(³)	Total manufacturing.....	131.2	207.5
Total mining and quarrying.....	43.3	70.6	Other groups.....	7.9	10.6
Manufacturing:			Total all groups.....	182.4	288.8
Chemicals and allied products.....	2.8	3.6			

¹ Computed at the standard corporation rate of 38 percent.
² The industry classification is the business activity reported on the tax return.

When multiple businesses are reported, the classification is the business activity which accounts for the largest percentage of total receipts.
³ Less than \$50,000.

TABLE 4.—Mineral depletion and related allowances for selected corporations, by principal mineral products, 1946

[Money figures in millions]

Principal mineral products	Number of corporations	Income subject to depletion		Depletion		Other capital recovery deductions	
		Gross ¹	Net ²	Allowable ³	Basis ⁴	Development costs ⁵	Exploration costs and losses on abandonment ⁶
Metals:							
Iron.....	20	\$335.0	\$56.2	\$18.9	\$5.6	\$6.1	\$0.1
Copper.....	12	240.4	91.2	23.3	12.0	.6	1.0
Lead and zinc.....	22	68.9	21.0	10.5	2.5	5.0	.3
Gold and silver.....	14	47.1	16.0	6.1	.3	.9	.1
Other metals.....	8	37.8	7.2	3.3	(?)	.1	(?)
Metals not allocable.....	9	32.1	8.5	3.0	.3	(?)	.2
Total, metals.....	85	761.3	200.2	65.0	20.8	12.7	1.8
Coal:							
Anthracite.....	17	209.6	27.7	8.1	5.0	(?)	(?)
Bituminous, lignite, etc.....	52	432.8	44.5	16.2	5.0	(?)	(?)
Total, coal.....	69	642.4	72.2	24.3	10.0	(?)	(?)
Oil and gas.....	163	1,837.6	904.2	447.1	41.9	381.2	161.3
Sulfur.....	8	66.2	34.5	12.3	(?)		20.7
Nonmetals:							
Entitled to percentage depletion ⁷	19	90.4	20.0	5.9	2.0		.1
Not entitled to percentage depletion.....	8	56.1	13.4	.2	.2	0.3	20.0
Total nonmetals.....	27	146.6	33.3	6.2	2.2	.3	20.2
Grand total.....	352	3,454.1	1,244.4	554.9	74.9	394.2	204.0

¹ Gross income subject to depletion represents the amount for which the taxpayer sells, or could sell, in the immediate vicinity of the mine or well, the crude mineral output thereof.

² Net income subject to depletion represents the gross income subject to depletion less the allowable tax deductions attributable to the particular mineral property.

³ Allowable depletion is the deduction permitted for income-tax purposes, and is the larger of either adjusted-basis depletion or percentage depletion.

⁴ Basis depletion is the deduction necessary to recover the unamortized portion of the taxpayers' depletable property over its estimated remaining useful life. The unamortized portion, or adjusted basis, is reduced each year by the amount of allowable depletion.

⁵ Development costs are expenditures for the preparation of mineral properties for production, which are deducted as expenses in the year incurred. Consequently, these expenditures are not included in the tax basis of the property and future cost or adjusted-basis depletion is correspondingly reduced. The treatment of development

costs as a current expense, however, does not diminish percentage depletion in subsequent years, since the latter is determined on the basis of income in those years.

⁶ Tax deductions for exploration costs represent expenditures which are made in the search for mineral deposits but which cannot be attributed to the capital costs of particular depletable properties. Abandonment losses represent tax deductions for recovery of capital invested in particular mineral properties which are abandoned before recovery of adjusted basis. Both exploration costs and abandonment losses represent tax deductions for capital recovery in addition to depletion deductions.

⁷ Less than \$50,000.

⁸ The following nonmetallies are entitled to percentage depletion: Fluorspar, ball and sagger clay, rock asphalt, potash, flake graphite, vermiculite, beryl, feldspar, mica, talc, lepidolite, spodumene, barite, bauxite, china clay, phosphate rock, bentonite, trona, gilsonite, and thenardite.

Source: Bureau of Internal Revenue, Statistical Division, special tabulation.

TABLE 5.—Mineral depletion and related allowances for selected corporations, by principal mineral products, 1947

[Money figures in millions]

Principal mineral products	Number of corporations	Income subject to depletion		Depletion		Other capital recovery deductions	
		Gross ¹	Net ²	Allowable ³	Basis ⁴	Development costs ⁵	Exploration costs and losses on abandonment ⁶
Metals:							
Iron.....	21	\$310.8	\$90.3	\$26.7	\$7.5	\$7.2	\$0.3
Copper.....	11	432.1	224.3	45.3	12.1	.9	.9
Lead and zinc.....	23	99.4	35.3	14.6	3.1	4.8	.1
Gold and silver.....	12	66.8	24.3	9.1	.2	1.1	1.6
Other metals.....	7	45.5	7.5	3.0	(?)	.1	(?)
Metals not allocable.....	12	54.6	17.6	5.5	.4	.1	.3
Total metals.....	86	1,009.2	399.2	104.2	23.3	14.3	3.2
Coal:							
Anthracite.....	16	211.6	18.3	7.5	4.7	(?)	
Bituminous, lignite, etc.....	55	612.5	87.2	25.4	6.2	.1	.3
Total coal.....	71	824.1	105.4	33.0	10.9	.1	.3
Oil and gas.....	153	\$2,691.5	\$1,544.9	\$677.7	\$42.6	\$471.1	\$199.9
Sulfur.....	8	80.3	43.8	14.9	(?)		25.8
Nonmetals:							
Entitled to percentage depletion ⁷	17	68.7	20.2	8.7	1.8	(?)	.2
Not entitled to percentage depletion.....	9	102.2	53.4	.3	.3	.4	25.1
Total nonmetals.....	26	170.9	73.6	9.0	2.1	.4	25.4
Grand total.....	344	4,775.9	2,166.9	838.7	78.8	486.0	254.5

¹ Gross income subject to depletion represents the amount for which the taxpayer sells, or could sell, in the immediate vicinity of the mine or well, the crude mineral output thereof.

² Net income subject to depletion represents the gross income subject to depletion less the allowable tax deductions attributable to the particular mineral property.

³ Allowable depletion is the deduction permitted for income-tax purposes, and is the larger of either adjusted-basis depletion or percentage depletion.

⁴ Basis depletion is the deduction necessary to recover the unamortized portion of the taxpayers' depletable property over its estimated remaining useful life. The unamortized portion, or adjusted basis, is reduced each year by the amount of allowable depletion.

⁵ Development costs are expenditures for the preparation of mineral properties for production, which are deducted as expenses in the year incurred. Consequently, these expenditures are not included in the tax basis of the property and future cost or adjusted-basis depletion is correspondingly reduced. The treatment of develop-

ment costs as a current expense, however, does not diminish percentage depletion in subsequent years, since the latter is determined on the basis of income in those years.

⁶ Tax deductions for exploration costs represent expenditures which are made in the search for mineral deposits but which cannot be attributed to the capital costs of particular depletable properties. Abandonment losses represent tax deductions for recovery of capital invested in particular mineral properties which are abandoned before recovery of adjusted basis. Both exploration costs and abandonment losses represent tax deductions for capital recovery in addition to depletion deductions.

⁷ Less than \$50,000.

⁸ The following nonmetallies are entitled to percentage depletion: Fluorspar, ball and sagger clay, rock asphalt, potash, flake graphite, vermiculite, beryl, feldspar, mica, talc, lepidolite, spodumene, barite, bauxite, china clay, phosphate rock, bentonite, trona, gilsonite, and thenardite.

Source: Bureau of Internal Revenue, Statistical Division, special tabulation.

TABLE 6.—Allowable and basis depletion related to income, selected corporations, by principal mineral products, 1946 and 1947
[Percent]

Principal mineral products	1946				1947			
	Percent of gross income		Percent of net income		Percent of gross income		Percent of net income	
	Allowable depletion ¹	Basis depletion ²	Allowable depletion ¹	Basis depletion ²	Allowable depletion ¹	Basis depletion ²	Allowable depletion ¹	Basis depletion ²
Metals:								
Iron.....	5.6	1.7	32.6	9.9	8.5	2.4	29.5	8.3
Copper.....	9.6	4.9	25.5	13.1	10.4	2.7	20.1	5.3
Lead and zinc.....	15.2	3.5	50.0	11.7	14.6	3.0	41.3	8.6
Gold and silver.....	12.8	.5	37.8	1.5	13.6	.3	37.4	.9
Other metals.....	8.6	(³)	44.3	.3	6.6	(³)	40.3	.1
Metals not allocable.....	9.4	.9	35.6	3.7	10.0	.7	31.0	2.2
Total metals.....	8.5	2.7	32.2	10.3	10.3	2.3	26.0	5.8
Coal:								
Anthracite.....	3.8	2.3	28.0	17.9	3.5	2.2	40.8	25.6
Bituminous, lignite, peat.....	3.7	1.1	35.5	11.0	4.1	1.0	28.7	6.9
Total coal.....	3.7	1.5	83.1	13.6	3.9	1.3	30.8	10.1

Principal mineral products	1946				1947			
	Percent of gross income		Percent of net income		Percent of gross income		Percent of net income	
	Allowable depletion ¹	Basis depletion ²	Allowable depletion ¹	Basis depletion ²	Allowable depletion ¹	Basis depletion ²	Allowable depletion ¹	Basis depletion ²
Oil and gas.....	24.3	2.2	49.3	4.6	25.1	1.5	43.8	2.7
Sulfur.....	18.6	(³)	35.7	(³)	18.5	(³)	33.9	(³)
Nonmetals:								
Entitled to percentage depletion ⁴	6.5	2.2	29.7	10.1	12.6	2.6	43.0	8.9
Not entitled to percentage depletion.....	.3	.2	1.5	1.2	.3	.2	.6	.4
Total nonmetals.....	4.2	1.4	18.4	6.5	5.2	1.2	12.2	2.8
Grand total.....	16.0	2.1	44.4	6.0	17.5	1.0	38.6	3.6

¹ Allowable depletion is the deduction permitted for income-tax purposes, and is the larger of either adjusted-basis depletion or percentage depletion.
² Basis depletion is the deduction necessary to recover the unamortized portion of the taxpayer's depletable property over its estimated remaining useful life. The unamortized portion, or adjusted basis, is reduced each year by the amount of allowable depletion.
³ Less than 0.1 of 1 percent.
⁴ The following nonmetallics are entitled to percentage depletion: fluorspar, ball and sagger clay, rock, asphalt, potash, flake graphite, vermiculite, beryl, feldspar, mica, talc, lepidolite, spodumene, barite, bauxite, china, clay, phosphate rock, bentonite, trona, gilsonite and thenardite.
Source: Bureau of Internal Revenue, Statistical Division, special tabulation.

TABLE 7.—Mineral depletion and related allowances for selected corporations, by size of total assets, 1946 and 1947
[Money figures in millions]

Total assets classes ¹ (in thousands)	Number of corporations ¹	Income subject to depletion		Depletion		Other capital recovery deductions	
		Gross ²	Net ³	Allowable ⁴	Basis ⁵	Development costs ⁶	Exploration costs and losses on abandonment ⁷
1946							
\$100 under \$1,000.....	320	\$22.7	\$5.3	\$2.0	\$0.1	\$0.1	\$0.1
\$1,000 under \$5,000.....	105	207.3	47.3	18.9	3.8	9.2	2.0
\$5,000 under \$10,000.....	46	135.4	47.7	18.9	3.4	5.3	2.3
\$10,000 under \$50,000.....	96	670.0	190.7	81.8	13.4	49.4	19.3
\$50,000 under \$100,000.....	17	283.1	88.6	35.9	8.7	15.7	8.9
\$100,000 and over.....	64	2,129.3	861.3	395.7	45.4	313.2	171.2
Total.....	348	3,447.8	1,241.0	553.2	74.8	392.9	203.7

Total assets classes ¹ (in thousands)	Number of corporations ¹	Income subject to depletion		Depletion		Other capital recovery deductions	
		Gross ²	Net ³	Allowable ⁴	Basis ⁵	Development costs ⁶	Exploration costs and losses on abandonment ⁷
1947							
\$100 under \$1,000.....	320	\$25.8	\$6.7	\$2.3	\$0.1	\$0.1	(⁸)
\$1,000 under \$5,000.....	101	268.3	72.5	26.8	3.4	11.0	\$1.8
\$5,000 under \$10,000.....	42	160.1	60.0	23.5	3.1	7.4	3.6
\$10,000 under \$50,000.....	97	870.2	301.7	118.4	14.4	59.0	25.8
\$50,000 under \$100,000.....	14	353.3	117.2	51.4	10.7	16.5	13.2
\$100,000 and over.....	68	3,108.7	1,604.8	614.3	47.1	390.8	209.6
Total.....	342	4,768.6	2,162.9	836.8	78.8	484.8	254.1

¹ Total asset classes are based on the net amount of total assets after reserves for depreciation, depletion, amortization and bad debts, as of the close of the taxable year 1946. Only corporations with balance sheets are included. Consequently, the number of corporations differs slightly from that in the tabulations by industry groups and by principal mineral products.
² Gross income subject to depletion represents the amount for which the taxpayer sells, or could sell, in the immediate vicinity of the mine or well, the crude mineral output thereof.
³ Net income subject to depletion represents the gross income subject to depletion less the allowable tax deductions attributable to the particular mineral property.
⁴ Allowable depletion is the deduction permitted for income tax purposes, and is the larger of either adjusted-basis depletion or percentage depletion.
⁵ Basis depletion is the deduction necessary to recover the unamortized portion of the taxpayers depletable property over its estimated remaining useful life. The unamortized portion, or adjusted basis, is reduced each year by the amount of allowable depletion.
⁶ Development costs are expenditures for the preparation of mineral properties for production, which are deducted as expenses in the year incurred. Consequently, these expenditures are not included in the tax basis of the property, and future cost or adjusted-basis depletion is correspondingly reduced. The treatment of development costs as a current expense, however, does not diminish percentage depletion in subsequent years, since the latter is determined on the basis of income in those years.
⁷ Tax deductions for exploration costs represent expenditures which are made in the search for mineral deposits but which cannot be attributed to the capital costs of particular depletable properties. Abandonment losses represent tax deductions for recovery of capital invested in particular mineral properties which are abandoned before recovery of adjusted basis. Both exploration costs and abandonment losses represent tax deductions for capital recovery in addition to depletion deductions.
⁸ Less than \$50,000.
Source: Bureau of Internal Revenue, Statistical Division, special tabulation.

TABLE 8.—Allowable and basis depletion related to income, selected corporations, by size of total assets, 1946 and 1947

Total assets classes ¹ (in thousands)	Percent of gross income		Percent of net income		Total assets classes ¹ (in thousands)	Percent of gross income		Percent of net income	
	Allowable depletion ²	Basis depletion ³	Allowable depletion ²	Basis depletion ³		Allowable depletion ²	Basis depletion ³	Allowable depletion ²	Basis depletion ³
1946					1947				
\$100 under \$1,000.....	8.9	0.4	38.2	1.7	\$100 under \$1,000.....	9.0	0.3	34.5	1.0
\$1,000 under \$5,000.....	9.1	1.8	39.4	8.4	\$1,000 under \$5,000.....	9.9	1.2	36.8	4.6
\$5,000 under \$10,000.....	13.9	2.5	39.7	7.1	\$5,000 under \$10,000.....	14.6	1.9	39.1	5.1
\$10,000 under \$50,000.....	12.2	2.0	42.5	6.9	\$10,000 under \$50,000.....	13.6	1.6	39.2	4.7
\$50,000 under \$100,000.....	12.6	3.0	40.4	9.7	\$50,000 under \$100,000.....	15.3	3.1	43.8	9.1
\$100,000 and over.....	18.5	2.1	45.8	5.2	\$100,000 and over.....	19.7	1.5	38.2	2.9
Total.....	16.0	2.1	44.4	6.0	Total.....	17.5	1.6	38.6	3.6

¹ Total asset classes are based on the net amount of total assets after reserves for depreciation, depletion, amortization and bad debts, as of the close of the taxable year 1946. Only corporations with balance sheets are included. Consequently, the number of corporations differs slightly from that in the tabulations by industry groups and by principal mineral products.

² Allowable depletion is the deduction permitted for income tax purposes, and is the larger of either adjusted-basis depletion or percentage depletion.

³ Basis depletion is the deduction necessary to recover the unamortized portion of the taxpayers depletable property over its estimated remaining useful life. The unamortized portion, or adjusted basis, is reduced each year by the amount of allowable depletion.

Source: Bureau of Internal Revenue, Statistical Division, special tabulation.

TABLE 9.—Income, deductions, and tax liabilities of 10 selected individual oil and gas operators, for the 5-year period, 1943-47

(Money figures in millions)

Individual operator	New income			Special deduction		Taxable net income	Income tax liability		Individual operator	New income			Special deduction		Taxable net income	Income tax liability	
	From oil and gas ¹	From other sources	Total	Percentage depletion ²	Development costs ³		Amount	Percent of total net income		From oil and gas ¹	From other sources	Total	Percentage depletion ²	Development costs ³		Amount	Percent of total net income
A.....	\$10.5	\$3.8	\$14.3	2.2	\$13.0	4-\$0.9	\$0.08	0.6	G.....	\$7.7	-\$1.3	\$6.4	3.5	\$2.1	\$0.8	\$0.5	7.8
B.....	5.0	.8	5.8	3.1	2.1	.6	.5	8.6	H.....	2.1	3.6	5.7	1.0	.6	4.1	2.2	38.6
C.....	3.9	.5	4.4	3.2	4.4	4-\$3.2	.15	3.4	I.....	1.7	.1	1.8	.5	1.0	.3	.2	11.1
D.....	9.3	.3	9.6	2.6	0	6.9	6.1	63.5	J.....	8.0	-.7	7.3	2.9	1.7	2.7	2.2	30.1
E.....	2.7	.8	3.5	1.0	.3	2.2	1.4	40.0	Total.....	52.6	9.3	61.9	20.9	26.7	14.3	13.93	22.5
F.....	1.7	1.4	3.1	.8	1.5	.8	.6	19.4									

¹ Income after deductions for operating expenses, depreciation, adjusted-basis depletion, exploration costs and losses on abandonment.

² Excess of percentage depletion over adjusted-basis depletion.

³ Development costs are expenditures for the preparation of mineral properties for production, which are deducted as expenses in the year incurred. Consequently, these expenditures are not included in the tax basis of the property and future cost of adjusted-basis depletion is correspondingly reduced. The treatment of development costs as a current expense, however, does not diminish percentage depletion in

subsequent years, since the latter is determined on the basis of income in those years.

⁴ While special deductions more than offset the total net income for the 5 years, some income tax was paid because there were deficits only in some years. A deficit caused by excess percentage depletion cannot be carried over against net taxable income of other years.

⁵ Includes only 4 years, 1943-46.

Source: Bureau of Internal Revenue, special tabulation.

Mr. DOUGLAS. Mr. President, one might ask, "Do you not have more recent reports from the Secretary of the Treasury than that?"

The point is that no Secretary of the Treasury since then has had the courage to face the issue. I hope the Secretary will take it up next year.

Mr. President, in 1955, the Joint Economic Committee asked a number of tax experts to participate in its study of Federal tax policy for economic growth and stability. One of the finest papers which was presented to the committee was that by William F. Hellmuth, Jr., of Oberlin College, who wrote on the subject of the "Erosion of the Federal Corporation Income Tax Base." This paper appears on pages 888 to 917. I ask unanimous consent that a section of that paper, which appears on pages 897 to 903 and which deals with the percentage depletion question, be printed at this point in the RECORD.

There being no objection, the section of the paper was ordered to be printed in the RECORD, as follows:

DEPLETION

Present depletion deductions are probably the most glaring and most widely con-

demned source of erosion in the corporate income-tax base. These deductions may also be the ones which have been most liberalized and extended over the past 15 years.

Corporations have been permitted a tax deduction for the exhaustion of oil and mineral resources since 1913. In economics and in our tax law, the principle is well established that the gradual exhaustion in use of a well or mineral deposit represents a cost of production for which deductions should be allowed in computing net income. Controversy exists as to timing and total amount of depletion deductions allowable.

On the basis of tax neutrality between different industries and economic activities, deductions from income over the life of a property would be limited to original cost, with annual tax-free recovery reflecting the portion of the total deposit which is extracted during the year. Using the business-income yardstick, there would be depletion deductions based on actual cost or in some cases no deductions at all for depletion.¹ Full recovery of actual cost under cost depletion would correspond to tax treatment

¹ Smith and Butters, op. cit., pp. 80-84. Some businesses make no deduction for depletion due to the difficulty of estimating the future life of a deposit accurately.

of depreciation or amortization for other capital assets.

Existing legislation allows taxpayers owning an economic interest in mineral deposits the choice of a depletion deduction based on cost or percentage depletion. Percentage depletion gives an annual deduction equal to the smaller of a statutory percentage of gross income from mineral property or 50 percent of net income from the property before any allowance for depletion. Total tax-free deductions under percentage depletion are not limited or even necessarily related to capital cost. Annual percentage depletion deductions are related to production, prices, net income, and statutory percentages. There is no ceiling on the total amount of these deductions and over the life of a property they may total many times a taxpayer's actual investment costs. Thus percentage depletion deductions diverge from allowable deductions which conform either to tax neutrality or to business-income concepts and are an important element of erosion.

The dollar estimate of the excess of percentage over cost depletion is based on Treasury studies of those corporations which accounted for 75 to 80 percent of all depletion allowances claimed by corporations during 1946-49.

Year	Number of corporations	Allowable depletion	Adjusted basis depletion	Excess of allowable over basis		
				Amount	Percent of allowable	Percent of net income
1946	352	\$555	\$75	\$480	86.5	38.4
1947	344	839	79	760	90.6	35.0
1948	260	1,291	77	1,214	94.0	36.3
1949	260	1,120	61	1,059	94.6	40.1
Total		3,805	292	3,513		
Weighted average					92.3	

NOTE.—See also an interpretation of the 1946–47 data by D. H. Eldridge, *Tax Incentives for Mineral Enterprise*, Journal of Political Economy, June 1950, pp. 222–240.

Sources: 1946 and 1957 data from Revenues Revision of 1950, hearings before the Committee on Ways and Means, House, 81st Cong., 2d sess., vol. I, pp. 194, 197; 1948 and 1949 data from E. E. Oakes, *Incentives for Mineral Industries*, the President's Materials Policy Commission, Resources for Freedom, vol. 5, pp. 14–15. Admittedly adjusted-basis depletion is not identical to cost depletion but is based on cost less allowable depletion (larger of percentage or cost depletion) in prior years.

This table indicates that total allowable depletion deduction were at least 10 times depletion deductions based on cost. As legislation in 1951 and 1954 further liberalized percentages depletion and extended the opportunity to expense (currently or deferred) exploration and development costs so they never are charged to a depletion basis, allowable depletion may now be nearer 20 times cost depletion. These figures conceal a wide variation between individual products. Percentage depletion deduction as a multiple of cost depletion during 1946–49 varied from a high of over 200 for sulfur to 19 for oil and gas down to about 3½ for copper and coal. Note that oil and gas accounted for more than 80 percent of all depletion deductions:

Allowable depletion compared with adjusted basis depletion for certain products, 1946–49 combined

(In millions)				
	Allowable depletion	Adjusted-basis depletion	Allowable as multiple of adjusted basis	Product-percent of total allowable
All products	\$3,805	\$292	3.7	100.0
Oil and gas	3,143	167	18.9	82.8
Sulfur	60	(1)	(1)	1.6
Coal	136	38	3.5	3.6
Copper	182	49	3.7	4.8

¹ Allowable depletion for sulfur was less than \$300,000 for all 4 years combined. Individual years' totals were too small to be reported in tables. Thus allowable depletion for sulfur was at least 200 times the amount of adjusted-basis depletion and possibly much more.

Source: Computed from Treasury depletion studies of several hundred large companies for 1946–49, op. cit.

The most recent Statistics of Income indicate corporate depletion deductions of \$2,126 million for 1952. Corporate depletion in 1955 might amount to \$2,500 million, assuming increased dollar volume and another \$100 million for the liberalization of depletion by the 1954 code. Ninety percent of this total gives \$2,250 million as the conservatively estimated amount of corporate income excluded from taxable income due to over-generous percentage depletion.²

Erosion of the tax base due to depletion has been rapid in recent years and perhaps has now come to a position of equilibrium, at a position of great liberality, with percentage depletion now available to every metallic and nonmetallic mineral from anorthosite to zinc, including even oystershells

² Since corporations account roughly for 80 percent of all depletion, an additional \$500 to \$600 million of depletion erosion would be estimated for the 1955 individual income-tax base. Revenue Revision of 1950, hearings before the Committee on Ways and Means, House, 81st Cong., 2d sess., vol. I, p. 180.

and peat. Under section 613(b) of the 1954 Code, only soil, sod, dirt, turf, water, and mosses, or minerals from sea water, the air, or similar inexhaustible sources are not eligible for percentage depletion.

But this hope—that there will be no further erosion from depletion—is probably too optimistic. Industries entitled to a low rate of percentage depletion are continually pressing for higher rates; pass-through of depletion deduction opportunities to corporate stockholders in extractive industries has been requested. A Federal circuit court recently held that the value of finished brick could be used in the income measure for percentage depletion.³ If this view prevails for brick, other industries will push for equal treatment, possibly even to the value of gasoline for a vertically integrated oil company.

The statutory history of depletion is a superb example of at least three types of tax changes which erode the corporate tax base.

The initial break from cost depletion came in 1918 when Congress allowed, to the discoverer only, tax-free deductions based on value of property at the time of the discovery or within 30 days thereafter. This was probably the first instance under the Federal income tax where increment of value after 1913 was not taxed. Usually, of course, discovery of oil or minerals increases the value of a property substantially over cost. This higher value was justified as an incentive to exploration and discovery to meet the World War I emergency. A comparable situation arose during World War II when percentage depletion, restricted until then to oil and gas (1926), and sulfur, metal mines, and coal (1932), was extended in 1942 to 3 nonmetals and in 1943 to 10 additional nonmetallic minerals. This expansion of percentage depletion was limited to the period of the war emergency to encourage production of minerals believed to be scarce for meeting the wartime demands. After both wars, these incentive features first introduced to meet temporary emergencies were not rescinded nor allowed to expire, but instead remained permanently in the tax structure. The first generalization is that temporary tax incentive are difficult or impossible to terminate.

A second observation from experience with depletion is that simplification of tax administration is often advanced at the expense of revenue or equity or both. To overcome administrative difficulties from the use of discovery value,⁴ percentage depletion was allowed in 1926 for oil and gas wells. A figure of 27½ percent of gross income was chosen, apparently to give approximately

³ *Cherokee Brick & Tile Co.* (122 Fed. Supp. 59 (5 CCA, 1954)).

⁴ Such questions as what was a new discovery, determination of value just after the discovery, and whether the owner was the discoverer plagued tax administrators.

equal dollar deductions under the new method as had been available under the discovery value method. But this percentage method became more valuable as tax rates rose far above the 1926 corporate rate of 13.5 percent and as price levels increased, causing a high revenue cost to the Treasury and arousing the envy of other industries still restricted to cost or discovery value depletion. And the percentage depletion method, as noted above, unlike the cost and discovery value methods, has no overall limit so that deductions continue as long as a property is producing income.

A third lesson is that it is difficult to limit tax favors to just those who discover a new oil or mineral deposit or even to a few selected entire industries, however justified this special incentive is on grounds of relative risks or probable scarcity relative to needs for economic growth and national security. The other extractive industries regarded the availability of percentage depletion at liberal rates to a few industries as unfair discrimination and a tax deduction to which they were equally entitled. Politically the have-nots broke the dikes against percentage depletion in 1947, 1951, and again in 1954. Coverage was extended, percentage rates were raised, processes covered were broadened, and even mine residues were made eligible for percentage depletion. Apparent discrimination against certain industries was ended by extending the liberal deductions to all.⁵ Companies exploiting sand and gravel pits and oystershells now qualify for percentage depletion along with oil companies and uranium prospectors, though at different rates.

The incentive value of percentage depletion for certain scarce minerals has been blunted by extending the favors to all. One problem is that there are no yardsticks to indicate the incentives needed to get the socially desired amount of investment in different fields. Congress has no guide to determine which industries are entitled to percentage depletion and what depletion rates produce the needed amount and distribution of investment in the extractive industries.⁶

The economic defense of generous percentage depletion results from national policy to provide an incentive or subsidy for certain selected minerals for reasons of national security. But on grounds of tax neutrality, tax equity, and conformity to business income accounting practice, the excess of percentage over cost depletion reflects erosion in the income-tax base. In fact from the standpoint of accounting or economics, it is questionable whether these deductions are properly called depletion since they do not relate to any capital sum which is being exhausted. In some cases the income against which the statutory percentages apply includes not only extraction but also processes which are essentially manufacturing in character, such as finished brick or industrial talc.

⁵ No reduction in depletion rates has ever been voted by Congress. In 1954 every amendment extending percentage depletion was passed in the Senate. It was impossible even to get the necessary 10 Senators to request a record rollcall on any of these votes. See CONGRESSIONAL RECORD, June 30, 1954, especially pp. 9301–9319.

⁶ The President's Materials Policy Commission, op. cit., vol. I, pp. 33–35. The Commission recommended that percentage depletion be retained because of its strong inducement to risk capital to enter the minerals field. It also recommended that no depletion rates be raised above the 1952 level and that recent additions to minerals eligible for percentage depletion be reexamined to see if incentives are needed for their production.

The excess of percentage over cost-depletion deductions reduces corporate taxable net income by about \$2¼ billion in 1955 and this figure, under existing legislation, will tend to increase with an expanding economy.

EXPLORATION AND DEVELOPMENT COSTS

Exploration and development costs are closely allied with the problem of depletion for mineral and oil producers. Current tax legislation allows these producers the option of capitalizing or expensing development and, with qualifications, exploration costs.

Oil and gas producers have enjoyed this option since 1917, first by Treasury regulation, now codified by the 1954 Internal Revenue Code. Intangible drilling and development costs include all costs of labor, fuel, repairs, materials, and construction, except cost of assets which have a salvage value, the latter assets being depreciated. The development costs eligible for expensing account on the average for about 75 percent of the costs incurred in bringing in a well.⁷

The Revenue Act of 1951 extended this option even more fully to mining. A taxpayer with mining interests may now decide each year for each mine to expense or capitalize development costs. Mine exploration and development costs can be deducted currently or set up as deferred expense to run over the life of ore benefited. In either case a deduction in lieu of cost depletion is given, but percentage-depletion deductions continue undiminished. Before 1951 all development costs in excess of current net income from a property during the development stage had to be capitalized.

This option to expense what are essentially capital costs is another loss to the tax base. Tax neutrality and conformity to business accounting would require that these costs be capitalized and amortized over the life of the assets or, if the assets cannot be moved, over the life of the mineral deposit, if it will be exhausted before the assets are fully depreciated.

The erosion here is twofold. First, the option to expense development costs allows deductions to be taken sooner than if these costs were capitalized and deducted gradually over a period of years. This means that total deductions to any given date are larger than if these costs were spread over several years. Secondly, expensing of development costs combined with percentage depletion allows double deductions for the same costs. To the extent that development costs are expensed, there is no need for depletion to recover investment. If 75 percent of the cost of an oil well is expensed, only the remaining 25 percent remains to be recovered tax free through cost depletion. But with percentage depletion, the annual and total deductions bear no direct relation to capital costs but depend on gross and net income. The dollar amount of deductions under percentage depletion is not influenced by the election to capitalize or expense.

Thus, with the expensing of development costs, percentage depletion becomes more than ever an additional deduction which must be justified on grounds other than recovery of costs for these are recovered through expensing. Leasehold costs cannot be expensed but they are usually in the form of royalty payments. Development costs may be offset against income from all sources, a feature which has attracted corporations (and individuals) primarily interested in other industries to finance new oil wells, thus reducing or even eliminating their taxable income while building up their capital assets.⁸

The Treasury study for 1946-47 cited above reported that 96.8 percent of all corporate development costs were claimed by oil and gas producers and that these deductions were about two-thirds of the excess of percentage over cost depletion. Applied to 1955, this suggests about \$1.5 billion of costs which are expense in addition to being recovered through percentage depletion. Without percentage depletion, to avoid any erosion these costs would still not be expense but would be capitalized and deducted gradually over the life of the assets or the life of the well, whichever is shorter; from this point of view erosion would be at least \$1.1

billion a year at first, declining gradually as annual depreciation charges accumulate for all such property in use.

The great value of these tax-saving features to the oil industry is documented by published 1954 annual reports. The following table compares the tax position of 3 companies which specialize in crude oil production, 24 large oil companies combined (whose annual reports were available), and all corporations. Note that the effective tax-rate increases from 9.2 percent for Tidewater, to 22.6 percent for 24-company aggregate, to 48.1 percent for all corporations.

Federal taxes and effective tax rates for oil companies and all corporations, 1954

	Net income before tax	Federal income tax	Effective tax rate	Per share	
				Earnings before tax	Federal income tax
	Millions	Millions	Percent		
Tidewater Associated Oil Co.....	\$38.0	\$3.5	9.2	\$3.45	\$0.32
Humble Oil & Refining Co.....	174.8	28.5	16.3	4.86	.79
Skelly Oil Co.....	36.1	6.7	18.5	6.28	1.16
24 large petroleum companies.....	2,541.0	575.0	22.6		
All corporations.....	34,042.0	16,369.0	48.1		

Source: Annual reports; Department of Commerce estimate of corporate profits and Federal tax liability.

Since the Revenue Act of 1951, mining companies may expense a limited amount of exploration costs, even if for a productive property. The limit on such costs of a mining taxpayer was raised to \$100,000 a year and \$400,000 total by the 1954 code. The cost here is relatively small, although taxpayers are increasing their tax saving by incorporating each mine separately. Exploratory expenses above these limits by mining corporations must be capitalized. Only exploratory expenses which lead to dry holes may be expensed currently by the oil and gas industry. This conforms to neutrality and accounting concepts.

Mr. DOUGLAS. Mr. President, among the other points Mr. Hellmuth makes is that in 1954, one major oil company paid taxes at an effective rate of 9.2 percent, another at 16.3 percent, and still another at 18.5 percent. He shows further that 24 large petroleum companies paid taxes at an effective rate of only 22.6 percent.

TAX RATES OF SPECIFIC COMPANIES

Mr. President, I, myself, have been collecting some facts and figures on the taxes paid by oil and gas producing companies. I have collected figures for these 27 companies since 1945; and I have figures which show the amount of income tax they have paid compared with the net income before taxes. We all know that since World War II the taxes of most corporations have been in the neighborhood of 47 percent to 52 percent. However, oil and gas companies have paid taxes at a considerably lower rate than one would believe they should pay, and what other corporations actually do pay.

I am calling these companies company A, company B, company C, and so forth. They have done nothing illegal, and I do not wish to condemn them. I merely wish to condemn the principle of percentage depletion. In the Biblical phrase, I am not condemning the sinner, but the sin. Perhaps, technically speaking, what they have done is not a sin at all. They are merely taking what the law and Congress permit them to take. Thus I have no reason to go after any individual company. I know them. I know who they are. I have collected

these figures. If anyone doubts the authenticity of my figures, I can supply him with the code which identifies the companies. I would not like to do so unless challenged by a fellow Senator. However, these figures are public information, and they can be obtained from Moody's Manual and other manuals on corporate earnings. I wish to illustrate the effects of the great many legal tax avoidance provisions of the code with respect to the taxes which these companies actually pay.

Let us consider the company identified as company W. From 1953 to 1958, a 6-year period, that company made \$65 million in profits, and paid on net no taxes whatever. In that same period, it received a net refund of \$425,000. I repeat that figure. In the 6-year period from 1952 to 1958 it made \$65 million in profits and paid on net no taxes whatever, and actually got \$425,000 in net refunds from the Federal Treasury. If I am challenged on the name of that company, I can give it. It is well known to Members of the Senate.

There are 26 other cases. Let me cite some of the others. Take company Y, for example. In 1958 it had profits of \$6,231,000 and paid no taxes.

Company I. In 1957 it made more than \$9 million in profits, and paid no taxes. In fact it received over \$5,000 in tax credits. How nice. Let us take the figure for 1958. It made \$7 million in profits, and not only paid no taxes but received \$23,352 in tax credits. That is a zero rate of tax.

Take company N. This is a good one. In 1958 it made \$5,378,973, and paid no taxes.

Company O. In 1957, it made a profit of \$1,573,165. No taxes were paid by the company. In 1956, it made \$1,034,094 in profits. No taxes were paid. In other years it received very generous allowances when it paid only 2.49 percent in taxes in one year; in another year, 2.6 percent; in another year 2.96 percent, and in still another year 1.11 percent. That was when other corporations were paying 52 percent, and the average per-

⁷ Oakes, op. cit., p. 17.

⁸ J. K. Butters, L. E. Thompson, L. L. Bollinger, *Effects of Taxation: Investments by individuals*, pp. 201-202 (1953). Some investors regard investments in the oil industry as a source of tax exempt income, competitive with State and municipal securities.

son 20 percent on the first \$2,000 of net taxable income.

One of the better companies is company G. In 1957, it made a profit of \$1,167,000, and paid \$115,000 in taxes. That is 9 percent. Ordinary companies pay 52 percent. In 1956 it had profits of \$560,000, and paid no taxes. It paid no taxes in 1955, though it had \$832,000 in profits. It paid no taxes in 1954, although it had \$785,000 in profits. It paid no taxes in 1953, although it had \$730,000 in profits.

I could cite company after company. I can only say that this situation is a scandal and a disgrace. It is also a scandal and a disgrace that these groups are so powerful in Congress that they cannot be touched.

Mr. President, I ask unanimous consent to have tabulations in that connection printed at this point in the RECORD.

There being no objection, the tabulations were ordered to be printed in the RECORD, as follows:

Company A				
Year	Net income before income taxes	Income taxes	Net income after income taxes	Percent of income taxes to income before taxes
1958	\$22,485,135	(1)	\$22,485,135	-----
1957	35,208,979	\$5,260,000	29,948,979	14.94
1956	29,523,395	3,024,000	26,499,395	10.24
1955	28,143,673	2,780,000	25,363,673	9.88
1954	21,029,684	1,252,000	19,777,684	5.95
1953	18,812,590	367,000	18,445,590	1.95
1952	16,550,361	654,000	15,896,361	3.95
1951	17,369,652	1,073,000	16,296,652	6.17
1950	18,467,607	3,068,000	15,399,607	16.61
1949	14,759,193	375,000	14,384,193	2.54
1948	27,367,252	4,725,000	22,642,252	17.27
1947	17,749,626	2,830,000	14,919,626	15.94
1946	10,130,975	1,275,000	8,855,975	12.59
1945	5,611,770	215,000	5,396,770	3.83

¹ Not available.

Company B				
Year	Net income before income taxes	Income taxes	Net income after income taxes	Percent of income taxes to income before taxes
1958	\$4,371,094	\$525,000	\$3,846,094	12.01
1957	5,392,505	150,000	5,242,505	2.78
1956	6,975,382	1,095,000	5,880,382	15.70
1955	5,975,382	485,000	5,490,382	8.03
1954	3,291,793	38,172	3,253,621	1.16
1953	5,594,074	1,552,500	4,041,574	27.75
1952	4,436,030	669,500	3,766,530	15.09
1951	5,561,770	714,880	4,846,890	12.85
1950	5,709,537	1,023,900	4,685,637	17.93
1949	3,259,928	163,040	3,096,888	5.00
1948	6,295,858	898,900	5,396,958	14.28
1947	4,011,073	1,023,126	2,987,947	25.51
1946	2,089,932	417,000	1,672,932	19.95
1945	2,321,605	205,908	2,115,697	8.87

Company C				
Year	Net income before income taxes	Income taxes	Net income after income taxes	Percent of income taxes to income before taxes
1958	\$5,402,894	\$481,413	\$4,921,481	8.91
1957	5,561,652	640,635	4,921,017	11.52
1956	4,770,495	261,837	4,508,658	5.49
1955	4,826,687	417,388	4,409,299	8.65
1954	4,625,759	336,889	4,288,870	7.28
1953	4,391,404	179,114	4,212,290	4.05
1952	3,588,107	91,660	3,496,447	2.55
1951	3,934,107	399,397	3,534,710	10.15
1950	3,696,584	847,072	2,849,512	22.91
1949	3,373,448	679,553	2,693,895	20.14
1948	4,542,842	982,540	3,560,302	21.63
1947	2,284,109	529,781	1,754,328	23.19
1946	161,816	212	161,604	.13
1945	33,896	256	33,639	.76

Company D				
Year	Net income before income taxes	Income taxes	Net income after income taxes	Percent of income taxes to income before taxes
1958	\$156,130	¹ \$13,000	\$169,130	0
1957	271,515	5,000	266,515	1.84
1956	472,556	35,000	437,556	7.41
1955	549,098	15,000	534,098	2.73
1954	309,405	-----	309,405	-----
1953	303,453	11,332	292,121	3.73
1952	159,084	25,686	133,398	16.15
1951	415,948	8,234	407,714	1.98
1950	277,514	1,500	276,014	.54
1949	177,187	1,000	176,187	.56
1948	526,061	35,000	491,061	6.65
1947	399,643	52,000	347,643	13.01
1946	139,923	1,000	138,923	.71
1945	140,101	1,500	138,601	1.07

¹ Credit.

Company E				
Year	Net income before income taxes	Income taxes	Net income after income taxes	Percent of income taxes to income before taxes
1958	\$8,108,706	\$800,000	\$7,308,706	9.87
1957	11,303,747	1,600,000	9,703,747	14.15
1956	11,379,241	1,900,000	9,479,241	16.69
1955	8,509,136	1,500,000	7,009,136	17.63
1954	5,320,750	-----	5,320,750	-----
1953	6,420,968	1,048,000	5,372,968	16.32
1952	5,601,723	1,400,000	4,201,723	24.50
1951	5,866,052	2,000,000	3,866,052	34.09
1950	4,951,476	1,500,000	3,451,476	30.29
1949	4,928,459	1,020,000	3,908,459	20.70
1948	5,766,543	960,000	4,806,543	16.65
1947	3,650,374	600,000	3,050,374	16.44
1946	3,248,813	200,000	3,048,813	6.16

Company F				
Year	Net income before income taxes	Income taxes	Net income after income taxes	Percent of income taxes to income before taxes
1958	\$54,865,371	\$7,400,000	\$47,465,371	13.49
1957	51,273,749	4,550,000	46,723,749	8.87
1956	67,517,000	15,700,000	51,817,000	23.25
1955	56,259,000	9,900,000	46,359,000	17.60
1954	50,383,000	8,700,000	41,683,000	17.27
1953	55,775,000	14,900,000	40,875,000	26.71
1952	52,488,000	14,400,000	38,088,000	27.43
1951	58,593,000	17,300,000	41,293,000	29.53
1950	57,407,000	15,000,000	42,407,000	26.13
1949	46,487,000	10,390,000	36,097,000	22.35
1948	74,080,000	19,863,000	54,217,000	26.81
1947	40,655,000	9,298,000	31,357,000	22.87
1946	22,599,000	3,585,000	19,014,000	15.86
1945	16,371,700	1,228,000	15,143,700	7.50

Company G				
Year	Net income before income taxes	Income taxes	Net income after income taxes	Percent of income taxes to income before taxes
1958	\$804,716	\$50,000	\$754,716	6.21
1957	1,167,546	115,000	1,052,546	9.85
1956	560,753	-----	560,753	-----
1955	832,765	832,765	-----	-----
1954	785,624	-----	785,624	-----
1953	730,699	-----	730,699	-----
1952	968,287	69,022	899,265	7.13
1951	935,134	137,220	797,914	14.67
1950	892,552	147,275	745,277	16.50
1949	969,991	204,860	765,131	21.12
1948	872,719	160,367	712,352	17.23
1947	654,922	160,452	494,470	24.45
1946	471,923	135,664	336,259	28.75
1945	461,448	180,808	280,640	39.18

Company H				
Year	Net income before income taxes	Income taxes	Net income after income taxes	Percent of income taxes to income before taxes
1958	\$1,760,794	0	\$1,760,794	0
1957	2,176,226	\$160,000	2,016,226	7.35
1956	2,647,058	93,000	2,554,058	3.51
1955	1,994,072	86,000	1,908,072	4.31
1954	2,276,415	238,329	2,038,086	10.47
1953	1,899,343	156,039	1,743,304	8.22
1952	1,998,758	370,291	1,628,467	18.53
1951	1,992,234	411,166	1,581,068	20.64
1950	1,270,271	72,843	1,197,428	5.73

NOTE.—Records available only for last 9 years.

Company I				
Year	Net income before income taxes	Income taxes	Net income after income taxes	Percent of income taxes to income before taxes
1958 ¹	\$7,076,455	² \$23,352	\$7,099,807	0
1957 ¹	9,079,022	² 5,860	9,084,882	0
1956	9,078,922	² 5,860	9,084,882	(³)
1955	8,886,172	151,000	8,735,172	1.69
1954	8,106,746	429,075	7,677,671	5.29
1953	6,769,145	196,335	6,572,810	2.90
1952	5,414,053	26,156	5,387,897	.48
1951	5,067,243	410,539	4,656,704	8.10
1950	4,477,673	404	4,477,269	.01
1949	3,456,001	202,087	3,253,914	5.85
1948	2,949,585	72,628	2,876,957	2.46
1947	2,774,079	201,176	2,572,903	7.25
1946	3,172,001	504,487	2,667,514	15.90
1945	755,220	258,488	496,732	34.23
1944	102,860	65,966	368,946	64.13

¹ 12 months ended June 30.

² Credit.

³ Credit taxes.

NOTE.—In total analysis 1956 equals 1957 on this company, etc.

Company J				
Year	Net income before income taxes	Income taxes	Net income after income taxes	Percent of income taxes to income before taxes
1958	\$2,950,700	\$90,000	\$2,860,700	3.05
1957	3,154,900	20,000	3,134,900	.62
1956	3,168,549	75,000	3,093,549	2.37
1955	3,656,274	150,000	3,506,274	4.10
1954	3,570,162	360,000	3,210,162	10.08
1953	3,363,964	500,000	2,863,964	14.86
1952	2,561,162	267,461	2,293,701	10.44
1951	3,971,870	965,230	3,006,640	24.30
1950	2,302,729	519,263	1,783,466	22.55
1949	1,551,586	104,000	1,447,586	6.70
1948	1,344,021	150,000	1,194,021	11.16
1947	1,230,364	50,000	730,364	4.06
1946	409,171	-----	409,171	-----
1945	328,260	-----	328,260	-----

Company K				
Year	Net income before income taxes	Income taxes	Net income after income taxes	Percent of income taxes to income before taxes
1958	\$14,145,331	\$2,300,000	\$11,845,331	16.23
1957	17,938,378	3,400,000	14,538,378	18.95
1956	16,316,268	2,500,000	13,816,268	15.32
1955	15,599,264	1,900,000	13,699,264	12.18
1954	11,541,464	1,278,154	10,263,310	10.01
1953	11,762,519	1,590,080	10,172,439	13.62
1952	9,218,224	1,875,000	7,343,224	20.34
1951	10,327,002	2,400,000	7,927,002	23.24
1950	8,723,484	2,000,000	6,723,484	22.93
1949	8,716,231	1,800,000	6,916,231	20.65
1948	17,245,547	4,000,000	13,245,547	23.19
1947	9,301,386	2,300,000	7,001,386	24.73
1946	5,321,560	1,010,000	4,311,560	18.98
1945	4,235,097	257,000	3,978,097	6.07

Company L—Liquidated Apr. 11, 1957

Year	Net income before income taxes	Income taxes	Net income after income taxes	Percent of income taxes to income before taxes
1954.....	\$7,762,785	\$1,275,000	\$6,487,785	16.42
1953.....	8,494,844	1,785,000	6,709,844	21.01
1952.....	7,844,057	1,500,000	6,344,057	19.12
1951.....	8,553,640	1,500,000	7,053,640	17.54
1950.....	8,086,702	1,983,000	6,103,702	24.52
1949.....	7,805,345	1,900,000	5,905,345	24.34
1948.....	7,512,733	1,726,006	5,786,727	22.97
1947.....	7,667,536	1,575,000	6,092,536	20.54
1946.....	5,146,094	1,100,000	4,046,094	21.38
1945.....	3,209,359	831,500	2,377,859	25.91
1944.....	3,519,208	1,068,760	2,450,448	30.37

Company M

Year	Net income before income taxes	Income taxes	Net income after income taxes	Percent of income taxes to income before taxes
1958.....	\$152,543,223	\$16,000,000	\$136,543,223	10.49
1957.....	192,910,393	17,000,000	175,910,393	8.81
1956.....	212,961,000	34,000,000	178,961,000	15.97
1955.....	215,997,000	41,000,000	174,997,000	18.98
1954.....	174,803,000	28,500,000	146,303,000	16.30
1953.....	207,757,854	43,500,000	164,257,854	20.94
1952.....	175,792,000	30,500,000	145,292,000	14.68
1951.....	220,981,000	51,500,000	169,481,000	23.30
1950.....	161,360,000	32,000,000	129,360,000	19.83
1949.....	138,480,000	18,000,000	120,480,000	13.00
1948.....	240,069,000	54,000,000	186,069,000	22.49
1947.....	153,207,000	29,100,000	124,107,000	18.99
1946.....	79,332,000	7,500,000	71,832,000	9.45
1945.....	80,395,000	9,500,000	70,895,000	11.82

Company N

Year	Net income before income taxes	Income taxes	Net income after income taxes	Percent of income taxes to income before taxes
1958.....	\$5,378,973	0	\$5,378,973	0
1957 ¹	7,972,558	\$1,727,910	6,244,648	21.67
1956.....	5,378,994	699,000	4,679,994	13.00
1955.....	2,502,867	18,000	2,484,867	.72
1954.....	1,603,682	23,923	1,579,759	1.49
1953.....	3,077,447	4,724	3,072,723	.15
1952.....	2,334,532	99,844	2,234,688	4.28
1951.....	1,209,045	31,250	1,177,795	2.58
1950.....	282,202	49,750	232,452	17.63
1949.....	1,225,576	6,949	1,218,627	.57
1948.....	1,395,517	29,053	1,366,464	2.08
1947.....	359,903	15,000	344,903	4.17
1946.....	106,098	200	105,898	.19
1945.....	1,537,551	406,500	1,131,051	26.44

¹ 12 months ended June 30.² Deficit.

NOTE.—In totals analysis, 1956=1957 on this company, etc.

Company O

Year	Net income before income taxes	Income taxes	Net income after income taxes	Percent of income taxes to income before taxes
1958.....	(¹)	(¹)	(¹)	-----
1957.....	\$1,573,165	-----	\$1,573,165	-----
1956.....	1,034,094	(²)	1,034,094	-----
1955.....	1,006,718	(³)	1,006,718	-----
1954.....	1,690,567	\$42,130	1,648,437	2.49
1953.....	1,873,226	50,000	1,823,226	2.67
1952.....	1,502,077	40,000	1,462,077	2.66
1951.....	2,714,277	30,000	2,684,277	1.11
1950.....	2,692,947	40,000	2,652,947	1.49
1949.....	3,382,140	42,323	3,339,817	1.25
1948.....	4,236,057	348,900	3,887,157	8.24
1947.....	1,517,480	48,919	1,468,561	3.22
1946 ²	689,609	10,241	679,368	1.52
1945 ²	664,526	4,103	660,423	.62
1954 ³	2,205,837	42,130	2,163,707	1.91
1953 ³	2,600,271	50,000	2,550,271	1.92
1952 ³	2,202,835	40,000	2,162,835	1.81
1951 ³	2,623,191	30,000	2,593,191	1.14
1950 ³	3,744,852	40,000	3,704,852	1.01
1949 ³	4,158,672	42,322	4,116,350	1.00
1948 ³	4,353,435	343,900	4,009,535	8.01

¹ Not available.² Not reported.³ Figures for 1954-48 restated as result of revision of estimates of recoverable oil and gas reserves.

NOTE.—Company O felt not liable for Federal income tax in this period.

Company P

Year	Net income before income taxes	Income taxes	Net income after income taxes	Percent of income taxes to income before taxes
1958.....	\$6,135,363	\$470,000	\$5,665,363	7.66
1957.....	6,611,110	660,000	5,951,110	9.98
1956.....	6,277,997	478,000	5,799,997	7.61
1955.....	6,211,916	470,000	5,741,916	7.56
1954.....	6,209,385	470,000	5,739,385	7.57
1953.....	6,761,834	515,000	6,246,834	7.62
1952.....	7,023,582	540,000	6,483,582	7.69
1951.....	7,008,444	535,000	6,473,444	7.63
1950.....	6,616,103	415,000	6,201,103	6.27
1949.....	4,940,029	270,000	4,670,029	5.47
1948.....	5,679,055	333,000	5,346,055	5.86
1947.....	2,827,824	159,000	2,668,824	5.62
1946.....	2,532,718	151,000	2,381,718	5.96
1945.....	2,522,301	157,075	2,365,226	6.23

Company Q

Year	Net income before income taxes	Income taxes	Net income after income taxes	Percent of income taxes to income before taxes
1958.....	\$16,344,274	\$3,271,000	\$12,873,274	20.26
1957.....	19,137,735	4,500,000	14,637,735	23.51
1956.....	10,590,947	2,703,000	7,887,947	25.52
1955.....	13,034,071	1,852,000	11,182,071	14.21
1954.....	14,484,813	1,967,000	12,517,813	13.58
1953.....	12,815,586	1,143,000	11,672,586	8.92
1952.....	9,570,934	602,000	8,968,934	6.29
1951.....	8,190,680	385,000	7,805,680	4.70
1950.....	6,263,638	400,000	5,863,638	6.39
1949.....	5,183,830	210,000	4,973,830	4.05
1948.....	7,713,057	407,623	7,305,434	5.28
1947.....	3,896,936	85,000	3,811,936	2.02
1946.....	1,614,888	65,000	1,549,888	4.02
1945.....	997,075	40,000	957,075	4.01

Company R

Year	Net income before income taxes	Income taxes	Net income after income taxes	Percent of income taxes to income before taxes
1958.....	\$3,620,312	¹ \$968,000	\$4,588,312	-----
1957.....	6,908,969	882,000	6,026,969	12.77
1956.....	10,595,588	2,040,000	7,955,588	24.92
1955.....	8,052,713	1,164,559	6,888,159	14.46
1954.....	8,395,561	1,636,500	6,759,061	19.49
1953.....	11,536,428	3,477,350	8,059,078	30.14
1952.....	13,532,095	3,884,000	9,648,095	28.70
1951.....	14,940,795	4,645,000	10,295,795	30.11
1950.....	10,850,226	2,351,801	8,498,425	21.68
1949.....	6,470,610	299,023	6,171,587	4.62
1948.....	8,229,656	1,635,000	6,594,656	19.87
1947.....	7,773,864	576,444	7,197,420	12.07
1946.....	2,475,239	370,000	2,105,239	14.95
1945.....	1,983,259	252,500	1,730,759	10.27

¹ Credit.

Company S

Year ¹	Net income before income taxes	Income taxes	Net income after income taxes	Percent of income taxes to income before taxes
1958 ¹	\$3,337,324	² \$236,642	\$3,100,682	7.09
1957 ¹	4,712,841	330,000	4,382,841	7.00
1956.....	4,712,841	330,000	4,382,841	7.02
1955.....	4,060,798	260,000	3,800,798	6.40
1954.....	4,284,521	220,000	4,064,521	5.13
1953.....	5,241,179	43,000	5,198,179	.82
1952.....	5,525,948	583,000	4,942,948	10.55
1951.....	5,618,762	1,425,000	4,193,762	25.36
1950.....	5,280,578	964,000	4,316,578	18.26
1949.....	2,944,322	191,000	2,753,322	6.49
1948.....	4,736,153	342,000	4,394,153	7.22
1947.....	4,213,001	266,000	3,947,001	6.31
1946.....	3,200,034	160,000	3,040,034	4.99
1945.....	1,809,404	30,000	1,779,404	1.66

¹ 12 months ended June 30.² Includes credit of \$171,642 prior years' tax adjustment.

NOTE.—In total analysis 1956=1957 for his company, etc.

Company T

Year	Net income before income taxes	Income taxes	Net income after income taxes	Percent of income taxes to income before taxes
1958.....	\$1,011,165	¹ \$235,320	\$1,246,485	0
1957.....	701,822	0	701,822	0
1956.....	949,659	138,000	811,659	14.53
1955.....	1,385,335	185,000	1,200,335	13.35
1954.....	542,208	2,500	539,708	4.61
1953.....	408,107	-----	408,107	-----
1952.....	431,569	-----	431,569	-----
1951.....	273,473	-----	273,473	-----
1950.....	183,116	5,000	178,116	2.73
1949.....	¹ 6,000	-----	¹ 6,000	-----

¹ Credit.

Company U

Year	Net income before income taxes	Income taxes	Net income after income taxes	Percent of income taxes to income before taxes
1958.....	(¹)	(¹)	(¹)	-----
1957.....	\$11,719,324	\$560,482	\$11,158,842	4.78
1956.....	9,568,842	200,000	9,368,842	2.09
1955 ²	9,340,810	900,000	8,440,810	9.64
1954.....	7,805,307	335,000	7,470,307	4.29
1953.....	7,140,132	600,000	6,540,132	8.40
1952.....	7,715,591	1,000,000	6,715,591	12.96
1951.....	10,239,600	2,900,000	7,339,600	28.32
1950.....	7,659,000	1,200,000	6,459,000	15.67
1949.....	6,556,347	875,000	5,681,347	13.15
1948.....	9,030,713	2,250,000	6,780,713	24.91
1947.....	7,191,002	1,250,000	5,941,002	17.38
1946.....	3,400,586	400,000	3,000,586	11.76

¹ Not available.² Restated to conform with accounting practice effective Jan. 1, 1956—method of charging intangible development costs was changed. 1956 net income would have been \$1,470,000 less without such change.

Company V, liquidated

Year	Net income before income taxes	Income taxes	Net income after income taxes	Percent of income taxes to income before taxes
1954.....	\$4,173,767	-----	\$4,173,767	-----
1953.....	3,951,367	\$350,000	3,601,367	8.86
1952.....	4,414,623	660,000	3,754,623	14.95
1951.....	3,112,871	-----	3,112,871	-----
1950.....	1,904,836	526,000	1,378,836	27.61
1949.....	¹ 592,448	7,500	584,948	1.26
1948.....	461,640	2,400	459,240	.52
1947.....	416,506	4,100	412,406	.98
1946.....	328,052	11,282	316,770	3.44
1945 ²	176,841	5,250	171,591	2.97
1944 ²	298,539	6,127	292,412	2.00

¹ Before \$653,408 loss on wells abandoned.² 12 months ended Apr. 30. In 1946, the company changed to a calendar year basis, so 1946, taxes are shown both ways.

Company W

Year ¹	Net income before income taxes	Income taxes	Net income after income taxes	Percent of in- come taxes to income before taxes
1958 ¹	\$16,726,337	² \$175,000	\$16,551,337	1.05
1957 ¹	18,877,389	0	18,877,389	0
1957	18,877,389	-----	18,877,389	-----
1956	5,040,752	³ 5,040,752	-----	-----
1956 ⁴	(5)	-----	(5)	-----
1955	3,395,446	-----	3,395,446	-----
1954	10,260,388	⁵ 100,000	10,360,388	(7)
1953	11,500,382	⁶ 500,000	12,000,382	(7)
1952	12,100,165	200,000	11,900,165	1.65
1951	15,195,639	1,900,000	13,295,639	12.03
1950	7,128,542	200,000	6,928,542	2.81
1949	7,483,443	200,000	7,283,443	2.67
1948	17,917,474	3,000,000	14,917,474	16.74
1947	5,266,897	400,000	4,866,897	7.58
1946	1,844,156	-----	1,844,156	-----
1945	5,422,254	450,000	4,972,254	8.28

1 12 months ended Aug. 31.

2 Foreign income taxes.

3 Same for both consolidated and company only.

4 Consolidated.

5 Same.

6 Credit.

7 Credit taxes.

NOTE.—In total analysis, 1956=1957 on this company, etc.

Company X

Year	Net income before income taxes	Income taxes	Net income after income taxes	Percent of income taxes to income before taxes
1958....	\$4,642,978	\$670,023	\$3,972,955	14.43
1957....	7,670,654	840,709	6,829,945	10.96
1956....	6,057,708	400,000	5,657,708	6.60
1955....	6,720,029	400,000	6,320,029	5.95
1954....	5,245,527	-----	5,245,527	-----
1953....	4,470,659	240,000	4,230,659	5.37
1952....	3,635,498	450,000	3,185,498	12.38
1951....	3,702,765	550,000	3,152,765	14.85
1950....	3,770,706	696,200	3,074,506	18.46
1949....	4,022,266	640,907	3,381,359	15.93
1948....	4,731,952	901,906	3,830,046	19.06
1947....	2,940,760	597,621	2,343,139	20.32
1946....	1,394,512	163,973	1,230,539	11.75
1945....	666,557	-----	666,557	-----

Company Y

Year	Net income before income taxes	Income taxes	Net income after income taxes	Percent of income taxes to income before taxes
1958....	\$6,231,481	0	\$6,231,481	0
1957....	7,802,218	\$570,000	7,232,218	7.31
1956....	7,859,694	650,000	7,209,694	8.27
1955....	8,449,374	500,000	7,949,374	5.92
1954....	8,256,034	400,000	7,856,034	4.85
1953....	8,874,068	1,275,000	7,599,068	14.37
1952....	8,101,335	1,255,000	6,846,335	15.49
1951....	8,009,124	1,185,000	6,824,124	14.79
1950....	7,047,367	1,050,000	5,997,367	14.89
1949....	7,048,753	710,000	6,338,753	10.07
1948....	9,186,038	1,725,000	7,461,038	18.78
1947....	4,883,907	760,000	4,123,907	15.56
1946....	2,428,249	315,000	2,113,249	12.97
1945....	1,934,850	175,000	1,759,850	9.04

Company Z

Year	Net income before income taxes	Income taxes	Net income after income taxes	Percent of income taxes to income before taxes
1958....	\$2,065,816	0	\$2,065,816	0
1957....	2,215,290	0	2,215,290	0
1956 ¹	746,447	-----	746,447	-----
1956 ²	1,602,988	-----	1,602,988	-----
1955....	1,262,177	-----	1,262,177	-----
1954....	1,720,086	-----	1,720,086	-----
1953....	1,508,988	-----	1,058,988	-----
1952....	1,547,048	-----	1,547,048	-----
1951....	703,747	-----	703,747	-----
1950....	151,488	-----	151,488	-----
1949....	154,707	-----	154,707	-----
1948....	134,881	-----	134,881	-----

¹ Adjusted.

² 7 months ending Dec. 31.

³ In totals analysis, May 31 ending years used.

NOTE.—Years end May 31 prior to 1957.

Company A-Z

Year	Net income before income taxes	Income taxes	Net income after income taxes	Percent of income taxes to income before taxes
1958....	\$909,982	0	\$909,982	0
1957....	891,025	0	891,025	0
1956....	783,082	-----	783,082	-----
1955....	981,994	-----	981,994	-----
1954....	647,516	-----	647,516	-----
1953....	1,008,416	\$80,000	928,416	7.93
1952....	768,664	-----	768,664	-----
1951....	1,143,004	283,000	860,004	24.76
1950....	969,156	264,774	704,382	27.32
1949....	394,227	-----	394,227	-----
1948....	874,306	173,000	701,306	19.79
1947....	655,289	73,000	582,289	11.14
1946....	227,789	-----	227,789	-----
1945....	322,232	-----	332,232	-----

Company B-Z

Year	Net income before income taxes	Income taxes	Net income after income taxes	Percent of income taxes to income before taxes
1958....	¹ \$31,647,420	² \$4,074,902	\$33,825,276	-----
1957....	35,009,503	² 1,827,610	35,669,759	-----

¹ State and foreign income taxes included.

² Credit.

Mr. LAUSCHE. Mr. President, will the Senator yield?

Mr. DOUGLAS. I yield.

Mr. LAUSCHE. Mr. President, I concur in what the Senator has said. What extenuating argument can the companies give to these devastating figures, when it is pointed out that if it were a corporation other than an oil company, the taxes would have been much higher, whereas the taxes paid by the oil companies are practically nothing?

Mr. DOUGLAS. The Senator from Ohio has been in the Senate ever since 1957. He has heard the defense made of the depletion allowance from time to time, that it is necessary to develop exploration, that the oil industry is a great industry in the economy of Oklahoma and Texas and Kansas and other States that are dependent upon it, and so forth.

Mr. LAUSCHE. The fact is that these profits are fixed and they will continue to be fixed into the future each year that follows, except for an economic breakdown, and they still will be paying practically no taxes, while other corporations will be paying 52 percent in taxes.

Mr. DOUGLAS. The Senator is correct. It is one of the great scandals of our tax system.

Mr. PROXMIRE. Mr. President, will the Senator yield?

Mr. DOUGLAS. I yield for a question.

Mr. PROXMIRE. The Senator has

put into the RECORD a series of very impressive statistics, showing that many big firms in the oil industry pay no taxes year after year, or very small taxes, and in most instances cited by the Senator they paid far less than 10 percent in taxes.

I invite the attention of Senators to the fact that to my certain knowledge one of the biggest oil companies, within the past year has made more than \$50 million in profits. What did it pay in taxes? Nothing. It received a \$750,000 refund from the Government.

This is not something that has happened years ago. It is happening today. It will happen next year. The Government will continue to lose this money. Is not the economic basis for all this the fact that the percentage depletion permits someone who has invested in an oil property to get far more of a tax writeoff than the cost of the oil property. He can write off more than the cost of the oil property. One study made by the Truman administration, showed that on the average these companies are able to write off their investment not once, not twice, not 10 times, but 19 times. They write it off over and over and over again.

Mr. DOUGLAS. That has occurred.

Mr. PROXMIRE. What the Senator from Illinois is doing is not to provide that they can write it off once or twice, but that, as I calculated on the basis of studies that have been made before, on the average they can write it off about 10 times instead of the 19 times that is now average. So what the Senator has proposed in a very modest restraint on the profit, after taxes, of the huge oil companies.

Mr. DOUGLAS. I am continually astounded at my own moderation. I say to the oil industry that the blind and powerful opposition which they have given to even this modest improvement may stir up against them a justifiable indignation which ultimately will sweep away the whole system of depletion.

Mr. PROXMIRE. Is it not true that one of the reasons why this enormous value of oil depletion has developed has nothing to do with the intent of Congress when it passed the law, because at the time in 1926, when the depletion allowance went into the law, the corporation income tax was about 13 percent?

Mr. DOUGLAS. The value of the allowance then amounted to 7 percent.

Mr. PROXMIRE. So now with the corporation income tax at 52 percent, the value of the depletion allowance is approximately four times as great; and the amendment of the Senator from Illinois would simply reduce the depletion value

for the big companies to, roughly, 60 percent of what it is at the present time.

Mr. DOUGLAS. That is correct.

Mr. PROXMIRE. Once again, the amendment of the Senator from Illinois is modest, because it would not return the value of the depletion allowance to what it was initially, when the law was passed in 1926; it would go only halfway toward that objective.

Mr. DOUGLAS. That is correct.

Mr. PROXMIRE. The Senator from Illinois pointed out that the economic effect of the depletion allowance has been not only to give some wealthy persons and some big corporations a tremendous tax advantage, but also to provide for overinvestment—a heavy overinvestment—and a misallocation of America's economic resources.

Mr. DOUGLAS. Yes; this is something which is not commonly understood.

Mr. PROXMIRE. And it is perhaps one of the most important economic effects.

Mr. DOUGLAS. It is one of the most important economic effects.

Mr. PROXMIRE. Is it not true, however, that oil companies are able to maintain high profits or increased profits at the expense of the consumer by operating on the basis of restraining their production, so that at the present time in Texas the oilfields pump only 8 or 10 days a month? In other words, they operate far, far below capacity, and some oil firms that are successful in maintaining a tax advantage are also successful in imposing quotas on the importation of oil.

Mr. DOUGLAS. That is correct.

Mr. PROXMIRE. So the American consumer gets virtually no benefit whatsoever from the enormous tax advantage.

Mr. DOUGLAS. And the question might very well be asked: If the great Texas field is producing during only 8 or 10 days a month, is it wise to drill additional wells under those circumstances?

Mr. PROXMIRE. That is exactly what the present depletion allowance encourages.

Mr. DOUGLAS. Yes. The Senator's questions are extremely good.

Mr. PROXMIRE. Is it not true that in the bill the oil companies or oil industry gets another tax advantage which seems extremely hard to justify, in that gas pipelines receive a special treatment not given to other utilities, namely, a 7-percent investment credit, as contrasted with the 3-percent investment credit permitted all other utilities?

Mr. DOUGLAS. That is correct. The Senator from Wisconsin a few days ago made a great fight against that; but the steamroller went over him, and the 7-percent investment credit for the gas pipelines was retained. This is one of the many injustices contained in the bill.

Mr. PROXMIRE. So rather than having the effect in this tax reform—and this is supposed to be a tax reform bill—of cutting back on the excessive privileges which this most profitable industry in America now enjoys, the bill aggravates and enhances the unjustifiable and

unjustified profits advantages which the gas and oil industry already enjoys.

Mr. DOUGLAS. The bill opens more loopholes than it closes.

Mr. President, one of the really major loopholes in the tax code is the method by which capital gains may be applied to oil and gas properties. Because this subject is little understood, I have again asked that a memorandum be prepared concerning it. I ask unanimous consent that the memorandum, entitled "Application of Capital Gains Treatment to Income From Oil and Gas Properties," be printed at this point in the RECORD.

There being no objection, the memorandum was ordered to be printed in the RECORD, as follows:

APPLICATION OF CAPITAL GAINS TREATMENT TO INCOME FROM OIL AND GAS PROPERTIES

A taxpayer owning rights in an oil and gas property may sell a fractional share in these rights and claim capital gains treatment with respect to the excess of the proceeds from the sale over his adjusted basis in the fractional share sold. The character of the fractional share as a capital asset within the meaning of section 1221 of the Internal Revenue Code of 1954 is not and has not been seriously questioned. The distinguishing characteristic of such fractional shares is that the original owner permanently divests himself of all interests therein, i.e., no provision is made for a return of the rights to him after a specified period of time, or after a specified volume of production or number of dollars of royalties realized with respect to the fractional share.

On the other hand, for some considerable time past there has been considerable confusion about the tax treatment of "carved out" oil payments. These differ from assignment or sale of fractional shares in that the taxpayer does not permanently relinquish rights to income in the oil and gas property but merely assigns or sells some portion thereof for a limited period of time. For example, he may sell the next 2 years' production, or the next 100,000 barrels, or the next \$1 million worth of output. Upon satisfaction of these conditions, the rights revert to the taxpayer. Numerous court decisions, at variance with Treasury rulings, maintained that the proceeds from such sales should be treated as capital gains.

Quite recently, however, the U.S. Supreme Court in the Lake case, ruled that proceeds from sale or exchange of carved-out oil payments were to be construed as realization of future income and therefore subject to ordinary income-tax treatment. The Treasury Department apparently feels that the Supreme Court ruling is sufficiently broad and sufficiently definite as to preclude further dispute about the tax treatment of carved-out oil payments. However, the ingenuity of the American taxpayer must never be underestimated.

Mr. PROXMIRE. Mr. President, it is my understanding, on the basis of estimates by the Committee on Unessential Expenditures that the concession to the gas industry, made in the bill, under the investment credit provision, will be worth more than \$51 million to them, in addition to the other advantages which they already have.

Mr. DOUGLAS. I think that is a conservative estimate.

Mr. MORSE. Mr. President, will the Senator from Illinois yield?

Mr. DOUGLAS. I yield.

Mr. MORSE. I always find it very educational to listen to the Senator from Illinois, and to a great seminar when I

listen to a colloquy between the Senator from Illinois and the Senator from Wisconsin [Mr. PROXMIRE]. I have enjoyed the educational aspect in regard to the shocking injustice to the American people, symbolized by the bill.

Could the Senator from Illinois cite to me to any article in the Democratic platform of 1960 which would justify the bill?

Mr. DOUGLAS. No.

Mr. MORSE. Does the Senator from Illinois think the Senator from Oregon would be mistaken in his point of view if he expressed the opinion that the bill cannot be reconciled with the Democratic platform of 1960?

Mr. DOUGLAS. I do not believe it can be reconciled. It is my intention to vote against the bill in its present form.

Mr. MORSE. Is it not true that the Democratic Party in its platform in 1960 sought to hold out some hope to the people of the country to pass a tax reform bill which deserved the name?

Mr. DOUGLAS. That promise was held out to the American people.

Mr. MORSE. The other day, in announcing my opposition to the bill, I characterized the bill as one which could best be described as a bill for tax dodgers. Does the Senator from Illinois believe that that was an unfair description of the bill, from the account which the Senator is now giving to the Senate as to how the bill increases the ducking and dodging ability of the oil industry to escape more taxes than it otherwise has been able to escape?

Mr. DOUGLAS. I should prefer to say that the bill is an unbalanced bill. It gives rewards to the wealthy and the powerful and denies protection to the average American.

So far as the oil industry is concerned, except for the gas pipelines, it is true that the bill does not make things any worse than they are now; but it does not make any improvement.

Mr. MORSE. A few minutes ago the Senator from Illinois said he was surprised at his own moderation. I think the statement he has just made is one of his great understatements, because I still am of the opinion that the description of the bill as stated by the Senator from Oregon is a much more accurate one than the modest understatement of the Senator from Illinois.

Mr. DOUGLAS. I expect to join with the Senator from Oregon in voting against the bill. I appreciate the services which he has given.

Mr. President, in addition, I ask unanimous consent to have printed at this point in the RECORD a paper entitled "Writeoffs, Cost Depletion, and Percentage Depletion—An Appraisal," written by Paul Haber, doctor of jurisprudence and doctor of philosophy.

There being no objection, the paper was ordered to be printed in the RECORD, as follows:

WRITEOFFS, COST DEPLETION, AND PERCENTAGE DEPLETION—AN APPRAISAL

(By Paul Haber, J.D., Ph. D.)

INTRODUCTION

Our Federal tax system is supposed to be based on the principle of progressive taxation or "ability to pay"—the higher the net

income, the higher the rate of tax. In the case of taxpayers who engage in the business of crude oil, however, this principle is made to work in reverse—the higher the net income from the production and sale of crude oil, the lower the rate of tax.

There seems to be considerable misconception as to the true value of the tax subsidy to crude oil. It is generally assumed that it consists of "percentage depletion" only, which is supposed to be worth about \$1.5 billion a year. Those who are acquainted with the subject know that the "writeoffs" subsidy is worth at least \$7 billion more. Nobody, however, seems to be aware of the fact that "cost depletion" also represents a subsidy to crude oil. Because this last subsidy is concealed in a provision of the code which on the surface seems to have nothing to do with depletion, it seems to have escaped everybody's attention. It is the "sleeper" subsidy and it is costing the country at least \$5 billion a year.

WHO ENTERS THE CRUDE OIL BUSINESS?

Consider the tax situation of individuals in the following groups:

1. The stockholders who own large blocks of stock in the corporations listed on the various stock exchanges, who receive fabulous incomes from dividends;
2. The active heads of these listed corporations, who receive substantial salaries for their services and dividends on any stock they may own in the corporation;
3. The professional advisers for these corporations, who receive large fees for their services;
4. The movie stars and other independent professional men who earn large salaries and fees;
5. The more than 150,000 partners, stockholders, and sole proprietors, who own the thousands of medium-size businesses in this country, who derive substantial income from dividends, salaries, interest, or profits.

The more than 200,000 individuals who compromise these 5 groups derive incomes anywhere from \$100,000 to \$25 million a year, are subject to taxes in the very top brackets. Would it be reasonable to assume that if these people are smart enough to earn such large incomes, they are naive enough to pay it out in taxes? Especially, when the tax laws applicable to crude oil offer them a safe and sure way out by transforming the "progressive tax rates" into "regressive tax rates," so that instead of paying out 90 percent of their incomes in taxes and keeping 10 percent they are able to keep 90 percent and pay out 10 percent?

THE WRITEOFFS SUBSIDY

Mr. Smith, whose income is \$1 million a year, decides to avail himself of the tax subsidies to crude oil instead of paying a 90-percent tax on the income. He spends his income buying fractional interests in a large number of pools or joint ventures which engage in the search for oil. In this manner, he spreads the risk over a large number of drilling operations, one or more of which are bound to find oil.

The million dollars thus spent by Mr. Smith is costing him \$100,000, because the tax laws permit him to write off the cost of the search for oil, irrespective of whether the search results in a dry hole, a commercial producer, or a gusher. Only a small fraction of the cost of the search must be capitalized, less than 12 percent, when the well finds any oil at all. Thus, as far as the costs of the search are concerned, the odds are 9 to 1 in favor of Mr. Smith, because Mr. Smith is drilling for oil with money which would otherwise have gone to pay the income tax on the million-dollar income. These 9-to-1 odds in favor of Mr. Smith more than make up for the risk of not finding oil. In actual practice, because the risk is spread over a great many drilling operations, the overall odds in favor of Mr. Smith are 20 to 1 that he

will come out a happier man drilling for oil than he would be paying income taxes. When a taxpayer enters the crude oil business, he forgets about income taxes; there simply are not any to pay, as we shall see below.

The best evidence as to Mr. Smith's probabilities of becoming a happy and prosperous oilman can be attested by the more than 55,000 wells which are being drilled each year in this country, at an average cost of \$150,000 per well, or a total cost of \$2,250 million a year. We are drilling in this country six times as many wells as the rest of the world does, even though our oil reserves are less than one-sixth the world's reserves (our 30 billion barrels to the world's 200 billion barrels).

Drilling for oil is like playing dice with the Treasury: "Heads I win, tails you lose," with the Treasury always on the losing end. As a matter of fact, high tax rates are a boon to the crude oil industry rather than a burden, because the higher the rate of tax the lower the net cost (the after-tax cost) of the drilling operation. This explains why the American Petroleum Institute does not support the National Association of Manufacturers in its fight to reduce the top tax bracket from 90 percent to 40 percent. If the rate were reduced to 40 percent, the search for crude oil would fall off tremendously, because the taxpayer's share of the cost of the search would have been increased from 10 percent (100 percent less 90 percent tax) to 60 percent (100 percent less 40 percent tax). As a matter of fact, the phenomenal growth of the crude oil industry dates back to the year 1940, the year in which the wartime rates were first brought into the statute.

It is evident from the above that taxwise it is far more profitable when the drilling operation is done by a taxpayer (as an individual) who is in the 90 percent tax bracket than by a corporation which is subject to the 52 percent tax bracket. That is why at least 40,000 wells a year, out of the total of 55,000, are drilled by individual taxpayers and only 15,000 are drilled by the major oil companies. On this altogether plausible assumption, the value of the "writeoffs" subsidy is \$6,557 million, computed as follows:

90 percent of 40,000 wells	
multiplied by \$150,000----	\$5,400,000,000
52 percent of 15,000 wells	
multiplied by \$150,000----	1,157,000,000
Total value of tax	
subsidy-----	6,557,000,000

THE "COST DEPLETION" SUBSIDY

Having gotten rid of his original income in the search for oil, the taxpayer's next problem is to get rid of the income from the oil property after an oil discovery. Since the taxpayer has no cost basis in the oil property (having previously written off the cost of the search through "writeoffs") the taxpayer cannot compute the deduction for depletion on the basis of full discovery value of the property. His deduction for depletion is limited to "percentage depletion" (27½ percent of the gross income from the property, not to exceed 50 percent of the net income from such property). This, however, would leave him with a substantial amount of income from oil, subject to ordinary income tax rates. To relieve him of such excess income the code contains a "sleeper" provision which makes it possible for him to convert the income from the oil property into capital gain without his giving up ownership in the property.

During the hearings conducted by the Senate Committee on Economic Growth ("Federal Tax Policy for Economic Growth," 84th Cong., 1st sess., Joint Committee on the Economic Report), neither Prof. Horace M. Gray nor Prof. Arnold C. Harberger, nor Prof. James R. Nelson—who argued against the depletion subsidy—were aware of the

"sleeper" provision in the code. Messrs. Henry B. Fernald, Lowell Stanley, and Arthur A. Smith, who argued in favor of depletion, were, of course, careful to keep the "sleeper" provision well hidden under cover.

The "sleeper" provision

Section 1239 of the 1954 code, which corresponds to section 117(o) of the 1939 code, provides as follows:

"(a) In the case of a sale or exchange, directly or indirectly, of property described in subsection (b)—

"1. Between a husband and wife; or

"2. Between an individual and a corporation more than 80 percent in value of the outstanding stock of which is owned by such individual, his spouse, and his minor children and minor grandchildren; any gain recognized to the transferor from the sale or exchange of such property shall be considered as gain from the sale or exchange of property which is neither a capital asset nor property described in section 1231.

"(b) This section shall apply only in the case of a sale or exchange by a transferor of property which in the hands of the transferee is property of a character which is subject to the allowance for depreciation."

In simple English, this section states that when property which is subject to depreciation, such as real estate, patents, etc., is sold to a spouse or to a corporation controlled by the transferor (and/or the transferor's spouse, minor children, and minor grandchildren), the gain realized on the sale is ordinary income not capital gain. The same rule applies when the sale is from one corporation to another corporation, if the selling corporation owns 80 percent or more of the stock of the buying corporation. The purpose of this provision in the code is to prevent fictitious sales, for the sole purpose of establishing a higher depreciation basis in the hands of the "related" transferee by the payment of a capital-gains tax on the part of the transferor.

Section 1239, however, does not apply to property which is subject to depletion, as distinguished from property which is subject to depreciation. Consequently, a taxpayer (whether an individual or a corporation) who has no cost basis in an oil property (such costs having been previously written off from the taxpayer's income) is not limited to the deduction of 27½ percent of the gross income from the property ("percentage depletion"). The income from the property can be made fully deductible through "cost depletion" by the sample device of a "sale" of the property for its full discovery value to one's spouse or to one's "controlled" corporation. The 25-percent capital-gains tax incurred on the transaction is then reported on the installment basis, spread over the life of the oil property. In this way the income from the oil property automatically is limited to a maximum tax rate of 25 percent, payable as, when, and if the oil is produced.

The value to the crude oil industry of this loophole in the law is approximately \$5 billion a year. Since the value of all the oil minerals produced in this country each year is \$8 billion (see "Facts and Figures for 1956," p. 149, published by the American Petroleum Institute), the depletion, if it were computed on the "percentage depletion" basis would have amounted to \$2.2 billion (27½ percent of \$8 billion). Computed on a "cost depletion" basis, the depletion is automatically increased from \$2.2 billion to \$8 billion, at a tax savings of some \$5 billion.

PERCENTAGE DEPLETION

This subsidy, which has been assumed generally to be the principal villain in our tax laws, is by comparison with the last two subsidies a small handout. Its principal purpose is to scoop up the tax leftovers to which the taxpayers in the crude oil busi-

ness may unexpectedly be exposed to. Thus, if the property should be found to contain oil after the deductions have been taken under the "cost depletion" methods, "percentage depletion" steps in to absorb the excess income with which the taxpayer is inconvenienced. "Percentage depletion" may be said to act as a sort of basket for any leftover income, left after the "cost depletion" subsidy has been fully availed of.

The value of "percentage depletion" subsidy to the crude oil industry is comparatively small, less than half a billion a year, as compared with a total of some \$12 billion from the "writeoffs" and "cost depletion" subsidies. This being the case, why does the crude oil industry so bitterly resist any cut in the 27½-percent rate?

Is it because by resisting a cut in the very smallest subsidy the people's attention remains focused on "percentage depletion" as the apparent villain and is thus diverted from the real villains—"writeoffs" and "cost depletion"—which are worth at least 25 times as much? There is no other explanation.

THE GROWTH OF THE INDUSTRY

As would be expected, an industry which is the beneficiary of three tax subsidies aggregating close to \$13 billion a year would grow fast and big. The crude oil industry has grown very fast and very big. The shares of the listed oil companies are worth more than \$50 billion, or more than the combined value of all the listed shares of the steel, chemical, and automobile industries. This does not include the value of the tens of thousands of unlisted companies, the stock of which is held by the hundreds of thousands of spouses, minor children, and minor grandchildren of the top bracket taxpayers engaged in the crude oil business. And to think that less than 20 years ago the crude oil industry was a small industry by comparison with either steel, chemicals, or automobiles.

The rate of the crude oil industry's growth may be better appreciated when the stock splitups of a few of the major oil companies are taken into consideration. Humble Oil Co., the second largest subsidiary of Standard Oil of New Jersey, has split its stock 5 times since 1922; 4 shares for 1 in 1922; 3 shares for 1 in 1933 (a depression year); 2 shares for 1 in 1943; 2 shares for 1 in 1951; 2 shares for 1 in 1957. Thus, each share of the 1922 vintage stock is today 96 shares, and this does not take into account the many stock dividends voted by the company from time to time. The stock is selling for approximately 100 times its earnings after taxes. What makes this stock so valuable? When 90 percent of a corporation's true income (concealed in the writeoffs and cost depletion) is exempt from income taxes and only 10 percent is subject to tax, a stock is bound to sell for 100 times the amount of earnings. In reality, however, the value of the stock reflects the fact that 90 percent of the company's true earnings are exempt from tax.

Standard Oil Co. of California split its stock twice in recent years: 2 for 1 in 1951 and 2 for 1 in 1956. The same is true of Texas Co. Standard of New Jersey had 2 recent splitups: 2 for 1 in 1951 and 3 for 1 in 1956. The latter company now has more than 200 million shares outstanding, selling around \$50, or a total of more than \$10 billion.

It may be interesting to observe that after each stock splitup the price of the postsplit stock soon catches up with the price of the presplit stock. Apparently you cannot keep a crude oil stock down. When a stock remains unsplit, as in the case of Superior Oil Co. of California, its price zooms to fantastic heights. This stock has recently been selling at \$1,800 per share, even though its earnings are about \$10 a share. Thus, the stock is selling at 180 times its net earnings. For the 5-year period from 1952 to

1956, the company wrote off on the average \$36 million a year; its net income before depletion was \$9 million a year, on the average; the average amount of income tax paid by it was \$40,000 a year. Even a religious organization could not ask for more.

The Oil Record, published by the Petroleum Institute Projects, lists several hundred oil companies, giving their financial operations for the 5-year period from 1952 to 1956. These results, of 25 companies selected at random, are reproduced in the table below. To appreciate the significance of the figures in the table, it is suggested that they be examined carefully, reading each line across rather than down.

Name of company	Writeoffs	Net income	Income tax paid
Union Oil & Gas Co. of Louisiana	\$7,000,000	\$3,000,000	\$30,000
Superior Oil Co. of California	36,000,000	9,000,000	40,000
Texas Pacific Coal & Oil Co.	6,000,000	7,500,000	800,000
Franco Wyoming Oil Co.	1,650,000	1,500,000	160,000
Kewanee Oil Co.	7,000,000	2,000,000	75,000
Crown Central Petroleum Co.	1,700,000	1,750,000	500,000
General Crude Oil Co.	6,000,000	3,500,000	200,000
Bishop Oil Co.	600,000	350,000	18,000
Humble Oil Co.	130,000,000	160,000,000	33,000,000
Tidewater Oil Co.	35,000,000	35,000,000	4,000,000
Sunray Mid-Continent Oil Co.	44,000,000	42,000,000	16,000,000
Phillips Petroleum Co.	90,000,000	85,000,000	22,000,000
Reserve Oil & Gas Co.	850,000	700,000	100,000
Skelly Oil Co.	30,000,000	30,000,000	10,000,000
Eason Oil Co.	700,000	600,000	45,000
Kerr-McGee Oil Industries	7,500,000	3,500,000	350,000
Anderson-Pritchard Oil Co.	7,750,000	4,750,000	500,000
Argo Oil Co.	2,750,000	4,000,000	225,000
Drilling & Exploration Co.	2,900,000	750,000	22,000
Petroleum Exploration	500,000	750,000	80,000
Getty Oil Co.	5,000,000	10,000,000	1,500,000
Aztec Oil & Gas Co.	650,000	600,000	-----
Weststates Petroleum Co.	575,000	150,000	30,000

Is it any wonder that the growth in the ranks of oil millionaires keeps pace with the growth in the ranks of unemployed? Such crude distortion of the principle of progressive taxation in the case of crude oil is bound to cause periodic depressions. When the people's purchasing power is being drained by high taxes in order to make up the loss of \$13 billion in revenue which should come from the crude oil industry, there is bound to be unemployment. Some people in high office say that the current depression is temporary—the economy is catching its breath. A more correct explanation for the current condition would be: The people are taking a rest to get up more strength to pay the taxes which should be paid by our largest industry.

How can we fight the battle of peace with any degree of success, when our own house is in such disorder? Our cause is not too convincing so long as people are allowed to bore into the vitals of our national economy through excessive drilling, to add to the swollen ranks of oil millionaires and the swollen ranks of jobless.

In order to eliminate one of the principal causes of periodic depressions and to restore a modicum of social justice, the following changes in our tax laws are proposed:

1. The deduction for intangible drilling costs should be limited to situations where the well finds no oil;

2. Intangible drilling costs should be capitalized when the well does find oil;

3. The loophole in section 1239 should be plugged, to discourage fictitious sales to related taxpayers or a controlled corporation, to prevent a stepped-up depletion basis based on cost;

4. Enact legislation to prevent the tens of thousands of reciprocal sales from one taxpayer to another, for the twofold purpose of establishing capital gains and cost-depletion basis. Apply the dealer rule to sales of oil properties which now applies to sales of real estate;

5. Eliminate percentage depletion as an unwarranted handout.

The above changes in our tax laws would discourage tax drilling and encourage scientific drilling. It would bring many billions of revenue to the Treasury.

The world's known oil reserves are estimated at 250 billion, enough to last us more than 100 years. Why not start using them?

The crude oil industry now enjoys a \$3 monopoly price per barrel of oil and a \$13 billion tax subsidy. The people can make it give up one or the other through reduced consumption of gas and oil.

Mr. DOUGLAS. Mr. President, there is an interesting history about this paper. I had it printed in the CONGRESSIONAL RECORD in another connection. The big oil companies learned about it and had Dr. Haber fired from his job. He is unemployed today and has lost his income. He wrote me a pitiful letter about the circumstances under which he is suffering.

This shows the power of the oil industry, their ruthlessness toward those who stand up against them and take some risk. In a sense, I feel guilty about this matter, because I mentioned Dr. Haber's name in connection with a previous discussion of this subject. I had no idea that the oil companies would hit him below the belt, but they have deprived a scholar and an impartial man of his job simply because he spoke his mind and told the truth. I thought those might be tactics used in Nazi Germany or Communist Russia; I did not think they were the tactics of democratic America. But now Dr. Haber has lost his job, and he is in trouble. I hope very much that this fact may induce some philanthropist to hire this man, who is a good economist, a good accountant, and a good lawyer. In fact, I should devote a little energy to see if I can get him another job.

Finally, Mr. President, I ask unanimous consent that correspondence between Dean Erwin N. Griswold, of the Harvard Law School, and Mr. Rex G. Baker, who was then general counsel of the Humble Oil & Refining Co., which first appeared in the Harvard Law Review, volume 64, No. 3, January 1951, and which was reproduced by the Joint Economic Committee in the Compendium on Federal Tax Policy, for Economic Growth and Stability, be printed at this point in the RECORD.

There being no objection, the correspondence was ordered to be printed in the RECORD, as follows:

PERCENTAGE DEPLETION—A CORRESPONDENCE¹
(By Rex G. Baker, general counsel, Humble Oil & Refining Co.; Erwin N. Griswold, dean, Harvard Law School)

(EDITOR'S NOTE.—On September 18, 1950, Dean Erwin N. Griswold made a speech before the tax section of the American Bar

¹ This correspondence appeared in the Harvard Law Review, vol. 64, No. 3, January 1951, and is reproduced here with the permission of the authors and the Harvard Law Review.

Association,² in which he referred to "gross inequities of the law in favor of the oil and gas interests." A number of newspaper accounts of the speech reported this as an attack on the percentage-depletion provision of the Internal Revenue Code.³ On the basis of these reports, Mr. Rex G. Baker, general counsel of the Humble Oil & Refining Co., wrote the letter that began the correspondence reproduced herein. Neither author had any intention to publish these letters at the time they were written. No revisions have been made except to eliminate those parts irrelevant to the percentage-depletion controversy and to add footnotes where it has been thought useful to refer to source materials.)

SEPTEMBER 22, 1950.

DEAR DEAN GRISWOLD: You will recall our conversation in Washington concerning the percentage-depletion allowance for oil and gas wells.

Your remarks before the tax section regarding the depletion allowance received widespread publicity, and I am afraid they will be very damaging to the producers of oil and gas in view of your reputation and the responsible position you occupy in the education world.

Both in peace and in war the country must have and is very dependent upon oil and gas. Our civilian economy and the national safety would be jeopardized if we failed to maintain adequate reserves of petroleum and a backlog of reserve producing capacity. This means that it is essential to our country's welfare and safety that the exploration for oil and gas within the United States be continued at an accelerated rate due to increasing demands for petroleum and its products year after year.

The exploration for petroleum is an extremely costly and hazardous business. Oilmen must lease vast areas, must spend large sums in geophysical operations, must drill very expensive wildcat wells, of which 4 out of 5 on the average are dry holes, and must then make enormous expenditures of money in developing proven or semiproven acreage. Risk capital is not invested unless there is hope of reward.

The producer of oil depletes his capital asset. If he is to stay in the business he must find and develop new sources of supply. If the depletion allowance were taken off, our present tax laws would tax away a large portion of his capital.

It must be remembered that a large percentage of exploratory activity is carried on by the independent wildcatter. He often spends a lot of money and goes broke without finding anything. To say that he would be protected by charging off losses ignores the fact that until he finds oil he has no income against which to charge off his losses. This is quite typical of the wildcatter. If he finally succeeds in finding oil he creates new capital and must be rewarded for the risks he has taken. This reward can be adequate only if the depletion allowance is maintained.

The fact of the matter is that the oil in-

dustry has consistently spent in exploratory effort a good deal more than the 27½-percent depletion allowance. It has thus had to look elsewhere for funds with which to help finance its quest for oil.

The 27½-percent depletion allowance was established in 1926. Congress has made searching inquiries on several occasions since as to the necessity for the depletion allowance and the wisdom of maintaining it at 27½ percent. Each time after full investigation and inquiry it has sustained the 27½-percent allowance. This fact alone should, it seems to me, cause anyone to be sure of his ground before he launches an attack upon the depletion allowance.

Herewith I enclose some material which I believe you will find helpful in your future consideration of this matter: a booklet entitled "Let's Keep on Hunting Oil," some statistical data which will show that the 30 leading oil companies have found it necessary to secure new capital by issuing stock and borrowing, that their net worth has consistently been lower than the comparable figures of manufacturing companies, that a large percentage of the net investment of the 30 leading oil companies is in oil and gas producing facilities, data showing the ratio of dividends to net income, the cost of replacing crude petroleum, this cost having steadily risen, financial information for the 25 leading oil companies which shows moderate incomes, and a chart showing a comparison of petroleum prices with the price of coal and oil commodities. This chart shows that the public have been the beneficiaries of the depletion allowance in the form of low prices for petroleum products.

Your attention is also invited to the hearings before the Committee on Ways and Means of the House of Representatives relating to the 1950 revision of the revenue laws.⁴

Yours sincerely,

REX G. BAKER.

SEPTEMBER 25, 1950.

DEAR MR. BAKER: Thank you very much for your letter of September 22, which has reached me this morning. I particularly appreciate its fair and restrained tone. This is in considerable contrast with the attitude which is often taken on this matter by others in your area.

As a matter of fact, I said nothing at all in my speech in Washington about percentage depletion. My remarks were directed entirely to the so-called in oil payment provisions which had been added to the bill by the Senate.⁵ This seemed to me, and still seems to me, to have been a rather clear matter of special privilege. Naturally, I am pleased that it was finally eliminated by the conference committee.

As I have indicated, I did not talk about percentage depletion and had no thought of doing so. There is lots to talk about there, though. In the first place, I would want to make it plain that I have never advocated eliminating the depletion allowance. That

would be taxing capital. There would be no more sense in it than in eliminating the depreciation allowance.

Nor do I disagree with you at all as to the importance of oil in our economy, and the desirability of encouraging the industry, particularly with respect to exploration. I do think, though, that there is real reason to question whether the present 27½-percent depletion allowance is not excessive, whether it does not cost more than other ways of achieving the same results, and whether a very large proportion of the benefits do not now go in fact to persons who are not the ones who do the exploring and take the risks.

How about direct subsidies to explorers, for example? Might this not be a better way, and at the same time, a cheaper way? We use subsidies in maritime shipping and elsewhere in our economy. It might be a much more effective stimulus than the present backhanded way of doing it through the depletion allowance.

For example, may I call your attention to the sentence in your letter which reads as follows: "To say that he would be protected by charging off losses ignores the fact that until he finds oil he has no income against which to charge off his losses." I think you will agree that this is really no argument, since it is equally applicable to the percentage depletion deduction. The wildcatter gets no depletion deduction until he finds oil. In other words, the method I suggested then, as far as this point is concerned, would be just as effective, indeed, even more effective (because I would allow a 100-percent deduction until all principal costs had been recovered while percentage depletion allows only a 27½-percent deduction) than is the percentage depletion allowance.

You must know of situations where the present system of taxing oil production works out outrageously. I hear about actual cases from time to time, and they must come to your attention much more frequently. What I would like to see us do is to work out a system which would maintain adequate incentive and stimulate further production of oil without granting enormous tax advantages to drones and others who take little or no risk. I think it is a very real problem, and it would be a great contribution if people in your area, who are familiar with the situation, would devote themselves toward developing a sound and sensible solution to it.

At any rate, having the benefit of percentage depletion, it would seem to me to be the heart of wisdom for persons interested in the oil industry not to jeopardize that advantage by seeking to get additional tax favors which are less warranted. I refer, of course, to such things as the in-oil provision, and others which are suggested from time to time. There is a good deal of feeling about percentage depletion but it is very likely that nothing can or will be done about it. I would point out, though, that the community property problem was finally solved, though it seemed for many years at least as difficult. The surest way that I can think of to focus attention of other parts of the country on the percentage-depletion situation, and possibly to produce fairly strong reaction, is to push it even more in the way of tax privileges.

Very truly yours,

ERWIN N. GRISWOLD.

OCTOBER 11, 1950.

DEAR DEAN GRISWOLD: I did not have an opportunity to hear your speech in Washington. My information came from remarks made by people who did hear it and from press reports. It is reassuring to be told that you had nothing to say in your speech about percentage depletion. As for

² Sec. 86 A. B. A. J. 999, 1057 (1950).

³ Internal Revenue Code, sec. 114(b) (3), provides as follows: "In the case of oil and gas wells the allowance for depletion under sec. 28(m) shall be 27½ percent of the gross income from the property during the taxable year, excluding from such gross income an amount equal to any rents or royalties paid or incurred by the taxpayer in respect of the property. Such allowances shall not exceed 50 percent of the net income of the taxpayer (computed without allowance for depletion) from the property, except that in no case shall the depletion allowance under sec. 23(m) be less than it would be if computed without reference to this paragraph."

⁴ Hearings before Committee on Ways and Means on H.R. 8920, 81st Cong., 2d sess., 49-60, 100-101, 119, 133-134, 177-309, 733-740, 818-895, 901-926, 1267-1269, 1282-1286, 2975-2983, 2999-3001, 3017-3026, 3028-3029, 3040-3046 (1950).

⁵ The Revenue Act of 1950, as reported by the Finance Committee of the Senate, provided that the amount received from the sale of the right to obtain a stated amount of production from an oil, gas, or mineral property, while retaining a continuing interest in such property, should be treated as proceeds from the sale or exchange of a capital asset. H.R. 8920, 81st Cong., 2d sess., sec. 214 (1950) (as passed by Senate); see S. Rept. 2375, 81st Cong., 2d sess., 66, 91 (1950).

the "in oil" payment provision referred to, I quite agree with you that this proposed legislation was not justified. I do not know who sponsored it. It is my belief that no responsible person in the oil industry did so. I, too, am pleased to know that the conference committee eliminated this measure from the bill that was finally passed.

It helps clarify our thinking for you to state that you have never advocated elimination of the depletion allowance. I agree with you that to do so would amount to taxing capital. The question is at what point the depletion allowance should be placed in order to encourage the generation of risk capital so essential in finding oil. Those of us in the oil industry who have lived close to the subject believe that the 27½-percent depletion allowance is more than justified.

The rate of 27½ percent for the depletion allowance has resulted over a period of years in a depletion which has been very nearly equal to the actual expenditures for finding oil by the industry. A survey by the Mid-Continent Oil and Gas Association of companies producing approximately half of the oil in the United States showed that in the period 1925-48 the expenditures for finding oil were within 10 percent of the allowable depletion. In 3 of the 5 years, 1944-48, the expenditures for finding oil exceeded the allowable depletion of this group of producers and for the 5-year period, 1944-48, allowable depletion was within about 6 percent of the expenditure for finding oil. These close relations indicate that the allowable depletion does have a direct effect on expenditures for finding oil and that the amount is not excessive in relation to the capital risked in the search for oil.

The rate of 27½ percent for depletion was determined by Congress after study of experience on the part of the industry in the years immediately prior to 1926 when this method was first adopted. The rate has been reexamined subsequently a number of times and approved by Congress in spite of attack by the Treasury Department. The depletion provision has encouraged the search for oil, resulting in great discoveries and supplies. Even if the rate of 27½ percent had been too high at one time, it has become part of the industry's cost and price structure so that any change in the rate now would tend to affect supply and price.

You have raised the question whether the 27½ percent depletion allowance does not cost more than other ways of achieving the same results. Percentage depletion probably costs less than any other way which could be devised to compensate for the risks involved in the exploration for oil and to encourage the necessary amount of exploration. This is probable from an economic standpoint, because the provision stimulates efficiency on the part of operators, since depletion is limited to 50 percent of the net profit margin. The operator has, in addition to the normal stimulus of profit from efficiency, the further attraction of a tax incentive under the present law. The depletion provision also attracts into the search for oil some capital that otherwise never would be risked in the industry, some of which adds to the discovery of oil and some of which is lost forever.

Direct subsidies to explorers probably would cost more and be less effective than percentage depletion. In the year 1949 there were 14,109 dry holes drilled in the United States. The average cost of these wells was at least \$50,000 and the total cost was about \$700 million. The Treasury Department has never claimed that taxes could be increased by any amount approaching such a figure through a change in percentage depletion. Even if Government subsidies involved paying only part of the cost of dry holes instead of the complete cost, the cost of the program might be greater than \$700 million a year because of the additional number of dry

holes that could be encouraged by the subsidies. A drilling contractor, unable to find sufficient work to keep all of his rigs busy, for example, very probably would be led by subsidies into drilling wells even if he did not expect to establish production. Efforts to limit the cost of the subsidy by controlling the drilling location of wells would involve the Government in endless details and expenses regarding geology, geophysics, and other matters, and subject the industry to stifling controls by men in Government who know nothing about the business of finding oil.

Subsidies in maritime shipping are closely related to the fact that the Government has imposed regulations on the shipping industry which result in high costs relative to the merchant marine of foreign countries. There is no comparable reason for subsidies in petroleum production. The oil-producing industry feels that it is entitled to reasonable tax treatment to avoid the taxation of the capital which it creates through the discovery of new reserves, but it does not seek subsidies which at best would be destructive of efficiency, difficult of interpretation and administration, and extremely expensive to the taxpayers. Oilmen are by nature individualists and are opposed in principle to Government subsidies.

You further inquire whether a very large portion of the benefits from the depletion allowance does not go to persons "who are not the ones who do the exploring and take the risks." Statistics cited by the Treasury Department in its latest proposal to reduce percentage depletion make it clear that the great majority of the benefits go to the companies—both small and large—which are now engaged in exploration and development.⁶ All of the large oil companies which produce more than half of the oil in the United States, are engaged in extensive and expensive exploration and development programs. A review of the annual reports of these companies demonstrates the vast sums of money, running into the billions of dollars, which have been poured into the search for and development of new reserves within the past few years. The small operators, similarly, are spending sums proportionately as large considering their production. It is not true, as is sometimes alleged, that the small operator searching for oil today sells his property upon development of production. Occasionally some operators sell producing properties, principally to put their estates in liquid condition to pay inheritance taxes, but the great majority of the operators, who discover production today develop their properties and produce them. Such operators are receiving the benefits of the reasonable tax provisions applicable to oil production as a result of taking risks in exploration and development.

The purchaser of a proved property, who is still taking considerable risks with respect to the amount of recoverable oil and the future price, generally pays a price which means that percentage depletion is of no benefit to him because it is less than cost depletion. At the present time, for example, developed oil reserves in the ground generally sell for about \$1 a barrel which exceeds the percentage depletion, amounting to a maximum of 71 cents a barrel on the present price of \$2.58 a barrel. If the percentage depletion provision is applicable and appears to place the purchaser in a position to save taxes, it influences the price he is willing to pay for the property and so results in a benefit to the operator who found and developed it. An inflationary trend which raises the price of all commodities may result in tax benefits even to a purchaser whose cost depletion at the time of the purchase exceeded the pre-

vailing percentage depletion, but that is the reason for criticism of the conditions which bring about inflation and not for criticism of the operator who purchased an oil property on the basis that it was a reasonable investment at the prices then prevailing.

Perhaps the criticism that the benefits of percentage depletion go to persons who are not the ones who do the exploring and taking of risk is meant to apply to royalty owners. Even the royalty owner, however, may take risks and there are, in fact, many royalty owners who are also engaged in exploration and drilling. In fact, many independent operators regularly buy royalties as part of their business. Basically, however, the reason for application of percentage depletion even to the royalty interest is to protect the capital of the royalty owner which arises from the discovery and development of oil. The royalty owner, as much as the producer, has a known capital value as soon as production is established and is entitled to protection of that capital value before his income is subjected to the ordinary tax rates.

In your comments relative to the "in oil" provision you seem to imply that percentage depletion is an advantage amounting to a tax favor, even though you can see it is warranted more than the provision regarding oil payments.⁷ In the opinion of the oil industry the percentage depletion provision is merely a recognition of the penalties inherent in the risks involved in finding oil, and is necessary to avoid a tax penalty amounting to taxation of its capital to which it should not be subjected. Percentage depletion merely places the oil industry, insofar as the taxing of capital is concerned, on an equal footing with other industries which do not create new capital through discovery of hidden resources.

Yours sincerely,

REX G. BAKER.

OCTOBER 14, 1950.

DEAR MR. BAKER: The figures which you cited in your last letter are interesting and significant. However, they do not, I believe, take account of the fact that a large proportion of these expenses are deducted in computing income taxes, in addition to the percentage depletion deduction. I am referring, of course, to the optional deduction allowed for intangible drilling costs, and other similar deductions.⁸ The figures you give would be more persuasive to me if they showed a comparison between the costs on the one hand and the aggregate deduction on the other. By aggregate deduction, I mean not only percentage depletion, but also the deduction allowed for intangible drilling costs and other expenses. I do not believe that the comparison would be nearly as favorable as the figures you give indicate. Indeed, I should think this might be a major weakness in your argument.

Now let me turn to the last paragraph of your letter. The basic difficulty here, it seems to me, is one which is rarely disclosed in discussions from the oil country. This is the "discovery" allowance which is implicit in percentage depletion. I know of no other area in our tax law where very large increments in capital value are wholly exempt from taxation. You say that percentage depletion is necessary to enable the industry to preserve its capital. But this is obviously using capital in a double sense, and in a sense which is not applicable to other taxpayers. For other taxpayers, that capital, recoverable through depreciation, or on sale, or otherwise, is their investment in the property. Only in the oil business do "discoveries" become capital for tax purposes.

⁶ Hearings before Committee on Ways and Means on H.R. 8920, 81st Cong., 2d sess., pp. 49-60 (1950).

⁷ See p. 365, supra.

⁸ U.S. Treasury Regulation III, sec. 29-23 (m)—16(b) 1943.

Frankly, I find some trouble seeing why this should be so.

You suggest that this is necessary because of the risks involved in finding oil. I do not minimize these risks. I know that in a sense, they are very great. However, I think a pretty good case can be made for the proposition that large outfits, like the Texas Co., or the various Standard Oil companies do not take very substantial risks, except in a sense analogous to that in which it is said that the New York Life Insurance Co. takes risks. Or, to put it another way, when the operations are on a large scale, as in the life insurance business, the probability that things will come out somewhat as planned is very great. I do not mean to say that the probability is nearly as great in the oil industry as in the life insurance business. Nevertheless, experience has shown over the past 20 years that the big oil companies stand a high probability of success. They have no difficulty recovering the costs of their unsuccessful ventures from the products of their successful ones. I really seriously question whether it can be shown that percentage depletion is a necessary compensation for risks taken in these cases. The situation with respect to wildcatters, and the problem of stripper wells, are quite different. But the big companies account for a very large proportion of the production. It is far from clear to me that percentage depletion is ever necessary either (a) to compensate them for risks taken or (b) to safeguard their capital investments.

Very truly yours,

ERWIN N. GRISWOLD.

OCTOBER 16, 1950.

DEAR DEAN GRISWOLD: Enclosed is a section of yesterday's Houston Chronicle which contains a good deal of information concerning the oil and gas industry.* It will give you some idea of the enormous cost involved in finding and developing oil and gas, and of the tax burdens borne by the industry.

Yours sincerely,

REX G. BAKER.

OCTOBER 20, 1950.

DEAR MR. BAKER: It was good of you to send me the oil progress section of last Sunday's Houston Chronicle. I have looked at this with much interest.

I must confess, though that I am still not impressed by the tax burdens borne by the industry. I have no doubt that the industry presents many problems and bears a good many burdens. But its tax burdens would surely seem to be lighter than those carried by most other industrial enterprises. Take a look someday at the proportion of taxes to net income of three large oil companies, on the one hand, and three large nonoil industrial enterprises on the other. The figures are astounding.

If you say that you are not talking about the big companies, but about the little fellows, then I think we might meet on common ground. But a very high proportion of the tax benefit goes to the big companies.

Very truly yours,

EDWIN N. GRISWOLD.

OCTOBER 26, 1950.

DEAR DEAN GRISWOLD: It is a pleasure to receive your letters of October 14 and 20 on the subject of taxes paid by the oil industry. Your interest in this subject leads me to set forth a few additional points about the operations of the oil industry, for it seems that the lack of general understanding of the peculiarities of oil production is one of the principal reasons why the tax provisions relating to oil production are often criticized.

A crucial point, as brought out in your letter of October 14, is the question of contribution of the developer of oil production and the measure of the capital which he is entitled to recover free of tax. Two points seem pertinent on this question.

In the first place, let us consider two individuals investing \$500,000 each, one in the search for oil and the other in an office building. The individual searching for oil may spend \$100,000 on each of five different leases and establish production on only one of the leases. The other individual erects an office building with his \$500,000. Would it be fair to allow the oil operator to recover as capital on his productive lease only the \$100,000 that he put into that lease? If the individual is to risk his money in the search for oil it would seem that he would do so only with the prospect that he would recover more than the \$500,000 spent on all of his ventures if he is successful. There is always the chance that he may find no production with his investment and all of his capital may be lost. To offset that risk there must be the attraction of a reward commensurate with his success if he finds oil. Another individual might venture \$500,000 in the search for oil and discover twice as many barrels of reserves as his competitor, due to skill and good fortune. In this latter case he has made a contribution to society which is worth twice as much as that of his competitor. As soon as the oil is discovered and developed it can be sold in place, without being produced, for a known capital value, and, in case of such sale, taxes are on the basis of capital gain rather than current income.

The second point is that a producer of oil realizes two distinct kinds of income; namely, a capital gain on the sale of an asset which has been held for a long period of time and a short-term income on the operation of a producing property. The capital gain is measured by the difference between his investment in establishing the production and the price at which he could sell the oil in place and turn it over to someone else who would then make the current profit on the operation of the producing property. The percentage-depletion provision results in substantially the same rate of taxation as would result from the separation of income into its two component economic parts and the taxation of one part as capital gains and one at current income-tax rates. In the absence of such consideration in the income-tax laws, operators discovering and developing oil would be encouraged to sell their oil in place rather than to continue in business. It would seem to be in the public interest for tax policy to permit and encourage successful operators to stay in the business rather than to sell their properties to others who may have been less successful in the search for oil.

You raise the question whether the operations of large oil companies do not in effect reduce the risks of this business to those comparable with a life-insurance company and suggest that the probability that things will come out somewhat as planned is very great. I am sure you would find that the life-insurance companies do not consider their business in any way comparable with that of oil production, else with their large funds they would already have entered this business. A life-insurance company not only knows the risks but also the precise amount of money which it is going to spend and take in. The company engaged in the search for oil has not such assurance. It only knows that if it has average experience more than 1 out of 3 wells that it drills will be dry, but it has no way of knowing how much oil its productive wells will develop or what the value of that production will be when the oil is produced over a period of 20 or 40 years. A decline in the price of

crude oil, for example, such as occurred between 1926 and 1933, can wipe out the apparent profits anticipated on the basis of cost and price realizations at the time of the investment. Naturally, the investments of the oil companies made during the depression seem very successful, but so do practically all other investments made at the same time. That fact does not provide any assurance against a decline in prices. The big oil companies are definitely taking very substantial risks which may break them as well as make them in the future. The Humble Oil & Refining Co., for example, has spent millions of dollars in Florida and to date established only a very small production. Unless our efforts and luck in that area improve, we stand to lose a very large sum of capital that Humble has risked in the venture. If we do lose our investment, we can deduct it in calculating our income-tax payments just as any other business could deduct its losses on an unsuccessful investment, but that does not return to us the capital which Humble has risked. In the year 1949 alone Humble's dry-hole costs were \$32,267,000, and even after consideration of the reduction in income taxes due to such loss it is clear that we risked and lost a very substantial sum of money. We can have no hope of realizing a return on that investment. Indeed, the investment itself is wiped out.

One final observation may help to throw additional light on the question of the oil industry's risks and the relation between its costs and deductions. I mentioned in the previous letter that a survey by the Mid-Continent Oil & Gas Association showed a close relation between the expenditures for finding oil and the allowable depletion. In your letter of October 14 you ask about the optional deduction allowed for intangible drilling costs. The same study previously referred to shows that the investment of the companies included in the survey in drilling and equipping productive wells exceeded their expenditures for finding oil. The sum of the expenditures for finding oil and for drilling and equipping productive wells was approximately twice the total allowable depletion of the companies for the period 1925-48. The investment in drilling and equipping productive wells was recovered only once as a deduction of intangible drilling costs and depreciation of tangible drilling costs. I did not mention this fact in my previous letter because percentage depletion relates to the depletion of the oil itself and, therefore, to the expenditures incurred in the search for oil rather than to the tangible and intangible investments in drilling, which are recovered through the option to expense intangible drilling costs and the depreciation of other drilling costs. This evidence is quite significant on the point which you considered a weakness in my previous argument.

In your letter of October 20, 1950, you suggest that we look at the proportion of taxes to net income for three large oil companies on the one hand and three industrial enterprises on the other. The point you are referring to can be illustrated from the comparison of the reports of United States Steel and Humble. In 1948 United States Steel showed a net income before Federal income taxes of \$239 million, compared with Humble's net income on the same basis of \$240 million, while United States Steel paid Federal income taxes of \$109 million and Humble paid \$54 million. In 1949 United States Steel paid \$126 million in Federal income taxes on a net income before taxes of \$292 million, whereas Humble paid Federal income taxes of \$18 million on an indicated net income before taxes of \$138 million. The explanation of the difference in the effective rate lies, of course, in the fact that a considerable part of Hum-

* Houston Chronicle, Oct. 15, 1950, sec. E.

ble's net income really represents capital gain on the sale of its oil, and this capital gain should be taxed at 25 percent rather than at the normal corporate income tax rate, also in the fact that Humble is taking its depreciation on intangible drilling costs as it makes such investment rather than spreading the depreciation over the life of the properties. If Humble were to quit drilling or to reduce its drilling operations, the effective income tax rate would materially increase. Over a period of time the only difference between the effective tax rate on a steel company and an oil-producing company would be because of the percentage depletion, which is thoroughly justified in order to afford fair treatment of the capital gains realized on the sale of oil as it is produced.

I have taken the liberty to write at length on points suggested by your letters because you have shown a genuine interest in an objective inquiry about the facts with respect to the tax provisions on oil production. We find in our own operations that the business of exploration for and development of oil and gas is very complicated and not always fully understood even by some of the operators engaged in this business. It has been my endeavor to set forth information which may help to give you a better picture of the problems of oil production. We believe that the problems and peculiarities of the oil-producing business warrant and require the tax provisions now applicable with respect to percentage depletion and the option to expense intangible drilling costs.

Sincerely yours,

REX G. BAKER.

NOVEMBER 6, 1950.

DEAR MR. BAKER: Please let me thank you for your letter of October 26. I have read it with much interest, and I would like to make certain observations.

In the first place, it seems to me entirely clear that the costs of any oil operations should be fully deductible from income, including subsequent income from other operations, where there is no current income against which the costs may be deducted. Taking as an example the situation given near the beginning of your letter, if a person spent \$100,000 on each of five different leases, and established production on only one of the leases, I would allow the full \$500,000 to be deducted against income, other current income from any source if there was such income, or against subsequent income from any source. This could be done by a system of carryovers. If the present 5-year limit¹⁰ on carryovers is not enough, I would have no objection to its being extended. I am entirely in favor of taxing no more than the net income of oil operations. I still find it somewhat difficult to see why we should tax less than that net income, which may be, and often is, the result of the 27½ percent depletion allowance, which goes on without limit, and without relation to (a) actual depletion sustained or (b) the aggregate amount invested by the taxpayer in oil production.

The rest of your letter is devoted to what seems to me to be the heart of your argument. In substance, you seem to be saying that all income from oil production should, in effect, be taxed as capital gain, and that this gives an adequate justification for the present depletion allowance. This argument, I must confess, I find very hard to follow.

Is it not clear that income derived from oil production is business income? Is there any other sort of business income which is taxable as capital gain? When the grocer sells you a can of peas, he sells you property, but the gain is taxable as ordinary income,

no matter how long he has held the peas. The same is true of a manufacturer, or of a real-estate operator. Indeed, the same is true of every other sort of business income. Why should income derived from oil production be treated in any other way? Perhaps the answer is that all income should be treated as capital gain. That would, of course, be attractive, and it would not result in discrimination between different types of business activity, as is the situation now. But it would hardly produce the revenue which, for better or for worse, is necessary under current conditions.

You mention the fact that in the year 1949 alone Humble's dry-hole costs were \$32,267,000. But every nickel of that was deducted against other income, and Humble was not taxed on anything in excess of its net income. On the contrary, Humble paid taxes on much less than its economic net income, as can easily be shown by comparing the company's net income, in its reports to stockholders, and the much lower figure for net income which was undoubtedly given on its income tax return as a result of the 27½-percent depletion deduction. It is true that Humble risked and lost a lot of money on dry holes. But it is also true that it made even more money on other activities. And no one suggests that it should be taxed on anything more than its net income, after making full allowance for all the losing ventures. Frankly, I find it very hard to see why the dry-hole costs, fully allowed as tax reductions, have any bearing on the justification of the depletion allowance. There are many other industries which have to risk large sums, without any immediate or current tax deduction. I need to refer only to the steel industry for an illustration. There, large sums must be spent which are capital costs, and not deductible at all, except through carefully measured and limited depreciation deductions. In this respect, it seems to me that the oil industry has a great tax advantage, quite apart from the unlimited depletion deduction.

When all is said and done, your argument seems to boil down to the proposition that income from oil production should be taxed as capital gain. This appears near the end of your letter when you state that the percentage depletion deduction "is thoroughly justified in order to afford fair treatment of the capital gains realized on the sale of oil as it is produced." This argument seems to me to be clearly unsound. I can see no reason why, if valid at all, it would not be equally valid to all other income from production. Take, for example, the income from farms or from manufacturing. The farmer produces property. The manufacturer produces property. Yet no one has ever seriously argued, I believe, that their gains on the sale of this property should be taxed as capital gains, or that they are capital gains. The income from the conduct of the business is clearly business income. Oil production is clearly a business. I can see no reason why the income derived from the business of oil production should not be taxed as ordinary income. I repeat that I refer only to the net income, after full allowance for all costs incurred and for all capital actually invested in the business. But the percentage depletion deduction goes far beyond this. It gives a very large deduction, which bears no relation either to costs or to actual capital investment. I am still puzzled why anyone should think that it has a proper place in a fair and equitable tax system.

I have no hostility to the oil industry. On the contrary, I admire its great achievements, and its great contributions to the country, its economy, and its defense. But there are also many other forms of activity which contribute greatly to the country, its economy, and its defense. Why should they

not all be treated the same? Why should the oil industry be the recipient of a tax deduction, enormous in the aggregate, which bears no relation to its costs, or to the capital invested in oil production?

Very truly yours,

ERWIN N. GRISWOLD.

NOVEMBER 8, 1950.

DEAR DEAN GRISWOLD: Your letter reveals the difficulty that even a man of your ability has in understanding the real nature of the oil business and the risks involved in finding and producing oil. After all, the basic principle involved in the depletion allowance is rather simple. The man who explores for oil must invest sums of risk capital. He may lose this capital altogether on unsuccessful ventures. He may through luck or skill succeed in finding an oilfield. If he does, he creates new capital. In producing that oil he depletes the corpus, and if the taxing away of his capital is to be avoided he must have a depletion allowance. Only in this way can he, under our existing tax rates, have enough left with which to do further exploratory work with the hope of finding new reserves to replace those depleted by production.

There is no way to compare his real situation with that of the steel manufacturer or the farmer mentioned in your letter. The man who builds a steel mill can depreciate every dollar of his investment in time, and through depreciation get his capital investment back tax free. The farmer who raises a crop does not deplete the corpus of his farm, for he is able to grow a new crop year after year. Therefore, any sums he may realize from the sale of his crops are ordinary income. Of course, he can charge off depreciation on his tools and equipment because they wear out and must be replaced.

Thus in its essentials depletion does nothing more than afford the oilman an opportunity to replace his capital. This is exactly what is done with the owner of the steel mill who is allowed depreciation on his plant investment. To me this analysis is simplicity itself and I cannot see how its validity can be questioned.

I sincerely hope that you will be able to come to Texas some day. Perhaps you would enjoy a trip to the oilfields and an opportunity to witness the widespread wildcat operations which are taking place in this part of the country. Then I believe you could better understand why the enormous risk capital involved in operations must be regenerated out of the depletion allowance on the oil that is found and produced.

Sincerely yours,

REX G. BAKER.

NOVEMBER 27, 1950.

DEAR MR. BAKER: It seems to me that your position boils down essentially to one matter; namely, that oil producers are entitled to special tax treatment because their income is essentially capital gain.

The argument that the present percentage depletion allowance is necessary to enable you to recover your actual cost will not stand up, particularly as applied to a company like yours. I have made it plain that you, or any other oil producer, should be able to recover all of your actual investment before any tax liability is incurred. As a matter of fact, though, the combination of the deduction of intangible drilling costs plus percentage depletion gives you, and most oil producers, a deduction far in excess of your costs. I have no doubt, for example, that the aggregate of these two deductions taken by Humble in the years since percentage depletion became available is far in excess of the aggregate of Humble's actual costs in those years. There is no other type of business enterprise in this country which receives deductions in excess of costs through depreciation or otherwise.

¹⁰ Internal Revenue Code, sec. 122.

In the case of certain independent wildcatters, it may be that a succession of dry holes will produce costs which cannot be offset, under present laws, against subsequent income. This should be largely taken care of, however, by the present provision of the law allowing losses to be carried forward for 5 years. If this is not enough, I would have no objection whatever to any change in the law which would make it plain that no oil producer was subject to tax until he had received deductions equal to all of his costs which had not previously been effectively deducted from gross income.

Let us try to test your capital gains argument. Suppose we had a tax, like the English tax or the Canadian tax, in which capital gains are not taxed at all. Could you successfully maintain the position that income from oil production is not subject to tax at all, because it is capital gain? It seems to me that the answer to this is quite plainly "No."

The tax systems which do not tax capital gains all draw the line closely between what they regard as capital gain and profits from trade or business. It is clear that the operations of oil production are a trade or business, within this concept, as well as under our own law.

We do not have to speculate about this. The Canadian income tax is a clear example. Under that law, capital gains are not taxed. But it has never been seriously suggested, as far as I know, that the income from the production of oil and gas in Canada should be wholly exempted from tax on the ground that it is capital gain. On the contrary, it is clear that it is regarded as income from trade or business, and subject to tax as income. It is true that there is special allowance for depletion under the Canadian tax law. This may, however, be a reflection of the special deduction allowed in the United States law.

On the whole it seems to me that the best position you have developed is the capital-gain one. Even on that basis, though, I think you claim too much. Under our law capital gains are taxed, though at a maximum rate of 25 percent. But the percentage depletion deduction is supposed to reflect the old discovery-value allowance. The effect of this was to make the capital gain on the discovery of oil (or other minerals) wholly exempt from tax. In other words, discovery value—and, therefore, percentage depletion, to some extent—clearly goes too far. I think I could understand a provision which said that income from oil and gas production should be taxed as capital gain, and which, accordingly, completely eliminated the percentage-depletion deduction. Trying to get both capital-gain treatment, and the percentage-depletion deduction, as in the recently defeated provision about in-oil payments, is clearly trying to get too much. And if income from oil production was taxable as capital gain, I should feel that, under current conditions, the present 25-percent rate was far too low.

However, it still seems to me that taxing income from oil production as capital gain would be quite wrong. Such income is clearly income from the conduct of a trade or business and is not capital in its nature, even though it arises, in a sense, out of increases in the value of property. After all, the income of any manufacturer or retailer likewise arises out of increases in the value of property; namely, the property which is manufactured or sold. Such income, however, is clearly not capital gain. There is no better reason, as far as I can see, why the business income of oil producers should be taxed as capital gain merely because it is derived by selling the property that they produce.

You suggest at various places in your letters that the oil producer should be able to

get tax free the capital he has produced. I do not know any other line of activity in which a person recovers tax free any capital he may have produced. Even in the case of capital gains, the basis for determining gain or loss will be only the amount actually invested in the property. It is only the oil industry which gets a return free of tax in excess of its actual capital investment.

Thus, the percentage depletion allowance turns out to be nothing more than a special subsidy. If that fact were more generally understood, I cannot help wondering whether the present allowance would be continued unmodified.

Very truly yours,

ERWIN N. GRISWOLD.

DECEMBER 12, 1950.

DEAR DEAN GRISWOLD: As I interpret your letter of November 28, you insist that oil producers receive special and unwarranted tax treatment and that all their income should be taxed as ordinary income, despite the fact that in your letter of September 25, you concede that oil producers are entitled to a depletion allowance, merely questioning the advisability of placing it at 27½ percent. Actually, the depletion allowance is applicable to relatively few oil-producing properties. In practice, cost depletion applies to the poorer properties. Furthermore, percentage depletion is limited to 50 percent of net income derived from a producing property. Thus, in general, it is improper to refer to 27½ percent depletion rate as applicable to all oil properties.

The producer of oil receives two different kinds of income. He realizes a capital gain or loss on the sale of an asset held over a long period of time and a normal income on the operation of a producing property. The income tax law authorizes the taxation of income and not capital. Therefore, any capital gain from the sale of an asset held over a long period of time should not be taxed as normal income. Only the income derived from producing operations can justly be taxed as normal income. Consequently, the depletion allowance, which makes it possible to avoid the taxing away of capital, does not give special treatment to the oil industry and is completely justified. This is proved by the fact that the profit figures for the oil industry clearly follow the same pattern as for other industries.

There is no evidence that the tax provisions have resulted in advantage for oil producers as compared with businesses in general. The fairness of a tax cannot be judged by merely looking at the most successful operators, but must be tested by considering the average results for all operators.

The function of such profits as are realized after taxes is to direct investment capital into different activities in proportion to need. There is no evidence that profits have been so high as to attract any more capital into the oil industry than is needed. While the oil industry has constantly expanded, the expansion has contributed greatly to the maintenance of low prices for fuels, to economic progress, and an expanding economy. If the profit rate on oil production had been reduced by higher taxes, the capital attracted into the industry would have been reduced; additions to oil reserves would have been less. The smaller supply of energy would have retarded economic progress in the United States, and the price of gasoline and other petroleum products to the consuming public would have been materially increased.

Thus, it seems clear that the wisdom of the depletion allowance is more than justified, and experience has demonstrated that the depletion allowance is not excessive but has been only enough to generate new risk capital required in exploring for oil.

Yours sincerely,

REX G. BAKER.

Mr. DOUGLAS. Mr. President, this completes the formal presentation of the material in support of my amendment.

I have not been in politics for a quarter of a century without knowing the forces which are alined against this amendment—the most powerful forces in the country, contributors to campaign funds, contributors to campaign committees, contributors to individual senatorial and congressional campaigns. In return, it is asked that the men so helped protect the depletion allowance. This is one of the most corrupting influences in American politics; and both parties are tarred with it.

I had hoped that my party—the party of Bryan, Woodrow Wilson, Franklin D. Roosevelt, and Harry Truman—might remain immune, or relatively immune, from this influence; but it is not so. Those in the know are well aware of the powerful influence of the oil companies upon Democratic policy and Democratic votes, and also—perhaps to an even greater degree—upon votes on the other side of the aisle.

But, Mr. President, if we are to retain any faith in our system, we must enforce the tax laws without fear or favor. By favoritism, we are encouraging evasion and avoidance on the part of millions, who say the whole system is a racket, that the big boys can get legal protection, so why should the others declare all their income? The expense accounts and the other forms of evasion are eating like an ugly cancer all through our national life; and we have made it worse in the last weeks in the Finance Committee and on the Senate floor, as measure after measure to help the powerful and the rich has gone through, but amendment after amendment to try to protect the average taxpayer has been voted down. We have seen the spectacle of a bipartisan political combination, operating on both sides of the aisle, move like a juggernaut in this direction.

Mr. President, I am well aware that when the issue is put to a vote—whether on a motion to lay on the table or whether a vote directly on the amendment there will be a majority, and probably a big majority, against this amendment. But I take some courage from the fact that when the vote was taken on the amendment of the Senator from Delaware [Mr. WILLIAMS], 30 Senators voted against laying it on the table.

I remember that back in 1951, when we began this fight, only nine Senators wanted to reduce the depletion allowance. They were the Senator from Oregon [Mr. MORSE], the Senator from Delaware [Mr. WILLIAMS], the Senator from Minnesota [Mr. HUMPHREY], myself, and five others, whose names I cannot remember at the moment—but only a total of nine. Now the number has grown, even on an incomplete rollcall, to 30; and I was especially pleased that the chairman of the Senate Finance Committee, the senior Senator from Virginia [Mr. BYRD], voted with us on that yea-and-nay vote. I think it is the first time he has done so. It may be indicative of the shift in public opinion.

We know we shall be beaten tonight; the bipartisan coalition will roll over us.

But we shall go down fighting, even at this late hour.

Some of the supporters of the depletion allowance scornfully say, "These amendments have been defeated before, and they will be defeated again. So pay no attention to them; they do not amount to anything."

Mr. President, I thought of some lines written by James Russell Lowell, who perhaps is out of fashion today, but who wrote some good poetry about the anti-slavery issue—poetry which also is applicable to the depletion-allowance issue. Since other Members of the Senate have quoted poetry—of an inferior nature—I hope I may be pardoned if I quote these lines from James Russell Lowell:

Truth, crushed to earth, shall rise again;
The eternal years of God are hers;
But Error, wounded, writhes in pain,
And dies among his worshippers.

Mr. President, it is solemn truth that the depletion allowance should be greatly reduced. We are going to be beaten tonight; but in God's good time we will not be beaten, and the powerful oil interests which have their representatives on this floor, and who will vote down this measure and who will be victorious this time, in due course of time will not be victorious, because they are defending something which is morally and economically wrong.

Mr. PROXMIRE. Mr. President, will the Senator from Illinois yield?

Mr. DOUGLAS. I am glad to yield for a question.

Mr. PROXMIRE. Will the Senator from Illinois inform the Senate how much this amendment would increase revenue?

Mr. DOUGLAS. The minimum estimate of the Treasury is about \$320 million. The Library of Congress estimate is approximately \$500 million. Probably the correct figure is somewhere between the two; and the amendment would roughly balance the tax bill.

Mr. PROXMIRE. That is my second question. One of the serious problems in connection with the pending tax bill—and in the judgment of many persons it is the most serious problem in this connection—is that this tax bill, which started as a revenue-raising bill, will now result in the loss of hundreds of millions of dollars of revenue.

Mr. DOUGLAS. That is correct.

Mr. PROXMIRE. But the effect of the amendment of the Senator from Illinois would be to change that situation and to compensate for the revenue losses caused by other parts of the bill; and thus the amendment would result in a balanced tax bill, which would not lose a substantial amount of revenue, and might even balance the revenue losses with a revenue gain.

Mr. DOUGLAS. The amendment would result in a roughly balanced bill—not a precisely balanced bill, but a roughly balanced bill.

Mr. PROXMIRE. Is it not true that perhaps the best test of justice or of what some might call liberalism is one's attitude toward revenue-raising measures? And is it not true that we can determine—on the basis of Senators'

votes whether they believe taxation should be based on ability to pay or that it should be based on political and economic power? Would not this seem to be the place, if any, to divide those who believe in economic and political justice from those who do not?

Mr. DOUGLAS. Amendments such as this one will, in the slang parlance, separate the men from the boys. Whatever may be one's view in regard to the general system of taxation—whether one believes it should be proportional, with the rate constant as income increases; or whether one believes that it should be regressive, with the rate decreasing as income increases; or whether one subscribes to the position to which I hold; namely, that the rate should increase as income increases—in any case those with equal incomes should pay equal taxes. But that is not the case when special groups receive special and favored treatment in regard to the taxation of income.

Mr. President, I yield the floor.

Mr. MONRONEY. Mr. President, I rise in opposition to the amendment of the distinguished Senator from Illinois.

At the beginning, I would like to say that many of us who have long supported the depletion allowance have done so from deepest conviction that it is not only economically sound, but that it has been indispensable to building in this country a reliable, available source of the mineral which is the most necessary to our economy in peace or war.

In my State oil is the second largest income producer, ranking only slightly below agriculture.

I assume that the distinguished Senator from Illinois is speaking with complete integrity as he discusses the various economic issues which he regards as important to the Nation or to the State of Illinois. I ask that the same credit for honest conviction be given to those of us who see this question in a different light.

The Senator implies that we are tools of the giant oil industry. It is also possible that on the merits of the issue, he is wrong and we are right.

The amendment the Senator offers would, I believe, be subject to severe criticism on many grounds. The Senator, in his amendment, is singling out oil as an evil thing and treating the depletion allowance as merely a means of grabbing extra income.

We in Oklahoma consider the depletion allowance as the greatest possible accelerator to make America self-sufficient in oil.

Like the Williams amendment, this amendment proposes to single out oil and gas and establish a sliding scale of depletion for that 1 mineral out of the 37 which enjoy comparable depletion allowances.

Not only does it single out one industry for different treatment, but it singles out the industry which consistently spends a greater percentage of its income to find and develop new supplies—the purpose of all depletion allowances—than any other mining industry. It singles out the only mining industry which consistently spends \$3 on exploration and development for new

supplies for every dollar that it retains in depletion.

The greatest objection to the amendment is that it would extend the maximum depletion allowance of 27½ percent to the very class of taxpayers who are least likely to reinvest in exploration—those whose gross income from oil and gas is less than \$1 million. In this group would be most royalty owners and one-shot speculative investors in wild-cat wells. It would reduce the allowance to the very classes of taxpayers that are most likely to reinvest not only the funds retained for depletion, but much more in exploration for new supplies. Thus, taxpayers with incomes from oil and gas of more than \$1 million but less than \$5 million would be given an allowance of 21 percent and those with incomes from oil and gas in excess of \$5 million an allowance of 15 percent.

The 33 largest oil companies in the United States are the subject of an annual report by the petroleum department of the Chase Manhattan Bank. All of these companies would have their depletion allowance reduced from 27½ to 15¼ percent on all oil and gas production. The latest issue of this report, entitled "Petroleum Industry, 1961," indicates that these companies spent in 1961 on exploration and development in the United States alone over \$100 million more than they retained for depletion, depreciation, and amortization combined.

We cannot have it both ways. If the American oil industry is to continue to find adequate supplies to meet the Nation's needs, it must obtain the necessary funds to pay for the cost of exploration. We must either retain the present depletion allowance, or accept a substantial increase in the cost of gasoline and other petroleum products. There are no other sources of the necessary money. The profits of this industry are consistently lower than the average profits of manufacturing industries in the United States.

Some of those who have been critical of the depletion allowance have frankly recognized that its withdrawal would require an increase in price. Prof. Arnold G. Harberger of the University of Chicago has testified that—

More oil can indeed be obtained by tax concessions * * * (but) * * * if the rest of the economy wants more oil, it should be willing to pay for it by way of a higher market price.

This means primarily an increase in the price of gasoline.

Rather than agree with the Senator that we are oversupplied or that we are wasteful in investing in oil, I am proud that we continue to have, within the borders of this Nation, an adequate supply of oil which has taken us through two World Wars and the Korean conflict.

I shudder to think, with all our mechanized equipment, from airplanes to submarines to diesel trains to compact cars, that we would have to suffer the outflow of dollars which would be required to import all the oil needed to keep our industrial machine on the move.

I feel that the way to get production is the way we have gotten it in the past,

that is to make it worth the gamble for men to drill. In the days when the depletion allowance originated, it was common to take a string of cable tools and drill 1,000 or 1,500 feet below the earth's surface and hit an oil well. Today we have gone below the 5,000-foot depth. We are probing the 10,000 depth. There are wells in my State which are searching for oil at the 15,000 foot level, and there is a search for oil where it has not been found before.

This is equally true of all search for oil today. The lush days of the east Texas field are gone. There has not been a field like that found in more than a score of years. Aside from the Williston Basin, the fields have been small in size and low in production. Yet the Senator from Illinois would take away the right of oil to be treated as any other mineral.

There are over 50 minerals that receive a depletion allowance. Oil and gas receive the top allowance, which is 27½ percent.

It is not generally recognized that the depletion allowance for the oil industry is limited to 27½ percent of its gross or 50 percent of its net earnings, whichever is less. For the industry as a whole, this results in an average depletion allowance of about 23 percent—the same as provided for sulfur, lead, zinc, uranium, nickel, in fact, for a total of 37 other mining industries. Even the producers of sand and clay have depletion allowances under our laws.

Mr. DOUGLAS. Mr. President, will the Senator yield?

If the Senator wishes to offer an amendment which would apply to sulfur, bauxite, and the other minerals which he has mentioned, the same depletion allowance as to oil, I would be willing to support the amendment.

Mr. MONRONEY. I am saying that oil which is found by a group that has \$1 million gross income a year is as much entitled to a depletion allowance of 27½ percent as a group that has a gross income from oil of only \$500,000. After all, profit is the thing we are trying to measure. In a situation such as this, those having a \$1 million gross income, whose depletion allowance would be cut from 27½ percent to 21 percent, are not giants. At \$3 a barrel, \$1 million gross would be produced by 300,000 barrels. This would produce a net profit, on the average, of 25 cents a barrel before taxes, or about \$73,000 a year. These are not giants whose depletion allowance would be reduced from 27½ percent to 21 percent.

Mr. PROXMIRE. Mr. President, will the Senator yield at that point?

Mr. MONRONEY. I yield.

Mr. PROXMIRE. Would the Senator support an amendment merely to reduce the level of oil depletion to that allowed sulfur, 23 percent, and permit oil to have the same depletion allowance as the second most favored group of minerals?

Mr. MONRONEY. Of course not, because sulfur is not found at 5,000 to 25,000 feet below the earth's surface. It does not require a well costing \$100,000 to \$1 million to determine whether it is

there at all. The other minerals are found near the surface of the earth.

I have listened patiently to the distinguished Senator's argument. I am trying to say that the much maligned 27½ percent depletion allowance does what I think all America wants; and that is, to make us self-sufficient in oil. It will be remembered that when the Suez Canal was closed we had to open our wells and produce enough to supply the free world.

I think it is a good investment to continue to develop our oil reserves, because we do not know when the war may grow hotter in Berlin, or whether we may have more trouble in Laos, or whether we may face another blowup in the Middle East.

Mr. PROXMIRE. May I ask the Senator another question?

Mr. MONRONEY. We must have a supply which is not only ample for ourselves but also ample for our allies. In order to have this supply there must be a profit motive, to make it profitable for the producer to drill, generally, nine holes in order to get one that will produce. Then, if he has nine such producing wells, new discovery wells, probably only one will prove to be economically feasible, to return a good investment on a good oil strike. I might repeat what I said earlier today in connection with the Williams amendment:

And if an oil producer invested \$300,000 in a well—and was allowed to recover tax free from the output of that well this same \$300,000 of his original investment, he could not normally go out and for \$300,000 find another well to replace the one he had depleted by production.

Wildcatting odds are dead against that. On the average, a man drilling rank wildcats—a man going out to find new reserves to replace those being depleted—would have to drill nine exploratory wells to find one that even qualified as a producer. But even at that, his one producing well out of nine would—if typical—turn out to be a financial failure. Under the prevailing odds, only about 3 percent of all the new field wildcat wells drilled are ultimately successful—producing oil or gas or both in quantities deemed sufficient to turn a profit. Ninety-seven percent of all new field wildcat wells are commercial failures.

Therefore, based on industry averages over a period of time, an oil producer who was depleting a well that cost him \$300,000 would have to have not his \$300,000 back but—at the very least—32 times that original investment—or \$9,600,000—to stand a fighting chance of bucking the mathematical odds and finding replacement reserves.

Giving him \$300,000 in tax deductions would be little better than giving him nothing. It would be the same as telling him to go out of business because—unless he had a very sensational and remarkable stroke of luck—he just wouldn't be able to find a new wildcat well if allowed no more of a deduction than his investment in a well that was depleting.

Mr. TOWER. Mr. President, will the Senator yield for a question?

Mr. MONRONEY. I yield to my distinguished colleague.

Mr. TOWER. Would not the effect of the amendment proposed by the distinguished Senator from Illinois be to penalize success, to discourage the pursuit of success? Is not the pursuit of success that which has built the great

industrial empire of our country? Should we penalize success?

Mr. MONRONEY. The Senator is exactly correct in stating the position which has been taken.

It is said, in effect, "The more successful and the more erudite are the geologists, the more carefully they plan the wildcatting and the exploration, the more we will cut them off, because the allowance is wrong. We must not allow a reward for success in finding oil." We are not asking that anything special be done for finding oil, but we think it is at least entitled to the same depletion allowance everybody else gets.

I cannot see any logic in saying that well A, which produces a commodity called oil, shall be allowed a 27½-percent depletion allowance—but never more than 50 percent of net, I remind Senators, on each well—and well B, because somebody else owns it, because the producer might make \$83,000 a year net on the production of \$1 million worth of oil gross, shall get a 21-percent depletion allowance on identical oil.

Is that the way to write tax legislation? I do not think so. We are singling out the oil industry, and making a target of it. I do not know why it is considered to be so evil, compared to other minerals. No other minerals have strings tied to the amount of gross income which can be produced—from a coal mine, a sulfur mine, a bauxite mine, or a borate mine.

Mr. DOUGLAS. Mr. President, will my good friend yield?

Mr. MONRONEY. I yield.

Mr. DOUGLAS. I should be perfectly willing to accept an amendment from the Senator to reduce the depletion allowances in the case of other minerals and to say that the depletion allowance shall not exceed 21 percent for the amounts from \$1 million to \$5 million and 15 percent for the amounts over \$5 million. If the Senator will propose that, I will accept it.

Mr. MONRONEY. I do not intend to propose it.

Mr. DOUGLAS. Of course the Senator does not intend to propose it.

Mr. MONRONEY. I don't apologize for refusing to legislate in total ignorance of the problems of those industries. I think the 27½-percent depletion allowance has delivered what it was intended to deliver, which is an adequate supply of oil for peace or war.

Today we are asked to cut down the allowance, though we are faced with threats around the world. I think such action would be foolish and irresponsible.

Mr. DOUGLAS. I say to my good friend, if he will yield, that, of course, the Senator understands that once the depletion allowance was provided for oil the pressure began for depletion allowances for sulfur and other minerals, partly to protect the oil depletion allowance and to bring in more allies, and partly because, with oil producers getting to the trough, other producers wanted to get there, too.

This is the greatest source of abuse, because more than \$2 billion of the \$3

billion we lose through the depletion allowance goes to the oil industry. Less than \$1 billion goes to all other minerals combined.

If the Senator wants to mete out the same treatment to other minerals as I would mete out to oil, I should be delighted to accept the amendment.

Mr. MONRONEY. I say to the Senator that I know as little about sulfur and some of the other minerals as I believe some of my colleagues know about oil.

Certainly I do not feel that it is a proper time, during one night, without any hearings as to the effect of the proposal, to drive a knife into the one thing which has kept a big industry solvent, moving ahead, and finding new sources of oil while, above all, maintaining the price of gasoline, which is the principal product, at what it was in the year 1920, exclusive of all the excise taxes that have been levied since that time.

I think this is a pretty good record. I think it is a record of a great American industry under a proved system of trying its dead level best to find the product we need and always to maintain an adequate supply.

Mr. CARROLL. Mr. President, will the Senator yield?

Mr. MONRONEY. I yield briefly. I should like to close in a moment.

Mr. CARROLL. I say to the Senator from Oklahoma that I think he is one of the experts in the field of our domestic oil industry. If my memory serves me correctly, the depletion allowance was enacted into a statute in 1926.

Mr. MONRONEY. That is my understanding.

Mr. CARROLL. The purpose of the statute initially was to aid in regard to exploration for oil in this country; does the Senator agree?

Mr. MONRONEY. It was to help develop an adequate supply of oil. It was also a means to have a uniform cost system to compensate for the exhaustion of a natural resource. What we are talking about is the resource which is discovered. As it is exhausted it cannot be produced the second time. The 27½-percent depletion allowance helps pay the cost of finding a replacement.

Mr. CARROLL. Basically, would not the Senator agree that the original purpose was to stimulate the exploration for oil, for the purpose which the able Senator from Oklahoma indicated, to help produce a domestic oil industry which could meet the needs of the Nation?

Mr. MONRONEY. That is correct.

Mr. CARROLL. I agree with that statement by the Senator from Oklahoma. I must confess that I disagree with some of my colleagues.

I think the President of the United States said at one time, in 1960, that there were about 108 commodities which had some type of this sort of support, and he intended to review them.

In 1932, in 1935, in 1937, in 1938, and in 1939, when we began to move into the foreign fields, the initial concept of the depletion allowance had nothing to do with other than the exploration for domestic oil. Today we know that

in Saudi Arabia, in Venezuela, and in other foreign countries the depletion allowance is being given to American oil companies operating in these areas.

I do not want to interfere with the Senator's presentation, because I agree with the basic premise about the need for developing, for exploring, strengthening a domestic oil industry in this Nation.

The question occurred to me about what we should do when we allow a depletion allowance, which was never contemplated in the original statute, to Saudi Arabia or to Venezuela, and we learn that great financial benefits are going to giant American oil companies who operate the major fields, and that oil is flowing into the United States, interfering and retarding our domestic oil economy?

Does the Senator want to go into that field?

Mr. MONRONEY. That is another matter. Briefly, the rearrangement of the contract makes depletion of little significance, because of the treatment of the royalty as a tax which is deductible. Therefore, as I understand the situation, very few of the Middle Eastern producers even consider the depletion allowance.

Mr. CARROLL. Mr. President, will the Senator yield further?

Mr. MONRONEY. I should like to conclude, but I yield.

Mr. CARROLL. I do not wish to interfere with the presentation by the Senator from Oklahoma, but I suggest that those contracts were negotiated with the support of the State Department. In Saudi Arabia, for example, the contract was set up by royal decree. The taxes paid to Saudi Arabia are offset under a statute, passed in 1918.

I do not wish to demean the presentation by the Senator from Oklahoma. We face a problem. I do not think we can solve it in a short time. We ought to examine the whole program, and consider whether we should limit the depletion allowance to the continental limits of the United States.

I believe I am correct in saying that the Senator from Oklahoma and the junior Senator from Colorado and some other Senators have asked the administration to control the importation of oil into this country because it affects our domestic industry.

Mr. MONRONEY. The Senator has been very helpful in that connection, as I have tried to be. Generally the amendment would have little or no effect in the areas of the Middle East, where the trouble occurs. It would have the effect of shutting down exploration and eliminating the development of fields in the United States. If the amendment were agreed to, we would be playing a dangerous game. We can pay the cost of finding oil in one of two ways. We would either pay it by providing an adequate depletion allowance, and the 27½ percent allowance has proved itself successful—or if we reduce that amount we will make up the difference in the price of gasoline and oil.

Mr. CARROLL. Mr. President, will the Senator yield?

Mr. MONRONEY. I yield.

Mr. CARROLL. Would it not be better for the Senate, the administration, and the Department of the Treasury to begin to direct its attention, first, to the question of the advisability of allowing depletion allowance to American oil companies operating in foreign countries, especially when the Department of State is or has been negotiating agreements in these areas and, second, to the question whether or not we should consider a modification of the offset tax statute?

Mr. MONRONEY. That would be a subject of legislation.

In closing I wish to again point out that the latest issue of the Chase National report entitled "Petroleum Industry—1961" indicates that in 1961 the 33 largest oil companies in the United States spent on exploration and development in the United States alone over \$100 million more than they retained for depreciation or amortization combined. I yield the floor.

Mr. MANSFIELD. Mr. President, it was my intention to move to table the amendment of the Senator from Illinois as I moved to table the amendment of the Senator from Delaware [Mr. WILLIAMS]. However, I notified the Senator from Delaware ahead of time that such was my intention. I did not so notify the Senator from Illinois.

Will the Senator from Illinois do me the courtesy of stating whether he prefers to have a motion to table made or would he prefer an outright vote on his amendment?

Mr. DOUGLAS. I would personally prefer to have an outright vote on the amendment.

Mr. MANSFIELD. Mr. President, I ask for the yeas and nays on the amendment.

The PRESIDING OFFICER. Is there a sufficient second?

The yeas and nays were ordered.

Mr. CARROLL. Mr. President, unless there has been a time limitation on debate, which the Senator from Colorado has not heard about, I wish to make a few remarks on the amendment.

Again we are confronted with one of the most complex economic taxing situations with which the Senate is called upon to consider. We cannot adequately discuss such an important proposal in 1 or 2 hours. The Senator from Oklahoma has made a very fine presentation from the standpoint of the domestic oil industry. He discussed the taxes paid by the major companies in our country.

I point out to the Senate that, according to my memory, one company in one taxing year in Saudi Arabia received a depletion allowance of \$120 million.

I previously have had the privilege of discussing this evening this subject with the senior Senator from Illinois [Mr. DOUGLAS]. Senator O'Mahoney and I had sponsored an amendment which would cut off depletion allowances at the continental limits of the United States. We found that there was no support for the measure among members of the independent oil industry because they were greatly influenced by the major companies who have enormous financial holdings in other countries.

Recently I received information that some of the small refiners and distributors are beginning to understand the consequences of the great outpouring of wealth resulting from foreign oil production into their own marketing and distributing situation here in the United States. The able Senator from Illinois and I discussed the subject only an hour or so ago. I had hoped that the Senator from Illinois would not ask for a record vote on the present proposal. Why? We cannot adequately discuss the question in an hour or two of debate on the sort of bill before the Senate.

The vote can only be symbolic. It will not be a definitive vote at all. The subject is one which should be discussed for hours in the Senate, and not in connection with this type of a tax bill. Many of us come from oil producing States and have voted consistently for the principle involved in the amendment of the Senator from Illinois. There has been no adequate time for preparation for this debate. We cannot discuss intelligently an issue of such importance in an hour and a half or 2 hours. The question involves a vital part of the economy of our Nation. It involves a presidential pledge on which we have not received any information, guidance, direction or leadership.

In this short time Senators who come from oil producing States should not be faced with the contention that we should have a depletion allowance only for the domestic oil industry. This amendment does not do justice to those of us who represent independent producers and distributors, and those who have deep convictions on the issue, and who seek a more timely and equitable solution.

No experienced Senator believes that the amendment will be approved. Unless we contemplate extended debate, the issue should not have been brought before the Senate in connection with the pending bill at the present time. Only with extensive debate, with statistics pro and con brought forth, should we be required to vote on the merits. The able Senator from Illinois [Mr. DOUGLAS] has presented the issue hour after hour, day after day, and year after year, and we have been defeated time after time. This late hour, when we are not prepared, when we are all tired, is not the proper time to discuss this important amendment. No one has really discussed the issue as it should have been debated.

I had hoped that we would not have a vote on the merits of the issue.

I should like to make my position clear. I should like to have had the opportunity to present the original O'Mahoney amendment, which would provide a larger gross income than the senior Senator from Illinois requested. Also I should like to have had the opportunity to present the original O'Mahoney-Carroll amendment limiting the oil depletion allowance to the continental limits of the United States. I should like then to have debated the question because these amendments have never been fully debated in the Senate. I repeat I was hopeful that we would not have to vote on the merits of the amend-

ment at the present time. Therefore I shall vote "no" for the first time on the general issue.

The PRESIDING OFFICER. The question is on agreeing to the amendment of the Senator from Illinois. On this question the yeas and nays have been ordered, and the clerk will call the roll.

The legislative clerk proceeded to call the roll.

Mr. ERVIN (when his name was called). On this vote I have a pair with the senior Senator from Mississippi [Mr. EASTLAND]. If he were present and voting he would vote "nay." If I were at liberty to vote I would vote "yea." I therefore withhold my vote.

Mr. LONG of Missouri (when his name was called). On this vote I have a pair with the senior Senator from Tennessee [Mr. KEFAUVER]. If he were present and voting he would vote "yea." If I were at liberty to vote I would vote "nay." I withhold my vote.

Mr. WILLIAMS of Delaware (when his name was called). On this vote I have a pair with the Senator from Kentucky [Mr. MORTON]. If he were present and voting he would vote "nay." If I were at liberty to vote I would vote "yea." I withhold my vote.

Mr. WILLIAMS of New Jersey (when his name was called). On this vote I have a pair with the Senator from Minnesota [Mr. HUMPHREY]. If he were present and voting he would vote "yea." If I were at liberty to vote I would vote "nay." I withhold my vote.

Mr. COOPER (when his name was called). On this vote I have a pair with the senior Senator from New York [Mr. JAVITS]. If he were present and voting he would vote "yea." If I were at liberty to vote, I would vote "nay." I withhold my vote.

The rollcall was concluded.

Mr. MANSFIELD. I announce that the Senator from Virginia [Mr. BYRD], the Senator from New Mexico [Mr. CHAVEZ], the Senator from Mississippi [Mr. EASTLAND], the Senator from Alabama [Mr. HILL], the Senator from Minnesota [Mr. HUMPHREY], the Senator from Tennessee [Mr. KEFAUVER], the Senator from Washington [Mr. MAGNUSON], the Senator from Oregon [Mrs. NEUBERGER], the Senator from Georgia [Mr. RUSSELL], and the Senator from Florida [Mr. SMATHERS] are absent on official business.

I further announce that the Senator from New Mexico [Mr. ANDERSON], the Senator from Nevada [Mr. BIBLE], the Senator from Wyoming [Mr. HICKEY], and the Senator from Missouri [Mr. SYMINGTON] are necessarily absent.

I further announce that, if present and voting, the Senator from Nevada [Mr. BIBLE], the Senator from New Mexico [Mr. CHAVEZ], the Senator from Wyoming [Mr. HICKEY], the Senator from Alabama [Mr. HILL], and the Senator from Florida [Mr. SMATHERS] would each vote "nay."

On this vote, the Senator from Oregon [Mrs. NEUBERGER] is paired with the Senator from New Mexico [Mr. ANDERSON]. If present and voting, the Senator from Oregon would vote "yea," and the Senator from New Mexico would vote "nay."

Mr. KUCHEL. I announce that the Senator from Utah [Mr. BENNETT], the Senator from South Dakota [Mr. BOTTRUM], the Senator from Arizona [Mr. GOLDWATER], the Senator from Kentucky [Mr. MORTON], and the Senator from New Hampshire [Mr. MURPHY] are necessarily absent.

The Senator from New York [Mr. JAVITS], the Senator from Vermont [Mr. PROUTY], and the Senator from Wisconsin [Mr. WILEY] are detained on official business.

If present and voting, the Senator from South Dakota [Mr. BOTTRUM], the Senator from Arizona [Mr. GOLDWATER], and the Senator from New Hampshire [Mr. MURPHY] would each vote "nay."

The respective pairs of the Senator from New York [Mr. JAVITS] and that of the Senator from Kentucky [Mr. MORTON] have been previously announced.

On this vote, the Senator from Wisconsin [Mr. WILEY] is paired with the Senator from Utah [Mr. BENNETT]. If present and voting, the Senator from Wisconsin would vote "yea," and the Senator from Utah would vote "nay."

The result was announced—yeas 23, nays 50, as follows:

[No. 246 Leg.]

YEAS—23

Aiken	Jackson	Pastore
Case	Keating	Pell
Church	Lausche	Proxmire
Clark	Long, Hawaii	Scott
Dodd	McCarthy	Smith, Mass.
Douglas	McNamara	Smith, Maine
Gore	Morse	Young, Ohio
Hart	Muskie	

NAYS—50

Allott	Fong	Metcalf
Bartlett	Fulbright	Miller
Beall	Gruening	Monroney
Boggs	Hartke	Moss
Burdick	Hayden	Mundt
Bush	Hickenlooper	Pearson
Butler	Holland	Randolph
Byrd, W. Va.	Hruska	Robertson
Cannon	Johnston	Saltonstall
Capehart	Jordan, N.C.	Sparkman
Carlson	Jordan, Idaho	Stennis
Carroll	Kerr	Talmadge
Cotton	Kuchel	Thurmond
Curtis	Long, La.	Tower
Dirksen	Mansfield	Yarborough
Ellender	McClellan	Young, N. Dak.
Engle	McGee	

NOT VOTING—27

Anderson	Goldwater	Murphy
Bennett	Hickey	Neuberger
Bible	Hill	Prouty
Bottrum	Humphrey	Russell
Byrd, Va.	Javits	Smathers
Chavez	Kefauver	Symington
Cooper	Long, Mo.	Wiley
Eastland	Magnuson	Williams, N.J.
Ervin	Morton	Williams, Del.

So Mr. DOUGLAS' amendment was rejected.

Mr. MANSFIELD. Mr. President, I move that the Senate reconsider the vote by which the amendment was rejected.

Mr. DIRKSEN. I move to lay that motion on the table.

The motion to lay on the table was agreed to.

Mr. GORE. Mr. President, it is said of the hill people from whence I come that they are given to starting fights and never want to quit. I fear I am afflicted with the latter limitation; but surely after many days and at this hour it is time to bring this fight to a close.

I have five more amendments, each of which I believe is of considerable importance, although they are not major amendments. With the cooperation of the distinguished senior Senator from Oklahoma, I should like to handle them for the RECORD in pro forma fashion. I shall make the briefest sort of statement with respect to each amendment and the reason why I believe the provision which is sought to be amended is unwise. I trust the distinguished Senator from Oklahoma will be equally brief.

Before calling up my amendments, let me say that this has been a long and grueling fight on a very technical and complicated subject. I have offered several amendments. I have not won any of them. Generally in the press the group with which I have been associated is referred to as a "little band."

But, Mr. President, with respect to three of the amendments offered by the junior Senator from Tennessee, a majority of the Democratic Members of the Senate voted for the amendments. I take some consolation from that fact. I take some consolation, too, because as a result of the lengthy efforts which I have devoted to attempting to remove preferential tax treatment of income earned abroad, some provisions are in the bill which might not otherwise have been there.

I hope that one benefit especially, may flow from this fight. I hope the Kennedy administration has learned a lesson and that it will profit from that lesson, the lesson being that a constant string of compromises and accommodations with respect to one special interest after another can lead to no good end; and if such a procedure is repeated with the big tax bill expected next year or the year after, a fiasco will be the result.

Mr. President, with those brief remarks, I call up my amendment designated 8-27-62—E.

The PRESIDING OFFICER. The amendment will be stated.

The CHIEF CLERK. On page 180, beginning with line 23; it is proposed to strike out all through line 5 on page 181 and insert the following:

(1) an amount equal to the sum of the deficits in earnings and profits for prior taxable years beginning after December 31, 1962; exceeds.

Mr. GORE. Mr. President, this amendment would strike from the bill a committee amendment which gives the privilege of carrying forward certain losses from a date prior to the effective date of the bill. This confers a benefit retroactively. I feel certain the distinguished Senator from Oklahoma feels differently. That ends my statement.

Mr. KERR. Mr. President, I am opposed to the amendment of the Senator from Tennessee. The report of the committee fully justifies the inclusion of the language in the bill.

The PRESIDING OFFICER. The question is on agreeing to the amendment of the Senator from Tennessee.

The amendment was rejected.

Mr. GORE. Mr. President, I call up my amendment designated "8-27-62—C."

The PRESIDING OFFICER. The amendment will be stated.

The CHIEF CLERK. On page 187, line 5, it is proposed to strike out "30 percent" and insert "20 percent".

On page 187, line 10, strike out "70 percent" and insert "80 percent".

Mr. GORE. Mr. President, the committee bill raises the de minimis rule from 20 percent, as contained in the House bill, to 30 percent. I am unable to justify it.

Mr. KERR. Mr. President, the amendment should not be adopted. I hope it will be rejected.

The PRESIDING OFFICER. The question is on agreeing to the amendment of the Senator from Tennessee.

The amendment was rejected.

Mr. GORE. Mr. President, I call up my amendment designated "8-27-62—J."

The PRESIDING OFFICER. The amendment will be stated.

The CHIEF CLERK. On page 31, line 20, it is proposed to strike out "7 percent" and insert "14 percent."

On page 32, line 6, after "equal to" insert "two times."

On page 32, line 21, after "equal to" insert "two times."

Mr. GORE. Mr. President, as the bill came to the Finance Committee from the House, the investment credit constituted a direct and specific subsidy with no offset whatsoever. The Finance Committee, in an effort to remove some of the elements of subsidy from the provision, decided that the basis of the equipment and machinery involved should be reduced by a percentage equal to the amount of the tax credit.

In this connection, the committee report states that this adjustment is made because "your committee believes that there is no reason to allow the taxpayer depreciation with respect to the portion of the investment in effect paid for by the Government." This would indicate that the committee felt that it was removing the subsidy element from this proposition. Such is not the case.

If all elements of subsidy were to be removed, it would be necessary to reduce the basis by double the amount of the credit allowed. As the bill now stands, a tax credit is being equated with a deduction from income otherwise taxable. In the case of the larger corporations, where most of this tax credit will be received, since the tax rate is approximately 50 percent, any adjustment on the deduction side must be equal to twice the adjustment on the credit side if matters are to be equalized. As the bill now stands, the manufacturer recovers only \$93 in depreciation after having received a refund of \$7 from the Government on the purchase of a \$100 piece of equipment. But this \$7 refund is worth a deduction of \$14 and the manufacturer is getting, in effect, depreciation of 107 percent of the cost of his new equipment.

There is another rather cute thing about this basis adjustment and the effect of the bill's restrictions on the amount of credit which can be taken. There is in the bill a little noticed "heads I win, tails I cannot possibly lose" item which provides that if, due to the various

restrictions in the bill, all the credit is not finally taken, the amount left over will be used in the following year as a deduction.

I am unable to support this provision of the bill; and the amendment I offer would correct it.

Mr. KERR. Mr. President, the only effect of this amendment would be to eliminate the investment credit benefits.

This amendment was fought out in the committee, and the Senator lost there.

Now the Senator has offered the amendment on the floor. I hope the amendment will be defeated again.

Mr. GORE. Mr. President, I regret to ask the Senator from Oklahoma to repeat his statement; I could not hear it.

Mr. KERR. I said the effect of the amendment would be to eliminate from the bill the investment credit. The amendment would substitute for the investment credit accelerated depreciation. The fight on the amendment has been made many times in the committee, and the Senator has lost there. Now the amendment has been offered on the floor; and I hope it will be rejected.

Mr. GORE. I did not offer the amendment in the committee; perhaps I should have.

But if that is the only justification the Senator from Oklahoma can offer for opposing the amendment, I am ready for the vote on the amendment to be taken.

Mr. KERR. The Senator asked me to be brief, and asked me to comment on the amendments which I thought unwise, and I have done so.

The PRESIDING OFFICER. The question is on agreeing to the amendment of the Senator from Tennessee.

The amendment was rejected.

Mr. GORE. Mr. President, I call up my amendment identified as "8-27-62—K."

The PRESIDING OFFICER. The amendment will be stated.

The CHIEF CLERK. On page 29, in lines 4 and 5, it is proposed to restore the matter stricken through, and to strike out the matter printed in italic.

Mr. GORE. Mr. President, I think this amendment relates to a particularly unmeritorious provision of the bill. The bill allows lessors to shift the tax credit to the lessee. This will open up many possibilities for abuse. A lessee will be able greatly to improve his cash position in this way. This is somewhat like the situation when an automobile salesman allows such a high trade-in and such a low downpayment that the purchaser walks out with a new car, plus cash.

There is here another small gimmick which would be overlooked in a casual reading of the bill. The taxpayer who manufactures or constructs a facility and then leases it would be entitled to the credit based on his cost or other basis. If the credit is shifted to the lessee, however, the credit can be figured on the basis of fair market value. The lessor, of course, gets a higher rent. Here again is a fertile field for abuse. Who is going to determine what the fair market value

is for an IBM machine which never is sold, but only is leased?

The entire leasing provision ought to be stricken from the bill.

Mr. President, I hope that even at this late hour—I will not hope that the provision will be stricken out.

Mr. KERR. Mr. President, since the Senator from Tennessee does not hope the provision will be stricken out, I share his "no hope," and I ask that the amendment be rejected.

Mr. GORE. Mr. President, my hope for improvements in the bill has been dulled in the past week. But I have tried.

Mr. KERR. Mr. President, the language included is for the benefit of the lessor. Under the House version of the bill, which the amendment seeks to restore, the tax credit would be available to the lessor if the lessee were in the business of leasing.

Our provision is that it is to be available to the lessor, regardless of whether the lessee is in that business. The benefit to the lessor is the same under either language.

The PRESIDING OFFICER. The question is on agreeing to the amendment of the Senator from Tennessee.

The amendment was rejected.

Mr. GORE. Mr. President, I call up my amendment identified as "8-27-62—L".

The PRESIDING OFFICER. The amendment will be stated.

The CHIEF CLERK. On page 24, in line 12, beginning with "The", it is proposed to strike out all through line 21, and to insert the following:

The preceding sentence shall not apply to nonlodging commercial facilities which are available to persons not using the lodging facilities on the same basis as they are available to persons using the lodging facilities.

Mr. GORE. Mr. President, when President Kennedy first suggested the investment credit, I was favorably impressed with the suggestion. The purpose of the proposal at that time was to provide an incentive, to give a reward, to one who improved his production facilities over and beyond what had been planned, over and beyond the depreciation allowance, and to give a reward or credit for so doing. But somewhere in this contorted process of tax legislation, the entire purpose was subverted, and the investment credit was turned into nothing more than tax reduction for the particular types of industry which can take advantage of it. Even as recently as the date of the publication of the committee report, we find the statement:

The objective of the investment credit is to encourage modernization and expansion of the Nation's productive facilities and thereby improve the economic potential of the country, with a resultant increase in job opportunities and betterment of our competitive position in the world economy.

I wonder how it is going to improve our competitive position in the world economy or how it is going to improve our industrial production facilities to give the investment credit to motels and hotels. The inclusion of equipment for transient motels and hotels is, in my

opinion, wholly without justification; there is no connection whatsoever with exports, and only a very remote connection with the betterment of the domestic economy.

I ask that this amendment be adopted.

Mr. KERR. Mr. President, the bill does not give the investment credit to a hotel or a motel, but gives it to the facilities and equipment used to furnish them.

Mr. GORE. I said equipment for motels and hotels.

Mr. KERR. I heard the Senator from Tennessee.

The facilities and equipment of a commercial motel or a commercial hotel are just like the facilities in a commercial factory or those in any other kind of a commercial industrial establishment or business. The building itself is not eligible in either event. The facilities whereby the building is utilized in the trade or business of the occupant are eligible for the credit; and the same is true with reference to the commercial business of furnishing facilities and equipment in a motel or a hotel.

Mr. GORE. Does the Senator say that improves our production facilities and helps our position in world trade?

The PRESIDING OFFICER. The question is on agreeing to the amendment of the Senator from Tennessee.

The amendment was rejected.

Mr. McCARTHY. Mr. President, I intend to offer an amendment which relates to the section of the bill which deals with foreign trusts. I think it will be in order to send the amendment to the desk and have it read; and then we can discuss possible modifications.

The PRESIDING OFFICER. The amendment of the Senator from Minnesota will be stated.

Mr. McCARTHY. Mr. President, the purpose of the amendment is to ease the adjustments which will be called for on the part of some of those who hold interest in foreign trusts. I am hopeful that some more time will be allowed—

The PRESIDING OFFICER. Does the Senator from Minnesota wish to have his amendment read?

Mr. McCARTHY. Yes.

The PRESIDING OFFICER. Very well; the amendment will be read.

The CHIEF CLERK. On page 90, at the end of line 17, after the word "made," it is proposed to add "more than 12 months."

The PRESIDING OFFICER. The Senator from Minnesota is recognized.

Mr. McCARTHY. Mr. President, the effect of the amendment would be to allow foreign trusts approximately 12 months from the date of enactment of this act to make whatever adjustments would be necessary. In my opinion, this is not an unreasonable time, since, so far as I can determine, those who established trusts of this kind did so in good faith and under existing law. I think quite suddenly and without adequate warning to have the law changed could be in many cases unfair. I would suggest that perhaps allowing them a year to change their plans and make the necessary adjustments and liquidation, or whatever may be needed, would be a reasonable proposition.

Mr. KERR. Mr. President, I would be agreeable—and I have talked this matter over with the Treasury—to accepting the Senator's amendment if he would make the end of the grace period December 31, 1962.

Under the bill, the termination of the tax haven privilege with reference to all direct income operations is as of that date, and I see no reason why a tax haven for trust fund income should be treated any differently.

If the Senator wanted to accept the suggestion on the same basis, which would be to insert the language "after December 31, 1962" instead of his language, which is 1 year from the date, or 6 months from the date, I would recommend the adoption of the amendment. Otherwise I would have to go to some extent to show why the amendment otherwise would be unjustified.

Mr. McCARTHY. I thank the Senator from Oklahoma. I have grave doubt as to whether a termination date of December 31, 1962, would be particularly helpful, but I am satisfied that, under the circumstances which exist here, we are not likely to be able to discuss a technical amendment at any great length. I am sorry it was not discussed in the committee.

So, under the circumstances, I am glad to accept the suggestion expressed by the Senator from Oklahoma, and express the hope that it may be helpful to those affected by the tax provisions in the bill.

Mr. KERR. It gives them 4 months, or nearly so. I believe it is adequate.

The PRESIDING OFFICER. The question is on agreeing to the amendment of the Senator from Minnesota, as modified by the amendment of the Senator from Oklahoma.

The amendment, as amended, was agreed to.

Mr. McCARTHY. Mr. President, I call up my amendment identified as "8-28-62—H" and ask to have it stated.

The PRESIDING OFFICER. The amendment offered by the Senator from Minnesota will be stated.

The legislative clerk proceeded to read the amendment.

Mr. McCARTHY. Mr. President, I ask unanimous consent that further reading of the amendment be dispensed with and that the amendment be printed in the RECORD.

The PRESIDING OFFICER. Without objection, it is so ordered.

The amendment offered by Mr. McCARTHY is, as follows:

On page 391, between lines 21 and 22, insert the following new section:

"SEC. 27. FOREIGN SUBSIDIARIES MANUFACTURING PRODUCTS ABROAD FOR SALE IN THE UNITED STATES.

"(a) Subpart B of part II of subchapter N of chapter 1 of the Internal Revenue Code of 1954 (relating to foreign corporations) is amended by adding at the end thereof the following new section:

"SEC. 885. CERTAIN FOREIGN CORPORATIONS PRODUCING PRODUCTS FOR SALE IN THE UNITED STATES.

"(a) GENERAL RULE.—In the case of any foreign corporation to which this section applies for the taxable year—

"(1) for purposes of section 882(a), such foreign corporation shall be deemed to be

engaged in trade or business within the United States, and

"(2) for purposes of this subtitle, the gross income of such corporation from sources within the United States shall be deemed to be not less than the gross income which it derives for such taxable year from the sale of competitive articles which are sold by it for ultimate use, consumption, or disposition in the United States.

"(b) CORPORATIONS TO WHICH SECTION APPLIES.—This section shall apply to a foreign corporation for the taxable year if—

"(1) at any time during such taxable year, one or more domestic corporations own, directly or through one or more other corporations, 10 percent or more of the outstanding stock of such corporation, and

"(2) for such taxable year, such foreign corporation derives 10 percent or more of its gross income from the sale of competitive articles which are sold by it for ultimate use, consumption, or disposition in the United States.

"(c) COMPETITIVE ARTICLE DEFINED.—For purposes of this section, the term 'competitive article' means any article mined, processed, or manufactured outside the United States for a foreign corporation which is the same as or similar to any article mined, processed, or manufactured in the United States (or formerly mined, processed, or manufactured in the United States) by—

"(1) any domestic corporation which, with respect to such foreign corporation, is described in subsection (b) (1); or

"(2) any subsidiary of a domestic corporation described in paragraph (1) of this subsection."

"(d) The table of sections for such subpart B is amended by adding at the end thereof the following:

"Sec. 885. Certain foreign corporations producing products for sale in the United States."

"(e) The amendments made by this section shall apply to taxable years beginning after December 31, 1962."

On page 391, line 22, strike out "27" and insert in lieu thereof "28".

Mr. McCARTHY. Mr. President, this amendment relates to the section of the bill which deals with taxation of foreign income.

In my opinion, as the bill now stands, the efforts to tax that income fall somewhat short in one particular—in the case where a domestic corporation buys abroad from its foreign subsidiary for its own use in the United States, the subsidiary pays no tax to the United States on the profits of the foreign subsidiary. The parent corporation is taxed in the United States on the profits from its domestic operations, but any tax on sale of the commodity, such as iron ore, abroad is lost to the United States. At least, the subsidiary would be subject only to the taxes of its host country.

H.R. 10650, as it stands, would affect that transaction only, as I see it, where intermediaries might be used, namely, if a Canadian subsidiary sold to a Panamanian subsidiary and the latter resold to the United States. The profits of the Panamanian subsidiary would probably be considered as tax-haven profits.

This amendment seeks to stop the loss of tax dollars to the United States from the type of transaction described by extending the definition of section 882 foreign corporations to include foreign corporations 10 percent or more of whose stock is owned by one or more U.S. corporations which derive 10 percent or

more of their gross income "from the sale of competitive articles * * * for ultimate use, consumption, or disposition in the United States"—that is, articles which are in competition with articles used in the United States.

The amendment aims to tax at regular U.S. corporation rates the profits from a transaction overseas between that subsidiary and the U.S. parent corporation.

It is estimated that an amount equal to the taxes owed would be repatriated to the parent corporation. In any event, the tax would be paid by the parent corporations.

This amendment raises the same problems and has the same limitations as those existing under and connected with section 12 of H.R. 10650, but I believe is consistent with the purposes indicated by the Senate in adopting the committee amendments up to this time. It would serve as a clarification and, in a sense, put these profits in the open, where they could be taxed by the U.S. Government. In any case, it would eliminate unfair competition in iron ore, and I assume copper, and other raw materials, as well as finished products, but particularly semifinished products which are brought back by parent corporations and are in competition with similar products produced in the United States.

Mr. HUMPHREY. Mr. President, will the Senator yield?

Mr. McCARTHY. I yield.

Mr. HUMPHREY. Many Senators have been concerned about the foreign subsidiary and parent corporation arrangement as it affects American employment and domestic industry. The amendment offered by my colleague is one that gets to the root of the trouble. We have this situation in our own State, and I assume it may be true in other States. The extractive industries, such as a mining company, may go into a country that offers unusual tax incentives. There is an incentive by the Canadian Government of 3 years with no taxes. Such a corporation sets up a subsidiary in Canada, ships ore into the United States, into the American domestic market, for the American domestic blast furnaces for the American steel industry, and displaces American industry, American miners, and American workers.

The Senator's amendment simply provides that if the purpose of a foreign subsidiary is not that of developing an international market for a commodity produced under an American name by an American corporation, but if the purpose is to displace American products in the American market with foreign commodities or foreign products owned or controlled or manufactured or extracted by an American company, and if such company's interest is over 10 percent of the total volume of the business, it shall be taxed at American corporate rates.

This is the amendment that really gets at some of the problems some Representatives and Senators have been concerned about, namely, taking jobs from American workers and displacing American workers and American production.

The same thing happened with respect to the radio industry, wherein radio

parts that are manufactured in another country are brought into this country under the terms of the American corporation's foreign subsidiary, and are placed on the American market after they are packaged into a unit called a radio, and sold on the American market, with little or no American labor or plant involved.

Mr. MORSE. Mr. President, will the Senator yield?

Mr. HUMPHREY. I yield.

Mr. MORSE. Would not the Senator say that was also true of music records and true of movies?

Mr. HUMPHREY. The Senator is correct.

Mr. MORSE. The Senator was present when we had a discussion of that problem this afternoon, when we tried to correct the wrong being done to those industries. We did not seem to get anywhere. The fact that we did not would not prevent me from supporting the amendment, but I suspect the Senator will have the same "hatchet job" done on him that we received earlier this afternoon.

Mr. HUMPHREY. I was hoping that the still hours of the night might somehow subdue passions, that reason might move to the forefront, and that the Senate of the United States might vote for the amendment offered by my distinguished colleague. I think the Senate may do so. Therefore, I yield the floor.

Mr. MORSE. The Senator is the greatest optimist I have ever seen.

Mr. KERR. Mr. President, will the junior Senator from Minnesota yield for a question?

Mr. McCARTHY. I yield to the Senator.

Mr. KERR. Would the effect of the proposal, in the event of the occurrence of the conditions set forth to make it applicable, be to tax the entire income of the foreign corporation?

Mr. McCARTHY. It would relate only to the portion derived from the sale of competitive articles for use in the United States.

Mr. KERR. Mr. President, I am entirely in sympathy with the purpose of the amendment. I seriously doubt its efficacy now. If the intent of the author is to make only that part of the business of the foreign corporation which consists of its shipping material into the United States applicable—

Mr. McCARTHY. That is the intention.

Mr. KERR. Then I would be willing to take it to conference, with the statement to the distinguished Senator that if counsel should advise us in conference it is unconstitutional I am sure it would be taken out. If the effect of it would be to "trigger" the applicability of the section to the entire income of the foreign corporation, when only 10 percent of it was owned in the United States and only 10 percent of its business was done in the United States, I think it should be amended to make it clear that the Senator intends the amendment to apply only to the percentage owned and the business done in the United States.

Mr. McCARTHY. It was my intention to have it apply only to that profit

or gain as a result of business which was done with the parent company in the United States.

Mr. KERR. For goods or merchandise or materials shipped into the United States?

Mr. McCARTHY. Shipped into the United States.

Mr. KERR. And to the extent to which ownership in the foreign corporation is vested in citizens of the United States?

Mr. McCARTHY. The Senator is correct.

Mr. KERR. With that understanding, I have no objection to taking the amendment to conference.

The PRESIDING OFFICER. The question is on agreeing to the amendment offered by the Senator from Minnesota.

The amendment was agreed to.

TAX STATUS OF COOPERATIVES

Mr. HUMPHREY. Mr. President, I should like to ask my colleague a question. Does the bill before us in any way deal with the question as to whether income to a cooperative is taxable to the cooperative where that income arises from its doing business with the Government? Am I correct that under the bill, as under existing law, that income is not taxable?

Mr. McCARTHY. The bill specifically provides that such income is not taxable to the cooperative if it is in turn distributed in accordance with the statutory requirements. This is also made clear in the general explanation of the pertinent provisions contained in the Finance Committee's general report—subparagraph 4 of heading C of section XVII.

Mr. HUMPHREY. I thank my colleague.

Mr. McCARTHY. I have one more question to ask the Senator from Oklahoma with regard to a section which is not in the bill. It pertains to the tax status of cooperatives.

A question has been raised concerning whether cooperatives are doing business "with" or "for" the Government. There are conflicting opinions and conflicting judgments with respect to this. My own opinion is that the two words should be used interchangeably, without distinction.

This does not refer to language in the particular bill before the Senate, I say to the Senator from Oklahoma, but it relates to an existing practice under tax laws, as to which there is some confusion and contradiction. I think it might be a good time to try to clarify the RECORD, that business done either with or for the Government, on the part of cooperatives, should be treated in the same way under the tax laws. Does the Senator sustain that opinion on my part?

Mr. KERR. Mr. President, it is my impression that the bill would not in any way change the existing statute in that regard.

Mr. McCARTHY. The Senator is correct.

Mr. KERR. The statute specifically permits cooperatives to do business with the Government without endangering

their tax-exempt status. That is the understanding of the Senator from Oklahoma.

Mr. McCARTHY. Yes. The question does not relate to anything in the bill.

Mr. KERR. Nothing in the bill would change that tax-exempt status.

Mr. McCARTHY. I am not concerned about what is in the bill in that regard. There have been some conflicting interpretations by the Internal Revenue Service with respect to the two words. In my judgment the history, experience, and application of the language of the existing code is such that business which may be described as business done "with" or "for" the Government is the same.

Mr. KERR. Mr. President, I would not want to speak authoritatively with reference to existing law. I have a distinct opinion about it. I have a positive conviction that nothing in the bill would lose to a cooperative any tax-exempt status it now has under existing law.

Mr. McCARTHY. Mr. President, I ask unanimous consent that a statement relating to the tax status of farmers' cooperatives may be printed in the RECORD at this point.

There being no objection, the statement was ordered to be printed in the RECORD, as follows:

STATEMENT RELATING TO THE TAX STATUS OF FARMERS' COOPERATIVES

The language, "Business done for the United States," first appeared in the Revenue Act of 1934. At that time, cooperatives only acted as occasional agents for the Government and the present modern system of agricultural price stabilization through which grain is purchased and sold by the CCC had not yet evolved. During the course of the consideration of the 1934 act, Senator Norris offered an amendment on the floor of the Senate which he said was identical to one he had earlier introduced in 1932. The Senate agreed to the amendment which read as follows:

"Neither shall any such association be denied exemption because it does not keep ledger accounts with nonmembers of the business it transacts with such nonmembers, but it shall only be required to keep such records of its business with nonmembers as will show the actual business done with such nonmembers; and provided further, that the profits, if any, derived from its business with nonmembers in any fiscal year of the association shall be allowed to remain in the business of the association, subject to the right of such nonmember to use his share upon a patronage basis to qualify as a member of the association." (78 CONGRESSIONAL RECORD, p. 6488, 73d Cong. 2d sess., Apr. 12, 1934, Senate print. H.R. 10236, May 9, 1932, pp. 75-76, 72d Cong., 1st sess.)

The amendment had a further proviso which appeared in the printed version of the Senate bill and read as follows: "Provided further, That business done for the Federal Government or any of its agencies shall not be considered as nonmember business within the meaning of this Act." (Senate print, H.R. 7835, 73d Cong., 2d sess., 1934.)

In view of the fact that the House version of the bill did not contain any portion of the Norris amendment, the issue was among those resolved in conference. The result was the language of the statute which is operative today. Representative Hill in explaining the intent of the conference committee in adopting the provision, made the following statement:

"This amendment provided that farmers' cooperative marketing or purchasing associations (1) need not keep ledger accounts of transactions with nonmembers and (2) that the members may purchase memberships with profit from nonmember business and (3) business done with the Federal Government or its agencies shall not be considered nonmember business. The Senate withdrew the first two points upon advice from the Treasury that they were already covered by existing law. On the third point, we got the Senate conferees to agree to put in a provision to the effect that business done with the United States or any of its agencies shall be disregarded in determining whether the association is entitled to exemption from income taxes." (78 CONGRESSIONAL RECORD, p. 7831, 73rd Cong., 2d sess., May 1, 1934.)

Thus, in the only written legislative history of section 521(b)(5) of the 1954 code and its predecessors, it is clear that the Congress provided that business done with the Federal Government or its agencies shall not be considered nonmember business and, therefore, would not threaten the tax-exempt status of cooperatives.

The Internal Revenue Service also recognizes that an exempt cooperative may do business with the United States. Section 522 of the current code exempts from taxable income amounts allocated to patrons that are not derived from "patronage." This section applies only where an organization has an exempt status under section 521. The regulations adopted by the Internal Revenue Service under the 1954 code state in section 1.522-2(d), that "business done with the United States shall constitute income not derived from patronage." It is, therefore, clear that the regulations assume that a cooperative that does business with the U.S. Government can have a tax exemption status under section 521.

Regulations issued by the Internal Revenue Service under prior codes contained similar provisions. (See Regulations 118, sec. 39.101(12)-1.) This regulation was acknowledged and followed by the Internal Revenue Service in a Revenue ruling in 1955 given with respect to the allocation of cooperative income resulting from the handling and storage of Commodity Credit Corporation grain (Revenue ruling 55-591 Cumulative Bulletin 1955-2; p. 553). On page 554 of the bulletin there appears the following statement:

"Section 39.101(12)-1(c) of Regulations 118, provides that business done with the United States or any of its agencies shall be disregarded in determining the right to exemption under section 101(12) (now 521(b)(5)) of the code."

Furthermore, I note in a copy of the President's tax message to the Congress, dated May 3, 1961, submitted by the Secretary of the Treasury, Douglas Dillon, at hearings conducted by the Committee on Ways and Means of the House of Representatives, that there is included an exhibit VII on cooperatives. In that exhibit, there is a discussion of farmers' marketing and purchasing cooperatives described in section 521 of the code. The discussion in the exhibit states (p. 271, U.S. Government Printing Office) that "income derived from business with the United States and distributed or allocated to its patrons on a patronage basis" is an allowable deduction from taxable income.

Under these circumstances it is clear that farmers' cooperatives that do business with the United States or any of its agencies do not jeopardize their otherwise tax-exempt status under section 521 of the Internal Revenue Code of 1954.

UNREASONABLE ACCUMULATION OF PROFITS—AMENDMENTS OF SENATOR McCARTHY

Mr. McCARTHY. Mr. President, I ask unanimous consent that a statement of

mine with reference to the amendment which I offered on last Friday may be printed in the RECORD.

There being no objection, the statement was ordered to be printed in the RECORD, as follows:

STATEMENT BY SENATOR MCCARTHY

I wish to refer to the statement read into the RECORD last Friday by Mr. MANSFIELD. I do not know the source of the memorandum, but it contains a great many errors which I wish to bring to the attention of the Senate. I think the Senate is entitled to the sources.

First, the memorandum states that it would cut between \$80 million and \$100 million. The staff estimate as to the effect of all of section 12 is \$50 million. This is the entire section 12 without my amendment. Then, Mr. MANSFIELD states that he was informed (I am at a loss to know where this information came from) that my amendment might reduce the revenue to \$2 million. This seems clearly erroneous. The staff of the Joint Committee on Internal Revenue Taxation estimates the revenue reasonably expected to result from my amendment would be in the neighborhood of \$30 million.

ONE NEEDS HIS OWN TRAINED STATISTICIAN

We have in the present law a special tax on domestic corporations who accumulate earnings beyond the reasonable needs of the business. If my amendment is effective, it would encourage foreign subsidiary corporations owned by Americans to distribute their earnings to their shareholders and in this way would add to the revenue. Judging from experience with existing law, I believe my amendment would go a long way toward forcing foreign corporations owned by Americans to distribute their earnings rather than accumulate them beyond the reasonable needs of the business for purposes of avoiding the American tax.

The memorandum declared my amendment would injure our balance of payments. Testimony before the Finance Committee and also in the report of the special committee of businessmen, appointed by the President, argued that the proposals of the pending bill will hurt our balance of payments.

John L. Connolly, general counsel of the Minnesota Mining & Manufacturing Co., pointed out in his testimony: "First of all, a substantial part of the investment is normally spent promptly for capital goods and services in the United States with a consequent return of dollars. Secondly, once the foreign activity is established, it usually generates additional exports in the form of materials, parts, services, and even finished goods. These exports in all likelihood would not occur if the investment had not been made. Thus, the short-run improvement that could be expected in our balance of payments from the proposed legislation is more apparent than real."

Pharmaceutical Manufacturers Association, Kenneth C. Royall: "A survey of 10 of the members of the association, which included several of the larger members, over the years 1956 through 1960 shows that the total inflow from these subsidiaries to the United States was \$618,600,000 and the total outflow was only \$78,500,000. Total inflow exceeded total outflow by \$540,100,000, or by a ratio of 7.9 to 1. Official Government statistics show that over the same period the average annual exports of all medicinal and pharmaceutical products were \$273 million and the average annual imports were only \$16 million. These amounts of inflow will be no longer available if this legislation is enacted, because there will be no foreign market."

Joy Manufacturing Co., J. D. A. Morrow: "[Joy's figures show] total 11-year parent company investment and advances to for-

eign subsidiaries of about \$7,400,000 and dollar expenses of operating abroad of \$11 million, a total dollar outflow of, roughly, \$18,400,000. Please note that these outlays brought \$170 million of exports in those 11 years, 60 percent of which went to or through our manufacturing subsidiaries abroad. In addition, payments of \$7 to \$8 million of engineering fees, royalties, dividends, and interest make a total net favorable balance of payments of \$159 million, and the U.S. Treasury collected more than \$16 million of income tax from these operations. Is that showing unfavorable to the U.S. balance of payments? Gentlemen, hundreds of other American foreign subsidiaries would present similar results if you had their figures."

Corn Products Co., Warren S. Adams: "We are a food company primarily. This means we operate on a low margin of profit. There is in Europe tremendous competition in the food industry. We have to meet this competition and we have to invest money in Europe in the process. For us the Treasury's proposals mean not that we shall no longer invest money in Europe, but that a significant part of the investments we will have to make to protect our present investment there will be more costly than heretofore, and, thus, return less profit for remission to the United States."

Sprague International, Ltd., William M. Adams: "As a business grows, more working capital is needed. At present, this is supplied from foreign sources in local currency that has been earned abroad. Therefore, if this bill passes, the parent company will have to supply this capital from U.S. dollars instead of foreign currency and, furthermore, will have to earn twice as many dollars as would be the case using local funds. How this is going to help the balance of payments is beyond me."

International Flavors & Fragrances, Inc., Eugene P. Grisanti: "If this bill is passed in its present form, it would seem far more likely that such funds, in the majority of cases, would be reinvested, and not necessarily in new business in the less developed countries where so many uncertain risks are faced, but in the expanding businesses where the existing subsidies are already situated. Funds which may well have been kept idle until the time was ripe to make a decision whether to repatriate them as dividends, or to invest in plant expansion, will be forced into plant expansion instead before the end of the tax year to escape the tax."

Pfizer International, John J. Powers, Jr.: "Treasury's ultimate position is that while direct investment abroad may, in the long run, have a beneficial effect on the balance of payments, it nevertheless has a short-term deleterious effect. This is simply a recognition of the obvious fact that a dollar invested today will not be returned until some time later. Thus, it follows that if the dollar were not invested, then during the period it would have taken to return it, the balance of payments would be favorably affected. But later, when the return from dividends, interest, exports, royalties, fees, etc., would have exceeded the prior capital outflow, the balance of payments would be permanently hurt, and to a far greater extent than it had been temporarily helped. The farmer who is short of money can cut down on his expenses by not planting seed in the spring. But where will he stand at harvesttime?"

"Pfizer International has really been in operation only since 1951. In the period 1951 through 1961, Pfizer operations have resulted in a net inflow to the United States of about \$250 million. This is despite the fact that it is only in very recent years that we have begun to pay substantial dividends to the parent company. Prior to that time, nearly all profits earned abroad were reinvested. In the face of such a circumstance

we nevertheless achieved this highly favorable balance because we exported almost \$200 million of U.S.-made goods to Pfizer foreign subsidiaries and because we brought home some \$50 million additional in dividends, royalties, fees, etc. Now that our investment has begun to mature and large dividends are being brought home, we are returning dollars at an annual rate of \$45 million. The parent company has not made any direct dollar investments abroad in many years and it is the policy of our company that its international organization provide its own financing."

Abbott Laboratories, George R. Cain: "For the 5-year period 1956-60, Abbott's exports from the United States exceeded its imports by \$50 million. Abbott also received from abroad loan repayments, dividends, and miscellaneous income in the amount of \$9.3 million—making a total inflow into this country of \$59.3 million."

"The total outflow of dollars from this country by Abbott, during the same 5-year period, in foreign investments and loans was only \$2.2 million. This gives our country a net favorable balance of \$57.1 million."

"Proponents of the foreign income provisions apparently would not understand how a company can expand its foreign operations rapidly with so little outflow of U.S. capital. The answer is simple and well known to all who have had international business experience. Foreign plants can be and are financed very heavily through the use of locally borrowed money in addition to earnings retained overseas. Thus, we increase our base upon which greater future earnings are built. These earnings redound to the benefit of the U.S. Treasury as well as our own shareholders. This is accomplished without a heavy immediate or long-term drain on U.S. capital."

The Machinery & Allied Products Institute: "The establishment of a permanent operation overseas serves to facilitate contacts with foreign customers and by giving the company greater local identification helps to penetrate markets which could not otherwise be penetrated. One company, with which we are familiar, prior to 1959 was unable to penetrate the German market to any significant degree. However, as a result of establishing an operation in that country it now finds that its German customers are not only willing to purchase from the German-based company unit, but, because of the greater local identification established by the U.S. company as a result of its German subsidiary, it now exports in substantial volume to the German market products which it is manufacturing in the United States."

Caterpillar Tractor Co., E. W. Kuhlman: "I wish to point out that none of our products are completely manufactured abroad; many of the components such as engines, transmissions, etc., are produced in our U.S. factories and exported to our foreign plants. If we did not manufacture the product abroad, the sale would not be made at all by us but would be made by a foreign competitor who would use no components manufactured in the United States. The significance of this factor is emphasized when it is noted that (1) our exports to Great Britain in 1960 were over four times those of 1950, the year before our subsidiary began operation; (2) our exports to Australia in 1960 were more than double those of 1955 when the subsidiary was formed; (3) our exports to Brazil in 1960 were more than five times those of 1956 when manufacturing began in Brazil."

Clark Equipment Co., Walter E. Schirmer: "Exports from Clark's U.S. plants in 1955 totaled \$5,500,000, consisting solely of machines and parts to distributors. By 1961 such sales had increased to \$12,500,000 and in addition component sales to manufacturing affiliates rose to \$10,500,000, for a total of

\$23 million total exports from U.S. plants, excluding Canada. While total sales of Clark products overseas in 1955 therefore was only \$5,500,000, in 1961 this figure has risen to \$88 million including \$65 million sales of the Clark manufacturing affiliates.

"Clark's program of investment overseas, far from being detrimental to our U.S. investment program, has produced profits for the parent company both in the sale of components, never sold overseas prior to this program, plus finished machines and service parts. This has provided increased funds in the parent company available for investment in facilities and working capital. During the years 1955-56 the parent company has invested in U.S. facilities and working capital \$40 million, and in that same period has invested in Clark International \$1 million.

"Thus, it is obvious that the Clark foreign investment program has not in any way interfered with our domestic program, nor has it to any material extent affected our balance of payments, since the earnings of the parent company on its overseas exports has exceeded by far the original investment in International."

International Economic Policy Association: "A large part of the world is not available as a market for increased U.S. exports for cash. The Iron Curtain countries are a limited potential market for trade expansion for the near-term future; the underdeveloped countries do not have the resources to buy for cash—they are candidates for gifts and grants and so-called long range, 50-year low or no-interest loans. Therefore, our chance of selling more for cash is restricted pretty much to industrialized Western European countries and Japan.

"The question is: Can these exports be increased, not on a reciprocal, but a one-way unilateral basis by between \$3 and \$4 billion? With regard to Common Market countries, this much expansion in exports would require an almost 100-percent increase over 1961 products of \$3.6 billion. In total the immediate prospects do not come up to our needs.

"It is not, therefore, enough merely to exhort American industry to export more, because it is not likely that the total solution of the balance-of-payments problem will lie in this field in the foreseeable future, as long as we have to maintain our Military Establishment and the scale of foreign aid expenditures at levels comparable to the present. Therefore, the United States must think in terms of a long-range solution to this problem by expanding U.S. earning power abroad in ways other than exports; namely, the sale of services, and the making of investments on which growing amounts of earnings may accrue and, in the normal course of business activity, be repatriated to the United States. The encouragement of private investments abroad in hard, convertible currency countries must become one of the major objectives of the administration, with as much emphasis as given to the encouragement of exports."

It was charged in the memorandum that my amendment would encourage the flight of American capital. This is imaginative writing. My amendment would have taxed earnings of controlled foreign corporations accumulated beyond the reasonable needs of the business. Amounts distributed by such corporations to their American shareholders would never have been touched by my amendment. Foreign subsidiaries which were returning a reasonable portion of their earnings to the shareholders in the form of dividends would have no reason to fear my amendment, and there was nothing in my amendment which would have encouraged American capital to go abroad. Quite the contrary, my amendment would have encouraged controlled foreign corporations to send their profits home.

This would obviously have aided our balance of payments. Now this involves another unproved and unprovable statement made in the memorandum, that is, that my amendment would be more likely to injure than to aid our balance of payments. The philosophy of the committee bill is that foreign investment should be discouraged because of its adverse effect on the balance of payments. Applying this philosophy to my amendment, the majority leader concludes that because my amendment does not discourage foreign investment it hurts our balance of payments. The adverse effects of foreign investments, if there are any, result from a time lag of 10 to 15 years between the export of capital and the return on the investment. If we look at the record of investment outflow and dividend and interest inflow for the last 12 years of the postwar period, we find that foreign investment has not adversely affected the balance of payments. Except for the year 1957, the inflow to the United States of dividends and interest on U.S. investments abroad has exceeded the outflow from direct investments in every year since 1950. Over the 12-year period, 1950-61, inclusive, the net inflow to the United States—the excess over what went out by way of investment—has been \$8,552 million. This is shown in the attached table prepared from data of the Department of Commerce:

SCHEDULE A

Dollar inflow and outflow to direct investment—Companies abroad, 1950-61

[In millions of dollars]

Year	Direct investment outflow	Dividends and interest inflow	Net inflow
1950.....	621	1,294	673
1951.....	528	1,492	964
1952.....	850	1,419	569
1953.....	751	1,442	721
1954.....	664	1,725	1,061
1955.....	779	1,912	1,133
1956.....	1,859	2,120	261
1957.....	2,482	2,249	-233
1958.....	1,181	2,140	959
1959.....	1,372	2,206	834
1960.....	1,694	2,348	654
1961.....	1,681	2,637	956
Total.....	14,432	22,984	8,552

NOTES

1. Data from Department of Commerce. See p. 3.
2. Covers all areas and all activities, branches, and subsidiaries.
3. Unremitted branch earnings are included in both "Outflow" and "Inflow" columns.

Cutting back on growth abroad would result in my judgment not in greater U.S. production but in lower, curtailed U.S. production as a result of lower levels of exports to support the overseas subsidiary operations. It will not improve the balance of payments. My amendment, on the other hand, by not encouraging foreign investments for legitimate purposes would lead only to increased U.S. production to support the overseas subsidiary operations and this increased production would favorably help our balance of payments.

The memorandum also states that the only tax haven income which would be covered by my amendment is income from insurance of U.S. risks. When asked to define a tax haven, Secretary Dillon told the Finance Committee that it was any country where tax rates were lower than U.S. tax rates and pointed to such countries as Liechtenstein and Switzerland. However, businessmen have made it plain that taxes is only one reason a particular country is chosen as the proper place to incorporate a foreign subsidiary. Switzerland, for example, is a financial and banking center. It has a large pool of skilled workers and language is no barrier. It has a stable gov-

ernment and stable currency. Its low tax rates apply primarily in the case of income derived from outside of Switzerland. American business which creates a Swiss subsidiary to handle its European affairs by virtue of their Swiss subsidiary pay a lower foreign tax than if a separate subsidiary was established in each European nation in which the corporation conducted business. The lower Swiss tax in such cases makes it possible for the subsidiary to send more earnings back to the United States because the foreign taxes have been reduced. Let me make that point clear. The U.S. tax is not avoided in any case.

Only foreign taxes are reduced by means of Swiss subsidiaries. We should not attempt to call Switzerland a tax haven country merely because it taxes earnings from business done in other European nations at a lower rate. If corporations take advantage of the low Swiss tax and accumulate unreasonably large amounts of earnings in a Swiss subsidiary, my amendment would have taxed those earnings just as effectively as the committee amendment. My amendment would not arbitrarily tax income of a Swiss subsidiary which was returning to its U.S. parent a substantial part of its earnings. The committee amendment might impose an arbitrary tax in such a case.

Another difficulty about such a concept is that it would encourage foreign countries with low rates of tax to raise their rates to equal ours.

The Treasury amendment sponsored by Senator KERR helps only well-established corporations and not the new or growing ones. It is much like the undistributed profits tax which was proposed in 1936 and repealed in 1941. Senator BYRD, at that time, opposed the proposal because it operated to give the old-established firms an unfair competitive advantage over the new and growing company because the new company could not distribute its earnings and stay in business, and had no surplus out of which to pay dividends. He stated in connection with the adoption of the conference report on the 1936 act:

"In other words, what this bill does is to entrench the great monopolies of the country, and protect them from competition. I make that statement without fear of successful contradiction, because the bill would leave the surpluses as they now are, and prevent any other company from establishing a surplus except by the sale of stock."

The committee amendments will encourage monopolies by giving relief only to large well-established businesses abroad and denying relief to the new struggling and growing companies. It will limit our investments abroad to old and established firms and freeze out new and growing ones.

The memorandum says that my amendment did not tax holding companies or service income. This is clearly erroneous. I do not see how he could make such a statement since my amendment would apply to both holding company income and service income which is not used for legitimate business operations.

As a matter of fact, my amendment on page 7, at line 21, creates a specific presumption that property held by a holding or investment company is accumulated beyond the reasonable needs of the business. Moreover, my amendment on page 4, beginning at line 2, makes it plain that service income from any source is included within the definition of earnings improperly accumulated.

The memorandum also stated that my amendment would encourage the retention of capital abroad to provide jobs for foreign workers. This is unproved. It was to the end the weight of testimony at the Finance Committee hearings that foreign investments actually increased American employ-

ment in order to provide needed equipment, services, and know-how to support foreign operations. Excerpts from statements of witnesses appearing before the Finance Committee who commented on this unemployment issue, follow:

Abbott Laboratories, George R. Cain: "Our foreign investments were not made at the expense of our exports from here, but rather because exports became difficult or impossible, due to trade barriers, tariffs, legislation, or arbitrary decisions protecting or favoring local industry in foreign nations, establishment of local factories and plants by competitors, etc."

"It is significant that Abbott Laboratories International Co.'s employment in Chicago, as a result of its increased capital investments abroad, rose 50 percent in the last 6 years."

"In addition, a large number of scientists, engineers, technicians, researchers, manufacturing and other personnel are now employed by our parent company, as a result of our expansion in foreign markets made possible by our increased investment abroad."

Joy Manufacturing Co., J. D. A. Morrow: "In 1961, nearly one-third of the employment at (Joy Manufacturing Co.'s) Franklin (Pa.) plant was derived from exports. The Treasury asserts that such cases are exceptional and not representative and should be disregarded. Here again the Treasury ignores the facts published by the Department of Commerce, which show that in 1960, out of \$18,900 million of exports, \$2,695 million went to or through foreign manufacturing subsidiaries of American corporations. These are not the statements of private industry, these are the Federal Government's own official figures."

Goodyear Tire & Rubber Co., Frank T. Quirk: "When domestic rubber companies decide to locate a plant overseas, most of the equipment for the plant is shipped from the United States and is made by American workmen. If further expansion is curtailed by revised tax provisions, not only will the foreign markets be taken over by foreign competitors but the machinery, equipment and supplies for their new plants will come from foreign producers."

"There are numerous examples in our industry where the annual purchases of replacement equipment, machinery, materials, and supplies to keep foreign plants operating represent more than the total U.S. dollar investment of the same company overseas. These purchases, amounting to many millions of dollars each year, provide work for thousands of people and are advantageous in our balance of payments position."

Pfizer International, John J. Powers, Jr.: "The key point is that those who say that direct business investment abroad results in the export of American jobs are simply wrong. For this to be true it would have to be demonstrated either (a) that such investments have been made for the purpose of producing goods for import into the United States in lieu of producing such goods in the United States, or (b) that U.S. direct investments abroad have produced goods for sale abroad which could otherwise have been exported from the United States. The facts do not significantly bear out either of these assumptions."

"For example, U.S.-owned manufacturing subsidiaries in Canada and Western Europe had total sales in 1960 of \$18.2 billion, of which only \$259 million was exported to the United States. It is preposterous to charge that U.S. business has gone abroad for the specific purpose of reselling a grand total of 1.4 percent of production back to the United States, or that \$259 million of such imports from foreign subsidiaries could cause any appreciable loss of jobs. Using ratios (jobs to sales) cited by labor officials, \$259 million of sales could mean about 30,000 jobs, or less than one-twentieth of 1

percent of the U.S. labor force—assuming that the goods represented by the \$259 million would have been made in the United States. But this assumption is not justified, for if U.S.-owned subsidiaries in Western Europe and Canada had not sold these goods to the U.S. market, it is more likely that other foreign companies would have supplied the goods, not U.S. factories. Thus it is hardly justifiable to say that the imports cited were responsible for the loss of any significant number of jobs."

"While U.S.-owned facilities in Canada and Western Europe were selling \$259 million of goods to the United States in 1960, these same subsidiaries were importing \$1,246 million worth of goods from the United States. Using the same job-sales ratio, these exports from the United States created more than 100,000 jobs."

Harnischfeger Corp., Frederick Salditt: "Prior to our active participation in overseas investment and manufacture, the exports of our U.S. products lagged slightly behind the exports of our entire industry. With the advent of our active overseas manufacturing program, which involved the use of foreign subsidiaries' reinvested profits, etc., our exports of U.S.-produced goods have steadily increased. They have substantially surpassed the average for our industry, which has generally been on a steady to downward trend."

"This means that we have been able to maintain rather steady domestic employment and even increase it in some of our plants during a most difficult and competitive period. As a matter of fact, during the years 1958-59, we probably would not even have been a domestic taxpayer at all had it not been for our foreign operations and exports, and we most certainly would have employed fewer people in the States of Wisconsin and Michigan."

Sprague International Ltd., William M. Adams: "Although the argument has been propounded that the establishment of foreign manufacturing facilities exports U.S. jobs, our experience indicates that this is just not so. I cannot give you an accurate figure of how many of our employees owe their jobs directly to export, but I can tell you that, in many instances, lines would have been temporarily closed or restricted and employees laid off had it not been for the welcome export business that came into the house at that time."

"In other words, foreign plants stimulate exports and exports tend to cancel out the slack periods that occur from time to time domestically."

Pfaudler Permutit, Inc., William G. von Berg: "It is a peculiar fact that in spite of our buildup of foreign manufacturing facilities, our export volume from plants in the United States did not suffer, but instead showed a tendency to increase. The reasons are several."

"First of all, we supply frit, a compound used in the glassing operation, to our foreign plants."

"Second, special parts and components are supplied from our U.S. plants to our factories abroad. As the activity of our foreign plants increase, so do our exports of frit, parts, and components."

"Third, as overseas customers became accustomed to our equipment and familiar with its advantages, orders for equipment in sizes which could not be made by our foreign plants were transferred to the larger U.S. plants for manufacture."

Dresser Industries, Inc., H. Neil Mallon: "In addition to the significant contribution which Dresser's export trade has made to our country's balance of payments, during the past 3 years over 5,800,000 man-hours of factory labor have been devoted to the production of export products. There is no way to determine how many additional man-hours of labor are attributable to our ex-

port trade as the result of our purchase of materials, components, supplies and services from others. If we assume that our suppliers, sales require the same number of man-hours per dollar as did ours, this additional employment due to our exports amounted to 3,405,000 man-hours."

"We hope to continue to do our part in improving the balance of payments and in promoting full employment. We cannot do so unless we will be competitive with foreign manufacturers who already enjoy many advantages not available to us."

Dow Chemical Co., Tyrone Gillespie: "More than 3,000 people and more than \$70 million in investment in the United States are directly employed in support of our foreign activities. Should foreign investment become unprofitable due to Government intervention, our judgment is that 60 percent or more of the domestic people and facilities supporting foreign sales might be idled."

Minnesota Mining & Manufacturing Co., Robert H. Tucker: "In 1951, a handful of our people handled our total foreign business. Today, 1 out of every 10 employees in our domestic factories owe their jobs to the fact that we are exporting products to foreign countries. Our experience is that exports are increased by foreign manufacturing operations. Business begets business."

I am of the opinion that the committee bill which actually discourages foreign investment would be far more harmful to American employment than would my amendment."

The memorandum also stated that if my amendment were adopted the conferees would be unable to agree on the committee version of the foreign income provisions but would have to adopt the much harsher rules of the House bill. This again is not correct. If my amendment were adopted the conferees would have much more latitude within which to reach an agreement than if the Fowler-Kerr amendment were adopted by the Senate. Furthermore, the Treasury has given no assurance that it will support the Fowler-Kerr amendment of the House bill, and we would be forced to take either the Treasury-Kerr amendment or the House bill."

TAX STATUS OF COOPERATIVES

Mr. HUMPHREY. Mr. President, will the Senator from Oklahoma yield to me for a question?

Mr. KERR. I yield.

Mr. HUMPHREY. I have discussed this question with my colleague from Minnesota, because he is on the Finance Committee, but I would like to ask the Senator in charge of the bill the same question.

My colleague and I, in discussing this subject, agreed that the bill specifically provides that income which may be derived from a cooperative doing business with the Government is not taxable to the cooperative, if it is in turn distributed in accordance with statutory requirements.

Mr. KERR. My understanding is that that is to be merely a continuation of existing law.

Mr. HUMPHREY. The Senator is correct. I wished the RECORD to be clear that there was nothing in the bill which modified that interpretation or that principle of law.

Mr. KERR. That was the effect of the answer by the Senator from Oklahoma a while ago to the Senator's colleague. The answer is the same now.

Mr. HUMPHREY. So far as we are concerned on this question, then, the bill before the Senate would not tax at different rates the income derived by a

cooperative, let us say, and grain storage with the Government, as compared to other income?

Mr. KERR. The Senator is talking about a contract with the Government?

Mr. HUMPHREY. That is correct.

Mr. KERR. That is the understanding of the Senator from Oklahoma.

Mr. HUMPHREY. There is no change?

Mr. KERR. That is correct.

The PRESIDING OFFICER. The bill is open to further amendment.

Mr. DIRKSEN. Mr. President, I offer my amendment 8-23-62—H.

The PRESIDING OFFICER. The amendment will be stated for the information of the Senate.

The CHIEF CLERK. On page 391, between lines 21 and 22, it is proposed to insert the following new section:

SEC. 27. INCREASE IN AMOUNT INDIVIDUALS ARE PERMITTED TO EARN WHILE RECEIVING BENEFITS UNDER TITLE II OF THE SOCIAL SECURITY ACT.

(a) INCREASE IN AMOUNT.—(1) Paragraphs (1), (3), and (4)(B) of subsection (f) of section 203 of the Social Security Act are each amended by striking out "\$100" where ever it appears therein and inserting in lieu thereof "\$150".

(2) The first sentence of paragraph (3) of such subsection (f) is amended by striking out ", except that of the first \$500 of such excess (or all of such excess if it is less than \$500), an amount equal to one-half thereof shall not be included".

(b) CONFORMING AMENDMENT.—Paragraph (1)(A) of subsection (h) of section 203 of such Act is amended by striking out "\$100" and inserting in lieu thereof "\$150".

(c) EFFECTIVE DATE.—The amendments made by the preceding subsections of this section shall be effective, in the case of any individual, with respect to taxable years of such individual ending after 1962.

On page 391, line 22, it is proposed to strike out "27" and to insert in lieu thereof "28".

Mr. DIRKSEN. Mr. President, I shall be brief. This is actually a social security amendment. It deals with the amount of income or earnings a beneficiary under social security might have before there would be a reduction in benefits. Under existing law it is \$1,200, plus the formula which takes it up to \$1,750.

This would simplify it by making it \$1,800 without any reduction in benefits.

I think the amendment needs no further discussion, because it has been before the Senate for a period of years.

Mr. KERR. Mr. President, I am entirely in sympathy with the objective of the distinguished Senator from Illinois. There have been times when the Senator from Oklahoma has been the author of a similar amendment. However, that was in connection with a social security bill, and in connection with action by the Congress to provide the additional revenue for the trust fund which would be required to meet the cost of benefits which would accrue to the beneficiaries by reason of the amendment.

Much as I sympathize with the objective of the distinguished Senator, I know he is aware that adoption of the amendment would cost hundreds of millions of dollars a year, which money would be

taken out of the old-age and survivors' insurance or social security trust fund. I urge the Senator not to press the amendment to this bill, but to wait until a social security bill is before the Senate, when we shall also be considering raising additional revenue to meet the costs of additional benefits which would be created by the amendment.

Mr. DIRKSEN. Mr. President, if I may interpret that as some reasonable assurance that the distinguished Senator from Oklahoma will give attention to it when a social security bill is before the Finance Committee, I shall be glad to withdraw the amendment.

Mr. KERR. I thank the Senator.

The PRESIDING OFFICER. The amendment is withdrawn.

Mr. KERR. I assure the Senator that his requests will at any time be acted upon in the manner of a response for hearings and consideration.

Mr. DIRKSEN. I thank the Senator.

Mr. YARBOROUGH. Mr. President, I offer an amendment which I send to the desk, and ask unanimous consent that the reading be waived, and that it be printed at this point in the RECORD.

The PRESIDING OFFICER. Without objection, it is so ordered.

The amendment is as follows:

On page 134, beginning with line 24, it is proposed to strike out all through line 25 on page 135 and insert the following:

"(a) GENERAL RULE.—In the case of an individual citizen of the United States who establishes to the satisfaction of the Secretary or his delegate that he has been a bona fide resident of a foreign country or countries for an uninterrupted period which includes an entire taxable year, amounts received from sources without the United States (except amounts paid by the United States or any agency thereof) which constitute earned income attributable to services performed during such uninterrupted period shall not be included in gross income and shall be exempt from taxation under this chapter. The amount excluded under this subsection for any taxable year shall be computed by applying the special rules contained in subsection (c)."

On page 137, strike out lines 4 through 13 and insert the following: "a daily basis at an annual rate of \$12,000."

On page 139, line 2, strike out "subsection (a) (1)" and insert "subsection (a)".

On page 139, strike out lines 3 through 20.

On page 140, beginning with line 16, strike out all through line 3 on page 141 and insert the following:

"(c) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 1962."

Mr. YARBOROUGH. Mr. President, the amendment is identical with the amendment of the Senator from Tennessee [Mr. GORE] designated "8-27-62—G," which would limit the amount of earned foreign income that could be deducted, except that on page 2, line 7 of the Gore amendment, at which point \$6,000 is provided, I have stricken out that amount and inserted \$12,000. The amendment would reduce the \$35,000 stated in the bill. The Gore amendment would reduce the amount to \$20,000; \$6,000 a year of income earned abroad would be exempt from taxation. My amendment would exempt the first \$12,000.

I hope the distinguished Senator from Oklahoma will give serious consideration to accepting the amendment. Since I live in close proximity to Mexico, I know that people earning a dollar abroad have a higher purchasing power than people in the United States. That is true in many countries. It seems to me that \$1,000 a month is a pretty generous exemption from taxation to allow a person for the first \$12,000 a year of his earnings abroad.

I invite attention to the fact that that is twice as much as was contained in the amendment proposed by the distinguished Senator from Tennessee. He would have exempted \$6,000 a year, or \$500 a month. The proposed amendment would exempt \$1,000 a month, or \$12,000 a year, of the first year's income. I have no further statement to make. I hope that the distinguished Senator from Oklahoma will give serious consideration to accepting the amendment.

Mr. KERR. Mr. President, I do not believe I completely understand the Senator's amendment. I cannot tell whether he would limit the exemption of an American citizen in the status of a non-resident of the country, and therefore a resident of the country in which he is working for a period of time under 18 months, under 2 years, or beyond 2 years. Would his amendment apply equally with reference to the American citizen who is a bona fide resident of another country for any period of time, or is there a period of time in which the bona fide resident in another country could acquire a different position under the amendment of the Senator from Texas than would be the case, let us say, for the first year of his absence from this country and being a bona fide resident of another country?

Mr. YARBOROUGH. The amendment is identical with the Gore amendment except that on page 2, line 7, of the Gore amendment, where he has provided an exemption of \$6,000, I have provided \$12,000, and that would be in lieu of the language in the bill on page 137. It would strike out lines 4 through 13.

Mr. KERR. Lines 4 through 13 on what page?

Mr. YARBOROUGH. Page 137 of the bill. That would include either an American temporarily abroad who had been a bona fide resident of a foreign country or countries for less than 3 years—17 or 18 months—in which case he would have a \$20,000 exemption, and would also apply to the American who had been abroad for more than 3 years, in which case the first \$35,000 would be exempt. The amendment would treat them all in the same category and exempt the first \$12,000 of earnings abroad from any taxation here. I have taken the language of the proposed Gore amendment, which would reduce the exempt amount to \$6,000 of the first \$35,000, and, in my amendment, reduce it to \$12,000.

It would apply to both categories. It would apply to the U.S. citizen who had been a bona fide resident of a foreign country or countries more than 3 years, and it would apply to the U.S. citizen who had been a bona fide resident of a

foreign country or countries less than 3 years. It would have to be a bona fide resident in each case. But under the bill as drawn if a man goes overseas and stays 18 months—a little over a year—he receives an exemption on the first \$20,000 of his income—if he stays there less than 3 years. If he stays more than 3 years, the exemption applies to the first \$35,000 of his income. The amendment would roll it into one exemption. He would have \$1,000 a month free and clear of any taxes whatsoever before he started on the usual deductions and exemptions that would apply to the rest of us living in this country. He would get \$1,000 scot free under that provision.

Mr. KERR. Mr. President, I must oppose the amendment. I tried to make clear this afternoon in the discussion of the amendment of the Senator from Tennessee [Mr. GORE] that the bill would not give to bona fide residents of our country working in a foreign country a benefit which they do not have under existing law. The bill would take from bona fide residents working in foreign countries benefits which they now have under the law. Under existing law, if an American citizen is a bona fide resident of another country for 18 months, the income he earns in that country, regardless of what the amount may be, is not subject to tax by our Government. We changed that. We provided that his exemption cannot exceed \$20,000 for the first 3 years, and cannot exceed \$35,000 thereafter.

As I stated today, the provision applies to American citizens who go abroad to operate businesses owned in this country and which are in competition with other local businesses in the respective foreign countries.

I referred to the fact that Sears, Roebuck was such a company. When a company such as Singer Sewing Machine Co., or whatever the American industry may be, goes into Buenos Aires, Rio de Janeiro or any other city in Latin America, Central America, Western Europe, or anywhere else in the world, it must compete with local distributors, not only of products produced or manufactured in the countries in which the business is located, but also against the products shipped in from any other industrial or productive area in the world. Senators can well understand that if an American company putting a place of business in South America could get a local national to operate it as efficiently as an American citizen trained here and going there could do, it would get the local national to do it because the local national of equal ability would receive a more favorable response and be a more effective operator of the business than someone sent from the United States.

But such is not the case. The only reason trained American citizens are sent abroad is that thereby the business can be more efficiently and successfully operated.

But to encourage American citizens to take their families and move away from these shores and go into a foreign country and handle a business there requires enough incentive to persuade them to leave the more favorable environment that exists here at home.

I ask Senators to remember that American businesses in the main sell in foreign countries products which are manufactured or produced in the United States. Every time they sell a dollar's worth of such products they help to insure jobs to American workmen here at home in our factories and our mills and in other productive facilities. Therefore, it is not only to the advantage of the American company doing business there to have the most efficient management possible, but it is also to the advantage of the economic condition of this country. It is to the advantage of the industry that produces products which are made here by labor paid here in communities supported by such industries which ship into other countries, to sell there. The profits come back to this country and are taxed by our Government, whereby dollars come to our country, which help our balance of payments.

The only reason that American companies pay the salaries they do and offer the incentive that they do is that they must do it to keep the kind of talent which can efficiently compete in foreign countries with others who are doing business there.

If we did not permit these exemptions, the corporations would have to pay much higher salaries. Citizens who are residents of foreign countries must pay local taxes in those foreign countries. To the extent that they pay local taxes on their salaries in foreign countries they receive a credit here against the tax liability that they would have on the same salary.

Therefore, the Senator's amendment would defeat its own purpose by impairing the efficiency of operation of the American companies doing business in foreign countries, with the advantage to our own economy and our own labor force that I have outlined.

Therefore I hope the Senator's amendment will be disapproved, as was the amendment of the Senator from Tennessee.

Mr. YARBOROUGH. Mr. President, I should like Senators to recall from their own experience how many people have come to their offices from their home States wanting Federal employment, provided they could go overseas. I point to the experience of the Peace Corps, not to a business activity. I point to young people and to the American spirit which permeates our whole society. Every Senator has had the experience of seeing people from his State asking if they could go to work overseas in a Government job. They want to go overseas.

Business organizations do not have a difficult time recruiting people to go overseas. The very reason that the distinguished Senator from Oklahoma gives as a reason for defeating the amendment is a reason why the amendment ought to be adopted. An American living overseas can deduct from his U.S. income tax the tax he pays to the foreign government before he begins to compute his American tax. When he deducted his foreign-paid tax, under the amendment, he would deduct another \$1,000, all absolutely tax free. He

is favored above any other Americans. He gets all tax exemptions that people get at home, and in addition he gets his travel and any other expenses. He is in a very favored position.

In addition, the living costs in many countries are very much lower. When we add the \$1,000 allowance, he is in an exceedingly favorable position.

I point out that many Americans come back with their earnings saved. Unless they have spent their time in Paris or in Germany, they come back with their savings, especially if they have lived in some of the underdeveloped countries of the world.

We maintain a great Army, a great Navy, a great Air Force, and a strong State Department to protect our people overseas. We have commercial attachés all over the world, consular officers, and consulates general, and embassies. We support these people with the military might of the most powerful nation in the world, and in that way protect investments and protect our personnel. Surely they ought to be willing to pay something for that protection while they earn their income.

I commend the distinguished Senator from Oklahoma. As he has correctly said, under present law such income is all tax free. A limitation of \$20,000 and \$35,000 has been set. That is a step in the right direction. However I point out that it is still exceedingly generous if we exempt a thousand dollars a month of that sum, free from income taxation.

I point out further that there is no equity in allowing individual U.S. citizens living abroad, either temporarily or on a more permanent bona fide basis, to pay less taxes than citizens and residents here at home. All benefit from services rendered by both the U.S. Government and the governments of their host countries. All should contribute toward the cost of United States and free world protection. It is particularly inappropriate to allow a phasing-in of taxes on fringe benefits.

I hope the distinguished Senator from Oklahoma will accept the amendment. Apparently he will not accept it, and I regret that he cannot do so.

Mr. KERR. I cannot accept the amendment.

The PRESIDING OFFICER. The question is on agreeing to the amendment offered by the Senator from Texas.

The amendment was rejected.

The PRESIDING OFFICER. The bill is open to further amendment. If there be no further amendment to be proposed, the question is on the engrossment of the amendments and third reading of the bill.

The amendments were ordered to be engrossed, and the bill to be read a third time.

The bill was read the third time.

COMMITTEE MEETINGS DURING SENATE SESSION TOMORROW

Mr. MANSFIELD. Mr. President, I ask unanimous consent that the Rivers and Harbors Subcommittee of the Committee on Public Works and the Permanent Subcommittee on Investigation of the Committee on Government Opera-

Digest of CONGRESSIONAL PROCEEDINGS

OF INTEREST TO THE DEPARTMENT OF AGRICULTURE

OFFICE OF
BUDGET AND FINANCE

(For information only;
should not be quoted
or cited)

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HIGHLIGHTS: Sen. Hickenlooper criticized and Sen. Humphrey defended Secretary's pledge of commodities to United Nations. Senate passed tax revision bill. Rep. Libonati commended forestry demonstration in Richmond, Va.

HOUSE

1. APPROPRIATIONS. Conferees were appointed on H. R. 12648, the agricultural appropriation bill. Senate conferees have already been appointed. p. 17573
The "Daily Digest" states that "Conferees met in executive session to resolve the differences between the Senate- and House-passed versions of H. R. 12648, fiscal 1963 appropriations for the Department of Agriculture, but did not reach final agreement, and will meet again tomorrow." p. D813
2. FORESTRY. Rep. Libonati described and commended a recent forestry demonstration in Richmond, Va. pp. 17609-11
3. BREAD. The Ways and Means Committee reported with amendment H. R. 3985, to amend the Tariff Act of 1930 to impose a duty upon the importation of bread (H. Rept. 2325). p. 17612
4. SOCIAL SECURITY; FARMERS. Rep. Rhodes, Pa., inserted an article about a farmer getting social security disability benefits, "Social Security Helps Farmer."

p. 17576

5. ATOMIC ENERGY. Received from the President the annual report of U. S. participation in Atomic Energy Agency (H. Doc. 538). p. 17582, p. 17614
6. LEGISLATIVE PROGRAM. Rep. Albert announced that H. R. 12365, health clinics for migratory farmworkers, will be considered on Mon., and S. 4, Padre Island National Seashore, will be brought up on Tues. p. 17575
7. ADJOURNED until Mon., Sept. 10. p. 17612

SENATE

8. FARM PROGRAM; PUBLIC LAW 480. Sen. Hickenlooper criticized Secretary Freeman's pledge of commodities to the United Nations food program, questioned whether the Secretary has authority under Public Law 480 to pledge commodities for this purpose, and contended it was "the first step in relinquishing our control over the distribution of our surplus food and agricultural commodities." Sen. Humphrey defended the Secretary's action, stating that "I believe it falls full well within the scope of authority granted by the Congress to the executive branch." pp. 17668, 17710
9. TAXATION. By a vote of 59 to 24, passed with amendments H. R. 10650, the proposed Revenue Act of 1962. Conferees were appointed. pp. 17620-1, 17624-6, 17632-41, 17648, 17650-9
10. MINING. Passed as reported S. 3451, to authorize the Secretary of the Interior to provide relief for residential occupants of unpatented mining claims upon which valuable improvements have been placed. pp. 17700-5
11. LAW; COURTS. Passed as reported H. R. 1960, to make it possible to bring actions against Government officials and agencies in U. S. district courts outside D. C., which, because of certain existing limitations on jurisdiction and venue, may now be brought only in the U. S. District Court for D. C. pp. 17699-700
12. CREDIT. The "Daily Digest" states that the Subcommittee on Production and Stabilization of the Banking and Currency Committee "by a vote of 5 to 4, defeated a motion to report to the full committee S. 1740, to require the disclosure of finance charges in connection with extensions of credit." p. D812
13. WILDLIFE. Passed over, at the request of Sen. Mansfield, H. J. Res. 489, to provide for protection of the golden eagle. p. 17696
14. RECLAMATION. The Interior and Insular Affairs Committee reported without amendment H. R. 11164, to approve an amendatory repayment contract negotiated with the Quincy Columbia Basin Irrigation District and authorize similar contracts with any of the other Columbia Basin irrigation districts (S. Rept. 2002). p. 17614
15. PERSONNEL. Agreed to as reported S. Con. Res. 53, declaring the sense of Congress that all official air travel by employees and officials of the Federal Government should be performed on U. S.-flag carriers except under the most limited circumstances. pp. 17693-4
Sen. Byrd, Va., submitted the report of the Joint Committee on Reduction of Nonessential Federal Expenditures on Federal employment and pay for July 1962. pp. 17615-9
Sen. Hickenlooper criticized the recent increase in the number of Federal employees and suggested that a moratorium be declared on the filling of all

STATEMENT BY SENATOR BYRD OF VIRGINIA

The cost of civilian employment in the executive branch of the Federal Government reached its alltime high in fiscal year 1962 which ended June 30, and average employment over the full 12 months was at its highest point since fiscal year 1954.

Federal civilian payroll costs during the year totaled \$14,296 million plus \$314 million in U.S. pay for foreign nationals not on the regular rolls. The personal service cost of the Government exceeded \$1 billion a month for the fourth consecutive year.

The payroll cost for employment by civilian agencies in fiscal year 1962 was \$7,978 million and for civilian employment in military agencies was \$6,318 million.

Figures by fiscal years since 1954 follow:

Annual Federal expenditures for civilian payroll, executive branch, fiscal year 1954-62
(In millions of dollars)

Fiscal year	Civilian agencies	Department of Defense ¹ (civilian employment)	Total
1954	\$4,865	\$4,588	\$9,453
1955	4,921	4,700	9,621
1956	5,359	5,167	10,526
1957	5,602	5,399	11,000
1958	6,040	5,415	11,455
1959	6,564	5,766	12,330
1960	6,877	5,760	12,637
1961	7,622	6,026	13,648
1962	7,978	6,318	14,296

¹ Excludes U.S. pay for foreign nationals not on regular rolls.

Employment by executive branch agencies during fiscal year 1962 (ended June 30) averaged 2,443,808 as compared with an average of 2,372,445 in the previous year. Employment by civilian agencies averaged 1,385,132, an increase of 50,043 as compared with an average of 1,335,089 in the previous year. Civilian employment by military agencies averaged 1,058,675, an increase of 21,319 as compared with an average of 1,037,356 in the previous year.

Average employment by fiscal years since 1954 follows:

Average civilian employment by Federal agencies, executive branch, fiscal year 1954-62

Fiscal year	Civilian agencies	Department of Defense ¹ (civilian employment)	Total
1954	1,183,389	1,252,775	2,436,164
1955	1,182,663	1,184,627	2,367,290
1956	1,189,458	1,174,584	2,364,042
1957	1,219,835	1,174,263	2,394,098
1958	1,242,941	1,104,403	2,347,344
1959	1,266,566	1,085,676	2,352,242
1960	1,331,605	1,054,740	2,386,345
1961	1,335,089	1,037,356	2,372,445
1962	1,385,132	1,058,675	2,443,808

¹ Excludes foreign nationals not on regular rolls (averaging 169,835 during fiscal year 1962).

JULY 1962 EMPLOYMENT

Monthly reports on personnel certified to the committee showed civilian employment by executive agencies of the Federal Government during July totaled 2,511,025 an increase of 14,530 over the previous month.

Civilian agencies reporting the larger increases were Post Office Department with 2,857; Department of Health, Education, and Welfare with 1,550; Treasury Department with 1,513; Agriculture Department with 1,467 and Interior Department 1,091. The increases in the Departments of Agriculture, Interior, and Post Office were largely seasonal.

Total employment inside the United States in July was 2,350,365 an increase of 14,393 as compared with June. Total employment

outside the United States in July was 160,660, an increase of 137 as compared with June.

Employment by civilian agencies in July totaled 1,438,694, an increase of 11,805 over June. Civilian employment by military agencies in July totaled 1,072,331, an increase of 2,725 as compared with June.

FOREIGN NATIONALS

The total of 2,511,025 civilian employees certified to the committee by executive agencies in their regular monthly personnel reports includes some foreign nationals employed in U.S. Government activities abroad, but in addition to these there were 170,144 foreign nationals working for U.S. agencies overseas during July who were not counted in the usual personnel report. The number in June was 171,109. A breakdown of this employment for July follows:

Country	Total	Army	Navy	Air Force	National Aeronautics and Space Administration
Australia	1				1
Canada	36			36	
Cuba	60			60	
England	3,151		90	3,061	
France	22,728	18,521	11	4,196	
Germany	80,947	67,865	84	12,998	
Greece	265			265	
Greenland	133			133	
Japan	53,452	19,268	14,265	19,919	
Korea	6,164	6,164			
Morocco	2,540		766	1,774	
Netherlands	53			53	
Trinidad	614		614		
Total	170,144	111,818	15,830	42,495	1

BILLS INTRODUCED

Bills were introduced, read the first time and, by unanimous consent, the second time, and referred as follows:

By Mr. CLARK:

S. 3699. A bill for the relief of Theodore S. Zoupanos; to the Committee on the Judiciary.

By Mr. DIRKSEN:

S. 3700. A bill for the relief of Jan Mru-gala; to the Committee on the Judiciary.

By Mr. HILL (for himself and Mr. SPARKMAN):

S. 3701. A bill providing for the extension of patent No. 2,439,502, issued April 13, 1948 relating to an automatic fire alarm system; to the Committee on the Judiciary.

By Mr. KEATING:

S. 3702. A bill relating to the effective date of the qualification of Bricklayers Local 45 (Buffalo, N.Y.) pension fund as a qualified trust under section 401(a) of the Internal Revenue Code of 1954; to the Committee on Finance.

(See the remarks of Mr. KEATING when he introduced the above bill, which appear under a separate heading.)

RESOLUTION

PROPOSED SELECT COMMITTEE ON TECHNOLOGICAL DEVELOPMENTS

Mr. LONG of Louisiana submitted the following resolution (S. Res. 380); which was referred to the Committee on Labor and Public Welfare:

Resolved, That (a) there is hereby established a select committee of the Senate to be known as the Select Committee on Technological Developments (referred to hereinafter as the "Committee") consisting of nine Members of the Senate, of whom six shall be members of the majority party and three

shall be members of the minority party. Members and the chairman thereof shall be appointed by the President of the Senate. Vacancies in the membership of the Committee shall not affect the authority of the remaining members to execute the functions of the Committee, and shall be filled in the same manner as original appointments there-to are made.

(b) A majority of the members of the Committee shall constitute a quorum thereof for the transaction of business, except that the Committee may fix a lesser number as a quorum for the purpose of taking sworn testimony. The Committee shall adopt rules of procedure not inconsistent with the rules of the Senate governing standing committees of the Senate.

(c) No legislative measure shall be referred to the Committee, and it shall have no authority to report any such measure to the Senate.

(d) The Committee shall cease to exist on January 31, 1965.

SEC. 2. (a) It shall be the duty of the Committee to conduct a comprehensive study and investigation with respect to—

(1) the extent to which departments and agencies of the United States Government, through research and development activities undertaken directly or by the use of facilities of private contractors and grantees, are responsible for scientific and technological developments achieved within the United States;

(2) the effect of such activities upon the scientific, technical, and economic progress of the United States and upon the structure of the economy of the United States; and

(3) the nature and extent of the action which is required to provide for the effective employment of such activities to promote to the greatest practicable extent the scientific, technical, and economic progress of the United States, the effective utilization of the manpower and material resources of the United States, the promotion of higher standards of living for the people of the United States, and the achievement of the maximum economic strength of the United States.

(b) On or before January 31 of each year, the Committee shall report to the Senate the results of its studies and investigations, together with its recommendations for any additional legislative or other measures which it may determine to be necessary or desirable to attain the objectives specified in paragraph (3) of subsection (a).

SEC. 3. (a) For the purposes of this resolution, the Committee is authorized to (1) make such expenditures; (2) hold such hearings; (3) sit and act at such times and places during the sessions, recesses, and adjournment periods of the Senate; (4) require by subpoena or otherwise the attendance of such witnesses and the production of such correspondence, books, papers, and documents; (5) administer such oaths; (6) take such testimony orally or by deposition; and (7) employ and fix the compensation of such technical, clerical, and other assistants and consultants as it deems advisable, except that the compensation so fixed shall not exceed the compensation prescribed under the Classification Act of 1949, as amended, for comparable duties.

(b) Upon request made by the members of the Committee selected from the minority party, the Committee shall appoint one assistant or consultant designated by such members. No assistant or consultant appointed by the Committee may receive compensation at an annual gross rate which exceeds by more than \$1,400 the annual gross rate of compensation of any individual so designated by the minority members of the Committee.

(c) With the prior consent of the executive department or agency concerned and

the Committee on Rules and Administration, the Committee may (1) utilize the services, information, and facilities of any such department or agency, and (2) employ on a reimbursable basis the services of such personnel of any such department or agency as it deems advisable. With the consent of any other committee of the Senate, or any subcommittee thereof, the Committee may utilize the facilities and the services of the staff of such other committee or subcommittee whenever the chairman of the Committee determines that such action is necessary and appropriate.

(d) Subpenas may be issued by the Committee over the signature of the chairman or any other member designated by him, and may be served by any person designated by such chairman or member. The chairman of the Committee or any member thereof may administer oaths to witnesses.

SEC. 4. The expenses of the Committee under this resolution, which shall not exceed \$—— through January 31, 1965, shall be paid from the contingent fund of the Senate upon vouchers approved by the chairman of the Committee.

EFFECTIVE DATE OF QUALIFICATION OF BUFFALO (N.Y.) BRICKLAYERS LOCAL 45 PENSION FUND AS A QUALIFIED TRUST

Mr. KEATING. Mr. President, I introduce, for appropriate reference, a bill relating to the effective date of the qualification of the Buffalo, N.Y., Bricklayers Local 45 pension fund as a qualified trust under the Internal Revenue Code. I ask unanimous consent that the text of the bill be printed in the RECORD at this point.

The PRESIDING OFFICER (Mr. METCALF in the chair). The bill will be received and appropriately referred; and, without objection, the bill will be printed in the RECORD.

The bill (S. 3702) relating to the effective date of the qualification of Bricklayers Local 45 (Buffalo, N.Y.) pension fund as a qualified trust under section 401(a) of the Internal Revenue Code of 1954, introduced by Mr. KEATING, was received, read twice by its title, referred to the Committee on Finance, and ordered to be printed in the RECORD, as follows:

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That the Bricklayers Local 45 (Buffalo, New York) pension fund, which was established by a collective bargaining agreement effective June 1, 1958, and which has been held by the Internal Revenue Service to constitute a qualified trust under section 401(a) of the Internal Revenue Code of 1954, and to be exempt from taxation under section 501(a) of such Code, for years ending on or after November 29, 1960, shall be held and considered to have been a qualified trust under such section 401(a), and to have been exempt from taxation under such section 501(a), for the period beginning on June 1, 1958, and ending on November 29, 1960, but only if it is shown to the satisfaction of the Secretary of the Treasury or his delegate that the trust has not in this period been operated in a manner which would jeopardize the interests of its beneficiaries.

MESSAGE FROM THE HOUSE

A message from the House of Representatives, by Mr. Bartlett, one of its

reading clerks, announced that the House had passed the bill (S. 2184) for the relief of Mrs. Heghine Tomassian, with an amendment, in which it requested the concurrence of the Senate.

The message also announced that the House had passed the joint resolution (S.J. Res. 60) to establish the Sesqui-centennial Commission for the Celebration of the Battle of New Orleans, to authorize the Secretary of the Interior to acquire certain property within Chalmette National Historical Park, and for other purposes, with amendments, in which it requested the concurrence of the Senate.

The message further announced that the House had disagreed to the amendments of the Senate to the bill (H.R. 12648) making appropriations for the Department of Agriculture and related agencies for the fiscal year ending June 30, 1963, and for other purposes; agreed to the conference asked by the Senate on the disagreeing votes of the two Houses thereon, and that Mr. WHITTEN, Mr. NATCHER, Mr. CANNON, Mr. HORAN, and Mr. TABER were appointed managers on the part of the House at the conference.

ENROLLED BILLS SIGNED

The message also announced that the Speaker had affixed his signature to the following enrolled bills, and they were signed by the President pro tempore:

S. 1108. An act authorizing the conveyance of certain property in the city of San Diego to the regents of the University of California;

S. 1878. An act to add certain lands to the Wasatch National Forest, Utah, and for other purposes;

S. 2421. An act to provide for retrocession of legislative jurisdiction over U.S. Naval Supply Depot Clearfield, Ogden, Utah;

S. 3071. An act for the relief of Hidayet Danish Nakashidze;

S. 3224. An act to provide for the exchange of certain lands in Puerto Rico; and

S. 3628. An act to amend title 10, United States Code, to authorize the appointment of citizens or nationals of the United States from American Samoa, Guam, or the Virgin Islands to the U.S. Military Academy, the U.S. Naval Academy, and the U.S. Air Force Academy.

ADDRESSES, EDITORIALS, ARTICLES, ETC., PRINTED IN THE APPENDIX

On request, and by unanimous consent, addresses, editorials, articles, etc., were ordered to be printed in the Appendix, as follows:

By Mr. HART:

Address delivered by Senator HARTKE before Labor Day celebration at Anderson, Ind., on September 3, 1962.

By Mr. HILL:

Address entitled "Auburn University: Past, Present, and Future," delivered by George C. Wallace, Governor-elect of Alabama, at Auburn University on August 1, 1962.

By Mr. HARTKE:

Article entitled "The Shadow of Unemployment" written by Ralph McGill and published in the Evening Star of September 4, 1962.

By Mr. MUNDT:

Letter to him written by John Jagger of Covina, Calif., September 3, 1962.

By Mr. SMATHERS:

Article entitled "The Menace of Communist Cuba," by William S. White, published in the Washington Evening Star, September 5.

THE TAX BILL

Mr. MORSE. Mr. President, I wish to thank the editors of the Washington Post for setting out in such concise, condensed, and unanswerable form the thesis of the speech which I would otherwise make against the shocking tax bill which now is before the Senate. I refer to the editorial entitled "Tax Bill Perversity," which is published this morning in the Washington Post. I ask unanimous consent that the editorial be printed at this point in the RECORD. It will constitute my speech, and will save the Senate's listening to me speak at some length this morning in opposition to the pending bill.

There being no objection, the editorial was ordered to be printed in the RECORD, as follows:

TAX BILL PERVERSITY

Faith in the processes of democratic government is hardly likely to be enhanced by the Revenue Act of 1962 which is about to be passed by the Senate. A week ago it was fair to charge that the administration's original proposals had been mutilated almost beyond recognition. In the interim the Senate in a veritable fit of perversity passed amendments which will make our system of personal taxation more inequitable and more difficult to administer than ever before.

In tracing the process of transmogrification, it is necessary to go back to President Kennedy's tax proposals of April 1960. At that time he outlined measures designed to close tax loopholes which covered interest and dividend income, savings institutions, expense accounts, and foreign corporate subsidiaries. His loophole-closing measures would have added \$2.3 billion to Federal revenues, thus more than offsetting the investment-credit loss of \$1.7 billion. But in their passage through the House and the Senate Finance Committee, the loophole-closing provisions were systematically weakened or eliminated and the bill that reached the floor of the Senate, shorn of its dividend-interest withholding provision, would have resulted in a net revenue loss of nearly \$700 million.

But the Senate was not satisfied with the handiwork of its Finance Committee and it proceeded to pervert as well as attenuate the remains of what had been a good tax bill. By a vote of 51 to 13 it joined the House in overturning a 1959 Supreme Court decision which declared that business-lobbying expenditures are not tax deductible. And it adopted an amendment offered by Senator DIRKSEN which exempts from taxation the profits on homes sold for less than \$30,000 by persons over 65. The first measure will, according to Senator DOUGLAS, "legitimize tremendous expenditures by special interests to affect legislation" while not providing comparable treatment to lobbyists for the general interest. DIRKSEN's amendment opens another capital-gains loophole which will work to the benefit of those who are not in need of tax relief.

The worst, however, is yet to come. Yesterday the Senate voted to table a measure already passed by the House (H.R. 10), which would allow self-employed persons to deduct up to \$1,750 annually in order to finance retirement plans. Assured of pas-

sage in the Senate, this bill would provide a tax windfall for upper income professionals. It is estimated by the Treasury that 53 percent of the tax benefits would accrue to persons with incomes of more than \$20,000 who constitute only 3 percent of the self-employed.

In the 28 months which have elapsed since the President made his original tax proposals the administration has suffered a series of humiliating defeats which it accepted without strong protest in order to obtain a few pallid reforms. But there is no longer any justification for giving ground. The self-employed pension bill is a piece of special interest legislation which should be promptly vetoed if it cannot be killed by other means.

Mr. MORSE. Mr. President, I only add to the editorial the point I made the other day; namely, this bill is for tax dodgers. The bill does not keep faith with the promises of the Democratic Party for tax reform. It is a shocking bill which, in my judgment, betrays the faith of the American taxpayers in the Democratic Party. It transfers to the shoulders of those least able to pay the tax burdens which should be assumed by those most able to pay.

CRITICISM OF NATIONAL CHAIRMAN OF THE DEMOCRATIC PARTY

Mr. MORSE. Mr. President, last night I criticized the role played by the national chairman of the Democratic Party, Mr. John Bailey, at the Western States Democratic Conference of 13 Western States. He brought to that conference the machine politics of the East characterized by smoke-filled hotel-room pressures. He left behind him a trail of deep resentment on the part of many Western Democrats who have a Democratic record of supporting Jeffersonian democracy that is not surpassed by the chairman of the Democratic Party.

TRIBUTE TO JUDGE EDWARD A. BEARD

Mr. SCOTT. Mr. President, Judge Edward A. Beard, of the District of Columbia juvenile court, is an excellent judge. He well deserves the tribute paid to him in an editorial in the Washington Daily News of September 5, 1962. I ask unanimous consent to insert the editorial in the RECORD.

There being no objection, the editorial was ordered to be printed in the RECORD, as follows:

APPLAUSE FOR JUDGE BEARD

Here's a belated huzzah for Municipal Judge Edward A. Beard who, while sitting in District Juvenile Court for 2 weeks recently in the absence of Judge Orman W. Ketcham not only managed to keep up with the regular docket but disposed of some 400 other cases in Judge Ketcham's sorry backlog of work undone.

The fact that Judge Beard was able to do this—and do it with a great deal of ease and commonsense—demonstrates what the Washington Daily News has been saying for the past several years—that Judge Ketcham, however well meaning, simply is not able to run the court as it can and should be run.

By taking swift, stern action against traffic offenders, Judge Beard disposed of some 200 jammed up cases in short order. Many other

cases involving minor offenses—some dating back for months—he simply dismissed.

"I could see no reason to try youngsters who have been home awaiting trial for 8 months to a year and who had got in no further trouble," he explained. As for the News editorial of August 7 which called for the wholesale dismissal of juvenile cases so old that the youngsters had forgotten the offense, Judge Beard simply remarked that he had beat us to the punch.

And so he had, we're delighted to agree. In fact, he found one case so old that even the arresting policeman was a bit hazy about it. Naturally, that went out, too.

We hope the two new judges appointed by President Kennedy to help Judge Ketcham run this court will avail themselves of Judge Beard's experience and comments.

In fact, the new three-man court, and the community at large, could very well take a fresh look at the juvenile court and its problems—not particularly those relating to the way it has been run in recent years, but to the court's overall philosophy, such as the kind of cases which properly should be referred to it. We're confident they could come up with some fresh and challenging ideas.

ACHIEVEMENTS OF THE PEACE CORPS

Mr. DODD. Mr. President, the New York Times of September 1, 1962, contained an account of a news interview held in Singapore by R. Sargent Shriver describing some of the achievements of the Peace Corps.

It was only a year ago that the first Peace Corps contingent was dispatched overseas. There were some who held grave misgivings about this project but a year's experience has laid to rest those misgivings.

All Americans may take justified pride in the accomplishments and progress of the Peace Corps. All of us owe a great debt to those young Americans who are laboring in our behalf and in behalf of the peoples of underdeveloped areas in such distant places as Thailand, North Borneo, Tanganyika, and Cyprus.

Under the driving idealistic leadership of a great public servant, Sargent Shriver, the Peace Corps has more than redeemed the hopes of those of us who supported this project from its inception.

I ask unanimous consent to insert at this point in the RECORD the brief New York Times article I referred to above which provides some idea of the scope and vitality of the Peace Corps operation.

There being no objection, the article was ordered to be printed in the RECORD, as follows:

SHRIVER SEES MAJOR U.S. GAIN IN PEACE CORPS WORK IN ASIA—OPERATION IS GOING ALMOST TOO WELL TO BE BELIEVED

SINGAPORE, August 31.—Peace Corps operations in Asia are "going almost too well to be believed," according to Sargent Shriver, Director of the Corps, a U.S. volunteer program to assist developing countries. A year ago today the first contingent of the Corps was dispatched overseas.

Mr. Shriver declared in an interview that all the countries he had visited on his current Asian tour had asked for "three to four times as many" Peace Corps workers as had been assigned. Of 2,600 volunteers sent overseas, Mr. Shriver said, 400 are in southeast

Asia and another 400 are coming to the area in September.

Corps members in southeast Asia are engaged principally in farm development, road-building, teaching, and medical work. Many are teaching English to southeast Asians eager to learn a language in which they can communicate with people from other countries. All the American volunteers speak the language of the people with whom they work.

In addition to their regular work, Mr. Shriver said, most Peace Corps members have undertaken some kind of extracurricular activity, such as coaching sports, directing Scout troops or running camps for underprivileged children.

SLOGANS SHIFT

All this, he declared, has helped to establish a more favorable image of the United States in Asian countries. The slogan "Yankee go home" has been replaced by "send us more Peace Corps volunteers," Mr. Shriver said.

The health of Peace Corps workers, who live exactly as local people do and eat the same food, has been "incredibly good," Mr. Shriver declared. He said that major illness had been almost unknown in the Corps, although all members abroad had experienced minor intestinal upsets from unfamiliar diets.

Mr. Shriver asserted that all members of the Peace Corps were thoroughly trained in simple precautions against illness, such as boiling drinking water and keeping inoculations up to date. He added that a U.S. Public Health Service physician was responsible for the health of Corps members in each country.

Mr. Shriver was barely preceded to the British Crown Colonies of North Borneo and Sarawak by 60 young men and women, some only 18 years old, who constitute the first U.S. Government mission of any kind in those primitive territories.

ROADS ARE STRESSED

Establishing roads is the principal project of the Corps in North Borneo and Sarawak, which contain some of the most extensive jungle areas in the world, Mr. Shriver said. Some Corps members will be living in the long houses of the Dyaks and other tribal people who inhabit the more remote parts of the two British colonies.

Mr. Shriver said that in Thailand, where the Prime Minister, Field Marshal Sarit Thanarat, had asked that the Peace Corps contingent be tripled, the Government plans to make a television film of Corps members at work.

As far as Mr. Shriver knows, Thailand may be the first country that has offered to publicize U.S. aid activities as part of its information program.

TRIBUTE TO SENATOR KEFAUVER

Mr. DODD. Mr. President, the August 24, 1962 edition of the Keene Evening Sentinel, published in Keene, N.H., contained an editorial about our distinguished colleague, the senior Senator from Tennessee, ESTES KEFAUVER, which I think ought to be given wide circulation.

The editorial recounts the long and lonely struggle carried on by Senator KEFAUVER to provide for the American people protection against unsafe and ineffective drugs. It reminds us of the abusive treatment meted out to our colleague and some of the defeats he encountered along the way. I believe this editorial is a reflection of the fact that the American people are coming to appreciate the important contributions to

their welfare that are being made daily by the great senior Senator from Tennessee.

I ask unanimous consent that the editorial entitled "Short Memories" be printed at this point in the RECORD.

There being no objection, the editorial was ordered to be printed in the RECORD, as follows:

SHORT MEMORIES

Most American newspaper readers have very short memories. But for those whose memories are more durable, there was a sardonic background to a story in the headlines earlier this week.

The story reported that the Senate Judiciary Committee had unanimously approved a bill which would give President Kennedy virtually all the authority he needs to protect the public from unsafe and ineffective drugs.

It required a tragedy—the deformities apparently caused by the drug thalidomide—to prompt the Senators to provide the drug bill with a set of dentures to replace all the teeth they had earlier extracted from it.

Senator ESTES KEFAUVER, Tennessee Democrat, who headed a Senate Antitrust Subcommittee probe of the drug industry in 1959, had offered stiff reform proposals in the first place, but the drug manufacturers' lobby had been too much for him.

This week, when the Senate Judiciary Committee reversed itself in the aftermath of the thalidomide scare, KEFAUVER's reform measures were put back into the legislation.

Those with good memories could not help but recall the wild-swinging campaign conducted against Kefauver by the Pharmaceutical Manufacturers Association, a campaign bolstered impressively by reprints of editorials from American newspapers—most of them, not surprisingly, in the South.

Many of the comments at that time were concerned with the price phase of the Kefauver probe, but the most important result of the investigation was the drug bill drafted by KEFAUVER, establishing safeguards to the Nation's health.

Money, however, not health, was uppermost in the minds of many newspapers in December 1959.

The Harrisonburg (Va.) News Record said: "The drug investigation is part of a 2-year probe of 'administered prices'—prices supposedly set arbitrarily without regard to supply and demand. The bread, steel and auto industries have already gotten the Kefauver treatment."

The Charleston (S.C.) News & Courier said: "Whether the Senate Antitrust Subcommittee, headed by Senator ESTES KEFAUVER, Democrat, of Tennessee, can conduct a fair and sensible investigation of drug prices is yet to be seen. Senator KEFAUVER is a confirmed headline hunter. Whatever he undertakes should be regarded warily."

The Montgomery (Ala.) Journal said: "Senator ESTES KEFAUVER, of Tennessee, is a smart man, but is one of our most easily recognized demagogues. This Senator has previously conducted some investigations which caused headlines but no legislation. He is now conducting another investigation; this time it is the price of drugs and medicines."

The Dallas (Tex.) News said: "It appears that the 59'ers of the political mining camps have discovered that there are votes in 'them thar scandals.' The scandal now alleged by a new Kefauver investigating committee is that the Schering Corp. has made a profit of 7,079 percent on a new drug combination which it recently marketed. The News is inclined to suspect a charge like that because of its sheer dimensions."

"The most patent, the most dangerous and most prevalent markup in American life today is the political markup. What men like ESTES KEFAUVER cost the taxpayer,

compared to what the Kefauvers are worth to the taxpayers, would probably be much more than 7,079 percent."

There were many more similar views expressed, and thoughtfully forwarded to other American newspapers by the Pharmaceutical Manufacturers Association in a not very subtle attempt to promote more of the same.

It would be interesting to know how many, if any, of the same newspapers are now satisfied that—quite aside from the price factor—KEFAUVER's investigation of the drug industry wasn't a waste of time, after all; that the public needs the protection it will belatedly get from the bill approved this week by the Senate Judiciary Committee.

It would also be interesting to know how many U.S. legislators have learned that the practice of closing doors after horses are stolen—as was the case in the thalidomide tragedy—is not a particularly progressive method of operation.

SOVIET SPACE VEHICLES

Mr. KERR. Mr. President, on Tuesday September 4 the distinguished chairman of the House Committee on Science and Astronautics, the Honorable GEORGE P. MILLER, and I, as chairman of the Senate Committee on Aeronautical and Space Sciences, jointly addressed an inquiry to the Administrator of the National Aeronautics and Space Administration. In our letter we referred to published reports that the Soviet Union had tried unsuccessfully to send a space vehicle to Venus on August 25 and to a subsequent denial by a leading Soviet space expert to the effect that the Soviet Union does not withhold information on such failures.

It was our conclusion that once again information of great significance concerning a Soviet launch failure had been widely circulated throughout the world on an unofficial basis and that an official spokesman for Soviet space programs had attempted to discredit this information.

In his reply to the Space Committees of the House and Senate, Mr. Webb quotes a report which he obtained from "appropriate agencies of this Government" stating that the Soviet Union has made two attempts to send spacecraft to Mars and four to Venus and that of these six attempts, only one probe was successfully launched on an interplanetary path.

The whole world can see that once again the Russians have been less than honest in releasing information about their space program. The advantages of our own policy of frank disclosure will be readily seen.

All Members of the Senate will, I am sure, find these letters of great interest. I ask unanimous consent that the two letters be printed in the RECORD at this point for the information of the Members of the Senate.

There being no objection, the letters were ordered to be printed in the RECORD, as follows:

U.S. SENATE,
COMMITTEE ON AERONAUTICAL
AND SPACE SCIENCES,
September 4, 1962.

HON. JAMES E. WEBB,
Administrator, National Aeronautics and
Space Administration, Washington, D.C.

DEAR DIRECTOR WEBB: In the past weeks there have been two reports in the press

which have troubled us as chairmen of the House and Senate Committees on Space.

(1) The Saturday morning newspapers carried an article reporting that the Soviet Union failed in an attempt to successfully send a space vehicle to Venus on August 25, 1962; (2) on August 30, 1962, Dr. L. I. Sedov, a leading Soviet space expert was interviewed by a professor of Tokyo University. The question was asked: "Since the Soviet Union has never made an advance announcement of launchings, some people suspect that there have been unsuccessful launchings in the past; would you tell me the truth, say, confidentially?" Sedov: "The Soviet Union makes an announcement as soon as a rocket is launched. There is no substantial difference between the Soviet Union and the United States in the way of announcement. If there is any failure, it must be known to the world."

It is our clear understanding that the Soviet Union does not announce all of its shots and therefore Dr. Sedov's answer appears to be in conflict with the information in our possession. Dr. Sedov's statement and the report of the Venus shot failure are so patently at variance that we feel it is important that if the U.S. Government possesses any information relative to unsuccessful attempts by the Soviet Union to launch a spacecraft to Venus, or other planetary probes, that this information should be made available to our committees and to the American people.

The world must of necessity admire the remarkable achievements of the Soviet Union in the field of space. A shadow is thrown over the entire space effort through their refusal to admit to failures. The United States is not without its failures, but we operate in a free society and our failures, as well as our successes, are made known to all.

We would appreciate an answer to this letter promptly.

Sincerely yours,

GEORGE P. MILLER,
Chairman, House Committee on Science
and Astronautics.

ROBT S. KERR,
Chairman, Senate Aeronautical and
Space Sciences Committee.

NATIONAL AERONAUTICS AND
SPACE ADMINISTRATION,
Washington, D.C., September 5, 1962.

HON. ROBERT S. KERR,
Chairman, Committee on Aeronautical and
Space Sciences, U.S. Senate, Washington,
D.C.

HON. GEORGE P. MILLER,
Chairman, Committee on Science and Astronautics, U.S. House of Representatives, Washington, D.C.

GENTLEMEN: I agree. The Soviets' broad policy of announcing successes but declining to admit failure does cast a shadow over their entire space effort—remarkable as it might be.

You jointly proposed that if the U.S. Government possesses any information relative to unsuccessful planetary probes by the Soviet Union, that this information should be made available to your committees and to the American people.

In response to this proposal, inquiry was made of appropriate agencies of this Government. The response was as follows:

"The Soviet Union has pursued a vigorous but unsuccessful program to send instrumented space probes to the planets. Thus far, two attempts have been made to send spacecraft to Mars and four to Venus. Of these six attempts, only one probe was successfully launched on an interplanetary path, the Venus probe of February 12, 1961. However, it was only a qualified success because its radio transmission failed after several days, long before it reached Venus. None of the five remaining attempts achieved a suc-

cessful trajectory because of rocket vehicle malfunctions.

"The same mission-planning philosophy and vehicle combination was used on each of the Soviet interplanetary series. A parking orbit technique is consistently exploited, whereby the first three stages attempt to launch the payload into a low earth satellite orbit as in the U.S. Mariner program. After one passage around the earth, the fourth or ejection stage is fired over Africa. If successful, this sends the instrumented probe on a ballistic path to the planets. Had the launching been successful in each of the six cases listed below, the probe would have arrived at Venus or Mars with too high a velocity to have been orbited around either planet. Optimum conditions were chosen for each launching attempted thus far so as to simplify the task of either guidance or performance—or both.

"1. October 10, 1960: A unannounced attempt to send a probe to Mars failed before a parking orbit was achieved. Had this probe been successful, it would have reached Mars in about 230 days.

"2. October 14, 1960: A second attempt to send a probe to Mars using virtually the same trajectory also failed before a parking orbit was achieved.

"3. February 4, 1961: The first attempt to send a spacecraft to Venus was successfully placed in its earth parking orbit, but could not be ejected into its planned Venus trajectory. The Soviet Union announced the launching as a successful earth satellite Sputnik VII and claimed for it a new weight in orbit record of 14,300 pounds. Had this probe been successfully ejected, it would have taken about 105 days to reach Venus.

"4. February 12, 1961: A partially successful attempt to send a 1,400-pound spacecraft to Venus was made on this date. All vehicle stages functioned normally, and the probe was correctly placed on its interplanetary path. The Soviet Union correctly announced that this was the first time that a spacecraft was successfully ejected outward from orbit. The probe took 97 days to reach the vicinity of Venus. The Soviets apparently experienced a failure in the power supply or radio transmitter, and the probe was last heard from at a distance of 4.5 million miles from earth.

"5. August 25, 1962: A third attempt to send a probe to Venus was made on this date. The payload was successfully placed into its satellite parking orbit, but apparently could not be ejected. Had this shot been successful, the probe would have arrived at Venus on about December 7, 1962, ahead of the U.S. Mariner II. It appears that the normal flight time of 112 days for this date was intentionally shortened to 104 days by sacrificing spacecraft weights. This launching attempt has not yet been announced by the Soviet Union.

"6. September 1, 1962: The fourth attempt to reach Venus was also successfully placed into a satellite parking orbit, but could not be ejected. The Soviet Union has not yet announced this attempt nor the presence of the unused components in orbit."

Sincerely,

JAMES E. WEBB,
Administrator.

TRIBUTE TO AN ALASKA LADY

Mr. BARTLETT. Mr. President, September 23 will mark the 90th birthday of one of Alaska's great ladies, Mrs. Margaret Keenan Harrais, of Valdez.

During her 48 years in Alaska she has devoted herself to community and public service. She has possessed always a young spirit in a pioneer land. Her experiences during almost half a century

in Alaska and the contributions she made as educator, U.S. Commissioner, and more recently as deputy magistrate for the State, a position from which she is about to retire, now are told in an excellent article written by a Valdez neighbor, Frances Walker. Mrs. Harrais' inspiring friendship has meant much to Mrs. Bartlett and me, as it has to countless Alaskans and all Alaska salutes her. My wife and I have perhaps especial reason to do so because it was long, long ago that we attended school in Fairbanks, Alaska, when Mrs. Harrais was superintendent there. Her life has been a model of all that is good and decent and constructive. All who know Mrs. Harrais, and those who have heard of her will want to join me in expressing the hope and wish that she will have many happy birthday anniversaries.

I ask unanimous consent to have the article printed in the RECORD.

There being no objection, the article was ordered to be printed in the RECORD, as follows:

MRS. HARRAIS WILL RETIRE (By Frances Walker)

VALDEZ.—Numerous messages of congratulations are being received this week by Mrs. Margaret Keenan Harrais, who will resign as deputy magistrate at Valdez. The resignation will end a career of nearly half a century in Alaska. Mr. Harrais will observe her 90th birthday September 23.

Originally Mrs. Harrais had been expected to end her deputy magistrate's duties this week, but she is continuing for a short time at the request of Superior Court Judge Edward V. Davis. The judge asked her to continue until he is able to name a successor, probably next week.

A schoolteacher by profession, Mrs. Harrais came to Alaska in 1914 at the age of 42 after a successful career in Idaho. In the span of years that followed, she served as first woman superintendent of schools in Fairbanks, administered "the last spanking he ever had in school" to Senator E. L. BARTLETT, Democrat, of Alaska, and drilled a sound foundation of parliamentary law into a freshman legislator, William A. Egan, now Governor of Alaska.

In addition, Mrs. Harrais served as a member of the territorial board of education for 18 years, and after the death of her husband, Martin, in 1936 succeeded him as U.S. commissioner in Valdez. Twice she was offered the U.S. commissioner's post in Anchorage and twice she refused the honor to stay home in Valdez. With statehood, her duties remained virtually the same under the new title of deputy magistrate.

While superintendent of schools in Fairbanks from 1916 until 1919, Mrs. Harrais, as "Margaret Kennan, spinster," wrote with an indelible pencil upon the memories of her pupils. Few could forget the whooping \$10,000 war bond drive in which each of the 200 children enrolled in school purchased a \$50 war bond through his or her own earnings. Parents were asked not to help. Mrs. Harrais set up an employment office at school and assisted the children in finding spare time jobs.

The women of Fairbanks and certainly the editor of the News-Miner, the late W. F. Thompson, could never forget her. She edited the unusual "Women's Edition" of the News-Miner on Thanksgiving eve, 1917, which enlisted the services of 55 women. The newspaper sparked to success a benefit which raised nearly \$4,000 in less than 1 month to sponsor six beds in the American Ambulance Hospital near Paris. Only one bed, at \$600, had been anticipated for all of Alaska, but Fairbanks alone had paid for six.

It was during her Fairbanks stay that Miss Margaret Keenan met Martin Harrais, a University of Washington graduate and an early day prospector of the neighboring camp city of Chena. Harrais, who had made and lost several large fortunes in gold, was keenly interested in statehood and had tossed his hat into the hot, five-pronged candidate field in 1912 which reelected Judge James Wicksham as Delegate to Congress. In 1920, Harrais transferred his mining interests to the McCarthy-Chitina district, taking with him Miss Keenan as his bride.

While he prospected, Mrs. Harrais taught at the tiny McCarthy school with the same devoted interest as she had handled the Fairbanks school system. On the eve of the 1929 stock market crash, Harrais was on the verge of another fortune, this time in copper. The crash not only dashed all hopes for success but with it went their investments and savings in Seattle banks and business buildings.

Undaunted the intrepid pair began anew, first near Cordova, then in Valdez where in 1934 Harrais accepted an appointment as U.S. commissioner. Upon his death 2 years later, Mrs. Harrais succeeded him in this capacity, maintaining an office in the Federal building until it was leveled by fire a few years later.

Since then, the perfectly kept records of the Valdez district, that include the 1912 recordings in the firm hand of Alaska statesmen, Anthony J. Dimond, have been kept in the front room of her modest home. A faded, time-worn shingle with the inscription, "U.S. Commissioner," still hangs over her doorway.

Throughout her years of service as U.S. commissioner and as deputy magistrate, Mrs. Harrais has conducted her office with such integrity that most of those whom she has fined or sentenced have offered a hesitant, respectful "thank you" as they departed.

Honors have come her way. In the latter 1920's, Mrs. Harrais was asked to serve on a 15-member national committee to survey and submit a report on law enforcement for the National Association of Women's Clubs. Her report, written at McCarthy, appeared with such notables of the times as Mrs. H. W. Peabody, Commander Evangeline Booth, and Carrie Chapman Catt.

In 1941, the 1,080 U.S. commissioners in other States and the 72 in Alaska were asked to write a report offering suggestions or criticisms of the U.S. commissioner system. Just two submissions were included in the final report, one from a district judge, and one from a U.S. commissioner, Mrs. Harrais.

Wide attention of the U.S. Interior Department was afforded Mrs. Harrais in 1944 when she engaged in a "merry scrap" with Secretary of the Interior Harold L. Ickes, the "old curmudgeon" and "Lord of Alaska." Her plea for statehood brought a sheaf of replies from well-placed Government officials, including Ickes.

In addition, Mrs. Harrais found time to serve as Democratic territorial committee woman and also president of the Alaska Women's Christian Temperance Union as well as membership in the Woman's Club. In Valdez she worked as chairman of the Valdez Hospital board and took a keen interest in the El Nathan Children's Home. In her spare time she devoted herself to the task each winter of mending the mittens, sweaters and socks for the 100 children of the home. Since the home has been closed she has turned to knitting afghans for disabled soldiers in veterans hospitals and is presently working on her 91st afghan. Folks in Valdez supply the yarn.

It was while she was in Fairbanks that Mrs. Harrais fell into the habit of writing a newsletter home during the week between Christmas and New Years because she was too busy during the school year and her summers were also occupied.

These letters have now arranged themselves into neat chapters of her life, with the most hilarious by far being the account of the "Woman's Edition" of the Fairbanks Daily News-Miner. Pieced together, the chapters give a glowing account of her entire life as well as an accurate history of her pioneer period. The book, if published, could rank in importance with the "Diary of Judge Wickersham."

Mrs. Harrais, of Scotch-Irish ancestry, was reared in Ohio, graduated from Valparaiso University, then engaged in a teaching career in Idaho.

In retirement Mrs. Harrais is looking forward to knitting more afghans for disabled veterans in the winter months, and devoting herself to her garden in the summer. Her interest in Alaska and the world at large will remain the same.

RUSK ASKS OAS PARLEY ON CUBA

Mr. WILEY. Mr. President, the Communist-supported arms buildup in Cuba is a matter of great concern, not only to the United States, but to the Western Hemisphere. For this reason, I urged last week that the Organization of American States—OAS—investigate these arms shipments to Cuba.

I quote from the statement:

The Organization of American States (OAS) has a fundamental responsibility for investigating—and taking action against—this menace to peace.

The OAS, too, I believe, could well (1) redefine its policy on such threatening actions; (2) determine more effective measures against export of communism and aggression from Cuba to the Latin American nations; and (3) reexpress a warning to the European-Asian Communist countries against further arms shipments invasion of the Western Hemisphere.

I am particularly gratified therefore that Secretary Dean Rusk has now proposed to members of the OAS that a foreign ministers' conference be held in September to discuss the possibility of new sanctions against Cuba.

I ask unanimous consent to have an article from today's Washington Post relating to this matter printed in the RECORD.

There being no objection, the article was ordered to be printed in the RECORD, as follows:

RUSK ASKS OAS PARLEY ON CUBA—FOREIGN MINISTERS WOULD CONSIDER NEW SANCTIONS
(By Dan Kurzman)

Secretary of State Dean Rusk proposed to members of the Organization of American States yesterday that a foreign ministers' conference be held late in September to discuss the possibility of new sanctions against Cuba.

Rusk asked the ambassadors of the OAS nations at an "informal" meeting to relay the request to their governments, U.S. sources said. The conference would take place in the United States, as the foreign ministers will be in New York for the United Nations General Assembly session opening on September 18.

The American proposal was made after Rusk explained and expanded on President Kennedy's announcement on Tuesday that Russia is dispatching large shipments of defensive military equipment to Cuba, together with about 3,500 technicians. The diplomats asked many questions about the nature and amount of aid being given, but, U.S. sources said, offered no opinions about the significance of this aid or what might be done about it.

The United States feels that the time is now psychologically ripe for a new foreign ministers' conference in view of Russia's increasing involvement in Cuba.

"This new Russian aid to Cuba could be a mixed blessing," one U.S. official said. "It should serve to dispel any doubts among the other Latin American countries that Cuba is a full-fledged Soviet satellite."

The OAS ousted Cuba from its ranks earlier this year at Washington's behest, but five countries opposed the move for "legal" reasons, weakening U.S. efforts to isolate Cuba completely.

Washington may propose at the projected conference that OAS members cut off all trade with Cuba. Some Latin American countries still maintain commercial relations with Havana.

In the past several months, U.S. officials pointed out, two of the countries that were opposed to an excessively tough policy toward Cuba—Argentina and Ecuador—have broken off diplomatic relations with Havana, a development that should further ease the way toward a strong united anti-Castro policy.

NO ALARM AT SOVIET AID

At the same time, Administration leaders reemphasized that there is no reason for alarm about the Soviet shipments, which they maintain comprise strictly defensive weapons according to what is now known.

One official said there is little meaning in statements like those of Senator KENNETH B. KEATING, Republican, of New York, that the Soviet technicians are in reality soldiers. Not only is there no evidence of this, the source said, but 3,500 common foot-soldiers would probably pose less danger to hemispheric security than 3,500 trained technicians.

U.S. officials stated further that if Russia has refrained from supplying Eastern Europe and Communist China with sophisticated offensive weapons, it probably will not furnish Cuba with such arms.

SOVIET SOURCES AGREE

Soviet sources agreed with this view, maintaining that Russia has no intention of furnishing Cuba with anything but defensive weapons.

"Actually, we are helping to stabilize the situation in Latin America," the Russian sources said. "Cuba will be so powerful defensively that your leaders will have to give up all thought of a new invasion, and think only of peace."

The informants said Cuba explained to the Soviet Union that it had to have sufficient defensive weapons to assure that no new U.S. military venture would be attempted, and Moscow heeded the plea.

In another development, the Czechoslovak Ambassador yesterday delivered a Cuban note to the United States charging that American planes have been guilty of about 20 violations of Cuban airspace. The Cuban diplomat said Edwin M. Martin, Assistant Secretary of State for Inter-American Affairs, promised to investigate the charges.

The Ambassador indicated that the note did not necessarily represent a reply to recent U.S. charges that two Cuban naval vessels fired on a U.S. Navy plane 15 miles off the Cuban coast.

The official Cuban newspaper *Revolucion* said yesterday that President Kennedy's statement on Tuesday was an "inadmissible intervention" in Cuba's internal affairs and "a new step along the path of criminal aggression." The newspaper added, "Don't think, Mr. Kennedy, that Cuba can be intimidated."

Premier Fidel Castro himself has issued no comment on the situation.

Mr. HUMPHREY. Mr. President, if there is no further morning business, I shall suggest the absence of a quorum.

Mr. LAUSCHE. Mr. President, the Senator from Minnesota need not do that. As agreed to last night—

The PRESIDING OFFICER. Does the Senator from Ohio have morning business to submit?

Mr. LAUSCHE. No, Mr. President, not morning business.

The PRESIDING OFFICER. If there is no further morning business to be submitted, morning business is closed.

REVENUE ACT OF 1962

The Senate resumed the consideration of the bill (H.R. 10650) to amend the Internal Revenue Code of 1954 to provide a credit for investment in certain depreciable property, to eliminate certain defects and inequities, and for other purposes.

Mr. LAUSCHE. Mr. President, I shall vote against the pending bill. I shall vote against it for a number of reasons.

If there are to be tax reductions, I should like to support them. But the reductions should be made on the basis, first, of achieving reductions in our expenditures.

I shall vote against the bill because its enactment will, first, reduce the revenues of the Federal Government by \$440 million in the fiscal year 1962; second, enactment of the bill will conflict with the advice and the request of the principal beneficiaries of the bill; third, enactment will prevent consideration of the various items in the bill in their relationship to the over-all tax reduction bill which will come before Congress in the next session; fourth, enactment will place the Government in a position of dealing unequally with different businesses in general, and also with businesses of a similar nature; fifth, enactment will decrease needed revenues, not only in the fiscal year 1963, but also in each year thereafter for as long as the provisions of the bill remain in effect.

With regard to item No. 1 as one of the bases for voting against the bill, I point out that, on page 9, the report on the bill shows that the revenue losses by means of the bill as it came before the Senate would be \$630 million. I have used the figure \$440 million, because there seems to be some controversy as to the exact amount. But the report shows that the loss will be \$630 million.

It is my view that inasmuch as in early January the Treasury Department made available to businesses, through a reformation of the formula on depreciation, the sum of \$1,500 million in the first year, we, by means of the enactment of this bill, contemplate providing another \$630 million, as set forth in the report, or \$440 million, which is my conservative estimate of what the bill will cost.

According to present figures, it is expected that there will be a deficit of \$3,900 million in the fiscal year 1963. This \$3,900 million does not at all include the losses which will be sustained as a result of the enactment of the pending bill. Thus, if we add to the \$3,900 million my figure of \$440 million—reflecting the losses which will be sustained if the

bill is enacted—there will be a deficit of \$4,340 million, to begin with.

But we must move on from that basis. For example, there are pending before the Senate a number of bills, as follows:

First. The stand-by public works bill, which will cost \$1,500 million.

Second. The \$2,700 million Federal-aid bill for colleges, universities, and student scholarships.

Third. The proposed Federal employees pay raise bill, which may provide an increased expenditure of one and a half billion dollars.

Fourth. The youth employment opportunities bill, which initially calls for an expenditure annually of \$240 million.

Fifth. The proposed temporary extended unemployment compensation bill could require outlays of several hundred million dollars.

Sixth. The \$500 million proposal to subsidize local, governmentally operated, transportation systems.

All of these figures forebode, in my judgment, a deficit operation in fiscal 1963 of at least \$6 or \$7 billion.

I submit we cannot suffer that situation in the face of the 26 deficits that we have had in the last 32 years of operation of this Government.

Now I come to my second point, and that is, the passage of the bill will conflict with the advice of the principal beneficiaries of the bill. The A.T. & T. is to be a beneficiary of at least \$75 million. My understanding is that it will be \$130 million. It testified that the bill should not be passed.

The U.S. Chamber of Commerce and the National Association of Manufacturers, having members that would be beneficiaries under the bill, testified that it should not be passed.

I cannot understand how, in the face of that advice and that judgment, given by corporations and individuals who are to be the principal beneficiaries of the bill, we ought to pass it, having in mind the dire impact will have on the fiscal situation of the future.

The AFL-CIO advise that the bill should not be passed, but they are not beneficiaries.

To me it seems that when A.T. & T., the national chamber of commerce, and the National Association of Manufacturers as beneficiaries take the position that it is not in the best interest of the country to pass the bill, we definitely ought not do so.

Point No. 3 is that it will prevent a consideration of the various items in the bill in their relation to the overall tax reduction proposal that will come before the Congress in the next session. That subject has been under discussion. The President has stated that he will recommend that the tax bill passed in the year 1963 be made retroactive as of January 1, 1963.

Mr. Reuther, president of the United Automobile Workers of America, called for a \$10 billion income tax cut. He, however, concentrated the recommendation to be applicable to the lower and middle income brackets.

President Kennedy has said that his tax cut proposal would provide a reduction for both corporate and individual income tax liabilities. This approach was endorsed as recently as July 3, 1962, by the Americans for Democratic Action, in advocating a reduction in the lowest income tax bracket rate to 10 percent from the present level of 20 percent.

If we are to have this subject before us in 1963, with all of its ramifications, I submit that we ought not in 1962 deal with it on a piecemeal basis. The whole context of the problem ought to be brought before the Senate, not only the proposed reduction that is to be made in 1963, but the several aspects contained in the bill now pending before the Senate.

Mr. MORSE. Mr. President, will the Senator yield?

Mr. LAUSCHE. I yield.

Mr. MORSE. I just could not agree with the Senator from Ohio more. If we are to have a tax reform bill, I think it ought to be considered in the light of the totality of the problem. What we are going to do here today is pass a makeshift bill, and a very bad makeshift bill. We are passing it under the great pressure the Senator from Ohio knows is being visited upon every Member of this body to get any compromise we have to accept in order to get some tax label bill passed so Congress can adjourn. Of course, what we ought to do is adjourn, go home, and let the voters react to this proposal, have the election, and then come back in November after the election or in January, and face the total tax reform problem and pass a sound bill, and not this kind of an unsound bill.

Mr. LAUSCHE. The fact that the President submitted a bill early that is different from what we are now acting upon and the fact that he will submit a bill in 1963 clearly indicates to me that to have an intelligent, related approach, the aspects of the bill pending before us and those that will come in 1963 ought to be viewed at one time. What we might want to do in field A will depend upon what happens in field B, C, or D.

Mr. MORSE. Mr. President, will the Senator yield for half a second?

Mr. LAUSCHE. Yes, I yield.

Mr. MORSE. I think it is very wise for the Senator from Ohio to point out for the official record that this is not the President's bill. This is a far cry from what the President of the United States recommended. I shall be very much interested, because I think this bill is going to be passed, in seeing whether or not the President of the United States signs a bill so different from the bill that he recommended, so unjust in many of its particulars, so full of tax escape loopholes.

I say to the President of the United States from my desk this morning, "America will be watching your pen when this bill reaches your desk, and, in my judgment, you owe it to the

Democratic Party and you owe it to the taxpayers of this country to veto this monstrosity when it reaches your desk."

Mr. LAUSCHE. Mr. President, next year there may come before us the question of changes in our tax structure again. There is a discussion about imposing:

First. Federal taxes on interest income from local and State bonds.

Second. The elimination of deductions for State or local taxes.

Third. The prohibition of splitting income by married couples.

Fourth. The elimination of deductions for interest paid on home mortgage loans.

Fifth. Curtailing deductions for medical expenses and for contributions to charitable and similar nonprofit organizations.

Sixth. Tightening of our present tax treatment of income from capital gains.

With these matters coming before us, I submit we cannot intelligently deal with them, and adequately, in the next year, if we have made disposition of items which will have a direct relationship to the separate items I have mentioned.

Now I come to item No. 4. It will place the Government in a position of dealing unequally with different businesses in general and also with businesses of a similar nature. In regard to this item, I have in mind the different treatment which is given to a businessman who wants to construct a building needed for his enterprise, as distinguished from the treatment given to the one who installs machinery and equipment. I also have in mind that the public utilities, contrary to what the Treasury Department recommended, are generally to be allowed a 3-percent tax credit as an inducement for expansion. The bill would not deal equally with the same businesses in a class, nor would it deal on a basis of equality with businesses in general.

Mr. MORSE. Mr. President, will the Senator yield at that point?

Mr. LAUSCHE. I yield.

Mr. MORSE. I am glad the Senator has brought out this difference between the deduction allowance for equipment to operate a business and the denial of that deduction for the building in which the equipment is to operate. Does the Senator agree with me that the equipment cannot operate unless the owner erects a building in which to place the equipment so that he has a place in which it can operate?

Mr. LAUSCHE. That is correct.

Mr. MORSE. The Senator pointed out that the bill contains this unfairness, in that it has one rule for the machinery, but a lack of the same policy for the building itself.

Mr. LAUSCHE. Yes. That is my view of it.

In addition, those who have been alert and who have installed modern equipment as they have gone along will not receive the benefits of the bill. Those who have been slothful will. I submit that is not equality of treatment.

Fifth. The bill would decrease needed revenues not only in fiscal year 1963 but also in each year hereafter. This is not to be a 1-year shot. It is to be a permanent tax bill. It would decrease the revenues each year hereafter so long as these provisions remain in the statutes of our country.

As a summary, I voted against lifting the debt ceiling. I did so because I thought the time had come to begin to pay off our debt, especially in a period of prosperity. How could I in July vote against lifting the debt ceiling and in September vote for a measure which would induce borrowing and create a situation when the administration again would have to come back to the Congress for another authorization to remove the limitation on the right to borrow?

There will be a \$6 billion deficit in fiscal year 1963. There is a prospective \$10 billion deficit, in my opinion, in fiscal year 1964.

This morning I read in the newspaper that the authorities are down in the caverns of Fort Knox hauling out gold. For what? Our international short-term creditors are demanding gold, being unwilling to take our dollars.

Daily in the newspapers is the discussion of the grave problem dealing with out adverse international balance of payments on dollars.

Mr. MORSE. Mr. President, will the Senator yield?

Mr. LAUSCHE. I yield.

Mr. MORSE. The Senator takes note, I am sure, that some of the same countries which want our gold also want our foreign aid, but our administration is not willing to eliminate the millions and millions and millions of dollars of waste in the foreign aid program, which has caused some of us to vote against the foreign aid bill.

Mr. LAUSCHE. During this debate there has been a discussion of the gold situation. There was a time when we had \$24 billion worth of gold. That is now down to about \$16 billion worth; \$11 billion of that \$16 billion worth of gold is earmarked by statute as being the support for our currency and for deposits in the Federal Reserve banks—\$11 billion taken from the \$16 billion leaves only \$5 billion worth of gold available to pay \$20 billion worth of debts, if our creditors demand gold instead of dollars.

For a month there was some sort of tranquillity in the international field, and there was confidence restored that we would not suffer a further attrition of this limited gold possession, but, as I say, I was startled this morning to see that at Fort Knox they are moving out gold, taking it to the banks in New York, where it will be used to pay off the short-term creditors.

If we have a deficit of from \$6 to \$7 billion in fiscal year 1963 and a deficit of \$10 billion in fiscal year 1964, there will be a further loss of gold.

The public does not generally understand the significance of this situation in our Government. In my opinion it is rather generally unmindful of what is happening.

I submit that the bill which is pending before the Senate, if passed, instead of remedying problems confronting our country, would aggravate them.

There is a grave question about the need of providing an incentive to industry and business for the purpose of inducing them to install capital equipment and machinery. An examination of the fiscal situation of corporation will show that money is available. If there is any hesitation about investing, it is because of fear rather than the absence of money.

To summarize, I am in favor of tax reductions, but those tax reductions must be first built upon a reduction of expenditures. There seems to be no purpose to reduce expenditures, and I cannot go along with the proposal. I shall vote against the bill.

RICHARD RODGERS

Mr. JAVITS. Mr. President, we have a New Yorker of whom we are extremely proud—Richard Rodgers, the great composer.

The hearings on various bills for support of the arts which have just been concluded by a special subcommittee of the Committee on Labor and Public Welfare have repeatedly emphasized the tremendous contribution that our artists are making toward enhancement of our national prestige abroad. One man whose music and songs have become world-famous as well as an integral part of American culture is the great composer, Richard Rodgers. Who does not know his songs from "Oklahoma," "South Pacific," "The King and I," "The Sound of Music," "No Strings," and many other famed works from his pen?

The 60th birthday of this talented, great-hearted and much beloved American was celebrated on June 28, 1962, and a luncheon in his honor was held on that day by his friends. I ask unanimous consent to have printed in the RECORD excerpts from the speeches of tribute by Robert W. Dowling; August Heckscher; Robert Moses; Dr. William Schuman, of the Lincoln Center for the Performing Arts; Dr. Peter Mennin, president of the Juilliard School; Bennett Cerf, publisher; Mary Martin; Stanley Adams, president of ASCAP; David Keiser, president of the New York Philharmonic; and Dr. Lawrence H. Chamberlain, vice president and provost of Columbia University, which were so deservedly paid to Richard Rodgers at the luncheon held at the Waldorf-Astoria Hotel, New York.

There being no objection, the excerpts were ordered to be printed in the RECORD, as follows:

Mr. DOWLING. Our guest of honor anticipated this event back in 1946 for in that year he composed and coproduced "Happy Birthday," and I am very privileged indeed to extend to him on behalf of Mayor Wagner and the 8 million people of our city our gratitude for what he is and our affectionate best wishes.

AUGUST HECKSCHER. Now, I am very proud and happy to be able to carry to this occasion a message from the President of the United States:

"I am delighted to join with you all in greeting Richard Rodgers on this significant birthday. He has written the music which the generation sings, songs of land and sea, of war and peace, reminding us in charming ways of the strange and wonderful experience it is to be an American in the 20th century. The musical theater in our country has reached new heights in considerable part due to his gifts. With all of you, I wish for Mr. Rodgers many more years and many more songs for our delight.

"JOHN F. KENNEDY."

There is really nothing that I can, or perhaps, should add. When we think of Dick Rodgers we think, do we not, of an inextinguishable and irrepressible quality about the man, music that comes from him as naturally as water bubbles up from a spring.

For such a man a birthday cannot be, in the end, a terribly significant event. The pattern of his life seems to be that of a radiance which moves outward from the center, not that of a journey marked by rather dreary milestones with its beginnings and its ends, with its ups and downs.

And yet, in spite of all that, it is wonderful, it seems to me, that we are having this party, which brings us all together, and I cannot but express my own delight that I am able to take part in the tribute.

In speaking of Mr. Rodgers, I could speak of the hours of wonder I have had along with millions of others, due to his music. I could speak, more solemnly, of what he has meant to the American theater here and across the world.

ROBERT MOSES. A tired public official does not regard the theater as a place of wrath and tears. He goes to Broadway not for torture and catharsis but to be transplanted into a world of melody somewhere between grand opera and Viennese waltzes. This is the domain where Dick Rodgers, working with Larry Hart, then with Oscar Hammerstein and now on his own, has reigned supreme.

New York put its OK on "Oklahoma," and a western State anthem in the authentic American idiom was born. And so it went until the conviction grew that in this composer there was more than a touch of the universal.

The yodeling of funereal Wagnerian Valkyries is for the aficionados. The tired husband cannot endure, even to support his wife's claims to culture, the throaty bellowing of vast pachyderms emoting in a foreign language, and so he surreptitiously closes his eyes and hopes he won't be caught napping.

But this barbarian is wide awake at Dick Rodgers' shows, chuckles, hums, marks time, and helps the conductor direct the orchestra.

Dick Rodgers, we salute you. Millions of feet will continue to beat time to your tunes when the works and voices of more pretentious men, who strut and fret on the stage today are mercifully forgotten.

Thank you for preserving our optimism, our faith and our very sanity in a bewitched, bothered, and bewildered world, and for giving us so many moments of unalloyed happiness.

Dr. WILLIAM SCHUMAN. I like to feel that I am not a freak because I neither sleep at Rodgers' plays nor at Wagnerian operas, nor at symphony concerts or concerts of chamber music or choral music or any other kind of music.

Dick Rodgers is a musical anti-isolationist. He has done more than almost any other man I can think of in the field of music to break down this kind of false isolationism to which the Commissioner made such witty and feeling reference.

I would say that, although I have been asked to speak for music, I can really only speak for myself and those of my colleagues whom I see in the audience, and many of

job of peacekeeping and policing the country and into the constructive job of economic and technical assistance.

Once this transition is accomplished, we will have made a major contribution toward lasting peace and security, not only in Africa but throughout the world.

This is what we hope will be achieved through the United Nations Congo plan of reconciliation. And this is why we are giving our full support and best efforts toward making this plan succeed.

We hope you will join us in support of this endeavor.

HIGHER EDUCATION AND ITS RELATIONSHIP TO ECONOMIC GROWTH

Mr. MANSFIELD. Mr. President, will the Senator from Minnesota yield me 1 minute?

Mr. HUMPHREY. I yield 1 minute to the Senator from Montana.

Mr. MANSFIELD. Mr. President, we all recognize the ever-increasing importance of college education and post-graduate work in this advanced technical age in which we live. The need for advanced education is not only limited to a person's advancement but there is also a direct relationship between education and economic growth. This is a subject recently discussed by the able president of Montana State College, Roland R. Renne, in an article he prepared for the September edition of Montana Education, the official publication of the Montana Education Association.

Mr. President, I ask unanimous consent that the article may be printed at this point in the RECORD.

There being no objection, the article was ordered to be printed in the RECORD, as follows:

HIGHER EDUCATION AND ECONOMIC GROWTH (By Roland R. Renne)

Quality education and research are essential to the future sound growth and prosperity of Montana and the Nation. The best proof of this is our record to date. There is no doubt that great natural resources, a capitalistic form of enterprise, freedom of trade and movement of products, services, and people among the 50 States have all contributed significantly to our record of growth and power. But these three factors are not unique with America.

What is unique and undoubtedly the most important single factor accounting for our progress is our system of universal free public schools. The emphasis on individual attainment and the opportunity to develop one's abilities to the fullest possible extent through publicly financed schools from kindergarten through college have raised the standards and increased the wants of our people, and have at the same time provided the means of fulfillment by increased productivity and invention.

The record is perhaps best exemplified in the field of agriculture. Just 100 years ago, the Congress of the United States created the Department of Agriculture and, by passage of the Morrill Act, authorized the establishment of at least one land-grant college of agriculture and mechanic arts in each State. Grants of land for the endowment of such colleges were authorized and annual appropriations made to meet part of the costs of instruction. Later (1887) an extensive system of agricultural research through experiment stations was set up to uncover new scientific facts and develop improved methods of production and mar-

keting agricultural products. Still later, in 1914, a system of adult education was established and financed by joint contributions of Federal, State, and county governments. This cooperative extension service takes the latest discoveries of the agricultural experiment stations and passes them on to farm and ranch operators who put them to practical use. In Montana, the main station is at Bozeman and the seven branch stations are spread over the State to meet the varied soil, weather, and other production influences peculiar to the different areas of Montana.

So effective has been this three-way system of resident instruction, research, and adult education that today American agriculture efficiency and achievement are the envy of the entire world. Only 8 percent of our population is required to produce all the food and fiber we need, with considerable to spare to help feed and clothe people in other lands. In some countries, over 90 percent of the population is required in agriculture and even the more advanced nations have about half of their labor force engaged in farming. Only one-fifth of our income is spent for food while in most other leading nations 40 to 50 percent is required.

This progress in agriculture has released millions of people from farming to do other things and has made possible our highly diversified, industrialized, and powerful Nation. In other words, we can have a high standard of living and at the same time spend billions on military strength. We can and do have both "guns and butter."

If there ever was a convincing record of the contributions of quality higher education and research to economic growth, it is plainly before us in what has happened and is happening in American agriculture, and Montana is high among the States in the dynamic growth and progress of its agriculture.

It seems strange, therefore, in the face of such convincing evidence, that the percentage of our national income spent on education, both public schools and higher education, has declined steadily for more than a decade and that Montana public education and research are suffering a serious dollar crisis. Today, less than 1 percent (nineteenths of 1 percent) of our gross national product is spent on higher education and only 3 percent on elementary and secondary education. The figures for Montana are quite comparable.

In the meantime, business and industry have stepped up their expenditures for research and development. In fact, in American industry competition has become "a race in innovation." Talk with businessmen in almost any field and you find them convinced that growing research budgets are a necessity for companies who want to survive. They say "Just stop your research for a year while your competitors keep right on. You'll be dead. Research fosters steady growth even in times of recession."

In the electronics industry, for example, it is estimated that products unknown 10 years ago account for 80 percent of its current sales. Chemical companies expect 60 percent of their 1975 sales to be based on new products which are now in the introductory stages or still to be invented. The National Science Foundation reports that during the decade 1945-55 the rate of growth of industrial research was about 14 percent per year, greater than that of any other major economic activity.

The scientists for this expanded research program and increased economic activity come from our college classrooms and laboratories. If the job of the colleges is poorly done, it will result in our inability to maintain an effective rate of growth and cause a serious lessening of our economic and national strength.

For the past several years, we have been living with shortages of chemists, physicists, engineers, and other physical scientists. For many years, we have known that we need more doctors and other medical personnel, including nurses, than have been available to maintain a desirable standard of health services. Shortages of qualified school teachers have constituted a serious problem since World War II, especially in the fields of mathematics and science. The expansion of college enrollments, with prospects of even greater numbers just ahead, has given us fair warning that there will soon be acute shortages of competent college and university teachers. We have also been hard pressed to provide adequate numbers of skilled workers and technicians in many fields.

This demand for an ever-growing number of scientifically educated and trained people seems to be built into our American system of free enterprise and economic growth. The availability of trained manpower hastens economic growth; its absence acts as a brake on advancement. There would be compelling reasons for our concern over a shortage of trained manpower, even if the Communist threat to freedom did not exist.

The investment we make in education is the heart of the solution to our manpower needs. Strengthening and improving educational institutions is the most important means of securing adequate numbers of highly trained people needed in numerous fields of activity. Aside from health, education constitutes society's major investment in people. We have reached the point where education must be recognized as an investment in quite new and different terms.

Whenever private enterprise or a business corporation sees an opportunity to expand, to increase its output and make a larger profit, it does not hesitate to increase its capital investment and enlarge its plant. Investment proceeds automatically by plowing back funds from earnings into capital expansion. Where such earnings are inadequate, borrowing occurs either through banks, issuance of bonds, or issuance of stock, but investment in people (education) is largely undertaken by the community from public funds.

Support for this public investment, of course, is dependent upon decisions by taxpayers or their elected representatives to transfer funds from other uses. However, the process by which the investment need or the relative investment needs are weighed is not automatic. Frequently, it is a much debated controversial subject because there are many who through ignorance, selfishness, misinformation or for other reasons, are not convinced that a tax dollar can be spent as efficiently for public investment as a dollar can be spent in the private sector of our economy. The result, too often, is that the tax cost is not related to benefits received, immediately or over the longer pull, but is branded as wasteful, so the public investment is not made.

The hour is late. Indeed it is later than we think. In a year or two much larger numbers of Montana high school graduates will be knocking at our college doors to be prepared for more effective service in our highly scientific and technological age. If our Montana economy is to grow and develop as it could and should, her leaders in business, agriculture, labor, and government must see to it that her higher educational institutions—the university system—receive adequate financial support. Only with adequate financial support can these institutions render services vital to growth and development.

The degree to which this responsibility is met will determine, more than any other single factor, the degree of Montana's future economic and cultural progress.

EXPRESSION OF THANKS TO SENATOR MORSE, SENATOR ENGLE, AND SENATOR KEATING

Mr. MANSFIELD. Mr. President, at this time I wish to thank the Senator from Oregon [Mr. MORSE], the Senator from California [Mr. ENGLE], and the Senator from New York [Mr. KEATING] for the consideration they showed last night in allowing the Senate to proceed to the third reading of the tax bill before they made their speeches and remarks. They held them in abeyance until that was done; and I thank them for the consideration they have shown.

REVENUE ACT OF 1962

The Senate resumed the consideration of the bill (H.R. 10650) to amend the Internal Revenue Code of 1954 to provide a credit for investment in certain depreciable property, to eliminate certain defects and inequities, and for other purposes.

Mr. HUMPHREY. Mr. President, I wish to renew my request of a few minutes ago for unanimous consent that there be a quorum call, and I call it to the attention of the minority leader. I ask unanimous consent that there now be a quorum call, and that the time required for it be divided equally between the two sides.

The PRESIDING OFFICER (Mr. BURDICK in the chair). Is there objection? Without objection, it is so ordered.

Mr. HUMPHREY. Then, Mr. President, I now suggest the absence of a quorum.

The PRESIDING OFFICER. The clerk will call the roll.

The Chief Clerk proceeded to call the roll.

Mr. HUMPHREY. Mr. President, I ask unanimous consent that further proceedings under the quorum call be suspended.

The PRESIDING OFFICER. Without objection, it is so ordered.

Mr. HUMPHREY. Mr. President, I understand the Senator from Wisconsin [Mr. PROXMIRE] would like to speak on the tax bill, and I will yield 15 minutes to him.

Mr. PROXMIRE. I thank the Senator.

The PRESIDING OFFICER. The Senator from Wisconsin.

Mr. PROXMIRE. Mr. President, any revenue measure which comes to the Senate or the House should meet, above all, the standard of justice and equity. It is important that it provide adequate revenues; but justice and equity should be the prime criteria for judging any revenue measure.

The tax bill before the Senate as it emerged from the administration was designed to do a number of things, but two primarily: First, to stimulate investment in plant and equipment; second, to plug a number of loopholes in our tax laws. As designed by the administration, it was expected to increase revenues by some \$500 million. This was the estimate of the Treasury.

The kind of tax bill now pending does not meet either the criteria of justice

or the criteria of revenue adequately. Furthermore, it will not achieve either of the two purposes for which the administration designed it. It will not stimulate investment. It will not significantly plug loopholes.

Mr. President, last year our Government's mammoth deficit was some \$6 to \$7 billion. In the coming year virtually everyone expects that we will suffer another heavy deficit. Under these circumstances it is unwise for the Congress to adopt a revenue measure which would sharply reduce revenues.

This is especially true in view of the fact that only a few weeks ago the administration acted to modify depreciation schedules to reduce, in effect, the tax liability of American business by \$1½ billion. This was a wise and necessary action. But it means that in the present year the big deficit previously predicted will be increased another \$1½ billion.

RED-INK BILL

The bill which is before the Senate cuts even deeper into red ink. The \$500 million surplus which the bill would have provided, as originally designed by the Treasury and the administration, now turns out to be a \$700 million revenue loser.

Mr. President, I want very briefly to run through the reasons for that revenue loss and point out how thoroughly and completely unjustified each of these cuts below administration recommendations is.

The issues I am going to discuss have to do with the actions taken by the Congress in contradicting the position originally taken by the administration and the President.

UTILITY GIVEAWAY THOROUGHLY UNJUSTIFIED

The administration recommended that utilities not be given an investment credit. Secretary Dillon made a very comprehensive study, one of the finest and most scholarly studies I have read, showing that the investment credit could not possibly increase the investment by utilities in plant and equipment.

I comprehensively documented the case against this utility giveaway by putting into the Record two superlative scholarly studies nailing the case to the mast in detail. The studies were made by higher competent economists. The credit for utilities is going to cost the Government of the United States \$225 million, and the testimony is overwhelming on the part of competent economists who have studied the subject that it could not increase the investment by utilities in plant and equipment. As a matter of fact, not only economists, but competent businessmen who are closest to this situation, even though they would benefit greatly, have said so. The vice president and comptroller of the American Telephone & Telegraph Co. testified that in the experience of this great company this investment credit provision was unwise and would not increase the A.T. & T. investment in plant and equipment, although A.T. & T. would get a \$75 million annual windfall, one-third of all the benefits going to utilities.

ADMINISTRATION'S PLUGGING FOREIGN INVESTMENT LOOPHOLE PLUGGED

In the second place, the Senate acted to eliminate the action which the administration recommended which would have ended the deferral of taxes. And in its other action on foreign investment it reduced by \$175 million the revenues designed to be obtained originally by the administration.

GAS PIPELINE GIVEAWAY

In the third place, probably the least justifiable provision in the bill is that gas pipelines are given, not an investment credit of 3 percent as all other utilities are given, but an investment credit of 7 percent. Of course, the administration recommended that gas pipelines be given no investment credit whatsoever, and Secretary Dillon was very specific in pointing out that there was no excuse at all to give gas pipelines an investment credit, since they build their pipelines on the basis of certificates of convenience and necessity, and since they have been expanding very rapidly indeed, and every pipeline is going to be built without any relation to their corporate income tax or any modification of their corporate income tax.

BUSINESS EXPENSE LOOPHOLE KEPT OPEN

In the fourth place, Mr. President, the Senate acted to refuse to close business expense loopholes significantly. It acted against the recommendations of the administration, and it acted in doing so in a way that loses virtually \$200 million of revenue which otherwise would have flowed to the Treasury.

As the Senator from Tennessee [Mr. GORE] pointed out so eloquently, this was not only a matter of raising revenues which should be raised and of having people pay taxes which should be paid, but also a very real and definite moral issue. One of the most unfortunate aspects of American economic life is the expense account racket, which we all recognize. It is one of the most morally degrading aspects of American life. Businessmen themselves in many cases recognize it is wrong, but Congress has decided not to take effective action against it, although there was a minor improvement in the law.

TWIN CITIES RAPID TRANSIT GETS FREE-VETO-PROOF RIDE

In addition to these actions, the Senate insisted on loading onto the tax bill special interest legislation for the Twin Cities Rapid Transit System. One company is to be given relief in the tax bill, a relief which the President refused to approve in a bill submitted to him last year. In fact, the President specifically vetoed the bill because it was unjustifiable. The Senate acted to put that relief for the Twin Cities Rapid Transit System onto the tax bill to make it vetoproof.

Mr. President, any Senator who conscientiously acts on the proposed legislation should be inclined to vote against the bill if only on the grounds of the special interest legislation for one company, and the precedent it would provide.

BILL SUBSIDIZES BUSINESS LOBBYING

In my judgment, the worst provision in the bill is the subsidizing of lobbying of the Congress, of State legislatures, and of city councils by business through the Federal Government, in effect, paying half the cost of that lobbying. This will be true because this bill authorizes corporations for the first time to deduct lobbying expenses in computing taxes. I think all of us who have served in State legislatures or in the Congress recognize that lobbying by business groups is very intense and very effective. Mostly, that lobbying is informative. I see no reason why it should be discouraged. As a matter of fact, there is a constitutional protection for lobbying. But I cannot see any justification for Congress writing into the tax laws a subsidy, in effect, for corporations to engage in this kind of lobbying, particularly in view of the fact that it would give a special advantage to those who seek pecuniary advantage out of legislation, as opposed to those who stand up to fight for conviction, for ideals, and for principles, but not so that they will get particular financial advantage from legislation.

Mr. President, in the Washington Post and Times Herald there was published this morning a very excellent editorial commenting on the tax bill, indicating why the tax bill should be rejected. I quote briefly from that editorial:

Faith in the processes of democratic government is hardly likely to be enhanced by the Revenue Act of 1962 which is about to be passed by the Senate. A week ago it was fair to charge that the administration's original proposals had been mutilated almost beyond recognition. In the interim the Senate in a veritable fit of perversity passed amendments which will make our system of personal taxation more inequitable and more difficult to administer than ever before.

In tracing the process of transmogrification, it is necessary to go back to President Kennedy's tax proposals of April, 1960. At that time he outlined measures designed to close tax loopholes which covered interest and dividend income, savings institutions, expense accounts and foreign corporate subsidiaries. His loophole-closing measures would have added \$2.3 billion to Federal revenues, thus more than offsetting the investment-credit loss of \$1.7 billion. But in their passage through the House and the Senate Finance Committee the loophole-closing provisions were systematically weakened or eliminated and the bill that reached the floor of the Senate, shorn of its dividend-interest withholding provision, would have resulted in a net revenue loss of nearly \$700 million.

SENATE REDUCED ADMINISTRATION'S RECOMMENDATION FOR PLUGGING LOOPHOLES BY A WHOPPING \$1.2 BILLIONS

In that connection I point out that with the \$600 million of loss through the knocking out of the withholding provision; with the \$225 million of loss through the provision for investment credit for utilities, which was opposed by the administration; with the \$190 million of loss as a result of the Senate failing to follow the administration's proposals for eliminating entertainment as a business expense; with the \$175 million loss through failing to follow this administration's recommendation to tighten up the evasion in foreign invest-

ment; there is a total of \$1,200 million of provisions recommended by the administration for loophole closing which were rejected by the Senate.

This involves \$1,200 million, ignoring the fact of the Dirksen amendment and ignoring the Douglas depletion allowance amendment or the Williams of Delaware depletion allowance amendment.

Mr. President, I quote further from the editorial:

But the Senate was not satisfied with the handiwork of its Finance Committee and it proceeded to pervert as well as attenuate the remains of what had been a good tax bill. By a vote of 51 to 13 it joined the House in overturning a 1959 Supreme Court decision which declared that business-lobbying expenditures are not tax deductible. * * * The * * * measure will, according to Senator DOUGLAS, "legitimize tremendous expenditures by special interests to affect legislation" while not providing comparable treatment to lobbyists "for the general interest."

NOT A KENNEDY OR BYRD BILL—A KERR BILL

Mr. President, I do not think anyone, on the basis of the Senate's record, could call this a "Kennedy bill." It certainly is not a Kennedy bill. No one could call it a "Dillon bill." It has very little identification with the recommendations made by the Secretary of the Treasury. No one can call it the "Byrd bill." I would expect the chairman of the Finance Committee to vote against the bill. For the first time in 30 years, he filed minority views.

This is the bill of the distinguished Senator from Oklahoma [Mr. KERR], the very able uncrowned king of the Senate.

In this connection, Mr. President, I should like to quote from a telling column published in the New York Times this morning entitled "A First Reader on Washington for Children of the Space Age":

Look, Jerry, look. See the New Frontiersman. Look and see the New Frontiersman run. He is running to the Capitol to save the program. Be careful. Do not get in his way or he will have to step on you. Why does the New Frontiersman have to step on people who get in his way?

Because, little children, he is pragmatic. He is tough minded. He is hard nosed. Look at his hard nose. See his tough mind. Is he not a splendid sight? He will soon teach Senator ROBERT S. KERR to leave the program alone. It is lucky that you are not Senator ROBERT S. KERR or you would have to look the New Frontiersman in the eye and feel his hard nose.

But what is this? Senator ROBERT S. KERR is throwing the program out the window. See the medicare bill fly away. See the tax bill fly away. See the trade bill scattered on the air. This will make the New Frontiersman very cross, will it not? Poor Senator ROBERT S. KERR.

Look, the New Frontiersman is advancing. Why is the Senator not running? Why is he smiling? Why is he tweaking the New Frontiersman's nose? Look, he is giving the New Frontiersman a new program. It is the Senator Robert S. Kerr program. The New Frontiersman is accepting it. He is smiling at the Senator and shaking the Senator's hand. What a splendid sight. This is democracy in action.

Why did the New Frontiersman not stop the Senator from throwing the President's program out the window? Children, you have much to learn. Remember, the New

Frontiersman is pragmatic. Stand back. Stand back. He is leaving for the White House. You must not smile at him or he will ask if you think there is something funny about trying to run a country.

The PRESIDING OFFICER. The time of the Senator from Wisconsin has expired.

Mr. PROXMIRE. Mr. President, I ask that I may have 2 minutes more.

Mr. MANSFIELD. Mr. President, I yield the Senator 2 additional minutes.

Mr. PROXMIRE. Mr. President, the fact is that this is a special interest tax bill. It is a tax bill for the gas interests. It is a tax bill for one company in Minnesota. It is a tax bill for the tax dodgers overseas and for the business expense tax dodgers. It is a tax bill that will increase our deficit, not decrease it. It is a tax bill which will provide no justice and no equity for the little taxpayer. It will provide no relief whatsoever for the little taxpayer, although it will reduce revenues by some \$700 million.

Mr. President, in conclusion, it seems to me that the one criterion on which any revenue measure must pass, if it is to be approved by the Congress, is that it be just and equitable.

Well justice and equity lost. Why? Justice lost because special interests care very deeply about tax legislation. They fight for it. They work for it. They spend time and effort—thousands of hours and huge sums—lobbying the public and the Congress.

They have able and diligent representatives in the Congress who know how to fight for their interest.

The special interests won because they cared—deeply cared. On the basis of any evaluation of the measure that comes before the Senate it is not just, it is not equitable; it is discriminatory and unfair. Mr. President, it should be rejected. For that reason I intend to vote against the tax bill. I yield the floor.

Mr. KERR. Mr. President, will the Senator from Montana yield to me 10 minutes on the bill?

Mr. MANSFIELD. I yield 10 minutes to the Senator from Oklahoma.

Mr. KERR. Mr. President, I have been very interested in the remarks of the Senator from Wisconsin. I wish to congratulate him on the high quality of the reading material he has been investigating and going over. I have been going over some of the reading material that he has made available to Senators. Day before yesterday, in supporting his amendment to strike from the bill the investment credit provision for regulated utilities, he placed into the RECORD about 22 pages of material which, I am frank to confess, Mr. President, I do not understand.

The Senator is one of the most renowned advocates of economy in the Senate. I am sure that his putting into the RECORD the material at a cost to the taxpayers of nearly \$2,000 showed marked restraint on his part, because he could have put in \$5,000 worth of material. When he put in only about \$2,000 worth, he was very moderate and entirely consistent with his advocacy of rigid economy.

He put into the RECORD a study which, he said, was a very scholarly study. Perhaps it is. The Senator from Oklahoma is not a very scholarly person and therefore would not be expected to recognize the attributes of scholarly writings when he sees them. The study is by Mr.—I presume it is a mister, though the sex is not stated—A-v-r-a-m K-i-s-s-e-l-g-o-f-f and Mr. F-r-a-n-c-o M-o-d-i-g-l-i-a-n-i. I notice that some of the footnotes referred to I. Friend and J. B-r-o-n-f-e-n-b-r-e-n-n-e-r, F. Modigliani and O. H. S-a-u-e-r-l-e-n-d-e-r, R. Eisner, and T. H-a-v-e-l-m-o.

Mr. President, I think they are economists. Since the Senator from Oklahoma is not an economist, he would not be expected to understand such things.

But the algebraic equations in the material inserted in the RECORD are what particularly intrigue the Senator from Oklahoma. For example, on page 17366 of the RECORD I noticed equations based upon the period 1924-41. The economic study of the Senator from Wisconsin was purportedly made in 1957. But I think it was an anthology of either mythology or antiquity.

On page 17366 I read that—

$$(I/A)_t = 18.9 - .162(II^r/A)_t + 62.9_t$$

Then appear some other algebraic figures with which the Senator from Oklahoma is not familiar. A plus sign over a minus sign appears. The Senator from Oklahoma has always thought that plus/minus equals minus. I do not know whether that is true in this case or not, but I rather suspect it is.

We then find:

$$\begin{array}{cc} (\pm .805) & (\pm 42.7) \\ R = .22 & S = 122.0 \end{array}$$

Then just below that equation I discover, to my mystification but delight, because I am curious—I love to learn things even if I do not understand them—that—

(2)

$$(I/A)_t = 297 - .909(II^r/A)_{t-1} + 61.7_{t-1}$$

I am mystified because in the equation above we had discovered that—

$$(I/A)_t = 18.9 - .162(II^r/A)_t + 62.9_t$$

Down beneath that equation I discovered, according to the printed expression, that the same designation, that is, $(I/A)_t$ equals 297 minus .909—something.

As I go through the study and observe the equations, I come to the statement,

This idea has been aptly developed by H. B. Chenery in "Overcapacity and Acceleration Principle," *Econometrica*.

The first time I looked at the expression I thought it was Metrecal. But I knew it could not have been because Metrecal had not been discovered when this knowledge first dawned upon whoever it was that the Senator from Wisconsin was quoting.

Then I thought it might mean "egocentric." But I know that nothing the Senator from Wisconsin would put into the RECORD could possibly be such or indicate such.

But I was glad that the idea was aptly developed by Mr. Chenery. If it had been a "c" it might have been chicory,

and I know what that is. That is something that one who lives in the South puts into his coffee if he wants to ruin it. I am not right sure, but I believe if this thing that he put into the RECORD was not ruined when he put it in, then it has been accomplished for him.

I notice that:

$$AP_t^{t+1} = (I+i)^2 P_{t-1}$$

A man who can figure that out and put it in the RECORD for the benefit of posterity has rendered a service that probably no other man in the Senate could render.

It distresses me that I am unable to evaluate the extent of the service. It even distresses me that there might be other Members of the Senate who are unaware of the extent of the service this renders. I am sure that it is a service, or the Senator from Wisconsin would not have done it.

Then I read:

This leads by substitution in equation (3) to:

$$\begin{aligned} I_t &= a [P_{t-1}(1+i)^2/S_{t-1} - (P/S)_t] \\ &= a(I+i)^2 [P_{t-1}/S_{t-1} - I/(I+i)^2 (P/S)_t] \end{aligned}$$

Right now I would suggest that the Public Printer use bigger type; or, if the Senator from Wisconsin is going to put this sort of thing in the RECORD, he should furnish Senators with magnifying glasses.

Mr. MANSFIELD. Mr. President, will the Senator yield?

Mr. KERR. I yield.

Mr. MANSFIELD. I would suggest most respectfully that the Senator from Oklahoma join the Senator from Pennsylvania [Mr. CLARK], who is urging that a new format be adopted for the CONGRESSIONAL RECORD. The Senator from Pennsylvania would also include cartoons and illustrations, and so forth.

Mr. KERR. Cartoons could not compete with this, because I could look at cartoons and get some idea of what the cartoonist had in mind. I am unable to conceive what the perpetrator of this thing had in mind.

The PRESIDING OFFICER. The time of the Senator has expired.

Mr. MANSFIELD. I yield 2 additional minutes to the Senator from Oklahoma.

Mr. KERR. Exploring through the ramifications of these algebraic equations has given me more pleasure than when I flunked Greek. I want to say about Greek, however, that there is a possibility that a man of limited intelligence can eventually learn something about Greek. On the other hand, if the Senator from Wisconsin understands what he put into the RECORD he has missed his calling. He ought to be out at CalTech directing the space probe that is on its way to Venus now. Instead of correcting its line of flight at 100 million miles out in space, to deflect it from its course, which would have taken it within 250,000 miles of Venus, with a correction calculated to get it within 9,000 miles of Venus, a man with the ability to understand these equations could very easily get the space probe within a quarter of a mile of Venus and never even touch a mountain peak

or fall into a crater which is terrible, because it might be better if he did.

In view of the fact that the taxpayers have paid nearly \$2,000 to put these algebraic equations into the RECORD, so that Senators in their spare time might conjure them, and so that posterity through all the years to come might be mystified or enthralled or captivated by them, I wish to express whatever is due the Senator from Wisconsin for having put them in the RECORD, because never again will the Senator from Oklahoma need to be bored or uninterested or minus something to captivate his imagination or to challenge his attention. Who knows—perhaps some day in the occupancy of this earth by the Senator from Oklahoma he may have a small portion of that kind or degree of intelligence which the Senator from Wisconsin possesses, which permitted the Senator from Wisconsin to make available to the Senator from Oklahoma and others this delightful, fascinating, mysterious, and unintelligible conglomeration of figures by a man whose name I spelled but could not pronounce, in order that all this may be available to the Members of the Senate to help them arrive at the conclusion as to how to vote on the pending bill.

Mr. MANSFIELD. Mr. President, I yield 15 minutes to the Senator from Pennsylvania.

Mr. CLARK. Mr. President, I thank the majority leader. I now yield to the Senator from Wisconsin.

PROXIMITY REPLY TO KERR ON SCHOLARLY WORK IN RECORD

Mr. PROXIMITY. I know the Senator from Pennsylvania has only 15 minutes, and that he would like to deliver his speech.

In response to the Senator from Oklahoma I merely wish to say that the Senator has made a typical response to my speech, which wholly ignored the merits of what I had to say about the tax bill.

The Senator spent all his time deriding scholarly studies I put into the RECORD. These were studies which had been cited by the Secretary of the Treasury as definitive and authoritative. They showed that in the utility industry and in the telephone industry, demand rather than cost elements determined investment in plant and equipment. The only way the investment credit could possibly stimulate investment would be by working through the corporation income tax, that is on cost.

It is perfectly clear, in view of the very comprehensive study to which the Senator from Oklahoma has referred, and that I placed in the RECORD, that it is not possible for investment to be stimulated by reducing utility costs. Mr. Kisselgoff and Mr. Modigliani, two very eminent economists who developed cost studies of this kind, are recognized economists throughout the world, and are extremely able. Mr. Paul Clark is another eminent economist who contributed excellent work. Both studies are recognized as definitive studies in this field.

It is a sad day in the Senate when a Senator cannot put into the RECORD

definitive and authoritative works in economics by recognized scholars in the field, without that work being sarcastically ridiculed, demeaned, and held up to scorn because the subject is complicated. Admittedly this is the kind of writing that takes hard work to understand.

While I have respect for the general intellectual capacity of the Senator from Oklahoma, the Senator from Oklahoma it is true may not be able to understand some of the complex economic studies without a great deal of effort.

On the other hand, I think there are Members of the Senate, a number of them on both sides of the aisle, who may be able to understand this more readily than can the Senator from Oklahoma.

Mr. President, should we follow a policy in the Senate of introducing nothing into the RECORD which the Senator from Oklahoma cannot understand that might reduce the size of the RECORD. But does it mean that he becomes the Senate's censor? I certainly think it was worthwhile to put this tremendously important and authoritative work into the RECORD, because these studies bore directly on my amendment. They were completely relevant in support of my position and in opposition to a provision that would have cost the Government not \$2,000, but \$225 million. In this kind of fight on the floor of the Senate to save the general taxpayers \$225 million, it is well worth calling scholarly work to the attention of all Senators.

I thank the Senator from Pennsylvania for yielding to me.

Mr. CLARK. Mr. President, this is indeed a sad day for the Senate. We are about to pass a bill which I hope will not bear the name of any Senator. I would like the names of all Senators to go down in history as eminent and able men whose names are affixed only to legislation of which they can be proud in the long course of history.

Searching around for a name for the bill, I have concluded that it might be just as well to call it the "tax dodger's delight." I think that would perhaps be better than to try to tag its authorship on any particular Senator, because so many Senators during the course of the long and sometimes tedious debate on the bill have played their fair share in earning for it the title which I suggest.

The original administration tax incentive and reform proposal would, according to the Treasury Department, have increased annual revenues by \$768 million. That was the kind of bill I hoped to be able to vote for and see enacted. One of my purposes during my term of office in the Senate has been to do what I could to eliminate inequitable and unjust tax loopholes through which large sums of money were seeping day by day, month by month, and year by year. This constant seepage resulted from inequitable loopholes, taken advantage of by those who, while we may not want to charge them with the harsh term "tax dodger," nonetheless were taking every possible advantage of tax avoidance made possible by these loopholes. In large part they not only have not been

closed, but, in some instances, have been widened. In at least one major instance, that of lobbying expenses, a new loophole has been created which did not exist before the bill which is about to be passed came to the floor.

The \$768 million of tax savings which the President's original proposal contemplated were reduced by the House to \$135 million. I think that was most unfortunate; but we still had in the House bill legislation which would have increased, not decreased, revenues.

As the bill now is before the Senate, my best estimate of the revenue loss is \$490 million. Stated differently, the Treasury, during the first full fiscal year that the bill will be in effect, would have been \$1,258 million better off under the original proposals of the administration than under the Senate committee bill. The Treasury would have been \$625 million better off under the House version than under the Senate version. In my opinion, the Treasury will be close to \$500 million worse off as the result of what the Senate is about to do than it is today.

I am aware that these estimates are not firm. They could not be, under the constantly changing situation as amendments are adopted or rejected on the floor of the Senate. I am aware also that the Treasury was willing to go along with the statement in the committee report that the net loss of revenue under the committee bill might be as small as \$15 million. The gross loss, they said, would have been \$210 million. But I have some reason to believe that the Treasury—at least, some of the responsible officials of the Treasury who are charged with making these estimates—were very unhappy with the figures of a \$210 million gross loss and a \$15 million net loss. I think that in moments of candor, perhaps off the record, many responsible Treasury officials would candidly admit that the \$500 million estimate I have given, which is based in large part on Treasury estimates but supplemented by studies made by the very able staffs of Senator DOUGLAS and Senator GORE, is much closer to the actual fact.

I think we may take it pretty much as true that the bill which originally was designed to close inequitable and unjust loopholes and to grant an investment credit to corporations and businesses, in the hope that the credit would stimulate their retooling, cut their costs, and thus contribute to a step-up in our economy and and increase in our gross national product, has now been converted into something far different.

Let me review briefly the major loopholes the administration requested legislation to close, which are not closed or only partially closed in the pending bill.

The first is the expense-account situation. In June of 1960, the Senate adopted, by a vote of 45 to 39, an amendment which I sponsored, which was called at that time the anti-swindle-sheet amendment. That amendment, which was promptly kicked out in conference by the Senate conferees, a majority of whom were opposed to it on

the floor, would, I think, have pretty well curtailed tax abuses of expense accounts and would have brought back, in my opinion, some fundamental integrity and ethics in the area of what is and what is not necessary and legitimate business expense. The Senate the other day reversed its action of 1960, and the end result is that a pale and ineffective expense-account amendment has been adopted, which in truth means no substantial change in what has come to be referred to as our expense-account economy. In other words, in large part, the loophole of the swindle sheet is still in effect.

Next, the effort to close the loophole dealing with the capital gain treatment of income derived from the sale of depreciable real property, which the administration favored taxing at ordinary tax rates, was completely eliminated.

Third, no effort was ever made to repeal the 4-percent dividend credit and the \$50 dividend exclusion, although their repeal was originally recommended by the administration.

Fourth, the treatment of foreign income was far less rigorous than the administration had requested. The bill which the Senate is about to pass relaxed the administration proposals, with a substantial loss of revenue.

Fifth, the proposal of the administration with respect to mutual insurance companies was also relaxed, with the result that the net yield will be less than the administration asked for.

Sixth, and perhaps most important of all, the withholding of tax on dividends and interest was eliminated from the House bill, resulting in the largest loss of revenue of all—approaching \$900 million per annum of revenue owed to the Government under existing law.

I have tried to follow the arguments in opposition to the withholding tax; and I find myself as confused as the Senator from Oklahoma [Mr. KERR] purported to be a few moments ago when he was commenting on some very helpful and useful treatises on the tax effects on our economy, which the Senator from Wisconsin [Mr. PROXMIRE] introduced into the RECORD. I simply cannot understand how anyone—

The PRESIDING OFFICER. The time yielded to the Senator from Pennsylvania has expired.

Mr. CLARK. Mr. President, I ask for 5 more minutes.

Mr. MANSFIELD. Mr. President, I have only 27 minutes remaining under my control. Will the Senator from Delaware yield 5 minutes to the Senator from Pennsylvania?

Mr. WILLIAMS of Delaware. Yes. Mr. President, I yield 5 minutes to the Senator from Pennsylvania.

The PRESIDING OFFICER. The Senator from Pennsylvania is recognized for 5 additional minutes.

Mr. CLARK. I thank the Senator from Delaware.

Mr. President, I cannot understand how anyone who has studied the situation could oppose the imposition of the withholding tax on dividends and interest. However, I have made my argument

in that regard, and a large portion of the Senate disagrees with me.

Seventh, a brandnew loophole—one with respect to lobbying expenditures—has been introduced into the bill.

The end result must be that a Senator is torn between deciding to vote for the bill or deciding to vote against it.

On the one hand, the administration suggests that the loss of revenue will be far less than many of us think, and urges that if the bill goes to conference, the House will stand firm for its version of the bill, and the conference report will be one which some of us might be able to accept.

On the other hand, the Senate version of the bill does not do in any way what the President wants to have done or what the House wanted to have done, or what some of us—but, unfortunately, not enough—here in the Senate want to have done.

Therefore, I am in a dilemma. I should like to be able to think that when the bill goes to conference, there will be a chance that the conference report will be such that those of us who hold to my philosophy can conscientiously vote for it.

On the other hand, this is a bad bill. I think—and I express only my own opinion—that it is an iniquitous bill.

It is very difficult for me to understand why the administration and the Treasury are willing to take a bill which is so far removed from what the President wanted.

I think it might be better if we put off the whole matter until next year. But because I should like to see the Senate face up to the revenue implications of the bill, I shall shortly offer a motion to recommit, with instructions to the Finance Committee to obtain from the Treasury current estimates of the revenue losses and revenue gains from the bill in its present form, and to report the bill back to the Senate at the earliest practicable time, with instructions which will equalize the revenue losses and the revenue gains to be derived therefrom.

But before I do so, I wish to refer briefly to another matter: During this session of Congress there has been a great deal of criticism because of our efforts to impose rigorous conflict-of-interest restrictions on the executive branch of the Government and on nominees to judicial offices and other offices. We have been rather strict in that regard. But with respect to ourselves, I think it only fair to say that we have been lax.

I have felt increasingly, as time has passed, that it would be wise for every Senator to have printed in the CONGRESSIONAL RECORD, at the beginning of each session, a statement, in general terms, of his assets, so that the public generally could determine to what extent, if at all, he was affected by conflicts of interest as he proceeded to act in committee and to vote on the floor with respect to particular pieces of legislation.

It has not seemed to me that it would be either necessary or desirable for members of the general public or, indeed, for other Senators to know the net worth of

Senators; but I think it desirable that they know what securities Senators hold and from what sources they derive outside income, if any. This seems to me to be particularly pertinent in connection with tax legislation.

So, Mr. President, I ask unanimous consent to have printed at this point in the RECORD, as part of my remarks, a list of the securities which I held on August 27, 1962.

There being no objection, the list was ordered to be printed in the RECORD, as follows:

LIST OF SECURITIES HELD BY SENATOR JOSEPH S. CLARK AUGUST 27, 1962

BONDS

Government

U.S. Treasury, 2½ percent.
U.S. Treasury notes, 4¾ percent.

Municipals

Allegheny County, Pa., Peoples Road.
Ambler Junior High School Authority, Pennsylvania.
Bethlehem School District.
City of Philadelphia, 3 percent.
City of Philadelphia, 3½ percent.
City of Lebanon, Pa., 3.30 percent.
Com. Pa. Turnpike Rev. Ref., 3½ percent.
Cumberland County Inst. District, 3½ percent.
Gettysburg School Authority, Pennsylvania, 3½ percent.
Haverford Township School District, 3½ percent.
Radnor Township School District, 2.55 percent.
Pennsylvania State Public School Building, 3½ percent.
State Highway and Bridge Authority Com., Pennsylvania, 2½ percent.
State Highway and Bridge Authority Com., Pennsylvania, 3½ percent.
West Goshen Sewer Authority, 3 percent.

COMMON STOCKS

American Telephone & Telegraph.
Armstrong Cork.
Avery Island, Inc.
Campbell Soup Co.
First Pennsylvania Banking & Trust Co.
Franklin Life Insurance Co.
Friends Suburban Housing, Inc.
Insurance Co. of North America.
International Business Machines Corp.
Johns-Manville.
Modern Community Developers, Inc.
Oxford Paper Co.
Penguin Books Regd.
Rohm & Haas Co.
Scott Paper Co.
Sel-Rex Corp.

PREFERRED STOCK

Newmont Mining Corp., 4 percent Cum. preferred.

MISCELLANEOUS

Bayhil Fund
Oil royalties paid by Humble Oil & Refining Co. on wells drilled on Clark family property at Avery Island, La.

Mr. CLARK. Mr. President, I point out, with respect to two of the items, that the Bayhil Fund is a closely held investment trust connected with an investment banking and brokerage firm which—

The PRESIDING OFFICER. The additional time yielded to the Senator from Pennsylvania has expired.

Mr. CLARK. Mr. President, I ask for 1 more minute.

Mr. MANSFIELD. Mr. President, I yield 1 more minute to the Senator from Pennsylvania.

The PRESIDING OFFICER. The Senator from Pennsylvania is recognized for 1 more minute.

Mr. CLARK. I thank the majority leader.

Mr. President, I was saying that the Bayhil Fund is a closely held investment trust connected with an investment banking and brokerage company which employs my son, and that the oil royalties paid to me by the Humble Oil & Refining Co. constitute the major part of my income outside my Senate salary.

So, Mr. President, I move that House bill 10650 be recommitted to the Senate Finance Committee, with instructions to obtain from the Treasury Department current estimates of revenue losses and revenue gains from the bill in its present form, and to report the bill back to the Senate at the earliest practicable time, with recommendations which will equalize the revenue losses and the revenue gains to be derived therefrom.

Before I yield to the majority leader—who, I understand, will make the point of order which he has told me he is prepared to make—I wish to state that I would not request a yea-and-nay vote on the question of agreeing to the motion to recommit.

I regret very much that the majority leader feels it necessary to make the point of order.

I yield the floor.

Mr. MANSFIELD. Mr. President, I, too, regret it; but I do so only because I have heard rumors to the effect that two Senators on the other side might also offer motions to recommit. So I think it necessary to face up to that situation at the present time.

But before I make my point of order, I should like to request—as the Senator from Pennsylvania [Mr. CLARK] has also requested—that there be printed in the RECORD a list of my assets; I have none.

Mr. President, I make the point of order that the motion of the Senator from Pennsylvania is out of order.

The PRESIDING OFFICER (Mr. BURDICK in the chair). The Chair is ready to rule.

The unanimous-consent agreement, entered into last evening, limits debate on the pending bill today to not exceeding 4 hours, beginning not later than 9:15 a.m. It further provides that after the limitation of debate has expired, a vote shall follow on the final passage of the bill, thereby fixing a specific day for passage. Any action that might or would prevent this final vote would be in contravention of the unanimous-consent agreement. If the motion to recommit were agreed to, it would prevent a vote on the final passage of the pending bill; and therefore the motion to recommit is not in order.

Mr. MANSFIELD. I thank the Chair. I say to the Senator from Pennsylvania that I deeply regret having had to do this; but, unfortunately, I had no other choice.

Mr. CLARK. Mr. President, will the Senator from Montana yield 30 seconds to me?

Mr. MANSFIELD. Mr. President, I yield 1 minute to the Senator from Pennsylvania.

The PRESIDING OFFICER. The Senator from Pennsylvania is recognized for 1 minute.

Mr. CLARK. Mr. President, I shall not appeal from the ruling of the Chair, although in my judgment the ruling is erroneous.

I point out that almost 2 hours remain before the time scheduled for a vote on the bill; that the vote on the motion to recommit would be, so far as I am concerned, a voice vote, and would take perhaps 2 minutes, thus not interfering in any way with the scheduled vote; and a majority of the Senate should always have the authority to modify an earlier consent agreement; and that therefore the point of order is not, either pragmatically or legally, well taken.

Mr. BUSH. Mr. President—

Mr. WILLIAMS of Delaware. Mr. President, I yield 10 minutes to the Senator from Connecticut.

The PRESIDING OFFICER. The Senator from Connecticut is recognized for 10 minutes.

Mr. BUSH. Mr. President, I regret very much that I feel constrained to vote, on the question of final passage, against the pending measure.

It is now estimated by the staff of the Joint Committee on Internal Revenue Taxation that the bill in its present form will produce a net loss of revenue approximating \$600 million. Coupled with this, we see no potential reduction in expenses of our Government for the coming year, but, on the contrary, we appear to be facing a deficit now of a minimum figure of \$5 billion. That figure has been reliably estimated—as a very conservative figure. I have heard at least one estimate from a source I consider reliable that would place the deficit at approximately \$10 billion in the fiscal year of 1963.

In the face of this very serious budgetary situation, which has very formidable implications so far as our balance of payments problem is concerned, I do not see how I can support a measure which will produce an additional deficit by virtue of the provisions in it.

The key item in the bill, I suppose, or the largest item, is the so-called investment tax credit provision. Having reviewed carefully the debate here and the testimony in hearings, I find very little support for the tax credit measure. It is opposed by most of the important organizations who one would think would be most interested in it and most competent to assess its value to American industry and business. The tax credit provision is directed solely toward that group. It is opposed by the U.S. Chamber of Commerce. It is opposed by the National Association of Manufacturers. It is opposed by the AFL-CIO. It is opposed by the American Farm Bureau Federation.

When one sees that group united in opposition to this provision, one sees a degree of unanimity that seldom appears.

This particular tax credit is a discriminatory measure in that it tends to militate against the well operated, successful, farsighted company that has

gone ahead and refurbished its plant, bought new machinery and equipment, so that for the next 5 years, let us say, it is going to be in very good shape, whereas a company which has been laggard in keeping up with modern equipment, and has done little modernization or improvement of plant, will get a windfall through the tax credit.

What we need in American business is not a tax credit for a small segment of American industry; what we need is a general tax revision bill, one which deals primarily with the income tax, which looks toward eliminating inequities in the income tax, both corporate and personal, and which provides more of an incentive for the savers of our country, at all levels, to invest in expanded plant facilities of all kinds, including real estate and buildings, which are excluded under this provision of the bill. What is needed is an incentive tax reform measure.

We have had testimony, as I have said, from leading industrial and commercial groups that this bill does not provide the incentive that is so sorely needed.

I saw in the papers this morning mention of the fact that the unemployment rate rose sharply and unexpectedly in mid-August, to a seasonally adjusted 5.8 percent of the work force, from 5.3 percent a month earlier. The rise disappointed Federal officials, who were pleased last month when the rate had fallen from 5.5 percent in mid-June.

This increase in the unemployment rate comes in the face of the pending tax bill, which appears likely to pass the Senate, as it did the House, and become law. So it seems clear that the so-called investment tax credit in prospect has had very little effect in reviving business confidence, as evidenced in the unemployment figures.

I recognize that there are some very useful features in the tax bill. Here again we face the same dilemma we always face in omnibus bills. I have frequently opposed an omnibus bill on the basis that we have to take the bitter with the sweet, but I am afraid it will be a long time before Congress will get away from the practice of considering omnibus bills. I think it is the type of legislation which enables unnecessary and unwarranted provisions to get into the bill in order for the Congress to avail itself of the more desirable provisions which do appear in the bill.

Here we face in the omnibus bill a net loss of some \$600 million, as estimated by the staff of the Joint Committee on Internal Revenue Taxation, in the face of a Federal deficit of from \$5 billion to as much as \$10 billion for the fiscal year 1963.

I fear the passage of this bill will forestall the possibility of a real tax reform measure in 1963. This has been promised by the administration, but even now we hear rumors from administration sources that there will not be any general tax reform bill in 1963.

If a tax reform bill is indeed considered, I feel that the pending bill will be a stumbling block and will be a hurdle that the Congress will find difficult

in negotiating. We would be much better off, in my opinion, if we postponed action on this tax legislation until next year, when the whole question of tax reform, the whole question of incentive taxation, can be seriously considered by the House Ways and Means Committee and then carefully reviewed by the Senate.

Among those who have the control of the investment of the savers of this country—corporate and individual savers—it is almost unanimously agreed that what is needed is a revision of the income tax laws of this country, which are oppressive, and which not only do not provide incentives, but which provide obstacles, which provide deterrents, to the investment of savings for the creation of new job opportunities for the rapidly growing population of this country.

I may say that the unemployment situation is a very serious one, to which the Joint Economic Committee of the Senate and House, of which I have been a member for a number of years, has given very considerable attention.

I hope that next week, when the Finance Committee gets down to business on the proposed Trade Expansion Act, which is now before it—and I hear the committee will be marking up the bill next week—it will scrutinize very carefully the provisions of this bill which may have a very serious adverse affect upon employment in this country.

The PRESIDING OFFICER. The time of the Senator has expired.

Mr. BUSH. Will the Senator yield me an additional 5 minutes?

Mr. WILLIAMS of Delaware. Yes; I yield the Senator from Connecticut an additional 5 minutes.

Mr. BUSH. Particularly, I hope the committee will give attention to amendments which provide congressional guidelines for trade agreements, which will give the Congress the constitutional authority which is inherent in it.

The question of the Common Market is involved. The bill is written under the assumption that the United Kingdom is to be a member of the Common Market. At the present time there seems to be grave doubt whether, indeed, the United Kingdom will be admitted to the Common Market, or whether it will decide it wishes to ask for admission. With such a grave doubt overhanging the bill, which is keyed so directly to the Common Market, it seems to me doubtful whether we ought to pass a bill so keyed without definite assurance—indeed, without positive assurance—that the United Kingdom will be a member of the Common Market.

Mr. President, the bill before the Finance Committee should be strengthened by giving the Tariff Commission a better status. That is an expert Commission. It is a Commission which has a large staff devoted to one subject, which is the study of the effects of tariffs, or other changes in our import and export laws, upon American business, upon American employers, and upon American jobs. I hope that amendments will be adopted which will

take into account that very important factor, rather than to disarm the Tariff Commission, as I believe the House bill is intended to do.

I also express the hope that attention will be given to the most-favored-nations amendments, which will ask those with whom we make trade agreements to extend, as we do, most favored nation's treatment to other countries. The effect of this would be to open up the markets of the Common Market to countries in the Far East like Japan, markets largely now closed to these important allies of ours in the Far East. Also, our friends in Latin America are likely to be strongly discriminated against unless the most favored nations rule is indeed modified so as to make our partners in trade agreements agree to most favored nations treatment the same as we do.

Finally, Mr. President, I hope that the traditional and historic concept of no serious injury, which began with Cordell Hull and President Franklin Roosevelt, and was further adhered to by President Truman and his administration and by President Eisenhower and his administration, will not be abandoned, as it appears the House bill would intend to abandon it.

Mr. President, I ask unanimous consent to have printed in the RECORD at this point a brief summary of some of the amendments which, in cooperation with other Senators, I have offered in connection with the trade bill.

There being no objection, the summary was ordered to be printed in the RECORD, as follows:

SUMMARY OF THE BUSH AMENDMENTS

1. RESTORE BALANCE—TRADITIONAL SAFEGUARDS

(a) Restore peril point procedure (amendments 6 (par. 1); 12).

On reductions exceeding 50 percent (80-percent test), make peril point findings mandatory (amendments 3c; 4).

Clarify peril point criteria (amendment 5 (par. 2)).

(b) Restore escape clause (amendments 18-22; 28a).

Clarify serious-injury criteria (amendment 26).

2. INSURE INTEGRITY FOR OUR TRADE CONCESSIONS

(a) In view of most-favored-nation rule: Amendment 11a: Between EEC and United States (treatment by EEC of our exports equivalent to that we grant EEC).

Amendment 11b: Negotiations only with the principal supplier.

Amendment 11c: Benefit Asia by opening markets in Europe.

(b) In view of widespread discrimination against U.S. exports: Amendments 16a-16e require Executive action to counteract discrimination.

(c) Enforcement as to most-favored-nation rule: Amendments 17a and 17b.

3. ADJUSTMENT ASSISTANCE (TITLE III)

(a) Industries: Escape clause only (amendments 20-22).

(b) Firms, not industries: Area Redevelopment Act (amendments 23, 24, 29, 33).

(c) Workers, not industries: Manpower Development and Training Act (amendments 25, 30-32, 34).

4. LEGISLATIVE OVERSIGHT

(a) Report by President to Congress in peril point cases (amendment 12).

(b) Congress authorized to make Tariff Commission recommendations effective—

escape clause cases: By privileged resolution—simple majority vote—60 days (amendment 28b).

5. CLARIFY NEGOTIATING POWER AND PROCEDURE

(a) Industry advisers during negotiations (amendment 15).

(b) Expand exports (amendment 1).

(c) State missing portions of EEC power: 80 to 25 percent test (amendment 3a).

Delete giveaways (amendment 3g). Tropical: Directly competitive test (amendments 5b and 5f).

(d) Delete 5-percent duty elimination power (amendment 2).

6. GROWTH INDUSTRIES (AMENDMENT 37)

(a) Preserve job-creating potential of high growth industries from destruction by excessive imports.

Tariff Commission advice to President prior to negotiations warning of such effect.

(b) Restore such job-creating potential by regulation of imports:

Tariff Commission findings.

Authority for the President to act if he deems national interest requires.

The Bush amendments carry out six key reforms of the trade bill.

1. RESTORE TRADITIONAL SAFEGUARDS

(a) Peril point procedure: They restore the existing peril point procedure. This requires the Tariff Commission to find the extent to which each duty proposed for negotiations can be reduced without causing serious injury to domestic industry, agriculture, or workers. The President is free to exceed these "peril points," but he must explain to the Congress in each instance why he did so.

The Bush amendments would make the peril point findings binding on the President on articles proposed for elimination of duty under the special EEC authority of the bill. This is necessary because the United States will be negotiating in broad categories of products with the EEC; selective, item-by-item negotiations will not be possible within these categories. The Bush amendments would remove from the legal definition of each such category those individual articles where the Commission finds that an elimination of duty would cause serious injury to the domestic industry, sector of agriculture, or workers producing the articles.

To provide greater certainty in peril point determinations, the Bush amendments would clarify the criteria of serious injury. Whenever the Commission finds that a duty reduction would result in increased imports which would take over a larger share of the domestic market than that accounted for by imports during a representative base period, and a decline in employment, wage payments, or profits, the Commission would be required to find that duty reduction could not take place without causing serious injury.

(b) Escape clause procedure: The Bush amendments would restore the existing escape clause. This was enacted in 1951 and improved by amendments in 1955 and 1958. Its key concepts are:

(1) A finding of injury may be made if increased imports result in part from a trade agreement concession.

(2) The increased imports causing injury may be an absolute increase or an increase relative to declining domestic production.

(3) The industry in question is that sector of the producing organizations engaged in the production of articles like or directly competitive with the imported article under investigation;

(4) Serious injury is determined on the basis of declining trends in production, sales, employment, wage payments, profits, or a higher or growing inventory in conjunction with an increase in the share of the market accounted for by imports.

H.R. 11970 repeals the existing procedure and each one of these concepts.

The criteria of serious injury are clarified to specify that a finding of injury by the Commission is mandatory when it determines that increased imports are accounting for the greater share of the domestic market than enjoyed by imports during a representative base period and there is a decline in employment, wage payments, or profits in the domestic industry producing articles competitive with the imports under investigation.

2. MAINTAIN LEGISLATIVE OVERSIGHT OF THE TRADE AGREEMENTS PROGRAM

The Bush amendments restore the requirement that the President must explain to Congress in writing his reasons for ignoring the Tariff Commission's peril point determinations when he reduces U.S. duties beyond the limits set by the Commission in its peril point investigation.

In escape clause cases, the Bush amendments would restore and strengthen the right of the Congress to make effective Tariff Commission recommendations when the President fails to do so. Under existing law the President must report to Congress his refusal to act on Tariff Commission recommendations; Congress then by a privileged resolution, adopted by a two-thirds majority within 60 days, may itself make the Commission's recommendations effective. H.R. 11970 deletes the privileged resolution and changes the two-thirds majority vote to a majority of the authorized membership of each House. The Bush amendments reinstate the privileged resolution and change the required vote to a simple majority.

3. INSURE THE INTEGRITY OF U.S. TRADE BENEFITS

(a) In the light of the operation of the most-favored-nation rule: The Bush amendments specify three principles which are designed to secure true reciprocity and actual value received for U.S. exports from U.S. tariff concessions; and, to open up European markets for Asiatic exports in order to strengthen those countries against economic penetration of communism as well as relieving the excessive pressure of their exports on the U.S. market.

Thus, the Bush amendments make it a condition of any new tariff concession granted to the Common Market that U.S. exports of the items covered by such concessions be admitted into the Common Market countries on terms as favorable as we extend to EEC exports. Under these amendments our tariff bargaining must be conducted with the principal supplier of each article so that we may demand the highest price from the nation that benefits the most from our concession. Finally, recognizing that European countries restrict the entry of Asiatic imports by quotas and other non-tariff barriers, while further penalizing Asiatic trade by withholding most-favored-nation treatment, the Bush amendments make it a condition of the grant of any new tariff concession to any country that it admit exports from Asiatic countries on terms as favorable as the recipient country requests of us for its exports to the United States. This principle will enable the United States, while increasing access for its exports to European markets, to apply leverage to European countries to take their share of Asiatic imports. This will relieve the pressure on the U.S. market which now exists as a result of European restrictions which divert most Asiatic trade to this country.

(b) In the light of the existence of widespread discrimination against U.S. exports and nullification of U.S. trade benefits: If the conditions referred to above, after being accepted by our trading partners, are subsequently dishonored by them, the Bush

amendments would require the President to suspend the benefit of the concessions which we granted to those countries on the strength of their commitments. Our concessions could be reinstated when their discriminatory practice ceased.

The meaning of section 252 of the bill prohibiting the President from granting new tariff concessions to countries which discriminate against and, thus, burden U.S. commerce and which directs him to withdraw prior concessions from such countries when their actions are inconsistent with our rights under existing trade agreements, is made more definite by the Bush amendments in deleting qualifying words, such as "unjustifiable" and "unlimited," which would make the President's duty to act purely discretionary on his part. These words also imply that restrictions or discriminations which burden our commerce contrary to the provisions of trade agreements could somehow be "justifiable."

4. CLARIFY NEGOTIATING POWER AND PROCEDURE

(a) Industry advisers: The negotiating teams of other countries customarily contain industry representatives. The high caliber of the technical advice available to these delegations places the United States at a disadvantage. The Bush amendments would require the President to receive advice and information from representatives of industry, agriculture, and labor during the course of negotiations concerning articles affecting their production.

(b) Expansion of exports as a primary purpose: The trade bill sets forth four separate purposes which are to govern the use of the President's power. Only one relates to an expansion of our exports. The Bush amendments would require this purpose always to be included among the purposes for which the President uses tariff-reducing power in trade negotiations.

(c) Complete the standards essential for identifying categories for duty-free EEC bargaining: If the exports of the United States and the EEC amount in the aggregate to 80 percent of world trade, H.R. 11970 authorizes the President to eliminate the duties on the articles in the category. This test of itself does not establish that the United States has any significant competitive strength in world trade in the article. The Bush amendments require that the United States account for at least 25 percent of the exports.

Since the 80 percent test in theory is designed to identify categories in which the United States and the European Common Market have competitive commercial strength in foreign trade, the statistical determination should exclude the value of cargoes financed under foreign aid programs. Such cargoes do not result from commercial demand for the exports in question. Their inclusion in the statistics simply distorts the identification of articles whose commercial competitive strength evidences some ability to withstand the effects of duty-free treatment for competitive imports.

The Bush amendments also complete the explicit statement of qualifications upon which the tropical agricultural and forestry commodity authority for duty elimination rests. The assumption is that products of the Tropics are not competitive with products of the United States. Since it is known that some species of tropical commodities, such as starch, lumber, fiber, and the like, are directly competitive with Temperate Zone products, the Bush amendments add the qualification to the tropical section that the articles selected for duty-free treatment not be directly competitive with items produced in substantial quantity in the United States.

(d) Delete the authority to transfer low duty items to the free list: The Bush amendments delete the power that would be granted to the President to eliminate duties

on the ground that they are 5 percent ad valorem or less. The low level of a duty is probably as much the function of repeated reductions under the various extensions of the trade agreements authority as any other factor. The level of the duty does not in and of itself indicate the importance of the duty to the competitive position of the domestic industry. "Administrative convenience" is the principal reason advanced for this power. It would be illogical to remove the remaining protection from domestic industries, agriculture, and workers on such a basis.

5. ELIMINATE SPECIAL ADJUSTMENT ASSISTANCE AS AN ALTERNATIVE TO REGULATION OF DAMAGING IMPORTS

The Bush amendments would reinstate the existing "no serious injury" rule which has been the guiding principle of our trade agreements program since 1934. The amendments, therefore, would delete from the bill the power of the President to grant special assistance to firms and workers as an alternative to regulating imports by tariff adjustment and quotas to correct serious import injury caused domestic industries, agriculture, and workers.

Recognizing the applicability of the Area Redevelopment Act and the Manpower Development and Training Act, passed by this Congress, to the situation of firms and groups of workers in distressed circumstances, the Bush amendments would make the remedies of those acts available to firms and groups of workers in cases where there is not widespread import injury.

The effect of the Bush amendments on title III of the bill, therefore, is to limit industries injured by imports to escape clause relief; and to limit the assistance to firms and workers to the benefits provided in present law.

6. PRESERVE THE NEW JOB-CREATING POTENTIAL OF DYNAMIC GROWTH INDUSTRIES

When an industry or its workers are injured by imports, the economy suffers. The Bush amendments recognize that the Nation's economy also suffers when rapidly increasing imports saturate the domestic market to such an extent that the growth potential which has sustained the expansion of growth industries is destroyed. Where an industry with a sustained rate of growth suffers a serious impairment of that rate of growth as a result of excessive imports, the Bush amendments would provide for a Tariff Commission, finding to that effect. The President would be cloaked with the power to adjust duties to the extent necessary to remove that impairment. This important concept would also be used by the Tariff Commission in peril point investigations in order to advise the President of any probable impairment to the growth factor of dynamic industries.

Mr. BUSH. Mr. President, I yield the floor.

Mr. WILLIAMS of Delaware. Mr. President, I yield myself 10 minutes.

The PRESIDING OFFICER. The Senator from Delaware is recognized for 10 minutes.

Mr. WILLIAMS of Delaware. Mr. President, the bill as it is pending before the Senate and as it was reported by the Senate Finance Committee, in my opinion, represents a substantial improvement over the bill as it was first approved by the House of Representatives. I think many of the changes incorporated in the bill by our committee are good. I am in complete agreement with many of these changes and support them. I think many features of the bill would be a substantial improvement over

our existing tax laws, and particularly those relating to the change in the method of taxing some mutual savings banks and saving and loan associations.

For the first time we have touched somewhat on the treatment of taxing of cooperatives, although in this connection I must say I do not think we have approached a solution to the problem. There are many features of the proposal in the bill which I do not think will work from the standpoint of cooperatives or from the standpoint of more equitably taxing this group. At the same time, there is a serious question as to the constitutionality of this section.

There will still be a situation in which farmers will be taxed on income which they never receive and over which they have no control.

Personally, I would have preferred a formula which I supported in the committee, this was the proposal recommended by the American Farm Bureau Federation, which I think would have come far closer to correcting this problem than the provision ultimately incorporated in the bill. Nevertheless, we are confronted with the bill as it is now before the Senate.

The investment credit provision which has been incorporated in the bill, is in my opinion unsound and I think will come back to haunt the Senate and the Congress. I have always favored a more liberal depreciation formula. I think American business generally favors such a liberalized formula.

But I do not like a formula wherein one can get a depreciation credit up to 107 percent of the cost of the asset as is possible under the Senate bill, and up to 114 percent of the cost under the House bill. That is an unsound principle.

Furthermore the formula is too complicated for the average businessman to understand. It was opposed almost unanimously by American industry.

Walter Slowinski, appearing in behalf of the U.S. Chamber of Commerce, with respect to the "investment credit" provisions, said:

The chamber again recommends against the adoption of this novel and untried preferential tax credit subsidy for business. It is also unnecessarily complex, and it will be difficult to administer.

Harold H. Scaff, chairman, Tax Committee, National Association of Manufacturers, said "investment credit would simply provide reduction in effective tax rates for taxpayers who use their income and other funds as the Government thinks is best for the economy at a particular time."

There has been a tendency to promote and discuss the investment tax credit apart from the price which it would exact in terms of other changes in the tax law. Even without the exaction of such a price, we would oppose the credit for the reasons set forth in the appendix attached hereto. Very simply, we believe that tax reductions should be afforded by direct means. We would take this position even if, in our opinion, all of the other provisions of H.R. 10650 constituted sound tax policy.

Charles B. Shuman, president, American Farm Bureau Federation, took the position that "these provisions are both

unsound and likely to have a number of undesirable effects. It would be far better to liberalize the treatment of depreciation and work toward a general reduction in income tax rates."

The proposed investment credit is a selective form of tax relief—in reality a subsidy. * * * The result would be to give some taxpayers a competitive advantage at the expense of others.

Stanley H. Ruttenberg, research director, AFL-CIO, urged the committee to "delete this provision from the bill," because those he represented thought:

It is a multibillion-dollar windfall that will not really contribute anything to our national goals and will not relieve our balance-of-payments problems as it is claimed.

Mr. President, even after taking into consideration the increased revenues

which would be provided by some of the changes in existing tax structures, based upon estimates furnished by the staff, the bill still would lose about \$600 million annually. We would lose this revenue at a time when the only manner in which we could finance the loss of revenue is to further increase the national debt, to borrow the money and charge it up against our grandchildren.

I have never favored tax reductions that can be financed only on borrowed money.

Mr. President, I ask unanimous consent to have printed in the RECORD a statement of the estimated full-year revenue effect of H.R. 10650.

There being no objection, the statement was ordered to be printed in the RECORD, as follows:

Estimated full-year revenue effect of H.R. 10650,¹ as passed by the House of Representatives, as amended by the Senate Committee on Finance, and as amended by the Senate

(Millions of dollars)

	As passed by the House of Representatives	As amended by the Com- mittee on Finance	As amended by the Senate
Investment tax credit.....	-1,395	-1,340	-1,340
Withholding on dividends and interest.....	+550		
Reporting of dividend and interest payments.....		+275	+275
Mutual banks and savings and loan associations.....	² +170	² +180	² +180
Entertainment, etc., expenses.....	+125	+85	+85
Capital gains on depreciable property.....	+110	+105	+105
Mutual fire and casualty companies.....	³ +25	³ +25	³ +25
Cooperatives.....	+30	+30	+30
Foreign items:			
Controlled foreign corporations.....	+50	+50	+50
Gross-up of dividends.....	+25	+15	+15
All other foreign items.....	+25	+25	+25
Secs. 21-26 of Senate Finance Committee bill.....		-5	-5
Other (sections added by Senate).....			-30
Total.....	-285	-555	-585

¹ At levels of income and investment estimated for the calendar year 1962, without taking into account effect of provisions on the economy; estimates are rounded to nearest \$5,000,000.

² The level of income for these thrift institutions in 1962 has been revised upward since the preparation of the revenue estimates for the House bill.

³ Revenue gain which would result if this provision were in effect for 1962 and had been in effect for the 5 preceding years, so that amounts added to the protection against loss account in the 1st year and not offset by losses would be brought into taxable income in 1962.

Source: Staff of the Joint Committee on Internal Revenue Taxation.

Mr. WILLIAMS of Delaware. Mr. President, a statement was issued by the Treasury Department, dated August 29, indicating that our national debt today stands at \$301.8 billion, as compared with \$293 billion only a year ago today. In other words, there has been an increase of \$8.8 billion in our national debt during the past 12 months.

We are still operating in the red and there is no prospect of a balanced budget at any time in the foreseeable future. Quite the contrary our spending is increasing.

During the same period we have been losing gold at the rate of \$1½ billion a year. Our gold holdings today stand at \$16,098 million. One year ago the holdings were \$17,600 million.

Mr. President, I noticed in the Washington Evening Star for yesterday an article calling our attention to the fact that our gold supply is getting smaller. The United States has been forced to dip into the Fort Knox gold for the first time in 17 years. It has become necessary to dip into these reserves to meet our commitments. Our gold reserves are going down all the time. This drain is largely the result of continued

deficit planning of the administration, and bills approved by the Congress.

Mr. President, I ask unanimous consent to have printed in the RECORD at this point the article to which I referred.

There being no objection, the article was ordered to be printed in the RECORD, as follows:

UNITED STATES FORCED TO DIP INTO FORT KNOX GOLD

For the first time in 17 years, a large amount of gold has been removed from storage at Fort Knox, Ky., in order to meet foreign demand for U.S. bullion.

The Treasury said today recent shipments from the Fort Knox depository represented the first significant reduction since 1945 in the amount of gold stored there.

Officials would not disclose the value of the bullion moved from Fort Knox to the Treasury's assay office in New York City. According to some accounts, which were neither confirmed nor denied, the total approached \$500 million.

Before the shipments were made, the Fort Knox bullion hoard totaled \$12.5 billion.

The Treasury emphasized that shipments of gold to the New York assay office have been routine in recent years because of the steady drain on the U.S. gold supply. However, officials said most shipments in the past were made from the mints in San Francisco and Denver.

The U.S. gold supply now totals \$16.1 billion, down from a postwar peak of about \$24 billion. The reduction came about because Americans have been spending, lending, and investing abroad more dollars than they have received from foreign sources.

Last year's payments deficit was \$2.5 billion, a drop of about \$1.5 billion from that of 1960. So far this year, the deficit has been running at an annual rate of about \$1.5 billion.

The Government has undertaken a number of programs to reduce the deficit, and Secretary of the Treasury Dillon has predicted payments will be in balance by the end of next year.

But meanwhile, foreign governments and foreign central banks have continued to buy American gold as they have built up supplies of dollars. Gold sales to foreigners in the past 12 months have exceeded \$1.3 billion.

Mr. WILLIAMS of Delaware. Mr. President, recently we had before our committee, the Director of the Bureau of the Budget, Mr. Bell. He boasted of the fact—and seemed rather proud of it—that this administration has been able to convert a prospective surplus last year of around \$1 billion into a \$4 to \$5 billion deficit.

This is the first time I ever heard of a Budget Director boasting of a deficit.

He told our committee this deficit was deliberately planned by the administration. They are still in the process of deliberately planning deficits and trying to live beyond our income.

The time is long overdue when we should recognize that we cannot spend ourselves into prosperity on borrowed money. That was unsuccessfully tried during the 1930's. It is being tried again today. As evidence that it is not succeeding, the Senator from Connecticut [Mr. BUSH] has just put into the RECORD reports showing that unemployment is again rising. This rise in unemployment comes at a time when we are still trying to borrow money and spend ourselves into prosperity.

This investment credit proposal is unsound and we cannot afford the loss in revenue at this time. For that and many other reasons I shall not support the bill at this time. I do not think we could justify a tax reduction at any time in the face of continued deficits. If the administration wishes a tax reduction, I will be the most enthusiastic supporter, if the reduction is approached with the idea of first cutting down on Government spending.

The PRESIDING OFFICER. The time of the Senator has expired.

Mr. WILLIAMS of Delaware. I yield myself 5 additional minutes.

If the administration would cut down on Government spending so that the saving could be passed on to the American taxpayers, it would be a constructive step. It would do more to stimulate business than anything else we could do.

I am a great believer in the thought that the American people better know how to spend their money than any bureaucrat in Washington knows. But we cannot get away from the fact that the administration proposals all call for more and more spending as time goes on. There has not been a single appropriation bill before the Congress which has

not averaged 5 percent, 8 percent, and sometimes 10 percent in increased expenditures. Many proposals now await consideration by Congress, none of which would reduce expenditures, but all of which would increase expenditures.

Recently the Joint Committee on the Reduction of Nonessential Federal Expenditures called attention to the fact that 34,900 new employees have been added in the month of June alone. These were added to the 70,000 which had been added in the preceding 11 months. We were adding employees during that particular period at the rate of 8,000 a week or assuming a 5-day week this was at the rate of 1,600 every day. If we were to consider operations of the Government on an 8-hour working day we find we are adding 200 employees an hour.

The American people cannot afford to support any unnecessary bureaucrats on the Federal payroll.

Personally I think this whole question of tax revision should be postponed until the President sends his tax message to the Congress next year. We can then consider all these questions together.

There are some good features in the bill, however, I believe it should be pointed out that the bill has made great steps toward the elimination of tax havens. I am glad to see such a provision incorporated in the bill. This is a long overdue correction. It may not completely solve the problem, but at least it is a major step in the right direction.

Certain modifications and corrections have been made with respect to expense accounts. Perhaps the provision does not go far enough in relation to expense accounts, but I still say that, as Members of Congress, rather than point the finger of scorn too much at the American businessman about his expense accounts, we should first attempt to set our own house in order. Sometimes we find in our own backyard some abuse in connection with congressional expense accounts. In that connection I ask unanimous consent to have printed at this point in the RECORD two articles dealing with the subject.

There being no objection, the articles were ordered to be printed in the RECORD, as follows:

[From the Washington Post, Sept. 4, 1962]

POWELL TOURS EUROPE HIGHSPOTS

(By Drew Pearson)

ADAM CLAYTON POWELL, the debonair Congressman from Harlem, has been sending postcards home from one of the most unique junkets in congressional history.

With Congress stewing over vitally important legislation, POWELL has gone off to the nightclubs, of Paris, the theaters of London, the film festival of Venice, and the delights of a cruise through the Greek islands, largely at Government expense.

He has taken with him two lady members of his staff, Mrs. Tamara J. Wall, a young blonde divorcee, and Miss Corrine Huff, receptionist in POWELL's office, a dark-complexioned former runner-up in the Miss Universe contest. Officially, they will study equal opportunity for women.

Meanwhile, the education bill for aid to colleges and universities is deadlocked in the Education and Labor Committee of which POWELL is chairman. POWELL, who

heads the largest Baptist church in the world, the Abyssinian Baptist Church of Harlem, favors outright grants to Catholic colleges—as do other House Members. The Senate opposes outright grants as contrary to separation of church and state, but is willing to vote loans.

The Congressman from Harlem did not seem worried about remaining in Washington to struggle with a bill badly needed to help the colleges.

CLUBS, ARMY CARS

Just before he sailed, he asked the State Department to arrange a plush sightseeing tour of Europe, and the State Department accordingly sent the following cable to its Embassies in London, Paris, Rome, Athens, and Venice:

"Congressman ADAM C. POWELL, chairman, Committee on Education and Labor, accompanied by Mrs. Tamara J. Wall and Miss Corrine Huff, staff members traveling Western Europe, accordance following itinerary:

"August 8, sailing *Queen Mary*, arriving Southampton, August 13; Paris, August 16; Venice, August 20; Rome, August 23; Athens, August 27; Delphi, August 30; sailing *Leonardo da Vinci*, September 15 from Gibraltar. Arrival times and flights forwarded when firm.

"Provisions handbook congressional travel apply. Codel and party authorized use local currencies 19FT561 funds. Meet assist appoint control officers."

This means that "codel," the cable abbreviation for POWELL's congressional delegation could get counterpart funds in each city without having to account for them. Counterpart funds are local currencies which American Embassies have on hand usually in payment for surplus farm products, and the State Department's cable meant that POWELL and his two secretaries could dip into these funds for shopping, nightclubbing, tips to doormen, etc.

MEET US WITH \$300

"Request one single and one double with bath as follows," continued the State Department cable. "London—Cumberland Marble Arch Hotel; Paris Hotel San Regis; Venice Royal Denielli; Rome (1), Excelsior (2) Flora (3) Victoria, whichever has special Embassy rates; Athens, beachhouse at Astir Hotel; Delphi, new Government hotel name unknown. Confirm Department soonest.

"London," continued the State Department cable "request three tickets August 14, 15 best shows playing, except Broadway plays." (Powell has seen the shows on Broadway in New York, so didn't want to repeat those which have moved to London.)

"Paris—codel (congressional delegation) desires use U.S. Army car and chauffeur. Reserve three for first show and dinner best table Lido August 16."

The Lido is the Paris nightclub famous for its undraped grrlles, and the head of the Abyssinian Baptist Church had the American Embassy, busy with Common Market and NATO problems, make sure he had the best table at the first show in order to study equal opportunities for women.

"Venice—if the film festival going on request three tickets August 20 or 21. Codel also requests use consulate's motorboat (for the Grand Canal of Venice).

"Athens—arrange use rental car trip to Delphi payable 19FT561 funds August 30." (This again meant the use of counterpart funds for a sightseeing trip.)

"Delphi—codel inquires whether boat trip about 6 days around islands possibility. Possible visit Rhodes."

The Greek islands obviously are a fascinating laboratory in which to study equal opportunities for women.

"Southampton—codel requests be met at Queen Mary Cherbourg with \$100 U.S. equivalent

in local currencies for each member party."

This meant that the busy U.S. Embassy in Paris had to send a man to Cherbourg, requiring a day round trip, just so the Congressman from Harlem and his two secretaries would have \$300 worth of French francs to spend immediately after they got off the boat. The average tourist steps up to the money change office and gets his money exchanged in 5 minutes. He doesn't have a representative from the American Embassy in Paris spend a whole day providing him with francs.

[From the New York Times, Sept. 6, 1962]

POWELL'S SHAMELESS JUNKET

In the midst of the important closing period of the congressional session, when a record of accomplishment versus nothingness is in the balance, the chairman of a major committee of the House is traveling about Europe on a frivolous junket. Almost needless to say, this is ADAM CLAYTON POWELL, chairman of the Education and Labor Committee, a Democrat from Harlem who annually vies with BUCKLEY of the Bronx for the dishonor of being among the most absent Members of Congress.

Representative POWELL sailed for Europe August 8 with Mrs. Tamara J. Wall, associate labor counsel for the committee, and Miss Corrine Huff, receptionist in his office. They are due back about September 21. Mr. POWELL is supposedly conducting an inquiry into equal opportunities for women in Europe, a study that will take him to a Paris nightclub show, a Venice film festival, and possibly on an Aegean cruise. State Department officials have been alerted to arrange hospitality and entertainment, as well as counterpart funds—other countries' reimbursement for our foreign aid—which conveniently need not be accounted for in detail by our traveling Congressmen. Mr. POWELL is not alone in the enjoyment of this and other abuses of the congressional privilege.

The reckless, irresponsible conduct of Mr. POWELL is a disgrace to the people of his district, to the U.S. Congress and to the Kennedy administration, which to its discredit sent Secretaries Ribicoff and Goldberg to New York last year to attend a POWELL glorification dinner.

We say it is time for the people of Harlem to wake up, quit making a hero out of this man who holds in such contempt his obligations in public office, and retire him from Congress before he has a chance to make good on his repeated promises to retire himself. As for the House of Representatives and the Kennedy administration, have they no discipline for a Member, and especially a committee chairman, who runs away to Europe for 6 weeks on idle whimsy like this "inquiry" just at a time when Congress is (belatedly) trying to get down to serious business.

Mr. KEATING. Mr. President, will the Senator yield?

Mr. WILLIAMS of Delaware. Mr. President, how much time have we remaining?

The PRESIDING OFFICER. The Senator has 1 hour and 9 minutes remaining.

Mr. WILLIAMS of Delaware. How much time does the Senator from New York desire?

Mr. KEATING. I should like 25 minutes. I do not wish to interfere with any Senator who desires to speak on the tax bill, because that will not be the subject of my remarks.

Mr. WILLIAMS of Delaware. I yield 25 minutes to the Senator from New York.

BUILDUP IN CUBA

Mr. KEATING. Mr. President, for the last few days we have all been absorbed in the latest, the most up-to-date details of Soviet military expansion on the Island of Cuba. Members of Congress including myself have made available to the American people detailed reports of day to day ship movements, vehicle alignments, and personnel maneuvering in and around Cuba with the object of making clear to the American people the fact that the last month has seen a tremendous increase in the Soviet commitment to Cuba and in the Communist forces now deployed on the island.

It has now been revealed that 64 ships with materiel and troops have arrived in Cuba—a fact, which has been somewhat played down, even by those of us who knew the facts. A much smaller number of ships has been referred to up to this point.

One of the results of the increased public discussion and interest in the Cuban situation—and to date it has been the only significant development on the part of our Government—but a very constructive one—is an official announcement from the President admitting for the first time that the Cubans possess missiles, extensive radar and electronic equipment, torpedo boats and guided missiles, and at least 3,500 so-called military technicians.

I do not intend to belabor the significance of the word "technicians," but anyone who has seen a modern American Army or Air Force recruitment poster knows that the military men in modern service are no longer GI Joes of what was called in World War I the flat foot variety. They are very definitely technicians, with a knowledge and ability to operate complicated weapons and weapons systems. In fact, the promise of being trained as a "technician" is one of the most effective incentives for enlistment. I am sure the Soviet Army also has its share of such technicians.

I refer to a statement in a news item published in today's issue of the Washington Post, which is undoubtedly typical of the reaction of someone in the Department of State. No one in the military forces could possibly have made such a statement. It is the reaction of those who wish to play down the situation, and who feel that those of us who believe that the American people should be alerted are unduly concerned. I read the statement of the official, without designating him. He said:

There is little meaning in statements like those of Senator KEATING that the Soviet technicians are in reality soldiers. Not only is there no evidence of this, the source said, but 3,500 common foot soldiers would probably pose less danger to hemispheric security than 3,500 trained technicians.

The clear implication of that article is that the Senator from New York has said there are 3,500 foot soldiers in Cuba. Of course, I have never made any such assumption or statement. Such is not the fact, and I entirely agree that technicians of that kind pose a much greater

threat to the security of the United States than do foot soldiers.

There are no foot soldiers, so far as I know, in Cuba. The soldiers who are there are what would be called in our Army, for the most part, Signal Corps personnel, labor battalions. They are under military discipline, they are under military orders, they move in military formation, they are dressed in uniforms, and they are what in American parlance are called soldiers. However, I am willing to accept the phrase "military technicians."

Mr. President, I am much more deeply concerned with the subtle shift in U.S. policy toward Cuba. Our Government describes the buildup in Cuba as a defensive rather than as an offensive capability. Whether a gun is offensive or defensive depends entirely on the man who holds the gun. Mig airplanes, tanks, halftracks, or missiles can be used in defense, it is true, but likewise they can also be used in offense, and whether they are defensive or offensive depends entirely on the intentions of the operator.

Furthermore, it is a little hard to understand what defensive purpose amphibious vehicles would have. It was said by the Senator from California (Mr. ENGLE) last night that the remarks of the Senator from New York, which were made on two occasions in considerable detail, were wrong because he had said there were amphibious vehicles in Cuba. What the Senator from New York has said was that amphibious vehicles had been observed in Cuba. I repeat the statement.

However, it is quite interesting that the distinguished Senator from California, who had indicated that there would be an effort made to show the inaccuracy of the remarks of the Senator from New York, pointed out nothing except this one sentence in the entire remarks of the Senator from New York.

That the facts given to the Senate on last Friday and on last Tuesday were accurate to the extent of 97 or 93 percent has been more than confirmed by subsequent disclosures.

Apparently the attitude of our Government is that we have no objection and that we raise no protest if these weapons which are in Cuba are directed only against the Cuban people; that it has ceased to be aggression in our vocabulary when Soviet Russian technicians and equipment are brought to Cuba to force their will upon the people of Cuba. The President referred only very briefly to "the unhappy people of Cuba." It is apparently of no concern to us that they are threatened by the so-called defensive weapons, that their homeland is put under the control of Communists from Moscow, that their children are sent to Russia for education, that their best brains and most capable workers are fleeing in droves from the tyranny that Castro and Khrushchev have established in Cuba. All this, we are now told, is not the concern of the people of the United States.

We have been told that this buildup in Cuba is permissible unless an overt offensive attack is made from Cuba upon

some other country in this hemisphere; that the Cuban question is no longer to be considered on its own merits but as a part of the worldwide challenge posed by the Communist threat to the peace."

The background, the geography, the entire basis of the Communist enslavement of Cuba is to be ignored, as in effect we seem to be prepared to accept the status quo of Cuba whatever it may be.

Mr. President, this approach represents a serious shift of U.S. policy, a complete reinterpretation of the Monroe Doctrine, and even more sharply a repudiation of the policies which the people of this country supported last year and the year before.

There has been a lot of talk as to what the Monroe Doctrine really means. Under the interpretations which have been forced upon it in the last few months, there is indeed very little meaning left in the doctrine. But if we can look briefly to President Monroe's own words in his seventh annual message of December 2, 1823, the essential meaning—and commonsense behind the Monroe Doctrine is perfectly clear. If we will substitute in our minds the words "Communist powers" where President Monroe spoke of "allied powers," the reasonableness and significance of President Monroe's words will be just as apparent today as when they were first enunciated.

I wish to recite briefly the pertinent part of the Monroe Doctrine. Said President Monroe:

The political system of the allied powers is essentially different in this respect from that of America. This difference proceeds from that which exists in their respective Governments; and to the defense of our own, which has been achieved by the loss of so much blood and treasure, and matured by the wisdom of their most enlightened citizens, and under which we have enjoyed unexampled felicity, this whole Nation is devoted. We owe it, therefore, to candor and to the amicable relations existing between the United States and those powers to declare that we should consider any attempt on their part to extend their system to any portion of this hemisphere as dangerous to our peace and safety. With the existing colonies or dependencies of any European power we have not interfered and shall not interfere. But with the Governments who have declared their independence and maintained it, and whose independence we have, on great consideration and on just principles, acknowledged, we could not view any interposition for the purpose of oppressing them, or controlling in any other manner their destiny, by any European power in any other light than as the manifestation of an unfriendly disposition toward the United States. It is impossible that the allied powers should extend their political system to any portion of either continent without endangering our peace and happiness; nor can anyone believe that our southern brethren, if left to themselves, would adopt it of their own accord. It is equally impossible, therefore, that we should behold such interposition in any form with indifference.

This is the substance and the core and the meaning of the Monroe Doctrine.

There is no doubt in my mind that President Monroe would clearly have considered the present situation in Cuba a direct threat against which the Monroe Doctrine should be enforced. In-

inter-American security system through the Organization of American States.

"Specifically the OAS Charter and the Rio Treaty (Sept. 2, 1947) provides the means for common action to protect the hemisphere against the interventionist and aggressive designs of international communism."

Later—on August 24, 1960—President Eisenhower said:

"The Monroe Doctrine has by no means been supplanted—it has been merely extended."

President Kennedy reaffirmed the position taken by preceding administrations relative to the Monroe Doctrine when, after the failure of Cuban exiles to invade Cuba in April 1961 he said:

"Let the record show that our restraint is not inexhaustible. Should it ever appear that the inter-American doctrine of non-interference merely conceals or excuses a policy of nonaction—if the nations of this hemisphere should fail to meet their commitments against outside Communist penetration—then I want it clearly understood that this Government will not hesitate in meeting its primary obligations which are to the security of our own Nation."

Now the situation has reached a point of decision. Shall the governments of Central and South American countries be gradually infiltrated and taken over by the Soviets? The Communist apparatus and agents already have begun to infiltrate every country, from Mexico down to the tip end of South America. If the Organization of American States does nothing and if the United States is acquiescent, the Communist foothold in Latin America will be strengthened and the Monroe Doctrine will be dead for all time.

It has been suggested that, if the United States takes forceful action in Cuba, this will cause the Soviets to raise questions about Western military bases in various parts of Europe. But this, too, would be merely a smokescreen, because Moscow knows that not a single group of military advisers or technicians from the West is today based in any of the Communist bloc countries. There is no parallel, therefore, and the issue remains whether the aggression via Cuba and the Soviet threat to Central and South American countries shall be ignored or some military and economic action shall be taken to nip it in the bud now before the buildup becomes a real menace to the security of the United States.

For in Cuba—just 90 miles from Florida—the Soviets have established their military advisers "to train Cuban servicemen," as the official Moscow communique describes it.

In accordance with precedent and custom, Mr. Kennedy may decide to ask Congress for a joint resolution authorizing him to take whatever military steps are deemed necessary to uphold the Monroe Doctrine. Since the present session of Congress may adjourn soon, such power might well be given to the Chief Executive as Commander in Chief of the Armed Forces so that he may be able to act promptly in whatever emergency may suddenly arise in Cuba or anywhere else in Latin America.

WILL CUBA BE ANOTHER "WALL OF SHAME"?

Mr. PEARSON. Mr. President, during the last 6 weeks the Soviet Union made a fateful decision to supply large-scale, industrial-military aid to Cuba. This decision by the Soviets to strengthen their foothold in this hemisphere has gone unchallenged by our Government.

Statements have been made on the Senate floor that the Soviets have landed troops in Cuba. The President

has responded that "we have no evidence of troops." The State Department admits that 3,000 to 5,000 Communist bloc "technicians," some of which are military specialists, have arrived in Cuba, along with military hardware. Whether these are "troops" or "technicians" is a matter of semantics. The clear fact is, the Soviet Union has reinforced its base within 90 miles of our shores with surface-to-air missiles, missile-equipped torpedo boats, trucks, munitions, radar and other electronic equipment, and the men who know how to use them. Moreover, while our attention has been focused on the recent arrival of 20 Soviet ships, the fact is, that over 60 ships, many of them leased from Great Britain, Greece, Norway, Italy, and West Germany—all NATO allies of the United States—have delivered Mig fighters, tanks, and artillery.

The present faltering and mismanaged Cuban economy and trumped-up fears of an American invasion have provided an excuse for the Soviets to furnish the Castro regime with these supplies and troops. The Soviet interest, however, is not concerned with the welfare of the Cuban people but with strengthening its base in this hemisphere; a base which will be costly for the United States to neutralize; a base from which it can export the Communist revolution to Latin and South America; a base from which it can apply leverage to offset U.S. activity in other areas of the world.

Cuba has thus become a strategically placed pawn in the cold war.

The next move is up to the President.

WHAT HAPPENED TO THE MONROE DOCTRINE?

The Monroe Doctrine was the result of an earlier attempt by Russia to push its domination into North America. It was announced by President Monroe in 1823 and has become a keystone of American foreign policy. President Monroe stated:

We owe it therefore to candor, and to the amicable relations existing between the United States and those (European) powers, to declare that we should consider any attempt on their part to extend their system to any portions of this hemisphere, as dangerous to our peace and safety.

The President reaffirmed this policy on September 4, 1962, but only insofar as it applies to the use of military force by Cuba to extend communism into South America. To date the President has preferred to consider the Soviet-supplied arms as defensive weapons, but recognizing their offensive potential has warned that "the Castro regime will not be allowed to export its aggressive purposes by force or threat of force."

If the Monroe Doctrine is in fact a part of our foreign policy, then it must apply to the Cuban situation in a broader sense. It must restrict nonmilitary as well as military aggression. We have learned from costly experience that a Communist aggression utilizes devices much more subtle than outright military action and granted a militarized base in the Western Hemisphere, the Soviets will export revolution to all of the Americas.

Failure to give this full meaning to the Monroe Doctrine, in this particular case,

as difficult as this might be, will make of Cuba a Western-Hemisphere Berlin wall, a wall of shame, a symbol of uncertainty and indecision.

SOLUTIONS—OPPORTUNITIES LOST

Invasion, or support of invasion, of Cuba by the United States has been ruled out by the President as antagonistic to some 220 million Latin Americans and untold millions in the undecided nations of the world. Yet it is a painful paradox to recall American military intervention in South Korea, Lebanon, and the Dominican Republic, and to observe current action in South Vietnam, Laos and Thailand, while we verbally sidestep the Soviet takeover of Cuba at our very doorstep.

The American policy of unilateral economic isolation was doomed at its inception because many members of the Organization of American States refused to cooperate. Any possibility of imminent internal Cuban collapse has now been eased by Russian economic aid.

Rebellion within a police state, heavily armed with Soviet weapons, is virtually impossible, as the Hungarians learned so violently.

Who would suggest that Castro could be wooed back to the hemisphere fold of free nations as a reformed neighbor?

MY POSITION

The responsibility for the administration of foreign affairs is vested by the Constitution in the President. Congress cannot, therefore, initiate the negotiations required to meet this deadly challenge to the sovereignty of the nations of this hemisphere. Numerous Members of Congress have warned of the danger of playing down the threat which Soviet intervention in Cuba poses. The failure of the "Bay of Pigs" invasion has apparently cooled administration enthusiasm for sponsoring a positive policy in this case.

These four positive successive steps could be taken:

First. The President should call upon the Organization of American States to condemn Cuba for its military buildup. At the same time the member countries should assure Cuba that they will not be parties to an invasion of Cuba if that country's militarizing ceases and if it abstains from subversive activities in the Americas.

Second. The President should call upon the members of NATO to discontinue the use of their ships for transporting military supplies and personnel into this hemisphere.

Third. The President should inform the Soviet Union that further shipment of military supplies to Cuba will be considered an aggressive act in violation of the Monroe Doctrine and ships carrying such supplies will be stopped and turned back.

Fourth. The President should call upon the Organization of American States to notify the Castro regime that unless free elections under OAS supervision are conducted in Cuba within a reasonable time, the threat of the Communist dictatorship to the welfare of the people of Cuba and to the security of

this hemisphere will require a full blockade of the island.

These are harsh steps with recognized dangers. Our past is dotted with the errors resulting from timidity and indecision which handed the Communists priceless victories—the Rhine, the 38th parallel, the Berlin wall. We will not be secure if Cuba is added to this list.

REVENUE ACT OF 1962

The Senate resumed the consideration of the bill (H.R. 10650) to amend the Internal Revenue Code of 1954 to provide a credit for investment in certain depreciable property, to eliminate certain defects and inequities, and for other purposes.

Mr. WILLIAMS of Delaware. Mr. President, I yield 5 minutes of my time to the Senator from Massachusetts.

Mr. SALTONSTALL. Mr. President, I shall vote against the tax bill. This has been a very difficult decision for me to make, because there are some good provisions in the bill which I would like to see put into the law, and there are some provisions in the bill of which I do not approve. In my opinion, it is a marginal bill, and for that reason it is a very difficult decision to determine how to vote on it.

The sections I would like to see become law, and which I hope will become law in any tax revision that is submitted at the first of the year by the President, concern:

First, revision of existing law with respect to the bad debt reserve provisions applied to mutual savings banks, domestic building and loan associations, and certain cooperative banks.

Second, correction of an imbalance which exists in the treatment of mutual fire and casualty insurance companies as compared to stock fire and casualty insurance companies.

Third, revision of the tax treatment of cooperatives and patrons.

Fourth, elimination of some tax havens abroad and lobbying abuses.

These are all provisions which would be helpful, and I would like to see them included in a tax revision bill.

Contrasted with these favorable provisions, is the question of the provision for investment credit. I voted against this section when it came before the Senate as an amendment, which, as I understand, would result in an annual revenue loss of approximately \$1,300 million. This provision is not fair, as I see it, because it will help some industries, but not others which are in the same category and in the same position.

I am in favor of a proper allowance for depreciation that will not be limited to a specific period of time. If industries have a proper allowance for depreciation, they will have a greater opportunity for improving their plants.

In addition, as a member of the Appropriations Committee, I have watched the appropriation bills this year. I cannot see that we have been able to effect any substantial decrease in appropriations to any of the departments; certainly we have not been able to do so up to the present time. We know that with

the problems we have in relation to our national security the Defense Department appropriations are going to increase over the next few years, rather than decrease.

So this issue involves the question of constant Federal deficits and a constant drain on our gold supply.

These are very fundamental reasons for opposing the bill. Although, as I have said, it does contain some good provisions, it is still a marginal bill. If the Senate passes the bill, it will then go into conference. There are more provisions in the House version of the bill that I would oppose. The Senate conferees will be in a position of having to yield something to the House conferees, which may result in the version of the bill containing certain provisions which I might strongly oppose.

We are also told there will be a new tax bill submitted for our consideration next year.

The bill, as amended by the Senate, would decrease governmental revenues on a full-year basis by \$585 million, and I believe perhaps even more.

For all the reasons I have stated, I shall vote against passage of the bill. As I say, I do it with considerable hesitation because of the good features in the bill, and because we know certain tax provisions should be improved. The overall balance is against the bill, and I shall vote against its passage.

Mr. WILLIAMS of Delaware. Mr. President, I yield 10 minutes to the Senator from Pennsylvania [Mr. SCOTT].

INFORMING THE AMERICAN PEOPLE ON WHAT IS REALLY HAPPENING IN CUBA

Mr. SCOTT. Mr. President, in his September 5 statement on Cuba, President Kennedy said that the administration would "continue to make information available as fast as it is obtained and properly verified." All Americans, I am sure, received this assurance with much relief. The American people become very restless if facts to which they are entitled, without danger to our security, are not made promptly available to them so that they can understand the policies of their government. To a certain extent, the assurance by the President of a steady flow of facts will do much to prepare the American people for developments in our foreign policy.

It should be noted that revelations to date with regard to the very serious crisis in Cuba have come on the initiative of the press and of the Congress. Revelations have been made by the press which were not made to the American people by the State Department and which were not the subject of statements by the President. They were revealed by such eminent Members of each body as the distinguished junior Senator from New York [Mr. KEATING], the distinguished Representative from California, Mr. HOSMER, and several others.

Right now, many Americans are worried about published information which has not received verification from the administration. Especially numerous are reported facts of this sort

about the Cuban situation. American fears could be alleviated if President Kennedy would fill the information vacuum concerning Cuba by "obtaining and properly verifying" the following news reports:

First. Is the international brigade of Communists in Cuba now numbering in the thirty-thousands? Is this brigade partially composed of 1,500 Ghanaian troops, 900 Red Chinese, 200 Algerians, and numerous Communist contingents from other Latin American countries? Are other troops from Asia and Africa billeted in Cuba? Where are these troops located? Are the Russians in Las Villas Province, the Red Chinese on the Isle of Pines, and the Ghanaians near Cienfuegos and Mariel? How many other Communist countries have military and technical personnel and in what numbers?

A dispatch by a writer for the London Daily Mail points out, for example, that from 5,000 to 8,000 Russians have arrived so far. The writer states:

A Western ambassador in Havana told me categorically:

I should like for Senators to note this quotation, because if the Western ambassador could talk to a London newspaperman, I ask whether anybody is talking to our State Department about the same things. And if they have been talking to our State Department, why have the American people not been told?

I read what the Western ambassador said:

I have reported to my government, despite all denials, that many of these men are Soviet troops, that they are arriving in increasing numbers, and this is all part of a carefully planned military operation to underwrite the Castro regime.

The writer of the article also says:

Arrivals of the Russians in large numbers is seen by many diplomats in Havana as driving a final nail into the coffin of the Monroe Doctrine—the statement of U.S. foreign policy which established, over a century ago, the "hands off" attitude to outside powers with ambitions in the American hemisphere.

This much is certain from what I have just seen in Cuba:

No large-scale attempt to overthrow the Castro regime could now be launched by the United States or Cuban exiles without Russian blood being spilled in the process.

I watched the Russians in two separate encampments—after being told they were a "ghost army" existing only in the imagination of Americans.

They looked pretty healthy ghosts to me.

That has to be contrasted with the President's press conference statement of "no troops," and with the incredible letter received by the Senator from New York [Mr. KEATING], on the 30th of August, stating that we have no information that any Soviet bloc troops have landed in Cuba.

However, I wish to congratulate the Senator from New York for hearing from the State Department, in reply to his letter of August 14, by letter of August 30, which is only a 16-day lapse in the reply to a minority Member of this body. I think that establishes a record. I hope that someday we may hear from them in even as brief a period of time as 13 days, or perhaps even 14

days after we address a communication to them.

I hope the President will have an opportunity to obtain the reports and to properly verify them.

Second. Is the Soviet Union setting up a base in Cuba for the tracking of space experiments? I refer to our space experiments off Cape Canaveral.

Third. How many missile sites are in being or are planned for the near future, using Soviet missiles? What is the range of such missiles?

Fourth. Is the Soviet Union supplying Cuban Communists with diversified late-model weapons? Is there a ring of such weapons—heavy artillery and anti-aircraft guns—surrounding the U.S. base at Guantanamo? Are all the Russian arms shipments payments or base rights given to them by Castro?

Fifth. How large is Castro's army? Does it now contain in the neighborhood of 300,000 troops? Is this the largest army in Latin America?

Sixth. Have Soviet Migs replaced the United States and British warplanes in the Cuban air force? Are there more than 100 jet fighters at 14 bases in Cuba?

Seventh. What is the significance of the arrangements for establishment of regular airline service between Havana and Moscow?

Eighth. Are the Russians handling all the installment of modern military equipment in Cuba? Is the operation of all such equipment in the hands of the Russians also?

Ninth. What is the precise number of Red Russian-owned or leased ships now docking at Cuban ports? Is the increase considerably higher than the 60 ships observed since mid-July?

Mr. President, all the above facts, if verified, clearly point to a violation of the Monroe Doctrine by the Soviet Union. I believe that most, perhaps all, can be verified. The Doctrine warns greedy foreign powers that "we should consider any attempt on their part to extend their system to any portion of this hemisphere as dangerous to our peace and safety." Mr. President, Khrushchev has already said that the Monroe Doctrine is dead. Castro has called the Doctrine a worthless document. Plainly both of these Communists are taking themselves seriously and acting as if the Doctrine did not exist.

But the Monroe Doctrine does exist. The big question is whether the United States intends to implement it. On this point, the President of the United States has again assured us that our Government "will not hesitate in meeting its primary obligations, which are to the security of our Nation." But the news items I have gathered do raise the question "when is the security of our country threatened?" When Communist infiltration of the magnitude now going on in Cuba takes place, many Americans feel that a definite threat already exists. President Kennedy could well allay these fears by acting as quickly as possible in examining, verifying publicly and mak-

ing available to the American public the whole story of this Red base of operations 90 miles from our shores.

If the facts are true, then a number of steps are open to the United States to deal with the Communist menace. Among the most feasible is to convince the Organization of American States to deal firmly with Castro. Mr. William S. White in his September 5 column has this to say:

We should try one more time to persuade the Organization of American States to act in honesty and honor against the Soviet cancer in the Caribbean.

The Secretary of State has called a conference of Latin American ambassadors. I suggest that we request all of our neighbors in this hemisphere to join with us in convening the Organization of American States, that we take the lead in securing the consent of as many of them as will join us in a multilateral warning to the Communist States to cease the arming in Cuba. I propose that we set a deadline, after which we should proceed, multilaterally if possible, unilaterally otherwise, to declare foreign military exports to Cuba to be contraband and subject to blockade. If we do so proceed, we can stop Communists from exporting revolutions to this hemisphere. If we do not, we will before long be faced with Communist dictatorships elsewhere in Latin America.

The PRESIDING OFFICER. The time of the Senator has expired.

Mr. WILLIAMS of Delaware. I yield an additional minute to the Senator from Pennsylvania.

Mr. SCOTT. Mr. President, I ask unanimous consent to have printed at this point in the RECORD a report known as an uncensored, eyewitness report entitled "Russians in Cuba Are Real," appearing in the Harrisburg Patriot and the article by Columnist William S. White to which I previously referred.

There being no objection, the articles were ordered to be printed in the RECORD, as follows:

COLUMN BY WILLIAM S. WHITE

WASHINGTON.—The Soviet Union's publicly boasted military penetration of the Western Hemisphere in Castro Cuba is many things, apart from the most insolent menace to the New World that the United States has ever tolerated.

It destroys forever the airy assurances of pseudo-liberals that revolutionary movements are fine things indeed—so long as they involve leftwingers.

It places a terrible responsibility before history upon all those Americans who cheered Fidel Castro on in Cuba long past the point where it was plain that he was transplanting the evil fungus of armed international communism to within 90 miles of our Florida coastline.

It bankrupts the whole evangelistic theory, parroted with religious fervor, that communism results from capitalistic injustice, et cetera, and will vanish at once, given the spreading of sufficient welfarism among the masses.

Cuba, before Castro, was never half so underprivileged as dozens of other lands which have never sought the lethal embrace of Moscow.

It fully supports what has long been fully obvious—that communism, like Hitlerism

before it, is a movement of bandit ferocity and cannot be explained by old-lady minds as simply springing from too little milk for the kiddies and too little free land for the workers and peasants.

It brings into the gravest question the practicality of the vast effort being made by the United States through the Alliance for Progress to cure all the ills of Latin America with economic aid.

Foreign aid is a sound and splendid thing—when it is given to nations willing and able to use it for freedom's strength and openly and unashamedly against communism.

But the bulk of the more powerful Latin American nations, while avidly ready for our economic aid, have repeatedly refused to follow us in any total quarantine of Castro Cuba. It is fashionable to say that we, the United States, should never force our views upon the recipients of our aid.

This is the line even when precisely our views are essential to maintain that freedom from "foreign domination" for which the Latins so endlessly clamor—especially those who have snuggled up closest to international communism.

Brought into question, too, is the very validity of the Organization of American States. This association of the nations of this hemisphere was created to prevent just the kind of foreign penetration which is and long has been so openly involved in Castro Cuba.

But an effective majority of the OAS has thus far been unwilling to take any fully rational step against Castro Cuba. The most ironic of all excuses is given by the nation closest in geography to us, Mexico. She has said that while she would like to help, she just can't find any precedent for it in international practice. There is a sour taste in this—for Mexico, of course, is famous for its scrupulous respect for both law and justice.

So what is now left to the United States? We should try one more time to persuade the Organization of American States to act in honesty and honor against the Soviet cancer in the Caribbean. Failing this, we should raise a new collective military organization from among the minority who are our real friends in Latin America.

Much the same was done in 1949, when we created the North Atlantic Treaty Organization from within the United Nations when it became clear that the U.N. would do nothing about Soviet aggression in Europe.

And failing this, the United States should act alone to clear the Soviet military apparatus from Castro Cuba, come what might.

UNCENSORED, EYEWITNESS REPORT—RUSSIANS IN CUBA ARE REAL

(By Keith Morfett)

(EDITOR'S NOTE.—Keith Morfett, roving Latin American correspondent, for the London Daily Mail, has visited Cuba eight times during the past 2½ years, most recently last week. He flew to Miami to write the revealing, uncensored story which the Patriot presents here because of its significance in the light of the Soviet buildup in nearby Cuba.)

Thousands of strapping young Russians are moving quietly into tented military encampments close to the outskirts of Havana in a vast Soviet buildup that is causing deep concern among diplomats in the Cuban capital.

From 5,000 to 8,000 Russians have arrived so far.

A Western ambassador in Havana told me categorically:

"I have reported to my government, despite all denials, that many of these men are

Soviet troops, that they are arriving in increasing numbers, and this is all part of a carefully planned military operation to underwrite the Castro regime."

Many of the Russians are in their early 20's. All have reached Cuba aboard three Soviet passenger liners.

At the same time, a continuous armada of cargo ships is now stretched out between Russia's Black Sea ports and Cuba, carrying trucks, jeeps, machinery, food, guns—and ground-to-air missiles for Fidel Castro's armed forces.

Arrivals of the Russians in large numbers is seen by many diplomats in Havana as driving a final nail into the coffin of the Monroe Doctrine—the statement of U.S. foreign policy which established, over a century ago, the "hands off" attitude to outside powers with ambitions in the American hemisphere.

This much is certain from what I have just seen in Cuba:

No large-scale attempt to overthrow the Castro regime could now be launched by the United States or Cuban exiles without Russian blood being spilled in the process.

I watched the Russians in two separate encampments—after being told they were a "ghost army" existing only in the imagination of Americans.

They looked pretty healthy ghosts to me.

Hefty, athletic, and looking a lot better fed than their Cuban hosts, they crowded up to barbed-wire fence at the first camp I found near the village of El Cano.

They appeared to be members of the kind of unit usually moved in advance of regular fighting troops to set up camps, establish communications networks and accomplish other related chores.

In the tropical heat they looked unhappy and homesick. They had cloth caps and denim trousers and clustered together for comfort like sheep on the range in a rainstorm.

The contrast between the El Cano crowd and the next lot I looked at was so great that it became clear Cuba's Russians fall into two distinct categories.

The El Cano Russians were recruited into "labor battalions" rather like the British Army's Pioneer Corps. They will dig ditches, lay cables and do all the donkey work.

A few miles away, down a rutted side road the whole countryside was suddenly swarming with Soviets. This time they were obviously on different business. Hundreds of them moved around among military vehicles parked under trees, in fields alongside hedges and between row upon row of khaki-colored tents.

Nearby, antiaircraft guns in freshly dug pits were manned by Cuban militiamen. Machineguns were mounted at all approach roads into the camp. By the tasks they were doing, checking their equipment on radio trucks, command vehicles and signal equipment, these Russians appeared to be military technicians such as signal, staff, and electronic engineers.

REVENUE ACT OF 1962

The Senate resumed the consideration of the bill (H.R. 10650) to amend the Internal Revenue Code of 1954 to provide a credit for investment in certain depreciable property, to eliminate certain defects and inequities, and for other purposes.

Mr. MANSFIELD. Mr. President, I yield 7 minutes to the Senator from Oklahoma.

Mr. KERR. Mr. President, H.R. 10650 is important urgent tax legislation. At a time when we are concerned with the rate of growth of our economy, it offers

effective stimulus to that growth. At a time when we are concerned with the continuing deficit in our balance of payments, it offers significant help to reducing and eliminating that deficit—and thus reducing the chronic drain on our gold reserves. At a time when we are concerned with the effect of our tax system on our society and our economy, it offers a solution to a number of long-standing tax problems. The provisions of this bill have been voted by the Senate after more than a year of careful consideration in the Congress, after 5 months of hearings and work by the Senate Finance Committee, and after more than a week of debate in this Chamber.

H.R. 10650 is a sound bill. Its provisions correct inequities and remove loopholes which have defied solution for years—the taxation of business income earned abroad, the taxation of personal income earned by nonresident citizens, the collection of taxes on interest and dividend income, the tax treatment of entertainment and travel expenses, the taxation of cooperatives, mutual thrift and mutual fire and casualty insurance companies, and the taxation of proceeds from the sale of depreciable property.

H.R. 10650 taxes those who have escaped taxation in the past, but, in no case is it punitive in intent or effect. Throughout the long process of shaping this bill both the Congress and the Treasury have met with responsibility and with understanding the needs of American business.

The main provision of the bill—the investment credit—will, I am convinced, in years to come, be viewed as the most important single measure to strengthen and revitalize the American economy enacted by the 87th Congress. It will provide American producers with the stimulus they need both to modernize to meet foreign competition and to accelerate expansion of our domestic economy. In addition, the foreign income provisions are designed to prevent any possible interference with productive American business operations overseas, and one particular section is specifically designed to assure that no additional burden is placed on firms primarily engaged in the sale of American-made products.

The sections of the bill covering taxation of income earned abroad are not aimed at capturing every possible dollar of tax revenue. They are aimed at ending tax abuses which harm this country by discouraging the return flow to our shores of dollars earned overseas. For balance-of-payments reasons, it is vitally important that we remove these tax barriers against the repatriation of money earned abroad by American citizens and American businesses.

Two other provisions deserve mention:

The reporting requirement on dividend and interest income may not be as effective as withholding, but it represents a significant step forward in an area in which tax evasion has long been widespread.

The provision covering travel and entertainment expenses, as voted by the

Senate, puts us in a good position to work out in the conference committee an effective means of curbing disgraceful abuses without interfering with genuine business travel or entertainment.

Finally, the bill is one which reflects a high degree of fiscal responsibility. While some initial revenue loss is possible, the fact remains that over the long run, enactment of H.R. 10650 will contribute immeasurably to the growth of the American economy. This will mean larger tax collections, without higher tax rates in the years to come. Now there are estimates that the full year revenue loss under the bill as amended would be as low as \$240 million. The highest estimate—the one made by the staff of our Joint Committee on Internal Revenue Taxation—reaches \$585 million. My own estimate is that the loss even in the beginning would be much less than either.

The distinguished Senator from Virginia [Mr. BYRD], in offering his reporting amendment to the bill, stated that in his judgment it would be as effective in collecting taxes as the withholding amendment would have been. I say that if it is half as effective, there will then be no deficit by reason of the enactment of the bill.

Will anyone seriously argue that this is too high a price to pay for legislation to increase the growth and vigor of the American economy, to strengthen our Nation's economic position in the world, and to improve the fairness of our tax system?

In summary, this bill gains ground in almost every single area sought by the President. It provides a critically needed source of new vitality for our domestic economy. It contains significant help to our balance of payments position. It plugs a number of tax loopholes, it removes a number of tax inequities, and it does these things without imposing hardship on any single taxpayer or on the taxpaying American public as a whole.

It is a good bill, and I believe it deserves the support of every Member of this body who would help build a stronger, healthier, revitalized American economy.

The bill as it is before the Senate has the support of the administration through the Treasury Department. That is a well-known and significant fact. I hope that it will be passed.

The PRESIDING OFFICER. The time of the Senator has expired.

Mr. MANSFIELD. Mr. President, I yield 2 additional minutes to the Senator from Oklahoma.

Mr. KERR. On page 17367 of the RECORD for September 4, I ask unanimous consent that the language beginning at the figure (3) down to and including the equation designated as "(4)" be printed in the RECORD.

There being no objection, the excerpt was ordered to be printed in the RECORD, as follows:

(3)

$$I_t = a[AP_{t+1}/S_{t-1} - (P/S)_t]$$

where I_t is investment, in real terms, in a given year t ; AP_{t+1} , output anticipated in the given year for the next year, $t+1$; S_{t-1} , the

amount of capacity in existence in the previous year; and a , a proportionality constant, reflecting the intensity of response to the stimulus to invest as well as the cost of providing additional capacity.

Since we have no direct information on anticipated output, AP_{t+1} , it is necessary to introduce some hypothesis as to how this variable might be approximated. Methods frequently used by electric utilities for estimating prospective demand are based on their past experience and amount roughly to an extrapolation of the sales trend. Since the latest information available on output is P_{t-1} , then, if demand is assumed to grow at a constant rate of i percent per year, we may write

$$AP_{t+1} = (1+i)^2 P_{t-1}.$$

This leads by substitution in equation (3) to:

(4)

$$\begin{aligned} I_t &= a[P_{t-1}(1+i)^2/S_{t-1} - (P/S)_t] \\ &= a(1+i)^2[P_{t-1}/S_{t-1} - 1/(1+i)^2(P/S)_t] \\ &= a'[P_{t-1}/S_{t-1} - (1-\gamma)(P/S)_t] \end{aligned}$$

where $a' = a(1+i)^2$ and $\gamma = 1 - 1/(1+i)^2$.

Mr. KERR. I say to the distinguished Senator from Wisconsin, who said that what he put in the RECORD was well known to himself, I would be very glad if at the appropriate time he would demonstrate his mastery of the science of mathematics and the information he put in the RECORD, by explaining it either orally or by written word of his own. If he would do so, the Senator from Oklahoma would be grateful.

Mr. BUTLER. Mr. President, I should like to ask the Senator from Delaware to yield me some time so that I may ask some questions of the Senator from Oklahoma.

Mr. WILLIAMS of Delaware. I yield 2 minutes to the Senator from Maryland.

Mr. BUTLER. Mr. President, earlier this week the Senate voted to eliminate subsection (C) of section 3 of H.R. 10650. This subsection was added by the Finance Committee as the result of an amendment which I proposed.

That amendment, as reported by the Finance Committee, would have made deductible ordinary and necessary business expenses incurred "in direct connection with communication of information between the taxpayer and an employee or stockholder with respect to legislation or proposed legislation of direct interest to the taxpayer."

In view of the adoption of section 3 without the amendment proposed by the Committee on Finance, would the cost of preparing and distributing the annual reports of companies be deductible if such reports comment on the pendency or the likelihood of legislation which would directly affect the company if the report does not exhort stockholders to write their Representatives or Senators with respect to such legislation?

Mr. KERR. I believe the answer to the Senator's question is "Yes," if there is no suggestion that they intervene by seeking out their legislators.

The PRESIDING OFFICER. The time of the Senator has expired.

Mr. WILLIAMS of Delaware. I yield 1 more minute to the Senator from Maryland.

Mr. BUTLER. Would section 3 as adopted by the Senate also make deduct-

ible the expenses of preparing and distributing regularly published internal news media intended for the information of employees or stockholders if such media comments on the pendency or the likelihood of Federal, State, or local legislative activity which would have direct impact on the company if such media does not exhort stockholders or employees to take any affirmative action with their Representatives or Senators, or other legislative representatives?

Mr. KERR. I believe the answer to that question is "Yes," if there is no suggestion that they intervene by seeking out their legislators.

Mr. BUTLER. Is the Senator's understanding that section 3 as approved by the Senate would also permit the deductibility of the cost of preparing and conducting or circulating other communications to employees or stockholders, if such communications are informative only and do not seek legislative action or the part of the recipients?

Mr. KERR. The answer is "Yes," if there is no suggestion of seeking legislative action, and the material is not designed or intended for that purpose.

Mr. BUTLER. I thank the Senator.

Mr. MANSFIELD. I yield 1 minute to the Senator from Florida.

Mr. SMATHERS. I associate myself with the able Senator from Oklahoma in stating I believe that this is a good bill. Actually this bill has been criticized from the so-called liberal side because Senators on that side believe it does not go far enough. It has been under fire also from what we call the conservative side, because Senators on that side feel that the bill goes too far. That is usually the legislative process; that happens when we finally get a good bill.

The bill closes many loopholes. It brings into the Treasury approximately \$755 million in the closing of the loopholes. On the other hand, by virtue of the investment credit features, the outflow is a little more than \$1 billion, which is calculated solely for the purpose of stimulating the economy.

I congratulate the very able Senator from Oklahoma who is in charge of the bill on the floor of the Senate, for his leadership in this whole matter. I congratulate also the able chairman of the Committee on Finance, the Senator from Virginia [Mr. BYRD] for the contribution which he has made. It is a good bill. It deserves the endorsement of the Members of the Senate.

Mr. WILLIAMS of Delaware. I yield 5 minutes to the Senator from New York.

Mr. JAVITS. Mr. President, I have had a struggle with my conscience about this bill, and I finally decided to vote in favor of it, for these reasons.

I believe the bill is a start upon that degree of tax reform, and especially tax incentive reform, which I have myself urged very strongly be undertaken this year and not deferred until next year.

I still believe that the President is unwise, in the interest of the economy, which, notwithstanding a few rosy glows, still shows that it needs the incentive and forward drive which an incentive

tax cut would give, in not proposing his plans to us this year but, instead, deferring them until next year.

We shall at least begin, in the bill, with this kind of tax reform.

Hence, I feel that that preponderates over the reservations which I have with respect to a number of features of the bill.

My reservations relate to certain provisions of the bill. For example, regarding the so-called lobbying expenses, though I think they could be somewhat justified on the ground that freedom of action in business management should equate generally with freedom of action in trade unions, the whole provision needs judicious handling by American business and effective enforcement by the Federal Government.

I believe that the provisions for the taxation of controlled foreign corporations will inhibit American business instead of freeing its hands in terms of foreign competition, which is urgently needed in the interest of the American economy and of our peace leadership in the world. However, I believe that the Senate provision is superior to the House provision in this respect, and I hope—if I may have the attention of the Senator from Oklahoma to my remarks on this subject—that the Senator from Oklahoma will be as tough minded in the conference on the matter of the Senate's provision with respect to section 12 as he has shown himself to be durable and capable on the floor of the Senate.

With respect to the provisions dealing with entertainment expenses which are contained in the bill, I believe that the provisions now in the law could be administered effectively for that purpose. However, I do not see that any very great harm will be done by this provision of the bill in terms of what is legitimate and accepted in promoting American business activities.

I am gratified that the provision for withholding taxes on dividends and interest has been deleted in the Senate bill because I believe that it was burdensome and unworkable, particularly for low-income recipients. The proposal which I and others made to the Finance Committee, for increased reporting by payers of interest and dividends to the Internal Revenue Service, has been adopted and will enable the new automatic data processing equipment to aid enforcement. Again, I very strongly urge the Senate conferees to insist on the Senate provision.

Finally, with respect to the equipment tax credit, I know that it is not in favor with some elements of business, and that it is not in favor with some elements of labor. I have the highest respect for people who feel that way. However, I deeply believe that the American productive machine is falling so rapidly behind in terms of obsolescence that we must not only couple the equipment tax credit with the new depreciation schedules which we are giving American producers, but must also put the whole impact of public opinion behind the fact that the credit should and must be used for new equipment.

Estimates as to the amount of the American industry's equipment which is obsolescent are ghastly. It is estimated it will take \$95 billion in new investment to bring the American business machine abreast of its responsibility.

For all of these reasons I shall vote for the bill, knowing always that legislation is neither black nor white, but gray. I believe that the advantages preponderate over the disadvantages. I especially emphasize, in closing, the fact that this is the first installment on tax reform and tax incentive urgently required if we are to get the economy moving forward, as the President promised in the 1960 campaign, but which he definitely has not done yet, as witnessed by the figures on endemic employment and other indexes such as the lack of confidence in many quarters in the economy. I add merely that I deplore greatly the unwillingness of the President and the administration to share their "creative tax plans," to use the words of the President, with the country, as I believe this would be an earnest to the country of the intention to go through with a truly effective tax reform program early in 1963.

As the matter stands now, with the President submitting his plans next year, we shall be lucky to get tax reform by late in the next session of Congress, when we should be thinking about it, at the latest, in January, February, and March.

I thank the Senator from Delaware for yielding time to me.

Mr. MANSFIELD. Mr. President, I yield myself 6 minutes.

I shall not detain the Senate long. I recognize that after a debate of 9 days Senators are anxious to get on to other matters. But I want to take a few moments to explain my position on the bill, and to indicate the Treasury's position by means of a letter I have received from Secretary Dillon.

First, Mr. President, I pay my respects to the arduous work done by the Finance Committee in the consideration of the bill. That committee has had a heavy agenda during this session of the 87th Congress, and in order to resolve that agenda its members have had to make considerable sacrifices. In particular, I pay tribute to the beloved chairman, the Senator from Virginia [Mr. BYRD], to the able floor manager of the bill, the Senator from Oklahoma [Mr. KERR], and to the ranking minority member, the Senator from Delaware [Mr. WILLIAMS]. I should also like to commend two members who dissented from many of the committee's recommendations, and who, through pertinent and well-argued debate, put their case to the Senate. I refer to the Senator from Tennessee [Mr. GORE] and the Senator from Illinois [Mr. DOUGLAS].

Mr. President, H.R. 10650, as amended, is an imperfect measure; it does not entirely satisfy any Member of this body. The Senator from Virginia, the Senator from Wisconsin [Mr. PROXMIER], the Senator from Illinois, and other Senators would prefer to eliminate the investment incentive from the bill. The Senator from Oklahoma, the

Senator from Montana, and other Senators would have preferred a more effective provision relating to the collection of revenues due from dividends and interest. The Senator from New York [Mr. JAVITS] and the Senator from Minnesota [Mr. McCARTHY] believe the foreign tax provisions are too stringent. There are other parts of the bill that find Senators in opposition, and there are omissions in the bill that many Senators regret. In this respect the situation is no different from that which has prevailed upon the adoption of every other tax bill that has come before Congress in my time. Because a major revenue measure is ultimately bound to affect every aspect of our economy, it reflects the divisions of interest that characterize the economy itself. The decisive question must be, not whether the bill is perfect in every respect, but whether, on balance, it serves the national interest.

In my judgment, this bill does.

Its major provision contains a credit for new investment in machinery and equipment. In the opinion of the Secretary of the Treasury, this tax incentive is necessary for the modernization of the American industrial plant. In the opinion of virtually every other qualified observer, the modernization of our industrial plant is necessary if this country is to compete in the world economy of the 1960's.

We are, I trust, about to adopt a major trade program that will enable us to deal with the great new economic engine represented by the EEC. In the trade relationships envisioned by the trade bill, there will be few benefits for a nation stuck with an antiquated industrial plant. We must modernize if we are to trade on favorable terms. The new depreciation schedules put into effect by the administration during the summer, and the investment incentive provided in this bill, are, in the judgment of men who bear the responsibility for American fiscal policy, essential to modernization.

The bill contains other salutary features. It raises new revenue from mutual thrift institutions—a long overdue reform in the tax schedules; it closes a number of tax haven abuses; it throws the burden on the taxpayer, instead of the Government, to prove that his entertainment expenses were required by his business activities. In some respects the House bill is stronger in dealing with these abuses, and I express the hope that the bill will be toughened by the conference.

As for the revenue loss occasioned by the investment incentive, and by the absence of a withholding provision: The Treasury's estimate is that the bill falls short of a balance by about \$210 million on a full-year basis. The Secretary says, however, that "this is a gross estimate that does not take into account the feedback effects of the investment credit. When those effects are considered, it is my judgment that the bill is at least in balance."

Mr. President, I ask unanimous consent that the letter from Secretary Dil-

lon to me, dated August 27, 1962, be printed in the RECORD.

There being no objection, the letter was ordered to be printed in the RECORD, as follows:

AUGUST 27, 1962.

HON. MIKE MANSFIELD,
U.S. Senate.

DEAR SENATOR MANSFIELD: The tax bill now before the Senate has a direct and important bearing upon the future course of our economy. It might be helpful, therefore, if I summarize briefly the administration's views on this key measure.

Both the Congress and the Treasury have worked long and painstakingly on this legislation, which has been under consideration since April 1961. The problems it seeks to solve are as difficult as they are important, and they clearly warrant the time devoted to dealing with them.

The President, in his tax message of April 1961, recommended that action be taken in a number of areas. In reviewing the bill in its present form, I find that, while the administration program has not been fully accepted, there has nevertheless been a significant advance over present law in all but one of the areas contained in the President's recommendations—the dividend credit and exclusion. The bill includes one major provision not requested by the President: deduction of certain lobbying expenses.

The central element of the President's recommendations was the need for an incentive for investment in machinery and equipment that would stimulate a higher rate of economic growth and better enable our industry to compete in markets at home and abroad. The investment credit contained in this bill will operate as a powerful stimulus to investment. In combination with the Treasury's recent administrative reform of depreciation, the credit will, at long last, give to American business tax treatment on new investment in machinery and equipment approaching that of its chief competitors in Western Europe, Canada, and Japan. Its adoption will constitute a major advance toward our national goals of greater economic growth and the increased productive efficiency and competitiveness necessary to a solution of our balance-of-payments problem.

To offset the initial revenue loss involved in the investment incentive—and to achieve much needed reforms in our tax laws—the President recommended a number of important changes in those laws. As I have stated, the bill contains provisions which deal with all but one of the areas in which changes were requested by the President. For example, solutions have been found for problems that have long plagued the Congress concerning the taxation of mutual thrift institutions, cooperatives, and mutual fire and casualty insurance companies. The bill's provisions will effect a far greater degree of equity in the tax treatment of these mutual institutions in relation to their competitors.

In the area of depreciable personal property, the bill closes a broad avenue of potential abuse under which ordinary income could be converted to capital gains on the sale of depreciable property. The bill thereby permits the Treasury's recent and much needed administrative reform of depreciation to operate without any possibility of windfall tax gains on sale of assets subject to faster depreciation.

In the field of foreign income, the bill at one stroke would sweep away abuse after abuse possible under present laws that now permit very significant escapes from taxation. The core of these changes lies in the "tax haven" provisions of the bill, which provide a workable set of rules to end the abuses we all know exist in this area. These rules have

been carefully constructed to avoid hampering the expansion of our export trade or restricting business activities that are not artificially tax motivated. When one takes account of the wide variety of our foreign activities abroad, the highly technical nature of present law in this area, and the divergent opinions on the concept of tax deferral for foreign income, the provisions of the bill in this area represent a major accomplishment.

Along with ending tax haven abuses, the bill is designed to shut off such avenues of escape from our tax laws as the establishment of foreign residence by individuals seeking to free their earnings from tax, the creation of foreign trusts to enable them to accumulate income tax free, the resort to foreign investment companies to convert ordinary income into capital gain, the investment in foreign real estate to escape our estate tax laws, and—as respects dividends earned in developed countries—the under-taxation that exists because of the partial double counting of foreign taxes under the foreign tax credit. The bill will also greatly strengthen the administration of our tax laws on foreign income through the establishment of more effective information and reporting requirements.

As for expense accounts—a problem that has concerned the Congress for a number of years—the bill contains provisions that will strengthen the hand of the Internal Revenue Service in ending flagrant and unconscionable abuses that have led us to be known as an “expense account society.” In addition to requiring detailed substantiation of entertainment and other expenses, the bill and accompanying committee report propose standards of deductibility with respect to entertainment, business gifts, and travel that are substantially more restrictive than present law. While the improvement over present law is marked, it is still considerably less than that recommended by the administration or that provided in the version passed by the House. In addition, the Finance Committee's report on expense accounts is not as clear as could be desired and is likely to raise difficult problems of interpretation in the future.

I regret that the Senate Finance Committee bill does not contain the withholding approach adopted by the House to end the present evasion of taxation on dividends and interest. But the committee bill does recognize that persistent evasion in this area is an extremely serious matter and must be halted. The dual requirement to report information on dividend and interest payments, both to the Government and to the payee, is bound to improve compliance and enforcement in this field. Nevertheless, this is a matter on which we must focus constant attention, for it is imperative that our tax laws be enforced. I therefore feel—as does the President—that the affirmative advantages of withholding will inevitably be recognized.

There is one provision of the bill that was not in the President's message—a deduction for certain lobbying expenses. This is a provision which the administration has consistently opposed for reasons set forth in my testimony before the Senate Finance Committee.

Now, for the fiscal aspects of the bill, our estimates show that it falls short of a balance by \$210 million on a full-year basis. However, this is a gross estimate that does not take into account the feedback effects of the investment credit. When those effects are considered, it is my judgment that the bill is at least in balance.

We would, of course, have preferred that the bill be in balance even on a gross basis. The inclusion of the withholding requirements on dividends and interest would have achieved that balance. In fact, withholding

would have produced an overall revenue gain under the bill of about \$300 million.

Even without the withholding provisions, however, the bill as reported provides more than \$800 million of new revenue from tax reforms. This revenue offsets practically all of the gross cost of the growth incentive embodied in the investment credit. Indeed, if the dividend and interest information reporting requirements of the Senate bill prove to be as efficacious as the committee staff estimates and half of the gain that we would realize from withholding is achieved through the application of those requirements then, under the Treasury's estimate of the revenue presently lost through evasion in this area, the revenue-raising features of this bill would be increased to just under \$1 billion. This would leave the bill approximately in balance on a gross basis.

In closing, I would like to say that the bill now before the Senate represents a major advance toward our national goal of a revised and modernized tax system. In its tax reform provisions the bill makes substantial headway in eliminating many long recognized abuses. The investment credit provides a significant stimulus both to economic growth and to the maintenance of America's competitive position in the world—an important consideration as we enter a new era of freer trade. The bill, in short, is a significant first step toward the reform of our present outmoded tax laws. As such, I believe it merits the support of every Member of the Senate, and I urge its favorable consideration and passage.

With best wishes.

Sincerely,

DOUGLAS DILLON.

Mr. MANSFIELD. In summary, Mr. President, the bill appears to be desirable and in the Nation's interest. It ought to be stronger, in my opinion; I hope it will be when it goes to the President. There has been a great outcry from some quarters that it does not close all the loopholes and meet all the abuses that are thought to exist under present law, and indeed the bill does not meet all the expectations of the Senator from Montana. But I think it is well to remember the advice of Mr. Dooley, as he was quoted the other day by the Senator from Minnesota [Mr. McCARTHY]. He told of a lady who could never seem to keep her boardinghouse entirely clean; she worked from morning until night, and still it showed signs of dirt and damage. She despaired; she said it was like a pigpen. “Madam,” said Dooley's friend Gallagher, “the trouble with this house is that it is occupied entirely by human beings. If t'was a vacant house,” he says, “it cud aisily be kept clean.”

Mr. President, I urge the passage of this imperfect bill.

Mr. President, I yield 2 minutes to the distinguished Senator from Minnesota.

Mr. HUMPHREY. Mr. President, the tax bill now before the Senate should be passed.

It is true that there is perhaps no single section of the bill to which objections cannot be raised—on the ground that it goes too far—or, conversely, not far enough. But it is equally true that every single section nevertheless embodies progress toward achievement of a fairer tax structure. In addition, this legislation contributes to our domestic economic growth and to improvement in our balance of payments position. These

contributions are of great importance when we face such heavy responsibilities on the international scene.

This bill has been represented by opponents as a hodgepodge of compromises which may even make our overall tax system worse rather than better. The changes made in administration proposals by the other body have been criticized, the changes and amendments made by your committee after 5 months of hearings and work have been criticized. The changes made by this body have been criticized.

As I see it, the overall effect of this bill is to greatly improve our tax system. Let me summarize some of the main provisions of this bill. A careful reading of the legislation will show that it represents a considerable step forward in tax reform.

For example, the present bill provides for reporting of income from interest and dividends, which is a substitute for withholding on such income. Reporting, to be sure, may not have the effectiveness of withholding, and this is a fair criticism. It may merely prove that in order to stop the flagrant tax evasion in this area that is now passing the billion-dollar-a-year mark, and rising every year, withholding should be adopted in the future. The reporting route deserves a fair trial, and there is no question but that it will stop a significant part of this tax evasion. But in view of the strong objections raised to withholding—both by payers of dividends and interest and by recipients who were falsely led to believe that withholding would endanger their current living standards, the reporting requirement is the most which could be enacted at this time. It is a step which may prove efficacious. It will, at the minimum, end any excuse for inadvertent nonreporting of dividend and interest income. It should also end some of the temptation for deliberate nonreporting.

The provisions for taxation of cooperatives, mutual thrift, and mutual fire and casualty companies also do not go as far as some would have liked, but also represent forward steps. They meet problems that have defied solution in the tax field for years. By imposing taxes on these institutions more nearly in accord with those imposed on their business competitors, they contribute to increased fairness in our tax system.

The provisions on travel and entertainment expenses are not as stringent as those sought by the administration, but they will prevent the disgraceful abuses now rampant in this area of tax deductions. Its defeat would make a mockery of President Kennedy's call for the death of that slogan of expense account society, that cry of all free spenders of other peoples' money, that banner of waste, luxury, and cynical disregard of tax equity—the slogan “it is deductible.”

Perhaps most importantly, the broad objective of improving the fairness of our tax structure is served by the 12 separate sections in the bill designed to deal with a whole galaxy of inequities

stemming from the present preferred tax treatment given to various types of income from foreign sources. The area of taxation of foreign income presented perhaps the most difficult set of problems which the Finance Committee confronted in its months of study of H.R. 10650. Not only are there technical problems of almost unimaginable proportions but, in addition, each proposed move in the area of taxation of foreign source income presents the danger that elimination of abuses may, simultaneously, work hardships on—or, at minimum, disadvantage legitimate business undertakings by Americans and American businesses overseas.

We cannot continue to condone tax avoidance on the part of Americans who shift their residence abroad for the purpose of escaping U.S. tax on their overseas earnings. We cannot continue to condone the creation of foreign trusts for the purpose of accumulation of untaxed income. We cannot continue to condone the use of foreign investment companies as a device to build capital free of U.S. tax. We cannot continue to condone the shifting of short-term capital abroad for the purpose of avoiding U.S. tax on a portion of the resulting interest income. We cannot continue to condone investment in foreign real estate by American citizens for the purpose of escaping inheritance taxes. We cannot continue to condone the creation and subsequent liquidation of foreign subsidiaries for the purpose of escaping ordinary income taxes and qualifying for taxation only at the advantageous capital gains rate. And finally, we cannot condone the proliferating use of "tax haven" subsidiaries overseas which exist purely for the purpose of escaping American taxes.

All of these abuses are effectively blocked or limited by the foreign income sections of H.R. 10650.

But at the same time, we have clearly recognized the need for—and desirability of—economically sound American business operations in other nations. Only real tax abuses must be stopped. These are all which will be stopped under the legislation now before us.

There are a number of specific provisions of the bill which are designed to assure that only recognizable tax abuses will be affected. Only companies earning a substantial portion of their income from tax haven operations—at least 30 percent—will be covered. Companies which pay relatively high local taxes in the country of incorporation or which make relatively large repatriations of foreign income—or some relatively large combination of both—will be exempted from coverage by this section of the bill. U.S.-controlled subsidiaries which are engaged largely in the sale of American-made products and which reinvest most of their income in the export sales aspect of their business will be exempted.

What will be curbed is tax haven abuses—overseas operations of American-controlled subsidiaries which have no demonstrable reason for existence other than tax avoidance. These purely tax haven operations are injuring the American economy.

They induce an outflow of investment funds from this country, which works a twofold injury upon us: it adds to our balance-of-payments deficit and it drains away money which might be put to productive use here building American industry and creating American jobs. Continued tax avoidance possibilities of tax haven operations also serve effectively to block the return flow of funds to this country, where their investment in American enterprises would benefit us all.

As this country enters a period of freer trade, it is imperative that we increase investment at home and expand our sales of goods abroad. The foreign income sections of H.R. 10650 are designed to assist in the attainment of this twin objective. As such, they reinforce and complement the objectives of the Trade Expansion Act and, as such, they are also closely linked with, and complementary to, the most important single section of the pending tax bill—the investment credit.

Without question, the two most serious economic problems we face today are our lagging rate of economic growth and the chronic deficit in our international balance of payments. While I could not claim that the investment credit promises instant or complete solution of either problem, its potential as a tool for solving both is too great for us to squander.

Our rate of economic growth must be accelerated if we are to meet successfully what President Kennedy has called "the major domestic challenge of the sixties"—insuring gainful employment for the millions of young workers who will be entering our labor force and for the millions of older workers who find their skills made obsolete by rapidly changing technology.

Without more rapid growth it will also be impossible for us, as a nation, to improve the lot of the disadvantaged members of our society—those who subsist on limited diets, occupy substandard housing, and send their children to inadequate schools—all those who live in economic or social distress.

But our economic health has importance far beyond our domestic needs. A billion people in the uncommitted world are being told that this Nation is weak and incapable of vital and continued development, and that a system of total state control is the only salvation for the underdeveloped. The Soviet Union's rapid expansion is extolled, and the United States is pictured as a dangerous model for economic development—weakened by recessions, plagued by chronic unemployment, and unable to extend a decent standard of living to all its people.

Our ability to maintain adequate defenses for ourselves and our allies, and to contribute to the development of a free world, also depends on our economic strength. We cannot meet domestic and international needs with a faltering economy.

Likewise, our strength and prosperity at home and our security in the world depend significantly upon reducing the deficit in our international balance of

payments and dispelling all doubts concerning the stability of the dollar.

Recurring drains on our stock of gold, which undermine confidence in the dollar, cannot be stopped unless our international payments are brought into equilibrium.

The dollar is the major reserve currency of the free world. Upon confidence in its stability depends the stability of other major currencies, our economic relations with all other nations, the viability of the international payments system and the economic health and national security of every friendly and uncommitted nation.

The investment credit plan contained in the legislation before us will prove an effective measure for increasing our rate of economic growth and reducing the deficit in our international payments.

By providing business with a direct incentive to investment in productive equipment, it will stimulate growth directly as increased orders for machinery and equipment create additional jobs and larger payrolls. But the major thrust of the credit will be longer term.

The credit will encourage the modernization of our factories and farms, the development of new technology and its rapid incorporation in the production process. The resulting gain in productive efficiency will bring important direct benefits.

It will insure our ability to keep American wages the highest in the world. The superior health, education and skill of our workers do not, by themselves, guarantee maintenance of their productivity margin over workers elsewhere—the margin which justifies our wage standards. To these endowments of our work force must be added use of the most modern and efficient equipment available anywhere in the world.

Increased productive efficiency will also enable us to assure that even when our goal of full employment is reached, our workers may enjoy an ever-improving standard of living without the threat of inflation. Renewal of inflation at some future date would force us to adopt restrictive budgetary policies which would starve needed welfare and resource development programs. It would also force us to turn, once again, to a policy of monetary restraint—thus dampening our economic growth and placing at a disadvantage those who must compete in the money markets to finance the construction of homes, schools and other public facilities.

Possibly most important of all, however, increased productive efficiency will enable us to sell American goods at competitive prices everywhere in the world. This will mean expanded export markets which, in turn, will mean more jobs for American workers and a more vigorous, more rapidly growing American economy.

Increased export sales also offer the only complete solution to our balance-of-payments problem—short of the unthinkable alternative of withdrawal from our world commitments.

Many steps to reduce our international payments deficit have been undertaken.

But the long-term answer lies in increasing our surplus of exports over imports.

The proposed Trade Expansion Act, on which this Senate will soon be voting, will, by lowering tariff barriers, encourage increased imports as well as exports. Thus, in the new world of freer trade, our producers must be able to maintain competitive prices in order to outsell foreign producers in our own home markets as well as to expand export sales. Improved productive efficiency is therefore essential to improvement of our trade balance on both sides of the export-import ledger.

There are those who have suggested that the investment credit is by no means the best method of increasing our economic growth—who charge that it is no more than a giveaway of tax revenue to American business.

They propose adding to Government expenditures as a means of increasing total demand, and thereby growth. Or they suggest reducing taxes for individuals, as a means of increasing demand and growth.

But increased Government expenditures—for education, public construction, health services, resource development or any of a host of entirely worthwhile programs—do very little in the short run to increase the productive efficiency and competitiveness of our industry. And it is in the short run—right now—that we need to increase our competitiveness and our export sales. Those who are still nervously watching our balance-of-payments figures will not hold off speculating against the dollar while essential but long-range Government programs add to our national resources. The payoff from increased investment in productive equipment is, on the other hand, fast.

Stimulating investment by building up from an enlarged base of demand also takes time we do not have. In addition, if we were to rely solely on tax reductions to increase demand to the point where it would put pressure on existing industrial capacity—and thus force investment in expanded facilities—a revenue loss far greater than the \$1 billion cost of the credit would be required.

We have, at present, excess capacity—another point made by some opponents of the credit. But steps are being taken outside the tax area—President Kennedy's proposed public works and unemployment insurance programs are such steps—to assure maintenance of strong and growing demand which will use our industrial capacity to the full. Although the investment credit will itself create additional demand, that is not its primary purpose.

The investment credit, will, however—coupled with the foreign income tax proposals in the pending bill—help solve a significant national problem as no proposed alternative would. This is the growing movement of investment capital from this country overseas.

Part of this outflow is solely for the purpose of avoiding taxes. The foreign income provisions of H.R. 10650 are aimed at reducing such tax-induced movements abroad.

But much of the outflow results from the more liberal tax treatment of investment in other industrialized countries. Quicker recovery of the cost of investment is now possible under more liberal tax laws in effect elsewhere. But enactment of the investment credit—which will apply, of course, only to investment in the United States—will close this cost recovery gap. It will thus help to block the movement overseas of both capital and jobs. No program for increasing demand in this country—by whatever means—will do this so directly.

Increasing the level of investment in productive equipment does increase national economic growth. To those who doubt this, I suggest a careful look at our recent economic performance, compared with that of other nations. A striking pattern emerges: The higher the level of investment, the greater the economic growth. The statistical picture is not without small deviations, but nearly so.

During the 10-year period, 1951 through 1960, investment in the United States averaged 5.7 percent of gross national product. After us, in ascending order, came Canada, with 8.0 percent; France, 8.4 percent; Italy, 9.1 percent; and West Germany, 11.5 percent. Growth rates for those countries followed exactly the same order: 3.3 percent for the United States; 3.9 percent for Canada; 4.3 percent for France; 5.9 percent for Italy, and 7.5 percent for West Germany. Available figures for Japan suggest that for the last half of the decade, she had the highest investment rate of all—and the highest growth as well. Among the major industrial nations, only the United Kingdom and Belgium had a higher level of investment than ours without a higher level of growth.

The effect of investment levels on export prices—and export markets—is suggested by the fact that from 1953 to 1960, our export prices for manufactured goods rose 14 percent while those of our foreign competitors remained the same or dropped. Moreover, the success of our competitors in stabilizing export prices came not from a slower rate of wage increases but a faster rise in productivity.

The potential gain to our American economy from the investment credit far outweighs the one item of risk. The risk—which is real—is the creation of additional technological unemployment as new and more modern equipment is put into place.

But if we attempt to stand still, we will create more unemployment in the long run.

For those of our businesses in which technological change is lagging, we will merely postpone the day of reckoning—and perhaps not even postpone it very long. We will insure only that their readjustment, when it comes, will be more protracted and more difficult—if, indeed, they survive at all. For inefficient companies do go out of business, thus lowering the ax of unemployment with one blow on all their workers and causing acute hardship for entire communities. The task of retraining or relocat-

ing workers then becomes almost unmanageable.

For the Nation as a whole, our failure to approve the investment credit would involve even greater risks. For unless we modernize our equipment, expand our productive base and assure maintenance of our economic vitality, there can be no assurance of security for our Nation and no lasting prosperity for our people.

The investment credit is the heart of the bill, but the other provisions, taken as a whole, are at least of equal importance. The overall effect of the bill will be positive, because the most of the provisions of every important change represent gains in tax fairness and increased economic efficiency.

This bill will go far toward eliminating many inequities, many abuses, many tax problems that have existed for years. In addition, it will provide significant help for our domestic economy and for our balance of payments.

It deserves the wholehearted support of Senators.

Finally, Mr. President, tax measures are never to be found in the category of what we call easy and pleasant legislation. We are dealing with the economic fabric of our society when we pass tax laws, and we are obviously affecting the economic life of individuals and business institutions. Tax measures are very controversial.

The purpose of the tax measure now being considered is to close some of the loopholes in the existing tax laws, and to provide additional incentive for investment and development in American industry. Those two purposes are, in part at least, being fulfilled by the measure before us and now about to be voted upon.

As I have said before, the failure to include a provision for the withholding of taxes on dividends and interest is a serious weakness in the bill; but it is my hope that the methods which have been proposed and are now under way administratively to improve the collection of taxes on interest and dividends will be beneficial. If not, we can return to a consideration of this proposal, and we shall.

I must say, further, that we have gone a long way toward meeting the requests of the President. Let that be clear. The bill does have administration support as it stands.

The Senator from Oklahoma [Mr. KERR], who has handled this highly complex and controversial legislation deserves our commendations for his detailed knowledge and exploration of its many provisions.

Senators on the other side of the aisle have given their cooperation in bringing this measure to a vote. We thank them.

Finally, it is my hope that when the bill comes back from conference, some improvements will have been made as a result of the deliberations between the conferees of the two Houses.

Next year Congress will have an opportunity to consider general tax legislation, and it will be then that Congress can work its will on overall tax policy.

The senior Senator from Minnesota believes that there is a necessity for a general overhauling of the tax laws, particularly to provide greater incentive for expansion and development and also to increase consumer purchasing power.

Mr. WILLIAMS of Delaware. Mr. President, I yield 2 minutes to the Senator from Kansas [Mr. CARLSON].

The PRESIDING OFFICER (Mr. BURDICK in the chair). The Senator from Kansas is recognized for 2 minutes.

Mr. CARLSON. Mr. President, if I may have the attention of the Senator from Oklahoma, I wish to say that on page 17363 of the CONGRESSIONAL RECORD for September 4, there appears a colloquy, in which he and I engaged, in regard to advertising. In that connection, I refer to the lower part of the first column on that page. I ask unanimous consent that the word "permitted" be changed to "denied," so as to make this part of the colloquy read:

Fourth, would a roadbuilding machinery company be denied deductions on a general plea for improved highways?

Then I come to the last sentence of the last paragraph in that column; and I ask that it be changed so as to read:

Is it not the intent of this legislation to prohibit advertising that deals with a legislative proposal arising under local, State, or National law when the advertising is in general directed toward pending or proposed legislation?

I ask the Senator from Oklahoma whether he has any objection to having those corrections or changes made.

Mr. KERR. I have no objection. I join in the request.

Mr. CARLSON. I thank the Senator from Oklahoma.

The PRESIDING OFFICER. The corrections will be made.

Mr. MANSFIELD. Mr. President, I suggest the absence of a quorum, and ask unanimous consent that the time required for it be taken equally out of the time available to both sides.

The PRESIDING OFFICER. Without objection, it is so ordered; and the clerk will call the roll.

The legislative clerk proceeded to call the roll.

Mr. MANSFIELD. Mr. President, I ask unanimous consent that the order for the quorum call be rescinded.

The PRESIDING OFFICER. Without objection, it is so ordered.

Mr. WILLIAMS of Delaware. Mr. President, I yield 2 minutes to the Senator from Iowa [Mr. HICKENLOOPER].

The PRESIDING OFFICER. Only 1½ minutes remain for each side.

Mr. HICKENLOOPER. Mr. President, I shall need only one-half a minute.

Mr. WILLIAMS of Delaware. Very well; I yield.

Mr. HICKENLOOPER. Mr. President, on behalf of my colleague, Senator MILLER, and myself, I send to the desk an explanation of the reasons why we will vote against the omnibus tax bill; and I ask unanimous consent that the explanation be printed at this point in the RECORD.

There being no objection, the statement was ordered to be printed in the RECORD, as follows:

STATEMENT BY SENATOR HICKENLOOPER AND SENATOR MILLER IN EXPLANATION OF THEIR VOTE ON HOUSE BILL 10650

We oppose the omnibus tax bill because its bad features far outweigh its good features.

It has some desirable features, such as tightening up deductions for business extravagance, business gifts, entertainment and travel expenses; investment returns on interest and dividends and the closing of some loopholes in the foreign income field.

On the other hand some of its undesirable features include the investment tax credit provision which would reduce Federal income by over a billion dollars and is highly discriminatory, benefiting primarily a limited number of large taxpayers; the almost unworkable provisions applicable to foreign business operations which would tend to frustrate the expansion of foreign trade and actually put foreign competitors in a more favorable position; and the deductions allowed for increased clearing of land which would only be of prime benefit to large landowners and bring more land into competitive production in an already surplus market.

To reduce Federal income at this time without at the same time reducing Federal expenditures is unwise. Especially is this so in the face of the greatest international tensions which this country has faced for many years. To keep on spending more than we take in will inevitably lead to further devaluation of the American dollar and to a further reduction of the purchasing power of our money.

We believe that tax reduction is essential, but it must be accompanied by sound and sensible reduction of Federal expenditures. Moreover, tax reduction should be of general application rather than advantageous to a comparative few.

The net reduction of Federal income under this bill would be over three-quarters of a billion dollars and we cannot afford this reduction at this time of great international tensions and in the face of increased spending demands of the administration.

Mr. WILLIAMS of Delaware. Mr. President, I yield the remaining time under my control to the junior Senator from Iowa [Mr. MILLER].

Mr. MILLER. Mr. President, following the passage of the tax bill by the House, an excellent article by the Honorable JOHN W. BYRNES, U.S. Representative from Wisconsin, was printed in the April issue of the Tax Review. The article is entitled "The Revenue Act of 1962: A Dissent." While I recognize that a number of problems which arose in connection with the House version of the bill have been avoided by the action of the Senate, nevertheless I think the article by Mr. BYRNES merits the attention of the people, and many of the statements in the article are entirely responsive to the situation presented by the bill as it is now before the Senate. Therefore, I ask unanimous consent that the article be printed in the RECORD.

There being no objection, the article was ordered to be printed in the RECORD, as follows:

THE REVENUE ACT OF 1962: A DISSSENT

(By Hon. JOHN W. BYRNES, U.S. Representative from Wisconsin)

If one is old-fashioned enough to believe that one of the ingredients of sound fiscal policy in a time of prosperity is a balanced budget, the need for generous doses of tranquilizer pills is apparent when a close look is taken at present Federal fiscal and tax policies. There has been submitted, it

is true, a balanced budget for fiscal 1963, but it is balanced only on paper, and the paper balance is achieved only through a process of wishful thinking.

Such wishful thinking for fiscal 1963 is a continuation of a trend already established. Since the original, seven new estimates have been made of the deficit for 1962, as follows: \$2.1 billion in March 1961, \$2.8 billion in March 1961, \$3.6 billion in May 1961, \$3.7 billion in June 1961, \$5.3 billion in October 1961, and \$7 billion in January 1962. The latest estimate now appears to be off by at least \$1 billion and the deficit will probably be around \$8 billion.

On paper the Federal budget for fiscal 1963 calls for expenditures of \$92.5 billion to be covered by \$93 billion of receipts. This precarious balance of less than one-half of 1 percent is to be achieved through an increase of about \$11 billion in receipts from corporate and individual income taxes attributable to a continuing high level of economic activity.

The realization of the necessary income in order to achieve this balance is predicated on some very highly speculative assumptions. It assumes that the recovery will continue on a steady rise for the next 16 months. Remember always that the projection and guesses go to July 1963. This steady rise is to carry the gross national product through this year to a record \$570 billion. Yet, we have already seen some slippage in January and February.

What about expenditures? While a balanced budget is of extreme importance, it is important to look at the level of Federal expenditures and particularly the change in that level from year to year.

Expenditures proposed for fiscal 1963 exceed those of 1962 by almost \$3.5 billion, and this follows an increase in Federal spending between 1961 and 1962 of about \$7.5 billion. In this 2-year span, we have raised Federal expenditures by more than \$11 billion.

This is clearly not a trend that is consistent with improvement of our international or domestic economic position. This kind of a trend cannot be supported by economic growth. It can only be supported by increased taxes.

If you think this is bad, look at some of the assumptions upon which the \$92.5 billion level of expenditures is based.

It assumes that the farm program proposed by the administration will reduce the cost of the Department of Agriculture by more than \$500 million, while still expanding the food stamp plan, lowering prices to the consumer and raising farm income—a real neat trick.

It assumes an end to the postal deficit. Yet, the postal rate increase bill which passed the House and is pending in the Senate is several hundred millions short of reaching a balance and the Congress is presently being asked for a 14-percent increase in postal workers' salaries which would add some more hundreds of million dollars to the postal deficit.

The expenditures are also based on the assumption of a resolution of the Berlin problem by June. For example, no funds were provided in the budget to carry the reservists and National Guard units called up last fall beyond June 30, and the administration is now requesting additional funds.

The interest on the debt is underestimated. If we have a deficit budget and the economic activity the Treasury is forecasting, then it is only reasonable to expect interest rates to rise.

We could go on and on enumerating the precarious assumptions on which the balanced budget is predicated. Suffice it to say, the budget has as many "ifs" as it has dollars—all of which must be favorably resolved if it is to be balanced on June 30, 1963.

It is alarming to note that the reliable and respected staff of the Joint Committee on Internal Revenue Taxation estimated on April 2 that present taxes would bring in \$4.3 billion less revenue in fiscal 1963 than the budget predicts and, on this basis alone, a deficit of \$3.8 billion is now indicated.

Knowing the propensities of Congress in an election year and the philosophy of the administration toward spending, I have no hesitation in predicting that we can well wind up with a deficit of from \$5 to \$7 billion next year.

Even if the budget, as presented, would produce a balance, there is a basic philosophy expressed in the administration's program that should cause grave concern. It is the philosophy that all increases in revenue resulting from improvement in the economy and from economic growth are to be preempted—yes, dedicated even in advance of realization—by Government for enlarged Government spending.

It is on Government spending that we are to place our reliance for curing every ill and for strengthening our economy. To advance economic growth, we are to place primary reliance upon the rocket power of climbing Federal spending. Every dollar of increased revenue is to be preempted for Government spending and not one cent is to be put to work to provide greater impetus to the private sector of our economy.

We did not achieve our position of world leadership by this route. This philosophy, if pursued, means we are to reduce our reliance on our private enterprise system and increase our reliance on Government in complete disregard of the fact that it is individual effort and enterprise that is the source of all present and future Government income. If there was ever a dangerous and reactionary road, this is it.

In report after report, including his economic and trade messages, the President has emphasized the need for growth, the strengthening of incentives for individual effort and for productive investment, the need to put our economy on a basis which will permit us to be competitive with the other industrial nations of the world—particularly with the rising Common Market area of Western Europe. Yet the growth-stunting potential of our tax system is completely ignored. The President's only mention of tax reduction is as a temporary expedient to fight recession—a preposterous proposal that Congress should surrender its taxing power, no matter how limited, to the Executive.

We have been told often in the past—like a broken record—"We know the rates are too high, we know it's unfair to apply this rule of taxation or that. We know tax relief is needed—but the Government needs the money."

Last December the President, in talking about the need for changes in tax depreciation allowances, said, "We are not unsympathetic, and I can think of very few changes that would be more useful to the country in stimulating employment and keeping us competitive, particularly with Western Europe. And the only reason we have limited ourselves to the proposal which is now before the House Ways and Means Committee is because we do not have the available revenue to provide for a tax reduction this year."

The philosophy of the budget and other messages, if pursued, will mean that we will never "have the available revenue to provide for a tax reduction," because any potential revenue that might be available for such a purpose is being preempted for additional Government spending. Keep in mind that the President, in his budget message proposing \$93.5 billion in spending, said, "Many desirable new projects and activities are being deferred."

Thus, the administration has talked about "tax reform" only in terms of taxing some people more while taxing others less. What the administration is really talking about is tax juggling, not tax reform. It strives to leave the impression that it can work miracles by closing loopholes in our tax laws.

The term "loophole," correctly used, defines a method used to avoid taxes which was not intended by Congress. Because we have a lot of ingenious tax experts in our land, unintended avenues for avoiding taxes are opened up from time to time. They, of course, should be closed. There are also inequities and these should be corrected. We have corrected some in the current tax bill.

The point, however, is that provisions of law that Congress enacted intentionally or are in the code historically in order to create equity are not loopholes. Yet it is these that seem to be the favorites of the demagogues, even though each has its history and reason for existence.

Many of these so-called loopholes exist to overcome the burdening disincentive caused by our extremely high tax rates. Eliminate the high rates and you eliminate the "loopholes."

The Treasury has announced it will unfurl new "tax reform" proposals early this summer. If the philosophy behind them is in keeping with the administration's tax bill which has passed the House, I must say that I can only view our fiscal and economic future with alarm.

While some of its 23 sections are good, desirable, laudable—and this can probably be attributed to the law of averages—overall, the bill violates the very basic concepts of sound tax policy and fiscal responsibility.

Regardless of how much figure juggling is done, the bill involves a revenue loss of \$1 billion in fiscal 1963. In one swoop, there goes the balanced budget which the budget message itself says is so important under present conditions. If this revenue loss would produce sound, growth-inducing tax reform, the House might have been justified in accepting the risks involved in a deficit budget.

The bill does not justify such risks.

Consider its two major provisions—the so-called investment credit and the tax on controlled foreign corporations.

Talk about closing loopholes. The investment credit is the biggest loophole and unwarranted subsidy ever seriously considered by the Congress. It is an outright subsidy of almost \$2 billion to a segment of the business community which business neither seeks nor wants.

It isn't often that we find the AFL-CIO, the NAM and the chamber of commerce all in bed together—but they all agree that this provision is unsound.

It can be supported by business only on the very selfish ground that they will be able to get their hands in the till and divide up \$2 billion.

It is perfectly clear that the Treasury never intended this to be a permanent part of the code, but when the public wakes up to the absolute windfall that will be enjoyed by some, plus the inequities and discrimination it will visit upon others, the temporary nature of the provision will be assured.

This credit has nothing to do with depreciation reform. It amounts, in essence, to payment by the Government of a part of the cost of buying certain depreciable property, but the taxpayer is not even required to adjust the basis of the asset by the amount of the credit, and this is the least that should be done.

It is supposed to be an incentive, but it applies to assets already placed in service just as long as it was subsequent to December 31 of last year.

What is needed is true depreciation re-

form. I have proposed that a provision for accelerated depreciation be substituted for the credit. It would permit an additional depreciation of 20 percent of the depreciation otherwise allowable.

This is not intended as the ultimate answer to the need for depreciation reform, but, coupled with the Treasury's consolidation and reduction of the useful lives prescribed in Bulletin F to be announced soon, it will at least be a move in the right direction.

The provision for applying withholding to dividends and interest is an administrative monstrosity, but the proposal to tax the undistributed earnings of controlled foreign corporations is not only that but highly dangerous as well.

Everyone talks about the need to simplify the code. If you want to see a tax nightmare, take a good look at section 13 of the tax bill, then get in a good supply of aspirin.

Section 13 contains an attack on American-owned business in foreign countries unprecedented in its harshness, its complexity, and its irrationality.

At this decisive time, when the smallness of the world has just been dramatically and heroically demonstrated, and when we have every reason to be thankful to American-owned business overseas for contributing to our balance of trade by providing a market for American-made products and contributing to our balance of payments by returning dividends and interest to this country, the bill unleashes an unprovoked attack on methods of doing business.

Entirely aside from its drastic substantive effects, this provision would discourage Americans from attempting to compete abroad merely because of its inordinate complexity.

One example: Section 13 is not content with taxing royalties actually received as such by foreign corporations. It proposes to impute royalties to a foreign corporation. Royalty income would be imputed to foreign corporations which have income from sales of manufactured items where it can be argued that part of the sales income is attributable to the use of patents, formulas, copyrights, or processes developed in the United States.

It means, for example, that any American-owned foreign corporation selling products abroad will be forced to allocate some portion of its sales proceeds to the patent or process and this will be taxed to the U.S. shareholder as royalty income.

The Treasury has complained about the difficulty of administering section 482 and the man-hours of revenue agents' time required to allocate income properly. By comparison to the problems that will arise from trying to impute royalty income, the administration of section 482 is a revenue agent's dream.

In my 16 years on the Ways and Means Committee, I have come to recognize the lust of the Treasury for complexities and their insatiable appetite for authority to make rules and regulations. I cannot, for the life of me, however, understand the philosophy behind section 13, and I cannot believe that the Senate, when it studies its far-ranging implications, will not reverse the mistake made by the House in adopting it.

Our immediate needs, if we are to develop sound tax policy, are apparent:

The current tax bill should provide for a constructive step toward depreciation reform instead of a discriminatory subsidy which will neither provide incentive toward the kind of investment we need nor provide a basis upon which such investment can be planned. It should take care of genuine foreign tax havens instead of penalizing and making impossible the efforts of American

business to compete in a world which is growing more competitive every minute.

Future tax bills should be aimed at true tax reform and not at tax law juggling. The attack must be upon the excessively high rates and the practical confiscations of profits and capital resulting from the present law if we are to evolve a truly growth-producing tax structure.

The basic need is an attitude toward Government spending which will not only strengthen our domestic and world economic and monetary position but will provide the leeway we desperately need for the kind of meaningful tax reform which we must have if we are successfully to compete in the new world in which we live. We need to discipline ourselves to the urgencies of the hour, for the race which looms ahead will go to the lean and self-reliant and not to the fat and well coddled.

Mr. MILLER. Mr. President, on Saturday, March 31, there appeared in the New York Daily Mirror an excellent editorial attacking the proposed withholding of tax on interest and dividends. Although such a provision is not in the bill, so many statements in favor of that proposal have been made that I believe it well to have the editorial brought to the attention of the readers of the CONGRESSIONAL RECORD. Therefore, I ask unanimous consent that the editorial be printed in the RECORD.

There being no objection, the editorial was ordered to be printed in the RECORD, as follows:

FIASCO OF A TAX BILL

Knuckling under to the administration's pressure and prodding, the House has passed the tax revision bill which President Kennedy labeled a "must." We can only hope that the Senate will exhibit stronger resolve and better judgment than did the House and will take a long, realistic look at the absurdities, inequities and failings of the legislation.

Apart from the enormous bureaucratic mushrooming and staggering expense that will be required to administer the bill if it ever becomes law, the package can be criticized on many scores. Today, we intend to confine our remarks to the proposal to withhold 20 percent of interest paid on savings accounts.

Presumably, by imposing a withholding tax on dividend and interest money, the bill will produce an extra \$650 million in revenue. Nobody argues that tax delinquents and deadbeats should not be forced to pay their share. But has Congress fully considered the administrative cost, the consequences and the unfairness of collecting this "extra revenue" by this method?

The way it will work with savings accounts is that a flat 20 percent will be withheld on interest credited to the depositor. This 20 percent will be lopped off his account whether or not he actually owes the money in taxes.

In other words, Uncle Sam will automatically get his fat cut of every saver's earned interest even where the Government isn't entitled to it.

Now, what happens when the saver wants that cut returned to him because his tax liability will not be high enough to warrant the application of this 20 percent levy on interest? Well, the saver merely has to make application for a refund and then cool his heels while his claim goes through the usual bureaucratic processing—and millions of taxpayers can testify from experience how long and agonizing is the wait for a refund.

THE ABSURDITIES NEVER END

Moreover, the saver has to make application for this refund every single time the

bank credits his account with earned interest. Thus, if interest is credited quarterly, the depositor, deprived of 20 percent of the money, must petition the Government to give it back to him four times a year.

Regular saving and the compounding of interest has been a cornerstone of this country's economy. Traditionally, by leaving his money in the bank, a depositor earns interest on every penny of his interest.

But now, only 80 percent of his earned interest can begin earning new interest immediately. The remaining 20 percent will have been handed over to the Government in anticipation of a tax bill which the depositor may never have to pay. When this 20 percent is refunded, it will have been deprived of its earning capacity for whatever length of time the Government held on to it.

The absurdities don't end there, either. The Government gets its 20 percent rakeoff even if the saver is a child, a nonworking dependent, or an elderly widow.

If such persons wish to be exempted from the withholding tax, they must file a certificate with the institution where their money is on deposit. This might be all right for people who are aware of this provision in the law and understand its import. But how about all the others, and we can presume there will be great numbers of them, who do not know that such a certificate must be filed or neglect to do so for one reason or another?

Going one step further, who knows how many tens of thousands of persons will never file their refund claims for tax deductions on earned interest because they do not understand the machinations of this complicated legislation?

The bookkeeping, correspondence, and recordkeeping that this new withholding system will involve is fearsome to contemplate.

There must surely be a better way to catch up with the taxpayers who fail to report their interest and dividend earnings.

The PRESIDING OFFICER. One minute remains.

Mr. MANSFIELD. Mr. President, I yield back 1 minute.

Mr. President, a parliamentary inquiry.

The PRESIDING OFFICER. The Senator from Montana will state it.

Mr. MANSFIELD. Is the vote to be taken at the conclusion of the debate or at 1:15, the time agreed to?

The PRESIDING OFFICER. The vote is to come immediately following conclusion of the debate.

Mr. MANSFIELD. Mr. President, on the question of whether the bill shall pass, have the yeas and nays been ordered?

The PRESIDING OFFICER. No.

Mr. MANSFIELD. Mr. President, on this question I request the yeas and nays.

The PRESIDING OFFICER. Is there a sufficient second?

The yeas and nays were ordered.

The PRESIDING OFFICER. The question is, Shall the bill pass?

The yeas and nays have been ordered; and the clerk will call the roll.

The legislative clerk called the roll.

Mr. MANSFIELD (after having voted in the affirmative). Mr. President, on this vote I have a pair with the Senator from Tennessee [Mr. GORE]. If he were present and voting, he would vote "nay." If I were at liberty to vote, I would vote "yea." Therefore, I withhold my vote.

Mr. KEFAUVER. Mr. President, on this vote I have a pair with the Senator from Missouri [Mr. SYMINGTON]. If he were present and voting, he would vote "yea." If I were at liberty to vote, I would vote "nay." Therefore, I withhold my vote.

The vote was recapitulated.

Mr. HUMPHREY. I announce that the Senator from Mississippi [Mr. EASTLAND], the Senator from Washington [Mr. MAGNUSON], the Senator from Oregon [Mrs. NEUBERGER], and the Senator from Tennessee [Mr. GORE] are absent on official business.

I further announce that the Senator from New Mexico [Mr. ANDERSON], the Senator from Nevada [Mr. BIBLE], the Senator from Wyoming [Mr. HICKEY], and the Senator from Missouri [Mr. SYMINGTON] are necessarily absent.

I further announce that, if present and voting, the Senator from New Mexico [Mr. ANDERSON], the Senator from Nevada [Mr. BIBLE], the Senator from Mississippi [Mr. EASTLAND] and the Senator from Washington [Mr. MAGNUSON] would each vote "yea."

On this vote, the Senator from Wyoming [Mr. HICKEY], is paired with the Senator from Oregon [Mrs. NEUBERGER]. If present and voting, the Senator from Wyoming would vote "yea," and the Senator from Oregon would vote "nay."

Mr. KUCHEL. I announce that the Senator from Utah [Mr. BENNETT], the Senator from South Dakota [Mr. BOTTUM], the Senator from Arizona [Mr. GOLDWATER], the Senator from Kentucky [Mr. MORTON], and the Senator from New Hampshire [Mr. MURPHY] are necessarily absent.

The Senators from Vermont [Mr. AIKEN and Mr. PROUTY] are absent on official business.

If present and voting, the Senator from Vermont [Mr. AIKEN], the Senator from Utah [Mr. BENNETT], the Senator from South Dakota [Mr. BOTTUM], and the Senator from New Hampshire [Mr. MURPHY] would each vote "yea."

On this vote, the Senator from Kentucky [Mr. MORTON] is paired with the Senator from Arizona [Mr. GOLDWATER]. If present and voting, the Senator from Kentucky would vote "yea," and the Senator from Arizona would vote "nay."

The result was announced—yeas 59, nays 24, as follows:

[No. 247 Leg.]

YEAS—59

Allott	Fulbright	Monroney
Beall	Hartke	Moss
Butler	Hayden	Mundt
Byrd, Va.	Hill	Muskie
Byrd, W. Va.	Holland	Pastore
Cannon	Humphrey	Pearson
Capehart	Jackson	Pell
Carlson	Javits	Randolph
Carroll	Johnston	Robertson
Case	Jordan, N.C.	Scott
Chavez	Jordan, Idaho	Smathers
Church	Kerr	Smith, Mass.
Cooper	Kuchel	Smith, Maine
Cotton	Long, Mo.	Sparkman
Dirksen	Long, Hawaii	Talmadge
Dodd	Long, La.	Wiley
Ellender	McCarthy	Williams, N.J.
Engle	McClellan	Young, N. Dak.
Ervin	McGee	Young, Ohio
Fong	Metcalf	

NAYS—24

Bartlett	Hart	Proxmire
Boggs	Hickenlooper	Russell
Burdick	Hruska	Saltanstill
Bush	Keating	Stennis
Clark	Lausche	Thurmond
Curtis	McNamara	Tower
Douglas	Miller	Williams, Del.
Gruening	Morse	Yarborough

NOT VOTING—17

Aiken	Goldwater	Morton
Anderson	Gore	Murphy
Bennett	Hickey	Neuberger
Bible	Kefauver	Prouty
Bottom	Magnuson	Symington
Eastland	Mansfield	

So the bill (H.R. 10650) was passed.

Mr. KERR. Mr. President, I move to reconsider the vote by which the bill was passed.

Mr. MANSFIELD. Mr. President, I move to lay that motion on the table.

The PRESIDING OFFICER. The question is on agreeing to the motion to lay on the table the motion to reconsider.

The motion to lay on the table was agreed to.

Mr. BYRD of Virginia. Mr. President, I move that the Senate insist upon its amendments and request a conference with the House of Representatives thereon; and that the Presiding Officer appoint the conferees on the part of the Senate.

The motion was agreed to; and the Presiding Officer appointed Mr. BYRD of Virginia, Mr. KERR, Mr. LONG of Louisiana, Mr. SMATHERS, Mr. WILLIAMS of Delaware, Mr. CARLSON and Mr. BENNETT conferees on the part of the Senate.

Mr. BYRD of Virginia. Mr. President, I ask unanimous consent that the bill, H.R. 10650, be printed with the amendments of the Senate numbered; and that in the engrossment of the amendments of the Senate to the bill the Secretary of the Senate be authorized to make all necessary technical and clerical changes and corrections, including corrections in sections, subsections, et cetera, designations, table of contents, and cross references thereto.

The PRESIDING OFFICER (Mr. HART in the chair). Is there objection to the request by the Senator from Virginia? The Chair hears none, and it is so ordered.

SELF-EMPLOYED INDIVIDUALS TAX RETIREMENT ACT OF 1961

Mr. MANSFIELD. Mr. President, I move that the Senate proceed to the consideration of Calendar No. 973, H.R. 10.

The PRESIDING OFFICER. The bill will be stated by title for the information of the Senate.

The LEGISLATIVE CLERK. A bill (H.R. 10) to encourage the establishment of voluntary pension plans by self-employed individuals.

The PRESIDING OFFICER. The question is on agreeing to the motion by the Senator from Montana.

The motion was agreed to; and the Senate proceeded to consider the bill (H.R. 10) to encourage the establishment of voluntary pension plans by self-employed individuals, which had been reported from the Committee on Finance,

with amendment, to strike out all after the enacting clause and insert:

That this Act may be cited as the "Self-Employed Individuals Tax Retirement Act of 1961".

SEC. 2. QUALIFICATION OF PLANS.

Section 401 of the Internal Revenue Code of 1954 (relating to qualified pension, profit-sharing, and stock bonus plans) is amended—

(1) by adding at the end of paragraph (5) of subsection (a) the following new sentence: "For purposes of this paragraph and paragraph (10), the total compensation of an individual who is an employee within the meaning of subsection (c)(1) means such individual's earned income (as defined in subsection (c)(2)), and the basic or regular rate of compensation of such an individual shall be determined, under regulations prescribed by the Secretary or his delegate, with respect to that portion of his earned income which bears the same ratio to his earned income as the basic or regular compensation of the employees under the plan bears to the total compensation of such employees.";

(2) by adding at the end of subsection (a) the following new paragraphs:

"(7) A trust shall not constitute a qualified trust under this section unless the plan of which such trust is a part provides that, upon its termination or upon complete discontinuance of contributions under the plan, the rights of all employees to benefits accrued to the date of such termination or discontinuance, to the extent then funded, or the amounts credited to the employees' accounts, are nonforfeitable. This paragraph shall not apply to benefits or contributions which, under provisions of the plan adopted pursuant to regulations prescribed by the Secretary or his delegate to preclude the discrimination prohibited by paragraph (4), may not be used for designated employees in the event of early termination of the plan.

"(8) A trust forming part of a pension plan shall not constitute a qualified trust under this section unless the plan provides that forfeitures must not be applied to increase the benefits any employee would otherwise receive under the plan.

"(9) In the case of a plan which provides contributions or benefits for employees some or all of whom are employees within the meaning of subsection (c)(1), a trust forming part of such plan shall not constitute a qualified trust under this section unless, under the plan, the entire interest of each employee—

"(A) either will be distributed to him not later than his taxable year in which he attains the age of 70½ years, or, in the case of an employee other than an owner-employee (as defined in subsection (c)(3)), in which he retires, whichever is the later, or

"(B) will be distributed, commencing not later than such taxable year, (i) in accordance with regulations prescribed by the Secretary or his delegate, over the life of such employee or over the lives of such employee and his spouse, or (ii) in accordance with such regulations, over a period not extending beyond the life expectancy of such employee or the life expectancy of such employee and his spouse.

"(10) In the case of a plan which provides contributions or benefits for employees some or all of whom are owner-employees (as defined in subsection (c)(3))—

"(A) paragraph (3) and the first and second sentences of paragraph (5) shall not apply, but—

"(1) such plan shall not be considered discriminatory within the meaning of paragraph (4) merely because the contributions or benefits of or on behalf of employees under the plan bear a uniform relationship

to the total compensation, or the basic or regular rate of compensation, of such employees, and

"(ii) such plan shall not be considered discriminatory within the meaning of paragraph (4) solely because under the plan contributions described in subsection (e)(3)(A) which are in excess of the amounts which may be deducted under section 404 (determined without regard to section 404(a)(10)) for the taxable year may be made on behalf of any owner-employee; and

"(B) a trust forming a part of such plan shall constitute a qualified trust under this section only if the requirements in subsection (d) are also met." and

(3) by redesignating subsection (c) as subsection (h) and inserting after subsection (b) the following new subsections:

"(c) DEFINITIONS AND RULES RELATING TO SELF-EMPLOYED INDIVIDUALS AND OWNER-EMPLOYEES.—For purposes of this section—

"(1) EMPLOYEE.—The term 'employee' includes, for any taxable year, an individual who has earned income (as defined in paragraph (2)) for the taxable year. To the extent provided in regulations prescribed by the Secretary or his delegate, such term also includes, for any taxable year—

"(A) an individual who would be an employee within the meaning of the preceding sentence but for the fact that the trade or business carried on by such individual did not have net profits for the taxable year, and

"(B) an individual who has been an employee within the meaning of the preceding sentence for any prior taxable year.

"(2) EARNED INCOME.—

"(A) IN GENERAL.—The term 'earned income' means the net earnings from self-employment (as defined in section 1402(a)) to the extent that such net earnings constitute earned income (as defined in section 911(b) but determined with the application of subparagraph (B)), but such net earnings shall be determined—

"(i) without regard to paragraphs (4) and (5) of section 1402(c),

"(ii) in the case of any individual who is treated as an employee under sections 3121(d)(3)(A), (C), or (D), without regard to paragraph (2) of section 1402(c), and

"(iii) without regard to items which are not included in gross income for purposes of this chapter, and the deductions properly allocable to or chargeable against such items.

For purposes of subparagraph (A), sections 911(b) and 1402, as in effect for a taxable year ending on December 31, 1961, and subparagraph (B), as in effect for a taxable year beginning on January 1, 1962, shall be treated as having been in effect for all taxable years ending before such date.

"(B) EARNED INCOME WHEN BOTH PERSONAL SERVICES AND CAPITAL ARE MATERIAL INCOME-PRODUCING FACTORS.—In applying section 911(b) for purposes of subparagraph (A), in the case of an individual who is an employee within the meaning of paragraph (1) and who is engaged in a trade or business in which both personal services and capital are material income-producing factors and with respect to which the individual actually renders personal services on a full-time, or substantially full-time, basis, so much of his share of the net profits of such trade or business as does not exceed \$2,500 shall be considered as earned income. In the case of any such individual who is engaged in more than one trade or business with respect to which he actually renders substantial personal services, if with respect to all such trades or businesses he actually renders personal services on a full-time, or substantially full-time, basis, there shall be considered as earned income with respect to the trades or businesses in which both personal services and capital are material income-producing factors—

"(i) so much of his share of the net profits of such trades or businesses as does not exceed \$2,500, reduced by

"(ii) his share of the net profits of any trade or business in which only personal services is a material income-producing factor.

The preceding sentences shall not be construed to reduce the share of net profits of any trade or business which under the second sentence of section 911(b) would be considered as earned income of any such individual.

"(3) OWNER-EMPLOYEE.—The term 'owner-employee' means an employee who—

"(A) owns the entire interest in an unincorporated trade or business, or

"(B) in the case of a partnership, is a partner who owns more than 10 percent of either the capital interest or the profits interest in such partnership.

To the extent provided in regulations prescribed by the Secretary or his delegate, such term also means an individual who has been an owner-employee within the meaning of the preceding sentence.

"(4) EMPLOYER.—An individual who owns the entire interest in an unincorporated trade or business shall be treated as his own employer. A partnership shall be treated as the employer of each partner who is an employee within the meaning of paragraph (1).

"(5) CONSTRUCTIVE OWNERSHIP.—An individual shall be treated as owning any interest in an unincorporated trade or business which is owned, directly or indirectly, by his spouse or minor children. An individual who owns any interest in an unincorporated trade or business or is an employee of such trade or business shall be treated as owning any interest in such unincorporated trade or business which is owned, directly or indirectly, by his ancestors or lineal descendants. Any interest treated as owned by any individual by reason of the application of the preceding sentences shall not be treated as owned by him for the purpose of applying such sentences in order to make any other individual the constructive owner of such interest. For purposes of this paragraph, a legally adopted child of an individual shall be treated as a child of such individual by blood.

"(6) CONTRIBUTIONS ON BEHALF OF OWNER-EMPLOYEES.—The term 'contribution on behalf of an owner-employee' includes, except as the context otherwise requires, a contribution under a plan—

"(A) by the employer for an owner-employee, and

"(B) by an owner-employee as an employee.

"(d) ADDITIONAL REQUIREMENTS FOR QUALIFICATION OF TRUSTS AND PLANS BENEFITING OWNER-EMPLOYEES.—A trust forming part of a pension or profit-sharing plan which provides contributions or benefits for employees some or all of whom are owner-employees shall constitute a qualified trust under this section only if, in addition to meeting the requirements of subsection (a), the following requirements of this subsection are met by the trust and by the plan of which such trust is a part:

"(1) In the case of a trust which is created on or after the date of the enactment of this subsection, or which was created before such date but is not exempt from tax under section 501(a) as an organization described in subsection (a) on the day before such date, the trustee is a bank, but a person (including the employer) other than a bank may be granted, under the trust instrument, the power to control the investment of the trust funds either by directing investments (including reinvestments, disposals, and exchanges) or by disapproving proposed investments (including reinvestments, disposals, and exchanges). This paragraph shall not apply to a trust created or organized outside the United States before the date of

the enactment of this subsection if, under section 402(c), it is treated as exempt from tax under section 501(a) on the day before such date. For purposes of this paragraph, the term 'bank' means a bank as defined in section 581, a corporation which under the laws of the State of its incorporation is subject to supervision and examination by the commissioner of banking or other officer of such State in charge of the administration of the banking laws of such State, and, in the case of a trust created or organized outside the United States, a bank or trust company, wherever incorporated, exercising fiduciary powers and subject to supervision and examination by governmental authority.

"(2) Under the plan—

"(A) the employees' rights to or derived from the contributions under the plan are nonforfeitable at the time the contributions are paid to or under the plan; and

"(B) in the case of a profit-sharing plan, there is a definite formula for determining the contributions to be made by the employer on behalf of employees (other than owner-employees).

Subparagraph (A) shall not apply to contributions which, under provisions of the plan adopted pursuant to regulations prescribed by the Secretary or his delegate to preclude the discrimination prohibited by subsection (a) (4), may not be used to provide benefits for designated employees in the event of early termination of the plan.

"(3) The plan benefits each employee having a period of employment of 3 years or more. For purposes of the preceding sentence, the term 'employee' does not include any employee whose customary employment is for not more than 20 hours in any one week or is for not more than 5 months in any calendar year.

"(4) Under the plan—

"(A) contributions or benefits are not provided for any owner-employee unless such owner-employee has consented to being included under the plan; and

"(B) no benefits may be paid to any owner-employee, except in the case of his becoming disabled (within the meaning of section 213(g) (3)), prior to his attaining the age of 59½ years.

"(5) The plan does not permit—

"(A) contributions to be made by the employer on behalf of any owner-employee in excess of the amounts which may be deducted under section 404 (determined without regard to section 404(a) (10)) for the taxable year;

"(B) in the case of a plan which provides contributions or benefits only for owner-employees, contributions to be made on behalf of any owner-employee in excess of the amounts which may be deducted under section 404 (determined without regard to section 404(a) (10)) for the taxable year; and

"(C) if a distribution under the plan is made to any employee and if any portion of such distribution is an amount described in section 72(m) (5) (A) (i), contributions to be made on behalf of such employee for the 5 taxable years succeeding the taxable year in which such distribution is made.

Subparagraphs (A) and (B) shall not apply to any contribution which is not considered to be an excess contribution (as defined in subsection (e) (1)) by reason of the application of subsection (e) (3).

"(6) Except as provided in this paragraph, the plan meets the requirements of subsection (a) (4) without taking into account for any purpose contributions or benefits under chapter 2 (relating to tax on self-employment income), chapter 21 (relating to Federal Insurance Contributions Act), title II of the Social Security Act, as amended, or any other Federal or State law. If—

"(A) of the contributions deductible under section 404 (determined without regard to section 404(a) (10)), not more than one-third is deductible by reason of contribu-

tions by the employer on behalf of owner-employees, and

"(B) taxes paid by the owner-employees under chapter 2 (relating to tax on self-employment income), and the taxes which would be payable under such chapter 2 by the owner-employees but for paragraphs (4) and (5) of section 1402(c), are taken into account as contributions by the employer on behalf of such owner-employees, then taxes paid under section 3111 (relating to tax on employers) with respect to an employee may, for purposes of subsection (a) (4), be taken into account as contributions by the employer for such employee under the plan.

"(7) Under the plan, if an owner-employee dies before his entire interest has been distributed to him, or if distribution has been commenced in accordance with subsection (a) (9) (B) to his surviving spouse and such surviving spouse dies before his entire interest has been distributed to such surviving spouse, his entire interest (or the remaining part of such interest if distribution thereof has commenced) will, within 5 years after his death (or the death of his surviving spouse), be distributed, or applied to the purchase of an immediate annuity for his beneficiary or beneficiaries (or the beneficiary or beneficiaries of his surviving spouse) which will be payable for the life of such beneficiary or beneficiaries (or for a term certain not extending beyond the life expectancy of such beneficiary or beneficiaries) and which will be immediately distributed to such beneficiary or beneficiaries. The preceding sentence shall not apply if distribution of the interest of an owner-employee has commenced and such distribution is for a term certain over a period permitted under subsection (a) (9) (B) (ii).

"(8) Under the plan—

"(A) any contribution which is an excess contribution, together with the income attributable to such excess contribution, is (unless subsection (e) (2) (E) applies) to be repaid to the owner-employee on whose behalf such excess contribution is made;

"(B) if for any taxable year the plan does not, by reason of subsection (e) (2) (A), meet (for purposes of section 404) the requirements of this subsection with respect to an owner-employee, the income for the taxable year attributable to the interest of such owner-employee under the plan is to be paid to such owner-employee; and

"(C) the entire interest of an owner-employee is to be repaid to him when required by the provisions of subsection (e) (2) (E).

"(9) (A) If the plan provides contributions or benefits for an owner-employee who controls, or for two or more owner-employees who together control, the trade or business with respect to which the plan is established, and who also control as an owner-employee or as owner-employees one or more other trades or businesses, such plan and the plans established with respect to such other trades or businesses, when coalesced, constitute a single plan which meets the requirements of subsection (a) (including paragraph (10) thereof) and of this subsection with respect to the employees of all such trades or businesses (including the trade or business with respect to which the plan intended to qualify under this section is established).

"(B) For purposes of subparagraph (A), an owner-employee, or two or more owner-employees, shall be considered to control a trade or business if such owner-employee, or such two or more owner-employees together—

"(i) own the entire interest in an unincorporated trade or business, or

"(ii) in the case of a partnership, own more than 50 percent of either the capital interest or the profits interest in such partnership.

87TH CONGRESS
2^D SESSION

H. R. 10650

IN THE SENATE OF THE UNITED STATES

SEPTEMBER 6, 1962

Ordered to be printed with the amendments of the Senate numbered

AN ACT

To amend the Internal Revenue Code of 1954 to provide a credit for investment in certain depreciable property, to eliminate certain defects and inequities, and for other purposes.

1 *Be it enacted by the Senate and House of Representa-*
2 *tives of the United States of America in Congress assembled,*

3 **SECTION 1. SHORT TITLE, ETC.**

4 (a) **SHORT TITLE.**—This Act may be cited as the
5 “Revenue Act of 1962”.

1 (b) TABLE OF CONTENTS.—

(1) Sec. 1. Short title, etc.

- (a) Short title.
- (b) Table of contents.
- (c) Amendment of 1954 code.

Sec. 2. Credit for investment in certain depreciable property.

- (a) Allowance of credit.
- (b) Rules for computing credit.
- (c) Certain corporate acquisitions.
- (d) Clerical amendment.
- (e) Effective date.

Sec. 3. Appearances, etc., with respect to legislation.

- (a) In general.
- (b) Effective date.

Sec. 4. Disallowance of certain entertainment, etc., expenses.

- (a) Denial of deduction.
- (b) Traveling expenses.
- (c) Effective date.

Sec. 5. Amount of distribution where certain foreign corporations distribute property in kind.

- (a) Amount distributed.
- (b) Basis.
- (c) Dividends received from certain foreign corporations.
- (d) Credit for foreign taxes.
- (e) Effective date.

Sec. 6. Amendment of section 482.

- (a) In general.
- (b) Clerical amendment.
- (c) Effective date.

Sec. 7. Distributions of foreign personal holding company income.

- (a) Definition of foreign personal holding company.
- (b) Amount of undistributed income.
- (c) Effective date.

Sec. 8. Mutual savings banks, etc.

- (a) Reserves for losses on loans.
- (b) Foreclosure on property securing loans.
- (c) Definition of domestic building and loan association.
- (d) Clerical amendments.
- (e) Repeal of exemption from communications and transportation of persons taxes.
- (f) Effective dates.

Sec. 9. Distributions by foreign trusts.

- (a) Definitions.
- (b) Accumulation distributions of foreign trusts.

1 (b) TABLE OF CONTENTS.—Continued

Sec. 9. Distributions by foreign trusts.—Continued

- (c) Allocation of accumulation distributions to preceding years.
- (d) Amounts treated as received in prior years.
- (e) Special rules for foreign trusts.
- (f) Information returns with respect to foreign trusts.
- (g) Failure to file information returns.
- (h) United States person defined.
- (i) Technical amendments.
- (j) Effective date.

Sec. 10. Mutual insurance companies (other than life, marine, and certain fire insurance companies), etc.

- (a) Imposition of tax.
- (b) Taxable investment income.
- (c) Statutory underwriting income or loss.
- (d) Mutual fire insurance companies operating on basis of premium deposits.
- (e) Election of certain mutual companies to be taxed on total income.
- (f) Technical amendments, etc.
- (g) Effective date.

Sec. 11. Domestic corporations receiving dividends from foreign corporations.

- (a) Entire amount of foreign tax to be taken into account.
- (b) Inclusion in gross income of amount equal to taxes deemed paid.
- (c) Determination of source of dividends received from certain foreign corporations.
- (d) Repeal of section 902(d).
- (e) Technical amendments.
- (f) Effective date.

Sec. 12. Earned income from sources without the United States.

- (a) Limitation on amount and type of income excluded.
- (b) Computation of employees' contributions.
- (c) Effective date.

Sec. 13. Controlled foreign corporations.

- (a) In general.
- (b) Technical and clerical amendments.
- (c) Effective date.

Sec. 14. Gain from dispositions of certain depreciable property.

- (a) In general.
- (b) Change in method of depreciation.
- (c) Salvage value of personal property.
- (d) Special rule for charitable contributions of section 1245 property.
- (e) Technical amendments.
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- Sec. 15. Foreign investment companies.
- (a) Treatment of sale of stock of foreign investment companies.
 - (b) Conforming amendments.
 - (c) Effective date.
- Sec. 16. Gain from certain sales or exchanges of stock in certain foreign corporations.
- (a) Treatment of gain from the redemption, cancellation, or sale of stock in certain foreign corporations.
 - (b) Clerical amendment.
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- Sec. 17. Tax treatment of cooperatives and patrons.
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- Sec. 18. Inclusion of foreign real property in gross estate.
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 - (b) Information as to organization or reorganization of foreign corporations and as to acquisitions of their stock.
 - (c) Civil penalty for failure to file return.
 - (d) Technical amendments.
 - (e) Effective date.
- Sec. 21. Treaties.
- Sec. 1. *Short title, etc.*
- (a) *Short title.*
 - (b) *Table of contents.*
 - (c) *Amendment of 1954 code.*
- Sec. 2. *Credit for investment in certain depreciable property.*
- (a) *Allowance of credit.*
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- (e) *Statutes of limitations and interest relating to investment credit carrybacks.*
- (f) *Technical amendment.*
- (g) *Clerical amendments.*
- (h) *Effective date.*

Sec. 3. Appearances, etc., with respect to legislation.

- (a) *In general.*
- (b) *Effective date.*

Sec. 4. Disallowance of certain entertainment, etc., expenses.

- (a) *Denial of deduction.*
- (b) *Traveling expenses.*
- (c) *Effective date.*

Sec. 5. Amount of distribution where certain foreign corporations distribute property in kind.

- (a) *Amount distributed.*
- (b) *Basis.*
- (c) *Dividends received from certain foreign corporations.*
- (d) *Effective date.*

Sec. 6. Mutual savings banks, etc.

- (a) *Reserves for losses on loans.*
- (b) *Foreclosure on property securing loans.*
- (c) *Definition of domestic building and loan association.*
- (d) *Clerical amendments.*
- (e) *Repeal of exemption from certain excise taxes.*
- (f) *Deduction for dividends or interest paid on deposits.*
- (g) *Effective dates.*

Sec. 7. Distributions by foreign trusts.

- (a) *Definitions.*
- (b) *Accumulation distributions of foreign trusts.*
- (c) *Allocation of accumulation distributions to preceding years.*
- (d) *Amounts treated as received in prior years.*
- (e) *Special rules for foreign trusts.*
- (f) *Information returns with respect to foreign trusts.*
- (g) *Failure to file information returns.*
- (h) *United States person defined.*
- (i) *Technical amendments.*
- (j) *Effective date.*

Sec. 8. Mutual insurance companies (other than life, marine, and certain fire or flood insurance companies), etc.

- (a) *Imposition of tax.*
- (b) *Taxable investment income.*

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Sec. 8. Mutual insurance companies—Continued

- (c) *Statutory underwriting income or loss.*
- (d) *Exemption from tax.*
- (e) *Mutual fire insurance companies operating on basis of premium deposits.*
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- (g) *Technical amendments, etc.*
- (h) *Effective date.*

Sec. 9. Domestic corporations receiving dividends from foreign corporations.

- (a) *Foreign taxes deemed paid by domestic corporations.*
- (b) *Inclusion in gross income of amount equal to taxes deemed paid.*
- (c) *Determination of source of dividends received from certain foreign corporations.*
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Sec. 10. Separate limitation on foreign tax credit with respect to certain interest income.

- (a) *Limitation on foreign tax credit.*
- (b) *Effective date.*

Sec. 11. Earned income from sources without the United States.

- (a) *Limitation on amount and type of income excluded.*
- (b) *Computation of employees' contributions.*
- (c) *Effective date.*

Sec. 12. Controlled foreign corporations.

- (a) *In general.*
- (b) *Technical and clerical amendments.*
- (c) *Effective date.*

Sec. 13. Gain from dispositions of certain depreciable property.

- (a) *In general.*
- (b) *Change in method of depreciation.*
- (c) *Salvage value of personal property.*
- (d) *Special rule for charitable contributions of section 1245 property.*
- (e) *Computation of taxable income for purposes of limitation on percentage depletion deduction.*
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Sec. 14. Foreign investment companies.

- (a) *Treatment of sale of stock of foreign investment companies.*
- (b) *Conforming amendments.*
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(a) *Treatment of gain from the redemption, cancellation, or sale of stock in certain foreign corporations.*

(b) *Clerical amendment.*

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Sec. 16. Sales and exchanges of patents, etc., to certain foreign corporations.

(a) *Treatment of gain as ordinary income.*

(b) *Clerical amendment.*

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Sec. 17. Tax treatment of cooperatives and patrons.

(a) *In general.*

(b) *Technical amendments.*

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Sec. 18. Inclusion of foreign real property in gross estate.

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(c) *Returns regarding payment of interest.*

(d) *Penalties for failure to file information returns.*

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(a) *Information to be furnished by individuals, domestic corporations, etc., with respect to certain foreign corporations.*

(b) *Information as to organization or reorganization of foreign corporations and as to acquisitions of their stock.*

(c) *Civil penalty for failure to file return.*

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- Sec. 33. Effective date of amendment to section 1374(b).*
- Sec. 34. Treaties.*

1 (c) AMENDMENT OF 1954 CODE.—~~(2)~~Whenever *Ex-*
 2 *cept as otherwise expressly provided, whenever* in this Act an
 3 amendment or repeal is expressed in terms of an amendment
 4 to, or repeal of, a section or other provision, the reference
 5 shall be considered to be made to a section or other provision
 6 of the Internal Revenue Code of 1954.

7 **SEC. 2. CREDIT FOR INVESTMENT IN CERTAIN DEPRE-**
 8 **CIABLE PROPERTY.**

9 (a) ALLOWANCE OF CREDIT.—Part IV of subchapter
 10 A of chapter 1 (relating to credits against tax) is amended
 11 by redesignating section 38 as section ~~(3)~~⁴⁰ 39 and by
 12 inserting after section 37 the following new section:

13 **“SEC. 38. INVESTMENT IN CERTAIN DEPRECIABLE PROP-**
 14 **ERTY.**

15 “(a) GENERAL RULE.—There shall be allowed, as a
 16 credit against the tax imposed by this chapter, the amount
 17 determined under subpart B of this part.

18 “(b) REGULATIONS.—The Secretary or his delegate
 19 shall prescribe such regulations as may be necessary to carry
 20 out the purposes of this section and subpart B.”

21 (b) RULES FOR COMPUTING CREDIT.—Part IV of sub-

1 chapter A of chapter 1 is amended by adding at the end
2 thereof the following new subpart:

3 **“Subpart B—Rules for Computing Credit for Investment**
4 **in Certain Depreciable Property**

“Sec. 46. Amount of credit.

“Sec. 47. Certain dispositions, etc., of section 38 property.

“Sec. 48. Definitions; special rules.

5 **“SEC. 46. AMOUNT OF CREDIT.**

6 **“(a) DETERMINATION OF AMOUNT.—**

7 **“(1) GENERAL RULE.—**The amount of the credit
8 allowed by section 38 for the taxable year shall be equal
9 to 7 percent of the qualified investment (as defined in
10 subsection (c)).

11 **“(2) LIMITATION BASED ON AMOUNT OF TAX.—**
12 Notwithstanding paragraph (1), the credit allowed by
13 section 38 for the taxable year shall not exceed—

14 **“(A)** so much of the liability for tax for the
15 taxable year as does not exceed \$25,000, plus

16 **“(B)** 25 percent of so much of the liability
17 for tax for the taxable year as exceeds \$25,000.

18 **“(3) LIABILITY FOR TAX.—**For purposes of para-
19 graph (2), the liability for tax for the taxable year shall
20 be the tax imposed by this chapter for such year,
21 reduced by the sum of the credits allowable under—

22 **“(A)** section 33 (relating to foreign tax
23 credit),

1 “(B) section 34 (relating to dividends re-
2 ceived by individuals),

3 “(C) section 35 (relating to partially tax-
4 exempt interest), and

5 “(D) section 37 (relating to retirement in-
6 come).

7 For purposes of this paragraph, any tax imposed for the
8 taxable year by section 531 (relating to accumulated
9 earnings tax) or by section 541 (relating to personal
10 holding company tax) shall not be considered tax
11 imposed by this chapter for such year.

12 “(4) MARRIED INDIVIDUALS.—In the case of a
13 husband or wife who files a separate return, the amount
14 specified under subparagraphs (A) and (B) of para-
15 graph (2) shall be \$12,500 in lieu of \$25,000. This
16 paragraph shall not apply if the spouse of the taxpayer
17 has no qualified investment for, and no unused credit
18 (4)*carryback or carryover* to, the taxable year of such
19 spouse which ends within or with the taxpayer’s taxable
20 year.

21 “(5) AFFILIATED GROUPS.—In the case of an
22 affiliated group, the \$25,000 amount specified under
23 subparagraphs (A) and (B) of paragraph (2) shall be
24 reduced for each member of the group by apportioning
25 \$25,000 among the members of such group in such

1 manner as the Secretary or his delegate shall by regula-
 2 tions prescribe. For purposes of the preceding sentence,
 3 the term 'affiliated group' has the meaning assigned to
 4 such term by section 1504 (a), except that all corpora-
 5 tions shall be treated as includible corporations (with-
 6 out any exclusion under section 1504 (b)).

7 **(5)“(b) 5-YEAR CARRYOVER OF UNUSED CREDITS.—**

8 “(1) ALLOWANCE OF CREDIT.—If the amount of
 9 the credit determined under subsection (a)(1) for any
 10 taxable year exceeds the limitation provided by subsec-
 11 tion (a)(2) for such taxable year (hereinafter in this
 12 subsection referred to as 'unused credit year'), such
 13 excess shall be added to the amount allowable as a credit
 14 by section 38 for each of the 5 succeeding taxable years
 15 to the extent not taken into account for taxable years
 16 intervening between the unused credit year and such
 17 succeeding taxable year.

18 “(2) LIMITATION.—The amount of the unused
 19 credit which may be added under paragraph (1) for any
 20 succeeding taxable year shall not exceed the amount by
 21 which the limitation provided by subsection (a)(2) for
 22 such taxable year exceeds the sum of—

23 “(A) the credit allowable under subsection
 24 (a)(1) for such taxable year, and

25 “(B) the amounts which, by reason of this

subsection, are added to the amount allowable for such taxable year and attributable to taxable years preceding the unused credit year.

“(b) CARRYBACK AND CARRYOVER OF UNUSED CREDITS.—

“(1) ALLOWANCE OF CREDIT.—If the amount of the credit determined under subsection (a)(1) for any taxable year exceeds the limitation provided by subsection (a)(2) for such taxable year (hereinafter in this subsection referred to as ‘unused credit year’), such excess shall be—

“(A) an investment credit carryback to each of the 3 taxable years preceding the unused credit year, and

“(B) an investment credit carryover to each of the 5 taxable years following the unused credit year,

and shall be added to the amount allowable as a credit by section 38 for such years, except that such excess may be a carryback only to a taxable year ending after June 30, 1962. The entire amount of the unused credit for an unused credit year shall be carried to the earliest of the 8 taxable years to which (by reason of subparagraphs (A) and (B)) such credit may be carried, and then to each of the other 7 taxable years

1 to the extent that, because of the limitation contained
2 in paragraph (2), such unused credit may not be added
3 for a prior taxable year to which such unused credit
4 may be carried.

5 “(2) *LIMITATION.*—The amount of the unused
6 credit which may be added under paragraph (1) for
7 any preceding or succeeding taxable year shall not
8 exceed the amount by which the limitation provided
9 by subsection (a)(2) for such taxable year exceeds
10 the sum of—

11 “(A) the credit allowable under subsection
12 (a)(1) for such taxable year, and

13 “(B) the amounts which, by reason of this sub-
14 section, are added to the amount allowable for such
15 taxable year and attributable to taxable years pre-
16 ceding the unused credit year.

17 “(3) *EFFECT OF NET OPERATING LOSS CARRY-*
18 *BACK.*—To the extent that the excess described in para-
19 graph (1) arises by reason of a net operating loss carry-
20 back, subparagraph (A) of paragraph (1) shall not
21 apply.

22 “(4) *TAXABLE YEAR BEGINNING BEFORE JULY*
23 *1, 1962.*—For purposes of determining the amount of an
24 investment credit carryback that may be added under
25 paragraph (1) for a taxable year beginning before July

1 1, 1962, and ending after June 30, 1962, the amount
 2 of the limitation provided by subsection (a)(2) is the
 3 amount which bears the same ratio to such limitation as
 4 the number of days in such year after June 30, 1962,
 5 bears to the total number of days in such year.

6 “(c) QUALIFIED INVESTMENT.—

7 “(1) IN GENERAL.—For purposes of this subpart,
 8 the term ‘qualified investment’ means, with respect to
 9 any taxable year, the aggregate of—

10 “(A) the applicable percentage of the basis of
 11 each new section 38 property (as defined in section
 12 48(b)) placed in service by the taxpayer during
 13 such taxable year, plus

14 “(B) the applicable percentage of the cost of
 15 each used section 38 property (as defined in section
 16 48(c)(1)) placed in service by the taxpayer dur-
 17 ing such taxable year.

18 “(2) APPLICABLE PERCENTAGE.—For purposes of
 19 paragraph (1), the applicable percentage for any prop-
 20 erty shall be determined under the following table:

“If the useful life is—	The applicable percentage is—
4 years or more but less than 6 years.....	33½
6 years or more but less than 8 years.....	66⅔
8 years or more.....	100

1 For purposes of this paragraph, the useful life of any
2 property shall be determined as of the time such property
3 is placed in service by the taxpayer.

4 “(3) PUBLIC UTILITY PROPERTY.—

5 “(A) In the case of section 38 property which
6 is public utility property, the amount of the qualified
7 investment shall be $\frac{3}{7}$ of the amount determined
8 under paragraph (1).

9 “(B) For purposes of subparagraph (A), the
10 term ‘public utility property’ means property used
11 predominantly in the trade or business of the fur-
12 nishing or sale of—

13 “(i) electrical energy, water, or sewage
14 disposal services,

15 “(ii) gas through a local distribution sys-
16 tem,

17 “(iii) telephone service, or

18 “(iv) telegraph service by means of do-
19 mestic telegraph operations (as defined in
20 section 222 (a) (5) of the Communications Act
21 of 1934, as amended; 47 U.S.C., sec. 222 (a)
22 (5)),

23 if the rates for such furnishing or sale, as the case
24 may be, have been established or approved by a
25 State or political subdivision thereof, by an agency

or instrumentality of the United States, or by a public service or public utility commission or other similar body of any State or political subdivision thereof.

(6)“(4) *CERTAIN REPLACEMENT PROPERTY.*—For purposes of paragraph (1), if section 38 property is placed in service by the taxpayer to replace property which was—

“(A) *destroyed or damaged by fire, storm, shipwreck, or other casualty, or*

“(B) *stolen,*

the basis of such section 38 property (in the case of new section 38 property), or the cost of such section 38 property (in the case of used section 38 property), which (but for this paragraph) would be taken into account under paragraph (1) shall be reduced by an amount equal to the amount received by the taxpayer as compensation, by insurance or otherwise, for the property so destroyed, damaged, or stolen, or to the adjusted basis of such property, whichever is the lesser. No reduction in basis or cost shall be made under the preceding sentence in any case in which the reduction in qualified investment attributable to the substitution required by section 47(a) (1) with respect to the property so destroyed, damaged,

1 *or stolen (determined without regard to section 47(a)*
 2 *(4)) is greater than the reduction described in the*
 3 *preceding sentence.*

4 “(d) LIMITATIONS WITH RESPECT TO CERTAIN PER-
 5 SONS.—

6 “(1) IN GENERAL.—In the case of—

7 “(A) an organization to which section 593
 8 applies,

9 “(B) a regulated investment company or a
 10 real estate investment trust subject to taxation un-
 11 der subchapter M (sec. 851 and following), and

12 “(C) a cooperative organization described in
 13 section 1381 (a),

14 the qualified investment and the \$25,000 amount
 15 specified under subparagraphs (A) and (B) of sub-
 16 section (a) (2) shall equal such person’s ratable share
 17 of such items.

18 “(2) RATABLE SHARE.—For purposes of para-
 19 graph (1), the ratable share of any person for any
 20 taxable year of the items described therein shall be—

21 “(A) in the case of an organization referred
 22 to in paragraph (1) (A), 50 percent thereof,

23 “(B) in the case of a regulated investment
 24 company or a real estate investment trust, the ratio
 25 (i) the numerator of which is its taxable income and

(ii) the denominator of which is its taxable income computed without regard to the deduction for dividends paid provided by section 852 (b) (2) (D) or 857 (b) (2) (C), as the case may be, and

“(C) in the case of a cooperative organization, the ratio (i) the numerator of which is its taxable income and (ii) the denominator of which is its taxable income increased by amounts to which section 1382 (b) or (c) applies and similar amounts the tax treatment of which is determined without regard to subchapter T (sec. 1381 and following).

For purposes of subparagraph (B) of the preceding sentence, the term ‘taxable income’ means in the case of a regulated investment company its investment company taxable income (within the meaning of section 852 (b) (2)), and in the case of a real estate investment trust its real estate investment trust taxable income (within the meaning of section 857 (b) (2)).

**“SEC. 47. CERTAIN DISPOSITIONS, ETC., OF SECTION 38
PROPERTY.**

“(a) GENERAL RULE.—Under regulations prescribed by the Secretary or his delegate—

“(1) EARLY DISPOSITION, ETC.—If during any taxable year any property is disposed of, or otherwise ceases to be section 38 property with respect to the tax-

1 payer, before the close of the useful life which was taken
2 into account in computing the credit under section 38,
3 then the tax under this chapter for such taxable year
4 shall be increased by an amount equal to the aggregate
5 decrease in the credits allowed under section 38 for all
6 prior taxable years which would have resulted solely
7 from substituting, in determining qualified investment,
8 for such useful life the period beginning with the time
9 such property was placed in service by the taxpayer and
10 ending with the time such property ceased to be section
11 38 property.

12 “(2) PROPERTY BECOMES PUBLIC UTILITY PROP-
13 PERTY.—If during any taxable year any property taken
14 into account in determining qualified investment becomes
15 public utility property (within the meaning of section
16 46 (c) (3) (B)), then the tax under this chapter for
17 such taxable year shall be increased by an amount equal
18 to the aggregate decrease in the credits allowed under
19 section 38 for all prior taxable years which would have
20 resulted solely from treating the property, for purposes
21 of determining qualified investment, as public utility
22 property (after giving due regard to the period before
23 such change in use) . If the application of this paragraph
24 to any property is followed by the application of para-

graph (1) to such property, proper adjustment shall be made in applying paragraph (1).

“(3) ~~(7)CARRYOVERS~~ *CARRYBACKS AND CARRYOVERS ADJUSTED.*—In the case of any cessation described in paragraph (1) or any change in use described in paragraph (2), the ~~(8)~~*carrybacks and carryovers* under section 46 (b) shall be adjusted by reason of such cessation (or change in use).

~~(9)~~“(4) *PROPERTY DESTROYED BY CASUALTY, ETC.*—No increase shall be made under paragraph (1) and no adjustment shall be made under paragraph (3) in any case in which—

“(A) any property is disposed of, or otherwise ceases to be section 38 property with respect to the taxpayer, on account of its destruction or damage by fire, storm, shipwreck, or other casualty, or by reason of its theft,

“(B) section 38 property is placed in service by the taxpayer to replace the property described in subparagraph (A), and

“(C) the reduction in basis or cost of such section 38 property described in the first sentence of section 46(c)(4) is greater than the reduction in qualified investment which (but for this paragraph)

1 *would be made by reason of the substitution required*
 2 *by paragraph (1) with respect to the property*
 3 *described in subparagraph (A).*

4 “(b) SECTION NOT TO APPLY IN CERTAIN CASES.—

5 Subsection (a) shall not apply to—

6 “(1) a transfer by reason of death, or

7 “(2) a transaction to which section 381 (a) applies.

8 For purposes of subsection (a), property shall not be treated
 9 as ceasing to be section 38 property with respect to the tax-
 10 payer by reason of a mere change in the form of conducting
 11 the trade or business so long as the property is retained in
 12 such trade or business as section 38 property and the tax-
 13 payer retains a substantial interest in such trade or business.

14 “(c) SPECIAL RULE.—Any increase in tax under sub-
 15 section (a) shall not be treated as tax imposed by this
 16 chapter for purposes of determining the amount of any credit
 17 allowable under subpart A.

18 “SEC. 48. DEFINITIONS; SPECIAL RULES.

19 “(a) SECTION 38 PROPERTY.—

20 “(1) IN GENERAL.—Except as provided in this
 21 subsection, the term ‘section 38 property’ means—

22 “(A) tangible personal property, or

23 “(B) other tangible property (not including
 24 a building and its structural components) but only
 25 if such property—

“(i) is used as an integral part of manufacturing, production, or extraction or of furnishing transportation, communications, electrical energy, gas, water, or sewage disposal services, or

“(ii) constitutes a research or storage facility used in connection with any of the activities referred to in clause (i).

Such term includes only property with respect to which depreciation (or amortization in lieu of depreciation) is allowable and having a useful life (determined as of the time such property is placed in service) of 4 years or more.

“(2) PROPERTY USED OUTSIDE THE UNITED STATES.—

“(A) IN GENERAL.—Except as provided in subparagraph (B), the term ‘section 38 property’ does not include property which is used predominantly outside the United States.

“(B) EXCEPTIONS.—Subparagraph (A) shall not apply to—

“(i) any aircraft which is registered by the Administrator of the Federal Aviation Agency and which is operated to and from the United States;

1 “(ii) rolling stock, of a domestic railroad
2 corporation subject to part I of the Interstate
3 Commerce Act, which is used within and with-
4 out the United States;

5 “(iii) any vessel documented under the
6 laws of the United States which is operated in
7 the foreign or domestic commerce of the United
8 States;

9 “(iv) any motor vehicle of a United States
10 person (as defined in section 7701 (a) (30))
11 which is operated to and from the United
12 States;

13 “(v) any container of a United States
14 person which is used in the transportation of
15 property to and from the United States; and

16 “(vi) any property (other than a vessel
17 or an aircraft) of a United States person which
18 is used for the purpose of exploring for, de-
19 veloping, removing, or transporting resources
20 from the outer Continental Shelf (within the
21 meaning of section 2 of the Outer Continental
22 Shelf Lands Act, as amended and supple-
23 mented; 43 U.S.C., sec. 1331).

24 “(3) PROPERTY USED FOR LODGING.—Property
25 which is used predominantly to furnish lodging or in

1 connection with the furnishing of lodging shall not be
2 treated as section 38 property. The preceding sentence
3 shall not apply to—

4 “(A) nonlodging commercial facilities which
5 are available to persons not using the lodging facili-
6 ties on the same basis as they are available to per-
7 sons using the lodging facilities, and

8 “(B) property used by a hotel or motel in con-
9 nection with the trade or business of furnishing
10 lodging where the predominant portion of the ac-
11 commodation is used by transients.

12 “(4) PROPERTY USED BY CERTAIN TAX-EXEMPT
13 ORGANIZATIONS.—Property used by an organization
14 (other than a cooperative described in section 521)
15 which is exempt from the tax imposed by this chapter
16 shall be treated as section 38 property only if such
17 property is used predominantly in an unrelated trade or
18 business the income of which is subject to tax under
19 section 511.

20 “(5) PROPERTY USED BY GOVERNMENTAL
21 UNITS.—Property used by the United States, any State
22 or political subdivision thereof, any international organ-
23 ization, or any agency or instrumentality of any of the
24 foregoing shall not be treated as section 38 property.

1 **(10)**“(6) *LIVESTOCK*.—*Livestock shall not be treated as*
 2 *section 38 property.*

3 “(b) **NEW SECTION 38 PROPERTY**.—For purposes of
 4 this subpart, the term ‘new section 38 property’ means sec-
 5 tion 38 property—

6 “(1) the construction, reconstruction, or erection
 7 of which is completed by the taxpayer after **(11)**~~Decem-~~
 8 ~~ber 31, 1961~~ *June 30, 1962*, or

9 “(2) acquired after **(12)**~~December 31, 1961~~ *June*
 10 *30, 1962*, if the original use of such property commences
 11 with the taxpayer and commences after such date.

12 In applying section 46 (c) (1) (A) in the case of property
 13 described in paragraph (1), there shall be taken into account
 14 only that portion of the basis which is properly attributable
 15 to construction, reconstruction, or erection after **(13)**~~Decem-~~
 16 ~~ber 31, 1961~~ *June 30, 1962*.

17 “(c) **USED SECTION 38 PROPERTY**.—

18 “(1) **IN GENERAL**.—For purposes of this subpart,
 19 the term ‘used section 38 property’ means section 38
 20 property acquired by purchase after **(14)**~~December 31,~~
 21 ~~1961~~ *June 30, 1962*, which is not new section 38 prop-
 22 erty. Property shall not be treated as ‘used section 38
 23 property’ if, after its acquisition by the taxpayer, it is
 24 used by a person who used such property before such
 25 acquisition (or by a person who bears a relationship

described in section 179 (d) (2) (A) or (B) to a person who used such property before such acquisition).

“(2) DOLLAR LIMITATION.—

“(A) IN GENERAL.—The cost of used section 38 property taken into account under section 46 (c) (1) (B) for any taxable year shall not exceed \$50,000. If such cost exceeds \$50,000, the taxpayer shall select (at such time and in such manner as the Secretary or his delegate shall by regulations prescribe) the items to be taken into account, but only to the extent of an aggregate cost of \$50,000. Such a selection, once made, may be changed only in the manner, and to the extent, provided by such regulations.

“(B) MARRIED INDIVIDUALS.—In the case of a husband or wife who files a separate return, the limitation under subparagraph (A) shall be \$25,000 in lieu of \$50,000. This subparagraph shall not apply if the spouse of the taxpayer has no used section 38 property which may be taken into account as qualified investment for the taxable year of such spouse which ends within or with the taxpayer’s taxable year.

“(C) AFFILIATED GROUPS.—In the case of an affiliated group, the \$50,000 amount specified under

1 subparagraph (A) shall be reduced for each mem-
2 ber of the group by apportioning \$50,000 among
3 the members of such group in accordance with their
4 respective amounts of used section 38 property
5 which may be taken into account.

6 “(D) PARTNERSHIPS.—In the case of a part-
7 nership, the limitation contained in subparagraph
8 (A) shall apply with respect to the partnership and
9 with respect to each partner.

10 “(3) DEFINITIONS.—For purposes of this sub-
11 section—

12 “(A) PURCHASE.—The term ‘purchase’ has
13 the meaning assigned to such term by section
14 179 (d) (2) .

15 “(B) COST.—The cost of used section 38
16 property does not include so much of the basis of
17 such property as is determined by reference to the
18 adjusted basis of other property held at any time by
19 the person acquiring such property. If property is
20 disposed of **(15)***(other than by reason of its destruc-*
21 *tion or damage, by fire, storm, shipwreck, or other*
22 *casualty, or its theft)* and used section 38 property
23 similar or related in service or use is acquired as a re-
24 placement therefor in a transaction to which the pre-
25 ceding sentence does not apply, the cost of the used

section 38 property acquired shall be its basis reduced by the adjusted basis of the property replaced. The cost of used section 38 property shall not be reduced with respect to the adjusted basis of any property disposed of if, by reason of section 47, such disposition involved an increase of tax or a reduction of the unused credit ~~(16)~~*carrybacks or* carryovers described in section 46 (b) .

“(C) AFFILIATED GROUP.—The term ‘affiliated group’ has the meaning assigned to such term by section 1504 (a) , except that—

“(i) the phrase ‘more than 50 percent’ shall be substituted for the phrase ‘at least 80 percent’ each place it appears in section 1504 (a) , and

“(ii) all corporations shall be treated as includible corporations (without any exclusion under section 1504 (b)) .

“(d) CERTAIN LEASED PROPERTY.—A person (other than a person referred to in section 46 (d)) ~~(17)~~*engaged in the business of leasing property who is a lessor of property* may (at such time, in such manner, and subject to such conditions as are provided by regulations prescribed by the Secretary or his delegate) elect with respect to any new section

1 38 property to treat the lessee as having acquired such prop-
 2 erty for an amount equal to—

3 “ (1) if such property was constructed by the lessor
 4 (or by a corporation which controls or is controlled by
 5 the lessor within the meaning of section 368 (c)), the
 6 fair market value of such property, or

7 “ (2) if paragraph (1) does not apply, the basis
 8 of such property to the lessor.

9 The election provided by the preceding sentence may be
 10 made only with respect to property which would be new
 11 section 38 property if acquired by the lessee. For purposes
 12 of the preceding sentence and section 46 (c) , the useful life
 13 of property in the hands of the lessee is the useful life of such
 14 property in the hands of the lessor. If a lessor makes the
 15 election provided by this subsection with respect to any
 16 property, the lessee shall be treated for all purposes of this
 17 subpart as having acquired such property. **(18)***If a lessor*
 18 *makes the election provided by this subsection with respect to*
 19 *any property, then, under regulations prescribed by the Secre-*
 20 *tary or his delegate, subsection (g) shall not apply with*
 21 *respect to such property and the deductions otherwise allow-*
 22 *able under section 162 to the lessee for amounts paid to the*
 23 *lessor under the lease shall be adjusted in a manner consistent*
 24 *with the provisions of subsection (g).*

25 “ (e) SUBCHAPTER S CORPORATIONS.—In the case of

1 an electing small business corporation (as defined in section
2 1371)—

3 “(1) the qualified investment for each taxable year
4 shall be apportioned pro rata among the persons who
5 are shareholders of such corporation on the last day of
6 such taxable year; and

7 “(2) any person to whom any investment has been
8 apportioned under paragraph (1) shall be treated (for
9 purposes of this subpart) as the taxpayer with respect
10 to such investment, and such investment shall not (by
11 reason of such apportionment) lose its character as an
12 investment in new section 38 property or used section
13 38 property, as the case may be.

14 “(f) ESTATES AND TRUSTS.—In the case of an estate
15 or trust—

16 “(1) the qualified investment for any taxable year
17 shall be apportioned between the estate or trust and the
18 beneficiaries on the basis of the income of the estate or
19 trust allocable to each,

20 “(2) any beneficiary to whom any investment has
21 been apportioned under paragraph (1) shall be treated
22 (for purposes of this subpart) as the taxpayer with re-
23 spect to such investment, and such investment shall not
24 (by reason of such apportionment) lose its character as

1 an investment in new section 38 property or used section
2 38 property, as the case may be, and

3 “(3) the \$25,000 amount specified under sub-
4 paragraphs (A) and (B) of section 46(a)(2) ap-
5 plicable to such estate or trust shall be reduced to an
6 amount which bears the same ratio to \$25,000 as the
7 amount of the qualified investment allocated to the
8 estate or trust under paragraph (1) bears to the entire
9 amount of the qualified investment.

10 (19)“(g) *ADJUSTMENTS TO BASIS OF PROPERTY.*—

11 “(1) *IN GENERAL.*—*The basis of any section 38*
12 *property shall be reduced, for purposes of this subtitle*
13 *other than this subpart, by an amount equal to 7 percent*
14 *of the qualified investment as determined under section*
15 *46(c) with respect to such property.*

16 “(2) *CERTAIN DISPOSITIONS, ETC.*—*If the tax*
17 *under this chapter is increased for any taxable year*
18 *under paragraph (1) or (2) of section 47(a) or an*
19 *adjustment in carrybacks or carryovers is made under*
20 *paragraph (3) of such section, the basis of the property*
21 *described in such paragraph (1) or (2), as the case may*
22 *be (immediately before the event on account of which*
23 *such paragraph (1), (2), or (3) applies), shall be in-*
24 *creased by an amount equal to the portion of such in-*

crease and the portion of such adjustment attributable to such property.

(20)~~“(g)”~~ *“(h) CROSS REFERENCE.—*

“For application of this subpart to certain acquiring corporations, see section 381(c)(23).”

(21)*(c) DEDUCTION FOR UNUSED CREDIT.—Part VI of subchapter B of chapter 1 (relating to itemized deductions for individuals and corporations) is amended by adding at the end thereof the following new section:*

“SEC. 181. DEDUCTION FOR CERTAIN UNUSED INVESTMENT CREDIT.

“If the amount of the credit determined under section 46(a)(1) for any taxable year exceeds the limitation provided by section 46(a)(2) for such taxable year and if the amount of such excess has not, after the application of section 46(b), been allowed to the taxpayer as a credit under section 38 for any taxable year, then an amount equal to the amount of such excess not so allowed as a credit shall be allowed to the taxpayer as a deduction for the first taxable year following the last taxable year in which such excess could under section 46(b) have been allowed as a credit. If a taxpayer dies or ceases to exist prior to the first taxable year following the last taxable year in which the excess described in the pre-

ceding sentence could under section 46(b) have been allowed as a credit, the amount described in the preceding sentence, or the proper portion thereof, shall, under regulations prescribed by the Secretary or his delegate, be allowed to the taxpayer as a deduction for the taxable year in which such death or cessation occurs.”

(22)(e)(d) CERTAIN CORPORATE ACQUISITIONS.—Section 381(c) (relating to items taken into account in certain corporate acquisitions) is amended by adding at the end thereof the following new paragraph:

“(23) CREDIT UNDER SECTION 38 FOR INVESTMENT IN CERTAIN DEPRECIABLE PROPERTY.—The acquiring corporation shall take into account (to the extent proper to carry out the purposes of this section and section 38, and under such regulations as may be prescribed by the Secretary or his delegate) the items required to be taken into account for purposes of section 38 in respect of the distributor or transferor corporation.”

(23)(e) STATUTES OF LIMITATIONS AND INTEREST RELATING TO INVESTMENT CREDIT CARRYBACKS.—

(1) ASSESSMENT AND COLLECTION.—Section 6501 (relating to limitations on assessment and collection) is amended by redesignating subsection (j) as

subsection (k), and inserting after subsection (i) the following new subsection:

“(j) *INVESTMENT CREDIT CARRYBACKS.*—In the case of a deficiency attributable to the application to the taxpayer of an investment credit carryback, such deficiency may be assessed at any time before the expiration of the period within which a deficiency for the taxable year of the unused investment credit which results in such carryback may be assessed.”

(2) *CREDIT OR REFUND.*—Subsection (d) of section 6511 (relating to limitations on credit or refund) is amended by adding after paragraph (3) thereof the following new paragraph:

“(4) *SPECIAL PERIOD OF LIMITATION WITH RESPECT TO INVESTMENT CREDIT CARRYBACKS.*—

“(A) *PERIOD OF LIMITATION.*—If the claim for credit or refund relates to an overpayment attributable to an investment credit carryback, in lieu of the 3-year period of limitation prescribed in subsection (a), the period shall be that period which ends with the expiration of the 15th day of the 40th month (or 39th month, in the case of a corporation) following the end of the taxable year of the unused investment credit which results in such

1 *carryback, or the period prescribed in subsection (c)*
2 *in respect of such taxable year, whichever expires*
3 *later. In the case of such a claim, the amount of*
4 *the credit or refund may exceed the portion of the*
5 *tax paid within the period provided in subsection*
6 *(b)(2) or (c), whichever is applicable, to the*
7 *extent of the amount of the overpayment attribut-*
8 *able to such carryback.*

9 “(B) *APPLICABLE RULES.*—If the allowance
10 *of a credit or refund of an overpayment of tax*
11 *attributable to an investment credit carryback is*
12 *otherwise prevented by the operation of any law*
13 *or rule of law other than section 7122, relating to*
14 *compromises, such credit or refund may be allowed*
15 *or made, if claim therefor is filed within the period*
16 *provided in subparagraph (A) of this paragraph.*
17 *In the case of any such claim for credit or refund,*
18 *the determination by any court, including the Tax*
19 *Court, in any proceeding in which the decision of*
20 *the court has become final, shall not be conclusive*
21 *with respect to the investment credit, and the effect*
22 *of such credit, to the extent that such credit is*
23 *affected by a carryback which was not in issue in*
24 *such proceeding.”*

25 (3) *INTEREST ON UNDERPAYMENTS.*—Section

1 6601(e) (relating to interest on underpayment, nonpay-
2 ment, or extensions of time for payment, of tax) is
3 amended to read as follows:

4 “(e) *INCOME TAX REDUCED BY CARRYBACK.*—

5 “(1) *NET OPERATING LOSS CARRYBACK.*—If the
6 amount of any tax imposed by subtitle A is reduced by
7 reason of a carryback of a net operating loss, such reduc-
8 tion in tax shall not affect the computation of interest
9 under this section for the period ending with the last
10 day of the taxable year in which the net operating loss
11 arises.

12 “(2) *INVESTMENT CREDIT CARRYBACK.*—If the
13 credit allowed by section 38 for any taxable year is in-
14 creased by reason of an investment credit carryback, such
15 increase shall not affect the computation of interest under
16 this section for the period ending with the last day of
17 the taxable year in which the investment credit carry-
18 back arises.”

19 “(4) *INTEREST ON OVERPAYMENTS.*—Section 6611
20 (f) (relating to interest on overpayments) is amended to
21 read as follows:

22 “(f) *REFUND OF INCOME TAX CAUSED BY CARRY-*
23 *BACK.*—

24 “(1) *NET OPERATING LOSS CARRYBACK.*—For
25 purposes of subsection (a), if any overpayment of tax

1 imposed by subtitle A results from a carryback of a net
 2 operating loss, such overpayment shall be deemed not
 3 to have been made prior to the close of the taxable year
 4 in which such net operating loss arises.

5 “(2) *INVESTMENT CREDIT CARRYBACK.*—For pur-
 6 poses of subsection (a), if any overpayment of tax im-
 7 posed by subtitle A results from an investment credit
 8 carryback, such overpayment shall be deemed not to
 9 have been made prior to the close of the taxable year
 10 in which such investment credit carryback arises.”

11 **(24)(f) *TECHNICAL AMENDMENT.***—Section 1016(a) (re-
 12 lating to adjustments to basis) is amended—

13 (1) by striking out the period at the end of para-
 14 graph (18) and inserting in lieu thereof a semicolon; and

15 (2) by adding after paragraph (18) the following
 16 new paragraph:

17 “(19) to the extent provided in section 48(g) in
 18 the case of property which is or has been section 38
 19 property (as defined in section 48(a));”.

20 **(25)(d) *CLERICAL AMENDMENT.***—Part IV of subchapter
 21 A of chapter 1 is amended by inserting after the heading and
 22 before the table of sections the following:

(g) CLERICAL AMENDMENTS.—

(1) Part IV of subchapter A of chapter 1 is amended by inserting after the heading and before the table of sections the following:

“Subpart A. Credits allowable.

“Subpart B. Rules for computing credit for investment in certain depreciable property.

“Subpart A—Credits Allowable”

(26)(2) The table of sections for part IV of subchapter A of chapter 1 is amended by striking out

“Sec. 38. Overpayments of tax.”

and inserting in lieu thereof

“Sec. 38. Investment in certain depreciable property.

“Sec. 39. Overpayments of tax.”

(3) The table of sections for part VI of subchapter B of chapter 1 is amended by adding at the end thereof the following:

“Sec. 181. Deduction for certain unused investment credit.”

(27)(e) (h) EFFECTIVE DATE.—The amendments made by this section shall apply with respect to taxable years ending after (28)December 31, 1961 June 30, 1962.

1 **SEC. 3. APPEARANCES, ETC., WITH RESPECT TO LEGIS-**
2 **LATION.**

3 (a) **IN GENERAL.**—Section 162 (relating to trade or
4 business expenses) is amended by redesignating subsection
5 (e) as subsection (f) and by inserting after subsection (d)
6 the following new subsection:

7 “(e) **APPEARANCES, ETC., WITH RESPECT TO LEGIS-**
8 **LATION.**—

9 “(1) **IN GENERAL.**—The deduction allowed by
10 subsection (a) shall include all the ordinary and neces-
11 sary expenses (including, but not limited to, traveling
12 expenses described in subsection (a) (2) and the cost
13 of preparing testimony) paid or incurred during the tax-
14 able year in carrying on any trade or business—

15 “(A) in direct connection with appearances
16 before, submission of statements to, or sending com-
17 munications to, the committees, or individual mem-
18 bers, of Congress or of any legislative body of a
19 State, a possession of the United States, or a politi-
20 cal subdivision of any of the foregoing with respect
21 to legislation or proposed legislation of direct inter-
22 est to the taxpayer, or

23 “(B) in direct connection with communication

1 of information between the taxpayer and an organ-
2 ization of which he is a member with respect to
3 legislation or proposed legislation of direct interest
4 to the taxpayer and to such organization,
5 and that portion of the dues so paid or incurred with
6 respect to any organization of which the taxpayer is a
7 member which is attributable to the expenses of the
8 activities described in subparagraphs (A) and (B)
9 carried on by such organization.

10 “(2) LIMITATION.—The provisions of paragraph
11 (1) shall not be construed as allowing the deduction of
12 any amount paid or incurred (whether by way of con-
13 tribution, gift, or otherwise) —

14 “(A) for participation in, or intervention in,
15 any political campaign on behalf of any candidate
16 for public office, or

17 “(B) in connection with any attempt to in-
18 fluence the general public, or segments thereof, with
19 respect to legislative matters, elections, or referen-
20 dums.”

21 (b) EFFECTIVE DATE.—The amendments made by this
22 section shall apply to taxable years beginning after Decem-
23 ber 31, 1962.

1 **SEC. 4. DISALLOWANCE OF CERTAIN ENTERTAINMENT,**
2 **ETC., EXPENSES.**

3 (a) **DENIAL OF DEDUCTION.—**

4 (1) Part IX of subchapter B of chapter 1 (relating
5 to items not deductible in computing taxable income) is
6 amended by adding at the end thereof the following new
7 section:

8 **“SEC. 274. DISALLOWANCE OF CERTAIN ENTERTAINMENT,**
9 **ETC., EXPENSES.**

10 “(a) **ENTERTAINMENT, AMUSEMENT, OR RECREA-**
11 **TION.—**

12 “(1) **IN GENERAL.**—No deduction otherwise allow-
13 able under this chapter shall be allowed for any item—

14 “(A) **ACTIVITY.**—With respect to an activity
15 which is of a type generally considered to consti-
16 tute entertainment, amusement, or recreation, unless
17 the taxpayer establishes that the item was directly
18 related to ~~(29)~~ *or associated with* the active conduct
19 of the taxpayer’s trade or business, or

20 “(B) **FACILITY.**—With respect to a facility
21 used in connection with an activity referred to in
22 subparagraph (A), unless the taxpayer establishes
23 that the facility was used primarily for the further-
24 ance of the taxpayer’s trade or business and that the

1 item was directly related to ~~(30)~~*or associated with*
 2 the active conduct of such trade or business,
 3 and such deduction shall in no event exceed the portion
 4 of such item directly related to ~~(31)~~*or associated with*
 5 the active conduct of the taxpayer's trade or business.

6 “(2) SPECIAL RULES.—For purposes of applying
 7 paragraph (1)—

8 “(A) Dues or fees to any social, athletic, or
 9 sporting club or organization shall be treated as
 10 items with respect to facilities.

11 “(B) An activity described in section 212
 12 shall be treated as a trade or business.

13 “(b) GIFTS.—

14 “(1) LIMITATION.—No deduction shall be allowed
 15 under section 162 or section 212 for any expense for
 16 gifts made directly or indirectly to any individual to the
 17 extent that such expense, when added to prior expenses
 18 of the taxpayer for gifts made to such individual during
 19 the same taxable year, exceeds \$25. For purposes of
 20 this section, the term ‘gift’ means any item excludable
 21 from gross income of the recipient under section 102
 22 which is not excludable from his gross income under any
 23 other provision of this ~~(32)chapter.~~ *chapter, but such*
 24 *term does not include—*

1 “(A) an item having a cost to the taxpayer not
2 in excess of \$4.00 on which the name of the taxpayer
3 is clearly and permanently imprinted and which is
4 one of a number of identical items distributed gen-
5 erally by the taxpayer,

6 “(B) a sign, display rack, or other promotional
7 material to be used on the business premises of the
8 recipient, or

9 “(C) an item of tangible personal property
10 having a cost to the taxpayer not in excess of \$100
11 which is awarded to an employee by reason of length
12 of service or for safety achievement.

13 “(2) SPECIAL RULES.—

14 “(A) In the case of a gift by a partnership, the
15 limitation contained in paragraph (1) shall apply
16 to the partnership as well as to each member
17 thereof.

18 “(B) For purposes of paragraph (1), a hus-
19 band and wife shall be treated as one taxpayer.

20 **(33)**“(C) TRAVELING.—In the case of any individual who
21 is traveling away from home in pursuit of a trade or business
22 or in pursuit of an activity described in section 212, no deduc-
23 tion shall be allowed under section 162 or section 212 for
24 that portion of the expenses of such travel otherwise allow-
25 able under such section which, under regulations prescribed

1 *by the Secretary or his delegate, is not allocable to such trade*
 2 *or business or to such activity. This subsection shall not*
 3 *apply to the expenses of any travel away from home which*
 4 *does not exceed one week or where the portion of the time*
 5 *away from home which is not attributable to the pursuit of*
 6 *the taxpayer's trade or business or an activity described in*
 7 *section 212 is less than 25 percent of the total time away*
 8 *from home on such travel.*

9 **(34)**~~“(e)~~ **“(d) SUBSTANTIATION REQUIRED.—**No deduc-
 10 tion shall be allowed—

11 **“(1)** under section 162 or 212 for any traveling
 12 expense (including meals and lodging while away from
 13 home),

14 **“(2)** for any item with respect to an activity which
 15 is of a type generally considered to constitute entertain-
 16 ment, amusement, or recreation, or with respect to a
 17 facility used in connection with such an activity, or

18 **“(3)** for any expense for gifts,
 19 unless the taxpayer substantiates by adequate records or by
 20 sufficient evidence corroborating his own statement (A) the
 21 amount of such expense or other item, (B) the time and
 22 place of the travel, entertainment, amusement, recreation, or
 23 use of the facility, or the date and description of the gift, (C)
 24 the business purpose of the expense or other item, and (D)
 25 the business relationship to the taxpayer of persons enter-

1 tained, using the facility, or receiving the gift. The Secre-
 2 tary or his delegate may by regulations provide that some
 3 or all of the requirements of the preceding sentence shall not
 4 apply in the case of an expense which does not exceed an
 5 amount prescribed pursuant to such regulations.

6 **(35)**~~“(d)~~ *“(e)* SPECIFIC EXCEPTIONS TO APPLICATION OF
 7 SUBSECTION (a).—Subsection (a) shall not apply to—

8 **“(1) BUSINESS MEALS.**—Expenses for food and
 9 beverages furnished to any individual under circum-
 10 stances which (taking into account the surroundings in
 11 which furnished, the taxpayer’s trade, business, or in-
 12 come-producing activity and the relationship to such
 13 trade, business, or activity of the persons to whom the
 14 food and beverages are furnished) are of a type gen-
 15 erally considered to be conducive to a business dis-
 16 cussion.

17 **“(2) FOOD AND BEVERAGES FOR EMPLOYEES.**—
 18 Expenses for food and beverages (and facilities used
 19 in connection therewith) furnished on the business
 20 premises of the taxpayer primarily for his employees.

21 **“(3) EXPENSES TREATED AS COMPENSATION.**—
 22 Expenses for goods, services, and facilities, to the ex-
 23 tent that the expenses are treated by the taxpayer, with
 24 respect to the recipient of the entertainment, amusement,
 25 or recreation, as compensation to an employee on the

1 taxpayer's return of tax under this chapter and as wages
2 to such employee for purposes of chapter 24 (relating
3 to withholding of income tax at source on wages).

4 “(4) REIMBURSED EXPENSES.—Expenses paid or
5 incurred by the taxpayer, in connection with the per-
6 formance by him of services for another person
7 (whether or not such other person is his employer),
8 under a reimbursement or other expense allowance
9 arrangement with such other person, but this para-
10 graph shall apply—

11 “(A) where the services are performed for
12 an employer, only if the employer has not treated
13 such expenses in the manner provided in paragraph
14 (3), or

15 “(B) where the services are performed for a
16 person other than an employer, only if the tax-
17 payer accounts (to the extent provided by sub-
18 section ~~(36)(e)~~ (d)) to such person.

19 “(5) RECREATIONAL, ETC., EXPENSES FOR EM-
20 PLOYEES.—Expenses for recreational, social, or similar
21 activities (including facilities therefor) primarily for
22 the benefit of employees (other than employees who
23 are officers, shareholders or other owners, or highly
24 compensated employees). For purposes of this para-
25 graph, an individual owning less than a 10-percent in-

1 terest in the taxpayer's trade or business shall not be
 2 considered a shareholder or other owner, and for such
 3 purposes an individual shall be treated as owning any
 4 interest owned by a member of his family (within the
 5 meaning of section 267 (c) (4)).

6 **(37)“(6) EMPLOYEE AND STOCKHOLDER BUSINESS**
 7 **MEETINGS.—**Expenses directly related to business meet-
 8 ings of employees or stockholders.

9 “(6) *EMPLOYEE, STOCKHOLDER, ETC., BUSINESS*
 10 *MEETINGS.—*Expenses incurred by a taxpayer which are
 11 *directly related to business meetings of his employees,*
 12 *stockholders, agents, or directors.*

13 “(7) **MEETINGS OF BUSINESS LEAGUES, ETC.—**
 14 Expenses directly related and necessary to attendance at
 15 a business meeting or convention of any organization
 16 described in section 501 (c) (6) (relating to business
 17 leagues, chambers of commerce, real estate boards, and
 18 boards of trade) and exempt from taxation under section
 19 501 (a) .

20 “(8) **ITEMS AVAILABLE TO PUBLIC.—**Expenses
 21 for goods, services, and facilities made available by the
 22 taxpayer to the general public.

23 “(9) **ENTERTAINMENT SOLD TO CUSTOMERS.—**
 24 Expenses for goods or services (including the use
 25 of facilities) which are sold by the taxpayer in a bona

1 fide transaction for an adequate and full consideration in
2 money or money's worth.

3 For purposes of this subsection, any item referred to in sub-
4 section (a) shall be treated as an expense.

5 **(38)**~~“(e) “(f)~~ INTEREST, TAXES, CASUALTY LOSSES.
6 ETC.—This section shall not apply to any deduction allowable
7 to the taxpayer without regard to its connection with his trade
8 or business (or with his income-producing activity). In the
9 case of a taxpayer which is not an individual, the preceding
10 sentence shall be applied as if it were an individual.

11 **(39)**~~“(f) “(g)~~ TREATMENT OF ENTERTAINMENT, ETC.,
12 TYPE FACILITY.—For purposes of this chapter, if deductions
13 are disallowed under subsection (a) with respect to any por-
14 tion of a facility, such portion shall be treated as an asset
15 which is used for personal, living, and family purposes (and
16 not as an asset used in the trade or business).

17 **(40)**~~“(g) “(h)~~ REGULATORY AUTHORITY.—The Secretary
18 or his delegate shall prescribe such regulations as he may
19 deem necessary to carry out the purposes of this section in-
20 cluding regulations prescribing whether subsection (a) or
21 subsection (b) applies in cases where both such subsections
22 would otherwise apply.”

1 (2) The table of sections for such part IX is
2 amended by adding at the end thereof the following:

“Sec. 274. Disallowance of certain entertainment, etc., ex-
penses.”

3 (b) TRAVELING EXPENSES.—Section 162 (a) (2) (re-
4 lating to traveling expenses) is amended by striking out
5 “(including the entire amount expended for meals and lodg-
6 ing)” and inserting in lieu thereof “(including (41)^a rea-
7 sonable allowance for amounts expended for meals and lodg-
8 ing)”. *amounts expended for meals and lodging other than*
9 *amounts which are lavish or extravagant under the*
10 *circumstances)”*.

11 (c) EFFECTIVE DATE.—The amendments made by this
12 section shall apply with respect to taxable years ending after
13 (42)~~June 30, 1962~~ *December 31, 1962*, but only in respect
14 of periods after such date.

15 SEC. 5. AMOUNT OF DISTRIBUTION WHERE CERTAIN
16 FOREIGN CORPORATIONS DISTRIBUTE PROP-
17 ERTY IN KIND.

18 (a) AMOUNT DISTRIBUTED.—Section 301 (b) (1)
19 (relating to amount distributed to corporate distributees) is
20 amended by adding at the end thereof the following new
21 subparagraph:

22 “(C) CERTAIN CORPORATE DISTRIBUTEES OF
23 FOREIGN CORPORATION.—Notwithstanding subpara-

graph (B), if the shareholder is a corporation and the distributing corporation is a foreign corporation, the amount taken into account with respect to property (other than money) shall be the fair market value of such property; except that if any deduction is allowable under section 245 with respect to such distribution, then the amount taken into account shall be the sum (determined under regulations prescribed by the Secretary or his delegate) of—

“(i) the proportion of the adjusted basis of such property (or, if lower, its fair market value) properly attributable to gross income from sources within the United States, and

“(ii) the proportion of the fair market value of such property properly attributable to gross income from sources without the United States.”

(b) BASIS.—Section 301 (d) (relating to basis of property) is amended by adding at the end thereof the following new paragraph:

“(3) CERTAIN CORPORATE DISTRIBUTEES OF FOREIGN CORPORATION.—In the case of property described in subparagraph (C) of subsection (b) (1), the basis shall be determined by substituting the amount deter-

1 mined under such subparagraph (C) for the amount
2 described in paragraph (2) of this subsection.”

3 (c) DIVIDENDS RECEIVED FROM CERTAIN FOREIGN
4 CORPORATIONS.—

5 (1) Section 245 (relating to dividends received
6 from certain foreign corporations) is amended by add-
7 ing at the end thereof the following new subsection:

8 “(b) PROPERTY DISTRIBUTIONS.—For purposes of sub-
9 section (a), the amount of any distribution of property other
10 than money shall be the amount determined by applying
11 section 301(b)(1)(B).”

12 (2) Section 245 is amended by striking out “In
13 the case of” and inserting in lieu thereof “(a) GENERAL
14 RULE.—In the case of”.

15 (43)(d) CREDIT FOR FOREIGN TAXES.—Section 902(a)-
16 ~~(relating to credit for foreign taxes)~~ is amended by adding
17 at the end thereof the following new sentence: “For pur-
18 poses of this subsection and subsection (b), the amount of
19 any distribution in property other than money shall be the
20 amount determined by applying section 301(b)(1)(B).”

21 (44)(e) (d) EFFECTIVE DATE.—The amendments made by
22 this section shall apply to distributions made after Decem-
23 ber 31, 1962.

24 (45)SEC. 6. AMENDMENT TO SECTION 482.

25 (a) IN GENERAL.—Section 482 ~~(relating to allocation~~

1 of income and deductions among taxpayers) is amended
 2 by adding at the end thereof the following new subsection:

3 “(b) SALES AND PURCHASES WITHIN A RELATED
 4 GROUP WHICH INCLUDES A FOREIGN ORGANIZATION.—

5 “(1) IN GENERAL.—In applying subsection (a)
 6 to sales of tangible property within a group of organiza-
 7 tions—

8 “(A) owned or controlled directly or indi-
 9 rectly by the same interests; and

10 “(B) at least one of which is a domestic or-
 11 ganization and at least one of which is a foreign
 12 organization;

13 the Secretary or his delegate may allocate the taxable
 14 income of the group arising from such sales in the
 15 manner set forth in paragraph (2). This subsection
 16 shall not apply with respect to any sale of tangible
 17 property for which the taxpayer can establish an arm's
 18 length price (within the meaning of paragraph (4)).

19 “(2) METHODS OF ALLOCATION.—

20 “(A) CONSIDERATION OF CERTAIN FAC-
 21 TORS.—Except as provided in subparagraph (B),
 22 the allocation referred to in paragraph (1) shall be
 23 made by the Secretary or his delegate by taking into
 24 consideration that portion of the following factors
 25 which is attributable to the United States and that

1 portion thereof which is not attributable to the
2 United States—

3 “(i) assets of the group, to the extent used
4 in the production, distribution, and sale of the
5 property;

6 “(ii) compensation of officers and em-
7 ployees, to the extent attributable to the pro-
8 duction, distribution, and sale of the property,
9 and

10 “(iii) advertising, selling, and sales promo-
11 tion expenses (including technical and servie-
12 ing expenses), to the extent attributable to the
13 property.

14 Such method of allocation may also give considera-
15 tion to other factors, including the special risks (if
16 any) of the market in which the property is sold.

17 “(B) ALTERNATIVE METHODS.—If the tax-
18 payer establishes to the satisfaction of the Secretary
19 or his delegate that an alternative method of alloca-
20 tion clearly reflects the income of each member of
21 the group with respect to the property referred to in
22 paragraph (1), such alternative method shall be
23 used (in lieu of the method provided in subpara-
24 graph (A)).

25 “(3) SPECIAL RULES.—In applying the method

of allocation referred to in paragraph ~~(2)(A)~~, the following rules shall be applied:

~~“(A) ADJUSTED BASIS OF ASSETS.—~~The values to be assigned to the assets referred to in paragraph ~~(2)(A)(i)~~ is their adjusted basis in the hands of the taxpayer or, if such basis is not available in the case of a foreign organization, then their book values, adjusted to approximate their adjusted basis.

~~“(B) INCLUDIBLE ASSETS.—~~The assets referred to in paragraph ~~(2)(A)(i)~~ include real property and tangible personal property (whether owned or leased by a member of the group), but do not include inventory and stock in trade.

~~“(4) ARM’S LENGTH PRICE DEFINED.—~~For purposes of this subsection, the term ‘arm’s length price’ means—

~~“(A) the price at which tangible property similar or comparable to the property referred to in paragraph (1) generally is or can be sold in transactions in the same areas involving unrelated persons and made under similar conditions of sale; and~~

~~“(B) if subparagraph (A) does not apply, the price at which tangible property similar or comparable to the property referred to in paragraph~~

1 ~~(1)~~ is sold in the same or other areas under similar
2 circumstances and in transactions involving unre-
3 lated persons, with adjustment for material differ-
4 ences in quantity, marketing conditions (including
5 customs duties and transportation costs); and other
6 relevant factors.

7 Subparagraph ~~(B)~~ shall apply only if the adjustment
8 referred to therein is properly determinable.

9 “~~(5)~~ SALES COMMISSIONS.—The Secretary or his
10 delegate shall by regulation prescribe rules for the allo-
11 cation of commissions arising from sales of tangible
12 property within a group of organizations described in
13 paragraph ~~(1)~~. Such rules shall be consistent with the
14 principles specified in the other paragraphs of this
15 subsection.

16 “~~(6)~~ GROSSLY INADEQUATE ASSETS, ETC., OUT-
17 SIDE UNITED STATES.—In allocating taxable income
18 under this subsection, no amount shall be allocated to a
19 foreign organization whose assets, personnel, and office
20 and other facilities which are not attributable to the
21 United States are grossly inadequate for its activities
22 outside the United States.

23 “~~(7)~~ INFORMATION NECESSARY FOR CONSIDERA-
24 TION OF FACTORS.—In the case of any transaction to
25 which paragraph ~~(2)~~ ~~(A)~~ applies, if—

1 “(A) the information submitted with respect
2 to the group of organizations is insufficient for the
3 proper application of the method of allocation set
4 forth in the first sentence of such paragraph; and

5 “(B) upon request of the Secretary or his
6 delegate, such group fails to furnish such additional
7 information with respect to such transaction as may
8 be reasonably supplied;

9 the Secretary or his delegate may estimate the taxable
10 income arising from such transaction and may allocate
11 such taxable income among the members of the group
12 or to any single member thereof.

13 “(8) TREATMENT OF FOREIGN TAXES.—

14 “(A) For purposes of this subsection, taxable
15 income shall be determined without regard to any
16 income, war profits, or excess profits taxes paid to
17 any foreign country or to any possession of the
18 United States.

19 “(B) Where the application of this subsection
20 results in a decrease in the taxable income of any
21 foreign organization and an increase in the taxable
22 income of any domestic organization, then any of
23 the taxes referred to in subparagraph (A) paid by
24 such foreign organization and attributable to the

1 taxable income so transferred shall be treated for
2 purposes of this chapter—

3 “(i) as paid by such domestic organiza-
4 tion, and

5 “(ii) as not paid by such foreign organi-
6 zation.”

7 ~~(b)~~ CLERICAL AMENDMENT.—Section 482 is amended
8 by striking out “In any case of two or more organizations”
9 and inserting in lieu thereof the following:

10 ~~“(a)~~ GENERAL RULE.—In the case of two or more
11 organizations”.

12 ~~(c)~~ EFFECTIVE DATE.—The amendments made by
13 this section shall apply with respect to taxable years begin-
14 ning after December 31, 1962.

15 **(46)SEC. 7. DISTRIBUTIONS OF FOREIGN PERSONAL**
16 **HOLDING COMPANY INCOME.**

17 ~~(a)~~ DEFINITION OF FOREIGN PERSONAL HOLDING
18 COMPANY.—So much of subsection ~~(a)~~ of section 552 ~~(re-~~
19 ~~lating to definition of foreign personal holding company)~~ as
20 precedes paragraph ~~(2)~~ is amended to read as follows:

21 ~~“(a)~~ GENERAL RULE.—For purposes of this subtitle,
22 the term ‘foreign personal holding company’ for a taxable
23 year beginning after December 31, 1962, means any for-
24 eign corporation if—

25 ~~“(1)~~ GROSS INCOME REQUIREMENT.—At least 20

percent of its gross income (as defined in section 555 (a)) for the taxable year is foreign personal holding company income (as defined in section 553). For purposes of this paragraph, there shall be included in the gross income the amount includible therein as a dividend by reason of the application of section 555(c) (2); and”.

(b) AMOUNT OF UNDISTRIBUTED INCOME.—Subsection (a) of section 556 (relating to undistributed foreign personal holding company income) is amended to read as follows:

“(a) DEFINITION.—For purposes of this part—

“(1) If the foreign personal holding company income of a foreign personal holding company exceeds 80 percent of its gross income, the ‘undistributed foreign personal holding company income’ of such company is its taxable income adjusted in the manner provided in subsection (b), minus the dividends paid deduction (as defined in section 561).

“(2) If the foreign personal holding company income of a foreign personal holding company does not exceed 80 percent of its gross income, the ‘undistributed foreign personal holding company income’ of such company is that amount which bears the same ratio to—

“(A) its taxable income adjusted in the man-

1 her provided in subsection (b), minus the dividends
 2 paid deduction (as defined in section 561), as
 3 “(B) its foreign personal holding company in-
 4 come bears to its gross income.”

5 ~~(e)~~ **EFFECTIVE DATE.**—The amendments made by this
 6 section shall apply only in respect of taxable years of foreign
 7 corporations beginning after December 31, 1962.

8 **SEC. (47)8 6. MUTUAL SAVINGS BANKS, ETC.**

9 (a) **RESERVES FOR LOSSES ON LOANS.**—Section 593
 10 is amended to read as follows:

11 **“SEC. 593. RESERVES FOR LOSSES ON LOANS.**

12 “(a) **ORGANIZATIONS TO WHICH SECTION APPLIES.**—
 13 This section shall apply to any mutual savings bank not
 14 having capital stock represented by shares, domestic building
 15 and loan association, or cooperative bank without capital
 16 stock organized and operated for mutual purposes and with-
 17 out profit.

18 “(b) **ADDITION TO RESERVES FOR BAD DEBTS.**—

19 “(1) **IN GENERAL.**—For purposes of section 166
 20 (c), the reasonable addition for the taxable year to the
 21 reserve for bad debts of any taxpayer described in sub-
 22 section (a) shall be an amount equal to the sum of—

23 “(A) the amount determined under section
 24 166(c) to be a reasonable addition to the reserve
 25 for losses on nonqualifying loans, plus

“(B) the amount determined by the taxpayer to be a reasonable addition to the reserve for losses on qualifying real property loans, but such amount shall not exceed the amount determined under paragraph (2), (3), or (4), whichever amount is the largest~~(48)~~, but the amount determined under this subparagraph, when added to the amount determined under subparagraph (A), shall in no case be greater than the amount by which 12 percent of the total deposits or withdrawable accounts of depositors of the taxpayer at the close of such year exceeds the sum of its surplus, undivided profits, and reserves at the beginning of such year (taking into account any portion thereof attributable to the period before the first taxable year beginning after December 31, 1951).

“(2) ~~(49)~~~~60 PERCENT~~ PERCENTAGE OF TAXABLE INCOME METHOD.—The amount determined under this paragraph for the taxable year shall be the excess of—

~~(50)~~“(A) an amount equal to 60 percent of the taxable income for such year, over

“(A) an amount—

“(i) in the case of a taxpayer other than a taxpayer described in clause (ii), equal to

1 60 percent of the taxable income for such year,
2 or

3 “(ii) in the case of a domestic building and
4 loan association having capital stock with respect
5 to which any distribution of property (as de-
6 fined in section 317(a)) is not allowable as a
7 deduction under section 591, equal to 50 percent
8 of the taxable income for such year, over

9 “(B) the amount referred to in paragraph
10 (1) (A) for such ~~(51)~~year, year,
11 ~~(52)~~but the amount determined under this paragraph
12 shall not exceed the amount necessary to increase the bal-
13 ance (as of the close of the taxable year) of the reserve for
14 losses on qualifying real property loans to 6 percent of
15 such loans outstanding at such time. For purposes of this
16 paragraph, taxable income shall be computed (i) by
17 excluding from gross income any amount included
18 therein by reason of subsection (f), and (ii) without
19 regard to any deduction allowable for any addition to the
20 reserve for bad debts.

21 “(3) ~~(53)~~3 PERCENT PERCENTAGE OF REAL
22 PROPERTY LOANS METHOD.—The amount determined
23 under this paragraph for the taxable year shall be an
24 amount equal to the amount necessary to increase the
25 balance (as of the close of the taxable year) of the

reserve for losses on qualifying real property loans
 (54) to 3 percent of such loans outstanding at such time.
 to an amount equal to—

“(A) 3 percent of such loans outstanding at
 such time, plus

“(B) in the case of a taxpayer which is a new
 company and which does not have capital stock with
 respect to which distributions of property (as defined
 in section 317(a)) are not allowable as a deduction
 under section 591, an amount equal to—

“(i) 2 percent of so much of the amount of
 such loans outstanding at such time as does not
 exceed \$4,000,000, reduced (but not below
 zero) by

“(ii) the amount, if any, of the balance (as
 of the close of such taxable year) of the tax-
 payer’s supplemental reserve for losses on loans.

For purposes of subparagraph (B), a taxpayer is a
 new company for any taxable year only if such taxable
 year begins not more than 10 years after the first day
 on which it (or any predecessor) was authorized to do
 business as an organization described in subsection (a).

“(4) EXPERIENCE METHOD.—The amount deter-
 mined under this paragraph for the taxable year shall
 be an amount equal to the amount determined under

1 section 166(c) (without regard to this subsection) to
2 be a reasonable addition to the reserve for losses on
3 qualifying real property loans.

4 “(c) TREATMENT OF RESERVES FOR BAD DEBTS.—

5 “(1) ESTABLISHMENT OF RESERVES.—Each tax-
6 payer described in subsection (a) which uses the reserve
7 method of accounting for bad debts shall establish and
8 maintain a reserve for losses on qualifying real property
9 loans, a reserve for losses on nonqualifying loans, and a
10 supplemental reserve for losses on loans. For purposes
11 of this title, such reserves shall be treated as reserves
12 for bad debts, but no deduction shall be allowed for any
13 addition to the supplemental reserve for losses on loans.

14 “(2) ALLOCATION OF PRE-1963 RESERVES.—For
15 purposes of this section, the pre-1963 reserves shall, as
16 of the close of December 31, 1962, be allocated to, and
17 constitute the opening balance of—

18 “(A) the reserve for losses on nonqualifying
19 loans,

20 “(B) the reserve for losses on qualifying real
21 property loans, and

22 “(C) the supplemental reserve for losses on
23 loans.

24 “(3) METHOD OF ALLOCATION.—The allocation
25 provided by paragraph (2) shall be made—

1 “(A) first, to the reserve described in para-
 2 graph (2) (A), to the extent such reserve is not
 3 increased above the amount which would be a
 4 reasonable addition under section 166(c) for a
 5 period in which the nonqualifying loans increased
 6 from zero to the amount thereof outstanding at the
 7 close of December 31, 1962;

8 “(B) second, to the reserve described in para-
 9 graph (2) (B), to the extent such reserve is not
 10 increased above the amount which would be deter-
 11 mined under paragraph ~~(55)(3)~~ (3) (A) or (4) of
 12 subsection (b) (whichever such amount is the
 13 larger) for a period in which the qualifying real
 14 property loans increased from zero to the amount
 15 thereof outstanding at the close of December 31,
 16 1962; and

17 “(C) then to the supplemental reserve for
 18 losses on loans.

19 “(4) PRE-1963 RESERVES DEFINED.—For purposes
 20 of this subsection, the term ‘pre-1963 reserves’ means
 21 the net amount, determined as of the close of December
 22 31, 1962 (after applying subsection (d) (1)), accumu-
 23 lated in the reserve for bad debts pursuant to section
 24 166(c) (or the corresponding provisions of prior reve-

1 nue laws) for taxable years beginning after December
2 31, 1951.

3 **(56)**“(5) *CERTAIN PRE-1952 SURPLUS.*—If after the
4 application of paragraph (3), the opening balance of the
5 reserve described in paragraph (2)(B) is less than the
6 amount described in paragraph (3)(B), then, for pur-
7 poses of this subsection, the term ‘pre-1963 reserves’ in-
8 cludes so much of the surplus, undivided profits, and bad
9 debt reserves (determined as of December 31, 1962)
10 attributable to the period before the first taxable year
11 beginning after December 31, 1951, as does not exceed
12 the amount by which such opening balance is less than
13 the amount described in paragraph (3)(B). For pur-
14 poses of the preceding sentence, the surplus, undivided
15 profits, and bad debt reserves attributable to the period
16 before the first taxable year beginning after December 31,
17 1951, shall be reduced by the amount thereof which is
18 attributable to interest which would have been excludable
19 from gross income under section 22(b)(4) of the Inter-
20 nal Revenue Code of 1939 (relating to interest on gov-
21 ernmental obligations) or the corresponding provisions of
22 prior laws. Notwithstanding the second sentence of
23 paragraph (1), any amount which, by reason of the ap-
24 plication of the first sentence of this paragraph, is allocated
25 to the reserve described in paragraph (2)(B) shall not

be treated as a reserve for bad debts for any purpose other than determining the amount referred to in subsection (b)(1)(B), and for such purpose such amount shall be treated as remaining in such reserve.

(57)~~“(5) “(6)~~ CHARGING OF BAD DEBTS TO RESERVES.—Any debt becoming worthless or partially worthless in respect of a qualifying real property loan shall be charged to the reserve for losses on such loans, and any debt becoming worthless or partially worthless in respect of a nonqualifying loan shall be charged to the reserve for losses on nonqualifying loans; except that any such debt may, at the election of the taxpayer, be charged in whole or in part to the supplemental reserve for losses on loans.

“(d) TAXABLE YEARS BEGINNING IN 1962 AND ENDING IN 1963.—In the case of a taxable year beginning before January 1, 1963, and ending after December 31, 1962, of a taxpayer described in subsection (a) which uses the reserve method of accounting for bad debts, the taxable income shall be the sum of—

“(1) that portion of the taxable income allocable to the part of the taxable year occurring before January 1, 1963, reduced by the amount of the deduction for an addition to a reserve for bad debts which would be allowable under section 166(c) (without regard to the

1 amendments made by section (58)8 6 of the Revenue
 2 Act of 1962) if such part year constituted a taxable
 3 year, plus

4 “(2) that portion of the taxable income allocable
 5 to the part of the taxable year occurring after December
 6 31, 1962, reduced by the amount of the deduction for
 7 an addition to a reserve for bad debts which would be
 8 allowed under section 166 (c) (taking into account the
 9 amendments made by section (59)8 6 of the Revenue
 10 Act of 1962) if such part year constituted a taxable
 11 year.

12 For purposes of the preceding sentence, the taxable income
 13 shall be determined without regard to any deduction under
 14 section 166 (c), and the portion thereof allocable to each
 15 part year shall be determined on the basis of the ratio which
 16 the number of days in such part year bears to the number
 17 of days in the entire taxable year.

18 “(e) LOANS DEFINED.—For purposes of this section—

19 “(1) QUALIFYING REAL PROPERTY LOANS.—The
 20 term ‘qualifying real property loan’ means any loan se-
 21 cured by an interest in improved real property or secured
 22 by an interest in real property which is to be improved
 23 out of the proceeds of the loan, but such term does not
 24 include—

1 “(A) any loan evidenced by a security (as de-
2 fined in section 165 (g) (2) (C)) ;

3 “(B) any loan, whether or not evidenced by a
4 security (as defined in section 165 (g) (2) (C)),
5 the primary obligor on which is—

6 “(i) a government or political subdivision
7 or instrumentality thereof;

8 “(ii) a bank (as defined in section 581) ;
9 or

10 “(iii) another member of the same affil-
11 iated group;

12 “(C) any loan, to the extent secured by a
13 deposit in or share of the taxpayer; or

14 “(D) any loan which, within a 60-day period
15 beginning in one taxable year of the creditor and
16 ending in its next taxable year, is made or acquired
17 and then repaid or disposed of, unless the trans-
18 actions by which such loan was made or acquired
19 and then repaid or disposed of are established to be
20 for bona fide business purposes.

21 For purposes of subparagraph (B) (iii), the term
22 ‘affiliated group’ has the meaning assigned to such term
23 by section 1504 (a) ; except that (i) the phrase ‘more
24 than 50 percent’ shall be substituted for the phrase ‘at

1 least 80 percent' each place it appears in section 1504
 2 (a), and (ii) all corporations shall be treated as
 3 includible corporations (without any exclusion under
 4 section 1504 (b)).

5 “(2) NONQUALIFYING LOANS.—The term ‘non-
 6 qualifying loan’ means any loan which is not a quali-
 7 fying real property loan.

8 “(3) LOAN.—The term ‘loan’ means debt, as the
 9 term ‘debt’ is used in section 166.

10 “(f) DISTRIBUTIONS TO SHAREHOLDERS.—

11 “(1) IN GENERAL.—For purposes of this chapter,
 12 any disribution of property (as defined in section 317
 13 (a)) by a domestic building and loan association to a
 14 shareholder with respect to its stock, if such distribution
 15 is not allowable as a deduction under section 591, shall
 16 be treated as made—

17 “(A) first out of its earnings and profits accu-
 18 mulated in taxable years beginning after December
 19 31, 1951, to the extent thereof,

20 “(B) then out of the reserve for losses on quali-
 21 fying real property loans, to the extent additions
 22 to such reserve exceed the additions which would
 23 have been allowed under subsection (b) (4),

24 “(C) then out of the supplemental reserve for
 25 losses on loans, to the extent thereof,

1 “(D) then out of such other accounts as may
2 be proper.

3 This paragraph shall apply in the case of any distribu-
4 tion in redemption of stock or in partial or complete
5 liquidation of the association, except that any such distri-
6 bution shall be treated as made first out of the amount
7 referred to in subparagraph (B), second out of the
8 amount referred to in subparagraph (C), third out of
9 the amount referred to in subparagraph (A), and then
10 out of such other accounts as may be proper.

11 “(2) AMOUNTS CHARGED TO RESERVE ACCOUNTS
12 AND INCLUDED IN GROSS INCOME.—If any distribution
13 is treated under paragraph (1) as having been made
14 out of the reserves described in subparagraphs (B) and
15 (C) of such paragraph, the amount charged against
16 such reserve shall be the amount which, when reduced
17 by the amount of tax imposed under this chapter and
18 attributable to the inclusion of such amount in gross
19 income, is equal to the amount of such distribution; and
20 the amount so charged against such reserve shall be
21 included in gross income of the taxpayer.

22 “(3) SPECIAL RULES.—

23 “(A) For purposes of paragraph (1) (B),
24 additions to the reserve for losses on qualifying real

1 property loans for the taxable year in which the
2 distribution occurs shall be taken into account.

3 “(B) For purposes of computing under this
4 section the amount of a reasonable addition to the
5 reserve for losses on qualifying real property loans
6 for any taxable year, any amount charged during
7 any year to such reserve pursuant to the provisions
8 of paragraph (2) shall not be taken into account.”

9 (b) FORECLOSURE ON PROPERTY SECURING LOANS.—
10 Part II of subchapter H of chapter 1 (relating to mutual
11 savings banks, etc.) is amended by adding at the end thereof
12 the following new section:

13 **“SEC. 595. FORECLOSURE ON PROPERTY SECURING LOANS.**

14 “(a) NONRECOGNITION OF GAIN OR LOSS AS A RESULT
15 OF FORECLOSURE.—In the case of a creditor which is an
16 organization described in section 593 (a), no gain or loss
17 shall be recognized, and no debt shall be considered as be-
18 coming worthless or partially worthless, as the result of such
19 organization having bid in at foreclosure, or having otherwise
20 reduced to ownership or possession by agreement or process
21 of law, any property which was security for the payment of
22 any indebtedness.

23 “(b) CHARACTER OF PROPERTY.—For purposes of
24 sections 166 and 1221, any property acquired in a trans-
25 action with respect to which gain or loss to an organization

1 was not recognized by reason of subsection (a) shall be
 2 considered as property having the same characteristics as
 3 the indebtedness for which such property was security. Any
 4 amount realized by such organization with respect to such
 5 property shall be treated for purposes of this chapter as a
 6 payment on account of such indebtedness, and any loss with
 7 respect thereto shall be treated as a bad debt to which the
 8 provisions of section 166 (relating to allowance of a deduc-
 9 tion for bad debts) apply.

10 “(c) BASIS.—The basis of any property to which sub-
 11 section (a) applies shall be the basis of the indebtedness for
 12 which such property was security (determined as of the date
 13 of the acquisition of such property) properly increased for
 14 costs of acquisition.

15 “(d) REGULATORY AUTHORITY.—The Secretary or his
 16 delegate shall prescribe such regulations as he may deem
 17 necessary to carry out the purposes of this section.”

18 (c) DEFINITION OF DOMESTIC BUILDING AND LOAN
 19 ASSOCIATION.—Paragraph (19) of section 7701 (a) (def-
 20 inition of domestic building and loan association) is amended
 21 to read as follows:

22 (60)“(19) DOMESTIC BUILDING AND LOAN ASSOCIA-
 23 TION.—The term ‘domestic building and loan associa-
 24 tion’ means a domestic building and loan association, a

1 domestic savings and loan association, and a Federal
 2 savings and loan association, which—

3 “(A) is an insured institution (within the
 4 meaning of section 401(a) of the National Housing
 5 Act (12 U.S.C., sec. 1724(a)), or

6 “(B) is subject by law to supervision and
 7 examination by State or Federal authority having
 8 supervision over such associations,

9 if substantially all of its business consists of accepting
 10 savings and investing the proceeds (i) in loans secured
 11 by an interest in real property which is (or, from the
 12 proceeds of the loan, will become) residential real
 13 property, and (ii) in other loans, to the extent such
 14 other loans would be authorized to be made by a Federal
 15 savings and loan association under section 5(e) of the
 16 Home Owners’ Loan Act, as amended (12 U.S.C., sec.
 17 1464(e)).”

18 “(19) DOMESTIC BUILDING AND LOAN ASSOCIA-
 19 TION.—The term ‘domestic building and loan association’
 20 means a domestic building and loan association, a domes-
 21 tic savings and loan association, and a Federal savings
 22 and loan association—

23 “(A) which either (i) is an insured institution
 24 (within the meaning of section 401(a) of the Na-
 25 tional Housing Act (12 U.S.C., sec. 1724(a)), or

(ii) is subject by law to supervision and examination by State or Federal authority having supervision over such associations;

“(B) substantially all of the business of which consists of acquiring the savings of the public and investing in loans described in subparagraph (C);

“(C) at least 90 percent of the amount of the total assets of which (as of the close of the taxable year) consists of (i) cash, (ii) obligations of the United States or of a State or political subdivision thereof, stock or obligations of a corporation which is an instrumentality of the United States or of a State or political subdivision thereof, and certificates of deposit in, or obligations of, a corporation organized under a State law which specifically authorizes such corporation to insure the deposits or share accounts of member associations, (iii) loans secured by an interest in real property and loans made for the improvement of real property, (iv) loans secured by a deposit or share of a member, (v) property acquired through the liquidation of defaulted loans described in clause (iii), and (vi) property used by the association in the conduct of the business described in subparagraph (B);

“(D) of the assets of which taken into account

1 *under subparagraph (C) as assets constituting the*
2 *90 percent of total assets—*

3 “(i) at least 80 percent of the amount of
4 such assets consists of assets described in clauses
5 (i) and (ii) of such subparagraph and of loans
6 secured by an interest in real property which is
7 (or, from the proceeds of the loan, will become)
8 residential real property or real property used
9 primarily for church purposes, loans made for
10 the improvement of residential real property or
11 real property used primarily for church pur-
12 poses, or property acquired through the liquida-
13 tion of defaulted loans described in this clause;
14 and

15 “(ii) at least 60 percent of the amount of
16 such assets consists of assets described in clauses
17 (i) and (ii) of such subparagraph and of
18 loans secured by an interest in real property
19 which is (or, from the proceeds of the loan, will
20 become) residential real property containing 4
21 or fewer family units or real property used pri-
22 marily for church purposes, loans made for the
23 improvement of residential real property con-

1 *taining 4 or fewer family units or real property*
 2 *used primarily for church purposes, or prop-*
 3 *erty acquired through the liquidation of de-*
 4 *faulted loans described in this clause;*

5 *“(E) not more than 18 percent of the amount of*
 6 *the total assets of which (as of the close of the taxable*
 7 *year) consists of assets other than those described*
 8 *in clause (i) of subparagraph (D), and not more*
 9 *than 36 percent of the amount of the total assets of*
 10 *which (as of the close of the taxable year) consists*
 11 *of assets other than those described in clause (ii) of*
 12 *subparagraph (D); and*

13 *“(F) except for property described in sub-*
 14 *paragraph (C), not more than 3 percent of the*
 15 *assets of which consists of stock of any corporation.*

16 *At the election of the taxpayer, the percentages specified*
 17 *in this paragraph shall be applied on the basis of the*
 18 *average assets outstanding during the taxable year, in lieu*
 19 *of the close of the taxable year, computed under regula-*
 20 *tions prescribed by the Secretary or his delegate.”*

21 (d) CLERICAL AMENDMENTS.—The table of sections
 22 for part II of subchapter H of chapter 1 is amended—

1 (1) by striking out the third item and inserting in
2 lieu thereof the following:

 “Sec. 593. Reserves for losses on loans.”

3 and

4 (2) by adding at the end thereof the following:

 “Sec. 595. Foreclosure on property securing loans.”

5 ~~(61)(e) REPEAL OF EXEMPTION FROM COMMUNICATIONS~~
6 ~~AND TRANSPORTATION OF PERSONS TAXES.—Not with-~~
7 ~~standing any other provision of law, Federal savings~~
8 ~~and loan associations shall not be exempt as such from the~~
9 ~~taxes imposed by section 4251 (relating to excise tax on~~
10 ~~communications) and section 4261 (relating to excise tax~~
11 ~~on transportation of persons) of the Internal Revenue Code~~
12 ~~of 1954.~~

13 (e) *REPEAL OF EXEMPTION FROM CERTAIN EXCISE*
14 *TAXES.—*

15 (1) *AMENDMENT TO HOME OWNERS' LOAN ACT.—*
16 *Section 5(h) of the Home Owners' Loan Act, as*
17 *amended (12 U.S.C. sec. 1464(h)), is amended to read*
18 *as follows:*

19 “(h) *EXEMPTION FROM DISCRIMINATORY STATE AND*
20 *LOCAL TAXATION.—No State, county, municipal, or local*
21 *taxing authority shall impose any tax on such associations or*
22 *their franchise, capital, reserves, surplus, loans, or income*
23 *greater than that imposed by such authority on other similar*

1 *local mutual or cooperative thrift and home financing institu-*
 2 *tions.”*

3 (2) CERTAIN DOCUMENTARY STAMP TAXES.—Sec-
 4 tion 4382(a)(2) (relating to exemptions from docu-
 5 mentary stamp taxes) is amended to read as follows:

6 “(2) DOMESTIC BUILDING AND LOAN ASSOCIA-
 7 TIONS AND MUTUAL DITCH OR IRRIGATION COM-
 8 PANIES.—Shares or certificates of stock issued by domes-
 9 tic building and loan associations and cooperative banks,
 10 to the extent such shares or certificates represent deposits
 11 or withdrawable accounts; or shares or certificates of
 12 stock and certificates of indebtedness issued by mutual
 13 ditch or irrigation companies.”

14 (62)(f) DEDUCTION FOR DIVIDENDS OR INTEREST PAID
 15 ON DEPOSITS.—Section 591 (relating to deduction for divi-
 16 dends paid on deposits) is amended—

17 (1) by striking out “and domestic building and
 18 loan associations” and inserting in lieu thereof the follow-
 19 ing: “domestic building and loan associations, and other
 20 savings institutions chartered and supervised as savings
 21 and loan or similar associations under Federal or State
 22 law”; and

23 (2) by inserting after “dividends” the following:
 24 “or interest”.

1 **(63)**~~(f)~~ *(g)* EFFECTIVE DATES.—

2 (1) The amendment made by subsection (a) shall
3 apply to taxable years ending after December 31, 1962,
4 except that section 593 (f) of the Internal Revenue
5 Code of 1954 shall apply to distributions after Decem-
6 ber 31, 1962, in taxable years ending after such date.

7 (2) The amendment made by subsection (b) shall
8 apply to transactions described in section 595 (a) of the
9 Internal Revenue Code of 1954 occurring after Decem-
10 ber 31, 1962, in taxable years ending after such date.

11 **(64)***(3) The amendment made by subsection (c) shall*
12 *apply to taxable years beginning after the date of the*
13 *enactment of this Act.*

14 **(65)**~~(3)~~ Subsection ~~(e)~~ of this section shall apply—
15 ~~(A)~~ in the case of the tax imposed by section
16 4251 of the Internal Revenue Code of 1954, with
17 respect to amounts paid pursuant to bills rendered
18 after June 30, 1962; and

19 ~~(B)~~ in the case of the tax imposed by section
20 4261 of such Code, with respect to transportation
21 beginning after June 30, 1962.

22 (4) Subsection (e) of this section shall become effec-
23 tive on January 1, 1963, except that—

24 (A) in the case of the tax imposed by section

4251 of the Internal Revenue Code of 1954, such subsection shall apply only with respect to amounts paid pursuant to bills rendered after December 31, 1962; and

(B) in the case of the tax imposed by section 4261 of such Code, such subsection shall apply only with respect to transportation beginning after December 31, 1962.

SEC. (66) 7. DISTRIBUTIONS BY FOREIGN TRUSTS.

(a) DEFINITIONS.—

(1) INCOME OF FOREIGN TRUST.—Section 643 (a)

(6) (relating to modifications taken into account in computing distributable net income) is amended to read as follows:

“(6) INCOME OF FOREIGN TRUST.—In the case of a foreign trust—

“(A) There shall be included the amounts of gross income from sources without the United States, reduced by any amounts which would be deductible in respect of disbursements allocable to such income but for the provisions of section 265 (1) (relating to disallowance of certain deductions).

“(B) Gross income from sources within the

1 United States shall be determined without regard
 2 to section 894 (relating to income exempt under
 3 treaty).

4 “(C) ~~(67)~~Subsection ~~(a)(3)~~ of this section
 5 *Paragraph (3)* shall not apply to a foreign trust
 6 created by a United States person. In the case of
 7 such a trust, (i) there shall be included gains from
 8 the sale or exchange of capital assets, reduced by
 9 losses from such sales or exchanges to the extent such
 10 losses do not exceed gains from such sales or ex-
 11 changes, and (ii) the deduction under section 1202
 12 (relating to deduction for excess of capital gains
 13 over capital losses) shall not be taken into account.”

14 (2) FOREIGN ~~(68)~~ESTATES AND TRUSTS.—Section
 15 643 (relating to definitions) is amended by adding at
 16 the end thereof the following new subsection:

17 “(d) FOREIGN TRUSTS CREATED BY UNITED STATES
 18 PERSONS.—For purposes of this part, the term ‘foreign trust
 19 created by a United States person’ means ~~(69)~~a foreign trust
 20 ~~(as defined in section 7701(a)(31))~~ to which money or
 21 property has been transferred that portion of a foreign trust
 22 (as defined in section 7701(a)(31)) attributable to money or
 23 property transferred directly or indirectly by a United States
 24 person (as defined in section 7701(a)(30)), or under the

1 will of a decedent who at the date of his death was a United
2 States citizen or resident.”

3 (b) ACCUMULATION DISTRIBUTIONS OF FOREIGN
4 TRUSTS.—

5 (1) Section 665 (b) (relating to definitions
6 applicable to subpart D) is amended by striking out
7 “(b) ACCUMULATION DISTRIBUTION.—For purposes
8 of this subpart,” and inserting in lieu thereof the fol-
9 lowing:

10 “(b) ACCUMULATION DISTRIBUTIONS OF TRUSTS
11 OTHER THAN CERTAIN FOREIGN TRUSTS.—For purposes of
12 this subpart, in the case of a trust (other than a foreign trust
13 created by a United States person),”.

14 (2) Section 665 is amended by redesignating sub-
15 sections (c) and (d) as (d) and (e), respectively,
16 and by inserting after subsection (b) the following
17 new subsection:

18 “(c) ACCUMULATION DISTRIBUTION OF CERTAIN
19 FOREIGN TRUSTS.—For purposes of this subpart, in the case
20 of a foreign trust created by a United States person, the term
21 ‘accumulation distribution’ for any taxable year of the trust
22 means the amount by which the amounts specified in para-
23 graph (2) of section 661 (a) for such taxable year exceed
24 distributable net income, reduced by the amounts specified

1 in paragraph (1) of section 661 (a). For purposes of this
 2 subsection, the amount specified in paragraph (2) of section
 3 661 (a) shall be determined without regard to section 666.
 4 Any amount paid to a United States person which is from
 5 a payor who is not a United States person and which is
 6 derived directly or indirectly from a foreign trust created by
 7 a United States person shall be deemed in the year of pay-
 8 ment to have been directly paid by the foreign trust."

9 (c) ALLOCATION OF ACCUMULATION DISTRIBUTIONS
 10 TO PRECEDING YEARS.—Section 666 (a) (relating to ac-
 11 cumulation distribution allocated to 5 preceding years) is
 12 amended—

13 (1) by striking out "(a) AMOUNT ALLOCATED.—
 14 In the case of a trust" and inserting in lieu thereof the
 15 following:

16 "(a) AMOUNT ALLOCATED.—In the case of a trust
 17 (other than a foreign trust created by a United States
 18 person)"; and

19 (2) by adding at the end thereof the following
 20 new sentence:

21 "In the case of a foreign trust created by a United States
 22 person, this subsection shall apply to the preceding tax-
 23 able years of the trust without regard to any provision of
 24 the preceding sentences which would (but for this sentence)
 25 limit its application to the 5 preceding taxable years."

1 (d) AMOUNTS TREATED AS RECEIVED IN PRIOR
 2 YEARS.—Section 668 (a) (relating to amounts treated as
 3 received in prior taxable years) is amended by adding at
 4 the end thereof the following new sentence: “Except as
 5 provided in section 669, in the case of a foreign trust created
 6 by a United States person the preceding sentence shall not
 7 apply to any beneficiary who is a United States person.”

8 (e) SPECIAL RULES FOR FOREIGN TRUSTS.—Subpart
 9 D of part I of subchapter J of chapter 1 (relating to treat-
 10 ment of excess distributions by trusts) is amended by adding
 11 at the end thereof the following new section:

12 **“SEC. 669. SPECIAL RULES APPLICABLE TO CERTAIN FOR-**
 13 **EIGN TRUSTS.**

14 “(a) LIMITATION ON TAX.—

15 “(1) GENERAL RULE.—At the election of a bene-
 16 ficiary who is a United States person (as defined in
 17 section 7701 (a) (30)) and who satisfies the require-
 18 ments of subsection (b), the tax attributable to the
 19 amounts treated under section 668 (a) as having been
 20 received by him from a foreign trust created by a United
 21 States person on the last day of a preceding taxable
 22 year of the trust shall not be greater than—

23 “(A) the tax determined under the next to the
 24 last sentence of section 668 (a), or

25 “(B) the tax determined by multiplying by

1 the number of preceding taxable years of the trust,
2 on the last day of each of which an amount is
3 deemed under section 666 (a) to have been distrib-
4 uted, the average of the increase in tax attributable
5 to recomputing the beneficiary's gross income for
6 the taxable year and each of his 2 taxable years im-
7 mediately preceding the year of the accumulation
8 distribution by adding to the income of each of such
9 years an amount determined by dividing the amount
10 required to be included in income under section
11 668 (a) by such number of preceding taxable years
12 of the trust. The recomputation for the taxable year
13 shall be made without regard to the inclusion in
14 income required by section 668 (a) of any amount
15 other than pursuant to this paragraph.

16 “(2) EXCEPTIONS.—

17 “(A) When an accumulation distribution is
18 deemed under section 666 (a) to have been distrib-
19 uted on the last day of less than 3 taxable years
20 of the trust, the taxable years of the beneficiary for
21 which a recomputation is made under subsection
22 (a) (1) (B) shall equal the number of years to
23 which section 666 (a) applies, commencing with
24 the most recent taxable year of the beneficiary.

1 “(B) If a beneficiary was not alive on the last
2 day of each preceding taxable year of the trust
3 with respect to which a distribution is deemed made
4 under section 666 (a), paragraph (1) (A) of this
5 subsection shall not apply. In applying paragraph
6 (1) (B) of this subsection, no recomputation shall
7 be made for a beneficiary for a taxable year for
8 which he was not alive; if he has no preceding tax-
9 able year, the recomputation shall be made on the
10 . basis of his taxable year without regard to the in-
11 clusion in income required by section 668 (a) of
12 any amount other than pursuant to paragraph
13 (1) (B).

14 “(3) EFFECT OF PRIOR ELECTION.—In comput-
15 ing the limitation on tax under paragraph (1) of this
16 subsection for any beneficiary—

17 “(A) SUBSEQUENT ELECTION UNDER PARA-
18 GRAPH (1)(A).—If an election has been made under
19 paragraph (1) (B) of this subsection, for purposes
20 of a subsequent election under paragraph (1) (A)
21 the income of any year with respect to which an
22 amount is deemed distributed to a beneficiary under
23 section 666 (a) shall include amounts previously
24 deemed distributed to such beneficiary for such

1 year as a result of an accumulation distribution with
2 respect to which an election under paragraph (1)
3 (B) was made.

4 “(B) SUBSEQUENT ELECTION UNDER PARA-
5 GRAPH (1)(B).—If with respect to an accumulation
6 distribution an election has been made under either
7 paragraph (1) (A) or paragraph (1) (B) of this
8 subsection, or the next to the last sentence of section
9 668 (a) has applied, for purposes of a subsequent
10 election under paragraph (1) (B) the number of
11 preceding taxable years of the trust with respect to
12 which an amount is deemed distributed to a benefi-
13 ciary under section 666 (a) shall be determined
14 without regard to any such year with respect to
15 which an amount was previously deemed distrib-
16 uted to such beneficiary.

17 “(b) INFORMATION REQUIREMENT.—The election of
18 a beneficiary to apply the limitations on tax provided in sub-
19 section (a) of this section shall not be effective unless the
20 beneficiary at the time of making the election supplies such
21 information with respect to the operation and accounts of the
22 trust, for each taxable year on the last day of which an
23 amount is deemed distributed under section 666 (a), as the
24 Secretary or his delegate may by regulations prescribe.”

25 (f) INFORMATION RETURNS WITH RESPECT TO FOR-

1 EIGN TRUSTS.—Subpart B of part III of subchapter A of
 2 chapter 61 (relating to information concerning transactions
 3 with other persons) is amended by adding at the end thereof
 4 the following new section:

5 **“SEC. 6047. RETURNS AS TO CREATION OF OR TRANSFERS**
 6 **TO CERTAIN FOREIGN TRUSTS.**

7 “(a) GENERAL RULE.—On or before the 90th day
 8 after—

9 “(1) the creation of any foreign trust by a United
 10 States person, or

11 “(2) the transfer of any money or property to a
 12 foreign trust by a United States person,
 13 the grantor in the case of an inter vivos trust, the fiduciary
 14 of an estate in the case of a testamentary trust, or the trans-
 15 feror, as the case may be, shall make a return in compliance
 16 with the provisions of subsection (b).

17 “(b) FORM AND CONTENTS OF RETURNS.—The re-
 18 turns required by subsection (a) shall be in such form and
 19 shall set forth, in respect of the foreign trust, such informa-
 20 tion as the Secretary or his delegate prescribes by regulation
 21 as necessary for carrying out the provisions of the income
 22 tax laws.

23 “(c) CROSS REFERENCES.—

“ (1) For provisions relating to penalties for violations
 of this section, see sections 6677 and 7203.

“ (2) For definition of the term ‘foreign trust created
 by a United States person’, see section 643(d).”

1 (g) FAILURE TO FILE INFORMATION RETURNS.—
2 Subchapter B of chapter 68 (relating to assessable penalties)
3 is amended by adding at the end thereof the following new
4 section:

5 “SEC. 6677. FAILURE TO FILE INFORMATION RETURNS
6 WITH RESPECT TO CERTAIN FOREIGN
7 TRUSTS.

8 “(a) CIVIL PENALTY.—In addition to any criminal
9 penalty provided by law, any person required to file a return
10 under section 6047 who fails to file such return at the time
11 provided in such section, or who files a return which does not
12 show the information required pursuant to such section, shall
13 pay a penalty equal to 5 percent of the amount transferred
14 to a trust, but not more than \$1,000, unless it is shown that
15 such failure is due to reasonable cause.

16 “(b) DEFICIENCY PROCEDURES NOT TO APPLY.—
17 Subchapter B of chapter 63 (relating to deficiency proce-
18 dures for income, estate, and gift taxes) shall not apply in
19 respect of the assessment or collection of any penalty
20 imposed by subsection (a).”

21 (h) UNITED STATES PERSON DEFINED.—Section
22 7701 (a) is amended by adding at the end thereof the
23 following new paragraphs:

“(30) UNITED STATES PERSON.—The term

‘United States person’ means—

“(A) a citizen or resident of the United States,

“(B) a domestic partnership,

“(C) a domestic corporation, and

“(D) any estate or trust (other than a foreign estate or foreign trust, within the meaning of section 7701 (a) (31)).

“(31) FOREIGN ESTATE OR TRUST.—The terms ‘foreign estate’ and ‘foreign trust’ mean an estate or trust, as the case may be, the income of which from sources without the United States is not includible in gross income under subtitle A.”

(i) TECHNICAL AMENDMENTS.—

(1) The table of sections for subpart D of subchapter J of chapter 1 (relating to treatment of excess distributions by trusts) is amended by adding at the end thereof

“Sec. 669. Special rules applicable to certain foreign trusts.”

(2) The table of sections for subpart B of part III of subchapter A of chapter 61 (relating to information concerning transactions with other persons) is amended by adding at the end thereof

“Sec. 6047. Returns as to creation of or transfers to certain foreign trusts.”

1 (3) The table of sections for subchapter B of
 2 chapter 68 (relating to assessable penalties) is amended
 3 by adding at the end thereof

“Sec. 6677. Failure to file information returns with respect
 to certain foreign trusts.”

4 (j) EFFECTIVE DATE.—The amendments made by this
 5 section (other than by subsections (f), (g), and (h)) shall
 6 apply with respect to distributions made ~~(70)~~in taxable
 7 years of trusts beginning after the date of the enactment of
 8 this Act after December 31, 1962.

9 SEC. ~~(71)~~⁴⁰ 8. MUTUAL INSURANCE COMPANIES (OTHER
 10 THAN LIFE, MARINE, AND CERTAIN FIRE
 11 ~~(72)~~OR FLOOD INSURANCE COMPANIES),
 12 ETC.

13 (a) IMPOSITION OF TAX.—So much of part II of sub-
 14 chapter L (relating to mutual insurance companies, other
 15 than life or marine or fire insurance companies issuing per-
 16 petual policies) of chapter 1 as precedes section 822 is
 17 amended to read as follows:

1 **"PART II—MUTUAL INSURANCE COMPANIES**
 2 **(OTHER THAN LIFE AND CERTAIN**
 3 **MARINE INSURANCE COMPANIES**
 4 **AND OTHER THAN FIRE (73)OR**
 5 **FLOOD INSURANCE COMPANIES**
 6 **WHICH OPERATE ON BASIS OF PER-**
 7 **PETUAL POLICIES OR PREMIUM**
 8 **DEPOSITS)**

"Sec. 821. Tax on mutual insurance companies to which
 part II applies.

"Sec. 822. Determination of taxable investment income.

"Sec. 823. Determination of statutory underwriting income
 or loss.

"Sec. 824. Adjustments to provide protection against losses.

"Sec. 825. Unused loss deduction.

"Sec. 826. Election by reciprocal.

9 **"SEC. 821. TAX ON MUTUAL INSURANCE COMPANIES TO**
 10 **WHICH PART II APPLIES.**

11 **"(a) IMPOSITION OF TAX.—**A tax is hereby imposed
 12 for each taxable year beginning after December 31, 1962,
 13 on the mutual insurance company taxable income of every
 14 mutual insurance company (other than a life insurance com-

pany and other than a ~~(74)~~ fire fire, flood, or marine insurance company subject to the tax imposed by section 831).
Such tax shall consist of—

~~(75)~~“(1) ~~NORMAL TAX.~~—A normal tax of 25 percent of the mutual insurance company taxable income, or 50 percent of the amount by which such taxable income exceeds \$6,000, whichever is the lesser; plus

“(1) *NORMAL TAX.*—

“(A) *TAXABLE YEARS BEGINNING BEFORE JULY 1, 1963.*—In the case of taxable years beginning before July 1, 1963, a normal tax of 30 percent of the mutual insurance company taxable income, or 60 percent of the amount by which such taxable income exceeds \$6,000, whichever is the lesser;

“(B) *TAXABLE YEARS BEGINNING AFTER JUNE 30, 1963.*—In the case of taxable years beginning after June 30, 1963, a normal tax of 25 percent of the mutual insurance company taxable income, or 50 percent of the amount by which such taxable income exceeds \$6,000, whichever is the lesser; plus

“(2) *SURTAX.*—A surtax of 22 percent of the mutual insurance company taxable income (computed without regard to the deduction provided in section 242 for partially tax-exempt interest) in excess of \$25,000.

1 “(b) MUTUAL INSURANCE COMPANY TAXABLE IN-
 2 COME DEFINED.—For purposes of this part, the term ‘mutual
 3 insurance company taxable income’ means, with respect to
 4 any taxable year, the amount by which—

5 “(1) the sum of—

6 “(A) the taxable investment income (as de-
 7 fined in section 822 (a) (1)),

8 “(B) the statutory underwriting income (as
 9 defined in section 823 (a) (1)), and

10 “(C) the amounts required by section 824 (d)
 11 to be subtracted from the protection against loss
 12 account, exceeds

13 “(2) the sum of—

14 “(A) the investment loss (as defined in sec-
 15 tion 822 (a) (2)),

16 “(B) the statutory underwriting loss (as de-
 17 fined in section 823 (a) (2)), and

18 “(C) the unused loss deduction provided by
 19 section 825 (a) .

20 “(c) ALTERNATIVE TAX FOR CERTAIN SMALL COM-
 21 PANIES.—

22 “(1) IMPOSITION OF TAX.—In the case of taxable
 23 years beginning after December 31, 1962, there is here-
 24 by imposed for each taxable year on the income of each
 25 mutual insurance company to which this subsection

1 applies a tax (which shall be in lieu of the tax imposed
2 by subsection (a)) computed as follows:

3 ~~(76)“(A) NORMAL TAX.—~~A normal tax of 25
4 percent of the taxable investment income, or 50
5 percent of the amount by which such taxable in-
6 come exceeds \$3,000, whichever is the lesser; plus

7 “(A) NORMAL TAX.—

8 “(i) TAXABLE YEARS BEGINNING BEFORE
9 JULY 1, 1963.—In the case of taxable years be-
10 ginning before July 1, 1963, a normal tax of
11 30 percent of the taxable investment income, or
12 60 percent of the amount by which such taxable
13 income exceeds \$3,000, whichever is the lesser;

14 “(ii) TAXABLE YEARS BEGINNING AFTER
15 JUNE 30, 1963.—In the case of taxable years be-
16 ginning after June 30, 1963, a normal tax of
17 25 percent of the taxable investment income, or
18 50 percent of the amount by which such taxable
19 income exceeds \$3,000, whichever is the lesser;
20 plus

21 “(B) SURTAX.—A surtax of 22 percent of the
22 taxable investment income (computed without re-
23 gard to the deduction provided in section 242 for
24 partially tax-exempt interest) in excess of \$25,000.

25 “(2) GROSS AMOUNT RECEIVED, OVER ~~(77)\$75,000~~

1 \$150,000 BUT LESS THAN (78)~~\$125,000~~ \$250,000.—If the
 2 gross amount received during the taxable year from the
 3 items described in section 822 (b) (other than paragraph
 4 (1) (D) thereof) and premiums (including deposits
 5 and assessments) is over (79)~~\$75,000~~ \$150,000 but
 6 less than (80)~~\$125,000~~ \$250,000, the tax imposed by
 7 paragraph (1) shall be reduced to an amount which
 8 bears the same proportion to the amount of the tax deter-
 9 mined under paragraph (1) as the excess over
 10 (81)~~\$75,000~~ \$150,000 of such gross amount received
 11 bears to (82)~~\$50,000~~ \$100,000.

12 “(3) COMPANIES TO WHICH SUBSECTION AP-
 13 PLIES.—

14 “(A) IN GENERAL.—Except as provided in
 15 subparagraph (B), this subsection shall apply to
 16 every mutual insurance company (other than a life
 17 insurance company and other than a (83)~~fire~~ *fire*,
 18 *flood*, or marine insurance company subject to the
 19 tax imposed by section 831) which received during
 20 the taxable year from the items described in section
 21 822 (b) (other than paragraph (1) (D) thereof)
 22 and premiums (including deposits and assessments)
 23 a gross amount in excess of (84)~~\$75,000~~ \$150,000
 24 but not in excess of (85)~~\$300,000~~ \$600,000.

1 “(B) EXCEPTIONS.—This subsection shall not
2 apply to a mutual insurance company for the tax-
3 able year if—

4 “(i) there is in effect an election by such
5 company made under subsection (d) to be tax-
6 able under subsection (a) ; or

7 “(ii) there is any amount in the protection
8 against loss account at the beginning of the
9 taxable year.

10 “(d) ELECTION TO INCLUDE STATUTORY UNDER-
11 WRITING INCOME OR LOSS.—

12 “(1) IN GENERAL.—Any mutual insurance com-
13 pany which is subject to the tax imposed by subsection
14 (c) may elect, in such manner and at such time as the
15 Secretary or his delegate may by regulations prescribe,
16 to be subject to the tax imposed by subsection (a) .

17 “(2) EFFECT OF ELECTION.—If an election is made
18 under paragraph (1), the electing company shall be
19 subject to the tax imposed by subsection (a) (and shall
20 not be subject to the tax imposed by subsection (c))
21 for the first taxable year for which such election is made
22 and for all taxable years thereafter unless the Secretary
23 or his delegate consents to a revocation of such election.

24 “(e) NO UNITED STATES INSURANCE BUSINESS.—
25 Foreign mutual insurance companies (other than a life

1 insurance company and other than a (86) ~~fire~~ fire, flood, or
 2 marine insurance company subject to the tax imposed by
 3 section 831) not carrying on an insurance business within
 4 the United States shall not be subject to this part but shall
 5 be taxable as other foreign corporations.

6 (87)“(f) *SPECIAL TRANSITIONAL UNDERWRITING LOSS.*—

7 “(1) *COMPANIES TO WHICH SUBSECTION AP-*
 8 *PLIES.*—*This subsection shall apply to every mutual*
 9 *insurance company which has been subject to the tax*
 10 *imposed by this section (as in effect before the enactment*
 11 *of this subsection) for the 6 taxable years immediately*
 12 *preceding January 1, 1963, and has incurred an under-*
 13 *writing loss for at least 5 of such 6 taxable years.*

14 “(2) *REDUCTION OF MUTUAL INSURANCE COM-*
 15 *PANY TAXABLE INCOME.*—*For purposes of this part,*
 16 *the mutual insurance company taxable income for the*
 17 *taxable year with respect to a company described in par-*
 18 *agraph (1) shall be the mutual insurance company tax-*
 19 *able income for the taxable year (determined without*
 20 *regard to this subsection) reduced by the amount by*
 21 *which—*

22 “(A) *the sum of the underwriting losses of such*
 23 *company for the 6 taxable years prior to January*
 24 *1, 1963, reduced by the underwriting gain for such*
 25 *years, exceeds*

1 “(B) the total amount by which the mutual in-
 2 insurance company taxable income was reduced by
 3 reason of this subsection for prior taxable years.

4 “(3) For purposes of this subsection—

5 “(A) The term ‘underwriting loss’ means
 6 statutory underwriting loss, computed without any
 7 deduction under section 824(a), and without any
 8 deduction for dividends to policyholders provided by
 9 section 832(c)(11).

10 “(B) The term ‘underwriting gain’ means
 11 statutory underwriting income, computed without
 12 any deduction under section 823(c) or any
 13 deduction under section 824(a).

14 “(4) YEARS TO WHICH SUBSECTION APPLIES.—
 15 This subsection shall apply with respect to any taxable
 16 year beginning after December 31, 1962, and before
 17 January 1, 1968, for which the taxpayer is subject to the
 18 tax imposed by subsection (a).

19 (88)(f) (g) CROSS REFERENCES.—

 “(1) For exemption from tax of certain mutual insur-
 ance companies, see section 501(c)(15).

 “(2) For alternative tax in case of capital gains, see
 section 1201(a).”

20 (b) TAXABLE INVESTMENT INCOME.—

21 (1) IN GENERAL.—Section 822 (relating to de-
 22 termination of mutual insurance company taxable

income) is amended by striking out the heading and subsection (a) and inserting in lieu thereof the following:

**“SEC. 822. DETERMINATION OF TAXABLE INVESTMENT
INCOME.**

“(a) DEFINITIONS.—For purposes of this part—

“(1) The term ‘taxable investment income’ means the gross investment income, minus the deductions provided in subsection (c).

“(2) The term ‘investment loss’ means the amount by which the deductions provided in subsection (c) exceed the gross investment income.”

(2) CONFORMING AMENDMENTS.—Subsections (c) and (e) of section 822 are each amended by striking out “mutual insurance company taxable income” each place it appears and inserting in lieu thereof “taxable investment income”.

(3) DIVIDENDS RECEIVED DEDUCTION.—Section 822 (c) (7) (relating to special deductions) is amended by adding at the end thereof the following new sentence: “In applying section 246 (b) (relating to limitation on aggregate amount of deductions for dividends received) for purposes of this paragraph, the reference in such section to ‘taxable income’ shall be treated as a reference to ‘taxable investment income’.”

1 (4) REDESIGNATION OF SECTION 823.—Part II of
2 subchapter L of chapter 1 is amended by striking out

3 “SEC. 823. OTHER DEFINITIONS.

4 “For purposes of this part—”,

5 and inserting in lieu thereof (at the end of section 822)

6 the following:

7 “(f) DEFINITIONS.—For purposes of this part—”.
8 (c) STATUTORY UNDERWRITING INCOME OR LOSS.—

9 Part II of subchapter L of chapter 1 is amended by adding
10 after section 822 (f) (as redesignated by subsection (b) (4)
11 of this section) the following new sections:

12 “SEC. 823. DETERMINATION OF STATUTORY UNDERWRIT-
13 ING INCOME OR LOSS.

14 “(a) IN GENERAL.—For purposes of this part—

15 “(1) The term ‘statutory underwriting income’
16 means the amount by which—

17 “(A) the gross income which would be taken
18 into account in computing taxable income under
19 section 832 if the taxpayer were subject to the tax
20 imposed by section 831, reduced by the gross in-
21 vestment income, exceeds

22 “(B) the sum of (i) the deductions which
23 would be taken into account in computing taxable
24 income if the taxpayer were subject to the tax im-
25 posed by section 831, reduced by the deductions

provided in section 822 (c) , plus (ii) the deductions provided in subsection (c) and section 824 (a) .

“(2) The term ‘statutory underwriting loss’ means the excess of the amount referred to in paragraph (1) (B) over the amount referred to in paragraph (1) (A) .

“(b) MODIFICATIONS.—In applying subsection (a)—

“(1) NET OPERATING LOSS DEDUCTION.—The deduction for net operating losses provided in section 172 shall not be allowed.

“(2) INTERINSURERS.—In the case of a mutual insurance company which is an interinsurer or reciprocal underwriter—

“(A) there shall be allowed as a deduction the increase for the taxable year in savings credited to subscriber accounts, or

“(B) there shall be included as an item of gross income the decrease for the taxable year in savings credited to subscriber accounts.

For purposes of the preceding sentence, the term ‘savings credited to subscriber accounts’ means such portion of the surplus as is credited to the individual accounts of subscribers before the 16th day of the third month following the close of the taxable year, but only if the company would be obligated to pay such amount

1 promptly to such subscriber if he terminated his con-
 2 tract at the close of the company's taxable year. For
 3 purposes of determining his taxable income, the sub-
 4 scriber shall treat any such savings credited to his ac-
 5 count as a dividend paid or declared.

6 “(c) SPECIAL DEDUCTION FOR SMALL COMPANY
 7 HAVING GROSS AMOUNT OF LESS THAN ~~(89)\$900,000~~
 8 ~~\$1,200,000~~.—

9 “(1) IN GENERAL.—If the gross amount received
 10 during the taxable year by a taxpayer subject to the tax
 11 imposed by section 821(a) from the items described
 12 in section 822(b) (other than paragraph (1) (D)
 13 thereof) and premiums (including deposits and assess-
 14 ments) does not equal or exceed ~~(90)\$900,000~~ \$1,200,-
 15 000, then in determining the statutory underwriting in-
 16 come or loss for the taxable year there shall be allowed an
 17 additional deduction of \$6,000; except that if such gross
 18 amount exceeds ~~(91)\$300,000~~ \$600,000, such addi-
 19 tional deduction shall be equal to 1 percent of the amount
 20 by which ~~(92)\$900,000~~ \$1,200,000 exceeds such gross
 21 amount.

22 “(2) LIMITATION.—The amount of the deduction
 23 allowed under paragraph (1) shall not exceed the
 24 statutory underwriting income for the taxable year,

computed without regard to any deduction under this subsection or section 824 (a).

“SEC. 824. ADJUSTMENTS TO PROVIDE PROTECTION AGAINST LOSSES.

“(a) ALLOWANCE OF DEDUCTION.—

“(1) IN GENERAL.—In determining the statutory underwriting income or loss for any taxable year there shall be allowed as a deduction the sum of—

“(A) an amount equal to 1 percent of the losses incurred during the taxable year (as determined under section 832 (b) (5)), plus

“(B) an amount equal to 25 percent of the underwriting gain for the taxable year, plus

“(C) if the concentrated windstorm, etc., premium percentage for the taxable year exceeds ~~(93)~~⁵⁰ 40 percent, an amount determined by applying so much of such percentage as exceeds ~~(94)~~⁵⁰ 40 percent to the underwriting gain for the taxable year ~~(95)~~, or one-half of such amount in the case of a taxpayer who elects to compute the concentrated windstorm, etc., premium percentage under paragraph (2) (A) (iii)

For purposes of this paragraph, the term ‘under-

1 writing gain' means statutory underwriting income, com-
2 puted without any deduction under this subsection.

3 “(2) SPECIAL RULE FOR COMPANIES HAVING CON-
4 CENTRATED WINDSTORM, ETC., RISKS.—For purposes
5 of paragraph (1) (C), the term ‘concentrated wind-
6 storm, etc., premium percentage’ means, with respect to
7 any taxable year, the percentage obtained by dividing—

8 “(A) the amount of the premiums earned
9 on insurance contracts during the taxable year (as
10 defined in section 832 (b) (4)), to the extent at-
11 tributable to insuring against losses (96) arising in
12 any one State arising—

13 “(i) in any one State;

14 “(ii) if the taxpayer so elects, within 200
15 miles of any fixed point selected by the taxpayer;
16 or

17 “(iii) if the taxpayer so elects, within 400
18 miles of any fixed point selected by the taxpayer,
19 from windstorm, hail, flood, earthquake, or similar
20 hazards, by

21 “(B) the amount of the premiums earned
22 on insurance contracts during the taxable year (as
23 so defined).

24 “(b) PROTECTION AGAINST LOSS ACCOUNT.—Each
25 insurance company subject to the tax imposed by section

1 821 (a) for any taxable year shall, for purposes of this part,
2 establish and maintain a protection against loss account.

3 “(c) ADDITIONS TO ACCOUNT.—There shall be added
4 to the protection against loss account for each taxable year
5 an amount equal to the amount allowable as a deduction for
6 the taxable year under subsection (a) (1).

7 “(d) SUBTRACTIONS.—

8 “(1) ANNUAL SUBTRACTIONS.—After applying
9 subsection (c), there shall be subtracted for the taxable
10 year from the protection against loss account—

11 ~~(97)“(A) first, an amount equal to the excess of~~
12 ~~the statutory underwriting loss for the taxable year~~
13 ~~over the underwriting loss (as defined in paragraph~~
14 ~~(6)) for the taxable year,~~

15 “(A) first, an amount equal to the excess (if
16 any) of the deduction allowed under subsection (a)
17 for the taxable year over the underwriting gain
18 (within the meaning of subsection (a)(1)) for the
19 taxable year,

20 “(B) then, the amount (if any) by which—

21 “(i) the sum of the investment loss for
22 such year and the ~~(98)underwriting loss stat-~~
23 ~~utory underwriting loss (reduced by the amount~~
24 ~~referred to in subparagraph (A)) for such~~
25 year, exceeds

1 “(ii) the sum of the statutory underwrit-
2 ing income for such taxable year and the taxable
3 investment income for such taxable year,

4 “(C) next (in the order in which the losses
5 occurred), amounts equal to the unused loss carry-
6 overs to such year,

7 “(D) next, any amount remaining which was
8 added to the account for the fifth preceding taxable
9 year, minus one-half of the amount remaining in the
10 account for such taxable year which was added
11 by reason of subsection (a) (1) (B), and

12 “(E) finally, the amount by which the total
13 amount in the account exceeds whichever of the
14 following is the greater:

15 “(i) 10 percent of premiums earned on in-
16 surance contracts during the taxable year (as
17 defined in section 832 (b) (4)) less dividends
18 to policyholders (as defined in section
19 832 (c) (11)), or

20 “(ii) the total amount in the account at
21 the close of the preceding taxable year.

22 “(2) RULES FOR CEILING ON PROTECTION
23 AGAINST LOSS ACCOUNT.—For purposes of paragraph
24 (1) (E), the total amount in the account shall be
25 determined—

1 “(A) after the application of this section with-
2 out regard to paragraph (1) (E), and

3 “(B) without taking into consideration
4 amounts remaining in the account which were
5 added, with respect to all taxable years, by reason
6 of subsection (a) (1) (C).

7 “(3) PRIORITIES.—The amounts required to be
8 subtracted from the protection against loss account—

9 “(A) under subparagraphs (A), (B), and
10 (C) of paragraph (1) shall be subtracted—

11 “(i) first (on a first-in, first-out, basis)
12 from amounts in the account with respect to
13 the five preceding taxable years and the taxable
14 year, and

15 “(ii) then from amounts in the account
16 with respect to earlier years,

17 “(B) under subparagraph (E) of paragraph
18 (1) shall be subtracted only from amounts in the
19 account with respect to the taxable year, and

20 “(C) under paragraphs (A), (B), (C), and
21 (E) of paragraph (1) shall, if the amount to be
22 subtracted from the total amounts in the account
23 with respect to any taxable year is less than such
24 total, be subtracted from each of the amounts (re-
25 ferred to in subsection (a) (1)) in the account with

1 respect to such year in the proportion which each
2 bears to such total.

3 “(4) TERMINATION OF TAXABILITY UNDER SEC-
4 TION 821.—If the taxpayer is not subject to tax under
5 section 821 for any taxable year, the entire amount in
6 the account at the close of the preceding taxable year
7 shall be subtracted from the account in such preceding
8 taxable year.

9 “(5) ELECTION TO SUBTRACT AMOUNT FROM
10 ACCOUNT.—

11 “(A) A taxpayer may elect for any taxable
12 year for which it is subject to tax under section
13 821 (a) to subtract from its protection against loss
14 account any amount which, but for the application of
15 this subparagraph, would be in such account as of
16 the close of such taxable year.

17 “(B) The election provided by subparagraph
18 (A) for any taxable year shall be made (in such
19 manner and in such form as the Secretary or his
20 delegate may by regulations prescribe) after the
21 close of such taxable year and not later than the time
22 prescribed by law for filing the return (including
23 extensions thereof) for the taxable year following
24 such taxable year. Such an election, once made,
25 may not be revoked.

(99)~~“(6)~~ UNDERWRITING LOSS DEFINED.—For purposes of paragraph ~~(1)~~, the term ‘underwriting loss’ means the amount by which—

~~“(A)~~ the deductions which would be taken into account in computing taxable income under section 832 if the taxpayer were subject to the tax imposed by section 831, reduced by the sum of ~~(i)~~ the deductions provided in section 822(c), and ~~(ii)~~ the deduction for dividends to policyholders provided by section 832(c)~~(11)~~, exceeds

~~“(B)~~ the amount referred to in section 823 ~~(a)(1)(A)~~.

“SEC. 825. UNUSED LOSS DEDUCTION.

“(a) AMOUNT OF DEDUCTION.—For purposes of this part, the unused loss deduction for the taxable year shall be an amount equal to the unused loss carryovers or carrybacks to the taxable year.

“(b) UNUSED LOSS DEFINED.—For purposes of this part, the term ‘unused loss’ means, with respect to any taxable year, the amount (if any) by which—

“(1) the sum of the statutory underwriting loss and the investment loss, exceeds

“(2) the sum of—

“(A) the taxable investment income,

“(B) the statutory underwriting income, and

1 “(C) the amounts required by section 824 (d)
2 to be subtracted from the protection against loss
3 account.

4 “(c) LOSS YEAR DEFINED.—For purposes of this part
5 the term ‘loss year’ means, with respect to any company
6 subject to the tax imposed by section 821 (a), any tax-
7 able year in which the unused loss (as defined in subsection
8 (b)) of such taxpayer is more than zero.

9 “(d) YEARS TO WHICH CARRIED.—The unused loss
10 for any loss year shall be—

11 “(1) an unused loss carryback to each of the 3
12 taxable years preceding the loss year, and

13 “(2) an unused loss carryover to each of the 5
14 taxable years following the loss year.

15 “(e) AMOUNT OF CARRYBACKS AND CARRYOVERS.—
16 The entire amount of the unused loss for any loss year shall
17 be carried to the earliest of the taxable years to which such
18 loss may be carried. The portion of such loss which shall
19 be carried to each of the other taxable years shall be the
20 excess (if any) of the amount of such loss over the sum
21 of the offsets (as defined in subsection (f)) for each of the
22 prior taxable years to which such loss may be carried.

23 “(f) OFFSET DEFINED.—For purposes of subsection
24 (e), the term ‘offset’ means with respect to any taxable year
25 (hereinafter referred to as the ‘offset year’) —

“ (1) in the case of an unused loss carryback from the loss year to the offset year, the mutual insurance company taxable income for the offset year; or

“ (2) in the case of an unused loss carryover from the loss year to the offset year, an amount equal to the sum of—

“ (A) the amount required to be subtracted from the protection against loss account under section 824 (d) (1) (C) for the offset year, plus

“ (B) the mutual insurance company taxable income for the offset year.

For purposes of paragraphs (1) and (2) (B), the mutual insurance taxable income for the offset year shall be determined without regard to any unused loss carryback or carryover from the loss year or any taxable year thereafter.

“ (g) LIMITATIONS.—For purposes of this part, an unused loss shall not be carried—

“ (1) to or from any taxable year beginning before January 1, 1963,

“ (2) to or from any taxable year for which the insurance company is not subject to the tax imposed by section 821 (a), nor

“ (3) to any taxable year if, between the loss year and such taxable year, there is an intervening taxable

1 year for which the insurance company was not subject
2 to the tax imposed by section 821 (a).

3 **“SEC. 826. ELECTION BY RECIPROCAL.**

4 “(a) IN GENERAL.—Except as otherwise provided in
5 this section, any mutual insurance company which is an
6 interinsurer or reciprocal underwriter (hereinafter in this
7 section referred to as a ‘reciprocal’) subject to the taxes im-
8 posed by section 821 (a) may, under regulations prescribed
9 by the Secretary or his delegate, elect to be subject to the
10 limitation provided in subsection (b). Such election shall
11 be effective for the taxable year for which made and for all
12 succeeding taxable years, and shall not be revoked except
13 with the consent of the Secretary or his delegate.

14 “(b) LIMITATION.—The deduction for amounts paid or
15 incurred in the taxable year to the attorney-in-fact by a
16 reciprocal making the election provided in subsection (a)
17 shall be limited to, but in no case increased by, the deduc-
18 tions of the attorney-in-fact allocable, in accordance with
19 regulations prescribed by the Secretary or his delegate, to the
20 income received by the attorney-in-fact from the reciprocal.

21 “(c) EXCEPTION.—An election may not be made by a
22 reciprocal under subsection (a) unless the attorney-in-fact
23 of such reciprocal—

24 “(1) is subject to the taxes imposed by section 11
25 (b) and (c) ;

“ (2) consents in such manner as the Secretary or his delegate shall prescribe by regulations to make available such information as may be required during the period in which the election provided in subsection (a) is in effect, under regulations prescribed by the Secretary or his delegate;

“ (3) reports the income received from the reciprocal and the deductions allocable thereto under the same method of accounting under which the reciprocal reports deductions for amounts paid to the attorney-in-fact; and

“ (4) files its return on the calendar year basis.

~~(100)“(d) SPECIAL RULE.—For purposes of computing the deduction provided in section 824(a) and the additions to the account provided by section 824(e) with respect to any reciprocal electing to be subject to the limitation provided in subsection (b), such limitation shall not be taken into account.~~

“(d) SPECIAL RULE.—In applying section 824(d)(1)(D), any amount which was added to the protection against loss account by reason of an election under this section shall be treated as having been added by reason of section 824(a)(1)(A).

“(e) CREDIT.—Any reciprocal electing to be subject to the limitation provided in subsection (b) shall be credited with so much of the tax paid by the attorney-in-fact as is

1 attributable, under regulations prescribed by the Secre-
 2 tary or his delegate, to the income received by the attorney-
 3 in-fact from the reciprocal in such taxable year.

4 “(f) SURTAX EXEMPTION DENIED.—Any increase in
 5 taxable income of a reciprocal attributable to the limitation
 6 provided in subsection (b) shall be taxed without regard
 7 to the surtax exemption provided in section 821 (a) (2).

8 “(g) ADJUSTMENT FOR REFUND.—If for any taxable
 9 year an attorney-in-fact is allowed a credit or refund for
 10 taxes paid with respect to which ~~(101)~~~~a reciprocal was~~
 11 ~~allowed a credit~~ *credit or refund to the reciprocal resulted*
 12 under subsection (e), the taxes of such reciprocal for such
 13 taxable year shall be properly adjusted under regulations
 14 prescribed by the Secretary or his delegate.

15 “(h) TAXES OF ATTORNEY-IN-FACT UNAFFECTED.—
 16 Nothing in this section shall increase or decrease the taxes
 17 imposed by this chapter on the income of the attorney-in-
 18 fact.”

19 ~~(102)~~~~(d)~~ *EXEMPTION FROM TAX.—Section 501(c)(15)*
 20 *(relating to exemption from tax of certain mutual insurance*
 21 *companies) is amended by striking out “\$75,000” and in*
 22 *lieu thereof inserting “\$150,000”.*

23 ~~(103)~~~~(d)~~ *(e) MUTUAL FIRE INSURANCE COMPANIES*
 24 *OPERATING ON BASIS OF PREMIUM DEPOSITS.—*

25 (1) APPLICATION OF SECTION 831(a).—Section

831 (a) (imposing a tax on certain mutual marine and fire insurance companies and on stock insurance companies which are not life insurance companies) is amended to read as follows:

“(a) IMPOSITION OF TAX.—Taxes computed as provided in section 11 shall be imposed for each taxable year or the taxable income of—

“(1) every insurance company (other than a life or mutual insurance company),

“(2) every mutual marine insurance company, and

“(3) every mutual fire (104)or flood insurance company—

“(A) exclusively issuing perpetual policies, or

“(B) whose principal business is the issuance of policies for which the premium deposits are the same, regardless of the length of the term for which the policies are written, if the unabsorbed portion of such premium deposits not required for losses, expenses, or establishment of reserves is returned or credited to the policyholder on cancellation or expiration of the policy.”

(2) TREATMENT OF UNABSORBED PREMIUM DEPOSITS.—Section 832 (b) (4) (relating to definition of premiums earned) is amended by adding at the end thereof the following new sentence: “For purposes of

1 this subsection, unearned premiums of mutual fire in-
 2 surance companies described in section 831 (a) (3) (B)
 3 means (with respect to the policies described in section
 4 831 (a) (3) (B)) the amount of unabsorbed premium
 5 deposits which the company would be obligated to re-
 6 turn to its policyholders at the close of the taxable year
 7 if all of its policies were terminated at such time; and
 8 the determination of such amount shall be based on the
 9 schedule of unabsorbed premium deposit returns for each
 10 such company then in effect.”

11 (3) CONFORMING AMENDMENT.—Section 832 (b)
 12 (1) (C) is amended by striking out “section 831 (a),”
 13 and inserting in lieu thereof “section 831 (a) (3) (A),”.

14 (4) ADJUSTMENT OF PREMIUM DEPOSIT.—Section
 15 832 (c) (11) is amended to read as follows:

16 “(11) dividends and similar distributions paid or
 17 declared to policyholders in their capacity as such, ex-
 18 cept in the case of a mutual fire insurance company de-
 19 scribed in section 831 (a) (3) (A). For purposes of
 20 the preceding sentence, the term ‘dividends and similar
 21 distributions’ includes amounts returned or credited to
 22 policyholders on cancellation or expiration of policies
 23 described in section 831 (a) (3) (B). For purposes of
 24 this paragraph, the term ‘paid or declared’ shall be con-
 25 strued according to the method of accounting regularly

employed in keeping the books of the insurance company; and”.

(5) ADDITIONAL ITEM OF INCOME.—Section 832 (b) (1) is amended by striking out “and” at the end of subparagraph (B), by striking out the period at the end of subparagraph (C) and inserting in lieu thereof “, and”, and by adding at the end thereof the following new subparagraph:

“(D) in the case of a mutual fire insurance company described in section 831 (a) (3) (B), an amount equal to 2 percent of the premiums earned on insurance contracts during the taxable year with respect to policies described in section 831 (a) (3) (B) after deduction of premium deposits returned or credited during the same taxable year.”

~~(105)(e)~~ (f) ELECTION OF CERTAIN MUTUAL COMPANIES TO BE TAXED ON TOTAL INCOME.—Section 831 is amended by redesignating subsection (c) as subsection (d), and by inserting after subsection (b) the following new subsection:

“(c) ELECTION FOR MULTIPLE LINE COMPANY TO BE TAXED ON TOTAL INCOME.—

“(1) IN GENERAL.—Any mutual insurance company engaged in writing marine, fire, and casualty insurance which for any 5-year period beginning after December 31, 1941, and ending before January 1, 1962,

1 was subject to the tax imposed by section 831 (or the
2 tax imposed by corresponding provisions of prior law)
3 may elect, in such manner and at such time as the
4 Secretary or his delegate may by regulations prescribe,
5 to be subject to the tax imposed by section 831, whether
6 or not marine insurance is its predominant source of
7 premium income.

8 “(2) EFFECT OF ELECTION.—If an election is
9 made under paragraph (1), the electing company shall
10 (in lieu of being subject to the tax imposed by section
11 821) be subject to the tax imposed by this section for
12 taxable years beginning after December 31, 1961.
13 Such election shall not be revoked except with the con-
14 sent of the Secretary or his delegate.”

15 **(106)(f) (g) TECHNICAL AMENDMENTS, ETC.—**

16 (1) CREDIT FOR FOREIGN TAXES.—Section 841
17 (relating to credit for foreign taxes) is amended
18 by striking out “and” at the end of paragraph (1), by
19 renumbering paragraph (2) as paragraph (3), and by
20 inserting after paragraph (1) the following new para-
21 graph:

22 “(2) in the case of the tax imposed by section
23 821 (a), the mutual insurance company taxable income
24 (as defined in section 821 (b)) ; and in the case of the

1 tax imposed by section 821 (c), the taxable investment
2 income (as defined in section 822 (a)), and”.

3 (2) ADJUSTMENTS TO BASIS FOR DEPRECIATION
4 SUSTAINED.—Section 1016 (a) (3) (relating to adjust-
5 ments to basis for depreciation, etc., sustained) is
6 amended by striking out “and” at the end of subpara-
7 graph (B), by inserting “and” at the end of sub-
8 paragraph (C), and by inserting after subparagraph
9 (C) the following new subparagraph:

10 “(D) since February 28, 1913, during which
11 such property was held by a person subject to tax
12 under part II of subchapter L (or the corresponding
13 provisions of prior income tax laws), to the extent
14 that paragraph (2) does not apply,”.

15 (3) ALTERNATIVE TAX ON CAPITAL GAINS.—
16 Section 1201 (a) (relating to alternative tax on corpo-
17 rations) is amended by striking out “821 (a) (1) or
18 (b),” and inserting in lieu thereof “821 (a) or (c),”.

19 ~~(107)(4) CLERICAL AMENDMENT.~~—The table of parts
20 for subchapter L is amended by striking out the portion
21 referring to part II and inserting in lieu thereof the
22 following:

“Part II. Mutual insurance companies (other than life and
certain marine insurance companies and other
than fire insurance companies which operate
on basis of perpetual policies or premium de-
posits).”

1 (4) *CLERICAL AMENDMENTS.*—,

2 (A) *The table of parts for subchapter L is*
 3 *amended by striking out the portion referring to part*
 4 *II and inserting in lieu thereof the following:*

“Part II. Mutual insurance companies (other than life and certain marine insurance companies and other than fire or flood insurance companies which operate on basis of perpetual policies or premium deposits).”

5 (B) *The heading to section 831 is amended to*
 6 *read as follows:*

7 “SEC. 831. TAX ON INSURANCE COMPANIES (OTHER THAN
 8 LIFE OR MUTUAL), MUTUAL MARINE INSURANCE
 9 COMPANIES, AND CERTAIN MUTUAL FIRE OR
 10 FLOOD INSURANCE COMPANIES.”

11 (C) *The table of sections for part III of sub-*
 12 *chapter L is amended by striking out the portion*
 13 *referring to section 831 and inserting in lieu*
 14 *thereof the following:*

“Sec. 831. Tax on insurance companies (other than life or mutual), mutual marine insurance companies, and certain mutual fire or flood insurance companies.”

15 (108)(g) (h) *EFFECTIVE DATE.*—The amendments made
 16 by this section (other than by subsection (109)(e) (f))
 17 shall apply with respect to taxable years beginning after
 18 December 31, 1962.

1 SEC. ~~(110)~~^H 9. DOMESTIC CORPORATIONS RECEIVING
 2 DIVIDENDS FROM FOREIGN CORPORA-
 3 TIONS.

4 ~~(111)~~^(a) ENTIRE AMOUNT OF FOREIGN TAX TO BE
 5 TAKEN INTO ACCOUNT.—

6 ~~(1)~~ DEFINITION OF ACCUMULATED PROFITS.—So
 7 much of paragraph ~~(1)~~ of section 902~~(c)~~ (relating to
 8 applicable rules for computing credit for corporate stock-
 9 holder in foreign corporation) as preceedes the semicolon
 10 is amended to read as follows:

11 “~~(1)~~ The term ‘accumulated profits’, when used in
 12 this section in reference to a foreign corporation, means
 13 the amount of its gains, profits, or income computed
 14 without reduction by the amount of the income, war
 15 profits, and excess profits taxes imposed on or with re-
 16 spect to such profits or income by any foreign country
 17 or any possession of the United States”.

18 ~~(2)~~ CONFORMING AMENDMENTS.—

19 ~~(A)~~ Section 902~~(a)~~ is amended by striking
 20 out “which the amount of such dividends bears to
 21 the amount of such accumulated profits” and insert-
 22 ing in lieu thereof “which the amount of such
 23 dividends (determined without regard to section

1 78) bears to the amount of such accumulated profits
2 in excess of such income, war profits, and excess
3 profits taxes (other than those deemed paid)".

4 ~~(B)~~ Section 902(b) is amended by striking
5 out "which the amount of such dividends bears to
6 the amount of such accumulated profits" and in-
7 serting in lieu thereof "which the amount of such
8 dividends bears to the amount of such accumulated
9 profits in excess of such income, war profits, and
10 excess profits taxes".

11 (a) *FOREIGN TAXES DEEMED PAID BY DOMESTIC*
12 *CORPORATIONS.*—Section 902 (relating to credit for
13 corporate stockholder in foreign corporations) is amended
14 to read as follows:

15 "SEC. 902. CREDIT FOR CORPORATE STOCKHOLDER IN FOREIGN
16 CORPORATION.

17 "(a) *TREATMENT OF TAXES PAID BY FOREIGN*
18 *CORPORATION.*—For purposes of this subpart, a domestic
19 corporation which owns at least 10 percent of the voting
20 stock of a foreign corporation from which it receives
21 dividends in any taxable year shall—

22 "(1) to the extent such dividends are paid by such
23 foreign corporation out of accumulated profits (as
24 defined in subsection (c)(1)(A)) of a year for which
25 such foreign corporation is not a less developed country

1 corporation, be deemed to have paid the same proportion
 2 of any income, war profits, or excess profits taxes paid
 3 or deemed to be paid by such foreign corporation to any
 4 foreign country or to any possession of the United
 5 States on or with respect to such accumulated profits,
 6 which the amount of such dividends (determined with-
 7 out regard to section 78) bears to the amount of such
 8 accumulated profits in excess of such income, war profits,
 9 and excess profits taxes (other than those deemed paid);
 10 and

11 “(2) to the extent such dividends are paid by such
 12 foreign corporation out of accumulated profits (as defined
 13 in subsection (c)(1)(B)) of a year for which such
 14 foreign corporation is a less developed country corpora-
 15 tion, be deemed to have paid the same proportion of any
 16 income, war profits, or excess profits taxes paid or deemed
 17 to be paid by such foreign corporation to any foreign
 18 country or to any possession of the United States on or
 19 with respect to such accumulated profits, which th-
 20 amount of such dividends bears to the amount of such
 21 accumulated profits.

22 “(b) FOREIGN SUBSIDIARY OF FOREIGN CORPORA-
 23 TION.—If such foreign corporation owns 50 percent or more
 24 of the voting stock of another foreign corporation from which
 25 it receives dividends in any taxable year, it shall be deemed to

1 have paid the same proportion of any income, war profits, or
 2 excess profits taxes paid by such other foreign corporation to
 3 any foreign country or to any possession of the United States,
 4 on or with respect to the accumulated profits of the corpora-
 5 tion from which such dividends were paid which—

6 “(1) for purposes of applying subsection (a)(1),
 7 the amount of such dividends bears to the amount of the
 8 accumulated profits (as defined in subsection (c)(1)
 9 (A)) of such other foreign corporation from which such
 10 dividends were paid in excess of such income, war profits,
 11 and excess profits taxes, or

12 “(2) for purposes of applying subsection (a)
 13 (2), the amount of such dividends bears to the amount
 14 of the accumulated profits (as defined in subsection
 15 (c)(1)(B)) of such other foreign corporation from
 16 which such dividends were paid.

17 “(c) *APPLICABLE RULES.*—

18 “(1) *ACCUMULATED PROFITS DEFINED.*—For
 19 purposes of this section, the term ‘accumulated profits’
 20 means with respect to any foreign corporation—

21 “(A) for purposes of subsections (a)(1) and
 22 (b)(1), the amount of its gains, profits, or income
 23 computed without reduction by the amount of the
 24 income, war profits, and excess profits taxes im-
 25 posed on or with respect to such profits or income

1 *by any foreign country or any possession of the*
2 *United States; and*

3 *“(B) for purposes of subsections (a)(2) and*
4 *(b)(2), the amount of its gains, profits, or income*
5 *in excess of the income, war profits, and excess*
6 *profits taxes imposed on or with respect to such*
7 *profits or income.*

8 *The Secretary or his delegate shall have full power*
9 *to determine from the accumulated profits of what year*
10 *or years such dividends were paid, treating dividends*
11 *paid in the first 60 days of any year as having been*
12 *paid from the accumulated profits of the preceding year*
13 *or years (unless to his satisfaction shown otherwise),*
14 *and in other respects treating dividends as having been*
15 *paid from the most recently accumulated gains, profits,*
16 *or earnings.*

17 *“(2) ACCOUNTING PERIODS.—In the case of a*
18 *foreign corporation, the income, war profits, and excess*
19 *profits taxes of which are determined on the basis of an*
20 *accounting period of less than 1 year, the word ‘year’*
21 *as used in this subsection shall be construed to mean such*
22 *accounting period.*

23 *“(d) LESS DEVELOPED COUNTRY CORPORATION*
24 *DEFINED.—For purposes of this section, the term ‘less de-*
25 *veloped country corporation’ means—*

1 “(1) a foreign corporation which, for its taxable
2 year, is a less developed country corporation within the
3 meaning of section 955(c) (1) or (2), and

4 “(2) a foreign corporation which owns 10 percent
5 or more of the total combined voting power of all classes
6 of stock entitled to vote of a foreign corporation which is
7 a less developed country corporation within the meaning
8 of section 955(c) (1), and—

9 “(A) 80 percent or more of the gross income
10 of which for its taxable year meets the requirement
11 of section 955(c) (1) (A); and

12 “(B) 80 percent or more in value of the assets
13 of which on each day of such year consists of prop-
14 erty described in section 955(c) (1) (B).

15 A foreign corporation which is a less developed country
16 corporation for its first taxable year beginning after December
17 31, 1962, shall, for purposes of this section, be treated as
18 having been a less developed country corporation for each
19 of its taxable years beginning before January 1, 1963.

20 “(e) CROSS REFERENCES.—

 “(1) For inclusion in gross income of an amount equal to taxes deemed paid under subsection (a)(1), see section 78.

 “(2) For application of subsections (a) and (b) with respect to taxes deemed paid in a prior taxable year by a United States shareholder with respect to a controlled foreign corporation, see section 960.

 “(3) For reduction of credit with respect to dividends paid out of accumulated profits for years for which certain information is not furnished, see section 6038.”

1 (b) INCLUSION IN GROSS INCOME OF AMOUNT
 2 EQUAL TO TAXES DEEMED PAID.—Part II of subchapter B
 3 of chapter 1 (relating to items specifically included in gross
 4 income) is amended by adding at the end thereof the fol-
 5 lowing new section:

6 “SEC. 78. DIVIDENDS RECEIVED FROM ~~(112)~~CERTAIN FOR-
 7 EIGN CORPORATIONS BY DOMESTIC CORPORA-
 8 TIONS CHOOSING FOREIGN TAX CREDIT.

9 “If a domestic corporation chooses to have the benefits
 10 of subpart A of part III of subchapter N (relating to foreign
 11 tax credit) for any taxable year, an amount equal to the
 12 taxes deemed to be paid by such corporation under section
 13 ~~(113)902~~ 902(a)(1) (relating to credit for corporate stock-
 14 holder in foreign corporation) or under section ~~(114)957(a)-~~
 15 960(a)(1)(C) (relating to taxes paid by foreign corpora-
 16 tion) for such taxable yera shall be treated for purposes
 17 of this title (other than section 245) as a dividend received
 18 by such domestic corporation from the foreign corporation.”

19 (c) DETERMINATION OF SOURCE OF DIVIDENDS RE-
 20 CEIVED FROM CERTAIN FOREIGN CORPORATIONS.—Section
 21 861(a)(2)(B) (relating to dividends from foreign corpo-
 22 rations treated as income from sources within the United
 23 States) is amended by striking out “to the extent exceeding
 24 the amount of the deduction allowable under section 245 in

1 respect of such dividends” and inserting in lieu thereof “to
 2 the extent exceeding the amount which is 100/85ths of the
 3 amount of the deduction allowable under section 245 in
 4 respect of such dividends”.

5 **(115)(d)** ~~REPEAL OF SECTION 902(d).~~—Subsection ~~(d)~~
 6 ~~(relating to special rules for certain wholly owned foreign~~
 7 ~~corporations)~~ is hereby repealed.

8 **(116)(e)** ~~(d)~~ TECHNICAL AMENDMENTS.—

9 (1) The table of sections for part II of subchapter
 10 B of chapter 1 is amended by adding at the end thereof
 11 the following:

“Sec. 78. Dividends received from **(117)** *certain* foreign
 corporations by domestic corporations choosing
 foreign tax credit.”

12 (2) Section 535 (b) (1) and the first sentence of
 13 section 545 (b) (1) are each amended by striking out
 14 “accrued during the taxable year,” and inserting in lieu
 15 thereof “accrued during the taxable year or deemed to
 16 be paid by a domestic corporation under section
 17 **(118)**~~902~~ 902(a)(1) or 960(a)(1)(C) for the tax-
 18 able year,”.

19 (3) Section 901 (d) is amended by adding the
 20 following new paragraph:

“(4) For reduction of credit for failure of a United
 States person to furnish certain information with re-
 spect to a foreign corporation controlled by him, see
 section 6038.”

(119)~~(4)~~ Section 902 is amended by striking out subsection ~~(e)~~ and inserting in lieu thereof the following:

~~“(d) CROSS REFERENCES.—~~

~~“(1) For inclusion in gross income of an amount equal to taxes deemed paid under this section, see section 78.~~

~~“(2) For reduction of credit with respect to dividends paid out of accumulated profits for years for which certain information is not furnished, see section 6038.”~~

(120)~~(f)~~ ~~(e)~~ EFFECTIVE DATE.—The amendments made by this section shall apply—

(1) in respect of any distribution received by a domestic corporation after December 31, 1964, and

(2) in respect of any distribution received by a domestic corporation before January 1, 1965, in a taxable year of such corporation beginning after December 31, 1962, but only to the extent that such distribution is made out of the accumulated profits of a foreign corporation for a taxable year (of such foreign corporation) beginning after December 31, 1962.

For purposes of paragraph (2), a distribution made by a foreign corporation out of its profits which are attributable to a distribution received from a foreign subsidiary to which section 902 (b) applies shall be treated as made out of the accumulated profits of a foreign corporation for a taxable

1 year beginning before January 1, 1963, to the extent that
 2 such distribution was paid out of the accumulated profits of
 3 such foreign subsidiary for a taxable year beginning before
 4 January 1, 1963.

5 **(121) SEC. 10. SEPARATE LIMITATION ON FOREIGN TAX CREDIT**

6 **WITH RESPECT TO CERTAIN INTEREST INCOME.**

7 *(a) LIMITATION ON FOREIGN TAX CREDIT.—Section*
 8 *904 (relating to limitations on foreign tax credit) is amended*
 9 *by redesignating subsection (f) as subsection (g) and by*
 10 *inserting after subsection (e) the following new subsection:*

11 *“(f) APPLICATION OF SECTION IN CASE OF CERTAIN*
 12 *INTEREST INCOME.—*

13 *“(1) IN GENERAL.—The provisions of subsections*
 14 *(a), (c), (d), and (e) of this section shall be applied*
 15 *separately with respect to—*

16 *“(A) the interest income described in paragraph*
 17 *(2), and*

18 *“(B) income other than the interest income de-*
 19 *scribed in paragraph (2).*

20 *“(2) INTEREST INCOME TO WHICH APPLICABLE.—*
 21 *For purposes of this subsection, the interest income de-*
 22 *scribed in this paragraph is interest other than interest—*

1 “(A) derived from any transaction which is
2 directly related to the active conduct of a trade or
3 business in a foreign country or a possession of the
4 United States,

5 “(B) derived in the conduct of a banking,
6 financing, or similar business,

7 “(C) received from a corporation in which the
8 taxpayer owns at least 10 percent of the voting
9 stock, or

10 “(D) received on obligations acquired as a
11 result of the disposition of a trade or business
12 actively conducted by the taxpayer in a foreign
13 country or possession of the United States or as a
14 result of the disposition of stock or obligations of a
15 corporation in which the taxpayer owned at least
16 10 percent of the voting stock.

17 “(3) OVERALL LIMITATION NOT TO APPLY.—The
18 limitation provided by subsection (a)(2) shall not ap-
19 ply with respect to the interest income described in para-
20 graph (2). The Secretary or his delegate shall by
21 regulations prescribe the manner of application of sub-
22 section (e) with respect to cases in which the limitation

1 provided by subsection (a)(2) applies with respect
2 to income other than the interest income described in para-
3 graph (2).

4 “(4) *TRANSITIONAL RULES FOR CARRYBACKS AND*
5 *CARRYOVERS.*—

6 “(A) *CARRYBACKS TO YEARS PRIOR TO REVE-*
7 *NUE ACT OF 1962.*—Where, under the provisions
8 of subsection (d), taxes (i) paid or accrued to any
9 foreign country or possession of the United States
10 in any taxable year beginning after the date of the
11 enactment of the Revenue Act of 1962 are deemed
12 (ii) paid or accrued in one or more taxable years
13 beginning on or before the date of enactment of the
14 Revenue Act of 1962, the amount of such taxes
15 deemed paid or accrued shall be determined without
16 regard to the provisions of this subsection. To the
17 extent the taxes paid or accrued to a foreign country
18 or possession of the United States in any taxable
19 year described in clause (i) are not, with the appli-
20 cation of the preceding sentence, deemed paid or
21 accrued in any taxable year described in clause (ii),
22 such taxes shall, for purposes of applying subsection
23 (d), be deemed paid or accrued in a taxable year
24 beginning after the date of the enactment of the
25 Revenue Act of 1962, with respect to interest

1 *income described in paragraph (2), and with re-*
2 *spect to income other than interest income described*
3 *in paragraph (2), in the same ratios as the amount*
4 *of such taxes paid or accrued with respect to inter-*
5 *est income described in paragraph (2), and the*
6 *amount of such taxes paid or accrued with respect to*
7 *income other than interest income described in*
8 *paragraph (2), respectively, bear to the total*
9 *amount of such taxes paid or accrued to such foreign*
10 *country or possession of the United States.*

11 “(B) CARRYOVERS TO YEARS AFTER REVE-
12 NUE ACT OF 1962.—Where, under the provisions of
13 subsection (d), taxes (i) paid or accrued to any for-
14 eign country or possession of the United States in
15 any taxable year beginning on or before the date
16 of the enactment of the Revenue Act of 1962 are
17 deemed (ii) paid or accrued in one or more taxable
18 years beginning after the date of the enactment of
19 the Revenue Act of 1962, the amount of such taxes
20 deemed paid or accrued in any year described in
21 clause (ii) shall, with respect to interest income
22 described in paragraph (2), be an amount which
23 bears the same ratio to the amount of such taxes
24 deemed paid or accrued as the amount of the taxes
25 paid or accrued to such foreign country or possession

1 for such year with respect to interest income de-
2 scribed in paragraph (2) bears to the total amount
3 of the taxes paid or accrued to such foreign country
4 or possession for such year; and the amount of such
5 taxes deemed paid or accrued in any year described
6 in clause (ii) with respect to income other than
7 interest income described in paragraph (2) shall
8 be an amount which bears the same ratio to the
9 amount of such taxes deemed paid or accrued for
10 such year as the amount of taxes paid or accrued
11 to such foreign country or possession for such year
12 with respect to income other than interest income
13 described in paragraph (2) bears to the total
14 amount of the taxes paid or accrued to such for-
15 eign country or possession for such year.”

16 (b) *EFFECTIVE DATE.*—The amendments made by
17 subsection (a) shall apply with respect to taxable years
18 beginning after the date of the enactment of this Act, but
19 only with respect to interest resulting from transactions con-
20 summated after April 2, 1962.

1 **SEC. (122) 11. EARNED INCOME FROM SOURCES WITH-**
 2 **OUT THE UNITED STATES.**

3 (a) **LIMITATION ON AMOUNT AND TYPE OF INCOME**
 4 **EXCLUDED.**—Section 911 (relating to earned income from
 5 sources without the United States) is amended to read as
 6 follows:

7 **“SEC. 911. EARNED INCOME FROM SOURCES WITHOUT**
 8 **THE UNITED STATES.**

9 “(a) **GENERAL RULE.**—The following items shall not
 10 be included in gross income and shall be exempt from taxa-
 11 tion under this subtitle:

12 “(1) **BONA FIDE RESIDENT OF FOREIGN COUN-**
 13 **TRY.**—In the case of an individual citizen of the United
 14 States who establishes to the satisfaction of the Secre-
 15 tary or his delegate that he has been a bona fide resident
 16 of a foreign country or countries for an uninterrupted
 17 period which includes an entire taxable year, amounts
 18 received from sources without the United States (except
 19 amounts paid by the United States or any agency there-
 20 of) which constitute earned income attributable to serv-

1 ices performed during such uninterrupted period. The
2 amount excluded under this paragraph for any taxable
3 year shall be computed by applying the special rules
4 contained in subsection (c).

5 “(2) PRESENCE IN FOREIGN COUNTRY FOR 17
6 MONTHS.—In the case of an individual citizen of the
7 United States who during any period of 18 consecutive
8 months is present in a foreign country or countries dur-
9 ing at least 510 full days in such period, amounts re-
10 received from sources without the United States (except
11 amounts paid by the United States or any agency
12 thereof) which constitute earned income attributable to
13 services performed during such 18-month period. The
14 amount excluded under this paragraph for any taxable
15 year shall be computed by applying the special rules
16 contained in subsection (c).

17 An individual shall not be allowed, as a deduction from his
18 gross income, any deductions (other than those allowed by
19 section 151, relating to personal exemptions) properly allo-
20 cable to or chargeable against amounts excluded from gross
21 income under this subsection.

22 “(b) DEFINITION OF EARNED INCOME.—For purposes
23 of this section, the term ‘earned income’ means wages, sal-
24 aries, or professional fees, and other amounts received as
25 compensation for personal services actually rendered, but

1 does not include that part of the compensation derived by
2 the taxpayer for personal services rendered by him to a
3 corporation which represents a distribution of earnings or
4 profits rather than a reasonable allowance as compensation
5 for the personal services actually rendered. In the case of
6 a taxpayer engaged in a trade or business in which both
7 personal services and capital are material income-producing
8 factors, under regulations prescribed by the Secretary or his
9 delegate, a reasonable allowance as compensation for the
10 personal services rendered by the taxpayer, not in excess of
11 30 percent of his share of the net profits of such trade or
12 business, shall be considered as earned income.

13 “(c) SPECIAL RULES.—For purposes of computing the
14 amount excludable under subsection (a), the following rules
15 shall apply:

16 “(1) LIMITATIONS ON AMOUNT OF EXCLUSION.—

17 The amount excluded from the gross income of an
18 individual under subsection (a) for any taxable year
19 shall not exceed an amount which shall be computed on
20 a daily basis at an annual rate of—

21 “(A) except as provided in subparagraph (B),
22 \$20,000 in the case of an individual who qualifies
23 under subsection (a), or

24 “(B) \$35,000 in the case of an individual who
25 qualifies under subsection (a) (1), but only with

1 respect to that portion of such taxable year occurring
2 after such individual has been a bona fide resident
3 of a foreign country or countries for an uninterrupted
4 period of 3 consecutive years.

5 “(2) **ATTRIBUTION TO YEAR IN WHICH SERVICES**
6 **ARE PERFORMED.**—For purposes of applying paragraph
7 (1), amounts received shall be considered received in
8 the taxable year in which the services to which the
9 amounts are attributable are performed.

10 “(3) **TREATMENT OF COMMUNITY INCOME.**—In
11 applying paragraph (1) with respect to amounts re-
12 ceived for services performed by a husband or wife
13 which are community income under community prop-
14 erty laws applicable to such income, the aggregate
15 amount excludable under subsection (a) from the gross
16 income of such husband and wife shall equal the amount
17 which would be excludable if such amounts did not con-
18 stitute such community income.

19 “(4) **REQUIREMENT AS TO TIME OF RECEIPT.**—
20 No amount received after the close of the taxable year
21 following the taxable year in which the services to which
22 the amounts are attributable are performed may be ex-
23 cluded under subsection (a).

24 “(5) **CERTAIN AMOUNTS NOT EXCLUDABLE.**—No
25 amount—

1 “(A) received as a pension or annuity, or

2 “(B) included in gross income by reason of
 3 section 402 (b) (relating to taxability of benefi-
 4 ciary of non-exempt trust), section 403 (c) (relat-
 5 ing to taxability of beneficiary under a non-quali-
 6 fied annuity), or section 403 (d) (relating to
 7 taxability of beneficiary under certain forfeitable
 8 contracts purchased by exempt organizations),
 9 may be excluded under subsection (a).

10 **(123)**“(6) *TEST OF BONA FIDE RESIDENCE.*—A state-
 11 ment by an individual who has earned income from
 12 sources within a foreign country to the authorities of that
 13 country that he is not a resident of that country, if he is
 14 held not subject as a resident of that country to the
 15 income tax of that country by its authorities with respect
 16 to such earnings, shall be conclusive evidence with respect
 17 to such earnings that he is not a bona fide resident of that
 18 country for purposes of subsection (a)(1).

19 **(124)**“(7) *CERTAIN NONCASH REMUNERATION.*—If an
 20 individual who qualifies under subsection (a)(1) receives
 21 compensation from sources without the United States
 22 (except from the United States or any agency thereof) in
 23 the form of the right to use property or facilities, the
 24 limitation under paragraph (1) applicable with respect
 25 to such individual—

1 “(A) for a taxable year ending in 1963, shall
2 be increased by an amount equal to the amount of
3 such compensation so received during such taxable
4 year;

5 “(B) for a taxable year ending in 1964, shall
6 be increased by an amount equal to two-thirds of
7 such compensation so received during such taxable
8 year; and

9 “(C) for a taxable year ending in 1965, shall
10 be increased by an amount equal to one-third of such
11 compensation so received during such taxable year.

12 “(d) CROSS REFERENCES.—

 “**For administrative and penal provisions relating to
the exclusion provided for in this section, see sections
6001, 6011, 6012(c), and the other provisions of subtitle F.**”

13 (b) COMPUTATION OF EMPLOYEES' CONTRIBU-
14 TIONS.—Section 72 (f) (relating to special rules for comput-
15 ing employees' contributions) is amended by adding after
16 paragraph (2) the following new sentences:

17 “Paragraph (2) shall not apply to amounts which were
18 contributed by the employer after December 31, 1962, and
19 which would not have been includible in the gross income of
20 the employee by reason of the application of section 911 if
21 such amounts had been paid directly to the employee at the
22 time of contribution. The preceding sentence shall not apply

1 to amounts which were contributed by the employer, as de-
 2 termined under regulations prescribed by the Secretary or his
 3 delegate, to provide pension or annuity credits, to the extent
 4 such credits are attributable to services performed before
 5 January 1, 1963, and are provided pursuant to pension or
 6 annuity plan provisions in existence on March 12, 1962,
 7 and on that date applicable to such services.”

8 **(125)(c) EFFECTIVE DATE.—**

9 ~~(1) IN GENERAL.—~~Except as provided in para-
 10 graph ~~(2)~~, the amendments made by this section shall
 11 apply to taxable years ending after December 31, 1962.

12 ~~(2) AMENDMENTS TO SECTION 911.—~~The amend-
 13 ment made by subsection ~~(a)~~ shall apply only with
 14 respect to amounts received after December 31, 1962,
 15 and which are attributable either to—

16 ~~(A)~~ services performed after such date; or

17 ~~(B)~~ services performed on or before such date;
 18 but only if on March 12, 1962, there existed
 19 no right ~~(whether forfeitable or nonforfeitable)~~ to
 20 receive such amounts.

21 **(c) EFFECTIVE DATES.—**

22 **(1) AMENDMENT TO SECTION 911.—**The amend-
 23 ment made by subsection (a) shall apply to taxable

1 *years ending after September 4, 1962, but only with*
 2 *respect to amounts—*

3 *(A) received after March 12, 1962, which*
 4 *are attributable to services performed after Decem-*
 5 *ber 31, 1962, or*

6 *(B) received after December 31, 1962, which*
 7 *are attributable to services performed on or before*
 8 *December 31, 1962, unless on March 12, 1962,*
 9 *there existed a right (whether forfeitable or non-*
 10 *forfeitable) to receive such amounts.*

11 *(2) AMENDMENT TO SECTION 72(f).—The amend-*
 12 *ment made by subsection (b) shall apply to taxable*
 13 *years ending after December 31, 1962.*

14 **(126)SEC. 13. CONTROLLED FOREIGN CORPORATIONS.**

15 ~~(a) IN GENERAL.~~—Part III of subchapter N of chapter
 16 ~~1~~ *(relating to income from sources without the United*
 17 *States)* is amended by adding at the end thereof the follow-
 18 *ing new subpart:*

19 **“Subpart F—Controlled Foreign Corporations**

 “Sec. 951. Amounts included in gross income of United
 States persons.

 “Sec. 952. Subpart F income defined.

 “Sec. 953. Investment of earnings in nonqualified property.

 “Sec. 954. Controlled foreign corporations.

 “Sec. 955. Rules for determining stock ownership.

 “Sec. 956. Exclusion from gross income of previously taxed
 earnings and profits.

 “Sec. 957. Special rules for foreign tax credit.

 “Sec. 958. Adjustments to basis of stock in controlled for-
 eign corporations and of other property.

1 **"SEC. 951. AMOUNTS INCLUDED IN GROSS INCOME OF**
 2 **UNITED STATES PERSONS.**

3 **~~"(a) AMOUNTS INCLUDED.—~~**

4 **~~"(1) IN GENERAL.—~~**If a foreign corporation is a
 5 controlled corporation on any day of a taxable year be-
 6 ginning after December 31, 1962, every United States
 7 person ~~(as defined in section 7701(a)(30))~~ who owns
 8 ~~(within the meaning of section 955(a))~~ stock in such
 9 corporation on the last day, in such year, on which such
 10 corporation is a controlled foreign corporation shall in-
 11 clude in his gross income, for his taxable year in which
 12 or with which such taxable year of the corporation
 13 ends—

14 **~~"(A) his pro rata share (determined under~~**
 15 **~~paragraph (2)) of the corporation's subpart F~~**
 16 **~~income for such year, and~~**

17 **~~"(B) his pro rata share (determined under~~**
 18 **~~section 953(a)(2)) of the corporation's increase~~**
 19 **~~in earnings invested in nonqualified property for~~**
 20 **~~such year (but only to the extent not excluded~~**
 21 **~~from gross income under section 956(a)(2)).~~**

22 **~~"(2) PRO RATA SHARE OF SUBPART F INCOME.—~~**

23 The pro rata share referred to in paragraph ~~(1)(A)~~
 24 in the case of any United States person is the amount—

25 **~~"(A) which would have been distributed with~~**

1 respect to the stock which such person owns (with-
 2 in the meaning of section 955(a)) in such cor-
 3 poration if on the last day, in its taxable year, on
 4 which the corporation is a controlled foreign cor-
 5 poration it had distributed pro rata to its share-
 6 holders an amount (i) which bears the same ratio
 7 to its subpart F income for the taxable year, as
 8 (ii) the part of such year during which the corpora-
 9 tion is a controlled foreign corporation bears to the
 10 entire year, reduced by

11 “(B) the amount of any distribution received
 12 by any other United States person during such
 13 year as a dividend with respect to such stock.

14 “(3) LIMITATION ON AMOUNT OF PRO RATA
 15 SHARE OF INVESTMENT IN NONQUALIFIED PROPERTY
 16 INCLUDED IN GROSS INCOME.—For purposes of para-
 17 graph (1)(B), the pro rata share of any United States
 18 person in the increase of the earnings of a controlled
 19 foreign corporation invested in nonqualified property
 20 shall not exceed an amount (A) which bears the same
 21 ratio to his pro rata share of such increase (as deter-
 22 mined under section 953(a)(2)) for the taxable
 23 year, as (B) the part of such year during which the
 24 corporation is a controlled foreign corporation bears to
 25 the entire year.

1 ~~“(b) LESS THAN 10 PERCENT OWNERSHIP.—~~No per-
 2 son shall be required to include any amount in gross income
 3 under subsection ~~(a)~~ unless he can be considered, by apply-
 4 ing the rules of ownership of section 955(b), as owning,
 5 directly or indirectly, on any day during the taxable year
 6 of the corporation on which it was a controlled foreign cor-
 7 poration, 10 percent or more of the total combined voting
 8 power of all classes of stock, or of the total value of shares
 9 of all classes of stock, of such corporation.

10 ~~“(c) COORDINATION WITH ELECTION OF A FOREIGN~~
 11 INVESTMENT COMPANY TO DISTRIBUTE INCOME.—A
 12 United States person who, for his taxable year, is a qualified
 13 shareholder ~~(within the meaning of section 1247(c))~~ of a
 14 foreign investment company with respect to which an elec-
 15 tion under section 1247 is in effect shall not be required to
 16 include in gross income, for such taxable year, subpart F
 17 income of such company.

18 **“SEC. 952. SUBPART F INCOME DEFINED.**

19 ~~“(a) IN GENERAL.—~~

20 ~~“(1) ITEMS TAKEN INTO ACCOUNT.—~~For purposes
 21 of this subpart, the term ‘subpart F income’ means, in
 22 the case of any controlled foreign corporation, the sum
 23 of—

1 ~~“(A) income derived from insurance of United~~
 2 ~~States risks (as determined under subsection (b))~~;

3 ~~“(B) income from United States patents,~~
 4 ~~copyrights, and exclusive formulas and processes~~
 5 ~~(as determined under subsection (c))~~; and

6 ~~“(C) the net foreign base company income~~
 7 ~~(as determined under subsection (d))~~; except that
 8 this subparagraph shall apply only in the case of a
 9 controlled foreign corporation in which 5 or fewer
 10 United States persons own, by applying the rules of
 11 ownership of section 955(b), more than 50 percent
 12 of the total combined voting power of all classes of
 13 stock entitled to vote.

14 ~~“(2) EXCLUSION OF UNITED STATES INCOME.—~~

15 Subpart F income does not include any item includible
 16 in gross income under this chapter (other than this sub-
 17 part) as income derived from sources within the United
 18 States of a foreign corporation engaged in trade or
 19 business in the United States.

20 ~~“(3) NOT TO EXCEED EARNINGS AND PROFITS.—~~

21 The subpart F income of any controlled foreign corpora-
 22 tion for any taxable year shall not exceed the earnings
 23 and profits of such corporation for such year.

24 ~~“(b) INCOME FROM INSURANCE OF UNITED STATES~~
 25 ~~RISKS.—~~

1 ~~“(1) GENERAL RULE.—~~If a controlled foreign cor-
 2 poration receives premiums or other consideration in
 3 respect of any reinsurance or the issuing of any insurance
 4 or annuity contract—

5 ~~“(A) in connection with property in, or resi-~~
 6 dents of, the United States, or

7 ~~“(B) in connection with property not in, or~~
 8 nonresidents of, the United States as the result of
 9 any arrangement whereby another corporation re-
 10 ceives a substantially equal amount of premiums or
 11 other consideration in respect of any reinsurance or
 12 the issuing of any insurance or annuity contract in
 13 connection with property in, or residents of, the
 14 United States,

15 then for purposes of subsection ~~(a)(1)(A)~~, the term
 16 ‘income derived from the insurance of United States
 17 risks’ means that income which ~~(subject to the modifi-~~
 18 cations provided by subparagraphs ~~(A)~~, ~~(B)~~, and ~~(C)~~
 19 of paragraph ~~(2)~~) would be taxed under subchapter L
 20 of this chapter if such corporation were a domestic
 21 corporation.

22 ~~“(2) SPECIAL RULES.—For purposes of paragraph~~
 23 ~~(1)—~~

24 ~~“(A) In the application of part I of subchapter~~

1 L, life insurance company taxable income is the
2 gain from operations as defined in section 809(b).

3 “(B) A corporation which would, if it were a
4 domestic corporation, be taxable under part II of
5 subchapter L shall apply paragraph (1) as if it
6 were taxable under part III of subchapter L.

7 “(C) The following provisions of subchapter L
8 shall not apply:

9 “(i) Section 809(d)(4) (operations loss
10 deduction).

11 “(ii) Section 809(d)(5) (certain non-
12 participating contracts).

13 “(iii) Section 809(d)(6) (group life,
14 accident, and health insurance).

15 “(iv) Section 809(d)(10) (small business
16 deduction).

17 “(v) Section 817(b) (gain on property
18 held on December 31, 1958, and certain sub-
19 stituted property acquired after 1958).

20 “(vi) Section 832(b)(5) (certain capital
21 losses).

22 “(D) ‘Gross amount’ to the extent provided in
23 section 809(c) (1) and (2), less ‘increase in
24 certain reserves’ as defined in section 809(d)(2),
25 and ‘premiums earned’ as defined in section 832(b)

~~(4)~~ shall be taken into account only to the extent they are in respect of any reinsurance or the issuing of any reinsurance or the issuing of any insurance or annuity contract described in paragraph ~~(1)~~.

~~“(E)~~ All items of income ~~(other than those taken into account under subparagraph (D))~~ and all items of expenses, losses, and deductions shall be properly allocated or apportioned under regulations prescribed by the Secretary or his delegate.

~~“(c) INCOME FROM UNITED STATES PATENTS, COPYRIGHTS, AND EXCLUSIVE FORMULAS AND PROCESSES.—~~

~~“(1) GENERAL RULE.—~~For purposes of subsection ~~(a)(1)(B)~~, the term ‘income from United States patents, copyrights, and exclusive formulas and processes’, means the amount of gross rentals, royalties, or other income derived from the license, sublicense, sale, exchange, use, or other means of exploitation of patents, copyrights, and exclusive formulas and processes—

~~“(A)~~ substantially developed, created, or produced in the United States, or

~~“(B)~~ acquired from any United States person which, directly or indirectly, owns or controls, or is owned or controlled by, or is under common ownership or control with, the controlled foreign corporation,

1 less the cost and expense allowance defined in para-
2 graph (2).

3 “(2) COST AND EXPENSE ALLOWANCE.—An al-
4 lowance shall be made, in accordance with regulations
5 prescribed by the Secretary or his delegate, for ordinary
6 and necessary expenses incurred by the controlled foreign
7 corporation in the receipt or production of the income
8 described in paragraph (1), including taxes and any
9 amortization or depreciation of the cost to such corpo-
10 ration of such property or rights described in paragraph
11 (1), but not including any production, manufacturing,
12 or similar expenses incurred in the use or other means
13 of exploitation of such property or rights.

14 “(3) DETERMINATION OF INCOME FROM USE.—
15 The income from use or other means of exploitation by
16 the controlled foreign corporation of the property or
17 right described in paragraph (1) shall be the amount
18 which would be obtained as a gross rent, royalty, or
19 other payment in an arm's length transaction with an
20 unrelated person for similar use or exploitation, of the
21 property or right.

22 “(d) NET FOREIGN BASE COMPANY INCOME.—For
23 purposes of subsection (a)(1)(C), the term ‘net foreign
24 base company income’ means—

25 “(1) the foreign base company income for the tax-

able year, determined under subsection (e), reduced
by

~~“(2) the increase in investment in qualified prop-
erty in less developed countries for the taxable year,
determined under subsection (f).~~

~~“(c) FOREIGN BASE COMPANY INCOME.—~~

~~“(1) IN GENERAL.—For purposes of subsection
(d)(1), the term ‘foreign base company income’ means
the foreign personal holding company income (as de-
fined in section 553) for the taxable year, modified and
adjusted as provided in this subsection.~~

~~“(2) CERTAIN SALES INCOME INCLUDED.—The
term ‘foreign base company income’ includes foreign
base company sales income if, for the taxable year, such
income is equal to at least 20 percent of the gross income
of the foreign corporation (not including for this purpose
other foreign base company income under this subsec-
tion). For purposes of this paragraph, the term ‘foreign
base company sales income’ means income (whether in
the form of profits, commissions, fees, or otherwise)
derived in connection with the purchase of personal
property from a related person and its sale to any per-
son, or the purchase of personal property from any
person and its sale to a related person, where—~~

~~“(A) the property which is purchased is manu-~~

1 factured, produced, grown, or extracted outside
2 the country under the laws of which the controlled
3 foreign corporation is created or organized, and

4 “(B) the property is sold for use, consumption,
5 or disposition outside such foreign country.

6 For purposes of the preceding sentence, a person is a
7 related person with respect to the controlled foreign
8 corporation if he, directly or indirectly, owns or con-
9 trols, or is owned or controlled by, or is under common
10 ownership or control with, the controlled foreign
11 corporation.

12 “(3) RENTS INCLUDED WITHOUT REGARD TO 50-
13 PERCENT LIMITATION.—All rents shall be included in
14 foreign base company income without regard to whether
15 or not such rents constitute more than 50 percent of
16 gross income.

17 “(4) INSURANCE AND PATENT INCOME EX-
18 CLUDED.—The term ‘foreign base company income’ does
19 not include any income derived from insurance of United
20 States risks (as determined under subsection (b)) or
21 income from United States patents, copyrights, and ex-
22 clusive formulas and processes (as determined under
23 subsection (c)).

24 “(5) INCOME OF CERTAIN BANKS AND BANK-

1 CONTROLLED CORPORATIONS EXCLUDED.—The term
2 ‘foreign base company income’ does not include—

3 “(A) the income of any corporation de-
4 scribed in section 552(b) (relating to excep-
5 tion for banks and exempt corporations), or

6 “(B) the income of any foreign corporation
7 if 50 percent or more of the fair market value of
8 its outstanding stock is owned directly or indirectly
9 by a domestic corporation which is either organ-
10 ized under section 25(a) of the Federal Reserve
11 Act (12 U.S.C., secs. 611–631), or has an agree-
12 ment or understanding with the Board of Gover-
13 nors of the Federal Reserve System under section
14 25 of the Federal Reserve Act (12 U.S.C., secs.
15 601–604), if all of the stock (except qualifying
16 shares) of the domestic corporation is owned by a
17 national or State bank which is a member of the
18 Federal Reserve System.

19 “(6) SPECIAL RULE WHERE FOREIGN BASE COM-
20 PANY INCOME IS LESS THAN 20 PERCENT OR MORE
21 THAN 80 PERCENT OF GROSS INCOME.—For purposes
22 of this subsection—

23 “(A) If the foreign base company income
24 (determined without regard to paragraph (7))

1 is less than 20 percent of gross income, no part of
 2 the gross income of the taxable year shall be
 3 treated as foreign base company income.

4 “(B) If the foreign base company income
 5 (determined without regard to paragraph (7))
 6 exceeds 80 percent of gross income, the entire
 7 gross income of the taxable year shall be taken
 8 into account in determining foreign base company
 9 income.

10 “(7) DEDUCTIONS TO BE TAKEN INTO AC-
 11 COUNT.—The foreign base company income for the tax-
 12 able year shall be reduced so as to take into account
 13 deductions (including taxes) properly allocable to such
 14 income.

15 “(f) INVESTMENT IN QUALIFIED PROPERTY IN LESS
 16 DEVELOPED COUNTRIES.—

17 “(1) GENERAL RULE.—For purposes of subsection
 18 (d)(2), the increase in investment in qualified property
 19 in less developed countries for any taxable year is the
 20 amount by which—

21 “(A) the aggregate amount of property de-
 22 scribed in sections 953(b)(2) (C) and (D) and
 23 property (including money) which is located out-
 24 side the United States and is ordinary and necessary
 25 for the active conduct of a qualified trade or business

described in section 953(b)(3)(A)(ii) held at the close of the taxable year, exceeds

“(B) the aggregate amount of property described in subparagraph (A) held at the close of the preceding taxable year.

“(2) INVESTMENTS AFTER CLOSE OF YEAR.—

Under regulations prescribed by the Secretary or his delegate, a controlled foreign corporation may elect to make the determinations under subparagraphs (A) and (B) of paragraph (1) as of the close of the 75th day after the close of each taxable year.

“(3) AMOUNT ATTRIBUTABLE TO PROPERTY.—

The amount taken into account under paragraph (1) with respect to any property shall be its adjusted basis, reduced by any liability to which the property is subject.

“SEC. 953. INVESTMENT OF EARNINGS IN NONQUALIFIED PROPERTY.

“(a) GENERAL RULES.—For purposes of this subpart—

“(1) AMOUNT OF INVESTMENT.—The amount of earnings of a controlled foreign corporation invested in nonqualified property at the close of any taxable year is the aggregate amount of such property held at the close of the taxable year, to the extent such amount does not exceed the sum of (A) the earnings and profits for the taxable year, and (B) the earnings and profits

1 accumulated for prior taxable years beginning after
2 December 31, 1962.

3 “(2) PRO RATA SHARE OF INCREASE FOR YEAR.—

4 In the case of any United States person, the pro rata
5 share of the increase for any taxable year in the earn-
6 ings of a controlled foreign corporation invested in a
7 nonqualified property is the amount determined by sub-
8 tracting—

9 “(A) his pro rata share of the amount deter-
10 mined under paragraph (1) for the close of the
11 preceding taxable year, reduced by amounts paid
12 during the taxable year to which section 956(c)(1)
13 applies, from

14 “(B) his pro rata share of the amount deter-
15 mined under paragraph (1) for the close of the
16 taxable year.

17 “(3) AMOUNT ATTRIBUTABLE TO PROPERTY.—

18 The amount taken into account under paragraph (1) or
19 (2) with respect to any property shall be its adjusted
20 basis, reduced by any liability to which the property
21 is subject.

22 “(b) NONQUALIFIED PROPERTY DEFINED.—For pur-
23 poses of this subpart—

24 “(1) GENERAL RULE.—The term ‘nonqualified

property' means any money or other property (tangible or intangible) acquired after December 31, 1962, which is not qualified property.

“(2) QUALIFIED PROPERTY.—The term ‘qualified property’ means—

“(A) Any money or other property which is located outside the United States and is ordinary and necessary for the active conduct of a qualified trade or business (as determined under paragraph (3)) carried on by the controlled foreign corporation.

“(B) Property which would qualify under subparagraph (A) except for the fact that it is located in the United States, but only if such property is—

“(i) obligations of the United States, money, or deposits with persons carrying on the banking business;

“(ii) property purchased in the United States for export to, or for use in, foreign countries; or

“(iii) any loan arising in connection with the sale of property if the amount of such loan outstanding at no time during the taxable year exceeds the amount which would be ordinary

1 and necessary to carry on the trade or business
2 of both the lending corporation and the borrow-
3 ing United States person had the sale been
4 made between unrelated persons.

5 “(C) Stock owned by the controlled foreign
6 corporation in another controlled foreign corpora-
7 tion in which it owns at least 10 percent of the vot-
8 ing stock and 10 percent of the value of all classes of
9 stock and in which it together with four or fewer
10 United States persons, owns, directly or indirectly,
11 more than 50 percent of the voting stock (unless
12 under the laws of a less developed country such per-
13 centage of ownership is not permitted, in which
14 case such lesser percentage as is permitted); but this
15 subparagraph shall apply only if—

16 “(i) substantially all of the property of
17 such other controlled foreign corporation is or-
18 dinary and necessary for the active conduct of
19 a trade or business engaged in by it almost
20 wholly within a less developed country or
21 countries, and

22 “(ii) such other controlled foreign cor-
23 poration is created or organized under the laws
24 of one of such countries in which it is so en-
25 gaged.

1 “(D) Any investment which is required
2 because of restrictions imposed by a less developed
3 country, and any investment which, when made,
4 was so required and which would result in substan-
5 tial losses if withdrawn.

6 ~~“(3) QUALIFIED TRADE OR BUSINESS.—~~

7 ~~“(A) A trade or business is a qualified trade or~~
8 ~~business if such trade or business (or substantially~~
9 ~~the same trade or business)—~~

10 ~~“(i) is carried on by the controlled foreign~~
11 ~~corporation outside the United States and has~~
12 ~~been so carried on by such corporation, while~~
13 ~~controlled by substantially the same United~~
14 ~~States persons since December 31, 1962, or~~
15 ~~during the 5-year period ending with the close~~
16 ~~of the preceding taxable year, or~~

17 ~~“(ii) is carried on by the controlled foreign~~
18 ~~corporation almost wholly within a less devel-~~
19 ~~oped country or countries.~~

20 ~~“(B) A trade or business which is a qualified~~
21 ~~trade or business for a corporation in which the~~
22 ~~controlled foreign corporation owns at least 80 per-~~
23 ~~cent of the total combined voting power of all classes~~
24 ~~of stock entitled to vote and at least 80 percent of~~

1 the total value of all classes of stock shall be treated
2 as a qualified trade or business for the controlled
3 foreign corporation if such percentage of stock was
4 owned continuously since December 31, 1962, or
5 during the 5-year period ending with the close of
6 the preceding taxable year.

7 “(4) SITUS OF CERTAIN PROPERTY.—Property
8 which is an obligation of, or pledges and guarantees
9 made with respect to obligations of, United States persons
10 shall be considered as property located in the United
11 States.

12 “(5) LESS DEVELOPED COUNTRY DEFINED.—The
13 term ‘less developed country’ means (in respect of any
14 foreign corporation) any foreign country (other than
15 an area within the Sino-Soviet bloc) or any possession
16 of the United States, with respect to which on the first
17 day of the taxable year, there is in effect an Executive
18 order by the President of the United States designating
19 such country or possession as an economically less de-
20 veloped country for purposes of this subpart. For pur-
21 poses of the preceding sentence, an oversea territory,
22 department, province, or possession may be treated as

a separate country. No designation shall be made under this paragraph with respect to—

Australia	Liechtenstein
Austria	Luxembourg
Belgium	Monaco
Canada	Netherlands
Denmark	New Zealand
France	Norway
Germany (Federal Republic)	Union of South Africa
Hong Kong	San Marino
Italy	Sweden
Japan	Switzerland
	United Kingdom

“SEC. 954. CONTROLLED FOREIGN CORPORATIONS.

“(a) **GENERAL RULE.**—For purposes of this subpart, the term ‘controlled foreign corporation’ means any foreign corporation of which more than 50 percent of the total combined voting power of all classes of stock entitled to vote is owned, directly or indirectly (within the meaning of section 955(b)), by United States persons on any day during the taxable year of such foreign corporation.

1 “(b) SPECIAL RULE FOR INSURANCE.—For purposes
2 only of taking into account income described in section
3 ~~952(a)(1)(A)~~ (relating to income derived from insurance
4 of United States risks), the term ‘controlled foreign corpora-
5 tion’ includes not only a foreign corporation as defined by
6 subsection (a) but also one of which more than 25 percent
7 of the total combined voting power of all classes of stock is
8 owned, directly or indirectly (within the meaning of sec-
9 tion ~~955(b)~~), by United States persons on any day dur-
10 ing the taxable year of such corporation, if the gross amount
11 of premiums or other consideration in respect of reinsurance
12 or the issuing of insurance or annuity contracts in connec-
13 tion with property in, or residents of, the United States, ex-
14 ceeds 75 percent of the gross amount of all premiums or
15 other consideration in respect of all risks.

16 “(c) SPECIAL RULE FOR CERTAIN LESS DEVELOPED
17 COUNTRIES.—In the case of any foreign corporation to
18 which section ~~953(b)(2)(C)~~ applies, the maximum per-
19 centage of ownership permitted under the laws of a less
20 developed country shall be considered, in lieu of the more
21 than 50 percent requirement in subsection (a), the per-
22 centage required under subsection (a) in order for the cor-
23 poration to be classified as a controlled foreign corporation.

1 **"SEC. 955. RULES FOR DETERMINING STOCK OWNERSHIP.**

2 ~~"(a)~~ FOR PURPOSES OF SECTION 951(a).—

3 ~~"(1)~~ GENERAL RULE.—For purposes of section
4 951(a), stock owned means—

5 ~~"(A)~~ stock owned directly, and

6 ~~"(B)~~ stock owned with the application of para-
7 graph (2).

8 ~~"(2)~~ STOCK OWNERSHIP THROUGH FOREIGN EN-
9 TITIES.—For purposes of subparagraph (B) of para-
10 graph (1), stock owned, directly or indirectly, by or
11 for a foreign corporation, foreign partnership, or foreign
12 trust or foreign estate (within the meaning of section
13 7701(a)-(31)) shall be considered as being owned pro-
14 portionately by its shareholders, partners, or benefici-
15 aries. Stock considered to be owned by a person by rea-
16 son of the application of the preceding sentence shall, for
17 purposes of applying such sentence, be treated as actually
18 owned by such person.

19 ~~"(3)~~ SPECIAL RULE FOR MUTUAL INSURANCE
20 COMPANIES.—For purposes of applying paragraph (1)
21 in the case of a foreign mutual insurance company, the
22 term 'stock' shall include any certificate entitling the
23 holder to voting power in the corporation.

1 “(b) OTHER PROVISIONS.—For purposes of sections 951
 2 ~~(b)~~, 952(a)(1)(C), and 954, section 318(a) ~~(relating to~~
 3 constructive ownership of stock) shall apply to the extent
 4 that the effect is to subject a United States person to the
 5 requirement of section 951(a), to treat 5 or fewer United
 6 States persons as owning more than 50 percent of all classes
 7 of stock entitled to vote of a controlled foreign corporation,
 8 or to make a foreign corporation a controlled foreign cor-
 9 poration under section 954, except—

10 “(1) In applying paragraph ~~(1)(A)~~ of section
 11 318(a), stock owned by a nonresident alien individual
 12 ~~(other than a foreign trust or foreign estate)~~ shall not
 13 be considered as owned by a citizen or by a resident
 14 alien individual.

15 “(2) In applying the first sentence of subpara-
 16 graphs ~~(A)~~ and ~~(B)~~, and in applying clause (i) of
 17 subparagraph ~~(C)~~, of section 318(a)(2)—

18 “~~(A)~~ if a partnership, estate, trust, or corpora-
 19 tion owns, directly or indirectly, more than 50 per-
 20 cent of the total combined voting power of all classes
 21 of stock entitled to vote of a corporation, it shall be
 22 considered as owning all the stock entitled to vote,
 23 and

24 “~~(B)~~ if a partnership, estate, trust, or corpora-
 25 tion owns, directly or indirectly, more than 50 per-

cent of the total value of shares of all classes of stock of a corporation, it shall be considered as owning the total value of all of the outstanding stock of such corporation. The application of this subparagraph shall not have the effect of increasing voting power of a partner, beneficiary, or shareholder, for purposes of subparagraph (A).

“(3) Stock owned by a partnership, estate, trust, or corporation, by reason of the application of the second sentence of subparagraphs (A) and (B), and the application of clause (ii) of subparagraph (C), of section 318(a)(2), shall not be considered as owned by such partnership, estate, trust, or corporation, for the purposes of applying the first sentence of subparagraphs (A) and (B), and in applying clause (i) of subparagraph (C), of section 318(a)(2).

“(4) In applying clause (i) of subparagraph (C) of section 318(a)(2), the 50-percent limitation contained in subparagraph (C) shall not apply.

“SEC. 956. EXCLUSION FROM GROSS INCOME OF PREVIOUSLY TAXED EARNINGS AND PROFITS.

(a) **EXCLUSION FROM GROSS INCOME OF UNITED STATES PERSONS.**—For purposes of this chapter, the earnings and profits for a taxable year of a foreign corporation attributable to amounts which are, or have been, included in

1 the gross income of a United States person under section
2 951(a) shall not, when—

3 “(1) such amounts are distributed to, or

4 “(2) such amounts would, but for this subsection,
5 be included under section 951(a)(1)(B) in the gross
6 income of,

7 such person (or any other United States person who acquires
8 from any person any portion of the interest of such United
9 States person in such foreign corporation, but only to the ex-
10 tent of such portion, and subject to such proof of the identity
11 of such interest as the Secretary or his delegate may by regu-
12 lations prescribe) directly, or indirectly through a chain of
13 ownership described under section 955(a), be again included
14 in the gross income of such United States person (or of such
15 other United States person).

16 “(b) EXCLUSION FROM GROSS INCOME OF CERTAIN
17 FOREIGN SUBSIDIARIES.—For purposes of section 951(a),
18 the earnings and profits for a taxable year of a controlled
19 foreign corporation attributable to amounts which are, or
20 have been, included in the gross income of a United States
21 person under section 951(a), shall not, when distributed
22 through a chain of ownership described under section 955
23 (a), be also included in the gross income of another con-
24 trolled foreign corporation in such chain for purposes of the
25 application of section 951(a) to such other controlled foreign

1 corporation with respect to such United States person ~~(or to~~
 2 any other United States person who acquires from any per-
 3 son any portion of the interest of such United States person
 4 in the controlled foreign corporation, but only to the extent of
 5 such portion, and subject to such proof of identity of such
 6 interest as the Secretary or his delegate may prescribe by
 7 regulations).

8 “~~(c)~~ ALLOCATIONS OF DISTRIBUTIONS.—For purposes
 9 of subsections ~~(a)~~ and ~~(b)~~, section 316~~(a)~~ shall be ap-
 10 plied by applying paragraph ~~(2)~~ thereof, and then para-
 11 graph ~~(1)~~ thereof—

12 “~~(1)~~ first to earnings and profits attributable to
 13 amounts included in gross income under section 951
 14 ~~(a)(1)(B)~~ ~~(or which would have been included except~~
 15 ~~for section 956(a)(2))~~;

16 “~~(2)~~ then to earnings and profits attributable to
 17 amounts included in gross income under section 951~~(a)~~
 18 ~~(1)(A)~~ ~~(but reduced by amounts not included under~~
 19 ~~section 951(a)(1)(B) because of the exclusion in sec-~~
 20 ~~tion 956(a)(2))~~; and

21 “~~(3)~~ then to other earnings and profits.

22 “~~(d)~~ DISTRIBUTIONS EXCLUDED FROM GROSS IN-
 23 COME NOT TO BE TREATED AS DIVIDENDS.—Except as
 24 provided in section 957~~(a)(3)~~, any distribution excluded
 25 from gross income under subsection ~~(a)~~ shall be treated, for

1 purposes of this chapter, as a distribution which is not a
2 dividend.

3 **"SEC. 957. SPECIAL RULES FOR FOREIGN TAX CREDIT.**

4 **~~"(a)~~ TAXES PAID BY A FOREIGN CORPORATION.—**

5 **~~"(1)~~ GENERAL RULE.—**For purposes of subpart A
6 of this part, if there is included, under section 951(a),
7 in the gross income of a domestic corporation any
8 amount attributable to earnings and profits—

9 **~~"(A)~~** of a foreign corporation at least 10 per-
10 cent of the voting stock of which is directly owned
11 by such domestic corporation; or

12 **~~"(B)~~** of a foreign corporation at least 50 per-
13 cent of the voting stock of which is directly owned
14 by a foreign corporation at least 10 percent of the
15 voting stock of which is in turn directly owned by
16 such domestic corporation;

17 then, under regulations, prescribed by the Secretary or
18 his delegate, such domestic corporation shall be deemed
19 to have paid the same proportion of the total income,
20 war profits, and excess profits taxes paid (or deemed
21 paid, if, paragraph (4) applies) to a foreign country
22 or possession of the United States for the taxable year
23 which the amount of earnings and profits of such foreign
24 corporation so included in gross income of the domestic
25 corporation bears to the entire amount of the total earn-

ings and profits of such foreign corporation for such taxable year.

~~“(2) TAXES PREVIOUSLY DEEMED PAID BY DOMESTIC CORPORATION.~~—If a domestic corporation receives a distribution from a foreign corporation, any portion of which is excluded from gross income under section 956, the income, war profits, and excess profits taxes paid or deemed paid by such foreign corporation to any foreign country or to any possession of the United States in connection with the earnings and profits of such foreign corporation from which such distribution is made shall not be taken into account for purposes of section 902, to the extent such taxes were deemed paid by such domestic corporation under paragraph (1) for any prior taxable year.

~~“(3) TAXES PAID BY FOREIGN CORPORATION AND NOT PREVIOUSLY DEEMED PAID BY DOMESTIC CORPORATION.~~—Any portion of a distribution from a foreign corporation received by a domestic corporation which is excluded from gross income under section 956(a) shall be treated by the domestic corporation as a dividend, solely for purposes of taking into account under section 902 any income, war profits, or excess profits taxes paid to any foreign country or to any possession of the United States, on or with respect to the accumulated profits of

1 such foreign corporation from which such distribution is
 2 made, which were not deemed paid by the domestic
 3 corporation under paragraph (1) for any prior taxable
 4 year.

5 “(4) TAXES PAID BY A FOREIGN SUBSIDIARY.—If
 6 subparagraph (A) of paragraph (1) applies with re-
 7 spect to an amount included in gross income under sec-
 8 tion 951(a) for a taxable year, then such amount shall
 9 be considered a dividend for purpose of the application
 10 of section 902(b).

11 (5) INCLUSION IN GROSS INCOME.—

“For inclusion in gross income of amount equal to
 taxes deemed paid under paragraph (1), see section 78.

12 “(b) SPECIAL RULES FOR FOREIGN TAX CREDIT IN
 13 YEAR OF RECEIPT OF PREVIOUSLY TAXED EARNINGS AND
 14 PROFITS.—

15 “(1) INCREASE IN SECTION 904 LIMITATION.—In
 16 the case of any taxpayer who—

17 “(A) either (i) chose to have the benefits of
 18 subpart A of this part for a taxable year in which
 19 he was required under section 951(a) to include in
 20 his gross income an amount in respect of a con-
 21 trolled foreign corporation, or (ii) did not pay or
 22 accrue for such taxable year any income, war profits

1 or excess profits taxes to any foreign country or to
2 any possession of the United States, and

3 “(B) chooses to have the benefits of subpart
4 A of this part for the taxable year in which he re-
5 ceives a distribution or amount which is excluded
6 from gross income under section 956(a) and which
7 is attributable to earnings and profits of the con-
8 trolled foreign corporation which was included in
9 his gross income for the taxable year referred to in
10 subparagraph (A), and

11 “(C) for the taxable year in which such dis-
12 tribution or amount is received, pays, or is deemed
13 to have paid, or accrues income, war profits, or ex-
14 cess profits taxes to a foreign country or to any
15 possession of the United States with respect to such
16 distribution or amount,

17 the applicable limitation under section 904 for the tax-
18 able year in which such distribution or amount is re-
19 ceived shall be increased as provided in paragraph (2),
20 but such increase shall not exceed the amount of such
21 taxes paid, or deemed paid, or accrued with respect
22 to such distribution or amount.

23 “(2) AMOUNT OF INCREASE.—The amount of in-

1 crease of the applicable limitation under section 904(a)
 2 for the taxable year in which the distribution or amount
 3 referred to in paragraph (1)(B) is received shall be
 4 an amount equal to—

5 “(A) the amount by which the applicable lim-
 6 itation under section 904(a) for the taxable year
 7 referred to in paragraph (1)(A) was increased by
 8 reason of the inclusion in gross income under section
 9 951(a) of the amount in respect of the controlled
 10 foreign corporation; reduced by

11 “(B) the amount of any income, war profits,
 12 and excess profits taxes paid, or deemed paid, or
 13 accrued to any foreign country or possession of the
 14 United States which were allowable as a credit
 15 under section 901 for the taxable year referred to in
 16 paragraph (1)(A) and which would not have been
 17 allowable but for the inclusion in gross income of the
 18 amount described in subparagraph (A).

19 “(3) CASES IN WHICH TAXES NOT TO BE AL-
 20 LOWED AS DEDUCTION.—In the case of any taxpayer
 21 who—

22 “(A) chose to have the benefits of subpart A
 23 of this part for a taxable year in which he was re-

quired under section 951(a) to include in his gross income an amount in respect of a controlled foreign corporation; and

“(B) does not choose to have the benefits of subpart A of this part for the taxable year in which he receives a distribution or amount which is excluded from gross income under section 956(a) and which is attributable to earnings and profits of the controlled foreign corporation which was included in his gross income for the taxable year referred to in subparagraph (A);

no deduction shall be allowed under section 164 for the taxable year in which such distribution or amount is received for any income, war profits, or excess profits taxes paid or accrued to any foreign country or to any possession of the United States on or with respect to such distribution or amount.

“(4) ~~INSUFFICIENT TAXABLE INCOME.~~—If an increase in the limitation under this subsection exceeds the tax imposed by this chapter for such year, the amount of such excess shall be deemed an overpayment of tax for such year.

1 **“SEC. 958. ADJUSTMENTS TO BASIS OF STOCK IN CON-**
2 **TROLLED FOREIGN CORPORATION AND OF**
3 **OTHER PROPERTY.**

4 ~~“(a) INCREASE IN BASIS.~~—Under regulations pre-
5 scribed by the Secretary or his delegate, the basis of a United
6 States person’s stock in a controlled foreign corporation, and
7 the basis of property of a United States person by reason of
8 which he is considered under section 955(a) ~~(2)~~ as owning
9 stock of a controlled foreign corporation, shall be increased
10 by the amount required to be included in his gross income
11 under section 951(a) with respect to such stock or with
12 respect to such property, as the case may be, but only to the
13 extent to which such amount was included in the gross
14 income of such person.

15 ~~“(b) REDUCTION IN BASIS.~~—

16 ~~“(1) IN GENERAL.~~—Under regulations prescribed
17 by the Secretary or his delegate, the adjusted basis of
18 stock or other property with respect to which a United
19 States person receives an amount which is excluded from
20 gross income under section 956(a) shall be reduced by
21 the amount so excluded.

22 ~~“(2) AMOUNT IN EXCESS OF BASIS.~~—To the ex-

1 tent that an amount excluded from gross income under
 2 section 956(a) exceeds the adjusted basis of the stock
 3 or other property with respect to which it is received,
 4 the amount shall be treated as gain from the sale or
 5 exchange of property.”

6 ~~(b)~~ TECHNICAL AND CLERICAL AMENDMENTS.—

7 ~~(1)~~ Section 551(b) (relating to foreign personal
 8 holding company income included in gross income of
 9 United States shareholders) is amended by adding at
 10 the end thereof the following new sentence: “The amount
 11 included in the gross income of any United States share-
 12 holder for any taxable year under the preceding sen-
 13 tence shall be reduced by such shareholder’s proportion-
 14 ate share of the undistributed personal holding company
 15 income which is included in his gross income under
 16 section 951(a)(1)(A) (relating to amounts included
 17 in gross income of United States persons) for such tax-
 18 able year as his pro rata share of the subpart F income
 19 of the company.”

20 ~~(2)~~ Section 901 (relating to foreign tax credit) is

1 amended by striking out "section 902" and inserting
 2 in lieu thereof "sections 902 and 957".

3 ~~(3)~~ Section 902(c) is amended to read as follows:

4 ~~"(c)~~ CROSS REFERENCES.—

"(1) For application of subsections (a) and (b) with respect to taxes deemed paid in a prior taxable year by a United States person with respect to a controlled foreign corporation, see section 957.

"(2) For reduction of credit with respect to dividends paid out of accumulated profits for years for which certain information is not furnished, see section 6038."

5 ~~(4)~~ Section 904(f) is amended to read as follows:

6 ~~"(f)~~ CROSS REFERENCES.—

"(1) For increase of applicable limitation under subsection (a) for taxes paid with respect to amounts received which were included in the gross income of the taxpayer for a prior taxable year as a United States person with respect to a controlled foreign corporation, see section 957(b).

"(2) For special rule relating to the application of the credit provided by section 901 in the case of affiliated groups which include Western Hemisphere trade corporations for years in which the limitation provided by subsection (a)(2) applies, see section 1503(d)."

7 ~~(5)~~ The table of subparts for part III of subchapter
 8 N of chapter 1 is amended by adding at the end thereof
 9 the following:

"Subpart F. Controlled foreign corporations."

~~(6)~~ Section 1016(a) ~~(relating to adjustments to basis)~~ is amended—

~~(A)~~ by striking out the period at the end of paragraph ~~(18)~~ and inserting in lieu thereof a semicolon; and

~~(B)~~ by adding after paragraph ~~(18)~~ the following new paragraph:

“(19) to the extent provided in section 958 in the case of stock in controlled foreign corporations ~~(or foreign corporations which were controlled foreign corporations)~~ and of property by reason of which a person is considered as owning such stock.”

~~(c)~~ EFFECTIVE DATE.—The amendments made by this section shall apply with respect to taxable years of foreign corporations beginning after December 31, 1962, and to taxable years of United States persons within which or with which such taxable years of such foreign corporations end.

SEC. 12. CONTROLLED FOREIGN CORPORATIONS.

(a) *IN GENERAL.*—Part III of subchapter N of chapter 1 (relating to income from sources without the United

1 States) is amended by adding at the end thereof the follow-
 2 ing new subparts:

3 **“Subpart F—Controlled Foreign Corporations**

“Sec. 951. Amounts included in gross income of United States share-
 holders.

“Sec. 952. Subpart F income defined.

“Sec. 953. Income from insurance of United States risks.

“Sec. 954. Foreign base company income.

“Sec. 955. Withdrawal of previously excluded subpart F income from
 qualified investment.

“Sec. 956. Investment of earnings in United States property.

“Sec. 957. Controlled foreign corporations; United States persons.

“Sec. 958. Rules for determining stock ownership.

“Sec. 959. Exclusion from gross income of previously taxed earnings and
 profits.

“Sec. 960. Special rules for foreign tax credit.

“Sec. 961. Adjustments to basis of stock in controlled foreign corpora-
 tions and of other property.

“Sec. 962. Election by individuals to be subject to tax at corporate rates.

“Sec. 963. Receipt of minimum distributions by domestic corporations.

“Sec. 964. Miscellaneous provisions.

4 **“SEC. 951. AMOUNTS INCLUDED IN GROSS INCOME OF UNITED**
 5 **STATES SHAREHOLDERS.**

6 **“(a) AMOUNTS INCLUDED.—**

7 **“(1) IN GENERAL.—**If a foreign corporation is a
 8 controlled foreign corporation for an uninterrupted period
 9 of 30 days or more during any taxable year beginning
 10 after December 31, 1962, every person who is a United
 11 States shareholder (as defined in subsection (b)) of
 12 such corporation and who owns (within the meaning of
 13 section 958(a)) stock in such corporation on the last
 14 day, in such year, on which such corporation is a con-

1 *trolled foreign corporation shall include in his gross in-*
2 *come, for his taxable year in which or with which such*
3 *taxable year of the corporation ends—*

4 “(A) the sum of—

5 “(i) except as provided in section 963, his
6 *pro rata share (determined under paragraph*
7 *(2)) of the corporation’s subpart F income for*
8 *such year, and*

9 “(ii) his *pro rata share (determined under*
10 *section 955(a)(3)) of the corporation’s pre-*
11 *viously excluded subpart F income withdrawn*
12 *from investment in less developed countries for*
13 *such year; and*

14 “(B) his *pro rata share (determined under*
15 *section 956(a)(2)) of the corporation’s increase in*
16 *earnings invested in United States property for such*
17 *year (but only to the extent not excluded from gross*
18 *income under section 959(a)(2)).*

19 “(2) *PRO RATA SHARE OF SUBPART F INCOME.—*

20 *The pro rata share referred to in paragraph (1)(A)(i)*
21 *in the case of any United States shareholder is the*
22 *amount—*

1 “(A) which would have been distributed with
 2 respect to the stock which such shareholder owns
 3 (within the meaning of section 958(a)) in such
 4 corporation if on the last day, in its taxable year,
 5 on which the corporation is a controlled foreign cor-
 6 poration it had distributed pro rata to its share-
 7 holders an amount (i) which bears the same ratio
 8 to its subpart F income for the taxable year, as
 9 (ii) the part of such year during which the cor-
 10 poration is a controlled foreign corporation bears
 11 to the entire year, reduced by

12 “(B) the amount of distributions received by
 13 any other person during such year as a dividend
 14 with respect to such stock, but only to the extent
 15 of the dividend which would have been received if
 16 the distribution by the corporation had been the
 17 amount (i) which bears the same ratio to the sub-
 18 part F income of such corporation for the taxable
 19 year, as (ii) the part of such year during which
 20 such shareholder did not own (within the meaning
 21 of section 958(a)) such stock bears to the entire
 22 year.

23 “(3) LIMITATION ON PRO RATA SHARE OF PRE-
 24 VIOUSLY EXCLUDED SUBPART F INCOME WITHDRAWN
 25 FROM INVESTMENT.—For purposes of paragraph (1)

(A)(ii), the pro rata share of any United States shareholder of the previously excluded subpart F income of a controlled foreign corporation withdrawn from investment in less developed countries shall not exceed an amount (A) which bears the same ratio to his pro rata share of such income withdrawn (as determined under section 955(a)(3)) for the taxable year, as (B) the part of such year during which the corporation is a controlled foreign corporation bears to the entire year.

“(4) LIMITATION ON PRO RATA SHARE OF INVESTMENT IN UNITED STATES PROPERTY.—For purposes of paragraph (1)(B), the pro rata share of any United States shareholder in the increase of the earnings of a controlled foreign corporation invested in United States property shall not exceed an amount (A) which bears the same ratio to his pro rata share of such increase (as determined under section 956(a)(2)) for the taxable year, as (B) the part of such year during which the corporation is a controlled foreign corporation bears to the entire year.

“(b) UNITED STATES SHAREHOLDER DEFINED.—For purposes of this subpart, the term ‘United States shareholder’ means, with respect to any foreign corporation, a United States person (as defined in section 957(d)) who owns (within the meaning of section 958(a)), or is

1 *considered as owning by applying the rules of ownership of*
2 *section 958(b), 10 percent or more of the total combined*
3 *voting power of all classes of stock entitled to vote of such*
4 *foreign corporation.*

5 “(c) *COORDINATION WITH ELECTION OF A FOREIGN*
6 *INVESTMENT COMPANY TO DISTRIBUTE INCOME.—A*
7 *United States shareholder who, for his taxable year, is a*
8 *qualified shareholder (within the meaning of section*
9 *1247(c)) of a foreign investment company with respect to*
10 *which an election under section 1247 is in effect shall not*
11 *be required to include in gross income, for such taxable*
12 *year, any amount under subsection (a) with respect to such*
13 *company.*

14 “(d) *COORDINATION WITH FOREIGN PERSONAL*
15 *HOLDING COMPANY PROVISIONS.—A United States share-*
16 *holder who, for his taxable year, is subject to tax under*
17 *section 551(b) (relating to foreign personal holding com-*
18 *pany income included in gross income of United States share-*
19 *holders) on income of a controlled foreign corporation shall*
20 *not be required to include in gross income, for such taxable*
21 *year, any amount under subsection (a) with respect to*
22 *such company.*

1 “SEC. 952. SUBPART F INCOME DEFINED.

2 “(a) *IN GENERAL.*—For purposes of this subpart,
3 the term ‘subpart F income’ means, in the case of any
4 controlled foreign corporation, the sum of—

5 “(1) the income derived from the insurance of
6 United States risks (as determined under section 953),
7 and

8 “(2) the foreign base company income (as deter-
9 mined under section 954).

10 “(b) *EXCLUSION OF UNITED STATES INCOME.*—Sub-
11 part F income does not include any item includible in gross in-
12 come under this chapter (other than this subpart) as income
13 derived from sources within the United States of a foreign
14 corporation engaged in trade or business in the United States.

15 “(c) *LIMITATION.*—For purposes of subsection (a),
16 the subpart F income of any controlled foreign corporation
17 for any taxable year shall not exceed the earnings and profits
18 of such corporation for such year reduced by the amount
19 (if any) by which—

20 “(1) an amount equal to—

21 “(A) the sum of the deficits in earnings and

1 *profits for prior taxable years beginning after De-*
2 *cember 31, 1962, plus*

3 “(B) *the sum of the deficits in earnings and*
4 *profits for taxable years beginning after December*
5 *31, 1959, and before January 1, 1963 (reduced*
6 *by the sum of the earnings and profits for such*
7 *taxable years); exceeds*

8 “(2) *an amount equal to the sum of the earnings*
9 *and profits for prior taxable years beginning after De-*
10 *cember 31, 1962, allocated to other earnings and profits*
11 *under section 959(c)(3).*

12 *For purposes of the preceding sentence, any deficit in earn-*
13 *ings and profits for any prior taxable year shall be taken into*
14 *account under paragraph (1) for any taxable year only to*
15 *the extent it has not been taken into account under such*
16 *paragraph for any preceding taxable year to reduce earn-*
17 *ings and profits of such preceding year.*

18 “(d) *SPECIAL RULE IN CASE OF INDIRECT OWNER-*
19 *SHIP.—For purposes of subsection (c), if—*

20 “(1) *a United States shareholder owns (within the*
21 *meaning of section 958(a)) stock of a foreign corpora-*
22 *tion, and by reason of such ownership owns (within the*
23 *meaning of such section) stock of any other foreign cor-*
24 *poration, and*

1 “(2) any of such foreign corporations has a deficit
 2 in earnings and profits for the taxable year,
 3 then the earnings and profits for the taxable year of each such
 4 foreign corporation which is a controlled foreign corpora-
 5 tion shall, with respect to such United States shareholder, be
 6 properly reduced to take into account any deficit described
 7 in paragraph (2) in such manner as the Secretary or his
 8 delegate shall prescribe by regulations.

9 “SEC. 953. INCOME FROM INSURANCE OF UNITED STATES
 10 RISKS.

11 “(a) GENERAL RULE.—For purposes of section 952
 12 (a)(1), the term ‘income derived from the insurance of
 13 United States risks’ means that income which—

14 “(1) is attributable to the reinsurance or the issuing
 15 of any insurance or annuity contract—

16 “(A) in connection with property in, or liability
 17 arising out of activity in, or in connection with the
 18 lives or health of residents of, the United States, or

19 “(B) in connection with risks not included in
 20 subparagraph (A) as the result of any arrange-
 21 ment whereby another corporation receives a sub-
 22 stantially equal amount of premiums or other con-
 23 sideration in respect to any reinsurance or the issu-
 24 ing of any insurance or annuity contract in connec-

1 tion with property in, or liability arising out of
2 activity in, or in connection with the lives or health
3 of residents of, the United States, and

4 “(2) would (subject to the modifications provided
5 by paragraphs (1), (2), and (3) of subsection (b))
6 be taxed under subchapter L of this chapter if such
7 income were the income of a domestic insurance corpo-
8 ration.

9 This section shall apply only in the case of a controlled
10 foreign corporation which receives, during any taxable year,
11 premiums or other consideration in respect of the reinsurance,
12 and the issuing, of insurance and annuity contracts described
13 in paragraph (1) in excess of 5 percent of the total
14 of premiums and other consideration received during such
15 taxable year in respect of all reinsurance and issuing of
16 insurance and annuity contracts.

17 “(b) SPECIAL RULES.—For purposes of subsection
18 (a)—

19 “(1) In the application of part I of subchapter L,
20 life insurance company taxable income is the gain from
21 operations as defined in section 809(b).

22 “(2) A corporation which would, if it were a
23 domestic insurance corporation, be taxable under part II
24 of subchapter L shall apply subsection (a) as if it were
25 taxable under part III of subchapter L.

1 “(3) *The following provisions of subchapter L shall*
2 *not apply:*

3 “(A) *Section 809(d)(4) (operations loss de-*
4 *duction).*

5 “(B) *Section 809(d)(5) (certain nonpar-*
6 *ticipating contracts).*

7 “(C) *Section 809(d)(6) (group life, accident,*
8 *and health insurance).*

9 “(D) *Section 809(d)(10) (small business*
10 *deduction).*

11 “(E) *Section 817(b) (gain on property*
12 *held on December 31, 1958, and certain substituted*
13 *property acquired after 1958).*

14 “(F) *Section 832(b)(5) (certain capital*
15 *losses).*

16 “(4) *The items referred to in—*

17 “(A) *section 809(c)(1) (relating to gross*
18 *amount of premiums and other considerations),*

19 “(B) *section 809(c)(2) (relating to net*
20 *decrease in reserves),*

21 “(C) *section 809(d)(2) (relating to net*
22 *increase in reserves), and*

23 “(D) *section 832(b)(4) (relating to pre-*
24 *miums earned on insurance contracts),*

25 *shall be taken into account only to the extent they are in*

1 *respect of any reinsurance or the issuing of any insurance*
 2 *or annuity contract described in subsection (a)(1).*

3 “(5) *All items of income, expenses, losses, and*
 4 *deductions (other than those taken into account under*
 5 *paragraph (4)) shall be properly allocated or appor-*
 6 *tioned under regulations prescribed by the Secretary or*
 7 *his delegate.*

8 “SEC. 954. *FOREIGN BASE COMPANY INCOME.*

9 “(a) *FOREIGN BASE COMPANY INCOME.*—*For pur-*
 10 *poses of section 952(a)(2), the term ‘foreign base com-*
 11 *pany income’ means for any taxable year the sum of—*

12 “(1) *the foreign personal holding company in-*
 13 *come for the taxable year (determined under subsection*
 14 *(c) and reduced as provided in subsection (b)(5)),*

15 “(2) *the foreign base company sales income for*
 16 *the taxable year (determined under subsection (d) and*
 17 *reduced as provided in subsection (b)(5)), and*

18 “(3) *the foreign base company services income*
 19 *for the taxable year (determined under subsection (e)*
 20 *and reduced as provided in subsection (b)(5)).*

21 “(b) *EXCLUSIONS AND SPECIAL RULES.*—

22 “(1) *EXCLUSION OF CERTAIN DIVIDENDS, IN-*
 23 *TEREST, AND GAINS FROM QUALIFIED INVESTMENTS*
 24 *IN LESS DEVELOPED COUNTRIES.*—*For purposes of sub-*

1 section (a), foreign base company income does not
2 include—

3 “(A) dividends and interest received during
4 the taxable year from investments which at the
5 time of receipt are qualified investments in less de-
6 veloped countries (as defined in section 955(b)),
7 or

8 “(B) if the gains from the sale or exchange
9 during the taxable year of investments which at the
10 time of sale or exchange are qualified investments
11 in less developed countries exceed the losses from
12 the sale or exchange during the taxable year of
13 such qualified investments, the amount by which
14 such gains exceed such losses.

15 The preceding sentence shall apply only to the extent
16 that the sum of the dividends and interest described in
17 subparagraph (A) and the amount described in sub-
18 paragraph (B) does not exceed the increase for the tax-
19 able year in qualified investments in less developed
20 countries of the controlled foreign corporation (as deter-
21 mined under subsection (f)).

22 “(2) EXCLUSION OF CERTAIN SHIPPING IN-
23 COME.—For purposes of subsection (a), foreign base
24 company income does not include income derived from,

1 or in connection with, the use (or hiring or leasing for
2 use) of any aircraft or vessel in foreign commerce, or
3 the performance of services directly related to the use of
4 any such aircraft or vessel.

5 “(3) SPECIAL RULE WHERE FOREIGN BASE COM-
6 PANY IS LESS THAN 30 PERCENT OR MORE THAN 70
7 PERCENT OF GROSS INCOME.—For purposes of subsec-
8 tion (a)—

9 “(A) If the foreign base company income
10 (determined without regard to paragraphs (1) and
11 (5)) is less than 30 percent of gross income, no part
12 of the gross income of the taxable year shall be treated
13 as foreign base company income.

14 “(B) If the foreign base company income
15 (determined without regard to paragraphs (1) and
16 (5)) exceeds 70 percent of gross income, the entire
17 gross income of the taxable year shall, subject to the
18 provisions of paragraphs (1), (2), (4), and (5), be
19 treated as foreign base company income.

20 “(4) EXCEPTION FOR FOREIGN CORPORATIONS
21 NOT AVAILED OF TO REDUCE TAXES.—For purposes of
22 subsection (a), foreign base company income does not
23 include any item of income received by a controlled
24 foreign corporation if it is established to the satisfaction
25 of the Secretary or his delegate with respect to such item

1 *that the creation or organization of the controlled foreign*
 2 *corporation receiving such item under the laws of the*
 3 *foreign country in which it is incorporated does not have*
 4 *the effect of substantial reduction of income, war profits,*
 5 *or excess profits taxes or similar taxes.*

6 “(5) DEDUCTIONS TO BE TAKEN INTO AC-
 7 COUNT.—For purposes of subsection (a), the foreign
 8 personal holding company income, the foreign base
 9 company sales income, and the foreign base company
 10 services income shall be reduced, under regulations
 11 prescribed by the Secretary or his delegate, so as to
 12 take into account deductions (including taxes) properly
 13 allocable to such income.

14 “(c) FOREIGN PERSONAL HOLDING COMPANY IN-
 15 COME.—

16 “(1) IN GENERAL.—For purposes of subsection
 17 (a)(1), the term ‘foreign personal holding company
 18 income’ means the foreign personal holding company
 19 income (as defined in section 553), modified and ad-
 20 justed as provided in paragraphs (2), (3), and (4).

21 “(2) RENTS INCLUDED WITHOUT REGARD TO 50
 22 PERCENT LIMITATION.—For purposes of paragraph
 23 (1), all rents shall be included in foreign personal hold-

1 *ing company income without regard to whether or not*
2 *such rents constitute 50 percent or more of gross income.*

3 “(3) *CERTAIN INCOME DERIVED IN ACTIVE CON-*
4 *DUCT OF TRADE OR BUSINESS.—For purposes of para-*
5 *graph (1), foreign personal holding company income*
6 *does not include—*

7 “(A) *rents and royalties which are derived in*
8 *the active conduct of a trade or business and which*
9 *are received from a person other than a related*
10 *person (within the meaning of subsection (d)*
11 *(3)), or*

12 “(B) *dividends, interest, and gains from the*
13 *sale or exchange of stock or securities derived in*
14 *the conduct of a banking, financing, or similar*
15 *business, or derived from the investments made by*
16 *an insurance company of its unearned premiums or*
17 *reserves ordinary and necessary for the proper con-*
18 *duct of its insurance business, and which are received*
19 *from a person other than a related person (within*
20 *the meaning of subsection (d)(3)).*

21 “(4) *CERTAIN INCOME RECEIVED FROM RELATED*
22 *PERSONS.—For purposes of paragraph (1), foreign per-*
23 *sonal holding company income does not include—*

24 “(A) *dividends and interest received from a*
25 *related person which (i) is organized under the*

1 laws of the same foreign country under the laws of
2 which the controlled foreign corporation is created
3 or organized, and (ii) has a substantial part of its
4 assets used in its trade or business located in such
5 same foreign country;

6 “(B) interest received in the conduct of a
7 banking, financing, or similar business from a re-
8 lated person engaged in the conduct of a banking,
9 financing, or similar business if the businesses of the
10 recipient and the payor are predominantly with per-
11 sons other than related persons; and

12 “(C) rents, royalties, and similar amounts re-
13 ceived from a related person for the use of, or the
14 privilege of using, property within the country under
15 the laws of which the controlled foreign corporation
16 is created or organized.

17 “(d) *FOREIGN BASE COMPANY SALES INCOME.*—

18 “(1) *IN GENERAL.*—For purposes of subsection
19 (a)(2), the term ‘foreign base company sales income’
20 means income (whether in the form of profits, commis-
21 sions, fees, or otherwise) derived in connection with the
22 purchase of personal property from a related person and
23 its sale to any person, the sale of personal property to
24 any person on behalf of a related person, the purchase
25 of personal property from any person and its sale to a

1 *related person, or the purchase of personal property*
2 *from any person on behalf of a related person where—*

3 *“(A) the property which is purchased (or in*
4 *the case of property sold on behalf of a related per-*
5 *son, the property which is sold) is manufactured,*
6 *produced, grown, or extracted outside the country*
7 *under the laws of which the controlled foreign*
8 *corporation is created or organized, and*

9 *“(B) the property is sold for use, consump-*
10 *tion, or disposition outside such foreign country, or,*
11 *in the case of property purchased on behalf of a*
12 *related person, is purchased for use, consumption,*
13 *or disposition outside such foreign country.*

14 *“(2) CERTAIN BRANCH INCOME.—For purposes*
15 *of determining foreign base company sales income*
16 *in situations in which the carrying on of activities by a*
17 *controlled foreign corporation through a branch or simi-*
18 *lar establishment outside the country of incorporation of*
19 *the controlled foreign corporation has substantially the*
20 *same effect as if such branch or similar establishment*
21 *were a wholly owned subsidiary corporation deriving*
22 *such income, under regulations prescribed by the Secre-*
23 *tary or his delegate the income attributable to the carry-*
24 *ing on of such activities of such branch or similar estab-*
25 *lishment shall be treated as income derived by a wholly*

1 *owned subsidiary of the controlled foreign corporation*
2 *and shall constitute foreign base company sales income*
3 *of the controlled foreign corporation.*

4 “(3) *RELATED PERSON DEFINED.*—For purposes
5 *of this section, a person is a related person with respect*
6 *to a controlled foreign corporation, if—*

7 “(A) *such person is an individual, partner-*
8 *ship, trust, or estate which controls the controlled*
9 *foreign corporation;*

10 “(B) *such person is a corporation which con-*
11 *trols, or is controlled by, the controlled foreign cor-*
12 *poration; or*

13 “(C) *such person is a corporation which is*
14 *controlled by the same person or persons which con-*
15 *trol the controlled foreign corporation.*

16 *For purposes of the preceding sentence, control means*
17 *the ownership, directly or indirectly, of stock possessing*
18 *more than 50 percent of the total combined voting*
19 *power of all classes of stock entitled to vote. For pur-*
20 *poses of this paragraph, the rules for determining owner-*
21 *ship of stock prescribed by section 958 shall apply.*

22 “(e) *FOREIGN BASE COMPANY SERVICES INCOME.*—

23 *For purposes of subsection (a)(3), the term ‘foreign base*
24 *company services income’ means income (whether in the*
25 *form of compensation, commissions, fees, or otherwise) de-*

1 rived in connection with the performance of technical, man-
 2 agerial, engineering, architectural, scientific, skilled, indus-
 3 trial, commercial, or like services which—

4 “(1) are performed for or on behalf of any related
 5 person (within the meaning of subsection (d)(3)), and

6 “(2) are performed outside the country under the
 7 laws of which the controlled foreign corporation is
 8 created or organized.

9 The preceding sentence shall not apply to income derived
 10 in connection with the performance of services which are di-
 11 rectly related to the sale or exchange by the controlled foreign
 12 corporation of property manufactured, produced, grown, or
 13 extracted by it and which are performed prior to the time of
 14 the sale or exchange, or of services directly related to an offer
 15 or effort to sell or exchange such property.

16 “(f) INCREASE IN QUALIFIED INVESTMENTS IN LESS
 17 DEVELOPED COUNTRIES.—For purposes of subsection (b)
 18 (1), the increase for any taxable year in qualified invest-
 19 ments in less developed countries of any controlled foreign
 20 corporation is the amount by which—

21 “(1) the qualified investments in less developed
 22 countries (as defined in section 955(b)) of the con-
 23 trolled foreign corporation at the close of the taxable
 24 year, exceeds

25 “(2) the qualified investments in less developed

1 *countries (as so defined) of the controlled foreign*
 2 *corporation at the close of the preceding taxable year.*

3 **“SEC. 955. WITHDRAWAL OF PREVIOUSLY EXCLUDED SUBPART**
 4 **F INCOME FROM QUALIFIED INVESTMENT.**

5 **“(a) GENERAL RULES.—**

6 **“(1) AMOUNT WITHDRAWN.—***For purposes of*
 7 *this subpart, the amount of previously excluded subpart*
 8 *F income of any controlled foreign corporation with-*
 9 *drawn from investment in less developed countries for*
 10 *any taxable year is an amount equal to the decrease in*
 11 *the amount of qualified investments in less developed*
 12 *countries of the controlled foreign corporation for such*
 13 *year, but only to the extent that the amount of such*
 14 *decrease does not exceed an amount equal to—*

15 **“(A) the sum of the amounts excluded under**
 16 *section 954(b)(1) from the foreign base company*
 17 *income of such corporation for all prior taxable*
 18 *years, reduced by*

19 **“(B) the sum of the amounts of previously**
 20 *excluded subpart F income withdrawn from invest-*
 21 *ment in less developed countries of such corporation*
 22 *determined under this subsection for all prior tax-*
 23 *able years.*

24 **“(2) DECREASE IN QUALIFIED INVESTMENTS.—**
 25 *For purposes of paragraph (1), the amount of the de-*

1 crease in qualified investments in less developed coun-
2 tries of any controlled foreign corporation for any tax-
3 able year is the amount by which—

4 “(A) the amount of qualified investments in
5 less developed countries of the controlled foreign
6 corporation at the close of the preceding taxable
7 year, exceeds

8 “(B) the amount of qualified investments in
9 less developed countries of the controlled foreign
10 corporation at the close of the taxable year,
11 to the extent the amount of such decrease does not
12 exceed the sum of the earnings and profits for the tax-
13 able year and the earnings and profits accumulated for
14 prior taxable years beginning after December 31, 1962.
15 For purposes of this paragraph, if qualified investments
16 in less developed countries are disposed of by the con-
17 trolled foreign corporation during the taxable year, the
18 amount of the decrease in qualified investments in less
19 developed countries of such controlled foreign corpora-
20 tion for such year shall be reduced by an amount equal
21 to the amount (if any) by which the losses on such
22 dispositions during such year exceed the gains on such
23 dispositions during such year.

24 “(3) PRO RATA SHARE OF AMOUNT WITH-
25 DRAWN.—In the case of any United States shareholder,

the pro rata share of the amount of previously excluded subpart F income of any controlled foreign corporation withdrawn from investment in less developed countries for any taxable year is his pro rata share of the amount determined under paragraph (1).

“(b) *QUALIFIED INVESTMENTS IN LESS DEVELOPED COUNTRIES.*—

“(1) *IN GENERAL.*—For purposes of this subpart, the term ‘qualified investments in less developed countries’ means property which is—

“(A) stock of a less developed country corporation held by the controlled foreign corporation, but only if the controlled foreign corporation owns 10 percent or more of the total combined voting power of all classes of stock of such less developed country corporation;

“(B) an obligation of a less developed country corporation held by the controlled foreign corporation, which, at the time of its acquisition by the controlled foreign corporation, has a maturity of one year or more, but only if the controlled foreign corporation owns 10 percent or more of the total combined voting power of all classes of stock of such less developed country corporation; or

“(C) an obligation of a less developed country,

1 “(2) *COUNTRY CEASES TO BE LESS DEVELOPED*
2 *COUNTRY.*—For purposes of this subpart, property which
3 would be a qualified investment in less developed coun-
4 tries, but for the fact that a foreign country has, after
5 the acquisition of such property by the controlled foreign
6 corporation, ceased to be a less developed country, shall
7 be treated as a qualified investment in less developed
8 countries.

9 “(3) *SPECIAL RULE.*—For purposes of this subpart,
10 a United States shareholder of a controlled foreign cor-
11 poration may, under regulations prescribed by the Sec-
12 retary or his delegate, make the determinations under
13 subsection (a)(2) of this section and under subsection
14 (f) of section 954 as of the close of the years following
15 the years referred to in such subsections, or as of the
16 close of such longer period of time as such regulations
17 may permit, in lieu of on the last day of such years. Any
18 election under this paragraph made with respect to any
19 taxable year shall apply to such year and to all suc-
20 ceeding taxable years unless the Secretary or his dele-
21 gate consents to the revocation of such election.

22 “(4) *EXCEPTION.*—For purposes of this subpart,
23 property shall not constitute qualified investments in less
24 developed countries if such property is disposed of
25 within 6 months after the date of its acquisition.

1 “(5) *AMOUNT ATTRIBUTABLE TO PROPERTY.*—

2 *The amount taken into account under this subpart with*
 3 *respect to any property described in paragraph (1) or*
 4 *(2) shall be its adjusted basis, reduced by any liability*
 5 *to which such property is subject.*

6 “(c) *LESS DEVELOPED COUNTRY CORPORATIONS.*—

7 “(1) *IN GENERAL.*—*For purposes of this sub-*
 8 *part, the term ‘less developed country corporation’*
 9 *mean a foreign corporation which during the taxable*
 10 *year is engaged in the active conduct of one or more*
 11 *trades or businesses and—*

12 “(A) *80 percent or more of the gross income*
 13 *of which for the taxable year is derived from sources*
 14 *within less developed countries; and*

15 “(B) *80 percent or more in value of the*
 16 *assets of which on each day of the taxable year*
 17 *consists of—*

18 “(i) *property used in such trades or busi-*
 19 *nesses and located in less developed countries,*

20 “(ii) *money, and deposits with persons*
 21 *carrying on the banking business,*

22 “(iii) *stock, and obligations which, at the*
 23 *time of their acquisition, have a maturity of one*
 24 *year or more, of any other less developed coun-*
 25 *try corporation,*

1 “(iv) an obligation of a less developed
2 country,

3 “(v) an investment which is required be-
4 cause of restrictions imposed by a less developed
5 country, and

6 “(vi) property described in section 956
7 (b)(2).

8 For purposes of subparagraph (A), the determination
9 as to whether income is derived from sources within less
10 developed countries shall be made under regulations
11 prescribed by the Secretary or his delegate.

12 “(2) SHIPPING COMPANIES.—For purposes of this
13 subpart, the term ‘less developed country corporation’
14 also means a foreign corporation—

15 “(A) 80 percent or more of the gross income of
16 which for the taxable year consists of—

17 “(i) gross income derived from, or in con-
18 nection with, the using (or hiring or leasing
19 for use) in foreign commerce of aircraft or
20 vessels registered under the laws of a less de-
21 veloped country, or from, or in connection with,
22 the performance of services directly related to
23 use of such aircraft or vessels, or from the sale
24 or exchange of such aircraft or vessels, and

25 “(ii) dividends and interest received from

1 *foreign corporations which are less developed*
2 *country corporations within the meaning of this*
3 *paragraph and 10 percent or more of the total*
4 *combined voting power of all classes of stock*
5 *of which are owned by the foreign corporation,*
6 *and gain from the sale or exchange of stock or*
7 *obligations of foreign corporations which are*
8 *such less developed country corporations, and*

9 “(B) 80 percent or more of the assets of which
10 *on each day of the taxable year consists of (i) assets*
11 *used, or held for use, for or in connection with the*
12 *production of income described in subparagraph*
13 *(A), and (ii) property described in section*
14 *956(b)(2).*

15 “(3) *LESS DEVELOPED COUNTRY DEFINED.*—For
16 *purposes of this subpart, the term ‘less developed coun-*
17 *try’ means (in respect of any foreign corporation) any*
18 *foreign country (other than an area within the Sino-*
19 *Soviet bloc) or any possession of the United States with*
20 *respect to which, on the first day of the taxable year, there*
21 *is in effect an Executive order by the President of the*
22 *United States designating such country or possession as*
23 *an economically less developed country for purposes of*
24 *this subpart. For purposes of the preceding sentence,*
25 *an overseas territory, department, province, or possession*

1 *may be treated as a separate country. No designation*
 2 *shall be made under this paragraph with respect to—*

3	<i>Australia</i>	<i>Liechtenstein</i>
4	<i>Austria</i>	<i>Luxembourg</i>
5	<i>Belgium</i>	<i>Monaco</i>
6	<i>Canada</i>	<i>Netherlands</i>
7	<i>Denmark</i>	<i>New Zealand</i>
8	<i>France</i>	<i>Norway</i>
9	<i>Germany (Federal</i>	<i>Union of South Africa</i>
10	<i>Republic)</i>	<i>San Marino</i>
11	<i>Hong Kong</i>	<i>Sweden</i>
12	<i>Italy</i>	<i>Switzerland</i>
13	<i>Japan</i>	<i>United Kingdom</i>

14 *After the President has designated any foreign country or*
 15 *any possession of the United States as an economically less*
 16 *developed country for purposes of this subpart, he shall not*
 17 *terminate such designation (either by issuing an Executive*
 18 *order for that purpose or by issuing an Executive order under*
 19 *the first sentence of this paragraph which has the effect of*
 20 *terminating such designation) unless, at least 30 days prior*
 21 *to such termination, he has notified the Senate and the House*
 22 *of Representatives of his intention to terminate such*
 23 *designation.*

1 “SEC. 956. INVESTMENT OF EARNINGS IN UNITED STATES
2 PROPERTY.

3 “(a) GENERAL RULES.—For purposes of this sub-
4 part—

5 “(1) AMOUNT OF INVESTMENT.—The amount of
6 earnings of a controlled foreign corporation invested in
7 United States property at the close of any taxable year
8 is the aggregate amount of such property held, directly
9 or indirectly, by the controlled foreign corporation at the
10 close of the taxable year, to the extent such amount
11 would have constituted a dividend (determined after the
12 application of section 955(a)) if it had been distributed.

13 “(2) PRO RATA SHARE OF INCREASE FOR YEAR.—
14 In the case of any United States shareholder, the pro
15 rata share of the increase for any taxable year in the
16 earnings of a controlled foreign corporation invested in
17 United States property is the amount determined by
18 subtracting his pro rata share of—

19 “(A) the amount determined under paragraph
20 (1) for the close of the preceding taxable year, re-
21 duced by amounts paid during such preceding taxable
22 year to which section 959(c)(1) applies, from

1 “(B) the amount determined under paragraph
2 (1) for the close of the taxable year.

3 The determinations under subparagraphs (A) and (B)
4 shall be made on the basis of stock owned (within the
5 meaning of section 958(a)) by such United States
6 shareholder on the last day during the taxable year on
7 which the foreign corporation is a controlled foreign
8 corporation.

9 “(3) AMOUNT ATTRIBUTABLE TO PROPERTY.—
10 The amount taken into account under paragraph (1) or
11 (2) with respect to any property shall be its adjusted
12 basis, reduced by any liability to which the property is
13 subject.

14 “(b) UNITED STATES PROPERTY DEFINED.—

15 “(1) IN GENERAL.—For purposes of subsection
16 (a), the term ‘United States property’ means any
17 property acquired after December 31, 1962, which is—

18 “(A) tangible property located in the United
19 States;

20 “(B) stock of a domestic corporation;

21 “(C) an obligation of a United States person;

22 or

1 “(D) any right to the use in the United States
2 of—

3 “(i) a patent or copyright,

4 “(ii) an invention, model, or design
5 (whether or not patented),

6 “(iii) a secret formula or process, or

7 “(iv) any other similar property right,
8 which is acquired or developed by the controlled
9 foreign corporation for use in the United States.

10 “(2) EXCEPTIONS.—For purposes of subsection
11 (a), the term ‘United States property’ does not in-
12 clude—

13 “(A) obligations of the United States, money,
14 or deposits with persons carrying on the banking
15 business;

16 “(B) property located in the United States
17 which is purchased in the United States for export
18 to, or use in, foreign countries;

19 “(C) any obligation of a United States per-
20 son arising in connection with the sale or processing
21 of property if the amount of such obligation out-

1 *standing at no time during the taxable year exceeds*
2 *the amount which would be ordinary and necessary*
3 *to carry on the trade or business of both the other*
4 *party to the sale or processing transaction and the*
5 *United States person had the sale or processing*
6 *transaction been made between unrelated persons;*

7 *“(D) any aircraft, railroad rolling stock, ves-*
8 *sel, motor vehicle, or container used in the trans-*
9 *portation of persons or property in foreign com-*
10 *merce and used predominantly outside the United*
11 *States;*

12 *“(E) an amount of assets of an insurance com-*
13 *pany equivalent to the unearned premiums or re-*
14 *serves ordinary and necessary for the proper con-*
15 *duct of its insurance business attributable to contracts*
16 *which are not contracts described in section*
17 *953(a)(1); and*

18 *“(F) an amount of assets of the controlled for-*
19 *ign corporation equal to the earnings and profits*
20 *accumulated after December 31, 1962, and excluded*
21 *from subpart F income under section 952(b).*

22 *“(c) PLEDGES AND GUARANTEES.—For purposes of*
23 *subsection (a), a controlled foreign corporation shall, under*
24 *regulations prescribed by the Secretary or his delegate, be*
25 *considered as holding an obligation of a United States per-*

1 son if such controlled foreign corporation is a pledgor or
 2 guarantor of such obligation.

3 **"SEC. 957. CONTROLLED FOREIGN CORPORATIONS; UNITED**
 4 **STATES PERSONS.**

5 **"(a) GENERAL RULE.**—For purposes of this sub-
 6 part, the term 'controlled foreign corporation' means any for-
 7 eign corporation of which more than 50 percent of the total
 8 combined voting power of all classes of stock entitled to vote
 9 is owned (within the meaning of section 958(a)), or is
 10 considered as owned by applying the rules of ownership of
 11 section 958(b), by United States shareholders on any day
 12 during the taxable year of such foreign corporation.

13 **"(b) SPECIAL RULE FOR INSURANCE.**—For purposes
 14 only of taking into account income described in section 953
 15 (a) (relating to income derived from insurance of United
 16 States risks), the term 'controlled foreign corporation' in-
 17 cludes not only a foreign corporation as defined by subsec-
 18 tion (a) but also one of which more than 25 percent of the
 19 total combined voting power of all classes of stock is owned
 20 (within the meaning of section 958(a)), or is considered as
 21 owned by applying the rules of ownership of section 958(b).
 22 by United States shareholders on any day during the tax-
 23 able year of such corporation, if the gross amount of pre-
 24 miums or other consideration in respect of the reinsurance or
 25 the issuing of insurance or annuity contracts described in sec-

1 *tion 953(a)(1) exceeds 75 percent of the gross amount of*
 2 *all premiums or other consideration in respect of all risks.*

3 “(c) *CORPORATIONS ORGANIZED IN UNITED STATES*
 4 *POSSESSIONS.—For purposes of this subpart, the term ‘con-*
 5 *trolled foreign corporation’ does not include any corporation*
 6 *created or organized in the Commonwealth of Puerto Rico or*
 7 *a possession of the United States or under the laws of the*
 8 *Commonwealth of Puerto Rico or a possession of the United*
 9 *States if—*

10 “(1) *80 percent or more of the gross income of*
 11 *such corporation (computed without regard to section*
 12 *931) for the 3-year period immediately preceding the*
 13 *close of the taxable year (or for such part of such period*
 14 *immediately preceding the close of such taxable year as*
 15 *may be applicable) was derived from sources within*
 16 *the Commonwealth of Puerto Rico or a possession of*
 17 *the United States; and*

18 “(2) *50 percent or more of the gross income of*
 19 *such corporation (computed without regard to section*
 20 *931) for such period, or for such part thereof, was*
 21 *derived from the active conduct within the Common-*
 22 *wealth of Puerto Rico or a possession of the United*
 23 *States of any trades or businesses constituting the manu-*
 24 *facture or processing of goods, wares, merchandise, or*
 25 *other tangible personal property; the processing of agri-*

1 *cultural or horticultural products or commodities (in-*
2 *cluding but not limited to livestock, poultry, or fur-*
3 *bearing animals); the catching or taking of any kind*
4 *of fish or the mining or extraction of natural resources,*
5 *or any manufacturing or processing of any products or*
6 *commodities obtained from such activities; or the owner-*
7 *ship or operation of hotels.*

8 *For purposes of paragraphs (1) and (2), the deter-*
9 *mination as to whether income was derived from sources*
10 *within the Commonwealth of Puerto Rico or a possession*
11 *of the United States and was derived from the active conduct*
12 *of a described trade or business within the Commonwealth*
13 *of Puerto Rico or a possession of the United States shall*
14 *be made under regulations prescribed by the Secretary or*
15 *his delegate.*

16 “(d) *UNITED STATES PERSON.*—*For purposes of this*
17 *subpart, the term ‘United States person’ has the meaning*
18 *assigned to it by section 7701(a)(30) except that—*

19 “(1) *with respect to a corporation organized under*
20 *the laws of the Commonwealth of Puerto Rico, such term*
21 *does not include an individual who is a bona fide resident*
22 *of Puerto Rico, if a dividend received by such individual*
23 *during the taxable year from such corporation would,*
24 *for purposes of section 933(1), be treated as income*
25 *derived from sources within Puerto Rico,*

1 “(2) with respect to a corporation organized under
 2 *the laws of the Virgin Islands, such term does not include*
 3 *an individual who is a bona fide resident of the Virgin*
 4 *Islands and whose income tax obligation under this*
 5 *subtitle for the taxable year is satisfied pursuant to sec-*
 6 *tion 28(a) of the Revised Organic Act of the Virgin*
 7 *Islands, approved July 22, 1954 (48 U.S.C. 1642),*
 8 *by paying tax on income derived from all sources both*
 9 *within and outside the Virgin Islands into the treasury*
 10 *of the Virgin Islands, and*

11 “(3) with respect to a corporation organized under
 12 *the laws of any other possession of the United States,*
 13 *such term does not include an individual who is a bona*
 14 *fide resident of any such other possession and whose*
 15 *income derived from sources within possessions of the*
 16 *United States is not, by reason of section 931(a), in-*
 17 *cludible in gross income under this subtitle for the*
 18 *taxable year.*

19 **“SEC. 958. RULES FOR DETERMINING STOCK OWNERSHIP.**

20 **“(a) DIRECT AND INDIRECT OWNERSHIP.—**

21 **“(1) GENERAL RULE.—***For purposes of this sub-*
 22 *part (other than sections 955(b)(1) (A) and (B),*
 23 *955(c)(2)(A)(ii), and 960(a)(1)), stock owned*
 24 *means—*

1 “(A) stock owned directly, and

2 “(B) stock owned with the application of para-
3 graph (2).

4 “(2) STOCK OWNERSHIP THROUGH FOREIGN EN-
5 TITIES.—For purposes of subparagraph (B) of para-
6 graph (1), stock owned, directly or indirectly, by or
7 for a foreign corporation, foreign partnership, or foreign
8 trust or foreign estate (within the meaning of section
9 7701(a)(31)) shall be considered as being owned pro-
10 portionately by its shareholders, partners, or bene-
11 ficiaries. Stock considered to be owned by a person by
12 reason of the application of the preceding sentence shall,
13 for purposes of applying such sentence, be treated as
14 actually owned by such person.

15 “(3) SPECIAL RULE FOR MUTUAL INSURANCE
16 COMPANIES.—For purposes of applying paragraph (1)
17 in the case of a foreign mutual insurance company, the
18 term ‘stock’ shall include any certificate entitling the
19 holder to voting power in the corporation.

20 “(b) CONSTRUCTIVE OWNERSHIP.—For purposes of
21 sections 951(b), 954(d)(3), and 957, section 318(a)
22 (relating to constructive ownership of stock) shall apply to
23 the extent that the effect is to treat any United States per-
24 son as a United States shareholder within the meaning of

1 *section 951(b), to treat a person as a related person within*
2 *the meaning of section 954(d)(3), or to treat a foreign*
3 *corporation as a controlled foreign corporation under section*
4 *957, except that—*

5 *“(1) In applying paragraph (1)(A) of section*
6 *318(a), stock owned by a nonresident alien individual*
7 *(other than a foreign trust or foreign estate) shall not*
8 *be considered as owned by a citizen or by a resident*
9 *alien individual.*

10 *“(2) In applying the first sentence of subpara-*
11 *graphs (A) and (B), and in applying clause (i) of*
12 *subparagraph (C), of section 318(a)(2), if a partner-*
13 *ship, estate, trust, or corporation owns, directly or in-*
14 *directly, more than 50 percent of the total combined*
15 *voting power of all classes of stock entitled to vote of a*
16 *corporation, it shall be considered as owning all the*
17 *stock entitled to vote.*

18 *“(3) Stock owned by a partnership, estate, trust,*
19 *or corporation, by reason of the application of the second*
20 *sentence of subparagraphs (A) and (B), and the ap-*
21 *plication of clause (ii) of subparagraph (C), of section*
22 *318(a)(2), shall not be considered as owned by such*
23 *partnership, estate, trust, or corporation, for purposes*
24 *of applying the first sentence of subparagraphs (A) and*

(B), and in applying clause (i) of subparagraph (C), of section 318(a)(2).

“(4) In applying clause (i) of subparagraph (C) of section 318(a)(2), the phrase ‘10 percent’ shall be substituted for the phrase ‘50 percent’ used in subparagraph (C).

“(5) The second sentence of subparagraphs (A) and (B), and clause (ii) of subparagraph (C), of section 318(a)(2) shall not be applied so as to consider a United States person as owning stock which is owned by a person who is not a United States person.

**“SEC. 959. EXCLUSION FROM GROSS INCOME OF PREVIOUSLY
TAXED EARNINGS AND PROFITS.**

“(a) **EXCLUSION FROM GROSS INCOME OF UNITED STATES PERSONS.**—For purposes of this chapter, the earnings and profits for a taxable year of a foreign corporation attributable to amounts which are, or have been, included in the gross income of a United States shareholder under section 951(a) shall not, when—

“(1) such amounts are distributed to, or

“(2) such amounts would, but for this subsection, be included under section 951(a)(1)(B) in the gross income of,

such shareholder (or any other United States person who

1 acquires from any person any portion of the interest of such
2 United States shareholder in such foreign corporation, but
3 only to the extent of such portion, and subject to such proof
4 of the identity of such interest as the Secretary or his delegate
5 may by regulations prescribe) directly, or indirectly through
6 a chain of ownership described under section 958(a), be
7 again included in the gross income of such United States
8 shareholder (or of such other United States person).

9 “(b) *EXCLUSION FROM GROSS INCOME OF CERTAIN*
10 *FOREIGN SUBSIDIARIES.*—For purposes of section 951(a),
11 the earnings and profits for a taxable year of a controlled
12 foreign corporation attributable to amounts which are, or
13 have been, included in the gross income of a United States
14 shareholder under section 951(a), shall not, when distributed
15 through a chain of ownership described under section
16 958(a), be also included in the gross income of another con-
17 trolled foreign corporation in such chain for purposes of the
18 application of section 951(a) to such other controlled foreign
19 corporation with respect to such United States shareholder
20 (or to any other United States shareholder who acquires
21 from any person any portion of the interest of such United
22 States shareholder in the controlled foreign corporation, but
23 only to the extent of such portion, and subject to such proof
24 of identity of such interest as the Secretary or his delegate
25 may prescribe by regulations).

1 “(c) *ALLOCATION OF DISTRIBUTIONS.*—For pur-
 2 poses of subsections (a) and (b), section 316(a) shall be
 3 applied by applying paragraph (2) thereof, and then para-
 4 graph (1) thereof—

5 “(1) first to earnings and profits attributable to
 6 amounts included in gross income under section 951
 7 (a)(1)(B) (or which would have been included ex-
 8 cept for subsection (a)(2) of this section),

9 “(2) then to earnings and profits attributable to
 10 amounts included in gross income under section 951
 11 (a)(1)(A) (but reduced by amounts not included un-
 12 der section 951(a)(1)(B) because of the exclusion in
 13 subsection (a)(2) of this section), and

14 “(3) then to other earnings and profits.

15 “(d) *DISTRIBUTIONS EXCLUDED FROM GROSS IN-*
 16 *COME NOT TO BE TREATED AS DIVIDENDS.*—Except as
 17 provided in section 960(a)(3), any distribution excluded
 18 from gross income under subsection (a) shall be treated, for
 19 purposes of this chapter, as a distribution which is not a
 20 dividend.

21 “SEC. 960. *SPECIAL RULES FOR FOREIGN TAX CREDIT.*

22 “(a) *TAXES PAID BY A FOREIGN CORPORATION.*—

23 “(1) *GENERAL RULE.*—For purposes of subpart
 24 A of this part, if there is included, under section 951(a),

1 *in the gross income of a domestic corporation any amount*
2 *attributable to earnings and profits—*

3 *“(A) of a foreign corporation at least 10 per-*
4 *cent of the voting stock of which is owned by such*
5 *domestic corporation, or*

6 *“(B) of a foreign corporation at least 50 per-*
7 *cent of the voting stock of which is owned by a foreign*
8 *corporation at least 10 percent of the voting stock of*
9 *which is in turn owned by such domestic corporation,*
10 *then, under regulations prescribed by the Secretary or*
11 *his delegate, such domestic corporation shall be deemed*
12 *to have paid the same proportion of the total income,*
13 *war profits, and excess profits taxes paid (or deemed*
14 *paid) by such foreign corporation to a foreign country or*
15 *possession of the United States for the taxable year on*
16 *or with respect to the earnings and profits of such foreign*
17 *corporation which the amount of earnings and profits*
18 *of such foreign corporation so included in gross income*
19 *of the domestic corporation bears to—*

20 *“(C) if the foreign corporation at least 10*
21 *percent of the voting stock of which is owned by such*
22 *domestic corporation referred to in subparagraph*
23 *(A) or (B) is not a less developed country cor-*
24 *poration (as defined in section 902(d)) for such*

1 *taxable year, the entire amount of the earnings and*
2 *profits of such foreign corporation for such taxable*
3 *year, or*

4 “(D) if the foreign corporation at least 10
5 *percent of the voting stock of which is owned by*
6 *such domestic corporation referred to in subpara-*
7 *graph (A) or (B) is a less developed country cor-*
8 *poration (as defined in section 902(d)) for such*
9 *taxable year, the sum of the entire amount of the*
10 *earnings and profits of such foreign corporation for*
11 *such taxable year and the total income, war profits,*
12 *and excess profits taxes paid by such foreign corpo-*
13 *ration to foreign countries or possessions of the*
14 *United States for such taxable year.*

15 “(2) *TAXES PREVIOUSLY DEEMED PAID BY DO-*
16 *MESTIC CORPORATION.—If a domestic corporation re-*
17 *ceives a distribution from a foreign corporation, any*
18 *portion of which is excluded from gross income under*
19 *section 959, the income, war profits, and excess profits*
20 *taxes paid or deemed paid by such foreign corporation to*
21 *any foreign country or to any possession of the United*
22 *States in connection with the earnings and profits of*
23 *such foreign corporation from which such distribution is*
24 *made shall not be taken into account for purposes of*

1 *section 902, to the extent such taxes were deemed paid*
 2 *by a domestic corporation under paragraph (1) for*
 3 *any prior taxable year.*

4 *“(3) TAXES PAID BY FOREIGN CORPORATION AND*
 5 *NOT PREVIOUSLY DEEMED PAID BY DOMESTIC CORPO-*
 6 *RATION.—Any portion of a distribution from a foreign*
 7 *corporation received by a domestic corporation which is*
 8 *excluded from gross income under section 959(a) shall*
 9 *be treated by the domestic corporation as a dividend,*
 10 *solely for purposes of taking into account under section*
 11 *902 any income, war profits, or excess profits taxes*
 12 *paid to any foreign country or to any possession of the*
 13 *United States, on or with respect to the accumulated*
 14 *profits of such foreign corporation from which such*
 15 *distribution is made, which were not deemed paid by*
 16 *the domestic corporation under paragraph (1) for any*
 17 *prior taxable year.*

18 *“(b) SPECIAL RULES FOR FOREIGN TAX CREDIT IN*
 19 *YEAR OF RECEIPT OF PREVIOUSLY TAXED EARNINGS*
 20 *AND PROFITS.—*

21 *“(1) INCREASE IN SECTION 904 LIMITATION.—*

22 *In the case of any taxpayer who—*

23 *“(A) either (i) chose to have the benefits of*
 24 *subpart A of this part for a taxable year in which*

1 *he was required under section 951(a) to include in*
2 *his gross income an amount in respect of a controlled*
3 *foreign corporation, or (ii) did not pay or accrue*
4 *for such taxable year any income, war profits, or*
5 *excess profits taxes to any foreign country or to any*
6 *possession of the United States, and*

7 *“(B) chooses to have the benefits of subpart*
8 *A of this part for the taxable year in which he re-*
9 *ceives a distribution or amount which is excluded*
10 *from gross income under section 959(a) and which*
11 *is attributable to earnings and profits of the con-*
12 *trolled foreign corporation which was included in*
13 *his gross income for the taxable year referred to in*
14 *subparagraph (A), and*

15 *“(C) for the taxable year in which such dis-*
16 *tribution or amount is received, pays, or is deemed*
17 *to have paid, or accrues income, war profits, or*
18 *excess profits taxes to a foreign country or to any*
19 *possession of the United States with respect to such*
20 *distribution or amount,*

21 *the applicable limitation under section 904 for the tax-*
22 *able year in which such distribution or amount is re-*
23 *ceived shall be increased as provided in paragraph (2),*
24 *but such increase shall not exceed the amount of such*

1 *taxes paid, or deemed paid, or accrued with respect to*
 2 *such distribution or amount.*

3 “(2) *AMOUNT OF INCREASE.—The amount of*
 4 *increase of the applicable limitation under section 904*
 5 *(a) for the taxable year in which the distribution or*
 6 *amount referred to in paragraph (1)(B) is received*
 7 *shall be an amount equal to—*

8 “(A) *the amount by which the applicable*
 9 *limitation under section 904(a) for the taxable year*
 10 *referred to in paragraph (1)(A) was increased by*
 11 *reason of the inclusion in gross income under section*
 12 *951(a) of the amount in respect of the controlled*
 13 *foreign corporation, reduced by*

14 “(B) *the amount of any income, war profits,*
 15 *and excess profits taxes paid, or deemed paid, or*
 16 *accrued to any foreign country or possession of the*
 17 *United States which were allowable as a credit*
 18 *under section 901 for the taxable year referred to in*
 19 *paragraph (1)(A) and which would not have been*
 20 *allowable but for the inclusion in gross income of*
 21 *the amount described in subparagraph (A).*

22 “(3) *CASES IN WHICH TAXES NOT TO BE AL-*
 23 *LOWED AS DEDUCTION.—In the case of any taxpayer*
 24 *who—*

25 “(A) *chose to have the benefits of subpart A of*

1 *this part for a taxable year in which he was re-*
2 *quired under section 951(a) to include in his gross*
3 *income an amount in respect of a controlled foreign*
4 *corporation, and*

5 *“(B) does not choose to have the benefits of*
6 *subpart A of this part for the taxable year in which*
7 *he receives a distribution or amount which is ex-*
8 *cluded from gross income under section 959(a) and*
9 *which is attributable to earnings and profits of the*
10 *controlled foreign corporation which was included*
11 *in his gross income for the taxable year referred*
12 *to in subparagraph (A),*

13 *no deduction shall be allowed under section 164 for the*
14 *taxable year in which such distribution or amount is*
15 *received for any income, war profits, or excess profits*
16 *taxes paid or accrued to any foreign country or to any*
17 *possession of the United States on or with respect to such*
18 *distribution or amount.*

19 *“(4) INSUFFICIENT TAXABLE INCOME.—If an*
20 *increase in the limitation under this subsection exceeds*
21 *the tax imposed by this chapter for such year, the*
22 *amount of such excess shall be deemed an overpayment*
23 *of tax for such year.*

1 “SEC. 961. ADJUSTMENTS TO BASIS OF STOCK IN CONTROLLED
2 FOREIGN CORPORATIONS AND OF OTHER PROP-
3 PERTY.

4 “(a) INCREASE IN BASIS.—Under regulations pre-
5 scribed by the Secretary or his delegate, the basis of a United
6 States shareholder’s stock in a controlled foreign corporation,
7 and the basis of property of a United States shareholder by
8 reason of which he is considered under section 958(a)(2)
9 as owning stock of a controlled foreign corporation, shall be
10 increased by the amount required to be included in his gross
11 income under section 951(a) with respect to such stock or
12 with respect to such property, as the case may be, but only
13 to the extent to which such amount was included in the gross
14 income of such United States shareholder. In the case of a
15 United States shareholder who has made an election under
16 section 962 for the taxable year, the increase in basis pro-
17 vided by this subsection shall not exceed an amount equal to
18 the amount of tax paid under this chapter with respect to the
19 amounts required to be included in his gross income under
20 section 951(a).

21 “(b) REDUCTION IN BASIS.—

22 “(1) IN GENERAL.—Under regulations prescribed
23 by the Secretary or his delegate, the adjusted basis of
24 stock or other property with respect to which a United
25 States shareholder or a United States person receives an

amount which is excluded from gross income under section 959(a) shall be reduced by the amount so excluded.

In the case of a United States shareholder who has made an election under section 962 for any prior taxable year, the reduction in basis provided by this paragraph shall not exceed an amount equal to the amount received which is excluded from gross income under section 959(a) after the application of section 962(d).

“(2) *AMOUNT IN EXCESS OF BASIS.*—To the extent that an amount excluded from gross income under section 959(a) exceeds the adjusted basis of the stock or other property with respect to which it is received, the amount shall be treated as gain from the sale or exchange of property.

“SEC. 962. *ELECTION BY INDIVIDUALS TO BE SUBJECT TO TAX AT CORPORATE RATES.*

“(a) *GENERAL RULE.*—Under regulations prescribed by the Secretary or his delegate, in the case of a United States shareholder who is an individual and who elects to have the provisions of this section apply for the taxable year—

“(1) the tax imposed under this chapter on amounts which are included in his gross income under section 951(a) shall (in lieu of the tax determined under section 1) be an amount equal to the tax which

1 *would be imposed under section 11 if such amounts*
2 *were received by a domestic corporation, and*

3 *“(2) for purposes of applying the provisions of*
4 *section 960 (relating to foreign tax credit) such amounts*
5 *shall be treated as if they were received by a domestic*
6 *corporation.*

7 *“(b) ELECTION.—An election to have the provisions*
8 *of this section apply for any taxable year shall be made*
9 *by a United States shareholder at such time and in such*
10 *manner as the Secretary or his delegate shall prescribe by*
11 *regulations. An election made for any taxable year may*
12 *not be revoked except with the consent of the Secretary*
13 *or his delegate.*

14 *“(c) SURTAX EXEMPTION.—For purposes of applying*
15 *subsection (a)(1), the surtax exemption provided by section*
16 *11(c) shall not exceed, in the case of any United States share-*
17 *holder, an amount which bears the same ratio to \$25,000 as*
18 *the amounts included in his gross income under section 951*
19 *(a) for the taxable year bears to his pro rata share of the*
20 *earnings and profits for the taxable year of all controlled*
21 *foreign corporations with respect to which such United States*
22 *shareholder includes any amount in gross income under*
23 *section 951(a).*

24 *“(d) SPECIAL RULE FOR ACTUAL DISTRIBUTIONS.—*
25 *The earnings and profits of a foreign corporation attributable*

1 to amounts which were included in the gross income of a
 2 United States shareholder under section 951(a) and with
 3 respect to which an election under this section applied shall,
 4 when such earnings and profits are distributed, notwithstand-
 5 ing the provisions of section 959(a) (1), be included in gross
 6 income to the extent that such earnings and profits so dis-
 7 tributed exceed the amount of tax paid under this chapter on
 8 the amounts to which such election applied.

9 “SEC. 963. RECEIPT OF MINIMUM DISTRIBUTIONS BY DOMES-
 10 TIC CORPORATIONS.

11 “(a) GENERAL RULE.—In the case of a United States
 12 shareholder which is a domestic corporation and which con-
 13 sents to all the regulations prescribed by the Secretary or his
 14 delegate under this section prior to the last day prescribed
 15 by law for filing its return of the tax imposed by this chapter
 16 for the taxable year, no amount shall be included in gross
 17 income under section 951(a)(1)(A)(i) for the taxable
 18 year with respect to the subpart F income of a controlled
 19 foreign corporation, if—

20 “(1) in the case of a controlled foreign corpora-
 21 tion described in subsection (c)(1), the United States
 22 shareholder receives a minimum distribution of the earn-
 23 ings and profits for the taxable year of such controlled
 24 foreign corporation;

25 “(2) in the case of controlled foreign corporations

1 described in subsection (c)(2), the United States
 2 shareholder receives a minimum distribution with re-
 3 spect to the consolidated earnings and profits for the
 4 taxable year of all such controlled foreign corporations;
 5 or

6 “(3) in the case of controlled foreign corporations
 7 described in subsection (c)(3), the United States
 8 shareholder receives a minimum distribution of the con-
 9 solidated earnings and profits for the taxable year of
 10 all such controlled foreign corporations.

11 “(b) *MINIMUM DISTRIBUTIONS.*—For purposes of this
 12 section, a minimum distribution with respect to the earnings
 13 and profits for the taxable year of any controlled foreign
 14 corporation or corporations shall, in the case of any United
 15 States shareholder, be its pro rata share of an amount deter-
 16 mined in accordance with the following table:

<i>“If the effective foreign tax rate is (percentage):</i>	<i>The required minimum dis- tribution of earnings and profits is (percentage):</i>
<i>Under 10</i> -----	<i>90</i>
<i>10 or over but less than 20</i> -----	<i>80</i>
<i>20 or over but less than 30</i> -----	<i>70</i>
<i>30 or over but less than 40</i> -----	<i>60</i>
<i>40 or over but less than 42</i> -----	<i>50</i>
<i>42 or over but less than 44</i> -----	<i>38</i>
<i>44 or over but less than 46</i> -----	<i>26</i>
<i>46 or over but not more than 47</i> -----	<i>14</i>
<i>Over 47</i> -----	<i>0</i>

17 “(c) *AMOUNTS TO WHICH SECTION APPLIES.*—

18 “(1) *FOREIGN SUBSIDIARIES.*—Subsection (a)(1)
 19 shall apply to amounts which (but for the provisions of

1 *this section) would be included in the gross income of the*
2 *United States shareholder under section 951(a)(1)(A)*
3 *(i) by reason of its ownership, within the meaning of*
4 *section 958(a)(1)(A), of stock of a controlled foreign*
5 *corporation.*

6 “(2) *CHAIN OF CONTROLLED FOREIGN CORPORA-*
7 *TIONS.—Subsection(a)(2) shall apply to amounts which*
8 *(but for the provisions of this section) would be included*
9 *in the gross income of the United States shareholder*
10 *under section 951(a)(1)(A)(i)—*

11 “(A) *by reason of its ownership, within the*
12 *meaning of section 958(a)(1)(A), of stock of a*
13 *controlled foreign corporation, and*

14 “(B) *to the extent that the United States share-*
15 *holder so elects, by reason of its ownership, within*
16 *the meaning of section 958(a)(2), of stock of any*
17 *other controlled foreign corporation (on account of*
18 *its ownership of the stock described in subparagraph*
19 *(A) or of stock described in this subparagraph),*
20 *but only if there is taken into account the earnings*
21 *and profits of each foreign corporation, whether or*
22 *not a controlled foreign corporation, by reason of*
23 *which the United States shareholder owns, within the*
24 *meaning of section 958(a)(2), stock of such con-*
25 *trolled foreign corporation.*

1 “(3) *ALL CONTROLLED FOREIGN CORPORA-*
 2 *TIONS.—Except as provided in paragraph (4), subsec-*
 3 *tion (a)(3) shall apply to amounts which (but for the*
 4 *provisions of this section) would be included in the gross*
 5 *income of the United States shareholder under section*
 6 *951(a)(1)(A)(i)—*

7 “(A) *by reason of its ownership, within the*
 8 *meaning of section 958(a)(1)(A), of stock of all*
 9 *controlled foreign corporations in which it owns*
 10 *stock within the meaning of such section, and*

11 “(B) *by reason of its ownership, within the*
 12 *meaning of section 958(a)(2), of stock of all con-*
 13 *trolled foreign corporations in which it owns stock*
 14 *within the meaning of such section, but only if there*
 15 *is taken into account the earnings and profits of*
 16 *each foreign corporation, whether or not a controlled*
 17 *foreign corporation, by reason of which the United*
 18 *States shareholder owns, within the meaning of*
 19 *section 958(a), stock of any of such controlled*
 20 *foreign corporations.*

21 “(4) *EXCEPTIONS AND SPECIAL RULES.—*

22 “(A) *LESS DEVELOPED COUNTRY CORPORA-*
 23 *TIONS.—If the United States shareholder so elects,*
 24 *subsection (a)(3) and paragraph (3) of this sub-*
 25 *section shall not apply to amounts which would be*

1 included in the gross income of such shareholder
2 under section 951(a)(1)(A)(i) by reason of its
3 ownership, within the meaning of section 958(a),
4 of stock of controlled foreign corporations which are
5 less developed country corporations (as defined in
6 section 955(c)). This subparagraph shall not
7 apply with respect to a less developed country corpo-
8 ration if, by reason of the ownership of the stock of
9 such corporation, the United States shareholder
10 owns, within the meaning of section 958(a)(2),
11 stock of any other controlled foreign corporation
12 which is not a less developed country corporation.
13 Except as provided in the preceding sentence, an
14 election under this subparagraph may be made only
15 with respect to all controlled foreign corporations
16 which are less developed country corporations and
17 with respect to which the domestic corporation
18 making the election is a United States shareholder.

19 “(B) FOREIGN BRANCHES.—In applying sub-
20 section (a)(3) and paragraph (3) of this subsec-
21 tion, if a United States shareholder so elects, all
22 branches maintained by such shareholder in foreign
23 countries, the Commonwealth of Puerto Rico, or
24 possessions of the United States shall, under regula-
25 tions prescribed by the Secretary or his delegate, be

1 *treated as wholly owned subsidiary corporations of*
2 *such shareholder organized under the laws of such*
3 *foreign countries, the Commonwealth of Puerto*
4 *Rico, or possessions of the United States, as the*
5 *case may be. Each branch so treated shall, for*
6 *purposes of this section, be considered to have distrib-*
7 *uted to the United States shareholder all of its*
8 *earnings and profits for the taxable year. This*
9 *subparagraph shall not apply to a branch main-*
10 *tained by a United States shareholder in the Com-*
11 *monwealth of Puerto Rico or a possession of the*
12 *United States unless—*

13 *“(i) such branch would be a controlled*
14 *foreign corporation (as defined in section 957)*
15 *if it were incorporated under the laws of the*
16 *Commonwealth of Puerto Rico or the possession*
17 *of the United States, as the case may be, and*

18 *“(ii) the gross income of the United States*
19 *shareholder for the taxable year includes income*
20 *derived from sources within the Commonwealth*
21 *of Puerto Rico and possessions of the United*
22 *States.*

23 *“(C) BLOCKED FOREIGN INCOME.—If a*
24 *United States shareholder so elects, the provisions*
25 *of subsection (a)(3) and of paragraph (3) of this*

1 subsection shall not apply with respect to any for-
2 eign corporation, if it is established to the satisfac-
3 tion of the Secretary or his delegate that the
4 earnings and profits of such foreign corporation
5 could not have been distributed to United States
6 shareholders who own (within the meaning of sec-
7 tion 958(a)) stock of such foreign corporation
8 because of currency or other restrictions or limita-
9 tions imposed under the laws of any foreign country.

10 “(d) *EFFECTIVE FOREIGN TAX RATE*.—For purposes
11 of this section, the term ‘effective foreign tax rate’ means—

12 “(1) with respect to a single controlled foreign cor-
13 poration, the percentage which—

14 “(A) the income, war profits, or excess profits
15 taxes paid or accrued to foreign countries or pos-
16 sessions of the United States by the controlled for-
17 eign corporation for the taxable year on or with re-
18 spect to its earnings and profits for the taxable year,
19 is of

20 “(B) the sum of (i) the earnings and profits
21 of the controlled foreign corporation described in
22 subparagraph (A) and (ii) and the taxes described
23 in subparagraph (A); and

24 “(2) with respect to two or more foreign corpora-
25 tions, the percentage which—

1 “(A) the total income, war profits, or excess
 2 profits taxes paid or accrued to foreign countries
 3 or possessions of the United States by such foreign
 4 corporations for the taxable year on or with respect
 5 to the total earnings and profits of such foreign
 6 corporations for the taxable year, is of

7 “(B) the sum of (i) the total earnings and
 8 profits of such foreign corporations described in
 9 subparagraph (A) and (ii) the taxes described in
 10 subparagraph (A).

11 For purposes of the preceding sentence, in the case of any
 12 United States shareholder, the computation of the effective
 13 foreign tax rate applicable with respect to any controlled
 14 foreign corporation or corporations shall be made without
 15 regard to distributions made by such controlled foreign corpo-
 16 ration or corporations to such United States shareholder.

17 “(e) SPECIAL RULES.—

18 “(1) YEAR FROM WHICH DISTRIBUTIONS ARE
 19 MADE.—For purposes of this section, the second sentence
 20 of section 902(c)(1) shall apply in determining from the
 21 earnings and profits of what year distributions are made
 22 by any foreign corporation, except that the Secretary or
 23 his delegate may by regulations provide a period in excess
 24 of 60 days in lieu of the 60-day period prescribed in
 25 such section.

1 “(2) *INSUFFICIENT DISTRIBUTIONS.—If—*

2 *“(A) a United States shareholder, in making its*
3 *return of the tax imposed by this chapter for any*
4 *taxable year, applies the provisions of this section*
5 *with respect to any controlled foreign corporation,*

6 *“(B) it is subsequently determined that this*
7 *section did not apply with respect to such controlled*
8 *foreign corporation for such taxable year due to the*
9 *failure of the United States shareholder to receive a*
10 *minimum distribution with respect to such controlled*
11 *foreign corporation, and*

12 *“(C) such failure is due to reasonable cause,*
13 *then a subsequent distribution made with respect*
14 *to such controlled foreign corporation may, if made*
15 *at a time and in a manner prescribed by the Secretary*
16 *or his delegate by regulations, be treated, for purposes of*
17 *this chapter, as having been made for, and received*
18 *in, the taxable year of the United States shareholder*
19 *for which such shareholder applied the provisions of*
20 *this section.*

21 “(3) *AFFILIATED GROUPS OF CORPORATIONS.—*

22 *An affiliated group of corporations which is eligible to*
23 *make a consolidated return under section 1501 for the*
24 *taxable year, may, if it so elects, be treated as a single*

1 *United States shareholder for purposes of applying this*
2 *section for the taxable year.*

3 “(f) *REGULATIONS.*—*The Secretary or his delegate*
4 *shall prescribe such regulations as he may deem necessary to*
5 *carry out the provisions of this section, including regulations*
6 *for the determination of the amount of foreign tax credit*
7 *in the case of distributions with respect to the earnings and*
8 *profits of two or more foreign corporations.*

9 “*SEC. 964. MISCELLANEOUS PROVISIONS.*

10 “(a) *EARNINGS AND PROFITS.*—*For purposes of this*
11 *subpart, the earnings and profits of any foreign corporation,*
12 *and the deficit in earnings and profits of any foreign corpora-*
13 *tion, for any taxable year shall be determined according to*
14 *rules substantially similar to those applicable to domestic*
15 *corporations, under regulations prescribed by the Secretary*
16 *or his delegate.*

17 “(b) *BLOCKED FOREIGN INCOME.*—*Under regulations*
18 *prescribed by the Secretary or his delegate, no part of the*
19 *earnings and profits of a controlled foreign corporation for*
20 *any taxable year shall be included in earnings and profits for*
21 *purposes of sections 952, 955, and 956, if it is established to*
22 *the satisfaction of the Secretary or his delegate that such part*

1 could not have been distributed by the controlled foreign
2 corporation to United States shareholders who own (within
3 the meaning of section 958(a)) stock of such controlled
4 foreign corporation because of currency or other restrictions
5 or limitations imposed under the laws of any foreign country.

6 “(c) RECORDS AND ACCOUNTS OF UNITED STATES
7 SHAREHOLDERS.—

8 “(1) RECORDS AND ACCOUNTS TO BE MAIN-
9 TAINED.—The Secretary or his delegate may by regula-
10 tions require each person who is, or has been, a United
11 States shareholder of a controlled foreign corporation
12 to maintain such records and accounts as may be pre-
13 scribed by such regulations as necessary to carry out
14 the provisions of this subpart and subpart G.

15 “(2) TWO OR MORE PERSONS REQUIRED TO
16 MAINTAIN OR FURNISH THE SAME RECORDS AND
17 ACCOUNTS WITH RESPECT TO THE SAME FOREIGN COR-
18 PORATION.—Where, but for this paragraph, two or more
19 United States persons would be required to maintain or
20 furnish the same records and accounts as may by regula-
21 tions be required under paragraph (1) with respect to
22 the same controlled foreign corporation for the same

1 *period, the Secretary or his delegate may by regulations*
2 *provide that the maintenance or furnishing of such*
3 *records and accounts by only one such person shall satisfy*
4 *the requirements of paragraph (1) for such other*
5 *persons.*

6 "Subpart G—Export Trade Corporations

"Sec. 970. Reduction of subpart F income of export trade corporations.

"Sec. 971. Definitions.

"Sec. 972. Consolidation of group of export trade corporations.

7 "SEC. 970. REDUCTION OF SUBPART F INCOME OF EXPORT
8 TRADE CORPORATIONS.

9 “(a) *EXPORT TRADE INCOME CONSTITUTING FOR-*
10 *EIGN BASE COMPANY INCOME.*—

“(1) *IN GENERAL.*—In the case of a controlled foreign corporation (as defined in section 957) which for the taxable year is an export trade corporation, the subpart F income (determined without regard to this subpart) of such corporation for such year shall be reduced by an amount equal to so much of the export trade income (as defined in section 971(b)) of such corporation for such year as constitutes foreign base company income (as defined in section 954), but only to the extent that such amount does not exceed whichever of the following amounts is the lesser:

1 “(A) an amount equal to $1\frac{1}{2}$ times so much of
2 the export promotion expenses (as defined in section
3 971(d)) of such corporation for such year as is
4 properly allocable to the export trade income which
5 constitutes foreign base company income of such
6 corporation for such year, or

7 “(B) an amount equal to 10 percent of so much
8 of the gross receipts for such year (or, in the case
9 of gross receipts arising from commissions, fees, or
10 other compensation for its services, so much of the
11 gross amount upon the basis of which such commis-
12 sions, fees, or other compensation is computed) ac-
13 cruing to such export trade corporation from the sale,
14 installation, operation, maintenance, or use of prop-
15 erty in respect of which such corporation derives
16 export trade income as is properly allocable to the
17 export trade income which constitutes foreign base
18 company income of such corporation for such year.

19 The allocations with respect to export trade income which
20 constitutes foreign base company income under sub-
21 paragraphs (A) and (B) shall be made under regula-
22 tions prescribed by the Secretary or his delegate.

23 “(2) OVERALL LIMITATION.—The reduction under

1 paragraph (1) for any taxable year shall not exceed
 2 an amount which bears the same ratio to the increase
 3 in the investments in export trade assets (as defined in
 4 section 971(c)) of such corporation for such year as
 5 the export trade income which constitutes foreign base
 6 company income of such corporation for such year bears
 7 to the entire export trade income of such corporation
 8 for such year.

9 “(b) *INCLUSION OF CERTAIN PREVIOUSLY EXCLUDED*
 10 *AMOUNTS.*—Each United States shareholder of a controlled
 11 foreign corporation which for any prior taxable year was an
 12 export trade corporation shall include in his gross income
 13 under section 951(a)(1)(A)(ii), as an amount to which sec-
 14 tion 955 (relating to withdrawal of previously excluded sub-
 15 part F income from qualified investment) applies, his pro rata
 16 share of the amount of decrease in the investments in export
 17 trade assets of such corporation for such year, but only to
 18 the extent that his pro rata share of such amount does not
 19 exceed an amount equal to—

20 “(1) his pro rata share of the sum of (A) the
 21 amounts by which the subpart F income of such cor-
 22 poration was reduced for all prior taxable years under
 23 subsection (a), and (B) the amounts not included in
 24 subpart F income (determined without regard to this

subpart) for all prior taxable years by reason of the application of section 972, reduced by

“(2) the sum of the amounts which were included in his gross income under section 951(a)(1)(A)(ii) under the provisions of this subsection for all prior taxable years.

“(c) INVESTMENTS IN EXPORT TRADE ASSETS.—

“(1) AMOUNT OF INVESTMENTS.—For purposes of this section, the amount taken into account with respect to any export trade asset shall be its adjusted basis, reduced by any liability to which the asset is subject.

“(2) INCREASE IN INVESTMENTS IN EXPORT TRADE ASSETS.—For purposes of subsection (a), the amount of increase in investments in export trade assets of any controlled foreign corporation for any taxable year is the amount by which—

“(A) the amount of such investments at the close of the taxable year, exceeds

“(B) the amount of such investments at the close of the preceding taxable year.

“(3) DECREASE IN INVESTMENTS IN EXPORT TRADE ASSETS.—For purposes of subsection (b), the amount of decrease in investments in export trade assets

1 of any controlled foreign corporation for any taxable
2 year is the amount by which—

3 “(A) the amount of such investments at the
4 close of the preceding taxable year (reduced by an
5 amount equal to the amount of net loss sustained
6 during the taxable year with respect to export trade
7 assets), exceeds

8 “(B) the amount of such investments at the
9 close of the taxable year.

10 “(4) SPECIAL RULE.—A United States shareholder
11 of an export trade corporation may, under regulations
12 prescribed by the Secretary or his delegate, make the
13 determinations under paragraphs (2) and (3) as of the
14 close of the 75th day after the close of the years referred
15 to in such paragraphs in lieu of on the last day of such
16 years. A United States shareholder of an export trade
17 corporation may, under regulations prescribed by the
18 Secretary or his delegate, make the determinations under
19 paragraphs (2) and (3) with respect to export trade
20 assets described in section 971(c)(3) as of the close of
21 the years following the years referred to in such para-
22 graphs, or as of the close of such longer period of time
23 as such regulations may permit, in lieu of on the last day
24 of such years and in lieu of on the day prescribed in the
25 preceding sentence. Any election under this paragraph

made with respect to any taxable year shall apply to such year and to all succeeding taxable years unless the Secretary or his delegate consents to the revocation of such election.

“SEC. 971. DEFINITIONS.

“(a) *EXPORT TRADE CORPORATION*.—For purposes of this subpart, the term ‘export trade corporation’ means—

“(1) *IN GENERAL*.—A controlled foreign corporation (as defined in section 957) which satisfies the following conditions:

“(A) 90 percent or more of the gross income of such corporation for the 3-year period immediately preceding the close of the taxable year (or such part of such period subsequent to the effective date of this subpart during which the corporation was in existence) was derived from sources without the United States, and

“(B) 75 percent or more of the gross income of such corporation for such period constituted gross income in respect of which such corporation derived export trade income.

“(2) *SPECIAL RULE*.—If 50 percent or more of the gross income of a controlled foreign corporation in the period specified in subsection (a)(1)(A) is gross income

1 in respect of which such corporation derived export trade
2 income in respect of agricultural products grown in the
3 the United States, it may qualify as an export trade
4 corporation although it does not meet the requirements
5 of subsection (a)(1)(B).

6 “(b) *EXPORT TRADE INCOME*.—For the purposes of
7 this subpart, the term ‘export trade income’ means net income
8 from—

9 “(1) the sale to an unrelated person for use, con-
10 sumption, or disposition outside the United States of
11 export property (as defined in subsection (e)), or from
12 commissions, fees, compensation, or other income from
13 the performance of commercial, industrial, financial,
14 technical, scientific, managerial, engineering, architec-
15 tural, skilled, or other services in respect of such sales
16 or in respect of the installation or maintenance of such
17 export property;

18 “(2) commissions, fees, compensation, or other
19 income from commercial, industrial, financial, technical,
20 scientific, managerial, engineering, architectural, skilled,
21 or other services performed in connection with the use
22 by an unrelated person outside the United States of
23 patents, copyrights, secret processes and formulas, good-
24 will, trademarks, trade brands, franchises, and other like
25 property acquired or developed and owned by the manu-

1 *facturer, producer, grower, or extractor of export prop-*
2 *erty in respect of which the export trade corporation*
3 *earns export trade income under paragraph (1);*

4 *“(3) commissions, fees, rentals, or other compensa-*
5 *tion or income attributable to the use of export property*
6 *by an unrelated person or attributable to the use of*
7 *export property in the rendition of technical, scientific,*
8 *or engineering services to an unrelated person; and*

9 *“(4) interest from export trade assets described in*
10 *subsection (c)(4).*

11 *For purposes of paragraph (3), if a controlled foreign cor-*
12 *poration receives income from an unrelated person attribut-*
13 *able to the use of export property in the rendition of services*
14 *to such unrelated person together with income attributable*
15 *to the rendition of other services to such unrelated person,*
16 *including personal services, the amount of such aggregate*
17 *income which shall be considered to be attributable to the use*
18 *of the export property shall (if such amount cannot be*
19 *established by reference to transactions between unrelated*
20 *persons) be that part of such aggregate income which the*
21 *cost of the export property consumed in the rendition of such*
22 *services (including a reasonable allowance for depreciation)*
23 *bears to the total costs and expenses attributable to such aggre-*
24 *gate income.*

1 “(c) *EXPORT TRADE ASSETS*.—For purposes of
2 this subpart, the term ‘export trade assets’ means—

3 “(1) working capital reasonably necessary for the
4 production of export trade income,

5 “(2) inventory of export property held for use,
6 consumption, or disposition outside the United States,

7 “(3) facilities located outside the United States for
8 the storage, handling, transportation, packaging, or
9 servicing of export property, and

10 “(4) evidences of indebtedness executed by persons,
11 other than related persons, in connection with payment
12 for purchases of export property for use, consumption, or
13 disposition outside the United States, or in connection
14 with the payment for services described in subsections
15 (b) (2) and (3).

16 “(d) *EXPORT PROMOTION EXPENSES*.—For pur-
17 poses of this subpart, the term ‘export promotion expenses’
18 means the following expenses paid or incurred in the receipt
19 or production of export trade income—

20 “(1) a reasonable allowance for salaries or other
21 compensation for personal services actually rendered for
22 such purpose,

23 “(2) rentals or other payments for the use of prop-
24 erty actually used for such purpose,

25 “(3) a reasonable allowance for the exhaustion,

1 wear and tear, or obsolescence of property actually used
2 for such purpose, and

3 “(4) any other ordinary and necessary expenses of
4 the corporation to the extent reasonably allocable to the
5 receipt or production of export trade income.

6 No expense incurred within the United States shall be treated
7 as an export promotion expense within the meaning of the
8 preceding sentence, unless at least 90 percent of each cate-
9 gory of expenses described in such sentence is incurred out-
10 side the United States.

11 “(e) *EXPORT PROPERTY*.—For purposes of this sub-
12 part, the term ‘export property’ means any property or any
13 interest in property manufactured, produced, grown, or ex-
14 tracted in the United States.

15 “(f) *UNRELATED PERSON*.—For purposes of this sub-
16 part, the term ‘unrelated person’ means a person other than a
17 related person as defined in section 954(d)(3).

18 **“SEC. 972. CONSOLIDATION OF GROUP OF EXPORT TRADE**
19 **CORPORATIONS.**

20 “For purposes of this subpart and subpart F of this
21 part, a United States shareholder of a controlled foreign cor-
22 poration which is an export trade corporation may, under
23 regulations prescribed by the Secretary or his delegate, treat
24 as a single controlled foreign corporation—

1 “(1) such controlled foreign corporation,

2 “(2) all controlled foreign corporations which are
3 export trade corporations and 80 percent or more of
4 the total combined voting power of all classes of stock
5 entitled to vote of which is owned by such controlled
6 foreign corporation; and

7 “(3) all controlled foreign corporations which are
8 export trade corporations and 80 percent or more of
9 the total combined voting power of all classes of stock
10 entitled to vote of which is owned by controlled for-
11 eign corporations described in paragraph (2).”

12 (b) *TECHNICAL AND CLERICAL AMENDMENTS.*—

13 (1) Section 901 (relating to foreign tax credit)
14 is amended by striking out “section 902” and inserting in
15 lieu thereof “sections 902 and 960”.

16 (2) Section 904(g) (as redesignated by section
17 10(a) of this Act) is amended to read as follows:

18 “(g) *CROSS REFERENCES.*—

 “(1) For increase of applicable limitation under sub-
section (a) for taxes paid with respect to amounts re-
ceived which were included in the gross income of the
taxpayer for a prior taxable year as a United States
shareholder with respect to a controlled foreign corpora-
tion, see section 960(b).

 “(2) For special rule relating to the application of the
credit provided by section 901 in the case of affiliated
groups which include Western Hemisphere trade corpo-
rations for years in which the limitation provided by
subsection (a)(2) applies, see section 1503(d).”

1 (3) *The table of subparts for part III of sub-*
2 *chapter N of chapter 1 is amended by adding at the end*
3 *thereof the following:*

"Subpart F. Controlled foreign corporations.

"Subpart G. Export trade corporations."

4 (4) *Section 1016(a) (relating to adjustments to*
5 *basis) is amended by adding after paragraph (19) (as*
6 *added by section 2(f) of this Act) the following new*
7 *paragraph:*

8 *"(20) to the extent provided in section 961 in the*
9 *case of stock in controlled foreign corporations (or for-*
10 *foreign corporations which were controlled foreign cor-*
11 *porations) and of property by reason of which a person*
12 *is considered as owning such stock."*

13 (c) *EFFECTIVE DATE.—The amendments made by*
14 *this section shall apply with respect to taxable years of foreign*
15 *corporations beginning after December 31, 1962, and to*
16 *taxable years of United States shareholders within which or*
17 *with which such taxable years of such foreign corporations*
18 *end.*

1 SEC. (127)¹⁴ 13. GAIN FROM DISPOSITIONS OF CERTAIN
2 DEPRECIABLE PROPERTY.

3 (a) IN GENERAL.—

4 (1) Part IV of subchapter P of chapter 1 (relating
5 to special rules for determining capital gains and losses)
6 is amended by adding at the end thereof the following
7 new section:

8 “SEC. 1245. GAIN FROM DISPOSITIONS OF CERTAIN DE-
9 PRECIABLE PROPERTY.

10 “(a) GENERAL RULE.—

11 “(1) ORDINARY INCOME.—Except as otherwise
12 provided in this section, if section 1245 property is dis-
13 posed of (128)¹⁴ after the date of the enactment of the
14 Revenue Act of 1962 during a taxable year beginning
15 after December 31, 1962, the amount by which the
16 lower of—

17 “(A) the recomputed basis of the property, or

18 “(B) (i) in the case of a sale, exchange, or
19 involuntary conversion, the amount realized, or

20 “(ii) in the case of any other disposition, the
21 fair market value of such property,

22 exceeds the adjusted basis of such property shall be
23 treated as gain from the sale or exchange of property
24 which is neither a capital asset nor property described in

1 section 1231. Such gain shall be recognized notwith-
2 standing any other provision of this subtitle.

3 “(2) RECOMPUTED BASIS.—For purposes of this
4 section, the term ‘recomputed basis’ means, with respect
5 to any property, its adjusted basis recomputed by adding
6 thereto all adjustments, ~~(129)~~for taxable years beginning
7 *attributable to periods* after December 31, 1961, reflected
8 in such adjusted basis on account of deductions (whether
9 in respect of the same or other property) allowed or
10 allowable to the taxpayer or to any other person for
11 depreciation, or for amortization under section 168. For
12 purposes of the preceding sentence, if the taxpayer can
13 establish by adequate records or other sufficient evidence
14 that the amount allowed for depreciation, or for amorti-
15 zation under section 168, for any ~~(130)~~taxable year
16 *period* was less than the amount allowable, the amount
17 added for such ~~(131)~~taxable year *period* shall be the
18 amount allowed.

19 “(3) SECTION 1245 PROPERTY.—For purposes
20 of this section, the term ‘section 1245 property’ means
21 any property (other than livestock) which is or has
22 been property of a character subject to the allowance
23 for depreciation provided in section 167 and is either—

24 “(A) personal property, or

1 “(B) other property (not including a building
2 or its structural components) but only if such other
3 property is tangible and has an adjusted basis in
4 which there are reflected adjustments described in
5 paragraph (2) for a period in which such prop-
6 erty (or other property) —

7 “(i) was used as an integral part of manu-
8 facturing, production, or extraction or of fur-
9 nishing transportation, communications, electri-
10 cal energy, gas, water, or sewage disposal serv-
11 ices, or

12 “(ii) constituted research or storage facili-
13 ties used in connection with any of the activi-
14 ties referred to in clause (i).

15 “(b) EXCEPTIONS AND LIMITATIONS.—

16 “(1) GIFTS.—Subsection (a) shall not apply to a
17 disposition by gift.

18 “(2) TRANSFERS AT DEATH.—Except as provided
19 in section 691 (relating to income in respect of a de-
20 cedent), subsection (a) shall not apply to a transfer at
21 death.

22 “(3) CERTAIN TAX-FREE TRANSACTIONS.—If the
23 basis of property in the hands of a transferee is deter-
24 mined by reference to its basis in the hands of the trans-
25 feror by reason of the application of section 332, 351,

1 361, 371 (a), 374 (a), 721, or 731, then the amount of
2 gain taken into account by the transferor under subsec-
3 tion (a) (1) shall not exceed the amount of gain recog-
4 nized to the transferor on the transfer of such property
5 (determined without regard to this section). This para-
6 graph shall not apply to a disposition to an organization
7 (other than a cooperative described in section 521)
8 which is exempt from the tax imposed by this chapter.

9 “(4) LIKE KIND EXCHANGES; INVOLUNTARY CON-
10 VERSIONS, ETC.—If property is disposed of and gain
11 (determined without regard to this section) is not rec-
12 ognized in whole or in part under section 1031 or 1033,
13 then the amount of gain taken into account by the trans-
14 feror under subsection (a) (1) shall not exceed the
15 sum of—

16 “(A) the amount of gain recognized on such
17 disposition (determined without regard to this sec-
18 tion), plus

19 “(B) the fair market value of property acquired
20 which is not section 1245 property and which is not
21 taken into account under subparagraph (A).

22 “(5) SECTION 1071 AND 1081 TRANSACTIONS.—
23 Under regulations prescribed by the Secretary or his
24 delegate, rules consistent with paragraphs (3) and (4)
25 of this subsection shall apply in the case of transactions

1 described in section 1071 (relating to gain from sale
2 or exchange to effectuate policies of FCC) or section
3 1081 (relating to exchanges in obedience to SEC
4 orders) .

5 “(6) PROPERTY DISTRIBUTED BY A PARTNERSHIP
6 TO A PARTNER.—

7 “(A) IN GENERAL.—For purposes of this sec-
8 tion, the basis of section 1245 property distributed
9 by a partnership to a partner shall be deemed to
10 be determined by reference to the adjusted basis of
11 such property to the partnership.

12 “(B) ADJUSTMENTS ADDED BACK.—In the
13 case of any property described in subparagraph
14 (A), for purposes of computing the recomputed
15 basis of such property the amount of the adjustments
16 added back for periods before the distribution by
17 the partnership shall be—

18 “(i) the amount of the gain to which sub-
19 section (a) would have applied if such property
20 had been sold by the partnership immediately
21 before the distribution at its fair market value
22 at such time, reduced by

23 “(ii) the amount of such gain to which
24 section 751 (b) applied.

25 “(c) ADJUSTMENTS TO BASIS.—The Secretary or his

1 delegate shall prescribe such regulations as he may deem
 2 necessary to provide for adjustments to the basis of property
 3 to reflect gain recognized under subsection (a).

4 “(d) APPLICATION OF SECTION.—This section shall
 5 apply notwithstanding any other provision of this subtitle.”

6 (2) The table of sections for such part IV is
 7 amended by adding at the end thereof the following:

“Sec. 1245. Gain from dispositions of certain depreciable
 property.”

8 (b) CHANGE IN METHOD OF DEPRECIATION.—Sub-
 9 section (e) of section 167 (relating to depreciation) is
 10 amended to read as follows:

11 “(e) CHANGE IN METHOD.—

12 “(1) CHANGE FROM DECLINING BALANCE
 13 METHOD.—In the absence of an agreement under sub-
 14 section (d) containing a provision to the contrary, a
 15 taxpayer may at any time elect in accordance with regu-
 16 lations prescribed by the Secretary or his delegate to
 17 change from the method of depreciation described in
 18 subsection (b) (2) to the method described in subsec-
 19 tion (b) (1).

20 “(2) CHANGE WITH RESPECT TO SECTION 1245
 21 PROPERTY.—A taxpayer may, (132)within such period
 22 after the date of the enactment of the Revenue Act of

1 ~~1962~~ on or before the last day prescribed by law (includ-
 2 ing extensions thereof) for filing his return for his first tax-
 3 able year beginning after December 31, 1962, and in
 4 such manner as the Secretary or his delegate shall by
 5 regulations prescribe, elect to change his method of
 6 depreciation in respect of section 1245 property (as
 7 defined in section 1245 (a) (3)) from any declining
 8 balance or sum of the years-digits method to the
 9 straight line method. An election may be made under
 10 this paragraph notwithstanding any provision to the
 11 contrary in an agreement under subsection (d).”

12 (c) SALVAGE VALUE OF PERSONAL PROPERTY.—

13 (1) AMOUNT TAKEN INTO ACCOUNT.—Section
 14 167 (relating to depreciation) is amended by redesignat-
 15 ing subsections (f), (g), and (h) as (g), (h), and
 16 (i), respectively, and by inserting after subsection (e)
 17 the following new subsection:

18 “(f) SALVAGE VALUE.—

19 “(1) GENERAL RULE.—Under regulations pre-
 20 scribed by the Secretary or his delegate, a taxpayer may,
 21 for purposes of computing the allowance under sub-
 22 section (a) with respect to personal property, reduce
 23 the amount taken into account as salvage value by an
 24 amount which does not exceed 10 percent of the basis
 25 of such property (as determined under subsection (g)

as of the time as of which such salvage value is required to be determined).

“(2) PERSONAL PROPERTY DEFINED.—For purposes of this subsection, the term ‘personal property’ means depreciable personal property (other than livestock) with a useful life of 3 years or more acquired after the date of the enactment of the Revenue Act of 1962.”

(2) CONFORMING AMENDMENTS.—

(A) Sections 179 (d) (5) and 642 (e) are each amended by striking out “167 (g)” and inserting in lieu thereof “167 (h)”.

(B) Section 179 (d) (8) is amended by striking out “167 (f)” and inserting in lieu thereof “167 (g)”.

(d) SPECIAL RULE FOR CHARITABLE CONTRIBUTIONS OF SECTION 1245 PROPERTY.—Section 170 (relating to charitable, etc., contributions and gifts) is amended by redesignating subsections (e) and (f) as (f) and (g), respectively, and by inserting after subsection (d) the following new subsection:

“(e) SPECIAL RULE FOR CHARITABLE CONTRIBUTIONS OF SECTION 1245 PROPERTY.—The amount of any charitable contribution taken into account under this section shall be reduced by the amount which would have been treated as gain to which section 1245 (a) applies if the prop-

erty contributed had been sold at its fair market value
(determined at the time of such contribution).”

(133)(e) *COMPUTATION OF TAXABLE INCOME FOR PURPOSES OF LIMITATION ON PERCENTAGE DEPLETION DEDUCTION.*—Section 613(a) (relating to percentage depletion) is amended by inserting after the second sentence thereof the following new sentence: “For purposes of the preceding sentence, the allowable deductions taken into account with respect to expenses of mining in computing the taxable income from the property shall be decreased by an amount equal to so much of any gain which (1) is treated under section 1245 (relating to gain from disposition of certain depreciable property) as gain from the sale or exchange of property which is neither a capital asset nor property described in section 1231, and (2) is properly allocable to the property.”

(134)(e)(f) *TECHNICAL AMENDMENTS.*—

(1) *SPECIAL RULE FOR PARTNERSHIPS.*—Section 751(c) (relating to definition of “unrealized receivables” for purposes of subchapter K) is amended by adding after paragraph (2) the following:
“For purposes of this section and sections 731, 736, and 741, such term also includes section 1245 property (as defined in section 1245(a)(3)), but only to the extent of the amount which would be treated as gain to which section

1 1245 (a) would apply if (at the time of the transaction de-
 2 scribed in this section or section 731, 736, or 741, as the
 3 case may be) such property had been sold by the partner-
 4 ship at its fair market value.”

5 (2) CORPORATE DISTRIBUTION OF PROPERTY.—

6 Subsections (b) and (d) of section 301 (relating to
 7 amount distributed) are each amended by striking out
 8 “subsection (b) or (c) of section 311” and inserting in
 9 lieu thereof “subsection (b) or (c) of section 311 or
 10 under section 1245 (a)”.

11 (3) EFFECT ON EARNINGS AND PROFITS.—Section

12 312 (c) (3) (relating to adjustments of earnings and
 13 profits) is amended by striking out “subsection (b)
 14 or (c) of section 311” and inserting in lieu thereof
 15 “subsection (b) or (c) of section 311 or under sec-
 16 tion 1245 (a)”.

17 (4) COLLAPSIBLE CORPORATIONS.—Section 341

18 (c) (relating to collapsible corporations) is amended
 19 by inserting after paragraph (11) the following new
 20 paragraph:

21 “(12) NONAPPLICATION OF SECTION 1245(a).—

22 For purposes of this subsection, the determination of
 23 whether gain from the sale or exchange of property
 24 would under any provision of this chapter be considered
 25 as gain from the sale or exchange of property which is

1 neither a capital asset nor property described in section
2 1231 (b) shall be made without regard to the applica-
3 tion of section 1245 (a).”

4 (5) INSTALLMENT OBLIGATIONS IN CERTAIN
5 LIQUIDATIONS.—

6 (A) Section 453 (d) (4) (A) (relating to
7 distribution of installment obligations in section 332
8 liquidations) is amended by adding at the end there-
9 of the following new sentence: “If the basis of the
10 property of the liquidating corporation in the hands
11 of the distributee is determined under section 334
12 (b) (2) then the preceding sentence shall not apply
13 to the extent that under paragraph (1) gain to the
14 distributing corporation would be considered as gain
15 to which section 1245 (a) applies.”

16 (B) Section 453 (d) (4) (B) (relating to dis-
17 tribution of installment obligations in liquidations
18 to which section 337 applies) is amended by adding
19 at the end thereof the following new sentence: “The
20 preceding sentence shall not apply to the extent that
21 under paragraph (1) gain to the distributing cor-
22 poration would be considered as gain to which sec-
23 tion 1245 (a) applies.”

24 (135)(f) ~~EFFECTIVE DATE.~~—The amendments made by this
25 section shall apply to taxable years beginning after December

1 31, 1961, and ending after the date of the enactment of
2 this Act.

3 (g) *EFFECTIVE DATES.*—The amendments made by
4 this section (other than the amendments made by subsection
5 (c)) shall apply to taxable years beginning after December
6 31, 1962. The amendments made by subsection (c) shall
7 apply to taxable years beginning after December 31, 1961,
8 and ending after the date of the enactment of this Act.

9 **SEC. (136)~~15~~ 14. FOREIGN INVESTMENT COMPANIES.**

10 (a) **TREATMENT OF SALE OF STOCK OF FOREIGN**
11 **INVESTMENT COMPANIES.**—

12 (1) **IN GENERAL.**—Part IV of subchapter P of
13 chapter 1 (relating to special rules for determining
14 capital gains and losses) is amended by adding after
15 section 1245 (as added by section (137)~~14~~ 13 of this
16 Act) the following new sections:

17 **“SEC. 1246. GAIN ON FOREIGN INVESTMENT COMPANY**
18 **STOCK.**

19 **“(a) TREATMENT OF GAIN AS ORDINARY INCOME.**—

20 **“(1) GENERAL RULE.**—In the case of a sale or
21 exchange (138)(or a distribution which, under section
22 302 or 331, is treated as an exchange of stock) after
23 December 31, 1962, of stock in a foreign corporation
24 which was a foreign investment company (as defined in
25 subsection (b)) at any time during the period during

1 which the taxpayer held such stock, any gain shall be
2 treated as gain from the sale or exchange of property
3 which is not a capital asset, to the extent of the tax-
4 payer's ratable share of the earnings and profits of such
5 corporation accumulated for taxable years beginning
6 after December 31, 1962.

7 “(2) RATABLE SHARE.—For purposes of this sec-
8 tion, the taxpayer's ratable share shall be determined
9 under regulations prescribed by the Secretary or his
10 delegate, but shall include only his ratable share of the
11 accumulated earnings and profits of such corporation—

12 “(A) for the period during which the taxpayer
13 held such stock, but

14 (139)“(B) ~~excluding such earnings and profits~~
15 ~~which were taxed to such taxpayer under section~~
16 ~~951 or under section 551.~~

17 “(B) *excluding such earnings and profits at-*
18 *tributable to any amount previously included in the*
19 *gross income of such taxpayer under section 951*
20 *(but only to the extent the inclusion of such amount*
21 *did not result in an exclusion of any other amount*
22 *from gross income under section 959).*

23 “(3) TAXPAYER TO ESTABLISH EARNINGS AND
24 PROFITS.—Unless the taxpayer establishes the amount
25 of the accumulated earnings and profits of the foreign

investment company and the ratable share thereof for the period during which the taxpayer held such stock, all the gain from the sale or exchange of stock in such company shall be considered as gain from the sale or exchange of property which is not a capital asset.

“(4) HOLDING PERIOD OF STOCK MUST BE MORE THAN 6 MONTHS.—This section shall not apply with respect to the sale or exchange of stock where the holding period of such stock as of the date of such sale or exchange is 6 months or less.

“(b) DEFINITION OF FOREIGN INVESTMENT COMPANY.—For purposes of this section, the term ‘foreign investment company’ means any foreign ~~(140) corporation—~~ *corporation which, for any taxable year beginning after December 31, 1962, is—*

“(1) registered under the Investment Company Act of 1940, as amended (15 U.S.C. 80a-1 to 80b-2), either as a management company or as a unit investment trust, or

“(2) engaged (or holding itself out as being engaged) primarily in the business of investing, reinvesting, or trading in securities (within the meaning of section 3 (a) (1) of such ~~(141) Act~~ *Act, as limited by paragraphs (2) through (10) (except paragraph (6) (C)) and paragraphs (12) through (15) of section 3*

1 *(c) of such Act)* at a time when more than 50 percent of
 2 the total combined voting power of all classes of stock
 3 entitled to vote, or of the total value of shares of all
 4 classes of stock, was held, directly or indirectly (within
 5 the meaning of section ~~(142)~~955 958 (a)), by United
 6 States persons (as defined in section 7701 (a) (30)).

7 “(c) STOCK HAVING TRANSFERRED OR SUBSTITUTED
 8 BASIS.—To the extent provided in regulations prescribed
 9 by the Secretary or his delegate, stock in a foreign corpora-
 10 tion, the basis of which (in the hands of the taxpayer selling
 11 or exchanging such stock) is determined by reference to the
 12 basis (in the hands of such taxpayer or any other person)
 13 of stock in a foreign investment company, shall be treated
 14 as stock of a foreign investment company and held by the
 15 taxpayer throughout the holding period for such stock (deter-
 16 mined under section 1223) .

17 “(d) RULES RELATING TO ENTITIES HOLDING FOR-
 18 EIGN INVESTMENT COMPANY STOCK.—To the extent pro-
 19 vided in regulations prescribed by the Secretary or his
 20 delegate—

21 “(1) trust certificates of a trust to which section
 22 677 (relating to income for benefit of grantor) applies,
 23 and

24 “(2) stock of a domestic corporation,
 25 shall be treated as stock of a foreign investment company

1 and held by the taxpayer throughout the holding period for
 2 such certificates or stock (determined under section 1223)
 3 in the same proportion that the investment in stock in a for-
 4 eign investment company by the trust or domestic corpora-
 5 tion bears to the total assets of such trust or corporation.

6 “(e) RULES RELATING TO STOCK ACQUIRED FROM A
 7 DECEDENT.—

8 “(1) BASIS.—In the case of stock of a foreign
 9 investment company acquired by bequest, devise, or
 10 inheritance (or by the decedent’s estate) from a dece-
 11 dent dying after December 31, 1962, the basis deter-
 12 mined under section 1014 shall be reduced (but not
 13 below the adjusted basis of such stock in the hands of
 14 the decedent immediately before his death) by the
 15 amount of the decedent’s ratable share of the (143)~~accu-~~
 16 ~~mulated earnings and profits of such company~~ *earnings*
 17 *and profits of such company accumulated after Decem-*
 18 *ber 31, 1962.* Any stock so acquired shall be treated as
 19 stock described in subsection (c).

20 “(2) DEDUCTION FOR ESTATE TAX.—If stock to
 21 which subsection (a) applies is acquired from a dece-
 22 dent, the taxpayer shall, under regulations prescribed
 23 by the Secretary or his delegate, be allowed (for the
 24 taxable year of the sale or exchange) a deduction from
 25 gross income equal to that portion of the decedent’s

1 estate tax deemed paid which is attributable to the excess
 2 of (A) the value at which such stock was taken into
 3 account for purposes of determining the value of the
 4 decedent's gross estate, over (B) the value at which
 5 it would have been so taken into account if such value
 6 had been reduced by the amount described in para-
 7 graph (1).

8 “(f) INFORMATION WITH RESPECT TO CERTAIN
 9 FOREIGN ~~(144)~~INVESTMENT.—*INVESTMENT COMPANIES.*—
 10 Every United States person who, on the last day of the tax-
 11 able year of a foreign investment company beginning after
 12 December 31, 1962, owns 5 percent or more in value of the
 13 stock of such company shall furnish with respect to such
 14 company such information as the Secretary or his delegate
 15 shall by regulations prescribe.

16 ~~(145)~~“(g) *NONAPPLICATION OF SECTION 367 IN CERTAIN*
 17 *CASES.*—*Section 367 shall not apply in respect of a foreign*
 18 *investment company described in paragraph (1) of subsection*
 19 *(b) which is a party to a reorganization in which all of its*
 20 *properties are acquired before January 1, 1964, by a*
 21 *domestic corporation which is a regulated investment company*
 22 *under section 851 for its first taxable year ending after the*
 23 *reorganization, but only if such foreign investment company*
 24 *made the election described in section 1247 with respect to its*
 25 *taxable years beginning after December 31, 1962.*

1 ~~(146)~~^{“(g)} “(h) CROSS REFERENCE.—

“For special rules relating to the earnings and profits
of foreign investment companies, see section 312(l).

2 “SEC. 1247. ELECTION BY FOREIGN INVESTMENT COM-
3 PANIES TO DISTRIBUTE INCOME CUR-
4 RENTLY.

5 “(a) ELECTION BY FOREIGN INVESTMENT COM-
6 PANY.—

7 “(1) IN GENERAL.—If a foreign investment com-
8 pany which is described in section 1246(b)(1) elects
9 (in the manner provided in regulations prescribed by
10 the Secretary or his delegate) on or before December
11 31, 1962, with respect to each taxable year beginning
12 after December 31, 1962, to—

13 “(A) distribute to its shareholders 90 percent
14 or more of what its taxable income would be if it
15 were a domestic corporation;

16 “(B) designate in a written notice mailed to
17 its shareholders at any time before the expiration
18 of ~~(147)~~ ~~30~~ 45 days after the close of its taxable
19 year the pro rata amount of the excess (determined
20 as if such corporation were a domestic corporation)
21 of the net long-term capital ~~(148)~~ ~~gains~~ *gain* over
22 the net short-term capital ~~(149)~~ ~~losses~~ *loss of the tax-*

1 *year*; and the portion thereof which is being distri-
 2 buted; and

3 “(C) provide such information as the Secre-
 4 tary or his delegate deems necessary to carry out the
 5 purposes of this section,

6 then section 1246 shall not apply with respect to the
 7 qualified shareholders of such company during any
 8 taxable year to which such election applies.

9 “(2) SPECIAL RULES.—

10 “(A) COMPUTATION OF TAXABLE INCOME.—

11 For purposes of paragraph (1) (A), the taxable
 12 income of the company shall be computed without
 13 regard to—

14 “(i) the excess of ~~(150) capital gains over~~
 15 ~~losses~~ *the net long-term capital gain over the net*
 16 *short-term capital loss* referred to in paragraph
 17 (1 (B),

18 “(ii) section 172 (relating to net operating
 19 losses), and

20 “(iii) any deduction provided by part VIII
 21 of subchapter B (other than the deduction pro-
 22 vided by section 248, relating to organizational
 23 expenditures).

“(B) DISTRIBUTIONS AFTER THE CLOSE OF THE TAXABLE YEAR.—For purposes of paragraph (1) (A), a distribution made after the close of the taxable year and on or before the 15th day of the third month of the next taxable year shall be treated as distributed during the taxable year to the extent elected by the company (in accordance with regulations prescribed by the Secretary or his delegate) on or before the 15th day of such third month.

“(C) CARRYOVER OF CAPITAL LOSSES FROM NONELECTION YEARS DENIED.—In computing the excess of ~~(151) capital gains over losses~~ *the net long-term capital gain over the net short-term capital loss* referred to in paragraph (1) (B), section 1212 shall not apply to losses incurred in or with respect to taxable years before the first taxable year to which the election applies.

“(b) YEARS TO WHICH ELECTION APPLIES.—The election of any foreign investment company under this section shall terminate as of the close of the taxable year preceding its first taxable year in which any of the following occurs:

“(1) the company fails to comply with the provi-

1 sions of subparagraph (A), (B), or (C) of subsection
 2 (a) (1), unless it is shown that such failure is due to
 3 reasonable cause and not due to willful neglect,

4 “(2) the company is a foreign personal holding
 5 company, or

6 “(3) the company is not a foreign investment com-
 7 pany which is described in section 1246(b) (1).

8 “(c) QUALIFIED SHAREHOLDERS.—For purposes of
 9 this section—

10 “(1) IN GENERAL.—The term ‘qualified share-
 11 holder’ means any shareholder who is a United States
 12 person **(152)** *(as defined in section 7701(a)(30))*, other
 13 than a shareholder described in paragraph (2).

14 “(2) CERTAIN UNITED STATES PERSONS EX-
 15 CLUDED FROM DEFINITION.—A United States person
 16 shall not be treated as a qualified shareholder for the
 17 taxable year if for such taxable year (or for any prior
 18 taxable year) he did not include, in computing his long-
 19 term capital gains in his return for such taxable year,
 20 the amount designated by such company pursuant to
 21 subsection (a) (1) (B) as his share of the undistributed
 22 capital gains of such company for its taxable year end-
 23 ing within or with such taxable year of the taxpayer.
 24 The preceding sentence shall not apply with respect

to any failure by the taxpayer to treat an amount as provided therein if the taxpayer shows that such failure was due to reasonable cause and not due to willful neglect.

(153)“(d) ADJUSTMENTS.—Under regulations prescribed by the Secretary or his delegate, proper adjustment shall be made—

“(1) in the earnings and profits of the electing foreign investment company, and

“(2) the adjusted basis of stock of such company held by qualified shareholders,

to reflect the inclusion in gross income by such shareholders of undistributed capital gains.

“(d) TREATMENT OF DISTRIBUTED AND UNDISTRIBUTED CAPITAL GAINS BY A QUALIFIED SHAREHOLDER.—Every qualified shareholder of a foreign investment company for any taxable year of such company with respect to which an election pursuant to subsection (a) is in effect shall include, in computing his long-term capital gains—

“(1) for his taxable year in which received, his pro rata share of the distributed portion of the excess of the net long-term capital gain over the net short-term capital loss for such taxable year of such company, and

1 “(2) for his taxable year in which or with which
2 the taxable year of such company ends, his pro rata share
3 of the undistributed portion of the excess of the net
4 long-term capital gain over the net short-term capital loss
5 for such taxable year of such company.

6 “(e) ADJUSTMENTS.—Under regulations prescribed
7 by the Secretary or his delegate, proper adjustment shall be
8 made—

9 “(1) in the earnings and profits of the electing
10 foreign investment company and a qualified shareholder’s
11 ratable share thereof, and

12 “(2) in the adjusted basis of stock of such company
13 held by such shareholder,
14 to reflect such shareholder’s inclusion in gross income of
15 undistributed capital gains.

16 “(f) ELECTION BY FOREIGN INVESTMENT COMPANY
17 WITH RESPECT TO FOREIGN TAX CREDIT.—A foreign in-
18 vestment company with respect to which an election pur-
19 suant to subsection (a) is in effect and more than 50 per-
20 cent of the value (as defined in section 851(c)(4)) of
21 whose total assets at the close of the taxable year consists
22 of stock or securities in foreign corporations may, for such
23 taxable year, elect the application of this subsection with
24 respect to income, war profits, and excess profits taxes
25 described in section 901(b)(1) which are paid by the for-

1 *foreign investment company during such taxable year to foreign*
2 *countries and possessions of the United States. If such elec-*
3 *tion is made—*

4 “(1) *the foreign investment company—*

5 “(A) *shall compute its taxable income, for pur-*
6 *poses of subsection (a)(1)(A), without any deduc-*
7 *tions for income, war profits, or excess profits taxes*
8 *paid to foreign countries or possessions of the United*
9 *States, and*

10 “(B) *shall treat the amount of such taxes, for*
11 *purposes of subsection (a)(1)(A), as distributed*
12 *to its shareholders;*

13 “(2) *each qualified shareholder of such foreign in-*
14 *vestment company—*

15 “(A) *shall include in gross income and treat*
16 *as paid by him his proportionate share of such taxes,*
17 *and*

18 “(B) *shall treat, for purposes of applying sub-*
19 *part A of part III of subchapter N, his proportion-*
20 *ate share of such taxes as having been paid to the*
21 *country in which the foreign investment company*
22 *is incorporated, and*

23 “(C) *shall treat as gross income from sources*
24 *within the country in which the foreign investment*
25 *company is incorporated, for purposes of applying*

1 subpart A of part III of subchapter N, the sum of
2 his proportionate share of such taxes and any
3 dividend paid to him by such foreign investment
4 company.

5 “(g) NOTICE TO SHAREHOLDERS.—The amounts to be
6 treated by qualified shareholders, for purposes of subsection
7 (f)(2), as their proportionate share of the taxes described in
8 subsection (f)(1)(A) paid by a foreign investment company
9 shall not exceed the amounts so designated by the foreign
10 investment company in a written notice mailed to its share-
11 holders not later than 45 days after the close of its taxable
12 year.

13 “(h) MANNER OF MAKING ELECTION AND NOTIFY-
14 ING SHAREHOLDERS.—The election provided in subsection
15 (f) and the notice to shareholders required by subsection (g)
16 shall be made in such manner as the Secretary or his delegate
17 may prescribe by regulations.

18 (154)“(e) “(i) LOSS ON SALE OR EXCHANGE OF CERTAIN
19 STOCK HELD LESS THAN 6 MONTHS.—If—

20 “(1) under this section, any qualified shareholder
21 treats any amount designated under subsection (a) (1)
22 (B) with respect to a share of stock as long-term capital
23 gain, and

24 “(2) such share is held by the taxpayer for less
25 than 6 months,

1 then any loss on the sale or exchange of such share shall,
 2 to the extent of the amount described in paragraph (1),
 3 be treated as loss from the sale or exchange of a capital
 4 asset held for more than 6 months.”

5 (2) The table of sections for such part IV is
 6 amended by adding at the end thereof the following:

“Sec. 1246. Gain on foreign investment company (155) *stock*.
 “Sec. 1247. Election by foreign investment companies to
 distribute income currently.”

7 (b) CONFORMING AMENDMENTS.—

8 (1) EARNINGS AND PROFITS OF FOREIGN IN-
 9 VESTMENT COMPANIES.—Section 312 (relating to
 10 effect on earnings and profits) is amended by adding
 11 after subsection (k) the following new subsection:

12 “(1) EARNINGS AND PROFITS OF FOREIGN INVEST-
 13 MENT COMPANIES.—

14 “(1) ALLOCATION WITHIN AFFILIATED GROUP.—

15 In the case of a sale or exchange of stock in a foreign
 16 investment company (as defined in section 1246 (b))
 17 by a United States person (as defined in section 7701
 18 (a) (30)), if such company is a member of an affiliated
 19 group, then the accumulated earnings and profits of all
 20 members of such affiliated group shall be allocated, under
 21 regulations prescribed by the Secretary or his delegate,
 22 in such manner as is proper to carry out the purposes of
 23 section 1246.

1 “(2) AFFILIATED GROUP DEFINED.—For purposes
 2 of ~~(156) paragraphs (1) and (2)~~ *paragraph (1)* of this
 3 subsection, the term ‘affiliated group’ has the meaning
 4 assigned to such term by section 1504 (a) ; except that
 5 (A) ‘more than 50 percent’ shall be substituted for
 6 ‘80 percent or more’, and (B) all corporations shall be
 7 treated as includible corporations (without regard to the
 8 provisions of section 1504 (b)).

9 “(3) PARTIAL LIQUIDATIONS AND REDEMP-
 10 TIONS.—

11 “(A) IN GENERAL.—If a foreign investment
 12 company (as defined in section 1246) distributes
 13 amounts in partial liquidation or in a redemption to
 14 which section 302 (a) or 303 applies, the part of
 15 such distribution which is properly chargeable to
 16 earnings and profits shall be an amount which is
 17 not in excess of the ratable share of the earnings
 18 and profits of the company accumulated after
 19 February 28, 1913, attributable to the stock so
 20 redeemed.

21 “(B) EFFECTIVE DATE.—Subparagraph (A)
 22 shall apply only with respect to distributions made
 23 after December 31, 1962.”

24 “(2) SALE OR EXCHANGE OF INTEREST IN PART-

1 NERSHIP.—Section 751 (d) (2) (relating to inventory
2 items which have appreciated substantially in value) is
3 amended by striking out “and” at the end of subpara-
4 graph (B), and by striking out subparagraph (C) and
5 inserting in lieu thereof the following new subparagraphs:

6 “(C) any other property of the partnership
7 which, if sold or exchanged by the partnership,
8 would result in a gain taxable under subsection (a)
9 of section 1246 (relating to gain on foreign invest-
10 ment company stock), and

11 “(D) any other property held by the partner-
12 ship which, if held by the selling or distributee part-
13 ner, would be considered property of the type
14 described in subparagraph (A), (B), or (C).”

15 (3) HOLDING PERIOD OF PROPERTY.—Section
16 1223 (relating to holding period of property) is amended
17 by redesignating paragraph (10) as paragraph (11)
18 and inserting after paragraph (9) the following para-
19 graph:

20 “(10) In determining the period for which the
21 taxpayer has held trust certificates of a trust to which
22 subsection (d) of section 1246 applies, or the period
23 for which the taxpayer has held stock in a corporation
24 to which subsection (d) of section 1246 applies, there

1 shall be included the period for which the trust or cor-
 2 poration (as the case may be) held the stock of foreign
 3 investment companies.”

4 (c) EFFECTIVE DATE.—The amendments made by
 5 this section shall apply with respect to taxable years begin-
 6 ning after December 31, 1962.

7 **SEC. (157)¹⁶ 15. GAIN FROM CERTAIN SALES OR EX-**
 8 **CHANGES OF STOCK IN CERTAIN FOR-**
 9 **EIGN CORPORATIONS.**

10 (a) TREATMENT OF GAIN FROM THE REDEMPTION,
 11 CANCELLATION, OR SALE OF STOCK IN CERTAIN FOREIGN
 12 CORPORATIONS.—Part IV of subchapter P of chapter 1
 13 (relating to special rules for determining capital gains and
 14 losses) is amended by adding after section 1247 (as added
 15 by section (158)¹⁵ 14 of this Act) the following new
 16 section:

17 **(159)¹⁴“SEC. 1248. GAIN FROM CERTAIN SALES OR EX-**
 18 **CHANGES OF STOCK IN CERTAIN FOR-**
 19 **EIGN CORPORATIONS.**

20 ~~“(a) REDEMPTIONS AND LIQUIDATIONS.—~~If a foreign
 21 corporation redeems its stock in an exchange to which sec-
 22 tion 302(a) applies, or if a foreign corporation cancels its
 23 stock in a complete or partial liquidation in an exchange to
 24 which section 331 applies, then the gain of a United States
 25 person (as defined in section 7701(a)(30)) from the ex-

1 change of such stock shall be included in the gross income
 2 of such person as a dividend, to the extent of such person's
 3 proportionate share of the earnings and profits of the foreign
 4 corporation accumulated after February 28, 1913.

5 “~~(b)~~ SALES AND OTHER EXCHANGES.—If a United
 6 States person ~~(as defined in section 7701(a)(30))~~ sells or
 7 exchanges stock in a foreign corporation, then the gain
 8 recognized on the sale or exchange of such stock shall be
 9 considered as gain from the sale or exchange of property
 10 which is not a capital asset, to the extent of such person's
 11 proportionate share of the earnings and profits of the foreign
 12 corporation accumulated during the period the stock sold or
 13 exchanged was held by such person.

14 “~~(c)~~ LIMITATIONS.—

15 “~~(1)~~ CONTROLLED FOREIGN CORPORATIONS.—
 16 Subsections ~~(a)~~ and ~~(b)~~ shall apply only if the foreign
 17 corporation the stock of which is sold or exchanged ~~(A)~~
 18 is a controlled foreign corporation ~~(as defined in section~~
 19 ~~954)~~ at the time of the sale or exchange, or ~~(B)~~ was
 20 such a controlled foreign corporation at any time during
 21 the 5-year period ending on the date of the sale or
 22 exchange.

23 “~~(2)~~ 10 PERCENT OWNERSHIP.—Subsections ~~(a)~~
 24 and ~~(b)~~ shall apply only to a United States person who
 25 can be considered, by applying the rules of constructive

1 ownership of section 955(b), as being the owner,
2 directly or indirectly, of 10 percent or more of the total
3 combined voting power of all classes of stock entitled
4 to vote of the foreign corporation at the time of the sale
5 or exchange, or at any time during the 5-year period
6 ending on the date of the sale or exchange.

7 “(3) ELIMINATION FROM EARNING AND PROFITS
8 OF AMOUNTS INCLUDED IN GROSS INCOME UNDER
9 SECTION 951.—In determining the amount to be con-
10 sidered a dividend under subsection (a), or as gain from
11 the sale or exchange of property which is not a capital
12 asset under subsection (b), the United States person's
13 proportionate share of earnings and profits of the foreign
14 corporation shall be reduced by the amount previously
15 included in the gross income of such person under section
16 951, with respect to the stock sold or exchanged, but
17 only to the extent such amount did not result in an
18 exclusion from gross income under section 956.

19 “(4) REDEMPTIONS TO PAY DEATH TAXES.—Sub-
20 sections (a) and (b) shall not apply to distributions to
21 which section 303 (relating to distributions in redemp-
22 tion of stock to pay death taxes) applies.

23 “(5) ADDITIONAL CONSIDERATION IN CERTAIN
24 REORGANIZATIONS.—Subsection (b) shall not apply to
25 gain recognized on exchanges to which section 356 (re-

1 relating to receipt of additional consideration in certain
2 reorganizations) applies.

3 “(6) TREATMENT OF AMOUNTS WHICH ARE ORDI-
4 NARY INCOME, ETC., UNDER OTHER PROVISIONS.—Sub-
5 sections (a) and (b) shall not apply with respect to any
6 amount to the extent that such amount is, under any
7 other provision of this title, treated as—

8 “(A) a dividend,

9 “(B) gain from the sale of an asset which is
10 not a capital asset, or

11 “(C) gain from the sale of an asset held for not
12 more than 6 months.

13 “(d) TAXPAYER TO ESTABLISH EARNINGS AND
14 PROFITS.—Unless the taxpayer establishes the amount of
15 the earnings and profits of the foreign corporation to be taken
16 into account under subsections (a) and (b), all gain from
17 the sale or exchange shall be considered a dividend under
18 subsection (a), or as gain from the sale or exchange of
19 property which is not a capital asset under subsection (b),
20 whichever applies.”

21 “SEC. 1248. GAIN FROM CERTAIN SALES OR EXCHANGES OF
22 STOCK IN CERTAIN FOREIGN CORPORATIONS.

23 “(a) GENERAL RULE.—If—

24 “(1) a United States person sells or exchanges
25 stock in a foreign corporation, or if a United States per-

1 son receives a distribution from a foreign corporation
2 which, under section 302 or 331, is treated as an ex-
3 change of stock, and

4 “(2) such person owns, within the meaning of sec-
5 tion 958(a), or is considered as owning by applying
6 the rules of ownership of section 958(b), 10 percent or
7 more of the total combined voting power of all classes of
8 stock entitled to vote of such foreign corporation at any
9 time during the 5-year period ending on the date of the
10 sale or exchange when such foreign corporation was a con-
11 trolled foreign corporation (as defined in section 957),
12 then the gain recognized on the sale or exchange of such
13 stock shall be included in the gross income of such person as
14 a dividend, to the extent of the earnings and profits of the
15 foreign corporation attributable (under regulations prescribed
16 by the Secretary or his delegate) to such stock which were
17 accumulated in taxable years of such foreign corporation
18 beginning after December 31, 1962, and during the period
19 or periods the stock sold or exchanged was held by such person
20 while such foreign corporation was a controlled foreign
21 corporation.

22 “(b) *LIMITATION ON TAX APPLICABLE TO INDIVID-*
23 *UALS.—*

24 “(1) *IN GENERAL.—*In the case of an individual,
25 the tax attributable to an amount included in gross in-

come as a dividend under subsection (a) shall not be greater than the tax described in paragraph (2) or in paragraph (3), whichever is lesser.

“(2) DOMESTIC CORPORATION LIMITATION.—

If the stock sold or exchanged is a capital asset (within the meaning of section 1221) and has been held for more than 6 months, a tax equal to the sum of—

“(A) a pro rata share of the excess of—

“(i) the taxes that would have been paid by the foreign corporation with respect to its income had it been taxed under this chapter as a domestic corporation (but without allowance for deduction of, or credit for, taxes described in clause (ii)), for the period or periods the stock sold or exchanged was held by the United States person in taxable years beginning after December 31, 1962, while the foreign corporation was a controlled foreign corporation, adjusted for distributions and amounts previously included in gross income of a United States shareholder under section 951, over

“(ii) the income, war profits, or excess profits taxes paid by the foreign corporation with respect to such income; and

“(B) an amount equal to a tax that would re-

1 *sult by including in gross income the amount de-*
 2 *scribed in subsection (a), reduced by the excess of*
 3 *the taxes described in subparagraph (A)(i) over the*
 4 *taxes described in subparagraph (A)(ii), as gain*
 5 *from the sale or exchange of a capital asset held for*
 6 *more than 6 months.*

7 “(3) *ANNUAL DISTRIBUTION LIMITATION.*—*A tax*
 8 *equal to the aggregate of the taxes which would have*
 9 *been attributable to the amount described in subsection*
 10 *(a) had it been included in the gross income of the*
 11 *individual as a dividend in the year or years in which*
 12 *earned by the foreign corporation, adjusted for losses and*
 13 *distributions as provided by regulations prescribed by*
 14 *the Secretary or his delegate.*

15 “(c) *DETERMINATION OF EARNINGS AND PROFITS.*—

16 “(1) *IN GENERAL.*—*For purposes of this section,*
 17 *the earnings and profits of any foreign corporation for*
 18 *any taxable year shall be determined according to rules*
 19 *substantially similar to those applicable to domestic*
 20 *corporations, under regulations prescribed by the Secre-*
 21 *tary or his delegate.*

22 “(2) *EARNINGS AND PROFITS OF SUBSIDIARIES*
 23 *OF FOREIGN CORPORATIONS.*—*If—*

24 “(A) *subsection (a) applies to a sale or ex-*
 25 *change by a United States person of stock of a for-*

1 *eign corporation and, by reason of the ownership of*
2 *the stock sold or exchanged, such person owned*
3 *within the meaning of section 958(a)(2) stock of*
4 *any other foreign corporation; and*

5 *“(B) such person owned, within the meaning*
6 *of section 958(a), or was considered as owning by*
7 *applying the rules of ownership of section 958(b),*
8 *10 percent or more of the total combined voting*
9 *power of all classes of stock entitled to vote of such*
10 *other foreign corporation at any time during the*
11 *5-year period ending on the date of the sale or*
12 *exchange when such other foreign corporation was*
13 *a controlled foreign corporation (as defined in section*
14 *957),*

15 *then, for purposes of this section, the earnings and profits*
16 *of the foreign corporation the stock of which is sold or*
17 *exchanged which are attributable to the stock sold or*
18 *exchanged shall be deemed to include the earnings and*
19 *profits of such other foreign corporation which—*

20 *“(C) are attributable (under regulations pre-*
21 *scribed by the Secretary or his delegate) to the stock*
22 *of such other foreign corporation which such person*
23 *owned within the meaning of section 958(a)(2)*
24 *(by reason of his ownership within the meaning of*
25 *section 958(a)(1)(A) of the stock sold or ex-*

1 *changed) on the date of such sale or exchange; and*
2 *“(D) were accumulated in taxable years of such*
3 *other corporation beginning after December 31, 1962,*
4 *and during the period or periods—*

5 *“(i) such other corporation was a con-*
6 *trolled foreign corporation, and*

7 *“(ii) such person owned within the mean-*
8 *ing of section 958(a)(2) the stock of such*
9 *other foreign corporation.*

10 *“(d) EXCLUSIONS FROM EARNINGS AND PROFITS.—*
11 *For purposes of this section, the following amounts shall be*
12 *excluded, with respect to any United States person, from*
13 *the earnings and profits of a foreign corporation:*

14 *“(1) AMOUNTS INCLUDED IN GROSS INCOME*
15 *UNDER SECTION 951.—Earnings and profits of the for-*
16 *foreign corporation attributable to any amount previously*
17 *included in the gross income of such person under section*
18 *951, with respect to the stock sold or exchanged, but only*
19 *to the extent the inclusion of such amount did not result*
20 *in an exclusion of an amount from gross income under*
21 *section 959.*

22 *“(2) GAIN REALIZED FROM THE SALE OR EX-*
23 *CHANGE OF PROPERTY IN PURSUANCE OF A PLAN OF*
24 *COMPLETE LIQUIDATION.—If a foreign corporation*
25 *adopts a plan of complete liquidation in a taxable year*

1 of a foreign corporation beginning after December 31,
2 1962, and if section 337(a) would apply if such foreign
3 corporation were a domestic corporation, earnings and
4 profits of the foreign corporation attributable (under
5 regulations prescribed by the Secretary or his delegate)
6 to any net gain from the sale or exchange of property.

7 “(3) LESS DEVELOPED COUNTRY CORPORA-
8 TIONS.—Earnings and profits accumulated by a foreign
9 corporation while it was a less developed country cor-
10 poration (as defined in section 902(d)), if the stock
11 sold or exchanged was owned for a continuous period of
12 at least 10 years, ending with the date of the sale or
13 exchange, by the United States person who sold or
14 exchanged such stock. In the case of stock sold or
15 exchanged by a corporation, if United States persons
16 who are individuals, estates, or trusts (each of whom
17 owned within the meaning of section 958(a), or were
18 considered as owning by applying the rules of owner-
19 ship of section 958(b), 10 percent or more of the total
20 combined voting power of all classes of stock entitled
21 to vote of such corporation) owned, or were considered
22 as owning, at any time during the 10-year period
23 referred to in subparagraph (B) more than 50 percent
24 of the total combined voting power of all classes of stock

1 *entitled to vote of such corporation, this paragraph shall*
2 *apply only if such United States persons owned, or were*
3 *considered as owning, at all times during the remainder*
4 *of such 10-year period more than 50 percent of the total*
5 *combined voting power of all classes of stock entitled to*
6 *vote of such corporation. For purposes of this para-*
7 *graph, stock owned by a United States person who is an*
8 *individual, estate, or trust which was acquired by reason*
9 *of the death of the predecessor in interest of such United*
10 *States person shall be considered as owned by such United*
11 *States person during the period such stock was owned by*
12 *such predecessor in interest, and during the period such*
13 *stock was owned by any other predecessor in interest if*
14 *between such United States person and such other prede-*
15 *cessor in interest there was no transfer other than by*
16 *reason of the death of an individual.*

17 “(4) *UNITED STATES INCOME.*—Any item includ-
18 *ible in gross income of the foreign corporation under this*
19 *chapter as income derived from sources within the United*
20 *States of a foreign corporation engaged in trade or busi-*
21 *ness in the United States.*

22 “(5) *AMOUNTS INCLUDED IN GROSS INCOME UN-*
23 *DER SECTION 1247.*—If the United States person whose
24 *stock is sold or exchanged was a qualified shareholder*
25 *(as defined in section 1247(c)) of a foreign corporation*

which was a foreign investment company (as described in section 1246(b)(1)), the earnings and profits of the foreign corporation for taxable years in which such person was a qualified shareholder.

“(e) SALES OR EXCHANGES OF STOCK IN CERTAIN DOMESTIC CORPORATIONS.—Under regulations prescribed by the Secretary or his delegate, if—

“(1) a United States person sells or exchanges stock of a domestic corporation, or receives a distribution from a domestic corporation which, under section 302 or 331, is treated as an exchange of stock, and

“(2) such domestic corporation was formed or availed of principally for the holding, directly or indirectly, of stock of one or more foreign corporations, such sale or exchange shall, for purposes of this section, be treated as a sale or exchange of the stock of the foreign corporation or corporations held by the domestic corporation.

“(f) EXCEPTIONS.—This section shall not apply to—

“(1) distributions to which section 303 (relating to distributions in redemption of stock to pay death taxes) applies;

“(2) gain realized on exchanges to which section 356 (relating to receipt of additional consideration in certain reorganizations) applies; or

1 “(3) any amount to the extent that such amount
2 is, under any other provision of this title, treated as—

3 “(A) a dividend,

4 “(B) gain from the sale of an asset which is
5 not a capital asset, or

6 “(C) gain from the sale of an asset held for
7 not more than 6 months.

8 “(g) *TAXPAYER TO ESTABLISH EARNINGS AND*
9 *PROFITS.*—Unless the taxpayer establishes the amount of the
10 earnings and profits of the foreign corporation to be taken
11 into account under subsection (a), all gain from the sale
12 or exchange shall be considered a dividend under subsection
13 (a), and unless the taxpayer establishes the amount of for-
14 eign taxes to be taken into account under subsection (b)
15 (2), the limitation of such subsection shall not apply.”

16 (b) *CLERICAL AMENDMENT.*—The table of sections for
17 such part IV is amended by adding at the end thereof the
18 following:

 “Sec. 1248. Gain from certain sales or exchanges of stock
 in certain foreign corporations.”

19 (c) *EFFECTIVE DATE.*—The amendments made by this
20 section shall apply with respect to sales or exchanges oc-
21 curring after (160)the date of the enactment of this Act
22 December 31, 1962.

1 **(161) SEC. 16. SALES AND EXCHANGES OF PATENTS, ETC., TO**
 2 **CERTAIN FOREIGN CORPORATIONS.**

3 *(a) TREATMENT OF GAIN AS ORDINARY INCOME.—*

4 *Part IV of subchapter P of chapter 1 (relating to special*
 5 *rules for determining capital gains and losses) is amended*
 6 *by adding after section 1248 (as added by section 15 of this*
 7 *Act) the following new section:*

8 **“SEC. 1249. GAIN FROM CERTAIN SALES OR EXCHANGES OF**
 9 **PATENTS, ETC., TO FOREIGN CORPORATIONS.**

10 *“(a) GENERAL RULE.—Except as provided in subsec-*
 11 *tion (c), gain from the sale or exchange after December 31,*
 12 *1962, of a patent, an invention, model, or design (whether*
 13 *or not patented), a copyright, a secret formula or process,*
 14 *or any other similar property right to any foreign corporation*
 15 *by any United States person (as defined in section 7701(a)*
 16 *(30)) which controls such foreign corporation shall, if such*
 17 *gain would (but for the provisions of this subsection) be*
 18 *gain from the sale or exchange of a capital asset or of prop-*
 19 *erty described in section 1231, be considered as gain from*
 20 *the sale or exchange of property which is neither a capital*
 21 *asset nor property described in section 1231.*

22 *“(b) CONTROL.—For purposes of subsection (a), con-*
 23 *trol means, with respect to any foreign corporation, the*
 24 *ownership, directly or indirectly, of stock possessing more*
 25 *than 50 percent of the total combined voting power of all*

1 *classes of stock entitled to vote. For purposes of this sub-*
 2 *section, the rules for determining ownership of stock pre-*
 3 *scribed by section 958 shall apply.*

4 “(c) *EXCEPTION.*—*This section shall not apply to gain*
 5 *realized from the sale or exchange for stock or contribution*
 6 *to capital of property described in subsection (a) where it*
 7 *is established to the satisfaction of the Secretary or his dele-*
 8 *gate that the principal purpose of the transfer is to enable*
 9 *the foreign corporation to use such property in its own manu-*
 10 *facturing operations.”*

11 “(b) *CLERICAL AMENDMENT.*—*The table of sections for*
 12 *such part IV is amended by adding at the end thereof the*
 13 *following:*

*“Sec. 1249. Gain from certain sales or exchanges of patents,
 etc., to foreign corporations.”*

14 “(c) *EFFECTIVE DATE.*—*The amendments made by this*
 15 *section shall apply to taxable years beginning after December*
 16 *31, 1962.*

17 **SEC. 17. TAX TREATMENT OF COOPERATIVES AND PA-**
 18 **TRONS.**

19 “(a) *IN GENERAL.*—*Chapter 1 (relating to normal*
 20 *taxes and surtaxes) is amended by adding at the end thereof*
 21 *the following new subchapter:*

1 “Subchapter T—Cooperatives and Their Patrons

“Part I. Tax treatment of cooperatives.

“Part II. Tax treatment by patrons of patronage dividends.

“Part III. Definitions; special rules.

2 “PART I—TAX TREATMENT OF COOPERATIVES

“Sec. 1381. Organizations to which part applies.

“Sec. 1382. Taxable income of cooperatives.

“Sec. 1383. Computation of tax where cooperative redeems nonqualified written notices of allocation.

3 “SEC. 1381. ORGANIZATIONS TO WHICH PART APPLIES.

4 “(a) IN GENERAL.—This part shall apply to—

5 “(1) any organization exempt from tax under sec-
6 tion 521 (relating to exemption of farmers’ cooperatives
7 from tax), and

8 “(2) any corporation operating on a cooperative
9 basis other than an organization—

10 “(A) which is exempt from tax under this
11 chapter,

12 “(B) which is subject to the provisions of—

13 “(i) part II of subchapter H (relating
14 to mutual savings banks, etc.), or

15 “(ii) subchapter L (relating to insurance
16 companies), or

17 “(C) which is engaged in furnishing electric

1 energy, or providing telephone service, to persons
2 in rural areas.

3 “(b) TAX ON CERTAIN FARMERS’ COOPERATIVES.—

4 An organization described in subsection (a) (1) shall be
5 subject to the taxes imposed by section 11 or 1201.

6 **“SEC. 1382. TAXABLE INCOME OF COOPERATIVES.**

7 “(a) GROSS INCOME.—Except as provided in subsec-
8 tion (b), the gross income of any organization to which this
9 part applies shall be determined without any adjustment
10 (as a reduction in gross receipts, an increase in cost of goods
11 sold, or otherwise) by reason of any allocation or distribution
12 to a patron out of the net earnings of such organization.

13 “(b) PATRONAGE DIVIDENDS.—In determining the
14 taxable income of an organization to which this part applies,
15 there shall not be taken into account amounts paid during
16 the payment period for the taxable year—

17 “(1) as patronage dividends (as defined in section
18 1388 (a)), to the extent paid in money, qualified writ-
19 ten notices of allocation (as defined in section 1388
20 (c)), or other property (except nonqualified written
21 notices of allocation (as defined in section 1388 (d)))
22 with respect to patronage occurring during such taxable
23 year; or

24 “(2) in money or other property (except written
25 notices of allocation) in redemption of a nonqualified

1 written notice of allocation which was paid as a patron-
2 age dividend during the payment period for the taxable
3 year during which the patronage occurred.

4 For purposes of this title, any amount not taken into ac-
5 count under the preceding sentence shall be treated in the
6 same manner as an item of gross income and as a deduction
7 therefrom.

8 “(c) DEDUCTION FOR NONPATRONAGE DISTRIBUTU-
9 TIONS, ETC.—In determining the taxable income of an or-
10 ganization described in section 1381 (a) (1), there shall be
11 allowed as a deduction (in addition to other deductions al-
12 lowable under this chapter) —

13 “(1) amounts paid during the taxable year as divi-
14 dends on its capital stock; and

15 “(2) amounts paid during the payment period for
16 the taxable year—

17 “(A) in money, qualified written notices of
18 allocation, or other property (except nonqualified
19 written notices of allocation) on a patronage basis
20 to patrons with respect to its earnings during such
21 taxable year which are derived from business done
22 for the United States or any of its agencies or from
23 sources other than patronage, or

24 “(B) in money or other property (except writ-
25 ten notices of allocation) in redemption of a non-

1 qualified written notice of allocation which was paid,
 2 during the payment period for the taxable year dur-
 3 ing which the earnings were derived, on a patron-
 4 age basis to a patron with respect to earnings de-
 5 rived from business or sources described in subpara-
 6 graph (A).

7 “(d) PAYMENT PERIOD FOR EACH TAXABLE YEAR.—
 8 For purposes of subsections (b) and (c) (2), the payment
 9 period for any taxable year is the period beginning with the
 10 first day of such taxable year and ending with the fifteenth
 11 day of the ninth month following the close of such year.
 12 (162) *For purposes of subsections (b) (1) and (c) (2) (A),*
 13 *a qualified check issued during the payment period shall be*
 14 *treated as an amount paid in money during such period if*
 15 *endorsed and cashed on or before the 90th day after the*
 16 *close of such period.*

17 “(e) PRODUCTS MARKETING UNDER POOLING AR-
 18 RANGEMENTS.—For purposes of subsection (b), in the case
 19 of a pooling arrangement for the marketing of products, the
 20 patronage shall (to the extent provided in regulations pre-
 21 scribed by the Secretary or his delegate) be treated as
 22 patronage occurring during the taxable year in which the
 23 pool closes.

24 “(f) TREATMENT OF EARNINGS RECEIVED AFTER
 25 PATRONAGE OCCURRED.—If any portion of the earnings

1 from business done with or for patrons is includible in the
 2 organization's gross income for a taxable year after the
 3 taxable year during which the patronage occurred, then for
 4 purposes of applying subsection (b) to such portion the
 5 patronage shall, to the extent provided in regulations pre-
 6 scribed by the Secretary or his delegate, be considered to
 7 have occurred during the taxable year of the organization
 8 during which such earnings are includible in gross income.

9 **"SEC. 1383. COMPUTATION OF TAX WHERE COOPERATIVE**
 10 **REDEEMS NONQUALIFIED WRITTEN NO-**
 11 **TICES OF ALLOCATION.**

12 "(a) GENERAL RULE.—If, under section 1382 (b) (2)
 13 or (c) (2) (B), a deduction is allowable to an organization
 14 for the taxable year for amounts paid in redemption of non-
 15 qualified written notices of allocation, then the tax imposed
 16 by this chapter on such organization for the taxable year
 17 shall be the lesser of the following:

18 "(1) the tax for the taxable year computed with
 19 such deduction; or

20 "(2) an amount equal to—

21 "(A) the tax for the taxable year computed
 22 without such deduction, minus

23 "(B) the decrease in tax under this chapter
 24 for any prior taxable year (or years) which would
 25 result solely from treating such nonqualified written

1 notices of allocation as qualified written notices of
2 allocation.

3 “(b) SPECIAL RULES.—

4 “(1) If the decrease in tax ascertained under sub-
5 section (a) (2) (B) exceeds the tax for the taxable year
6 (computed without the deduction described in subsection
7 (a)) such excess shall be considered to be a payment
8 of tax on the last day prescribed by law for the payment
9 of tax for the taxable year, and shall be refunded or
10 credited in the same manner as if it were an overpay-
11 ment for such taxable year.

12 “(2) For purposes of determining the decrease in
13 tax under subsection (a) (2) (B), the stated dollar
14 amount of any nonqualified written notice of allocation
15 which is to be treated under such subsection as a quali-
16 fied written notice of allocation shall be the amount paid
17 in redemption of such written notice of allocation which
18 is allowable as a deduction under section 1382 (b) (2)
19 or (c) (2) (B) for the taxable year.

20 “(3) If the tax imposed by this chapter for the tax-
21 able year is the amount determined under subsection
22 (a) (2), then the deduction described in subsection (a)
23 shall not be taken into account for any purpose of this
24 subtitle other than for purposes of this section.

1 **“PART II—TAX TREATMENT BY PATRONS OF**
2 **PATRONAGE DIVIDENDS**

“Sec. 1385. Amounts includible in patron’s gross income.

3 **“SEC. 1385. AMOUNTS INCLUDIBLE IN PATRON’S GROSS**
4 **INCOME.**

5 “(a) **GENERAL RULE.**—Except as otherwise provided
6 in subsection (b), each person shall include in gross
7 income—

8 “(1) the amount of any patronage dividend which
9 is paid in money, a qualified written notice of allocation,
10 or other property (except a nonqualified written notice
11 of allocation), and which is received by him during the
12 taxable year from an organization described in section
13 1381 (a), and

14 “(2) any amount, described in section 1382 (c) (2)
15 (A) (relating to certain nonpatronage distributions by
16 tax-exempt farmers’ cooperatives), which is paid in
17 money, a qualified written notice of allocation, or other
18 property (except a nonqualified written notice of alloca-
19 tion), and which is received by him during the taxable
20 year from an organization described in section 1381 (a)
21 (1).

22 “(b) **EXCLUSION FROM GROSS INCOME.**—Under regu-
23 lations prescribed by the Secretary or his delegate, the

1 amount of any patronage dividend, and any amount re-
2 ceived on the redemption, sale, or other disposition of a non-
3 qualified written notice of allocation which was paid as a
4 patronage dividend, shall not be included in gross income to
5 the extent that such amount—

6 “(1) is properly taken into account as an adjust-
7 ment to basis of property, or

8 “(2) is attributable to personal, living, or family
9 items.

10 “(c) TREATMENT OF CERTAIN NONQUALIFIED WRIT-
11 TEN NOTICES OF ALLOCATION.—

12 “(1) APPLICATION OF SUBSECTION.—This sub-
13 section shall apply to any nonqualified written notice of
14 allocation which—

15 “(A) was paid as a patronage dividend, or

16 “(B) was paid by an organization described in
17 section 1381 (a) (1) on a patronage basis with re-
18 spect to earnings derived from business or sources
19 described in section 1382 (c) (2) (A).

20 “(2) BASIS; AMOUNT OF GAIN.—In the case of
21 any nonqualified written notice of allocation to which
22 this subsection applies, for purposes of this chapter—

23 “(A) the basis of such written notice of alloca-
24 tion in the hands of the patron to whom such written
25 notice of allocation was paid shall be zero,

“(B) the basis of such written notice of allocation which was acquired from a decedent shall be its basis in the hands of the decedent, and

“(C) gain on the redemption, sale, or other disposition of such written notice of allocation by any person shall, to the extent that the stated dollar amount of such written notice of allocation exceeds its basis, be considered as gain from the sale or exchange of property which is not a capital asset.

“PART III—DEFINITIONS; SPECIAL RULES

“Sec. 1388. Definitions; special rules.

“SEC. 1388. DEFINITIONS; SPECIAL RULES.

“(a) PATRONAGE DIVIDEND.—For purposes of this subchapter, the term ‘patronage dividend’ means an amount paid to a patron by an organization to which part I of this subchapter applies—

“(1) on the basis of quantity or value of business done with or for such patron,

“(2) under an obligation of such organization to pay such amount, which obligation existed before the organization received the amount so paid, and

“(3) which is determined by reference to the net earnings of the organization from business done with or for its patrons.

1 Such term does not include any amount paid to a patron to
 2 the extent that (A) such amount is out of earnings other
 3 than from business done with or for patrons, or (B)
 4 such amount is out of earnings from business done with or
 5 for other patrons to whom no amounts are paid, or to whom
 6 smaller amounts are paid, with respect to substantially
 7 identical transactions.

8 “(b) WRITTEN NOTICE OF ALLOCATION.—For pur-
 9 poses of this subchapter, the term ‘written notice of alloca-
 10 tion’ means any capital stock, revolving fund certificate,
 11 retain certificate, certificate of indebtedness, letter of advice,
 12 or other written notice, which discloses to the recipient the
 13 stated dollar amount allocated to him by the organization
 14 and the portion thereof, if any, which constitutes a patronage
 15 dividend.

16 “(c) QUALIFIED WRITTEN NOTICE OF ALLOCATION.—

17 “(1) DEFINED.—For purposes of this subchapter,
 18 the term ‘qualified written notice of allocation’ means—

19 “(A) a written notice of allocation which may
 20 be redeemed in cash at its stated dollar amount at
 21 any time within a period beginning on the date such
 22 written notice of allocation is paid and ending not
 23 earlier than 90 days from such date, but only if the
 24 distributee receives written notice of the right of

redemption at the time he receives such written notice of allocation; and

“(B) a written notice of allocation which the distributee has consented, in the manner provided in paragraph (2), to take into account at its stated dollar amount as provided in section 1385 (a).

(163) *Such term does not include any written notice of allocation which is paid as part of a patronage dividend or as part of a payment described in section 1382(c)(2)(A), unless 20 percent or more of the amount of such patronage dividend, or such payment, is paid in money or by qualified check.*

“(2) MANNER OF OBTAINING CONSENT.—A distributee shall consent to take a written notice of allocation into account as provided in paragraph (1) (B) only by—

“(A) making such consent in writing, **(164)**~~or~~

“(B) obtaining or retaining membership in the organization after—

“(i) such organization has adopted (after the date of the enactment of the Revenue Act of 1962) a bylaw providing that membership in the organization constitutes such consent, and

1 “(ii) he has received a written notifica-
 2 tion and copy of such ~~(165) bylaw~~ *bylaw*, or
 3 **(166)**“(C) if neither subparagraph (A) nor (B)
 4 *applies, endorsing and cashing a qualified check,*
 5 *paid as a part of the patronage dividend or pay-*
 6 *ment of which such written notice of allocation is*
 7 *also a part, on or before the 90th day after the close*
 8 *of the payment period for the taxable year of the*
 9 *organization for which such patronage dividend or*
 10 *payment is paid.*

11 “(3) PERIOD FOR WHICH CONSENT IS EFFEC-
 12 TIVE.—

13 “(A) GENERAL RULE.—Except as provided in
 14 subparagraph (B) —

15 “(i) a consent described in paragraph
 16 (2) (A) shall be a consent with respect to all
 17 patronage of the distributee with the organiza-
 18 tion occurring (determined with the application
 19 of section 1382 (e)) during the taxable year of
 20 the organization during which such consent is
 21 made and all subsequent taxable years of the
 22 organization; and

23 “(ii) a consent described in paragraph
 24 (2) (B) shall be a consent with respect to all
 25 patronage of the distributee with the organiza-

tion occurring (determined without the application of section 1382 (e)) after he received the notification and copy described in paragraph (2) (B) (ii) .

“(B) REVOCATION, ETC.—

“(i) Any consent described in paragraph (2) (A) may be revoked (in writing) by the distributee at any time. Any such revocation shall be effective with respect to patronage occurring on or after the first day of the first taxable year of the organization beginning after the revocation is filed with such organization; except that in the case of a pooling arrangement described in section 1382 (e) , a revocation made by a distributee shall not be effective as to any pool with respect to which the distributee has been a patron before such revocation.

“(ii) Any consent described in paragraph (2) (B) shall not be effective with respect to any patronage occurring (determined without the application of section 1382 (e)) after the distributee ceases to be a member of the organization or after the bylaws of the organization cease to contain the provision described in paragraph (2) (B) (i) .

1 **(167)**“(4) *QUALIFIED CHECK*.—For purposes of this
2 subchapter, the term ‘qualified check’ means only a check
3 (or other instrument which is redeemable in money)
4 which is paid as a part of a patronage dividend, or as a
5 part of a payment described in section 1382(c)(2)(A),
6 to a distributee who has not given consent as provided
7 in paragraph (2) (A) or (B) with respect to such
8 patronage dividend or payment, and on which there is
9 clearly imprinted a statement that the endorsement and
10 cashing of the check (or other instrument) constitutes the
11 consent of the payee to include in his gross income, as
12 provided in the Federal income tax laws, the stated dollar
13 amount of the written notice of allocation which is a part
14 of the patronage dividend or payment of which such
15 qualified check is also a part. Such term does not
16 include any check (or other instrument) which is paid
17 as part of a patronage dividend or payment which does
18 not include a written notice of allocation (other than
19 a written notice of allocation described in paragraph
20 (1)(A)).

21 “(d) *NONQUALIFIED WRITTEN NOTICE OF ALLOCA-*
22 *TION*.—For purposes of this subchapter, the term ‘nonquali-
23 fied written notice of allocation’ means a written notice of
24 allocation which is not described in subsection (c) **(168)**or
25 a qualified check which is not cashed on or before the 90th day

1 *after the close of the payment period for the taxable year for*
 2 *which the distribution of which it is a part is paid.*

3 “(e) DETERMINATION OF AMOUNT PAID OR RE-
 4 CEIVED.—For purposes of this subchapter, in determining
 5 amounts paid or received—

6 “(1) property (other than a written notice of allo-
 7 cation) shall be taken into account at its fair market
 8 value, and

9 “(2) a qualified written notice of allocation shall
 10 be taken into account at its stated dollar amount.”

11 (b) TECHNICAL AMENDMENTS.—

12 (1) Section 521 (a) (relating to exemption of farm-
 13 ers’ cooperatives from tax) is amended by striking out
 14 “section 522” each place it appears therein and inserting
 15 in lieu thereof “part I of subchapter T (sec. 1381 and
 16 following) ”.

17 (2) Section 522 (relating to tax on farmers’ coop-
 18 eratives) is hereby repealed.

19 ~~(169)(3)~~ Section 6044 ~~(relating to returns regarding~~
 20 ~~patronage dividends)~~ is amended to read as follows:

21 **“SEC. 6044. RETURNS REGARDING PATRONAGE DIVI-**
 22 **DENDS.**

23 “Any organization to which part I of subchapter T of
 24 chapter 1 ~~(relating to tax treatment of cooperatives)~~ ap-
 25 plies which pays amounts described in section 1382(b), or

1 ~~(in the case of an organization described in section 1381~~
 2 ~~(a)-(1))~~ amounts described in section 1382(c)(2), shall,
 3 when required by regulations of the Secretary or his delegate,
 4 make a return showing—

5 “~~(1)~~ the name and address of each patron to whom
 6 it has made such payments during the calendar year; and

7 “~~(2)~~ the amount of such payments to each patron.”

8 ~~(170)(4)~~ (3) Section 6072 (d) (relating to time for
 9 filing income tax returns of exempt cooperative associa-
 10 tions) is amended to read as follows:

11 “(d) RETURNS OF COOPERATIVE ASSOCIATIONS.—In
 12 the case of an income tax return of—

13 “(1) an exempt cooperative association described
 14 in section 1381 (a) (1), or

15 “(2) an organization described in section 1381
 16 (a) (2) which is under an obligation to pay patronage
 17 dividends (as defined in section 1388 (a)) in an
 18 amount equal to at least 50 percent of its net earnings
 19 from business done with or for its patrons, or which
 20 paid patronage dividends in such an amount out of the
 21 net earnings from business done with or for patrons dur-
 22 ing the most recent taxable year for which it had such
 23 net earnings,

24 a return made on the basis of a calendar year shall be filed
 25 on or before the 15th day of September following the close

1 of the calendar year, and a return made on the basis of a
2 fiscal year shall be filed on or before the 15th day of the 9th
3 month following the close of the fiscal year.”

4 ~~(171)(5)~~ (4) The table of subchapters for chapter 1 is
5 amended by adding at the end thereof the following:

“SUBCHAPTER T. Cooperatives and their patrons.”

6 ~~(172)(6)~~ (5) The table of sections for part III of sub-
7 chapter F of chapter 1 is amended by striking out the
8 last line thereof.

9 (c) EFFECTIVE DATES.—

10 (1) FOR THE COOPERATIVES.—Except as provided
11 in paragraph (3), the amendments made by subsections
12 (a) and (b) shall apply to taxable years of organiza-
13 tions described in section 1381 (a) of the Internal Reve-
14 nue Code of 1954 (as added by subsection (a)) begin-
15 ning after December 31, 1962.

16 (2) FOR THE PATRONS.—Except as provided in
17 paragraph (3), section 1385 of the Internal Revenue
18 Code of 1954 (as added by subsection (a)) shall
19 apply with respect to any amount received from any
20 organization described in section 1381 (a) of such Code,
21 to the extent that such amount is paid by such organiza-
22 tion in a taxable year of such organization beginning
23 after December 31, 1962.

1 (3) APPLICATION OF EXISTING LAW.—In the case
2 of any money, written notice of allocation, or other prop-
3 erty paid by any organization described in section
4 1381 (a) —

5 (A) before the first day of the first taxable
6 year of such organization beginning after December
7 31, 1962, or

8 (B) on or after such first day with respect to
9 patronage occurring before such first day,
10 the tax treatment of such money, written notice of allo-
11 cation, or other property (including the tax treatment of
12 gain or loss on the redemption, sale, or other disposition
13 of such written notice of allocation) by any person shall
14 be made under the Internal Revenue Code of 1954 with-
15 out regard to subchapter T of chapter 1 of such Code.

16 **SEC. 18. INCLUSION OF FOREIGN REAL PROPERTY IN**
17 **GROSS ESTATE.**

18 (a) AMENDMENTS TO INCLUDE FOREIGN REAL PROP-
19 erty.—

20 (1) Section 2031 (a) (relating to definition of gross
21 estate) is amended by striking out “, except real prop-
22 erty situated outside of the United States”.

23 (2) The following provisions of chapter 11 (impos-
24 ing an estate tax) are amended by striking out “(except
25 real property situated outside of the United States)”:

(A) section 2033 (relating to property in which the decedent had an interest),

(B) section 2034 (relating to dower or curtesy interests),

(C) section 2035 (a) (relating to transactions in contemplation of death),

(D) section 2036 (a) (relating to transfers with retained life estate),

(E) section 2037 (a) (relating to transfers taking effect at death),

(F) section 2038 (a) (relating to revocable transfers),

(G) section 2040 (relating to joint interests), and

(H) section 2041 (a) (relating to powers of appointment).

(b) EFFECTIVE DATE.—

(1) Except as provided in paragraph (2), the amendments made by subsection (a) shall apply to the estates of decedents dying after the date of the enactment of this Act.

(2) In the case of a decedent dying after the date of the enactment of this Act and before July 1, 1964, the value of real property situated outside of the United

1 States shall not be included in the gross estate (as de-
2 fined in section 2031 (a)) of the decedent—

3 (A) under section 2033, 2034, 2035 (a),
4 2036 (a), 2037 (a), or 2038 (a) to the extent the
5 real property, or the decedent's interest in it, was
6 acquired by the decedent before February 1, 1962;

7 (B) under section 2040 to the extent such
8 property or interest was acquired by the decedent
9 before February 1, 1962, or was held by the dece-
10 dent and the survivor in a joint tenancy or tenancy
11 by the entirety before February 1, 1962; or

12 (C) under section 2041 (a) to the extent that
13 before February 1, 1962, such property or interest
14 was subject to a general power of appointment (as
15 defined in section 2041) possessed by the decedent.

16 In the case of real property, or an interest therein, sit-
17 uated outside of the United States (including a general
18 power of appointment in respect of such property or
19 interest, and including property held by the decedent
20 and the survivor in a joint tenancy or tenancy by the
21 entirety) which was acquired by the decedent after
22 January 31, 1962, by gift within the meaning of sec-
23 tion 2511, or from a prior decedent by devise or inherit-
24 ance, or by reason of death, form of ownership, or other
25 conditions (including the exercise or nonexercise of a

power of appointment), for purposes of this paragraph such property or interest therein shall be deemed to have been acquired by the decedent before February 1, 1962, if before that date the donor or prior decedent had acquired the property or his interest therein or had possessed a power of appointment in respect of the property or interest.

**(173) SEC. 19. WITHHOLDING OF INCOME TAX AT SOURCE
ON INTEREST, DIVIDENDS, AND PATRON-
AGE DIVIDENDS.**

~~(a) IN GENERAL.—~~

~~(1) AMENDMENT OF SUBTITLE C.—~~Subtitle C (relating to employment taxes and collection of income tax at source) is amended by redesignating chapter 25 as chapter 26 and by inserting after chapter 24 the following new chapter:

**“CHAPTER 25—COLLECTION OF INCOME TAX
AT SOURCE ON INTEREST, DIVIDENDS,
AND PATRONAGE DIVIDENDS**

~~“SUBCHAPTER A. Interest.~~

~~“SUBCHAPTER B. Dividends.~~

~~“SUBCHAPTER C. Patronage dividends.~~

~~“SUBCHAPTER D. General provisions.~~

“Subchapter A—Interest

~~“Sec. 3451. Income tax collected at source on interest.~~

~~“Sec. 3452. Interest defined.~~

1 **“SEC. 3451. INCOME TAX COLLECTED AT SOURCE ON**
 2 **INTEREST.**

3 ~~“(a) REQUIREMENT OF WITHHOLDING.~~—Except as
 4 otherwise provided in this chapter, every person who pays
 5 interest shall deduct and withhold on such interest a tax
 6 equal to 20 percent of the amount thereof.

7 ~~“(b) PAYEE UNKNOWN.~~—If the withholding agent is
 8 unable to determine the person to whom the interest is pay-
 9 able, the tax under this section shall be deducted and with-
 10 held at the time payment of the interest would be made if
 11 such person were known.

12 ~~“(c) CROSS REFERENCES.—~~

 “(1) For credit, against income tax of the recipient
 of the income, of amounts deducted and withheld
 under this section, see section 39.

 “(2) For special rules as to credit or refund of such
 amounts, see sections 3484, 3485, 3486, 3487, and 3505.

 “(3) For exemption from requirement of deducting
 and withholding on certain interest paid to certain
 persons, see section 3483.

13 **“SEC. 3452. INTEREST DEFINED.**

14 ~~“(a) GENERAL RULE.~~—For purposes of this chapter,
 15 the term ‘interest’ means—

16 ~~“(1) interest on evidences of indebtedness (includ-~~
 17 ing bonds, debentures, notes, and certificates) issued by
 18 a corporation with interest coupons or in registered
 19 form, and, to the extent provided in regulations pre-

scribed by the Secretary or his delegate, interest on other evidences of indebtedness issued by a corporation of a type offered by corporations to the public;

“(2) interest on deposits with persons carrying on the banking business;

“(3) amounts (whether or not designated as interest) paid by a mutual savings bank, savings and loan association, building and loan association, cooperative bank, homestead association, credit union, or similar organization, in respect of deposits, investment certificates, or withdrawable or repurchasable shares;

“(4) interest on amounts held by an insurance company under an agreement to pay interest thereon;

“(5) interest on deposits with stockbrokers;

“(6) interest on obligations of the United States;

and

“(7) in the case of a non-interest-bearing obligation of the United States—

“(A) issued on a discount basis, and

“(B) having a maturity date more than one year from the date of issue,

the amount by which the amount paid on surrender or redemption exceeds the issue price.

“(b) EXCEPTIONS.—For purposes of this chapter, the term ‘interest’ does not include—

1 ~~“(1) interest on obligations described in section~~
2 ~~103(a) (1) or (3) (relating to interest on certain~~
3 ~~governmental obligations);~~

4 ~~“(2) any amount paid by—~~

5 ~~“(A) a foreign government or international~~
6 ~~organization;~~

7 ~~“(B) a foreign corporation not engaged in~~
8 ~~trade or business within the United States;~~

9 ~~“(C) a nonresident alien individual not en-~~
10 ~~gaged in trade or business within the United States,~~
11 ~~or~~

12 ~~“(D) a partnership not engaged in trade or~~
13 ~~business within the United States and composed in~~
14 ~~whole or in part of nonresident aliens;~~

15 ~~“(3) interest on deposits with persons carrying on~~
16 ~~the banking business paid to a person described in para-~~
17 ~~graph (2) (B), (C), or (D);~~

18 ~~“(4) any amount paid by one corporation to an-~~
19 ~~other corporation, if both corporations are members of~~
20 ~~the same affiliated group which filed a consolidated re-~~
21 ~~turn for the preceding taxable year of the affiliated~~
22 ~~group;~~

23 ~~“(5) interest subject to withholding under subchap-~~
24 ~~ter A of chapter 3 (sec. 1441 and following, relating to~~
25 ~~withholding of tax on nonresident aliens and foreign cor-~~

porations) by the person paying such interest, or which would be so subject to withholding by such person, but for the fact that it is not treated as income from sources within the United States;

“(6) any amount on which the withholding agent is required to deduct and withhold a tax under section 1451 (relating to tax-free covenant bonds), or would be so required but for section 1451(d) (relating to benefit of personal exemptions);

“(7) to the extent provided in regulations prescribed by the Secretary or his delegate, any amount payable with respect to deposits in school savings accounts; and

“(8) any amount described in subsection (a)(2), (3), or (7) paid to a State or a foreign government or international organization (other than any amount described in subsection (a)(3) paid in respect of a transferable certificate or share).

“(e) EXEMPTION FOR UNITED STATES.—The Secretary may authorize exemption from the tax imposed by section 3451 for any amount paid by the United States or any wholly owned agency or instrumentality thereof to the United States or any wholly owned agency or instrumentality thereof if the Secretary determines that the imposition of the tax with respect to such amount will cause a burden

1 or expense which can be avoided by granting the tax
2 exemption.

3 **“Subchapter B—Dividends**

“Sec. 3461. Income tax collected at source on dividends.

“Sec. 3462. Dividend defined.

4 **“SEC. 3461. INCOME TAX COLLECTED AT SOURCE ON** 5 **DIVIDENDS.**

6 “(a) REQUIREMENT OF WITHHOLDING.—Except as
7 otherwise provided in this chapter, every person who pays
8 a dividend shall deduct and withhold on such dividend a tax
9 equal to 20 percent of the amount thereof.

10 “(b) PAYEE UNKNOWN.—If the withholding agent is
11 unable to determine the person to whom the dividend is
12 payable, the tax under this section shall be deducted and
13 withheld at the time payment of the dividend would be
14 made if such person were known.

15 “(c) AMOUNT OF DIVIDEND UNKNOWN.—If the with-
16 holding agent is unable to determine the portion of a dis-
17 tribution which is a dividend, the tax under this section
18 shall be computed on the entire amount of the distribution.

19 “(d) CROSS REFERENCES.—

“ (1) For credit, against income tax of the recipient of the income, of amounts deducted and withheld under this section, see section 39.

“ (2) For special rules as to credit or refund of such amounts, see sections 3484, 3485, 3486, 3487, and 3505.

“ (3) For exemption from requirement of deducting and withholding on dividends paid to certain individuals, see section 3483.

1 “SEC. 3462. DIVIDEND DEFINED.

2 “(a) GENERAL RULE.—For purposes of this chapter,
3 the term ‘dividend’ means—

4 “(1) any distribution by a corporation which is a
5 dividend (as defined in section 316); and

6 “(2) any payment made by a stockbroker to any
7 person as a substitute for a dividend (as so defined).

8 “(b) EXCEPTIONS.—For purposes of this chapter, the
9 term ‘dividend’ does not include—

10 “(1) any amount paid in the stock, or rights to
11 acquire the stock, of the distributing corporation if the
12 distribution is not includible in gross income of the re-
13 cipient under the provisions of section 305 (relating to
14 distributions of stock and stock rights);

15 “(2) any distribution to the extent that, under
16 chapter 1—

17 “(A) the amount thereof is treated by the re-
18 cipient as an amount received on the sale or ex-
19 change of property; or

20 “(B) gain or loss to the recipient is not recog-
21 nized;

22 “(3) any amount which is includible in gross in-
23 come as a taxable dividend by reason of the provisions
24 of section 302 (relating to redemptions of stock), 306

1 ~~(relating to dispositions of certain stock), 356 (relating~~
2 ~~to receipt of additional consideration in connection with~~
3 ~~certain reorganizations), or 1081(c)(2) (relating to~~
4 ~~certain distributions pursuant to order of the Securities~~
5 ~~and Exchange Commission);~~

6 ~~“(4) any amount paid by one corporation to an-~~
7 ~~other corporation, if both corporations are members of~~
8 ~~the same affiliated group which filed a consolidated re-~~
9 ~~turn for the preceding taxable year of the affiliated~~
10 ~~group;~~

11 ~~“(5) an amount which—~~

12 ~~“(A) is subject to withholding under subchap-~~
13 ~~ter A of chapter 3 (sec. 1441 and following, relating~~
14 ~~to withholding of tax on nonresident aliens and for-~~
15 ~~ign corporations) by the person paying such~~
16 ~~amount, or~~

17 ~~“(B) would be subject to withholding under~~
18 ~~such subchapter A by the person paying such~~
19 ~~amount but for—~~

20 ~~“(i) the fact that it is attributable to in-~~
21 ~~come from sources outside the United States, or~~

22 ~~“(ii) the fact that the payor thereof is~~
23 ~~excepted from the application of section~~
24 ~~1441(a) by the provisions of section 1441(c);~~

25 ~~“(6) any amount paid by a foreign corporation not~~

engaged in trade or business within the United States;

“(7) any amount described in section 1373 (relating to undistributed taxable income of electing small business corporations); and

“(8) amounts paid pursuant to the terms of a lease entered into before January 1, 1954, if under such lease the shareholders of the lessor corporation are entitled to such amounts without deduction for any tax which any law of the United States might require to be deducted and withheld on the payment of dividends.

“Subchapter C—Patronage Dividends

“Sec. 3471. Income tax collected at source on patronage dividends.

“Sec. 3472. Amounts subject to withholding.

“SEC. 3471. INCOME TAX COLLECTED AT SOURCE ON PATRONAGE DIVIDENDS.

“(a) REQUIREMENT OF WITHHOLDING.—Except as otherwise provided in this chapter, every cooperative to which part I of subchapter T of chapter 1 applies which pays an amount described in section 3472 shall deduct and withhold on such amount a tax equal to 20 percent of such amount.

“(b) PAYEE UNKNOWN.—If the withholding agent is unable to determine the person to whom the amount is payable, the tax under this section shall be deducted and with-

1 held at the time payment of the amount would be made if
 2 such person were known.

3 ~~“(c) CROSS REFERENCES.—~~

~~“(1) For credit, against income tax of the recipient
 of the income, of amounts deducted and withheld
 under this section, see section 39.~~

~~“(2) For special rules as to credit or refund of such
 amounts, see sections 3484, 3485, 3486, 3487, and 3505.~~

~~“(3) For exemption from requirement of deducting
 and withholding on amounts paid to certain indi-
 viduals, see section 3483.~~

4 **“SEC. 3472. AMOUNTS SUBJECT TO WITHHOLDING.**

5 ~~“(a) GENERAL RULE.—~~Except as otherwise provided
 6 in this section or section 3483, the amounts subject to deduc-
 7 tion and withholding under section 3471 are—

8 ~~“(1) the amount of any patronage dividend (as~~
 9 ~~defined in section 1388(a)) which is paid in money,~~
 10 ~~qualified written notices of allocation (as defined in sec-~~
 11 ~~tion 1388(e)), or other property (except nonqualified~~
 12 ~~written notices of allocation as defined in section~~
 13 ~~1388(d)), and~~

14 ~~“(2) any amount, described in section 1382(e) (2)~~
 15 ~~(A) (relating to certain nonpatronage distributions),~~
 16 ~~which is paid in money, qualified written notices of al-~~
 17 ~~location, or other property (except nonqualified written~~
 18 ~~notices of allocation) by an organization exempt from~~
 19 ~~tax under section 521 (relating to exemption of farm-~~
 20 ~~ers' cooperatives from tax).~~

1 “(b) **EXCEPTIONS.**—The provisions of section 3471
2 shall not apply to—

3 “(1) any amount paid by one corporation to an-
4 other corporation, if both corporations are members of
5 the same affiliated group which filed a consolidated re-
6 turn for the preceding taxable year of the affiliated
7 group;

8 “(2) an amount which—

9 “(A) is subject to withholding under sub-
10 chapter A of chapter 3 (sec. 1441 and following,
11 relating to withholding of tax on nonresident aliens
12 and foreign corporations) by the person paying such
13 amount, or

14 “(B) would be subject to withholding under
15 such subchapter A by the person paying such
16 amount but for the fact that it is attributable to
17 income from sources outside the United States; and

18 “(3) any amount paid by a foreign corporation
19 not engaged in trade or business within the United
20 States.

21 “(c) **EXEMPTION FOR CERTAIN CONSUMER COOPERA-**
22 **TIVES.**—A cooperative which the Secretary or his delegate
23 determines is primarily engaged in selling at retail goods
24 or services of a type that are generally for personal, living,
25 or family use shall, upon application to the Secretary or his

1 delegate, be granted exemption from the tax imposed by
 2 section 3471. Application for exemption under this sub-
 3 section shall be made in accordance with regulations pre-
 4 scribed by the Secretary or his delegate.

5 “(d) DETERMINATION OF AMOUNT PAID.—For pur-
 6 poses of this subchapter, in determining amounts paid—

7 “(1) property (other than a written notice of
 8 allocation) shall be taken into account at its fair market
 9 value; and

10 “(2) a qualified written notice of allocation shall
 11 be taken into account at its stated dollar amount.

12 “Subchapter D—General Provisions

“Sec. 3481. Liability for return and payment of withheld
 tax.

“Sec. 3482. Return and payment by United States.

“Sec. 3483. Exemption certificates.

“Sec. 3484. Refund of tax to individuals.

“Sec. 3485. Refund of tax to States, tax-exempt organiza-
 tions, etc.

“Sec. 3486. Refund of tax to corporation.

“Sec. 3487. Credit for tax withheld on corporation.

“Sec. 3488. Obligation sold between interest-payment dates.

“Sec. 3489. Presumption.

“Sec. 3490. Definitions.

13 “SEC. 3481. LIABILITY FOR RETURN AND PAYMENT OF 14 WITHHELD TAX.

15 “(a) GENERAL RULE.—Every person required to de-
 16 duct and withhold any tax under this chapter shall, on or be-
 17 fore the last day of the first month following the close of each
 18 quarter of his taxable year, make a return of the tax required

1 to be deducted and withheld during such quarter and pay the
2 tax to the officer designated in section 6151. The withhold-
3 ing agent shall be liable for the payment of the taxes required
4 to be deducted and withheld under this chapter, and shall not
5 otherwise be liable to any person for the amount of any
6 such payment.

7 ~~“(b) TAX PAID BY RECIPIENT.~~—If the withholding
8 agent, in violation of the provisions of this chapter, fails to
9 deduct and withhold any tax under this chapter, and there-
10 after the tax against which such tax may be credited is
11 paid, the tax so required to be deducted and withheld shall
12 not be collected from the withholding agent; but this sub-
13 section shall in no case relieve the withholding agent from
14 liability for any penalties or additions to the tax otherwise
15 applicable in respect of such failure to deduct and withhold.

16 ~~“(c) CROSS REFERENCE.~~—

**“For limitation on the use of Government depositories
in the collection of taxes deducted and withheld under
this chapter, see the last sentence of section 6302(e).**

17 **“SEC. 3482. RETURN AND PAYMENT BY UNITED STATES.**

18 **“If the withholding agent is the United States the re-**
19 **turn of the tax deducted and withheld under this chapter may**
20 **be made by an officer or employee of the United States**
21 **having control of the payment of the amount subject to**
22 **withholding, or appropriately designated for that purpose.**

1 **“SEC. 3483. EXEMPTION CERTIFICATES.**

2 ~~“(a)~~ **GENERAL RULES.—**

3 ~~“(1)~~ **INDIVIDUALS UNDER AGE 18.**—Any indi-
 4 vidual may file with any withholding agent an exemp-
 5 tion certificate on which he certifies the date of his
 6 birth. If such a certificate is filed, all amounts pay-
 7 able by such withholding agent to such individual, on
 8 and after the effective date for such certificate and
 9 before the beginning of the calendar year during which
 10 the certificate indicates that he will attain age 18, shall
 11 be exempt from the requirement of deducting and with-
 12 holding under this chapter.

13 ~~“(2)~~ **INDIVIDUALS OVER AGE 17.**—Any individual
 14 may file with any withholding agent an exemption
 15 certificate on which he certifies—

16 ~~“(A)~~ that he will have attained age 18 before
 17 the close of the calendar year for which such certifi-
 18 cate is filed, and

19 ~~“(B)~~ that he reasonably believes that he will
 20 not ~~(after the application of the credits against tax~~
 21 provided by part IV of subchapter A of chapter 1,
 22 other than the credits under sections 31 and 39) be
 23 liable for the payment of any tax under chapter 1 for
 24 each of his taxable years any portion of which is

1 included in the period for which such certificate
2 will be in effect.

3 If such a certificate is filed, all amounts payable by such
4 withholding agent to such individual during the period
5 such certificate is in effect shall be exempt from the
6 requirement of deducting and withholding under this
7 chapter. Except as may otherwise be provided in regu-
8 lations prescribed by the Secretary or his delegate, an
9 exemption certificate filed by an individual described in
10 this paragraph shall remain in effect only for the period
11 beginning on the effective date of such certificate and
12 ending at the close of the calendar year in which such
13 period begins.

14 “~~(3)~~ TAX EXEMPT ORGANIZATIONS.—

15 “~~(A)~~ Any organization ~~(other than a coopera-~~
16 ~~tive described in section 521)~~ which is exempt from
17 the tax imposed by chapter 1 may file with any
18 withholding agent who pays amounts described in
19 section 3452(a) ~~(2)~~, ~~(3)~~, or ~~(7)~~ an exemption
20 certificate on which it certifies that it is such an
21 organization. If such a certificate is filed, all
22 amounts described in section 3452(a) ~~(2)~~,
23 ~~(3)~~, and ~~(7)~~ payable by such withholding agent
24 to such organization on and after the effective date
25 for such certificate shall ~~(except as provided in sub-~~

1 paragraph (B)) be exempt from the requirement
2 of deducting and withholding under this chapter.

3 “(B) An exemption certificate filed by an
4 organization under subparagraph (A) shall cease
5 to be effective on the thirtieth day after the day on
6 which the withholding agent, with whom such cer-
7 tificate was filed, is notified by either the organiza-
8 tion or the Secretary or his delegate that the
9 organization is no longer exempt from the tax im-
10 posed by chapter 1. If an organization ceases to be
11 exempt from such tax, it shall, within the time speci-
12 fied in regulations prescribed by the Secretary or his
13 delegate, so notify each withholding agent with
14 whom it has an exemption certificate in effect.

15 “(b) EXCEPTIONS AND SPECIAL RULES.—

16 “(1) CERTAIN EXCEPTIONS.—This section shall
17 not apply to any amount—

18 “(A) described in section 3452(a)(1) (re-
19 lating to interest on evidences of indebtedness),

20 “(B) described in section 3452(a)(3) paid
21 in respect of a transferable certificate or share, or

22 “(C) described in section 3452(a)(6) (relat-
23 ing to interest on obligations of the United States).

24 “(2) Series E BONDS, ETC.—In the case of trans-
25 actions involving the redemption of one or more obliga-

tions described in section 3452(a)(7) (relating to certain obligations of the United States issued on a discount basis); a separate certificate shall be filed with respect to each such transaction.

“(3) NOMINEES, CUSTODIANS, AND JOINT OWNERSHIPS.—Under regulations prescribed by the Secretary or his delegate, the exemption provided by subsection (a) may be extended, in a manner consistent with the other provisions of this section, to—

“(A) amounts (other than amounts described in section 3462(a), relating to dividends) paid through nominees;

“(B) amounts paid to custodians; and

“(C) amounts paid jointly to 2 or more individuals.

“(4) EFFECTIVE DATE OF CERTIFICATE.—Any exemption certificate under this section shall take effect on such day as is specified in accordance with regulations prescribed by the Secretary or his delegate.

“(5) FORM AND CONTENTS OF CERTIFICATE AND NOTICE.—Any exemption certificate under this section, and any notice under subsection (a)(3)(B), shall be in such form and contain such information as the Secretary or his delegate may by regulations prescribe.

1 “(c) CROSS REFERENCE.—

“For penalty for filing fraudulent certificate, or for failing to provide notice, under this section, see section 7205.

2 “SEC. 3484. REFUND OF TAX TO INDIVIDUALS.

3 “(a) GENERAL RULE.—Except as provided in subsec-
 4 tion (c), the tax deducted and withheld under this chapter
 5 with respect to amounts received by an individual during
 6 any quarter (other than the fourth quarter) of his taxable
 7 year (together with any tax so deducted and withheld on
 8 amounts which were received by him during any prior quar-
 9 ter of such year and with respect to which no allowable claim
 10 for refund has been filed under this section) shall, to the
 11 extent such tax does not exceed his refund allowance as of
 12 the time the claim for refund is filed, be promptly refunded
 13 to him as an overpayment of tax. A refund of tax shall be
 14 made under this section only if the amount claimed and
 15 allowable equals or exceeds \$10.

16 “(b) REFUND ALLOWANCE.—For purposes of this sec-
 17 tion, the refund allowance of an individual as of the time the
 18 claim for refund is filed is an amount equal to the excess, if
 19 any, of—

20 “(1) an amount equal to 22 percent of—

21 “(A) the total of the deductions which, on the
 22 basis of facts existing at the time the claim for refund

1 is filed, such individual would be allowed for the tax-
2 able year under section 151 (relating to deductions
3 for personal exemptions), plus

4 “(B) in the case of an individual who, at the
5 time the claim for refund is filed, reasonably ex-
6 pects that he will be allowed a credit under section
7 37 (relating to retirement income) for the taxable
8 year, the amount which, at such time, such individ-
9 ual reasonably expects to be the amount of his re-
10 tirement income (as defined in section 37(c) and as
11 limited by section 37(d)) for the taxable year,
12 less

13 “(C) the amounts (other than amounts on
14 which tax is required to be deducted and withheld
15 under this chapter) which, at the time the claim for
16 refund is filed, such individual reasonably expects
17 to be includible in his gross income for the taxable
18 year; over

19 “(2) the amounts of tax with respect to which an
20 allowable claim for refund has been previously filed
21 under this section during taxable year.

22 For purposes of paragraph (1)(C), an individual who files
23 more than one claim for refund under this section for any
24 taxable year may use the estimate for the preceding claim
25 for such year unless, at the time he files the claim, he reason-

ably expects the amounts referred to in paragraph ~~(1)-(C)~~ to exceed such prior estimate by more than \$100.

~~“(c) MARRIED INDIVIDUALS.~~—For purposes of subsections ~~(a)~~, ~~(b)~~, and ~~(d)~~, married individuals shall be treated as an individual if, at the time the claim for refund is filed, they reasonably expect that they will file a joint return for the taxable year in which such claim is filed.

~~“(d) TIME FOR FILING CLAIM.~~—Not more than one claim may be filed under this section by any individual during any quarter of his taxable year. A refund of tax deducted and withheld on amounts received during a taxable year shall be made under this section only if claim therefor is filed on or before the last day of such taxable year.

~~“(e) INDIVIDUALS NOT ELIGIBLE FOR REFUND.~~—No claim for refund may be filed under this section by—

~~“(1) any individual (other than an individual referred to in paragraph ~~(2)~~ or ~~(3)~~) unless, at the time the claim for refund is filed, he reasonably expects that his gross income for the taxable year will not exceed \$5,000;~~

~~“(2) any married individual unless, at the time the claim for refund is filed, he reasonably expects that the aggregate gross income of such individual and his spouse for the taxable year will not exceed \$10,000;~~

~~“(3) a head of a household (as defined in section~~

~~1(b)(2)~~ or a surviving spouse (as defined in section ~~2(b)~~) unless, at the time the claim for refund is filed, he reasonably expects that his gross income for the taxable year will not exceed \$10,000; or

~~“(4) any child, unless, at the time the claim for refund is filed, he reasonably expects that no deduction would be allowed for him under section 151(c)(1)(B) for the taxable year of his parent (or parents) beginning with or within the calendar year in which the claim for refund is filed.~~

~~“(f) CROSS REFERENCE.—~~

“For credit or refund of amounts not refunded under this section, see section 39.

“SEC. 3485. REFUND OF TAX TO STATES, TAX-EXEMPT ORGANIZATIONS, ETC.

~~“(a) GENERAL RULE.—~~In the case of a person which is—

~~“(1) the United States or a State,~~

~~“(2) an organization (other than a cooperative described in section 521) which is exempt from the tax imposed by chapter 1,~~

~~“(3) a foreign government or international organization, or~~

~~“(4) a foreign central bank of issue,~~

1 if the tax deducted and withheld under this chapter with re-
 2 spect to amounts received by such person during any calendar
 3 quarter exceeds the credit, if any, claimed by and allowable
 4 to such person under section 3505 (relating to credit against
 5 employment taxes) for such quarter; the excess (together
 6 with any such excess for any prior quarter of the same
 7 calendar year with respect to which no refund has been
 8 claimed and allowed under this section) shall be promptly
 9 refunded or credited to such person as an overpayment of
 10 tax. In the case of a person to which paragraph (4) ap-
 11 plies, the amount which may be refunded or credited under
 12 this section shall not exceed the amount of tax deducted
 13 and withheld under section 3451 on interest paid on obliga-
 14 tions of the United States which are not held for, or used in
 15 connection with, the conduct of commercial banking functions
 16 or other commercial activities.

17 **“(b) CROSS REFERENCES.—**

“(1) For period of limitation for filing claim under this section, see section 6511.

“(2) For presumed date of payment for purposes of (A) period of limitation, see section 6513(b), and (B) allowance of interest on overpayments, see section 6611(d).

18 **“SEC. 3486. REFUND OF TAX TO CORPORATION.**

19 **“(a) GENERAL RULE.—**If the tax deducted and with-
 20 held under this chapter with respect to amounts received by
 21 a corporation (other than a corporation described in section

1 3485(a)) during any quarter (other than the fourth quar-
 2 ter) of its taxable year exceeds the amount claimed by and
 3 allowable to such corporation under section 3487 as a credit
 4 against its liability for tax under this chapter for such quar-
 5 ter, the excess (together with any such excess for any prior
 6 quarter of the same year with respect to which no refund has
 7 been claimed and allowed under this section) shall be
 8 promptly refunded or credited to such corporation as an over-
 9 payment of tax. A refund of tax shall be made under this
 10 section only if claim therefor is filed after the close of the
 11 period covered by the claim and on or before the last day
 12 of the taxable year.

13 “(b) CROSS REFERENCE.—

“For credit or refund of amounts not refunded
 under this section, see section 39.

14 “SEC. 3487. CREDIT FOR TAX WITHHELD ON CORPORA-
 15 TION.

16 “(a) GENERAL RULE.—Any tax deducted and with-
 17 held under this chapter with respect to amounts received
 18 by a corporation (other than a corporation described in sec-
 19 tion 3485(a)) during a taxable year shall, to the extent not
 20 claimed and allowable as a credit or refund to the corporation
 21 under section 3486, be allowed, under regulations prescribed
 22 by the Secretary or his delegate, as a credit against (but

1 not in excess of) the tax for which such corporation is liable
 2 under this chapter in respect of amounts paid by it during
 3 such year.

4 “(b) DIVIDENDS AND PATRONAGE DIVIDENDS PAID
 5 DURING TAXABLE YEAR.—For purposes of determining the
 6 credit allowable to any corporation under subsection (a), a
 7 dividend, or amount subject to withholding under section
 8 3471, paid by it may be considered as having been paid
 9 during the taxable year—

10 “(1) in the case of a personal holding company, if
 11 treated as paid during such taxable year under section
 12 563(b),

13 “(2) in the case of a regulated investment com-
 14 pany, if treated as paid during such taxable year under
 15 section 855(a),

16 “(3) in the case of a real estate investment trust, if
 17 treated as paid during such taxable year under section
 18 858(a), or

19 “(4) in the case of a cooperative described in sec-
 20 tion 1381(a), if paid during the payment period (as
 21 defined in section 1382(d)) for such taxable year.

22 “(c) SPECIAL RULE FOR CORPORATIONS WHICH ARE
 23 MEMBERS OF AN AFFILIATED GROUP.—To the extent and
 24 subject to such conditions as may be provided in regulations
 25 prescribed by the Secretary or his delegate, the tax deducted

1 and withheld under this chapter with respect to amounts
2 received by a corporation which is a member of an affiliated
3 group which filed a consolidated return for the preceding tax-
4 able year of the affiliated group may, for purposes of this
5 section, be treated as tax deducted and withheld under this
6 chapter from any corporation which is a member of the
7 same affiliated group.

8 **"SEC. 3488. OBLIGATION SOLD BETWEEN INTEREST-PAY-**
9 **MENT DATES.**

10 "For purposes of any credit or refund provided in sec-
11 tion 3484, 3485, 3486, or 3487, in the case of an obliga-
12 tion which is sold or exchanged between interest-payment
13 dates the amount required to be deducted and withheld on
14 the interest at the end of the interest-payment period shall
15 be treated in the manner provided in section 39(c).

16 **"SEC. 3489. PRESUMPTION.**

17 "For purposes of establishing that any person is entitled
18 to a credit or refund of any tax required to be deducted and
19 withheld under this chapter with respect to amounts received
20 by such person, the correct amount of such tax shall, in the
21 absence of evidence to the contrary, be presumed to have
22 been so deducted and withheld.

23 **"SEC. 3490. DEFINITIONS.**

24 "For purposes of this chapter—

25 **"(1) PERSON.**—The term 'person' includes the

1 United States, a State, a foreign government, and an
2 international organization.

3 “(2) STATE.—The term ‘State’ includes a State, the
4 District of Columbia, a possession of the United States,
5 any political subdivision of any of the foregoing, and any
6 wholly owned agency or instrumentality of any one or
7 more of the foregoing.

8 “(3) FOREIGN GOVERNMENT.—The term ‘foreign
9 government’ includes a foreign government, a politi-
10 cal subdivision of a foreign government, and any wholly
11 owned agency or instrumentality of any one or more of
12 the foregoing.

13 “(4) NONRESIDENT ALIEN.—The term ‘nonresident
14 alien individual’ includes an alien resident of Puerto
15 Rico.”

16 (2) CLERICAL AMENDMENTS, ETC.—

17 (A) The heading for subtitle C is amended to
18 read as follows:

19 **["Subtitle C—Employment Taxes and**
20 **Collection of Income Tax at Source"]**

21 (B) The table of chapters for subtitle C is
22 amended by striking out the last line and inserting
23 in lieu thereof the following:

“CHAPTER 25. Collection of income tax at source on interest,
dividends, and patronage dividends.

“CHAPTER 26. General provisions relating to employment
taxes and collection of income taxes at
source.”

(C) The table of subtitles under the heading “Internal Revenue Title” at the beginning of the Internal Revenue Code of 1954 is amended by striking out the third line and inserting in lieu thereof the following:

“~~SUBTITLE C.~~ Employment taxes and collection of income tax at source.”

(D) The heading for chapter 26 (as redesignated by paragraph (1) of this subsection) is amended to read as follows:

“CHAPTER 26—GENERAL PROVISIONS RELATING TO EMPLOYMENT TAXES AND COLLECTION OF INCOME TAXES AT SOURCE”

~~(b) CREDITS AGAINST INCOME TAX FOR TAX WITHHELD.—~~

~~(1) ALLOWANCE OF CREDIT.—~~Part IV of subchapter A of chapter 1 (relating to credits against tax) is amended by inserting after section 38 (added by section 2 of this Act) the following new section:

“SEC. 39. TAX WITHHELD ON INTEREST, DIVIDENDS, AND PATRONAGE DIVIDENDS.

~~“(a) GENERAL RULE.—~~Under regulations prescribed by the Secretary or his delegate, the tax deducted and withheld under chapter 25 (relating to withholding at source

1 on interest, dividends, and patronage dividends) shall be
 2 allowed, to the recipient of the amount with respect to which
 3 such tax was deducted and withheld, as a credit against the
 4 tax imposed by this subtitle for the taxable year in which
 5 such amount is received.

6 “(b) SPECIAL RULE FOR DEPENDENT CHILDREN.—
 7 If—

8 “(1) the taxpayer for his taxable year is entitled
 9 to a deduction under section 151(c)(1)(B) with re-
 10 spect to a child, and

11 “(2) such child had, for the calendar year ending
 12 with or within the taxpayer’s taxable year—

13 “(A) gross income of less than \$600, and

14 “(B) no wages (as defined in section 3401
 15 (a)) with respect to which withholding was re-
 16 quired under chapter 24,

17 then, under regulations prescribed by the Secretary or his
 18 delegate, the taxpayer shall be entitled to the credit pro-
 19 vided by subsection (a) with respect to amounts received
 20 by such child during such calendar year, but only if such
 21 child has not filed any claim for credit or refund of any por-
 22 tion of the tax deducted and withheld with respect to such
 23 amounts.

24 “(c) APPORTIONMENT OF CREDIT.—For purposes of

1 subsection (a), if an obligation is sold or exchanged between
2 interest payments dates—

3 ~~(1)~~ so much of the amount required to be deducted
4 and withheld on the interest at the end of the interest-
5 payment period as is properly allocable to that part of
6 such period which ends on the date of the sale or ex-
7 change shall be treated as an amount deducted and with-
8 held from the transferor on the date of the sale or
9 exchange, and

10 ~~“(2)~~ so much of such amount as is properly al-
11 locable to that part of such period which begins on the
12 day after the date of the sale or exchange shall be treated
13 as an amount deducted and withheld from the transferee.

14 ~~“(d)~~ LIMITATIONS.—The credit provided by subsection
15 (a) shall not be allowed—

16 ~~“(1)~~ REFUND TO INDIVIDUALS.—To any indi-
17 vidual with respect to any amount of tax allowed him
18 as a refund under section 3484.

19 ~~“(2)~~ CREDIT OR REFUND TO STATES, ETC.—To
20 any person with respect to any amount of tax allowable
21 to such person as a credit or refund under section 3485
22 or as a credit under section 3505.

23 ~~“(3)~~ CREDIT OR REFUND TO CORPORATIONS.—To
24 any person with respect to any amount of tax allowed

1 such person as a credit or refund under section 3486 or
2 as a credit under section 3487.

3 “(4) CERTAIN DEPENDENT CHILDREN.—To any
4 person with respect to any amount of tax which has
5 been claimed and is allowable as a credit to such
6 person’s parent by reason of the provisions of subsection
7 (b).”

8 “(5) NOMINEES, ETC.—To any person with respect
9 to any amount of tax allowed such person as a credit
10 under section 1444(b).”

11 “(2) COMMON TRUST FUNDS.—Section 584(e) (re-
12 lating to the income of participants in the fund) is
13 amended by adding at the end thereof the following
14 new paragraph:

15 “(3) TAX WITHHELD AT SOURCE ON INTEREST,
16 DIVIDENDS, AND PATRONAGE DIVIDENDS.—In any case
17 where tax under chapter 25 is deducted and withheld
18 on any amounts received by a common trust fund, for
19 purposes of any credit or refund provided in section 39
20 or 3505, or chapter 25, such tax shall, in accordance
21 with regulations prescribed by the Secretary or his dele-
22 gate, be considered as having been deducted and with-
23 held proportionately from each participant.”

24 “(3) ESTATES AND TRUSTS.—Section 642(a) (re-
25 lating to special rules for credits and deductions in the

1 ease of estates and trusts) is amended by adding at the
2 end thereof the following new paragraph:

3 “(4) TAX WITHHELD AT SOURCE ON INTEREST,
4 DIVIDENDS, AND PATRONAGE DIVIDENDS.—In any case
5 where tax under chapter 25 is deducted and withheld
6 on any amounts received by an estate or trust, for pur-
7 poses of any credit or refund provided in section 39
8 or 3505, or chapter 25, such tax shall, in accordance
9 with regulations prescribed by the Secretary or his dele-
10 gate, be considered as having been deducted and with-
11 held from each beneficiary in an amount which, when
12 added to the amounts paid, credited, or required to be
13 distributed to him, equals the amounts which would
14 have been paid, credited, or required to be distributed
15 to him in the absence of chapter 25. Any tax under
16 chapter 25 which is deducted and withheld on amounts
17 received by the estate or trust shall be considered as
18 withheld from such estate or trust to the extent it is
19 not considered as withheld from a beneficiary under
20 the provisions of the preceding sentence.”

21 (4) TECHNICAL AMENDMENTS.—

22 (A) Section 164(b)(1) (relating to deduc-
23 tion denied in the case of certain taxes) is amended
24 by—

1 ~~(i)~~ striking out the word “and” at the end
2 of subparagraph ~~(B)~~;

3 ~~(ii)~~ striking out the comma at the end of
4 subparagraph ~~(C)~~ and inserting “; and”; and

5 ~~(iii)~~ adding after subparagraph ~~(C)~~ the
6 following new subparagraph:

7 “~~(D)~~ the tax withheld at source under chapter
8 25 ~~(relating to collection of income tax at source~~
9 on interest, dividends, and patronage dividends),”.

10 ~~(B)~~ Section 874(a) ~~(relating to allowance of~~
11 deductions and credits to nonresident alien indi-
12 viduals) is amended by striking “31 and 32” and
13 inserting in lieu thereof “31, 32, and 39”.

14 ~~(C)~~ Section 1314(e) ~~(relating to inapplica-~~
15 bility of part II of subchapter Q of chapter 1 of
16 subtitle A to taxes imposed by subtitle C) is
17 amended by striking “employment taxes” and in-
18 serting in lieu thereof “employment taxes and
19 collection of income tax at source”.

20 ~~(D)~~ Section 6211(b)(1) ~~(relating to rules~~
21 applicable in determination of deficiency) is
22 amended by striking “31” and inserting in lieu
23 thereof “31 or 39”.

~~(E)~~ The table of sections for part IV of subchapter A of chapter 1 is amended by striking out

“Sec. 38. Overpayments of tax.”

and inserting in lieu thereof

“Sec. 38. Investment in certain depreciable property.

“Sec. 39. Tax withheld on interest, dividends, and patronage dividends.

“Sec. 40. Overpayments of tax.”

~~(c)~~ INTEREST AND DIVIDENDS PAID TO NONRESIDENT ALIENS, ETC.—

~~(1)~~ WITHHOLDING RATE.—

~~(A)~~ Section 1441 (relating to withholding of tax on nonresident aliens) is amended by adding at the end thereof the following new subsection:

“~~(c)~~ TREATIES.—In the case of amounts described in section 3452(a) (relating to interest); section 3462(a) (relating to dividends); and section 3472(a) (relating to patronage dividends); the tax required to be deducted and withheld under subsection (a) shall not by reason of the provisions of any treaty be less than 20 percent of such amounts.”

~~(B)~~ Section 1442 (relating to withholding of tax on foreign corporations) is amended by adding at the end thereof the following new sentence: “In the case of amounts described in section 3452(a)

1 ~~(relating to interest)~~, section 3462(a) ~~(relating to~~
 2 dividends), and section 3472(a) ~~(relating to pa-~~
 3 tronage dividends), the tax required to be deducted
 4 and withheld under the preceding sentence shall
 5 not by reason of the provisions of any treaty be
 6 less than 20 percent of such amounts.”

7 ~~(2)~~ NOMINEES, ETC.—Subchapter A of chapter
 8 3 ~~(relating to withholding of tax on nonresident aliens~~
 9 and foreign corporations) is amended by adding at the
 10 end thereof the following new section:

11 **“SEC. 1444. INTEREST AND DIVIDENDS PAID TO NOMI-**
 12 **NEES; CREDITS TO WITHHOLDING AGENTS.**

13 “(a) WITHHOLDING OF TAX BY PAYOR.—Under regu-
 14 lations prescribed by the Secretary or his delegate, every
 15 person who pays amounts subject to withholding under
 16 chapter 25 and who has been notified by a payee thereof that
 17 the payee is a nominee required to deduct and withhold
 18 on such amounts under section 1441 or 1442 shall, in
 19 lieu of the nominee, deduct and withhold from such amounts
 20 paid to the nominee the tax required to be deducted and
 21 withheld under section 1441 or 1442, in the same manner
 22 as if such amounts were paid by such person directly to the
 23 beneficial owner thereof.

24 “(b) CREDITS TO WITHHOLDING AGENTS.—In the case
 25 of any person who is required to deduct and withhold tax

1 under section 1441 or 1442 in respect of amounts received
 2 by him during any calendar year on which tax was deducted
 3 and withheld (or, in the case of amounts described in section
 4 ~~39(e)(1)~~, was treated as deducted and withheld) under
 5 chapter 25, the taxes so deducted and withheld (or treated
 6 as deducted and withheld) under chapter 25 shall, under
 7 regulations prescribed by the Secretary or his delegate, be
 8 allowed as a credit against (but not in excess of) his liability
 9 for the year in respect of the taxes imposed by sections 1441
 10 and 1442.”

11 ~~(3)~~ CLERICAL AMENDMENT.—The table of sec-
 12 tions for subchapter A of chapter 3 is amended by add-
 13 ing at the end thereof the following:

“Sec. 1444. Interest and dividends paid to nominees; credits
 to withholding agents.”

14 ~~(d)~~ CREDIT FOR STATES AND TAX-EXEMPT ORGANI-
 15 ZATIONS.—

16 ~~(1)~~ ALLOWANCE OF CREDIT.—Chapter 26 (gen-
 17 eral provisions relating to employment taxes and income
 18 tax withheld at source) is amended by adding at the
 19 end thereof the following new section:

20 “SEC. 3505. SPECIAL CREDIT IN CASE OF STATES OR TAX-
 21 EXEMPT ORGANIZATIONS.

22 “(a) GENERAL RULE.—In the case of a person which is
 23 a State (as defined in section 3490(2)) or which is an or-

ganization (other than a cooperative described in section 521) which is exempt from the tax imposed by chapter 1, the tax deducted and withheld under chapter 25 with respect to amounts received by it during any calendar quarter shall be allowed, under regulations prescribed by the Secretary or his delegate, as a credit against (but not in excess of) such person's liability (after the adjustments, if any, provided for in sections 6205(a) and 6413(a)) for such quarter in respect of the taxes imposed by chapter 21 (Federal Insurance Contributions Act) and by chapter 24 (collection of income tax at source on wages). Such credit shall be allowed only if claim therefor is made, in accordance with such regulations, at the time of the filing of the return with respect to the taxes under chapter 21 and chapter 24 for such quarter.

“(b) OBLIGATIONS SOLD BETWEEN INTEREST PAYMENT DATES.—For purposes of this section, in the case of an obligation which is sold or exchanged between interest-payment dates, the amount required to be deducted and withheld on the interest at the end of the interest-payment period shall be treated in the manner provided in section 39(c).

“(c) CROSS REFERENCE.—

“For refund under chapter 25, see section 3485.”

~~(2)~~ TECHNICAL AMENDMENTS.—

~~(A)~~ Section 3502 ~~(relating to nondeductibil-~~
ity of taxes in computing taxable income) is
amended by adding at the end thereof the following
new subsection:

“(e) The tax deducted and withheld under chapter 25
shall not be allowed as a deduction in computing taxable
income under subtitle A either to the person deducting and
withholding the tax or to the recipient of the amounts sub-
ject to withholding.”

~~(B)~~ The table of sections for enapter 26 is
amended by adding at the end thereof the following:

“Sec. 3505. Special credit in ease of States or tax-exempt
organizations.”

~~(c)~~ OTHER TECHNICAL AMENDMENTS.—

~~(1)~~ DECLARATION OF ESTIMATED INCOME TAX
BY INDIVIDUALS.—Section 6015(a) ~~(relating to dec-~~
laration of estimated income tax by individuals) is
amended by striking out the period at the end of para-
graph ~~(2)~~ and inserting in lieu thereof “and amounts on
which tax is required to be deducted and withheld under
chapter 25.”

1 ~~(2)~~ ADJUSTMENT OF TAX; UNDERPAYMENT.—

2 ~~(A)~~ Subsection ~~(a)(1)~~ of section 6205 ~~(re-~~
3 relating to special rules relating to assessment of em-
4 ployment taxes) is amended by striking out “or
5 3402 is paid with respect to any payment of
6 wages or compensation,” and inserting in lieu there-
7 of “3402, 3451, 3461, or 3471 is paid with respect
8 to any payment of remuneration, interest, dividends,
9 or other amounts.”

10 ~~(B)~~ Subsection ~~(b)~~ of such section is amended
11 by striking out “or 3402 is paid or deducted with re-
12 spect to any payment of wages or compensation”
13 and inserting in lieu thereof “3402, 3451, 3461, or
14 3471 is paid or deducted with respect to any pay-
15 ment of remuneration, interest, dividends, or other
16 amounts”.

17 ~~(C)~~ The heading for such section is amended
18 to read as follows:

1 "SEC. 6205. SPECIAL RULES APPLICABLE TO CERTAIN
2 TAXES UNDER SUBTITLE C."

3 ~~(D)~~ The table of sections for subchapter A of
4 chapter 63 is amended by striking out

"Sec. 6205. Special rules applicable to certain employment
taxes."

5 and inserting in lieu thereof

"Sec. 6205. Special rules applicable to certain taxes under
subtitle C."

6 ~~(3)~~ USE OF GOVERNMENT DEPOSITARIES.—Section
7 6302(c) ~~(relating to use of Government depositaries)~~
8 is amended by adding at the end thereof the following
9 new sentence: "The Secretary or his delegate shall
10 not require the deposit under this subsection of any
11 tax deducted and withheld under chapter 25 ~~(relating~~
12 ~~to collection of income tax at source on interest, divi-~~
13 ~~dends, and patronage dividends)~~ in a Government
14 depositary before the last day prescribed in section 3481
15 for payment of the tax."

1 ~~(4)~~ EXCESSIVE WITHHOLDING.—Section 6401
 2 ~~(b)~~ ~~(relating to excessive withholding)~~ is amended to
 3 read as follows:

4 “~~(b)~~ EXCESSIVE WITHHOLDING.—If the amounts al-
 5 lowable as credits under section 31 ~~(relating to credit for tax~~
 6 withheld at source under chapter 24) and section 39 ~~(relat-~~
 7 ing to credit for tax withheld on interest, dividends, and
 8 patronage dividends under chapter 25) exceed the taxes
 9 imposed by chapter 1 against which such credits are allow-
 10 able, the amount of such excess shall be considered an over-
 11 payment.”

12 ~~(5)~~ ADJUSTMENT OF TAX; OVERPAYMENT.—

13 ~~(A)~~ Subsection ~~(a)~~~~(1)~~ of section 6413 ~~(re-~~
 14 lating to special credit and refund rules applicable
 15 to certain employment taxes) is amended by striking
 16 out “or 3402 is paid with respect to any payment
 17 of remuneration,” and inserting in lieu thereof
 18 “3402, 3451, 3461, or 3471 is paid with respect
 19 to any payment of remuneration, interest, dividends,
 20 or other amounts,”.

21 ~~(B)~~ Subsection ~~(b)~~ of such section is
 22 amended—

23 ~~(i)~~ By striking from the heading of such
 24 subsection the words “OF CERTAIN EMPLOY-
 25 MENT TAXES”; and

(ii) By striking out “or 3402 is paid or deducted with respect to any payment of remuneration” and inserting in lieu thereof “3402, 3451, 3461, or 3471 is paid or deducted with respect to any payment of remuneration, interest, dividends, or other amounts”.

(C) The following new subsection is added at the end of such section:

“(e) CROSS REFERENCES.—

“For special refunds or credits of tax withheld on interest, dividends, or patronage dividends under chapter 25, see sections 3484, 3485, 3486, 3487, and 3505.”

(D) The heading for such section is amended to read as follows:

“SEC. 6413. SPECIAL RULES APPLICABLE TO CERTAIN TAXES UNDER SUBTITLE C.”

(E) The table of sections for subchapter B of chapter 65 is amended by striking out

“Sec. 6413. Special rules applicable to certain employment taxes.”

and inserting in lieu thereof

“Sec. 6413. Special rules applicable to certain taxes under subtitle C.”

(6) OVERPAYMENT NOT DEDUCTED AND WITHHELD.—Section 6414 (relating to income tax withheld)

1 is amended by striking “chapter 3” and inserting in lieu
2 thereof “chapter 3 or 25”.

3 ~~(7)~~ TIME TAX CONSIDERED PAID.—Section 6513
4 ~~(b)~~ ~~(relating to time tax considered paid)~~ is amended
5 by adding at the end thereof the following new sen-
6 tences: “For purposes of section 6511 or 6512, any
7 tax deducted and withheld under chapter 25 which is
8 allowable under section 39, 3484, 3485, or 3486
9 as a credit against tax or as a refund of an overpayment
10 ~~(or an amount treated as an overpayment)~~ of the tax
11 imposed by chapter 1 shall, in respect of the person en-
12 titled to such credit or refund, be deemed to have been
13 paid by him on the last day prescribed for filing the re-
14 turn ~~(determined without regard to any extension of~~
15 ~~time for filing such return)~~ of tax under chapter 1 for
16 his taxable year in which the amount subject to with-
17 holding under chapter 25 is received by him or, if such
18 person has no taxable year, on the fifteenth day of the
19 fifth calendar month following the close of such person’s
20 annual accounting period within which such amount
21 is received by him. In the case of an amount allowable
22 as a credit under section 39 ~~(b)~~ to the parent of a child,
23 such amount shall, if claimed by the parent, be deemed
24 to have been paid on the last day for filing his return
25 ~~(determined without regard to any extension of time~~

for filing such return) for his taxable year which begins with or within the calendar year in which amounts subject to withholding under chapter 25 were received by the child."

~~(8)~~ FAILURE TO PAY ESTIMATED INCOME TAX.—

~~(A)~~ INDIVIDUALS.—Subsections ~~(e)~~ and ~~(f)~~ of section 6654 (relating to failure by individual to pay estimated income tax) are amended to read as follows:

~~"(e)~~ APPLICATION OF SECTION IN CASE OF WITHHELD TAXES.—For purposes of applying this section—

~~"(1)~~ the estimated tax shall be computed without any reduction for amounts which the individual estimates as his credits under section 31 (relating to tax withheld at source on wages) and section 39 (relating to tax withheld on interest, dividends, and patronage dividends): and

~~"(2)~~ the amount of the credits allowed under sections 31 and 39 for the taxable year shall be deemed a payment of estimated tax, and an equal part of such amount shall be deemed paid on each installment date (determined under section 6153) for such taxable year, unless the taxpayer establishes the dates on which all amounts were actually withheld (or in the case of amounts described in section 39~~(e)~~(1), were treated

1 as withheld), in which case the amounts so withheld
 2 shall be deemed payments of estimated tax on such
 3 dates.

4 “~~(f)~~ TAX COMPUTED AFTER APPLICATION OF
 5 CREDITS AGAINST TAX.—For purposes of subsections ~~(b)~~
 6 and ~~(d)~~, the term ‘tax’ means the tax imposed by chapter
 7 1 reduced by the credits against tax allowed by part IV of
 8 subchapter A of chapter 1, other than the credits against
 9 tax provided by section 31 (relating to tax withheld on
 10 wages) and section 39 (relating to tax withheld on interest,
 11 dividends, and patronage dividends).”

12 ~~(B)~~ CORPORATIONS.—Section 6655 (relating
 13 to failure by corporation to pay estimated income
 14 tax) is amended—

15 (i) by striking out the period at the end
 16 of subsection ~~(c)~~(2)~~(B)~~ and inserting in lieu
 17 thereof “, other than the credit against tax
 18 provided by section 39 (relating to tax with-
 19 held on interest, dividends, and patronage divi-
 20 dends).”; and

21 (ii) by redesignating subsection ~~(f)~~ as
 22 subsection ~~(g)~~ and inserting after subsection
 23 ~~(e)~~ the following new subsection:

1 “(f) APPLICATION OF SECTION IN CASE OF TAX
2 WITHHELD ON INTEREST, DIVIDENDS, AND PATRONAGE
3 DIVIDENDS.—For purposes of applying this section—

4 “(1) the estimated tax shall be computed without
5 any reduction for the amount which the corporation
6 estimates as its credit under section 39 (relating to tax
7 withheld on interest, dividends, and patronage divi-
8 dends); and

9 “(2) the amount of the credit allowed under sec-
10 tion 39 for the taxable year shall be deemed a payment
11 of estimated tax, and an equal part of such amount shall
12 be deemed paid on each installment date (determined
13 under section 6154) for such taxable year, unless the
14 corporation establishes the dates on which all amounts
15 were actually withheld (or in the case of amounts de-
16 scribed in section 39(c)(1), were treated as withheld);
17 in which case the amounts so withheld shall be deemed
18 payments of estimated tax on such dates.”

19 “(g) PENALTY FOR FILING FRAUDULENT EXEMP-
20 TION CERTIFICATE.—Section 7205 (relating to fraudu-
21 lent withholding exemption certificate or failure to sup-
22 ply information) is amended by adding the following
23 new sentence at the end thereof: “Any person who

1 willfully files an exemption certificate with any with-
2 holding agent under section 3483, on which the certifica-
3 tion is known by him to be fraudulent or to be false as
4 to any material matter, or who is required to file a notice
5 under subsection ~~(a) (3) (B)~~ of section 3483 and who
6 willfully fails to provide such notice in the manner, at
7 the time, and showing the information required under
8 such subsection ~~(a) (3) (B)~~, or the regulations pre-
9 scribed thereunder, shall, in lieu of any penalty otherwise
10 provided, upon conviction thereof, be fined not more than
11 \$500, or imprisoned not more than 1 year, or both."

12 ~~(10)~~ OFFENSES WITH RESPECT TO COLLECTED
13 TAXES.—The last sentence of section 7215(b) ~~(relating~~
14 ~~to offenses with respect to collected taxes)~~ is amended to
15 read as follows: "For purposes of paragraph ~~(2)~~, a lack
16 of funds existing immediately after the payment of wages
17 or amounts subject to withholding under chapter 25
18 ~~(whether or not created by the payment of such wages~~
19 ~~or amounts)~~ shall not be considered to be circumstances
20 beyond the control of a person."

21 ~~(11)~~ DEFINITION OF WITHHOLDING AGENT.—See-

tion 7701(a)(16) (defining the term “withholding agent”) is amended by striking out “or 1461” and inserting in lieu thereof “1461, 3451, 3461, or 3471”.

(f) EFFECTIVE DATES.—

(1) GENERAL RULE.—Except as provided in paragraph (2), the provisions of this section shall apply in the case of interest and dividends paid on or after January 1, 1963.

(2) SPECIAL RULES.—

(A) In the case of transferable obligations described in paragraph (1) or (6) of section 3452(a) of the Internal Revenue Code of 1954, the provisions of this section shall apply only to interest paid with respect to interest payment periods commencing on or after January 1, 1963.

(B) The provisions of this section shall apply to amounts described in section 3472 of such Code paid on or after January 1, 1963, with respect to patronage occurring on or after the first day of the first taxable year of the cooperative beginning on or after January 1, 1963.

1 SEC. 19. REPORTING OF INTEREST, DIVIDEND, AND PATRON-
 2 AGE DIVIDEND PAYMENTS OF \$10 OR MORE DURING
 3 A YEAR.

4 (a) RETURNS REGARDING PAYMENT OF DIVI-
 5 DENDS.—Section 6042 (relating to returns regarding cor-
 6 porate dividends, earnings, and profits) is amended to read
 7 as follows:

8 “SEC. 6042. RETURNS REGARDING PAYMENTS OF DIVIDENDS
 9 AND CORPORATE EARNINGS AND PROFITS.

10 “(a) REQUIREMENT OF REPORTING.—

11 “(1) IN GENERAL.—Every person—

12 “(A) who makes payments of dividends aggre-
 13 gating \$10 or more to any other person during any
 14 calendar year, or

15 “(B) who receives payments of dividends as a
 16 nominee and who makes payments aggregating \$10
 17 or more during any calendar year to any other per-
 18 son with respect to the dividends so received,

19 shall make a return according to the forms or regulations
 20 prescribed by the Secretary or his delegate, setting forth
 21 the aggregate amount of such payments and the name
 22 and address of the person to whom paid.

23 “(2) RETURNS REQUIRED BY THE SECRETARY.—

24 Every person who makes payments of dividends aggregat-

1 *ing less than \$10 to any other person during any*
2 *calendar year shall, when required by the Secretary or*
3 *his delegate, make a return setting forth the aggregate*
4 *amount of such payments, and the name and address of*
5 *the person to whom paid.*

6 “(b) *DIVIDEND DEFINED.*—

7 “(1) *GENERAL RULE.*—For purposes of this sec-
8 *tion, the term ‘dividend’ means—*

9 “(A) *any distribution by a corporation which is*
10 *a dividend (as defined in section 316); and*

11 “(B) *any payment made by a stockbroker to*
12 *any person as a substitute for a dividend (as so*
13 *defined).*

14 “(2) *EXCEPTIONS.*—For purposes of this section,
15 *the term ‘dividend’ does not include—*

16 “(A) *to the extent provided in regulations pre-*
17 *scribed by the Secretary or his delegate, any dis-*
18 *tribution or payment—*

19 “(i) *by a foreign corporation, or*

20 “(ii) *to a foreign corporation, ‘a nonresi-*
21 *dent alien, or a partnership not engaged in*
22 *trade or business in the United States and*
23 *composed in whole or in part of nonresident*
24 *aliens; and*

1 “(B) any amount described in section 1373
2 (relating to undistributed taxable income of elect-
3 ing small business corporations).

4 “(3) SPECIAL RULE.—If the person making any
5 payment described in subsection (a)(1) (A) or (B) is
6 unable to determine the portion of such payment which is
7 a dividend or is paid with respect to a dividend, he shall,
8 for purposes of subsection (a)(1), treat the entire
9 amount of such payment as a dividend or as an amount
10 paid with respect to a dividend.

11 “(c) STATEMENTS TO BE FURNISHED TO PERSONS
12 WITH RESPECT TO WHOM INFORMATION IS FUR-
13 NISHED.—Every person making a return under subsection
14 (a)(1) shall furnish to each person whose name is set forth
15 in such return a written statement showing—

16 “(1) the name and address of the person making
17 such return, and

18 “(2) the aggregate amount of payments to the per-
19 son as shown on such return.

20 The written statement required under the preceding sentence
21 shall be furnished to the person on or before January 31 of
22 the year following the calendar year for which the return
23 under subsection (a)(1) was made. No statement shall be
24 required to be furnished to any person under this subsection

1 *if the aggregate amount of payments to such person as shown*
2 *on the return made under subsection (a)(1) is less than \$10.*

3 “(d) *STATEMENTS TO BE FURNISHED BY CORPORA-*
4 *TIONS TO SECRETARY.*—Every corporation shall, when re-
5 quired by the Secretary or his delegate—

6 “(1) *furnish to the Secretary or his delegate a state-*
7 *ment stating the name and address of each shareholder,*
8 *and the number of shares owned by each shareholder;*

9 “(2) *furnish to the Secretary or his delegate a*
10 *statement of such facts as will enable him to determine*
11 *the portion of the earnings and profits of the corporation*
12 *(including gains, profits, and income not taxed) accum-*
13 *ulated during such periods as the Secretary or his dele-*
14 *gate may specify, which have been distributed or ordered*
15 *to be distributed, respectively, to its shareholders during*
16 *such taxable years as the Secretary or his delegate may*
17 *specify; and*

18 “(3) *furnish to the Secretary or his delegate a*
19 *statement of its accumulated earnings and profits and*
20 *the names and addresses of the individuals or share-*
21 *holders who would be entitled to such accumulated earn-*
22 *ings and profits if divided or distributed, and of the*
23 *amounts that would be payable to each.”*

1 **(b) RETURNS REGARDING PAYMENT OF PATRONAGE**
 2 *DIVIDENDS.*—Section 6044 (relating to returns regarding
 3 *patronage dividends*) is amended to read as follows:

4 “SEC. 6044. RETURNS REGARDING PAYMENTS OF PATRONAGE
 5 *DIVIDENDS.*

6 “(a) *REQUIREMENT OF REPORTING.*—

7 “(1) *IN GENERAL.*—Except as otherwise provided
 8 *in this section, every cooperative to which part I of sub-*
 9 *chapter T of chapter 1 applies, which makes payments*
 10 *of amounts described in subsection (b) aggregating \$10*
 11 *or more to any person during any calendar year, shall*
 12 *make a return according to the forms or regulations*
 13 *prescribed by the Secretary or his delegate, setting forth*
 14 *the aggregate amount of such payments and the name*
 15 *and address of the person to whom paid.*

16 “(2) *RETURNS REQUIRED BY THE SECRETARY.*—

17 *Every such cooperative which makes payments of*
 18 *amounts described in subsection (b) aggregating less*
 19 *than \$10 to any person during any calendar year shall,*
 20 *when required by the Secretary or his delegate, make a*
 21 *return setting forth the aggregate amount of such pay-*
 22 *ments and the name and address of the person to whom*
 23 *paid.*

24 “(b) *AMOUNTS SUBJECT TO REPORTING.*—

25 “(1) *GENERAL RULE.*—Except as otherwise pro-

vided in this section, the amounts subject to reporting under subsection (a) are—

“(A) the amount of any patronage dividend (as defined in section 1388 (a)) which is paid in money, qualified written notices of allocation (as defined in section 1388 (c)), or other property (except nonqualified written notices of allocation as defined in section 1388 (d)),

“(B) any amount described in section 1382(c)(2)(A) (relating to certain nonpatronage distributions) which is paid in money, qualified written notices of allocation, or other property (except nonqualified written notices of allocation) by an organization exempt from tax under section 521 (relating to exemption of farmers’ cooperatives from tax), and

“(C) any amount described in section 1382(b)(2) (relating to redemption of nonqualified written notices of allocation) and, in the case of an organization described in section 1381(a)(1), any amount described in section 1382(c)(2)(B) (relating to redemption of nonqualified written notices of allocation paid with respect to earnings derived from sources other than patronage).

“(2) EXCEPTIONS.—The provisions of subsection

1 *(a) shall not apply, to the extent provided in regulations*
 2 *prescribed by the Secretary or his delegate, to any*
 3 *payment—*

4 *“(A) by a foreign corporation, or*

5 *“(B) to a foreign corporation, a nonresident*
 6 *alien, or a partnership not engaged in trade or*
 7 *business in the United States and composed in whole*
 8 *or in part of nonresident aliens.*

9 *“(c) EXEMPTION FOR CERTAIN CONSUMER COOPER-*
 10 *ATIVES.—A cooperative which the Secretary or his delegate*
 11 *determines is primarily engaged in selling at retail goods*
 12 *or services of a type that are generally for personal, living,*
 13 *or family use shall, upon application to the Secretary or his*
 14 *delegate, be granted exemption from the reporting require-*
 15 *ments imposed by subsection (a). Application for exemption*
 16 *under this subsection shall be made in accordance with regu-*
 17 *lations prescribed by the Secretary or his delegate.*

18 *“(d) DETERMINATION OF AMOUNT PAID.—For pur-*
 19 *poses of this section, in determining the amount of any*
 20 *payment—*

21 *“(1) property (other than a qualified written notice*
 22 *of allocation) shall be taken into account at its fair*
 23 *market value, and*

1 “(2) a qualified written notice of allocation shall
2 be taken into account at its stated dollar amount.

3 “(e) *STATEMENTS TO BE FURNISHED TO PERSONS*
4 *WITH RESPECT TO WHOM INFORMATION IS FUR-*
5 *NISHED.*—Every cooperative making a return under subsec-
6 tion (a)(1) shall furnish to each person whose name is
7 set forth in such return a written statement showing—

8 “(1) the name and address of the cooperative mak-
9 ing such return, and

10 “(2) the aggregate amount of payments to the per-
11 son as shown on such return.

12 The written statement required under the preceding sentence
13 shall be furnished to the person on or before January 31 of
14 the year following the calendar year for which the return
15 under subsection (a)(1) was made. No statement shall be
16 required to be furnished to any person under this subsection
17 if the aggregate amount of payments to such person as
18 shown on the return made under subsection (a)(1) is less
19 than \$10.”

20 (c) *RETURNS REGARDING PAYMENT OF INTEREST.*—
21 Subpart B of part III of subchapter A of chapter 61 (relat-
22 ing to information returns) is amended by adding after sec-

tion 6047 (as added by section 7(f) of this Act) the following
new section:

“SEC. 6048. RETURNS REGARDING PAYMENTS OF INTEREST.

“(a) REQUIREMENT OF REPORTING.—

“(1) IN GENERAL.—Every person—

“(A) who makes payments of interest (as defined in subsection (b)) aggregating \$10 or more to any other person during any calendar year, or

“(B) who receives payments of interest as a nominee and who makes payments aggregating \$10 or more during any calendar year to any other person with respect to the interest so received.

shall make a return according to the forms or regulations prescribed by the Secretary or his delegate, setting forth the aggregate amount of such payments and the name and address of the person to whom paid.

“(2) RETURNS REQUIRED BY THE SECRETARY.—

Every person who makes payments of interest (as defined in subsection (b)) aggregating less than \$10 to any other person during any calendar year shall, when required by the Secretary or his delegate, make a return setting forth the aggregate amount of such payments and the name and address of the person to whom paid.

“(3) OTHER RETURNS REQUIRED BY SECRE-

TARY.—Every corporation making payments, regardless of amounts, of interest other than interest as defined in subsection (b) shall, when required by regulations prescribed by the Secretary or his delegate, make a return according to the forms or regulations prescribed by the Secretary or his delegate, setting forth the amount paid and the name and address of the recipient of each such payment.

“(b) *INTEREST DEFINED.*—

“(1) *GENERAL RULE.*—For purposes of subsections (a) (1) and (2), the term ‘interest’ means—

“(A) interest on evidences of indebtedness (including bonds, debentures, notes, and certificates) issued by a corporation in registered form, and, to the extent provided in regulations prescribed by the Secretary or his delegate, interest on other evidences of indebtedness issued by a corporation of a type offered by corporations to the public;

“(B) interest on deposits with persons carrying on the banking business;

“(C) amounts (whether or not designated as interest) paid by a mutual savings bank, savings and loan association, building and loan association, cooperative bank, homestead association, credit

1 union, or similar organization, in respect of de-
2 posits, investment certificates, or withdrawable or
3 repurchasable shares;

4 “(D) interest on amounts held by an insurance
5 company under an agreement to pay interest thereon;
6 and

7 “(E) interest on deposits with stockbrokers and
8 dealers in securities.

9 “(2) EXCEPTIONS.—For purposes of subsections
10 (a) (1) and (2), the term ‘interest’ does not include—

11 “(A) interest on obligations described in section
12 103(a) (1) or (3) (relating to interest on certain
13 governmental obligations);

14 “(B) to the extent provided in regulations pre-
15 scribed by the Secretary or his delegate, any amount
16 paid by or to a foreign corporation, a nonresident
17 alien, or a partnership not engaged in trade or
18 business in the United States and composed in whole
19 or in part of nonresident aliens; and

20 “(C) any amount on which the person making
21 payment is required to deduct and withhold a tax
22 under section 1451 (relating to tax-free covenant
23 bonds), or would be so required but for section
24 1451(d) (relating to benefit of personal exemp-
25 tions).

1 “(c) *STATEMENTS TO BE FURNISHED TO PERSONS*
2 *WITH RESPECT TO WHOM INFORMATION IS FUR-*
3 *NISHED.*—Every person making a return under subsection
4 (a)(1) shall furnish to each person whose name is set forth
5 in such return a written statement showing—

6 “(1) the name and address of the person making
7 such return, and

8 “(2) the aggregate amount of payments to the per-
9 son as shown on such return.

10 The written statement required under the preceding sentence
11 shall be furnished to the person on or before January 31
12 of the year following the calendar year for which the return
13 under subsection (a)(1) was made. No statement shall be
14 required to be furnished to any person under this subsection
15 if the aggregate amount of payments to such person as shown
16 on the return made under subsection (a)(1) is less than \$10.”

17 (d) *PENALTIES FOR FAILURE TO FILE INFORMATION*
18 *RETURNS.*—Section 6652 (relating to failure to file certain
19 information returns) is amended to read as follows:

20 “SEC. 6652. *FAILURE TO FILE CERTAIN INFORMATION RE-*
21 *URNS.*

22 “(a) *RETURNS RELATING TO PAYMENTS OF DIVI-*
23 *DENDS, INTEREST, AND PATRONAGE DIVIDENDS.*—In the
24 case of each failure to file a statement of the aggregate
25 amount of payments to another person required by section

1 6042(a)(1) (relating to payments of dividends aggregating
2 \$10 or more), section 6044(a)(1) (relating to payments of
3 patronage dividends aggregating \$10 or more), or section
4 6048(a)(1) (relating to payments of interest aggregating
5 \$10 or more), on the date prescribed therefor (determined
6 with regard to any extension of time for filing), unless it is
7 shown that such failure is due to reasonable cause and not to
8 willful neglect, there shall be paid (upon notice and demand
9 by the Secretary or his delegate and in the same manner as
10 tax), by the person failing to so file the statement, \$10 for
11 each such statement not so filed, but the total amount imposed
12 on the delinquent person for all such failures during any
13 calendar year shall not exceed \$25,000.

14 “(b) *OTHER RETURNS.*—In the case of each failure to
15 file a statement of a payment to another person required un-
16 der authority of section 6041 (relating to certain information
17 at source), section 6042(a)(2) (relating to payments of
18 dividends aggregating less than \$10), section 6044(a)(2)
19 (relating to payments of patronage dividends aggregating
20 less than \$10), section 6048(a)(2) (relating to payments
21 of interest aggregating less than \$10), section 6048(a)(3)
22 (relating to other payments of interest by corporations),
23 or section 6051(d) (relating to information returns with
24 respect to income tax withheld), on the date prescribed there-
25 for (determined with regard to any extension of time for

1 filing), unless it is shown that such failure is due to reason-
 2 able cause and not to willful neglect, there shall be paid
 3 (upon notice and demand by the Secretary or his delegate
 4 and in the same manner as tax) by the person failing to so
 5 file the statement, \$1 for each such statement not so filed,
 6 but the total amount imposed on the delinquent person for
 7 all such failures during the calendar year shall not exceed
 8 \$1,000.

9 “(c) ALCOHOL AND TOBACCO TAXES.—

“For penalties for failure to file certain information re-
 turns with respect to alcohol and tobacco taxes, see,
 generally, subtitle E.”

10 (e) PENALTIES FOR FAILURE TO FURNISH STATE-
 11 MENTS TO PERSONS WITH RESPECT TO WHOM RETURNS
 12 ARE FILED.—Subchapter B of chapter 68 (relating to
 13 assessable penalties) is amended by adding after section 6677
 14 (as added by section 7(g) of this Act) the following new
 15 section:

16 “SEC. 6678. FAILURE TO FURNISH CERTAIN STATEMENTS.

17 “In the case of each failure to furnish a statement under
 18 section 6042(c), 6044(e), or 6048(c) on the date prescribed
 19 therefor to a person with respect to whom a return has been
 20 made under section 6042(a)(1), 6044(a)(1), or 6048(a)
 21 (1), respectively, unless it is shown that such failure is due to
 22 reasonable cause and not to willful neglect, there shall be

1 paid (upon notice and demand by the Secretary or his dele-
 2 gate and in the same manner as tax), by the person failing to
 3 so furnish the statement, \$10 for each such statement not so
 4 furnished, but the total amount imposed on the delinquent
 5 person for all such failures during any calendar year shall
 6 not exceed \$25,000."

7 (f) *TECHNICAL AMENDMENTS*.—Section 6041 (relat-
 8 ing to information at source) is amended—

9 (1) by striking out, in subsection (a) thereof,
 10 "(other than payments described in section 6042(1) or
 11 section 6045)" and inserting in lieu thereof "(other than
 12 payments to which section 6042(a)(1), 6044(a)(1),
 13 or 6048(a)(1) applies, and other than payments with
 14 respect to which a statement is required under the au-
 15 thority of section 6042(a)(2), 6044(a)(2), 6045,
 16 6048(a)(2), or 6048(a)(3))"; and

17 (2) by striking out subsection (c) thereof.

18 (g) *CLERICAL AMENDMENTS*.—

19 (1) The table of sections for subpart B of part III
 20 of subchapter A of chapter 61 is amended—

21 (A) by striking out

"Sec. 6042. Returns regarding corporate dividends, earn-
 ings, and profits."

22 and inserting in lieu thereof

"Sec. 6042. Returns regarding payments of dividends and
 corporate earnings and profits.";

1 (B) by striking out

"Sec. 6044. Returns regarding patronage dividends."

2 and inserting in lieu thereof

"Sec. 6044. Returns regarding payments of patronage dividends.";

3 and

4 (C) by adding at the end of such table the
5 following:

"Sec. 6048. Returns regarding payments of interest."

6 (2) The table of sections for subchapter B of chap-
7 ter 68 is amended by adding at the end thereof the fol-
8 lowing:

"Sec. 6678. Failure to furnish certain statements."

9 (h) EFFECTIVE DATES.—

10 (1) DIVIDENDS AND INTEREST.—The amendments
11 made by this section shall apply to payments of dividends
12 and interest made on or after January 1, 1963.

13 (2) PATRONAGE DIVIDENDS.—The amendments
14 made by this section shall apply to payments of amounts
15 described in section 6044(b) of the Internal Revenue
16 Code of 1954 made on or after January 1, 1963,
17 with respect to patronage occurring on or after the first
18 day of the first taxable year of the cooperative beginning
19 on or after January 1, 1963.

1 SEC. 20. INFORMATION WITH RESPECT TO CERTAIN
2 FOREIGN ENTITIES.

3 (a) INFORMATION TO BE FURNISHED BY INDIVID-
4 UALS, DOMESTIC CORPORATIONS, ETC., WITH RESPECT
5 TO CERTAIN FOREIGN CORPORATIONS.—Section 6038 is
6 amended to read as follows:

7 “SEC. 6038. INFORMATION WITH RESPECT TO CERTAIN
8 FOREIGN CORPORATIONS.

9 “(a) REQUIREMENT.—

10 “(1) IN GENERAL.—Every United States person
11 shall furnish, with respect to any foreign corporation
12 which such person controls (within the meaning of
13 subsection (d) (1)), such information as the Secretary
14 or his delegate may prescribe by regulations relating to—

15 “(A) the name, the principal place of busi-
16 ness, and the nature of business of such foreign
17 corporation, and the country under whose laws
18 incorporated;

19 “(B) the accumulated profits (as defined in
20 section 902 (c)) of such foreign corporation, in-
21 cluding the items of income (whether or not in-
22 cluded in gross income under chapter 1) , deductions
23 (whether or not allowed in computing taxable in-
24 come under chapter 1) , and any other items taken
25 into account in computing such accumulated profits;

1 “(C) a balance sheet for such foreign corpora-
2 tion listing assets, liabilities, and capital;

3 “(D) transactions between such foreign cor-
4 poration and—

5 “(i) such person,

6 “(ii) any other corporation which such
7 person controls, and

8 “(iii) any United States person owning,
9 at the time the transaction takes place, 10 per-
10 cent or more of the value of any class of stock
11 outstanding of such foreign corporation; and

12 “(E) a description of the various classes of
13 stock outstanding, and a list showing the name and
14 address of, and number of shares held by, each
15 United States person who is a shareholder of record
16 owning at any time during the annual accounting
17 period 5 percent or more in value of any class of
18 stock outstanding of such foreign corporation.

19 The Secretary or his delegate may also require the fur-
20 nishing of any other information which is similar or
21 related in nature to that specified in the preceding
22 sentence.

23 “(2) PERIOD FOR WHICH INFORMATION IS TO BE
24 FURNISHED, ETC.—The information required under para-
25 graph (1) shall be furnished for the annual accounting

1 period of the foreign corporation ending with or within
2 the United States person's taxable year. The informa-
3 tion so required shall be furnished at such time and in
4 such manner as the Secretary or his delegate shall by
5 regulations prescribe.

6 “(3) LIMITATION.—No information shall be re-
7 quired to be furnished under this subsection with respect
8 to any foreign corporation for any annual accounting
9 period unless such information was required to be fur-
10 nished under regulations in effect on the first day of such
11 annual accounting period.

12 “(b) EFFECT OF FAILURE TO FURNISH INFORMA-
13 TION.—

14 “(1) IN GENERAL.—If a United States person fails
15 to furnish, within the time prescribed under paragraph
16 (2) of subsection (a), any information with respect to
17 any foreign corporation required under paragraph (1)
18 of subsection (a), then—

19 “(A) in applying section 901 (relating to
20 taxes of foreign countries and possessions of the
21 United States) to such United States person for the
22 taxable year, the amount of taxes (other than taxes
23 reduced under subparagraph (B)) paid or deemed
24 paid (other than those deemed paid under section
25 904(d)) to any foreign country or possession of the

United States for the taxable year shall be reduced by 10 percent, and

“(B) in applying sections 902 (relating to foreign tax credit for corporate stockholder in foreign corporation) and ~~(174)~~⁹⁵⁷ 960 (relating to special rules for foreign tax credit) to any such United States person which is a corporation (or to any person who acquires from any other person any portion of the interest of such other person in any such foreign corporation, but only to the extent of such portion) for any taxable year, the amount of taxes paid or deemed paid by each foreign corporation with respect to which such person is required to furnish information during the annual accounting period or periods with respect to which such information is required under paragraph (2) of subsection (a) shall be reduced by 10 percent.

If such failure continues 90 days or more after notice by the Secretary or his delegate to the United States person, then the amount of the reduction under this ~~(175) subsection~~ paragraph shall be 10 percent plus an additional 5 percent for each 3-month period, or fraction thereof, during which such failure to furnish information continues after the expiration of such 90-day period.

~~(176)~~“(2) *LIMITATION.*—*The amount of the reduction*

1 *under paragraph (1) for each failure to furnish infor-*
 2 *mation with respect to a foreign corporation required*
 3 *under subsection (a)(1) shall not exceed whichever of*
 4 *the following amounts is the greater:*

5 “(A) \$10,000, or

6 “(B) the income of the foreign corporation for
 7 *its annual accounting period with respect to which*
 8 *the failure occurs.*

9 **(177)**~~“(2)~~ “(3) SPECIAL RULES.—

10 “(A) No taxes shall be reduced under this sub-
 11 section more than once for the same failure.

12 “(B) For purposes of this subsection, the time
 13 prescribed under paragraph (2) of subsection (a)
 14 to furnish information (and the beginning of the
 15 90-day period after notice by the Secretary) shall
 16 be treated as being not earlier than the last day on
 17 which (as shown to the satisfaction of the Secretary
 18 or his delegate) reasonable cause existed for failure
 19 to furnish such information.

20 “(C) In applying subsections (a) and (b) of
 21 section 902, and in applying subsection (a) of sec-
 22 tion **(178)**~~956~~ 960, the reduction provided by this
 23 subsection shall not apply for purposes of determin-
 24 ing the amount of accumulated profits in excess of
 25 income, war profits, and excess profits taxes.

1 “(c) TWO OR MORE PERSONS REQUIRED TO FURNISH
2 INFORMATION WITH RESPECT TO SAME FOREIGN COR-
3 PORATION.—Where, but for this subsection, two or more
4 United States persons would be required to furnish informa-
5 tion under subsection (a) with respect to the same foreign
6 corporation for the same period, the Secretary or his dele-
7 gate may by regulations provide that such information shall
8 be required only from one person. To the extent practicable,
9 the determination of which person shall furnish the informa-
10 tion shall be made on the basis of actual ownership of stock.

11 “(d) DEFINITIONS.—For purposes of this section—

12 “(1) CONTROL.—A person is in control of a cor-
13 poration if such person owns stock possessing more than
14 50 percent of the total combined voting power of all
15 classes of stock entitled to vote, or more than 50 per-
16 cent of the total value of shares of all classes of stock,
17 of a corporation. If a person is in control (within the
18 meaning of the preceding sentence) of a corporation
19 which in turn owns more than 50 percent of the total
20 combined voting power of all classes of stock entitled to
21 vote of another corporation, or owns more than 50 per-
22 cent of the total value of the shares of all classes of stock
23 of another corporation, then such person shall be
24 treated as in control of such other corporation. For
25 purposes of this paragraph, the rules prescribed by

1 section 318(a) for determining ownership of stock
 2 shall apply; ~~(179)~~except that clause ~~(i)~~ of section 318
 3 ~~(a)(2)(C)~~ shall be applied without regard to the 50
 4 percent limitation contained in such section: *except that—*

5 “(A) the second sentence of subparagraphs
 6 (A) and (B), and clause (ii) of subparagraph
 7 (C), of section 318(a)(2) shall not be applied so
 8 as to consider a United States person as owning
 9 stock which is owned by a person who is not a United
 10 States person, and

11 “(B) in applying clause (i) of subparagraph
 12 (C) of section 318(a)(2), the phrase ‘10 percent’
 13 shall be substituted for the phrase ‘50 percent’ used
 14 in subparagraph (C).

15 “(2) ANNUAL ACCOUNTING PERIOD.—The annual
 16 accounting period of a foreign corporation is the annual
 17 period on the basis of which such corporation regularly
 18 computes its income in keeping its books.

19 “(e) CROSS REFERENCES.—

“(1) For provisions relating to penalties for violations
 of this section, see section 7203.

“(2) For definition of the term ‘United States person’.
 see section 7701(a)(30).”

20 (b) INFORMATION AS TO ORGANIZATION OR REOR-
 21 GANIZATION OF FOREIGN CORPORATIONS AND AS TO AC-
 22 QUISSIONS OF THEIR STOCK.—Section 6046 (relating to

1 returns as to creation or organization, or reorganization, of
 2 foreign corporations) is amended to read as follows:

3 **“SEC. 6046. RETURNS AS TO ORGANIZATION OR REORGAN-**
 4 **IZATION OF FOREIGN CORPORATIONS AND**
 5 **AS TO ACQUISITIONS OF THEIR STOCK.**

6 “(a) REQUIREMENT OF RETURN.—A return comply-
 7 ing with the requirements of subsection (b) shall be made
 8 by—

9 “(1) each United States citizen or resident who
 10 is ~~(180)an officer or director of a foreign corporation on~~
 11 ~~January 1, 1963~~ *on January 1, 1963 an officer or*
 12 *director of a foreign corporation, 5 percent or more in*
 13 *value of the stock of which is owned by a United States*
 14 *person, or who becomes such an officer or director at*
 15 *any time after such date,*

16 “(2) each United States person who on January
 17 1, 1963, owns 5 percent or more in value of the stock
 18 of a foreign corporation, or who, at any time after such
 19 date—

20 “(A) acquires stock which, when added to any
 21 stock owned on January 1, 1963, has a value equal
 22 to 5 percent or more of the value of the stock of a
 23 foreign corporation, or

24 “(B) acquires an additional 5 percent or more

1 in value of the stock of a foreign corporation, and
 2 “(3) each person who at any time after January 1,
 3 1963, becomes a United States person while owning
 4 5 percent or more in value of the stock of a foreign
 5 corporation.

6 “(b) FORM AND CONTENTS OF RETURNS.—The re-
 7 turns required by subsection (a) shall be in such form and
 8 shall set forth, in respect of the foreign corporation, such
 9 information as the Secretary or his delegate prescribes by
 10 forms or regulations as necessary for carrying out the pro-
 11 visions of the income tax laws(181), *except that in the case*
 12 *of persons described only in subsection (a) (1) the information*
 13 *required shall be limited to the names and addresses of persons*
 14 *described in subsection (a) (2).*

15 “(c) OWNERSHIP OF STOCK.—For purposes of subsec-
 16 tion (a) (182)(2) and (3), stock owned directly or indi-
 17 rectly by a person (including, in the case of an individual,
 18 stock owned by members of his family) shall be taken into
 19 account. For purposes of the preceding sentence, the family
 20 of an individual shall be considered as including only his
 21 brothers and sisters (whether by the whole or half blood),
 22 spouse, ancestors, and lineal descendants.

23 “(d) TIME FOR FILING.—Any return required by sub-

1 section (a) shall be filed on or before the 90th day after
 2 the day on which, under any provision of subsection (a), the
 3 United States citizen, resident, or person becomes liable to
 4 file such return.

5 **(183)**“(e) *LIMITATION.*—No information shall be required
 6 to be furnished under this section with respect to any foreign
 7 corporation unless such information was required to be fur-
 8 nished under regulations which, on the date on which the
 9 United States citizen, resident, or person becomes liable to
 10 file a return required under subsection (a)—

11 “(1) if such liability arises on or after January 1,
 12 1963, and before March 1, 1963, have been in effect
 13 since January 1, 1963 (but only if such regulations
 14 were prescribed before December 1, 1962), or

15 “(2) if such liability arises on or after March 1,
 16 1963, have been in effect for at least 90 days.

17 **(184)**“(e) “(f) *CROSS REFERENCE.*—

“For provisions relating to penalties for violations
 of this section, see sections **(185)**6678 6679 and 7203.”

18 (c) *CIVIL PENALTY FOR FAILURE TO FILE RETURN.*—
 19 Subchapter B of chapter 68 (relating to assessable penal-
 20 ties) is amended by adding **(186)**at the end thereof after

1 *section 6678 (as added by section 19(e) of this Act) the*
 2 *following new section:*

3 **“SEC. (187)~~6678~~ 6679. FAILURE TO FILE RETURNS AS TO**
 4 **ORGANIZATION OR REORGANIZA-**
 5 **TION OF FOREIGN CORPORATIONS**
 6 **AND AS TO ACQUISITIONS OF**
 7 **THEIR STOCK.**

8 “(a) **CIVIL PENALTY.**—In addition to any criminal
 9 penalty provided by law, any person required to file a return
 10 under section 6046 who fails to file such return at the time
 11 provided in such section, or who files a return which does
 12 not show the information required pursuant to such section,
 13 shall pay a penalty of \$1,000, unless it is shown that such
 14 failure is due to reasonable cause.

15 “(b) **DEFICIENCY PROCEDURES NOT TO APPLY.**—Sub-
 16 chapter B of chapter 63 (relating to deficiency procedure
 17 for income, estate, and gift taxes) shall not apply in respect
 18 of the assessment or collection of any penalty imposed by
 19 subsection (a).”

20 (d) **TECHNICAL AMENDMENTS.**—

21 (1) Section 318(b) (relating to cross references)
 22 is amended by striking out “and” at the end of paragraph
 23 (5), by striking out the period at the end of paragraph
 24 (6) and inserting in lieu thereof “; and”, and by add-
 25 ing at the end thereof the following:

“**(7) section 6038(d)(2) (relating to information with
 respect to certain foreign corporations).**”

(2) The table of sections for subpart B of part III of subchapter A of chapter 61 is amended by striking out

“Sec. 6046. Returns as to creation or organization, or reorganization, of foreign corporations.”

and inserting in lieu thereof

“Sec. 6046. Returns as to organization or reorganization of foreign corporations and as to acquisitions of their stock.”

(3) The table of sections for subchapter B of chapter 68 is amended by adding at the end thereof the following:

“Sec. ~~(188) 6678~~ 6679. Failure to file returns as to organization or reorganization of foreign corporations and as to acquisitions of their stock.”

(e) EFFECTIVE DATE.—

(1) The amendments made by subsection (a) shall apply with respect to annual accounting periods of foreign corporations beginning after December 31, 1962.

(2) The amendments made by subsection (b) shall take effect on January 1, 1963.

(189) SEC. 21. EXPENDITURES BY FARMERS FOR CLEARING LAND.

(a) ALLOWANCE OF DEDUCTION.—Part VI of subchapter B of chapter 1 (relating to itemized deductions for individuals and corporations) is amended by adding after

1 section 181 (as added by section 2(c) of this Act) the
2 following new section:

3 “SEC. 182. EXPENDITURES BY FARMERS FOR CLEARING LAND.

4 “(a) *IN GENERAL.*—A taxpayer engaged in the busi-
5 ness of farming may elect to treat expenditures which are
6 paid or incurred by him during the taxable year in the clear-
7 ing of land for the purpose of making such land suitable
8 for use in farming as expenses which are not chargeable to
9 capital account. The expenditures so treated shall be allowed
10 as a deduction.

11 “(b) *LIMITATION.*—The amount deductible under sub-
12 section (a) for any taxable year shall not exceed whichever
13 of the following amounts is the lesser:

14 “(1) \$5,000, or

15 “(2) 25 percent of the taxable income derived from
16 farming during the taxable year.

17 For purposes of paragraph (2), the term ‘taxable income
18 derived from farming’ means the gross income derived from
19 farming reduced by the deductions allowed by this chapter
20 (other than by this section) which are attributable to the
21 business of farming.

22 “(c) *DEFINITIONS.*—For purposes of subsection (a)—

23 “(1) The term ‘clearing of land’ includes (but is
24 not limited to) the eradication of trees, stumps, and brush,

1 *the treatment or moving of earth, and the diversion of*
 2 *streams and watercourses.*

3 “(2) *The term ‘land suitable for use in farming’*
 4 *means land which as a result of the activities described*
 5 *in paragraph (1) is suitable for use by the taxpayer or*
 6 *his tenant for the production of crops, fruits, or other*
 7 *agricultural products or for the sustenance of livestock.*

8 “(d) *EXCEPTIONS, ETC.—*

9 “(1) *EXCEPTIONS.—The expenditures to which*
 10 *subsection (a) applies shall not include—*

11 “(A) *the purchase, construction, installation,*
 12 *or improvement of structures, appliances, or facili-*
 13 *ties which are of a character which is subject to the*
 14 *allowance for depreciation provided in section 167,*
 15 *or*

16 “(B) *any amount paid or incurred which is*
 17 *allowable as a deduction without regard to this*
 18 *section.*

19 “(2) *CERTAIN PROPERTY USED IN THE CLEARING*
 20 *OF LAND.—*

21 “(A) *ALLOWANCE FOR DEPRECIATION.—The*
 22 *expenditures to which subsection (a) applies shall*
 23 *include a reasonable allowance for depreciation with*
 24 *respect to property of the taxpayer which is used in*
 25 *the clearing of land for the purpose of making such*

1 *land suitable for use in farming and which, if used*
 2 *in a trade or business, would be property subject*
 3 *to the allowance for depreciation provided by sec-*
 4 *tion 167.*

5 “(B) *TREATMENT AS DEPRECIATION DEDUC-*
 6 *TION.—For purposes of this chapter, any expendi-*
 7 *ture described in subparagraph (A) shall, to the*
 8 *extent allowed as a deduction under subsection (a),*
 9 *be treated as an amount allowed under section 167*
 10 *for exhaustion, wear and tear, or obsolescence of the*
 11 *property which is used in the clearing of land.*

12 “(e) *ELECTION.—The election under subsection (a) for*
 13 *any taxable year shall be made within the time prescribed*
 14 *by law (including extensions thereof) for filing the return*
 15 *for such taxable year. Such election shall be made in such*
 16 *manner as the Secretary or his delegate may by regulations*
 17 *prescribe. Such election may not be revoked except with*
 18 *the consent of the Secretary or his delegate.”*

19 “(b) *CLERICAL AMENDMENT.—The table of sections*
 20 *for such part VI is amended by adding at the end thereof*
 21 *the following:*

 “*Sec. 182. Expenditures by farmers for clearing land.*”

22 “(c) *EFFECTIVE DATE.—The amendments made by this*
 23 *section shall apply with respect to taxable years beginning*
 24 *after December 31, 1962.*

1 (190)SEC. 22. CHARITABLE CONTRIBUTIONS MADE FROM IN-
2 COME ATTRIBUTABLE TO SEVERAL TAXABLE
3 YEARS.

4 (a) TREATMENT FOR PURPOSES OF PART I OF SUB-
5 CHAPTER Q.—Section 1307 (relating to rules applicable to
6 part I of subchapter Q) is amended by adding at the end
7 thereof the following new subsection:

8 “(e) ELECTION WITH RESPECT TO CHARITABLE
9 CONTRIBUTIONS.—In the case of an individual who elects
10 (in such manner and at such time as the Secretary or his
11 delegate prescribes by regulations) to have the provisions of
12 this subsection apply, an amount received or accrued to which
13 this part applies shall be reduced, for purposes of computing
14 the tax liability of the taxpayer under this part with respect
15 to the amount so received or accrued, by an amount equal to
16 that portion of (1) the amount of charitable contributions
17 made by the taxpayer during the taxable year in which the
18 amount is so received or accrued which are allowable as a
19 deduction for such year under section 170 (determined with-
20 out regard to this part), as (2) the amount received or ac-
21 crued to which this part applies is of the adjusted gross income
22 for the taxable year (determined without regard to this part).
23 In any case in which the taxpayer elects to have the pro-
24 visions of this subsection apply, no portion of the amount to
25 which this part applies shall, for purposes of computing

1 the limitation on tax under this part, be taken into account
 2 for purposes of computing the limitation under section
 3 170(b)(1) for the taxable year in which the amount to
 4 which this part applies is received or accrued.”

5 (b) *EFFECTIVE DATE.*—The amendment made by sub-
 6 section (a) shall apply with respect to amounts received or
 7 accrued in taxable years beginning after December 31, 1961.

8 (191)SEC. 23. *EFFECTIVE DATE OF SECTION 1371(c) OF THE*
 9 *INTERNAL REVENUE CODE OF 1954.*

10 (a) *IN GENERAL.*—Subject to the provisions of subsec-
 11 tion (b), section 1371(c) of the Internal Revenue Code of
 12 1954 (as added by section 2(a) of the Act entitled “An Act
 13 to amend the Internal Revenue Code of 1954 to provide a
 14 personal exemption for children placed for adoption and to
 15 clarify certain provisions relating to the election of small busi-
 16 ness corporations as to taxable status”, approved September
 17 23, 1959 (Public Law 86-376)), shall (notwithstanding
 18 the provisions of the first sentence of section 2(d) of such
 19 Act) also apply to taxable years beginning after December
 20 31, 1957, and before January 1, 1960.

21 (b) *ELECTION AND CONSENT BY CORPORATIONS;*
 22 *CONSENTS BY SHAREHOLDERS.*—Subsection (a) shall apply
 23 with respect to any corporation and its shareholders only if,
 24 within one year after the date of the enactment of this Act—
 25 (1) such corporation (in such manner as the Secre-

1 *tary of the Treasury or his delegate prescribes by regula-*
2 *tions) elects to have the provisions of subsection (a) apply*
3 *and consents to the application of subsection (c); and*

4 *(2) each person who is a shareholder of such cor-*
5 *poration on the date on which such corporation makes*
6 *such election, and each person who was a shareholder of*
7 *such corporation during any taxable year of such cor-*
8 *poration beginning after December 31, 1957, and ending*
9 *before the date of such election, consents (in such manner*
10 *and at such time as the Secretary of the Treasury or*
11 *his delegate prescribes by regulations) to such election*
12 *and to the application of subsection (c).*

13 *(c) TOLLING OF STATUTES OF LIMITATIONS.—In any*
14 *case in which a corporation makes an election under sub-*
15 *section (b)—*

16 *(1) if the assessment of any deficiency against the*
17 *corporation making such election, or any shareholder*
18 *of such corporation who consents to such election, for*
19 *any taxable year is prevented, at any time on or before*
20 *the expiration of one year after the date of such election,*
21 *by the operation of any law or rule of law, assessment*
22 *of such deficiency may, nevertheless, be made, to the*
23 *extent such deficiency is attributable to the application*
24 *of subsection (a), at any time on or before the expiration*
25 *of such one-year period; and*

1 (2) if credit or refund of any overpayment of tax
2 by the corporation making such election, or any share-
3 holder of such corporation who consents to such election,
4 for any taxable year is prevented, at any time on or
5 before the expiration of one year after the date of such
6 election, by the operation of any law or rule of law,
7 credit or refund of such overpayment may, nevertheless,
8 be allowed or made, to the extent such overpayment is
9 attributable to the application of subsection (a), if claim
10 therefor is filed on or before the expiration of such
11 one-year period.

12 **(192) SEC. 24. CERTAIN LOSSES SUSTAINED IN CONVERTING**
13 **FROM STREET RAILWAY TO BUS OPERATIONS.**

14 (a) *IN GENERAL.*—If a corporation has a net operating
15 loss for the taxable year ending December 31, 1953, or the
16 taxable year ending December 31, 1954, principally as the
17 result of conversion from street railways to bus operations
18 with respect to part or all of the company's operations, then
19 its unused conversion loss will be subject to the treatment
20 provided in subsection (c).

21 (b) *UNUSED CONVERSION LOSS DEFINED.*—The
22 amount of the unused conversion loss shall be the aggregate
23 of the net operating losses for years described in subsection
24 (a) reduced to the extent that they have been used as net oper-

1 *ating loss carryovers or carrybacks to reduce taxable income*
 2 *for any taxable year beginning before January 1, 1960.*

3 *(c) TREATMENT OF UNUSED CONVERSION LOSS.—If*
 4 *a taxpayer has an unused conversion loss, then in determin-*
 5 *ing the amount of the net operating loss carryover from the*
 6 *taxable year ending December 31, 1959, to each of the 5 tax-*
 7 *able years following such taxable year for purposes of sec-*
 8 *tion 172 of the Internal Revenue Code of 1954, such unused*
 9 *conversion loss shall be treated as a net operating loss for the*
 10 *taxable year ending December 31, 1959. This subsection*
 11 *shall apply only for years in which the taxpayer is engaged*
 12 *in the furnishing or sale of transportation (as defined in*
 13 *section 1503(c)(1)(A) of the Internal Revenue Code of*
 14 *1954).*

15 *(d) REGULATIONS.—The Secretary of the Treasury, or*
 16 *his delegate, may prescribe by regulation such rules as may*
 17 *be necessary to carry out the purposes of this section.*

18 **(193) SEC. 25. PENSION PLAN OF LOCAL UNION NUMBERED 435,**
 19 **INTERNATIONAL HOD CARRIERS' BUILDING**
 20 **AND COMMON LABORERS' UNION OF AMERICA.**

21 *The pension plan of Local Union Numbered 435 of the*
 22 *International Hod Carriers' Building and Common*
 23 *Laborers' Union of America, which was negotiated to take*
 24 *effect May 1, 1960, pursuant to an agreement between such*

1 union and the Building Trades Employers Association of
 2 Rochester, New York, Incorporated, and which has been
 3 held by the Internal Revenue Service to constitute a qualified
 4 trust under section 401(a) of the Internal Revenue Code
 5 of 1954, and to be exempt from taxation under section
 6 501(a) of such Code, shall be held and considered to have
 7 been a qualified trust under such section 401(a), and to have
 8 been exempt from taxation under such section 501(a), for the
 9 period beginning May 1, 1960, and ending April 20, 1961,
 10 but only if it is shown to the satisfaction of the Secretary
 11 of the Treasury or his delegate that the trust has not in this
 12 period been operated in a manner which would jeopardize
 13 the interests of its beneficiaries.

14 **(194)SEC. 26. CONTINUATION OF A PARTNERSHIP YEAR FOR**
 15 **SURVIVING PARTNER IN A TWO-MAN PARTNER-**
 16 **SHIP WHERE ONE DIES.**

17 (a) **CLOSE OF TAXABLE YEAR OF TWO-MAN PART-**
 18 **NERSHIP WHEN ONE PARTNER DIES.**—Section 188 of
 19 the Internal Revenue Code of 1939 (relating to different
 20 taxable years of partner and partnership) is amended—
 21 (1) by striking out “If” and inserting in lieu
 22 thereof “(a) **GENERAL RULE.**—If”; and

1 (2) by adding at the end of such section 188 the
2 following new subsection:

3 “(b) *TWO-MAN PARTNERSHIP.*—For the purpose of
4 this chapter, the death of one of the partners of a partnership
5 consisting of two members shall not, if the surviving partner
6 so elects within one year after the date of enactment of this
7 subsection, result in the termination of the partnership or
8 in the closing of the taxable year of the partnership with
9 respect to the surviving partner prior to the time the partner-
10 ship year would have closed if neither partner had died or
11 disposed of his interest.”

12 (b) *EFFECTIVE DATE, ETC.*—The amendments made by
13 subsection (a) shall apply with respect to taxable years of a
14 partnership beginning after December 31, 1946, to which
15 the Internal Revenue Code of 1939 applies. If refund or
16 credit of any overpayment resulting from the application of
17 the amendments made by subsection (a) of this section (includ-
18 ing interest, additions to the tax, and additional amounts),
19 is prevented on the date of enactment of this Act, or within
20 one year from such date, by the operation of any law or rule
21 of law (other than section 3760 of the Internal Revenue Code
22 of 1939 or section 7121 of the Internal Revenue Code of

1 1954, relating to closing agreements, and other than section
 2 3761 of the Internal Revenue Code of 1939 or section 7122
 3 of the Internal Revenue Code of 1954, relating to compro-
 4 mises), such refund or credit of such overpayment, may,
 5 nevertheless, be made or allowed if claim therefor is filed
 6 within one year after the date of the enactment of this Act.
 7 No interest shall be allowed or paid on any overpayment
 8 resulting from the enactment of this section.

9 **(195)SEC. 27. EXCLUSION FROM GROSS INCOME OF CERTAIN**
 10 **AWARDS MADE PURSUANT TO EVACUATION**
 11 **CLAIMS OF AMERICAN-JAPANESE INDIVIDUALS.**

12 (a) *IN GENERAL.*—No amount received as an award
 13 under the Act entitled “An Act to authorize the Attorney
 14 General to adjudicate certain claims resulting from evacua-
 15 tion of certain persons of Japanese ancestry under military
 16 orders”, approved July 2, 1948, as amended by Public Law
 17 116, Eighty-second Congress, and Public Law 673, Eighty-
 18 fourth Congress (50 U.S.C. App., secs. 1981–1987), shall
 19 be included in gross income for purposes of chapter 1 of the
 20 Internal Revenue Code of 1939 or chapter 1 of the Internal
 21 Revenue Code of 1954.

22 (b) *EFFECTIVE DATE, ETC.*—Subsection (a) shall
 23 apply with respect to taxable years ending after July 2,

1 1948. If refund or credit of any overpayment of Federal
 2 income tax resulting from the application of subsection (a)
 3 (including interest, additions to the tax, additional amounts,
 4 and penalties) is prevented on the date of the enactment of
 5 this Act, or within one year from such date, by the opera-
 6 tion of any law or rule of law, the refund or credit of such
 7 overpayment may nevertheless be made or allowed if claim
 8 therefor is filed within one year after the date of enactment of
 9 this Act. In the case of a claim to which the preceding
 10 sentence applies, the amount to be refunded or credited as
 11 an overpayment shall not be diminished by any credit or
 12 setoff based upon any item other than the amount of the
 13 award referred to in subsection (a). No interest shall be
 14 allowed or paid on any overpayment resulting from the
 15 application of this section.

16 **(196)SEC. 28. DEDUCTION FOR DEPRECIATION BY TENANT-**
 17 **STOCKHOLDER OF COOPERATIVE HOUSING**
 18 **CORPORATION.**

19 (a) *ALLOWANCE OF DEDUCTION.*—Section 216 (relat-
 20 ing to deductions by tenant-stockholders of a cooperative
 21 housing corporation) is amended by—

1 (1) amending the heading thereof to read as fol-
2 lows:

3 “SEC. 216. DEDUCTION OF TAXES, INTEREST, AND DEPRECIA-
4 TION BY COOPERATIVE HOUSING CORPORATION
5 TENANT-STOCKHOLDER.”; and

6 (2) adding at the end of section 216 the following
7 new subsection:

8 “(c) *TREATMENT AS PROPERTY SUBJECT TO DEPRE-*
9 *CIATION.*—So much of the stock of a tenant-stockholder in a
10 cooperative housing corporation as is allocable, under regula-
11 tions prescribed by the Secretary or his delegate, to a pro-
12 prietary lease or right of tenancy in property subject to the
13 allowance for depreciation under section 167(a) shall, to the
14 extent such proprietary lease or right of tenancy is used by
15 such tenant-stockholder in a trade or business or for the pro-
16 duction of income, be treated as property subject to the allow-
17 ance for depreciation under section 167(a).”

18 (b) *EFFECTIVE DATE.*—The amendment made by sub-
19 section (a) shall be effective with respect to taxable years
20 beginning after December 31, 1961.

1 **(197)SEC. 29. EXCLUSION FROM GROSS INCOME OF GAIN FROM**
2 **SALE OF RESIDENCE BY INDIVIDUAL AGE 65 OR**
3 **OVER.**

4 *(a) EXCLUSION FROM GROSS INCOME.—Part III of*
5 *subchapter B of chapter 1 (relating to items specifically*
6 *excluded from gross income) is amended by renumbering*
7 *section 121 as 122, and by inserting after section 120 the*
8 *following new section:*

9 **“SEC. 121. GAIN FROM SALE OR EXCHANGE OF RESIDENCE OF**
10 **INDIVIDUAL WHO HAS ATTAINED AGE 65.**

11 *“(a) GENERAL RULE.—In the case of an individual,*
12 *gross income does not include gain from the sale or exchange*
13 *after December 31, 1962, of property used by the taxpayer*
14 *as his principal residence, if—*

15 *“(1) the taxpayer has attained the age of 65 years*
16 *before such sale or exchange occurs, and*

17 *“(2) such property has been used by the taxpayer*
18 *as his principal residence for a period of not less than*
19 *5 years at the time such sale or exchange occurs.*

20 *“(b) LIMITATION TO \$30,000.—The amount of gain*

1 *which is not recognized as the result of subsection (a) shall*
2 *not exceed the same proportion of such gain which \$30,000*
3 *is of the total sales price of such property.*

4 “(c) *PROPERTY HELD JOINTLY BY HUSBAND AND*
5 *WIFE.*—*In the case of property held by a husband and wife*
6 *as joint tenants or as tenants by the entirety, the age re-*
7 *quirement contained in subsection (a)(1) and the use re-*
8 *quirement contained in subsection (a)(2) shall be treated*
9 *as having been met by both the husband and the wife if it is*
10 *met by either spouse.*

11 “(d) *PROPERTY USED IN PART AS PRINCIPAL RESI-*
12 *DENCE.*—*In the case of property only a portion of which is*
13 *used by the taxpayer as his principal residence, subsection*
14 *(a) shall apply to so much of the gain from the sale or ex-*
15 *change of such property as is determined, under regulations*
16 *prescribed by the Secretary or his delegate, to be attributable*
17 *to the portion of the property used by the taxpayer as his*
18 *principal residence.*

19 “(e) *INVOLUNTARY CONVERSIONS.*—*For purposes of*
20 *subsection (a), the destruction, seizure, requisition, or con-*

1 demnation of property, occurring after December 31, 1962,
2 shall be treated as the sale or exchange of such property.”

3 (b) *TABLE OF CONTENTS.*—The table of sections for
4 such part is amended by striking out

“Sec. 121. Cross references to other Acts.

5 and inserting in lieu thereof

“Sec. 121. Gain from sale or exchange of residence of indi-
vidual who has attained age 65.

“Sec. 122. Cross references to other Acts.”

6 (c) *TECHNICAL AMENDMENTS.*—(1) Section 1033(h)
7 (relating to involuntary conversions) is amended by adding
8 at the end thereof the following new paragraph:

“(3) For exclusion from gross income of gain from in-
voluntary conversion occurring after December 31, 1962,
of residence of taxpayer who has attained aged 65, see
section 121.”

9 (2) Section 1034 (relating to sale or exchange of resi-
10 dence) is amended by adding at the end thereof the following
11 new subsection:

12 “(k) *CROSS REFERENCE.*—

“For exclusion from gross income of gain from sale
or exchange after December 31, 1962, of residence of tax-
payer who has attained age 65, see section 121.”

1 (d) *EFFECTIVE DATE.*—*The amendments made by this*
 2 *section shall apply to taxable years beginning after Decem-*
 3 *ber 31, 1962.*

4 **(198)SEC. 30. DEDUCTION FOR INCOME TAX PURPOSES OF**
 5 **CONTRIBUTIONS TO CERTAIN ORGANIZATIONS**
 6 **FOR JUDICIAL REFORM.**

7 *For purposes of section 170 of the Internal Revenue*
 8 *Code of 1954 (relating to deduction for charitable, etc., con-*
 9 *tributions and gifts), a contribution or gift made after De-*
 10 *cember 31, 1961, with respect to a referendum occurring dur-*
 11 *ing the calendar year 1962 to or for the use of any nonprofit*
 12 *organization created and operated exclusively—*

13 (1) *to consider proposals for the reorganization*
 14 *of the judicial branch of the government of any State*
 15 *of the United States or political subdivision of such State,*
 16 *and*

17 (2) *to provide information, make recommendations,*
 18 *and seek public support or opposition as to such proposals,*
 19 *shall be treated as a charitable contribution if no part of the*
 20 *net earnings of such organization inures to the benefit of any*

1 *private shareholder or individual. The provisions of the*
2 *preceding sentence shall not apply to any organization which*
3 *participates in, or intervenes in, any political campaign on*
4 *behalf of any candidate for public office.*

5 **(199)SEC. 31. AMENDMENT TO TITLE I OF THE SOCIAL SECU-**
6 **RITY ACT RELATING TO STATEMENT OF**
7 **FINANCIAL STATUS OF CLAIMANTS FOR MEDI-**
8 **CAL ASSISTANCE FOR THE AGED.**

9 *Paragraph (11) of section 2(a) of the Social Security*
10 *Act is amended (1) by striking out “and” and at the end of*
11 *clause (D), (2) by striking out the period at the end of*
12 *clause (E) and inserting in lieu thereof “; and”, and (3) by*
13 *adding after clause (E) the following new clause:*

14 *“(F) may provide that any statement required*
15 *of a claimant for medical assistance for the aged, if*
16 *made in writing and signed by the claimant, shall,*
17 *insofar as such statement relates to the financial*
18 *status of such claimant, be presumed by such State*
19 *agency to be factually correct for purposes of deter-*
20 *mining his eligibility for such assistance.”*

1 **(200)SEC. 32. FOREIGN SUBSIDIARIES MANUFACTURING PROD-**
 2 **UCTS ABROAD FOR SALE IN THE UNITED**
 3 **STATES.**

4 *(a) Subpart B of part II of subchapter N of chapter*
 5 *1 (relating to foreign corporations) is amended by adding*
 6 *at the end thereof the following new section:*

7 **“SEC. 885. CERTAIN FOREIGN CORPORATIONS PRODUCING**
 8 **PRODUCTS FOR SALE IN THE UNITED STATES.**

9 *“(a) GENERAL RULE.—In the case of any foreign cor-*
 10 *poration to which this section applies for the taxable year—*

11 *“(1) for purposes of section 882(a), such foreign*
 12 *corporation shall be deemed to be engaged in trade or*
 13 *business within the United States, and*

14 *“(2) for purposes of this subtitle, the gross income*
 15 *of such corporation from sources within the United*
 16 *States shall be deemed to be not less than the gross in-*
 17 *come which it derives for such taxable year from the*
 18 *sale of competitive articles which are sold by it for ulti-*
 19 *mate use, consumption, or disposition in the United*
 20 *States.*

21 *“(b) CORPORATIONS TO WHICH SECTION APPLIES.—*
 22 *This section shall apply to a foreign corporation for the*
 23 *taxable year if—*

1 “(1) at any time during such taxable year, one
2 or more domestic corporations own, directly or through
3 one or more other corporations, 10 percent or more of
4 the outstanding stock of such corporation, and

5 “(2) for such taxable year, such foreign corpora-
6 tion derives 10 percent or more of its gross income from
7 the sale of competitive articles which are sold by it for
8 ultimate use, consumption, or disposition in the United
9 States.

10 “(c) *COMPETITIVE ARTICLE DEFINED.*—For purposes
11 of this section, the term ‘competitive article’ means any ar-
12 ticle mined, processed, or manufactured outside the United
13 States for a foreign corporation which is the same as or sim-
14 ilar to any article mined, processed, or manufactured in the
15 United States (or formerly mined, processed, or manufac-
16 tured in the United States) by—

17 “(1) any domestic corporation which, with respect
18 to such foreign corporation, is described in subsection
19 (b)(1); or

20 “(2) any subsidiary of a domestic corporation
21 described in paragraph (1) of this subsection.”

1 (b) The table of sections for such subpart B is amended
2 by adding at the end thereof the following:

"Sec. 885. Certain foreign corporations producing products for sale in the United States."

3 (c) The amendments made by this section shall apply
4 to taxable years beginning after December 31, 1962.

5 **(201)**SEC. 33. *EFFECTIVE DATE OF AMENDMENT TO SECTION*
6 *1374(b).*

7 *The amendment made by section 2(b) of Public Law*
8 *86-376 (73 Stat. 699) shall take effect on September 2,*
9 *1958.*

10 SEC. (202)~~21~~ 34. TREATIES.

11 (203)Section 7852(d) of the Internal Revenue Code of 1954
12 (relating to treaty obligations) shall not apply in respect of
13 any amendment made by this Act.

14 *No provision of this Act shall apply in any case where*
15 *its application would be contrary to any treaty obligation*
16 *of the United States.*

Passed the House of Representatives March 29, 1962.

Attest: RALPH R. ROBERTS,
Clerk.

Passed the Senate with amendments September 6, 1962.

Attest:

FELTON M. JOHNSTON,
Secretary.

AN ACT

To amend the Internal Revenue Code of 1954 to provide a credit for investment in certain depreciable property, to eliminate certain defects and inequities, and for other purposes.

IN THE SENATE OF THE UNITED STATES

SEPTEMBER 6, 1962

Ordered to be printed with the amendments of the
Senate numbered

Sept 10, 1962

2. PUBLIC LANDS. The Interior and Insular Affairs Committee reported with amendments S. 3160, to amend the act of March 8, 1922 (permitting entry on and patent for land containing minerals) so as to extend its provisions to the townsite laws applicable in Alaska (S. Rept. 2022). p. 17836
3. PERISHABLE COMMODITIES. Conferees were appointed on S. 1037, to amend the Perishable Agricultural Commodities Act regarding fees, oral hearings, and relicensing. House conferees have not yet been appointed. p. 17862
4. WILDLIFE; RECREATION. Sens Williams, N. J., and Keating submitted amendments intended to be proposed to H. R. 1171, to increase the public benefits from the national fish and wildlife conservation areas through their incidental or secondary use for public recreation. pp. 17862-3
5. TAXATION. Passed with amendments H. R. 6413, to extend to fishermen the same treatment accorded farmers in relation to estimated income tax. p. 17864
6. FOREIGN TRADE. Sen. Humphrey inserted an article, "Challenge for America: Trade or Fade," supporting enactment of the proposed Trade Expansion Act of 1962. pp. 17837-40
7. EMPLOYMENT; ECONOMICS. Sen. Douglas submitted a resolution to authorize the printing of additional copies of hearings of the Jt. Economic Committee, "State of the Economy and Policies for Full Employment." pp. 17836, 17837
Sen. Humphrey inserted an article by Leon Keyserling, "One Prescription for Unemployment." pp. 17840-1
8. HOUSING. Sen. McNamara submitted a resolution to authorize the printing of additional copies of a committee print of the Special Committee on Aging, "Housing for the Elderly." p. 17837
9. CUBA; FOREIGN AGRICULTURE. Sen. Dodd inserted several articles discussing the situation in Cuba, including the shortage of food supplies. pp. 17874-7
10. INFORMATION. Sen. Thurmond inserted several articles on a new book, "Washington Cover-Up," regarding the use of executive privilege in withholding information from Congress. pp. 17865-6

HOUSE

11. FARM PROGRAM. The "Daily Digest" states, "Conferees continued, in executive session, to resolve the differences between the Senate- and House-passed versions of H. R. 12391, proposed Food and Agriculture Act of 1962, but did not reach final agreement, and will meet again tomorrow." p. D821
12. MIGRANT LABOR. Passed with amendment S. 1130, to amend title III of the Public Health Service Act to authorize grants for improving domestic agricultural migratory workers' health services and conditions. A similar bill, H. R. 12365, was laid on the table. pp. 17804, 17808-14
13. MILITARY CONSTRUCTION APPROPRIATIONS. Conferees were appointed on H. R. 12870, the military construction appropriation bill. Senate conferees have already been appointed. p. 17802
14. TAXATION. Conferees were appointed on H. R. 10650, the proposed Revenue Act of 1962. Senate conferees have already been appointed. p. 17802

Digest of CONGRESSIONAL PROCEEDINGS

OF INTEREST TO THE DEPARTMENT OF AGRICULTURE

OFFICE OF
BUDGET AND FINANCE

(For information only;
should not be quoted
or cited)

Issued Sept. 11, 1962
For actions of Sept. 10, 1962
87th-2d, No. 162

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HIGHLIGHTS: Senate agreed to House amendments to public works acceleration bill.
Sen. Humphrey inserted article supporting proposed foreign trade bill.

SENATE

1. PUBLIC WORKS. By a vote of 45 to 22, agreed to the House amendments to S. 2965, the public works acceleration bill (pp. 17842, 17847-61). This bill will now be sent to the President. As agreed to the bill authorizes an immediate \$900 million public works program in those areas which are designated by the Secretary of Commerce under the Area Redevelopment Act as "redevelopment areas" and those areas which the Secretary of Labor designates each month as having been areas of substantial unemployment for at least 9 of the preceding 12 months. Of the \$900 million authorized to be appropriated, \$300 million is to be reserved for allocation in areas designated under Sec. 5 (b) of the Area Redevelopment Act relating to unemployment in rural areas.

By a vote of 30 to 38, rejected an amendment by Sen. Cooper to correct a technical error in the bill which erroneously refers to a section not in the bill. pp. 17842, 17847-52

Rejected an amendment by Sen. Lausche to strike out a House amendment which alters the amount of money that local and State governments may post to qualify themselves for participation in the grants that are to be made. pp. 17856-



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No. 162

House of Representatives

The House met at 12 o'clock noon.

Rt. Rev. Dr. Theodosios L. Sideris, bishop of Ancona, Greek Orthodox Archdiocese of North and South America, sixth archdiocesan district, Pittsburgh, Pa., offered the following prayer:

Eternal God, from whom all blessings flow, we reverently bow our heads in prayer before Thy magnificence, thanking Thee for Thy many and bountiful gifts. We pray for our beloved President of these United States, for the Members of this respected Congress, and for all principals and authorities, that they may be enabled to discharge the duties of their respective office with honesty and ability.

We further pray for our brethren, our fellow citizens throughout the United States and for all mankind throughout the world, that we may be blessed in the knowledge, sanctified in the observance of Thy most holy law, and that we may abide in union and peace, guided always by Thy divine providence.

In these difficult and strenuous times in which we live, we realize even more the importance of Thy strength and wisdom to offset the human weakness and limitations we experience from time to time.

Heavenly Father, we beseech Thee to strengthen our leaders and people, that we might become the living example for all nations in the universal struggle for peace and concord.

May the Lord bless us and keep us, make His face to shine upon us and give us everlasting peace. Amen.

THE JOURNAL

The Journal of the proceedings of Thursday, September 6, 1962, was read and approved.

MESSAGE FROM THE SENATE

A message from the Senate by Mr. McGown, one of its clerks, announced that the Senate had passed without amendment bills and a joint resolution of the House of the following titles:

H.R. 4635. An act for the relief of Hattie and Joseph Patrick, Sr., and for the legal

guardian of Betty Ann Smith and the legal guardian of Stanley Smith, and for the legal guardian of James E. Harris, Jr.;

H.R. 6021. An act for the relief of Lt. Don Walsh and Lt. Lawrence A. Shumaker;

H.R. 10242. An act to amend Private Law 86-339;

H.R. 10383. An act to amend the Federal Home Loan Bank Act to give Puerto Rico the same treatment as a State in the election of Federal Home Loan Bank Directors;

H.R. 12024. An act for the relief of Librande P. Caltagirone; and

H.J. Res. 627. Joint resolution extending the duration of copyright protection in certain cases.

The message also announced that the Senate had passed, with amendments in which the concurrence of the House is requested, bills of the House of the following titles:

H.R. 8038. An act to amend section 491 of title 18, United States Code, prohibiting certain acts involving the use of tokens, slugs, disks, devices, papers, or other things which are similar in size and shape to the lawful coins or other currency of the United States;

H.R. 8355. An act to authorize executive agencies to grant easements in, over, or upon real property of the United States under the control of such agencies, and for other purposes; and

H.R. 11217. An act to amend section 6112 of title 10, United States Code.

The message also announced that the Senate had passed, with an amendment in which the concurrence of the House is requested a bill of the House of the following title:

H.R. 10. An act to encourage the establishment of voluntary pension plans by self-employed individuals.

The message also announced that the Senate insists upon its amendment to the foregoing bill, requests a conference with the House on the disagreeing votes of the two Houses thereon, and appoints Mr. BYRD of Virginia, Mr. KERR, Mr. LONG of Louisiana, Mr. SMATHERS, Mr. WILLIAMS of Delaware, Mr. CARLSON, and Mr. BENNETT to be the conferees on the part of the Senate.

The message also announced that the Senate had passed, with amendments in which the concurrence of the House is requested, a bill of the House of the following title:

H.R. 10650. An act to amend the Internal Revenue Code of 1954 to provide a credit for investment in certain depreciable property, to eliminate certain defects and inequities, and for other purposes.

The message also announced that the Senate insists upon its amendments to the foregoing bill, requests a conference with the House on the disagreeing votes of the two Houses thereon, and appoints Mr. BYRD of Virginia, Mr. KERR, Mr. LONG of Louisiana, Mr. SMATHERS, Mr. WILLIAMS of Delaware, Mr. CARLSON, and Mr. BENNETT to be the conferees on the part of the Senate.

The message also announced that the Senate had passed, with amendments in which the concurrence of the House is requested, a bill of the House of the following title:

H.R. 12870. An act making appropriations for military construction for the Department of Defense for the fiscal year ending June 30, 1963, and for other purposes.

The message also announced that the Senate insists upon its amendments to the foregoing bill, requests a conference with the House on the disagreeing votes of the two Houses thereon, and appoints Mr. STENNIS, Mr. CHAVEZ, Mr. MONRONEY, Mr. SALTONSTALL, and Mr. KUCHEL to be the conferees on the part of the Senate.

The message also announced that the Senate had passed bills, a joint resolution, and a concurrent resolution of the following titles, in which the concurrence of the House is requested:

S. 2773. An act to amend section 503 of the Federal Aviation Act to provide substantive Federal law relating to the validity of conveyances which affect title to or interests in civil aircraft of the United States and related equipment;

S. 3154. An act to amend Public Law 86-184, an act to provide for the striking of medals in commemoration of the 100th anniversary of the admission of West Virginia into the Union as a State;

S. 3451. An act to provide relief for residential occupants of unpatented mining claims upon which valuable improvements have been placed, and for other purposes;

S. 3646. An act to amend the Communications Act of 1934, as amended, relative to merger of domestic telegraph carriers;

S.J. Res. 214. Joint resolution authorizing the President of the United States to

designate the period from November 26, 1962, through December 2, 1962, as National Cultural Center Week; and

S. Con. Res. 53. Concurrent resolution favoring air travel by legislative and Government officers and employees on U.S.-flag air carriers.

The message also announced that the Senate agrees to the amendments of the House of Representatives to the concurrent resolution (S. Con. Res. 86) entitled "Concurrent resolution favoring the suspension of deportation of certain aliens" with an amendment as follows: Page 2, after line 3, insert:

Page 5, after line 4, insert:

"SEC. 5. The Congress approves the granting of the status of permanent residence in the case of the alien hereinafter named, in which case the Attorney General has determined that such alien is qualified under the provisions of section 4 of the Displaced Persons Act of 1948, as amended (62 Stat. 1011; 64 Stat. 219; 50 App. U.S.C. 1953):

"A-7116387, Rock, Feiga Altmann."

The message also announced that the Senate agrees to the report of the committee of conference on the disagreeing votes of the two Houses on the amendments of the House to the bill (S. 167) entitled "An act to authorize the Attorney General to compel the production of documentary evidence required in civil investigations for the enforcement of the antitrust laws, and for other purposes."

MAKING APPROPRIATIONS FOR MILITARY CONSTRUCTION FOR THE DEPARTMENT OF DEFENSE FOR FISCAL YEAR 1963 AND FOR OTHER PURPOSES

Mr. SIKES. Mr. Speaker, I ask unanimous consent to take from the Speaker's table the bill (H.R. 12870) making appropriations for military construction for the Department of Defense for fiscal year 1963 and for other purposes, with Senate amendments thereto, disagree to the Senate amendments, and agree to the conference asked by the Senate.

The SPEAKER. Is there objection to the request of the gentleman from Florida? The Chair hears none, and appoints the following conferees: Messrs. SHEPPARD, SIKES, CANNON, JONAS, and TABER.

AMENDING INTERNAL REVENUE CODE OF 1954

Mr. MILLS. Mr. Speaker, I ask unanimous consent to take from the Speaker's table the bill (H.R. 10650) to amend the Internal Revenue Code of 1954 to provide a credit for investment in certain depreciable property, to eliminate certain defects and inequities, and for other purposes, with Senate amendments thereto, disagree to the Senate amendments, and agree to the conference requested by the Senate.

The SPEAKER. Is there objection to the request of the gentleman from Arkansas?

Mr. GROSS. Mr. Speaker, reserving the right to object, can the gentleman give us any information as to when he would expect to go to conference, either this week or next week?

Mr. MILLS. In all probability, it would be next week; I cannot be certain, but not before Friday of this week.

Mr. GROSS. Mr. Speaker, I withdraw my reservation of objection.

The SPEAKER. Is there objection to the request of the gentleman from Arkansas?

The Chair hears none, and appoints the following conferees: Messrs. MILLS, KING of California, BOGGS, KEOGH, BYRNES of Wisconsin, and BAKER.

VOLUNTARY PENSION PLANS BY SELF-EMPLOYED INDIVIDUALS

Mr. MILLS. Mr. Speaker, I ask unanimous consent to take from the Speaker's table the bill (H.R. 10) to encourage the establishment of voluntary pension plans by self-employed individuals, with Senate amendments thereto, disagree to the Senate amendments and agree to the conference requested by the Senate.

The SPEAKER. Is there objection to the request of the gentleman from Arkansas?

Mr. BYRNES of Wisconsin. Mr. Speaker, reserving the right to object, I wonder if the chairman of the committee could advise us whether the conference on this bill will be under the same schedule he recently suggested?

Mr. MILLS. It would be impossible for us to get to conference before Friday of this week on either of these two bills.

Mr. BYRNES of Wisconsin. Mr. Speaker, I withdraw my reservation of objection.

The SPEAKER. Is there objection to the request of the gentleman from Arkansas?

The Chair hears none and appoints the following conferees: Messrs. MILLS, KING of California, KEOGH, MASON, BYRNES of Wisconsin, and BAKER.

NATIONAL SAFETY COUNCIL 50TH ANNIVERSARY YEAR

Mr. FORRESTER. Mr. Speaker, I ask unanimous consent for the immediate consideration of the joint resolution (S. J. Res. 222) providing for the designation of the period October 1962 through October 1963 as "National Safety Council 50th Anniversary Year."

The Clerk read the title of the joint resolution.

The SPEAKER. Is there objection to the request of the gentleman from Georgia?

There was no objection.

The Clerk read as follows:

Whereas October 1962 marks the beginning of the fiftieth anniversary observance of the founding of the National Safety Council; and

Whereas the council has striven faithfully during this half century to develop and implement sound, effective programs directed toward the prevention of accidents of all kinds; and

Whereas the prevention of accidents is of the greatest importance to the success of our economy and the well-being of our Nation; and

Whereas the records have shown a notable and steady decline in the rates of accidental

death and injury as a result of national programs of the organized safety movement; and

Whereas this decline in accident rates demonstrates the value of nationwide safety activities as carried on under the leadership of the National Safety Council; and

Whereas the Congress enacted a Federal charter for the National Safety Council; and

Whereas the National Safety Council, as a guardian of the public interest, has proved its dedication to the safety and welfare of the Nation's citizens, as set forth in its Federal charter: Therefore be it

Resolved by the Senate and House of Representatives of the United States of America in Congress assembled, That the President is authorized and requested to issue a proclamation designating the period October 1962 through October 1963 as "National Safety Council Fiftieth Anniversary Year," and calling upon the governments of the States and communities and the people of the United States to join in observance of this significant occasion and to increase their efforts to reduce the number of accidents in homes, in industry, in public places, and on our streets and highways.

The joint resolution was ordered to be read a third time, was read the third time, and passed.

A motion to reconsider was laid on the table.

STANDBY AUTHORITY TO CALL UP MILITARY RESERVISTS

(Mr. ALBERT asked and was given permission to address the House for 1 minute and to revise and extend his remarks.)

Mr. ALBERT. Mr. Speaker, I take this time to advise the House that the distinguished chairman of the Committee on Armed Services, the gentleman from Georgia [Mr. VINSON], will today introduce a resolution implementing the President's request for standby authority to call up military reservists for 1 year.

I am sure the American people will support the President's decision in this instance in overwhelming numbers. This action reaffirms the policy of the Government of the United States that, in this dangerous age in which we live, we shall at all times operate from a position of strength and preparedness. We shall be ready for any and every emergency around the clock and through the calendar.

To this same end, this Congress in the last 18 months has provided additional funds totaling some \$9 billion to improve both our nuclear and our conventional capabilities.

To this same end also, I am sure the Congress will expedite action on the resolution to be introduced today by the gentleman from Georgia to implement the President's request.

CRIMES AND OFFENSES

Mr. FORRESTER. Mr. Speaker, I ask unanimous consent to take from the Speaker's desk the bill (H.R. 8038) to amend section 491 of title 18, United States Code, prohibiting certain acts involving the use of tokens, slugs, disks, devices, papers, or other things which are similar in size and shape to the lawful coins or other currency of the United

Sept. 25, 1967

to accomplish," and inserted correspondence with Secretary Freeman to "clear up this misunderstanding." p. 19510

13. TRANSPORTATION. Passed as reported H. R. 5700, to authorize the Secretary of the Treasury to designate any contract carrier, authorized to act as such by any agency of the U. S., as a carrier of bonded merchandise for the final release of which from customs custody a permit has not been issued. p. 19533
14. TAXATION. The "Daily Digest" states that conferees agreed to file a conference report on H. R. 10650, the proposed Revenue Act of 1962, by next Sat. or Mon. p. D891
15. STATISTICS. The Post Office and Civil Service Committee voted to report (but did not actually report) H. R. 7791, to provide for the collection and publication of foreign commerce and trade statistics. p. D888
16. PUBLIC WORKS. Sen. Long, Mo., urged the construction of a new youth institution in St. Francois County, Mo., with funds made available by the Public Works Acceleration Act. pp. 19501-2
17. RESEARCH. Sen. Boggs inserted an address by the associate director of the agricultural experiment station, Ohio State University, "Research Will Govern the Future." pp. 19499-501
18. WATER POLLUTION. Sen. Keating commended the Schenectady Jaycees for their project to control pollution of the Mohawk River. pp. 19522-3
19. PERSONNEL. Sen. Clark commended the committee action to increase annuities for Federal retirees. p. 19465
20. FORESTRY. Passed as reported H. R. 12688, to authorize the Secretary of Agriculture to encourage and assist the States in carrying on a program of forestry research by providing grants and other assistance for forestry research to land-grant colleges and universities or agricultural experimental stations and other colleges and universities offering graduate training in sciences basic to forestry. p. 19528
21. TAXATION. Passed as reported H. R. 5260, to continue for an additional three-year period the existing suspensions of the tax on the first domestic processing of coconut oil, palm oil, palm-kernel oil, and fatty acids, salts, combinations, or mixtures thereof. pp. 19532-3
22. MINERALS. The Interior and Insular Affairs Committee voted to report (but did not actually report) H. R. 11049, to provide for the relief of certain oil and gas lessees under the Mineral Leasing Act, and with amendment S. 1696, to authorize the Secretary of the Interior to conduct a survey of federally owned lands for the purpose of locating strategic minerals. p. D888
23. PATENTS. The Judiciary Committee voted to report (but did not actually report) S. 2225, to fix the fees payable to the Patent Office; S. 2639, relating to the oath of applicant for patent, and verification by the applicant of application for trademark registration; and H. R. 12513, to provide for public notice of settlements in patent interferences. p. D889
24. WATER RESOURCES. Sen. Anderson inserted an address by Secretary of Interior Udall on water resource development at the dedication of the Navajo Dam, San Juan County, N. Mex. pp. 19498-9

25. EDUCATION. The Labor and Public Welfare Committee voted to report (but did not actually report) with amendment S. 3477, to provide for a program to assist the States in further developing their programs of general university extension education. p. D889
26. FOREIGN AGRICULTURE. Sen. Dodd and Wiley inserted articles discussing the shortage of food in Communist China. pp. 19494-6- 19502

ITEMS IN APPENDIX

27. TRANSPORTATION. Extension of remarks of Rep. Berry inserting an article indicating the losses suffered by South Dakota industry due to the Chicago and North Western Railway strike. p. A7081
28. FOREIGN AID. Extension of remarks of Rep. Derounian inserting an article supporting House cuts in the foreign aid program. p. A7090
29. FOREIGN TRADE. Extension of remarks of Rep. Lane inserting an article indicating that the Trade Expansion Act will not adversely affect the New England textile industry. p. A7094
- Extension of remarks of Rep. Philbin condemning free trade as a threat to American industry and labor. pp. A7094-5
- Extension of remarks of Rep. Lane inserting an article commending the Congress for its "far-sighted" passage of the Trade Expansion Act. p. A7095

PRINTED HEARINGS RECEIVED IN THIS OFFICE

30. APPROPRIATIONS. Foreign operations appropriations for 1963, part 4; and supplemental appropriation bill, 1963. H. Appropriations Committee.
31. TOBACCO. H. R. 12855 and H. R. 12910, exemption of certain tobaccos relating to lease and transfer of tobacco acreage. H. Agriculture Committee.
32. FHA LOANS. H. R. 12653, increase loan limitations of Farmers Home Administration. H. Agriculture Committee.
33. WILDLIFE. S. 3504 and other bills relating to fish and wildlife legislation. S. Commerce Committee.
34. PURCHASING. Administration of the Davis-Bacon Act, part 1. H. Education and Labor Committee.

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COMMITTEE HEARINGS SEPT. 26:

Agricultural appropriation bill, conferees (exec).
House Agriculture (exec., on pending legislation).
Administration's transportation bills, S. Commerce

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29. **TRADE FAIRS.** Passed under suspension of the rules S. 3389, to promote the foreign commerce of the U. S. through the use of mobile trade fairs.
pp. 20354, 20399-401
30. **AGRICULTURE COMMITTEE.** The "Daily Digest" states that the Agriculture Committee "Passed over without prejudice H. R. 10101, to provide for a program of agricultural land development in Alaska; S. 3589, to acquire lands in Wright County, Minn., and exchange them with the State of Minnesota for State-owned lands in the Superior National Forest; and S. 3517, to establish and carry out a program to promote the flow of domestically produced lumber in commerce."
p. D919
31. **TRANSPORTATION.** Passed under suspension of the rules, H. R. 12968, to remove the time limitation within which a vessel, otherwise qualified under this exception, could redocument under United States registry. pp. 20402-3
32. **TAXATION.** Received the conference report on H. R. 10650, the proposed Revenue Act of 1962 (H. Rept. 2508)... pp. 20413-27
33. **FOREIGN AFFAIRS.** Received from the Secretary of State a draft of a proposed bill "authorizing an appropriation to enable the United States to extend an invitation to the Food and Agriculture Organization (FAO) of the United Nations to hold a World Food Congress in the United States in 1963"; to Foreign Affairs Committee. p. 20443
34. **WILDLIFE.** The Merchant Marine and Fisheries Committee reported without amendment H. R. 13176, to increase the participation by counties in revenue from the national wildlife refuge system. p. 20443
35. **SMALL BUSINESS.** The Select Committee on Small Business issued a report on the financing problems of small business (H. Rept. 2500). p. 20443
36. **PUBLIC WORKS.** The Public Works Committee reported with amendment H. R. 13273, the public works authorization bill (H. Rept. 2504). p. 20443

ITEMS IN APPENDIX

37. **FOREIGN AID.** Various insertions favoring and opposing the reductions made by the House in foreign aid appropriations. pp. A7187, A7197, A7213-4, A7218, A7223-5
38. **TRANSPORTATION.** Rep. McCormack commended and inserted an address by the president of the U. S. Freight Co., "Our Transportation Problems--Time for Action." pp. A7191-3
39. **LEGISLATIVE PROGRAM.** Extension of remarks of Rep. Pike reporting on the accomplishments of the 87th Congress. pp. A7195-6
40. **INFORMATION.** Extension of remarks of Sen. Humphrey inserting an article, "Representative John Moss Fights to Let Public Know What's Going On." pp. A7200-1
41. **INTERGOVERNMENTAL RELATIONS.** Extension of remarks of Rep. Fountain inserting a tabulation of the endorsement of State legislative recommendations of the Advisory Commission on Intergovernmental Relations. pp. A7211-2

BILLS INTRODUCED

42. IMPORTS. S. 3771, by Sen. Carlson, to amend the Tariff Act of 1930 to impose a duty upon the importation of bread; to Finance Committee.
43. PUBLIC WORKS. S. 3773, by Sen. Kerr, authorizing the construction, repair, and preservation of certain public works on rivers and harbors for navigation, flood control; placed on the calendar.
44. WILDLIFE. S. 3774, by Sen. Williams, N. J., to provide for a national black-bird control program; to Interior and Insular Affairs Committee. Remarks of author pp. 20337-9
45. PERSONNEL. H. R. 13280, by Rep. Beckworth, to amend the Civil Service Act of January 16, 1883, with respect to the filling of positions in the competitive civil service; to Post Office and Civil Service Committee.
46. FARM PROGRAM. H. R. 13281, by Rep. Betts, to reinstate the 15-acre farm marketing quota exemption for 1963; to Agriculture Committee.
H. R. 13286, by Rep. Findley, to establish a corn support program for 1964; to Agriculture Committee.
47. FOREIGN TRADE. H. R. 13285, by Rep. Dingell, to amend the Export-Import Bank Act of 1945 to facilitate exports to areas with respect to which the United States is incurring a trade deficit; to Banking and Currency Committee.

BILLS APPROVED BY THE PRESIDENT

48. HOUSING. H. R. 12628, to authorize a program of housing for the elderly in rural areas, which includes authorization of \$50 million additional in loan funds for Farmers Home Administration loans to the elderly for building or purchasing homes in rural areas, authorization for the appropriation of \$50 million for a new program of direct loans to private nonprofit corporations and consumer cooperatives to build moderate-cost rental housing for the elderly, a new insurance program to provide rental housing for the elderly in rural areas, and an increase in the rural grant ceiling from \$500 to \$1,000 for home improvements by owner-occupants whose incomes are so low they cannot qualify for loans from any source. Approved September 28, 1962 (Public Law 87-723).
49. FEDERAL-STATE COOPERATION. S. 3475, to provide further for cooperation with States in administration and enforcement of certain Federal laws relating to the marketing of agricultural products and to the eradication or control of plant and animal diseases and pests. Approved September 28, 1962 (Public Law 87-718).
50. PETRIFIED WOOD. H. R. 10540, to exclude deposits of petrified wood from appropriation under the United States mining laws. Approved September 28, 1962 (Public Law 87-713).
51. WILDLIFE; RECREATION. H. R. 1171, to increase the public benefits from the national fish and wildlife conservation areas through their incidental or secondary use for public recreation. Approved September 28, 1962 (Public Law 87-714).
52. STOCKPILING. H. R. 12416, to waive the statutory requirement for a 6-month waiting period before GSA is authorized to dispose of 4,000 long tons of chestnut tannin extract from the national stockpile. Approved September 28,

REVENUE ACT OF 1962

OCTOBER 1, 1962.—Ordered to be printed

Mr. MILLS, from the committee of conference,
submitted the following

CONFERENCE REPORT

[To accompany H.R. 10650]

The committee of conference on the disagreeing votes of the two Houses on the amendments of the Senate to the bill (H.R. 10650) to amend the Internal Revenue Code of 1954 to provide a credit for investment in certain depreciable property, to eliminate certain defects and inequities, and for other purposes, having met, after full and free conference, have agreed to recommend and do recommend to their respective Houses as follows:

That the Senate recede from its amendments numbered 11, 12, 13, 14, 28, 30, 50, 95, 145, 146, 197, 199, 200, and 203.

That the House recede from its disagreement to the amendments of the Senate numbered 2, 3, 4, 6, 7, 8, 10, 15, 16, 17, 18, 19, 20, 21, 22, 23, 24, 25, 26, 27, 32, 33, 34, 35, 36, 37, 38, 39, 40, 41, 42, 43, 44, 45, 46, 47, 49, 51, 52, 53, 55, 56, 57, 58, 59, 62, 63, 64, 65, 66, 67, 68, 70, 71, 72, 73, 74, 75, 76, 77, 78, 79, 80, 81, 82, 83, 84, 86, 88, 93, 94, 97, 98, 100, 101, 102, 103, 105, 106, 107, 108, 109, 110, 111, 112, 113, 114, 115, 116, 117, 118, 119, 120, 121, 122, 123, 124, 125, 127, 128, 129, 130, 131, 132, 133, 134, 135, 136, 137, 138, 139, 141, 142, 143, 144, 147, 148, 149, 150, 151, 152, 153, 154, 155, 156, 157, 158, 160, 162, 163, 164, 165, 166, 167, 168, 169, 170, 171, 172, 174, 175, 176, 177, 178, 179, 181, 182, 184, 185, 186, 188, 191, 193, and 194, and agree to the same.

Amendment numbered 1:

That the House recede from its disagreement to the amendment of the Senate numbered 1, and agree to the same with amendments as follows:

Page 3, line 6, of the Senate engrossed amendments, strike out "date" and insert *dates*

Page 4 of the Senate engrossed amendments, strike out lines 27 and 28 and insert:

- (b) *Conforming amendment.*
- (c) *Clerical amendment.*
- (d) *Effective date.*

Page 5 of the Senate engrossed amendments, strike out lines 1 to 24, inclusive, and insert:

Sec. 27. Exclusion from gross income of certain awards made pursuant to evacuation claims of Japanese-American persons.

- (a) *In general.*
- (b) *Effective date, etc.*

Sec. 28. Deduction for depreciation by tenant-stockholder of cooperative housing corporation.

- (a) *Allowance of deduction.*
- (b) *Clerical amendment.*
- (c) *Effective date.*

Sec. 29. Deduction for income tax purposes of contributions to certain organizations for judicial reform.

Sec. 30. Effective date of amendment to section 1374(b).

Sec. 31. Treaties.

And the Senate agree to the same.

Amendment numbered 5:

That the House recede from its disagreement to the amendment of the Senate numbered 5, and agree to the same with amendments as follows:

Page 6, line 13, of the Senate engrossed amendments, strike out "June 30, 1962" and insert *December 31, 1961*

Page 7 of the Senate engrossed amendments, strike out lines 14 to 22, inclusive, and insert:

"(4) TAXABLE YEAR BEGINNING BEFORE JANUARY 1, 1962.—For purposes of determining the amount of an investment credit carry-back that may be added under paragraph (1) for a taxable year beginning before January 1, 1962, and ending after December 31, 1961, the amount of the limitation provided by subsection (a)(2) is the amount which bears the same ratio to such limitation as the number of days in such year after December 31, 1961, bears to the total number of days in such year.

And the Senate agree to the same.

Amendment numbered 9:

That the House recede from its disagreement to the amendment of the Senate numbered 9, and agree to the same with an amendment as follows:

Page 9, line 19, of the Senate engrossed amendments, after "is", insert *equal to or*; and the Senate agree to the same.

Amendment numbered 29:

That the House recede from its disagreement to the amendment of Senate numbered 29, and agree to the same with an amendment as follows:

In lieu of the matter proposed to be inserted by the Senate amendment insert the following: , or, in the case of an item directly preceding or following a substantial and bona fide business discussion (including business meetings at a convention or otherwise), that such item was associated with,

And the Senate agree to the same.

Amendment numbered 31:

That the House recede from its disagreement to the amendment of the Senate numbered 31, and agree to the same with an amendment as follows:

In lieu of the matter proposed to be inserted by the Senate amendment insert the following: , or, in the case of an item described in subparagraph (A) directly preceding or following a substantial and bona fide business discussion (including business meetings at a convention or otherwise), the portion of such item associated with,

And the Senate agree to the same.

Amendment numbered 48:

That the House recede from its disagreement to the amendment of the Senate numbered 48, and agree to the same with an amendment as follows:

In lieu of the matter proposed to be inserted by the Senate amendment insert the following: , but the amount determined under this subparagraph shall in no case be greater than the larger of—

“(i) the amount determined under paragraph (4), or

“(ii) the amount which, when added to the amount determined under subparagraph (A), equals the amount by which 12 percent of the total deposits or withdrawable accounts of depositors of the taxpayer at the close of such year exceeds the sum of its surplus, undivided profits, and reserves at the beginning of such year (taking into account any portion thereof attributable to the period before the first taxable year beginning after December 31, 1951)

And the Senate agree to the same.

Amendment numbered 54:

That the House recede from its disagreement to the amendment of the Senate numbered 54, and agree to the same with an amendment as follows:

Page 46, after line 4, of the House engrossed bill insert:

“(5) **LIMITATION IN CASE OF CERTAIN DOMESTIC BUILDING AND LOAN ASSOCIATIONS.**—If the percentage of the assets of a domestic building and loan association which are not assets described in section 7701(a)(19)(D)(ii) exceeds 36 percent for the taxable year (as determined for purposes of section 7701(a)(19) for such year), the amount determined under paragraph (2), and the amount determined under paragraph (3), shall in each case be the amount (determined without regard to this paragraph but with regard to the limits contained in paragraphs (2), (3), and (1)(B)) reduced by the amount determined under the following table:

If the percentage exceeds—	but does not exceed—	the reduction shall be the following proportion of the amount so determined without regard to this paragraph—
36 percent.....	37 percent.....	1/12
37 percent.....	38 percent.....	1/6
38 percent.....	39 percent.....	1/4
39 percent.....	40 percent.....	1/3
40 percent.....	41 percent.....	5/12

And the Senate agree to the same.

Amendment numbered 60:

That the House recede from its disagreement to the amendment of the Senate numbered 60, and agree to the same with amendments as follows:

Page 24, line 15, of the Senate engrossed amendments, strike out the parenthesis at the beginning of the line.

Page 25, line 23, of the Senate engrossed amendments, strike out "(i) and (ii)" and insert (i), (ii), (iv), and (vi)

Page 26, line 10, of the Senate engrossed amendments, strike out "(i) and (ii)" and insert (i), (ii), (iv), and (vi)

Page 27, after line 6, of the Senate engrossed amendments, insert:
The term 'domestic building and loan association' also includes any association which, for the taxable year, would satisfy the requirements of the first sentence of this paragraph if '41 percent' were substituted for '36 percent' in subparagraph (E). Except in the case of the taxpayer's first taxable year beginning after the date of the enactment of the Revenue Act of 1962, the second sentence of this paragraph shall not apply to an association for the taxable year unless such association (i) was a domestic building and loan association within the meaning of the first sentence of this paragraph for the first taxable year preceding the taxable year, or (ii) was a domestic building and loan association solely by reason of the second sentence of this paragraph for the first taxable year preceding the taxable year (but not for the second preceding taxable year).

And the Senate agree to the same.

Amendment numbered 61:

That the House recede from its disagreement to the amendment of the Senate numbered 61, and agree to the same with amendments as follows:

Page 27, line 13, of the Senate engrossed amendments, strike out "EXCISE".

Page 27, line 15, of the Senate engrossed amendments, after "ACT", insert OF 1933

Page 27, line 16, of the Senate engrossed amendments, after "Act", insert of 1933

Page 27, lines 19 and 20, of the Senate engrossed amendments, strike out "EXEMPTION FROM DISCRIMINATORY STATE AND LOCAL TAXATION.—".

And the Senate agree to the same.

Amendment numbered 69:

That the House recede from its disagreement to the amendment of the Senate numbered 69, and agree to the same with amendments as follows:

Page 64, line 9, of the House engrossed bill, strike out "6047" and insert 6048

Page 65, line 13, of the House engrossed bill, strike out "6047" and insert 6048

Page 67, after line 6, of the House engrossed bill, strike out "6047" and insert 6048

And the Senate agree to the same.

Amendment numbered 85:

That the House recede from its disagreement to the amendment of the Senate numbered 85, and agree to the same with an amendment as follows:

In lieu of the matter proposed to be inserted by the Senate amendment insert the following: \$500,000; and the Senate agree to the same.

Amendment numbered 87:

That the House recede from its disagreement to the amendment of the Senate numbered 87, and agree to the same with an amendment as follows:

In lieu of the matter proposed to be inserted by the Senate amendment insert the following:

“(f) *SPECIAL TRANSITIONAL UNDERWRITING LOSS.*—

“(1) *COMPANIES TO WHICH SUBSECTION APPLIES.*—*This subsection shall apply to every mutual insurance company which has been subject to the tax imposed by this section (as in effect before the enactment of this subsection) for the 5 taxable years immediately preceding January 1, 1962, and has incurred an underwriting loss for each of such 5 taxable years.*

“(2) *REDUCTION OF STATUTORY UNDERWRITING INCOME.*—*For purposes of this part, the statutory underwriting income of a company described in paragraph (1) for the taxable year shall be the statutory underwriting income for the taxable year (determined without regard to this subsection) reduced by the amount by which—*

“(A) *the sum of the underwriting losses of such company for the 5 taxable years immediately preceding January 1, 1962, exceeds*

“(B) *the total amount by which the company's statutory underwriting income was reduced by reason of this subsection for prior taxable years.*

“(3) *UNDERWRITING LOSS DEFINED.*—*For purposes of this subsection, the term ‘underwriting loss’ means statutory underwriting loss, computed without any deduction under section 824(a) and without any deduction under section 832(c)(11).*

“(4) *YEARS TO WHICH SUBSECTION APPLIES.*—*This subsection shall apply with respect to any taxable year beginning after December 31, 1962, and before January 1, 1968, for which the taxpayer is subject to the tax imposed by subsection (a).*

And the Senate agree to the same.

Amendment numbered 89:

That the House recede from its disagreement to the amendment of the Senate numbered 89, and agree to the same with an amendment as follows:

In lieu of the matter proposed to be inserted by the Senate amendment insert the following: \$1,100,000; and the Senate agree to the same.

Amendment numbered 90:

That the House recede from its disagreement to the amendment of the Senate numbered 90, and agree to the same with an amendment as follows:

In lieu of the matter proposed to be inserted by the Senate amendment insert the following: \$1,100,000; and the Senate agree to the same.

Amendment numbered 91:

That the House recede from its disagreement to the amendment of the Senate numbered 91, and agree to the same with an amendment as follows:

In lieu of the matter proposed to be inserted by the Senate amendment insert the following: \$500,000; and the Senate agree to the same.

Amendment numbered 92:

That the House recede from its disagreement to the amendment of the Senate numbered 92, and agree to the same with an amendment as follows:

In lieu of the matter proposed to be inserted by the Senate amendment insert the following: \$1,100,000; and the Senate agree to the same.

Amendment numbered 96:

That the House recede from its disagreement to the amendment of the Senate numbered 96, and agree to the same with an amendment as follows:

In lieu of the matter proposed to be inserted by the Senate amendment insert the following: *arising, either in any one State or within 200 miles of any fixed point selected by the taxpayer,*

And the Senate agree to the same.

Amendment numbered 99:

That the House recede from its disagreement to the amendment of the Senate numbered 99, and agree to the same with an amendment as follows:

Page 85, line 4, of the House engrossed bill, after "insurance", insert *company*; and the Senate agree to the same.

Amendment numbered 104:

That the House recede from its disagreement to the amendment of the Senate numbered 104, and agree to the same with amendments as follows:

Page 89, line 10, of the House engrossed bill, after "mutual fire", insert *or flood*

Page 89, line 19, of the House engrossed bill, after the period and before the quotation marks, insert *Premiums paid by the subscriber of a mutual flood insurance company referred to in paragraph (3) of section 831(a) shall be treated, for purposes of computing the taxable income of such subscriber, in the same manner as premiums paid by a policyholder to a mutual fire insurance company referred to in such paragraph (3).*

Page 90, line 18, of the House engrossed bill, after "mutual fire", insert *or flood*

And the Senate agree to the same.

Amendment numbered 126:

That the House recede from its disagreement to the amendment of the Senate numbered 126, and agree to the same with amendments as follows:

Page 62, line 7, of the Senate engrossed amendments, before "is", insert *income*

Page 64, line 24, of the Senate engrossed amendments, after "is", insert *created or*

Page 82, lines 6 and 7, of the Senate engrossed amendments, strike out “(computed without regard to section 931)”

Page 82, lines 14 and 15, of the Senate engrossed amendments, strike out “(computed without regard to section 931)”

Page 100 of the Senate engrossed amendments, strike out the table following line 10 and insert:

<i>“If the effective foreign tax rate is (percentage)—</i>	<i>The required minimum distribution of earnings and profits is (percentage)—</i>
<i>Under 10-----</i>	<i>90</i>
<i>10 or over but less than 20-----</i>	<i>86</i>
<i>20 or over but less than 28-----</i>	<i>82</i>
<i>28 or over but less than 34-----</i>	<i>75</i>
<i>34 or over but less than 39-----</i>	<i>68</i>
<i>39 or over but less than 42-----</i>	<i>55</i>
<i>42 or over but less than 44-----</i>	<i>40</i>
<i>44 or over but less than 46-----</i>	<i>27</i>
<i>46 or over but less than 47-----</i>	<i>14</i>
<i>47 or over-----</i>	<i>0</i>

Page 106, line 3, of the Senate engrossed amendments, strike out “total” and insert *consolidated*

Page 106, line 5, of the Senate engrossed amendments, strike out “total” and insert *consolidated*

Page 107, lines 20 and 21, of the Senate engrossed amendments, strike out “is eligible to make” and insert *makes*

And the Senate agree to the same.

Amendment numbered 140:

That the House recede from its disagreement to the amendment of the Senate numbered 140, and agree to the same with an amendment, as follows:

Page 123, line 14, of the Senate engrossed amendments, after “1962” insert a comma; and the Senate agree to the same.

(within the meaning of section 1221) and has been held for more than 6

Amendment numbered 159:

That the House recede from its disagreement to the amendment of the Senate numbered 159, and agree to the same with amendments as follows:

Page 130 of the Senate engrossed amendments, beginning with line 8, strike out all through page 131 and insert the following:

“(b) *LIMITATION ON TAX APPLICABLE TO INDIVIDUALS.*—*In the case of an individual, if the stock sold or exchanged is a capital asset (within the meaning of section 1221) and has been held for more than 6 months, the tax attributable to an amount included in gross income as a dividend under subsection (a) shall not be greater than a tax equal to the sum of—*

“(1) *a pro rata share of the excess of—*

“(A) *the taxes that would have been paid by the foreign corporation with respect to its income had it been taxed under this chapter as a domestic corporation (but without allowance for deduction of, or credit for, taxes described in subparagraph (B)), for the period or periods the stock sold or exchanged was held by the United States person in taxable years beginning after December 31, 1962, while the foreign corporation was a controlled foreign corporation, adjusted for distributions and amounts previously included in gross income of a United States shareholder under section 951, over*

*“(B) the income, war profits, or excess profits taxes paid by the foreign corporation with respect to such income; and
 “(2) an amount equal to the tax that would result by including in gross income, as gain from the sale or exchange of a capital asset held for more than 6 months, an amount equal to the excess of (A) the amount included in gross income as a dividend under subsection (a), over (B) the amount determined under paragraph (1).”*

Page 135, lines 9 and 10, of the Senate engrossed amendments, strike out “referred to in subparagraph (B)” and insert *ending on the date of the sale or exchange*

Page 137, line 25, of the Senate engrossed amendments, strike out “(2)”.

And the Senate agree to the same.

Amendment numbered 161:

That the House recede from its disagreement to the amendment of the Senate numbered 161, and agree to the same with amendments as follows:

Page 139 of the Senate engrossed amendments, insert quotation marks after “apply.” in line 7 and strike out lines 8 to 14, inclusive; and the Senate agree to the same.

Amendment numbered 173:

That the House recede from its disagreement to the amendment of the Senate numbered 173, and agree to the same with amendments, as follows:

Page 150, line 4, of the Senate engrossed amendments, strike out “6047” and insert 6048

Page 150, line 6, of the Senate engrossed amendments, strike out “6048” and insert 6049

Page 154, line 13, of the Senate engrossed amendments strike out “6048(a)(1)” and insert 6049(a)(1)

Page 155, line 4, of the Senate engrossed amendments, strike out “6048(a)(2)” and insert 6049(a)(2)

Page 155, line 5, of the Senate engrossed amendments, strike out “6048(a)(3)” and insert 6049(a)(3)

Page 156, line 5, of the Senate engrossed amendments, strike out “6048(c)” and insert 6049(c)

Page 156, line 8, of the Senate engrossed amendments, strike out “6048(a)(1)” and insert 6049(a)(1)

Page 156, line 22, of the Senate engrossed amendments, strike out “6048(a)(1)” and insert 6049(a)(1)

Page 156, line 25, of the Senate engrossed amendments, strike out “6048(a)(2), or 6048(a)(3)” and insert 6049(a)(2), or 6049(a)(3)

Page 157, line 19, of the Senate engrossed amendments, strike out “6048” and insert 6049; and the Senate agree to the same.

Amendment numbered 180:

That the House recede from its disagreement to the amendment of the Senate numbered 180, and agree to the same with an amendment as follows:

Page 159, line 18, of the Senate engrossed amendments, after “person”, insert *(as defined in section 7701(a)(30))*

And the Senate agree to the same.

Amendment numbered 183:

That the House recede from its disagreement to the amendment of the Senate numbered 183, and agree to the same with an amendment as follows:

In lieu of the matter proposed to be inserted by the Senate amendment insert the following:

“(e) *LIMITATION.*—

“(1) *GENERAL RULE.*—*Except as provided in paragraph (2), no information shall be required to be furnished under this section with respect to any foreign corporation unless such information was required to be furnished under regulations which have been in effect for at least 90 days before the date on which the United States citizen, resident, or person becomes liable to file a return required under subsection (a).*

“(2) *EXCEPTION.*—*In the case of liability to file a return under subsection (a) arising on or after January 1, 1963, and before June 1, 1963—*

“(A) *no information shall be required to be furnished under this section with respect to any foreign corporation unless such information was required to be furnished under regulations in effect on or before March 1, 1963, and*

“(B) *if the date on which such regulations become effective is later than the day on which such liability arose, any return required by subsection (a) shall (in lieu of the time prescribed by subsection (d)) be filed on or before the 90th day after such date.*

And the Senate agree to the same.

Amendment numbered 187:

That the House recede from its disagreement to the amendment of the Senate numbered 187, and agree to the same with an amendment as follows:

Page 239, after line 3, of the House engrossed bill, strike out “6038(d)(2)” and insert 6038(d)(1); and the Senate agree to the same.

Amendment numbered 189:

That the House recede from its disagreement to the amendment of the Senate numbered 189, and agree to the same with amendments as follows:

Page 163, after line 23, of the Senate engrossed amendments, insert:

(b) *CONFORMING AMENDMENT.*—*Section 263(a)(1) (relating to disallowance of deductions for capital expenditures) is amended by striking out “or” at the end of subparagraph (C), by striking out the period at the end of subparagraph (D) and inserting “, or”, and by adding at the end thereof the following new subparagraph:*

“(E) *expenditures by farmers for clearing land deductible under section 182.”*

Page 163, line 24, of the Senate engrossed amendments, strike out “(b)” and insert (c)

Page 164, line 4, of the Senate engrossed amendments, strike out “(c)” and insert (d)

And the Senate agree to the same.

Amendment numbered 190:

That the House recede from its disagreement to the amendment of the Senate numbered 190, and agree to the same with an amendment as follows:

Page 165 of the Senate engrossed amendments, strike out lines 4 through 10 and insert:

In any case in which the taxpayer elects to have the provisions of the preceding sentence apply, for purposes of computing the limitation on tax under this part—

“(1) only the same proportion of the amount to which this part applies shall be taken into account for purposes of computing the limitations under section 170(b)(1)(A) and (B) for taxable years before the taxable year in which such amount is received or accrued as (A) the excess of the maximum amount which could, if the taxpayer had made additional contributions described in clause (i), (ii), or (iii) of section 170(b)(1)(A), have been described in clause (1) of the preceding sentence over the amount described in such clause (1), bears to (B) such maximum amount, and

“(2) the portion of the amount of charitable contributions described in the preceding sentence shall not be taken into account in computing the tax for the taxable year in which the amount to which this part applies is received or accrued.”

And the Senate agree to the same.

Amendment numbered 192:

That the House recede from its disagreement to the amendment of the Senate numbered 192, and agree to the same with an amendment as follows:

Page 168, of the Senate engrossed amendments, strike out lines 6 to 11, inclusive, and insert:

(b) UNUSED CONVERSION LOSS DEFINED.—The amount of the unused conversion loss shall be the sum of the part of the net operating loss for each year described in subsection (a) which (without regard to this section) would be carried over to the sixth taxable year following the loss year if section 172(b) of the Internal Revenue Code of 1954 (or, where applicable, section 122(b)(2)(B) of the Internal Revenue Code of 1939) permitted such a carryover.

And the Senate agree to the same.

Amendment numbered 195:

That the House recede from its disagreement to the amendment of the Senate numbered 195, and agree to the same with an amendment as follows:

Page 171, line 19, of the Senate engrossed amendments, strike out “AMERICAN-JAPANESE INDIVIDUALS” and insert **JAPANESE-AMERICAN PERSONS**; and the Senate agree to the same.

Amendment numbered 196:

That the House recede from its disagreement to the amendment of the Senate numbered 196, and agree to the same with amendments as follows:

Page 173, line 9, of the Senate engrossed amendments, after "AND", insert **BUSINESS**

Page 174, after line 2, of the Senate engrossed amendments, insert:

(b) *CLERICAL AMENDMENT.*—*The table of sections for part VII of subchapter B of chapter 1 is amended by striking out the item relating to section 216 and inserting in lieu thereof the following:*

"Sec. 216. Deduction of taxes, interest, and business depreciation by cooperative housing corporation tenant-stockholder."

Page 174, line 3, of the Senate engrossed amendments, strike out "(b)" and insert (c)

And the Senate agree to the same.

Amendment numbered 198:

That the House recede from its disagreement to the amendment of the Senate numbered 198, and agree to the same with an amendment as follows:

Page 177, line 2, of the Senate engrossed amendments, strike out "30" and insert 29; and the Senate agree to the same.

Amendment numbered 201:

That the House recede from its disagreement to the amendment of the Senate numbered 201, and agree to the same with an amendment as follows:

Page 181, line 8, of the Senate engrossed amendments, strike out "33" and insert 30; and the Senate agree to the same.

Amendment numbered 202:

That the House recede from its disagreement to the amendment of the Senate numbered 202, and agree to the same with an amendment as follows:

In lieu of the matter proposed to be inserted by the Senate amendment insert the following: 31; and the Senate agree to the same.

W. D. MILLS,
CECIL R. KING,
HALE BOGGS,
EUGENE J. KEOGH,
JOHN W. BYRNES,
HOWARD H. BAKER,

Managers on the Part of the House.

HARRY F. BYRD,
ROBT. B. KERR,
By R. S. K.
RUSSELL B. LONG,
GEORGE SMATHERS,
By H. F. B.
JOHN J. WILLIAMS,
FRANK CARLSON,
WALLACE BENNETT,

Managers on the Part of the Senate.

STATEMENT OF THE MANAGERS ON THE PART OF THE HOUSE

The managers on the part of the House at the conference on the disagreeing votes of the two Houses on the amendments of the Senate to the bill (H.R. 10650) to amend the Internal Revenue Code of 1954 to provide a credit for investment in certain depreciable property, to eliminate certain defects and inequities, and for other purposes, submit the following statement in explanation of the effect of the action agreed upon by the conferees and recommended in the accompanying conference report:

The following Senate amendments made technical, clerical, clarifying, or conforming changes: 1, 2, 3, 4, 7, 8, 15, 16, 20, 22, 24, 25, 26, 27, 34, 35, 36, 38, 39, 40, 44, 47, 49, 51, 53, 55, 57, 58, 59, 63, 66, 67, 68, 71, 72, 73, 74, 77, 78, 83, 86, 88, 89, 101, 103, 105, 106, 107, 108, 109, 110, 112, 114, 115, 116, 117, 118, 119, 120, 122, 127, 134, 136, 137, 138, 139, 142, 144, 146, 148, 149, 150, 151, 152, 154, 155, 156, 157, 158, 164, 165, 169, 170, 171, 172, 174, 175, 177, 178, 182, 184, 185, 186, 187, 188, and 202. With respect to these amendments (1) the House either recedes or recedes with amendments which are technical, clerical, clarifying, or conforming in nature, or (2) the Senate recedes in order to conform to other action agreed upon by the committee of conference.

CREDIT FOR INVESTMENT IN CERTAIN DEPRECIABLE PROPERTY

Amendments Nos. 5 and 23: Under the bill as passed by both the House and the Senate the amount of the investment credit which may be allowed for any taxable year may not exceed so much of the liability for tax for the taxable year as does not exceed \$25,000, plus 25 percent of so much of the liability for tax for the taxable year as exceeds \$25,000. Under the bill as passed by the House, any unused credit resulting from this limitation was to be carried forward to each of the 5 succeeding taxable years to the extent not taken into account in intervening years. Under Senate amendment No. 5, such unused credit is first carried back to the 3 preceding taxable years and then carried over to the 5 succeeding taxable years. This rule is subject to 3 exceptions: (1) The unused credit may be a carryback only to taxable years ending after June 30, 1962, (2) to the extent that an unused credit arises by reason of a net operating loss carryback, such unused credit is taken into account only as a carryover and not as a carryback from such year, and (3) in the case of a taxable year beginning before July 1, 1962, and ending after June 30, 1962, the limitation on the credit allowable for such year for purposes of the carryback to such year is the amount which bears the same ratio to the limitation otherwise applicable as the number of days in such year after June 30, 1962, bears to the total number of days in such year. The House recedes with amendments conforming the unused credit carryback provisions to the conference action on Senate amendment No. 28 (which

provides that the investment credit is to apply to taxable years ending after December 31, 1961).

Senate amendment No. 23 amends the provisions of the code relating to periods of limitation and interest to conform to the Senate amendments providing for the unused credit carryback. The House recedes.

Amendments Nos. 6 and 9: The bill as passed by the House (sec. 46(c) of the code, as added by the bill) defined the qualified investment for purposes of the investment credit as the aggregate of (1) the applicable percentage of the basis of each new section 38 property placed in service during the taxable year, plus (2) the applicable percentage of the cost of each used section 38 property placed in service during the taxable year. These applicable percentages vary according to the useful life of the property. If any such property is disposed of, or otherwise ceases to be section 38 property with respect to the taxpayer, before the close of the useful life that was taken into account in computing the investment credit, then the income tax for the taxable year of the disposition is increased (sec. 47 of the code, as added by the bill) by an amount equal to the decrease in credits which would have resulted had the useful life used in determining the credit been the period beginning with the time the property was placed in service and ending with the time it ceased to be section 38 property.

The bill as passed by the Senate retains these rules except in cases where section 38 property is placed in service by the taxpayer to replace property which was stolen or was destroyed or damaged by fire, storm, shipwreck, or other casualty. Under Senate amendment No. 6, the basis (if new property) or cost (if used property) of the replacement section 38 property taken into account in determining qualified investment is required to be reduced by an amount equal to the amount received by the taxpayer as compensation (by insurance or otherwise) for the property destroyed, damaged, or stolen, or by an amount equal to the adjusted basis of such property, whichever is the lesser. This rule is not to apply if the reduction in qualified investment attributable to the substitution required by section 47(a)(1) of the code with respect to the property so destroyed, damaged, or stolen is greater than the reduction required under the new paragraph (4) added to section 46(c) by Senate amendment No. 6.

Senate amendment No. 9 adds a new paragraph (4) to section 47(a) of the code (relating to certain dispositions, etc., of sec. 38 property) to coordinate the provisions of such section 47(a) with the new rules provided under Senate amendment No. 6. In general, the new paragraph (4) of section 47(a) provides that paragraphs (1) and (3) of section 47(a) shall not apply to property which ceases to be section 38 property on account of its destruction or damage by fire, storm, shipwreck, or other casualty, or by reason of its theft, if such property is replaced by property to which the new paragraph (4) of section 46(c) (added by Senate amendment No. 6) applies, and if the reduction under that new paragraph is greater than the reduction in qualified investment under paragraph (1) of section 47(a).

The House recedes on Senate amendment No. 6 and recedes with a technical clarifying amendment on Senate amendment No. 9.

Amendment No. 10: This amendment adds a new paragraph (6) to new section 48(a) of the code (defining "section 38 property" for purposes of the investment credit) to provide that livestock is not to be treated as section 38 property. The House recedes.

Amendments Nos. 11, 12, 13, and 14: The bill as passed by the House defined the term "new section 38 property" as section 38 property (1) the construction, reconstruction, or erection of which is completed by the taxpayer after December 31, 1961, or (2) acquired after December 31, 1961, if the original use of such property commences with the taxpayer and commences after such date. In determining qualified investment described in clause (1) of the preceding sentence, only that portion of the basis which is properly attributable to construction, reconstruction, or erection after December 31, 1961, is to be taken into account. The bill as passed by the House also limited the definition of "used section 38 property" to property acquired by purchase after December 31, 1961. Senate amendments Nos. 11, 12, 13, and 14 changed these dates from December 31, 1961, to June 30, 1962. The Senate recedes.

Amendment No. 17: Under the bill as passed by the House, a person engaged in the business of leasing property would be permitted to elect with respect to any new section 38 property to treat the lessee as having acquired the property. Under Senate amendment No. 17, the lessor is not required to be engaged in the business of leasing property in order to make the election. The House recedes.

Amendments Nos. 18 and 19: Senate amendment No. 19 adds a new subsection (g) to new section 48 of the code (containing definitions and special rules relating to the investment credit). The new subsection requires that for purposes of subtitle A of the code (relating to income tax), other than for purposes of the investment credit, the basis of any section 38 property be reduced by an amount equal to 7 percent of the qualified investment with respect to such property. The new subsection provides, however, that if the tax under chapter 1 of the code is increased, or an adjustment in carrybacks or carryovers is made, under new section 47(a) of the code, the basis of the property is to be increased by an amount equal to the portion of the increase in tax and the portion of the adjustment attributable to such property. The House recedes.

It is the understanding of the conferees on the part of both the House and the Senate that the purpose of the credit for investment in certain depreciable property, in the case of both regulated and non-regulated industries, is to encourage modernization and expansion of the Nation's productive facilities and to improve its economic potential by reducing the net cost of acquiring new equipment, thereby increasing the earnings of the new facilities over their productive lives.

Senate amendment No. 18 provides that if a lessor makes an election to treat the lessee as having acquired the property then, under regulations prescribed by the Secretary of the Treasury or his delegate, the new subsection (g) added by amendment No. 19 is not to apply and the deductions otherwise allowable under section 162 of the code to the lessee for amounts paid to the lessor under the lease are to be adjusted in a manner consistent with the provisions of the new subsection (g). The House recedes.

Amendment No. 21: This amendment adds a new section 2(c) to the bill, adding a new section 181 to part VI of subchapter B of chapter 1 of the code (relating to itemized deductions for individuals and corporations). If after applying the carrybacks and carryovers of any unused investment credit any amount thereof remains unused, this amount is to be allowed to the taxpayer as a deduction for the first taxable year following the last taxable year in which the unused

amount could have been allowed as a credit. However, if a taxpayer dies or ceases to exist before such first taxable year, the amount described in the preceding sentence (or proper portion thereof) is, under regulations, to be allowed to the taxpayer as a deduction for the taxable year in which such death or cessation occurs. The House recedes.

Amendment No. 28: Under the bill as passed by the House, the amendments made by section 2 (relating to credit for investment in certain depreciable property) were to apply with respect to taxable years ending after December 31, 1961. Under Senate amendment No. 28, the amendments were to apply with respect to taxable years ending after June 30, 1962. The Senate recedes.

DISALLOWANCE OF CERTAIN ENTERTAINMENT, ETC., EXPENSES

Amendments Nos. 29, 30, and 31: The bill as passed by both the House and the Senate adds a new section 274 to the code (relating to disallowance of certain entertainment, etc., expenses). Section 274(a)(1) as passed by the House provided that no deduction otherwise allowable under chapter 1 of the code is to be allowed for any item—

(1) with respect to an activity which is of a type generally considered to constitute entertainment, amusement, or recreation, unless the taxpayer establishes that the item was directly related to the active conduct of the taxpayer's trade or business, or

(2) with respect to a facility used in connection with such an activity, unless the taxpayer establishes that the facility was used primarily for the furtherance of the taxpayer's trade or business and that the item was directly related to the active conduct of such trade or business,

and such deduction is in no event to exceed the portion of such item directly related to the active conduct of the taxpayer's trade or business.

Senate amendments Nos. 29, 30, and 31 inserted the words "or associated with" after the words "directly related to" each place they appeared in the new section 274(a)(1) as passed by the House.

Under the conference agreement the House recedes on Senate amendment No. 29 with an amendment providing that deductions otherwise allowable under chapter 1 of the code shall not be allowed for any item with respect to an entertainment type activity "unless the taxpayer establishes that the item was directly related to, or, in the case of an item directly preceding or following a substantial and bona fide business discussion (including business meetings at a convention or otherwise), that such item was associated with," the active conduct of the taxpayer's trade or business. Under the conference agreement, the Senate recedes on amendment No. 30, and the House recedes on amendment No. 31 with an amendment conforming to the action on amendment No. 29.

The rule of the House bill as described in the report of the Committee on Ways and Means is more strict than the "or associated with" rule of the Senate amendment. The rule of the House bill would not allow deduction of expenditures for entertainment occurring under circumstances where there is little or no possibility of conducting business affairs or carrying on negotiations or discussions relating thereto, such as where the group of persons entertained is large or the distractions substantial.

It is the understanding of the conferees, both on the part of the House and the Senate, that the alternative Senate "or associated with" test as described in the report of the Finance Committee would apply to certain entertaining primarily to encourage goodwill where the evidence of business connection is clear, whether or not business is actually transacted or discussed during the entertainment. The conference agreement would permit a deduction for the cost of an entertainment item, even though the item is not directly related to the active conduct of the taxpayer's trade or business, if the item is associated with it, so long as the entertainment activity directly precedes or follows a substantial and bona fide business discussion. The conditions under which an item is "associated with" the active conduct of a trade or business are contained in the report of the Committee on Finance. The deductibility of other items of entertainment expense, as well as items with respect to facilities, would be governed by the rule of the House bill.

Section 274(a) as agreed to by the conferees will allow as a deduction the cost of entertaining connected with what are primarily business meetings. For example, if the taxpayer conducts substantial negotiations with a group of business associates and that evening entertains the group and their wives at a restaurant, theater, concert, or sporting event, such entertainment expenses, if associated with the active conduct of the taxpayer's business, will be deductible even though the purpose of the entertainment is merely to promote goodwill in such business. Moreover, if a group of business associates with whom the taxpayer is conducting business meetings comes from out of town to the taxpayer's place of business to hold substantial business discussions, the entertainment of such business guests by the taxpayer the evening prior to the business discussions will be regarded as directly preceding the business discussions.

Similarly, if in between, or in the evenings after, business meetings at a convention, the taxpayer entertains his business associates or prospective customers attending such meetings (and their wives), such entertainment will be considered as directly preceding or following a business discussion.

Any entertainment which is a part of substantial and bona fide business discussions, where the conduct of business is the principal activity during the combined entertainment and business time spent together by the taxpayer and the person or persons entertained, will be deductible if the expense is associated with the active conduct of the taxpayer's trade or business.

Also, the cost of banquets at meetings of professional and business associations would normally be deductible. As in the above cases, if the expense is associated with the active conduct of a trade or business, it would not be necessary for the person paying for the banquet to attend the banquet himself. For example, a dental equipment supplier would be able to deduct the cost of purchasing a table at a dental association banquet for dentists who are actual or prospective customers for his equipment.

Thus, under the business meal exception contained in proposed section 274(e)(1), and the conference agreement, the cost of providing food and beverages at most business meetings and banquets would be deductible, as well as almost all restaurant and most hotel entertaining. In neither of the situations covered by the conference agreement

nor under the business meal exception is there a requirement that business must actually be discussed in order to get a deduction.

Amendment No. 32: Section 274(b), as added to the code by the bill as passed by both the House and the Senate, provides in effect that no deduction is to be allowed under section 162 or 212 of the code for any expense for gifts to any individual to the extent that the total expenses of the taxpayer for gifts to such individual during the same taxable year exceed \$25. For purposes of the new section 274, the term "gift" is defined to mean any item excludable from gross income of the recipient under section 102 of the code which is not excludable from his gross income under any other provision of chapter 1 of the code. Senate amendment No. 32 adds a new provision providing that such term does not include—

(1) an item having a cost to the taxpayer not in excess of \$4 on which the name of the taxpayer is clearly and permanently imprinted and which is one of a number of identical items distributed generally by the taxpayer,

(2) a sign, display rack, or other promotional material to be used on the business premises of the recipient, or

(3) an item of tangible personal property having a cost to the taxpayer not in excess of \$100 which is awarded to an employee by reason of length of service or for safety achievement.

The House recedes.

Amendment No. 33: This amendment adds a new subsection (c) to the new section 274 added to the code by the bill. The new subsection (c) provides that in the case of any individual who is traveling away from home in pursuit of a trade or business or in pursuit of an activity described in section 212 of the code (relating to expenses for production of income), no deduction is to be allowed under section 162 or 212 for that portion of the expenses of such travel otherwise allowable under such section which, under regulations prescribed by the Secretary of the Treasury or his delegate, is not allocable to such trade or business or to such activity. The new subsection (c) is not to apply to the expenses of any travel away from home which does not exceed 1 week or where the portion of the time away from home which is not attributable to the pursuit of the taxpayer's trade or business or an activity described in section 212 is less than 25 percent of the total time away from home on such travel. The House recedes.

Amendment No. 37: Under subsection (e)(6) of the new section 274 of the code, as added by the bill as passed by the House, section 274(a) (relating to disallowance of entertainment, amusement, or recreation expenses) was not to apply to expenses directly related to business meetings of employees or stockholders. Under Senate amendment No. 37, section 274(a) is not to apply to expenses incurred by a taxpayer which are directly related to business meetings of his employees, stockholders, agents, or directors. Under this provision, the members of a partnership are to be considered as agents. The House recedes.

Amendment No. 41: Section 162 of the code provides that there shall be allowed as a deduction all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, including "traveling expenses (including the entire amount expended for meals and lodging) while away from home in the pursuit of a trade or business." Under the bill as passed by the House, the

parenthetical matter quoted in the preceding sentence would be changed to "(including a reasonable allowance for amounts expended for meals and lodging)". Under Senate amendment No. 41, such parenthetical matter would be changed to "(including amounts expended for meals and lodging other than amounts which are lavish or extravagant under the circumstances)". The House recedes.

Amendment No. 42: Under the bill as passed by the House, the amendments made by the bill with respect to the disallowance of certain entertainment, etc., expenses were to apply with respect to taxable years ending after June 30, 1962, but only in respect of periods after such date. Under Senate amendment No. 42, the amendments are to apply with respect to taxable years ending after December 31, 1962, but only in respect of periods after such date. The House recedes.

AMOUNT OF DISTRIBUTION WHERE CERTAIN FOREIGN CORPORATIONS DISTRIBUTE PROPERTY IN KIND

Amendment No. 43: Subsection (d) of section 5 of the bill as passed by the House would amend section 902(a) of the code (relating to credit for foreign taxes) to provide that for purposes of section 902 (a) and (b) the amount of any distribution in property other than money is to be determined under section 301(b)(1)(B) of the code. Under section 301(b)(1)(B) the amount of a distribution of property to a corporate shareholder is the lesser of (1) the fair market value of such property, or (2) the adjusted basis of such property (in the hands of the distributing corporation immediately before the distribution). Senate amendment No. 43 strikes out subsection (d) of section 5 of the bill. The House recedes.

AMENDMENT TO SECTION 482 OF THE INTERNAL REVENUE CODE

Amendment No. 45: Section 6 of the bill as passed by the House amended section 482 of the code (relating to allocation of income and deductions among taxpayers) by designating the existing text as subsection (a) and by adding a new subsection (b) to provide special rules for allocating taxable income, arising from sales of tangible property within a related group which includes a foreign organization, among the members of the group. The allocation was to be made by the Secretary of the Treasury or his delegate by taking into consideration that portion of the factors listed in the bill which is attributable to the United States and that portion which is not attributable to the United States. The bill also permitted consideration of other factors (including special risks, if any, of the market in which the property is sold). If the taxpayer established to the satisfaction of the Secretary or his delegate that an alternative method of allocation clearly reflects the income of each member of the group with respect to the property in question, the alternative method was required to be used.

Senate amendment No. 45 strikes out section 6 of the bill as passed by the House.

The House recedes. The conferees on the part of both the House and the Senate believe that the objectives of section 6 of the bill as passed by the House can be accomplished by amendment of the regulations under present section 482. Section 482 already contains broad authority to the Secretary of the Treasury or his delegate to allocate

income and deductions. It is believed that the Treasury should explore the possibility of developing and promulgating regulations under this authority which would provide additional guidelines and formulas for the allocation of income and deductions in cases involving foreign income.

DISTRIBUTIONS OF FOREIGN PERSONAL HOLDING COMPANY INCOME

Amendment No. 46: Section 7 of the bill as passed by the House amended section 552(a) of the code to substitute a 20-percent gross income requirement for the requirement now contained in the definition of a foreign personal holding company that more than 60 percent (or 50 percent in certain cases) of its gross income consist of foreign personal holding company income. Such section 7 also amended the definition of "undistributed foreign personal holding company income" contained in section 556(a) of the code to mean taxable income (adjusted as provided by existing law) if the foreign personal holding company income exceeds 80 percent of the company's gross income, and to mean a proportionate part of such taxable income if the foreign personal holding company income does not exceed 80 percent of its gross income.

Senate amendment No. 46 strikes out section 7 of the bill as passed by the House. The House recedes.

MUTUAL SAVINGS BANKS, ETC.

Amendment No. 48: The bill as passed by both the House and the Senate amends section 593 of the code to provide rules relating to reserves for losses on loans by mutual savings institutions listed in the bill. Subsection (b)(1) of the amended section 593 prescribes the method for determining the reasonable addition for the taxable year to the reserve for bad debts under section 166(c) of the code and also specifies the reserves to which such additions are to be made. Such reasonable addition is the sum of two amounts—(1) the amount determined under section 166(c) to be the reasonable addition to the reserve for losses on nonqualifying loans, plus (2) the amount determined by the taxpayer to be a reasonable addition to the reserve for losses on qualifying real property loans (but the amount so determined by the taxpayer is not to exceed the amount determined under pars. (2), (3), or (4) of sec. 593(b), whichever amount is the largest). Senate amendment No. 48 adds a further limitation providing that the amount of the addition for a taxable year to the reserve for losses on qualifying real property loans, when added to the amount of the addition to the reserve for losses on nonqualifying loans, shall in no case be greater than the amount by which 12 percent of the total deposits or withdrawable accounts of depositors of the taxpayer at the close of such year exceeds the sum of its surplus, undivided profits, and reserves at the beginning of such year (taking into account any portion thereof attributable to the period before the first taxable year beginning after December 31, 1951). The House recedes with a substitute for the Senate amendment which provides, in effect, that the 12-percent ceiling is not to apply in the case of a taxpayer using the experience method for the taxable year.

Amendments Nos. 50 and 52: Under section 593(b)(2) of the code as amended by the bill as passed by the House, the amount of the

reasonable addition to the reserve for losses on qualifying real property loans for a taxable year was limited to the excess of an amount equal to 60 percent of the taxable income for such year over the amount determined under section 166(c) to be a reasonable addition to the reserve for losses on nonqualifying loans. For purposes of this method, taxable income is determined without regard to any deduction for any additions to the reserves for bad debts, and also by excluding from gross income any amount included therein by reason of subsection (f) (relating to the treatment of certain distributions of property to stockholders by a domestic building and loan association).

Senate amendment No. 50 provided that, in the case of a domestic building and loan association having capital stock with respect to which any distribution of property is not allowable as a deduction under section 591 (relating to dividends paid on deposits), an amount equal to 50 percent of the taxable income is substituted for the 60 percent provided by the bill as passed by the House. The Senate recedes.

Senate amendment No. 52 provides that the amount of the addition determined under section 593(b)(2) is not to exceed the amount necessary to increase the balance (as of the close of the taxable year) of the reserve for losses on qualifying real property loans to 6 percent of such loans outstanding at such time. The House recedes.

Amendment No. 54: Under section 593(b)(3) of the code as amended by the bill as passed by the House, the amount of the reasonable addition to the reserve for losses on qualifying real property loans for a taxable year was limited to an amount equal to the amount necessary to increase the balance (as of the close of the taxable year) of such reserve to 3 percent of such loans outstanding at such time. Senate amendment No. 54 permits the balance of the reserve for losses on qualifying real property loans to be increased to a larger amount in the case of a mutual savings institution which is a new company and which does not have capital stock with respect to which distributions of property are not allowable as a deduction under section 591 of the code. This larger amount is the sum of two amounts: (1) 3 percent of qualifying real property loans outstanding at the close of the taxable year, plus (2) an amount equal to 2 percent of so much of such loans as does not exceed \$4,000,000, reduced (but not below zero) by the amount, if any, of the balance (as of the close of such year) of the taxpayer's supplemental reserve for losses on loans. A taxpayer is a "new company" for any taxable year only if such taxable year begins not more than 10 years after the first day on which it (or any predecessor) was authorized to do business as a mutual savings institution described in section 593(a) of the code.

The House recedes with an amendment. Under the conference action the text of section 593(b)(3) of the code is the same as it is under Senate amendment numbered 54. In addition, under the conference action the new section 593(b)(5) of the code provides that in the case of certain domestic building and loan associations there will be a reduction in the amount determined under paragraph (2) (60 percent of taxable income method) and paragraph (3) (percentage of real property loans method) of section 593(b). For purposes of computing this reduction, the amount determined under paragraph (2), and the amount determined under paragraph (3), shall in each case be the amount determined without regard to the new section 593(b)(5), but with regard to the 12-percent ceiling added by Senate amendment

numbered 48 and, in the case of the amount determined under paragraph (2), the 6-percent ceiling added by Senate amendment numbered 52. The reduction provided by the new section 593(b)(5) will apply only in the case of a domestic building and loan association which qualifies as such for the taxable year solely by reason of the second sentence of section 7701(a)(19) (see the discussion of Senate amendment numbered 60), which changes the 36-percent requirement of subparagraph (E) of the first sentence of section 7701(a)(19) to a 41-percent requirement. The reduction varies from one-twelfth to five-twelfths, depending on the number of percentage points (and fractions thereof) by which the association fails to satisfy the 36-percent requirement.

Amendment No. 56: Section 593(c) of the code, as amended by the bill as passed by the House provides for the allocation of pre-1963 reserves (that is, the net amount, determined as of December 31, 1962, accumulated in the reserve for bad debts for taxable years beginning after December 31, 1951)—

(1) first, to the reserve for losses on nonqualifying loans, to the extent such reserve is not increased above the amount which would be a reasonable addition under section 166(c) of the code for a period in which such loans increased from zero to the amount outstanding at the close of 1962,

(2) second, to the reserve for losses on qualifying real property loans, to the extent such reserve is not increased above the amount equal to 3 percent of the loans outstanding at the close of 1962 or, if larger, the amount which would be a reasonable addition under section 166(c) of the code for a period in which such loans increased from zero to the amount outstanding at the close of 1962, and

(3) then to a supplemental reserve for losses on loans.

Senate amendment No. 56 adds a new paragraph (5) to section 593(c) providing, in effect, that if the pre-1963 reserves are insufficient to bring the balance of the reserve for qualifying real property loans up to the amount referred to in paragraph (2) above then the term "pre-1963 reserves" includes so much of the surplus, undivided profits, and bad debt reserves (determined as of Dec. 31, 1962) attributable to the period before the first taxable year beginning after December 31, 1951, as is necessary to bring the balance of the reserve for qualifying real property loans up to the amount referred to in paragraph (2) above. This rule is to apply only for the purpose of determining reasonable additions under the amended section 593 to such reserve, and for such purpose the amount so allocated is to be treated as remaining in such reserve. The House recedes.

Amendment No. 60: Section 7701(a)(19) of the code defines the term "domestic building and loan association" as a domestic building and loan association, a domestic savings and loan association, and a Federal savings and loan association, substantially all of the business of which is confined to making loans to members.

The bill as passed by the House amended section 7701(a)(19) to provide that the term "domestic building and loan association" means any domestic building and loan association, domestic savings and loan association, and Federal savings and loan association which met each of two requirements. The first requirement was that the association be either (i) an insured institution within the meaning of section 401(a) of the National Housing Act, or (ii) subject by law to supervision and

examination by State or Federal authority having supervision over such associations. The second requirement was that substantially all of the business of the association must consist of accepting savings and investing the proceeds in (i) loans secured by an interest in real property which is, or from the proceeds of the loan will become, residential real property, and (ii) other loans to the extent they would be authorized to be made by a Federal savings and loan association under section 5(c) of the Home Owners' Loan Act of 1933.

Senate amendment No. 60 adopts without change the first requirement of the bill as passed by the House, but replaces the second requirement with six new requirements:

(1) Substantially all of the business of the association must consist of acquiring the savings of the public and investing in loans described in paragraph (2) below.

(2) At least 90 percent of the amount of the total assets (determined as of the close of the taxable year) of the association must consist of (i) cash, (ii) obligations of the United States, a State, or a political subdivision of a State, stock or obligations of a corporation which is an instrumentality of one of those governmental units, and certificates of deposit in, or obligations of, a corporation organized under a State law which specifically authorizes such corporation to insure the deposit or share accounts of member associations, (iii) loans secured by an interest in real property and loans made for the improvement of real property, (iv) loans secured by a deposit or share of a member, (v) property acquired through the liquidation of defaulted loans described in clause (iii) of this paragraph, and (vi) property used by the association in the conduct of the business described in paragraph (1) above.

(3) Of the assets taken into account as assets constituting the 90 percent of total assets, at least 80 percent of such 90 percent must consist of (i) assets of the types described in clauses (i) and (ii) of paragraph (2) above, and (ii) loans secured by an interest in real property which is, or from the proceeds of the loan will become, residential real property or real property used primarily for church purposes, loans made for the improvement of residential real property or real property used primarily for church purposes, or property acquired through the liquidation of defaulted loans described in this paragraph.

(4) Of the assets taken into account as assets constituting the 90 percent of total assets, at least 60 percent of such 90 percent must consist of (i) assets of the types described in clauses (i) and (ii) of paragraph (2) above, and (ii) loans secured by an interest in real property which is, or from the proceeds of the loan will become, residential real property containing four or fewer family units or real property used primarily for church purposes, loans made for the improvement of residential real property containing four or fewer family units or real property used primarily for church purposes, or property acquired through the liquidation of defaulted loans described in this paragraph.

(5) Not more than 18 percent of the amount of the total assets (determined as of the close of the taxable year) of the association may consist of assets other than those referred to in paragraph (3) above, and not more than 36 percent of the amount of such total assets may consist of assets other than those referred to in paragraph (4) above.

(6) Except for property described in paragraph (2) above, not more than 3 percent of the total assets of the association may consist of stock of any corporation.

Senate amendment No. 60 also provides that, at the election of the association, the percentages specified in paragraph (2) through (6) above shall be applied on the basis of the average assets outstanding during the taxable year, rather than at the close of the taxable year, as computed under regulations prescribed by the Secretary of the Treasury or his delegate.

The House recedes with amendments. Under the conference action, loans secured by a deposit or share of a member, and property used by the association in the conduct of its savings and loan business, are in effect to be taken into account (1) in the same manner as loans on residential real property for purposes of section 7701(a)(19)(D)(i), and (2) in the same manner as loans on residential real property for four or fewer family units for purposes of section 7701(a)(19)(D)(ii).

Under the conference action, a second sentence and a third sentence are added to section 7701(a)(19). The new second sentence provides that the term "domestic building and loan association" also includes any association which would satisfy the requirements of the first sentence if "41 percent" were substituted for "36 percent" in subparagraph (E) of the first sentence. The new third sentence provides in effect that, except in the case of the association's first taxable year (whenever occurring in the case of a new association) beginning after the date of the enactment of the bill, the modification of the 36-percent requirement is to be available to it for a taxable year only if—

(1) it met the requirements of the first sentence of section 7701(a)(19) for the immediately preceding taxable year, or

(2) it qualified as a domestic building and loan association for the immediately preceding taxable year solely by reason of the second sentence of section 7701(a)(19) and (if the taxable year is the third or any succeeding taxable year of the association beginning after the date of the enactment of the bill) it met the requirements of the first sentence of section 7701(a)(19) for the second preceding taxable year.

Amendment No. 61: The bill as passed by the House repealed the exemption of Federal savings and loan associations from the taxes imposed by sections 4251 and 4261 of the code (relating, respectively, to the excise tax on communications and the excise tax on the transportation of persons). Senate amendment No. 61 amends section 5(h) of the Home Owners' Loan Act of 1933 (12 U.S.C., sec. 1464(h)) so as to eliminate entirely the exemptions from Federal taxes which that section now provides in the case of Federal savings and loan associations.

Under section 4382(a)(2) of the code, capital stock and certificates of indebtedness issued by domestic building and loan associations and cooperative banks are exempt from the documentary stamp taxes imposed by chapter 34 of the code. Senate amendment No. 61 amends section 4382(a)(2) so as to eliminate this exemption insofar as it extends (i) to all certificates of indebtedness issued by a domestic building and loan association or cooperative bank, and (ii) to shares or certificates of stock issued by such a domestic building and loan association or cooperative bank, to the extent that such shares or certificates of stock do not represent deposits or withdrawable accounts.

The House recedes with clerical and clarifying amendments.

Amendment No. 62: This Senate amendment adds a new provision to the bill as passed by the House which would amend section 591 of the code (relating to the deduction for dividends paid on deposits by mutual savings banks, cooperative banks, and domestic building and loan associations) so as to make clear that a deduction will be allowable under section 591 for (1) interest paid or credited to the accounts of depositors or holders of accounts on their deposits or withdrawable accounts by mutual savings banks, cooperative banks, and domestic building and loan associations, and (2) dividends and interest described in section 591 paid by a savings institution chartered and supervised as a savings and loan or similar association under Federal or State law. The House recedes.

Amendment No. 64: Under the bill as passed by the House, the change in the definition of the term "domestic building and loan association" would have taken effect on the enactment of the bill. Senate amendment No. 64 adds a new provision under which the new definition will apply to taxable years beginning after the date of the enactment of the bill. The House recedes.

Amendment No. 65: The bill as passed by the House provided an effective date of July 1, 1962, for the termination of the exemption of domestic building and loan associations from the excise taxes on communications and transportation of persons. Senate amendment No. 65 provides an effective date of January 1, 1963, for the termination, resulting from Senate amendment No. 61 of exemptions from Federal taxes. The House recedes.

DISTRIBUTIONS BY FOREIGN TRUSTS

Amendment No. 69: The bill as passed by the House defined the term "foreign trust created by a United States person" (for purposes of the provisions of the bill relating to distributions by foreign trusts) as, in general, a foreign trust to which money or property has been transferred directly or indirectly by a United States person, or under the will of a decedent who at the date of his death was a United States citizen or resident. Senate amendment No. 69 provides that such term means that portion of a foreign trust attributable to money or property transferred directly or indirectly by such a person or under the will of such a decedent. The House recedes with clerical amendments.

Amendment No. 70: Under the bill as passed by the House, the amendments to subchapter J of chapter 1 of the code with respect to distributions by foreign trusts were to apply with respect to distributions made in taxable years of trusts beginning after the date of the enactment of the bill. Senate amendment No. 70 provides that these amendments are to apply with respect to distributions made after December 31, 1962. The House recedes.

MUTUAL INSURANCE COMPANIES (OTHER THAN LIFE, MARINE, AND CERTAIN FIRE OR FLOOD INSURANCE COMPANIES)

Amendments Nos. 75 and 76: These are amendments to conform, in the case of insurance companies subject to tax under part II of subchapter L of chapter 1 of the code, the normal tax rates on mutual insurance company taxable income and on taxable investment income to the action taken by the Congress in the Tax Rate Extension Act of 1962. The House recedes.

Amendments Nos. 79, 80, 81, 82, and 102: Under existing law and under the bill as passed by the House, mutual insurance companies other than life or marine are exempt from income tax if the gross amount received from specified items does not exceed \$75,000. Under the bill as passed by the House, if this gross amount is over \$75,000 but less than \$125,000, the alternative tax imposed by the new section 821(c)(1) of the code on small companies is proportionately reduced. Under Senate amendment No. 102, a mutual insurance company other than life or marine is exempt from income tax if the gross amount does not exceed \$150,000. Senate amendments Nos. 79, 80, 81, and 82 provide for a proportionate decrease in the alternative tax if the gross amount is over \$150,000 but less than \$250,000. The House recedes.

Amendments Nos. 84 and 85: Under the bill as passed by the House, the alternative tax for certain small companies provided by the new section 821(c) of the code applied for a taxable year only if the gross amount referred to in section 821(c)(3) for the taxable year exceeded \$75,000 but did not exceed \$300,000. Under Senate amendments Nos. 84 and 85 the \$75,000 and \$300,000 amounts are changed to \$150,000 and \$600,000, respectively. The House recedes on Senate amendment No. 84. The House recedes on Senate amendment No. 85 with an amendment changing the \$600,000 amount provided by the Senate amendment to \$500,000.

Amendment No. 87: This amendment adds a new subsection (f) to section 821 of the code and provides a special transitional underwriting loss deduction for taxable years beginning after 1962 and before 1968 for mutual insurance companies which were subject to the tax imposed by existing section 821 for the 6 taxable years immediately preceding 1963 and which incurred an underwriting loss for at least 5 of such 6 years. The mutual insurance company taxable income with respect to such a company is reduced each year by the amount by which (1) the sum of the underwriting losses of such company for such 6 years, reduced by the underwriting gain for such years, exceeds (2) the total amount by which mutual insurance company taxable income was reduced under the new subsection (f) for prior taxable years. The House recedes with a substitute under which (1) the new subsection (f) applies only in the case of a company which has been subject to the tax imposed by section 821 for each of the 5 taxable years immediately preceding 1962, and has incurred an underwriting loss for each of such 5 taxable years, and (2) such losses are to be used as an offset only to statutory underwriting income.

Amendments Nos. 90, 91, and 92: Section 823(c) of the code, as added by the bill as passed by the House, provided a special deduction (not to exceed \$6,000 in amount) in determining the statutory underwriting income or loss for the taxable year if the gross amount received from the items specified in section 823(c) does not equal or exceed \$900,000. Under Senate amendments Nos. 90, 91, and 92 this special deduction decreases to zero when the gross amount equals \$1,200,000. The House recedes with an amendment under which the deduction decreases to zero when the gross amount equals \$1,100,000.

Amendments Nos. 93, 94, 95, and 96: Under the bill as passed by the House, paragraph (1) of the new section 824(a) added to the code (relating to deduction to provide protection against losses) provides

that in determining the statutory underwriting income or loss for any taxable year there is to be allowed as a deduction the sum of—

(1) an amount equal to 1 percent of the losses incurred during the taxable year, plus

(2) an amount equal to 25 percent of the underwriting gain for the taxable year, plus

(3) if the concentrated windstorm, etc., premium percentage (as defined in the bill) for the taxable year exceeds 50 percent, an amount determined by applying so much of such percentage as exceeds 50 percent to the underwriting gain for the taxable year.

Under the bill as passed by the House, paragraph (2) of the new section 824(a) defines the term "concentrated windstorm, etc., premium percentage" as the percentage obtained by dividing (A) premiums earned on insurance contracts during the taxable year, to the extent attributable to insuring against losses arising in any one State, from windstorm, hail, flood, earthquake, or similar hazards, by (B) premiums earned on insurance contracts during the taxable year.

Senate amendments Nos. 93 and 94 increase the scope of the coverage of paragraph (3) above and increase the amount of the deduction by striking out the references to 50 percent and inserting in lieu thereof 40 percent. The House recedes.

Senate amendment No. 96 changes the definition of "concentrated windstorm, etc., premium percentage" to permit the percentage to be determined by reference to premiums attributable to insuring against losses arising (1) in any one State, (2) if the taxpayer so elects, within 200 miles of any fixed point selected by the taxpayer, or (3) if the taxpayer so elects, within 400 miles of any fixed point selected by the taxpayer. Senate amendment No. 95 provides that, in the case of a taxpayer making the election described in clause (3) of the preceding sentence, the amount of the deduction allowable by reason of section 824(a)(1)(C) is to be one-half of the amount it would be but for this amendment. The House recedes on Senate amendment No. 96 with an amendment under which the percentage is to be determined by reference to premiums attributable to losses arising either (1) in any one State, or (2) within 200 miles of any fixed point selected by the taxpayer. The Senate recedes on Senate amendment No. 95.

Amendments Nos. 97, 98, and 99: Subsection (d) of the new section 824 of the code, as added by the bill, sets forth the amounts which are to be subtracted from the protection against loss account. These amounts are taken into account for purposes of determining mutual insurance company taxable income.

Under the bill as passed by the House, the first subtraction from the account was to be made for so much of the statutory underwriting loss as was generated either by the deduction for dividends to policyholders or by the deduction provided in section 824(a) for protection against losses. Thus, under the bill as passed by the House, any underwriting loss attributable to policy dividends could not be applied against taxable investment income unless the balance in the protection against loss account had first been reduced to zero.

The effect of Senate amendments Nos. 97, 98, and 99 is to permit any portion of the statutory underwriting loss attributable to the deduction for dividends to policyholders to be first applied against

taxable investment income. The House recedes on Senate amendments Nos. 97 and 98, and recedes on Senate amendment No. 99 with a clerical amendment.

Amendment No. 100: New section 826 of the code, as added by the bill, in effect permits a mutual insurance company which is an inter-insurer or reciprocal underwriter to elect to combine certain income of its attorney-in-fact with its own underwriting income. If the company so elects, it is credited with so much of the tax paid by the attorney-in-fact as is attributable to such income of the attorney-in-fact. Under the bill as passed by the House, subsection (d) of section 826 provided, in effect, that the protection against loss deduction of the reciprocal making the election and the addition to its protection against loss account were to be computed without regard to the election. Senate amendment No. 100 strikes out this provision, thus permitting the protection against loss deduction, and the amount added to the protection against loss account, to reflect amounts attributable to such income of the attorney-in-fact. The amendment inserts a new subsection (d) providing, in effect, that no part of the amount added to the protection against loss account by reason of the election by the reciprocal may remain in the account (and thus be subject to tax deferral) for more than 5 years. The House recedes.

Amendment No. 104: Under this amendment (and Senate amendment No. 74) mutual flood insurance companies are to be taxed under part III of subchapter L of chapter 1 of the code (which imposes a tax on certain marine and mutual fire insurance companies and on certain stock insurance companies which are not life insurance companies).

The House recedes with technical conforming amendments making it clear that the taxation of these mutual flood insurance companies (and of their subscribers or policyholders) is to be the same as the present tax treatment of so-called factory mutuals (and of their policyholders).

DOMESTIC CORPORATIONS RECEIVING DIVIDENDS FROM FOREIGN CORPORATIONS

Amendments Nos. 111 and 113: These amendments deal with (1) the method to be used for determining the amount of foreign income tax deemed to have been paid by domestic corporations with respect to dividends received from foreign corporations for purposes of the allowance of a foreign tax credit under section 902 of the code, and (2) the amount to be treated as received as a dividend by reason of the tax so deemed paid. Under the bill as passed by the House, the entire amount of foreign income tax of the foreign corporation was to be taken into account in determining the foreign income tax deemed to be paid by the domestic corporation, and (under new sec. 78) an amount equal to the taxes deemed paid was required to be included in income as a dividend. Senate amendment No. 111 would (A) retain existing law with respect to dividends paid by a foreign corporation out of accumulated profits of a year for which it is a "less developed country corporation," and (B) provide, with respect to all other dividends paid by a foreign corporation, the same rules as were provided by the bill as passed by the House. Under Senate amendment No. 113, the new section 78 is amended to exclude from the application of the new section 78 dividends referred to in clause (A) above. The House recedes on Senate amendments Nos. 111 and 113.

SEPARATE LIMITATION ON FOREIGN TAX CREDIT WITH RESPECT TO
CERTAIN INTEREST INCOME

Amendment No. 121: Section 904 of the code provides a per-country limitation on the amount of the foreign tax credit or (at the election of the taxpayer) an overall limitation may be applied. Senate amendment No. 121 adds a new section to the bill to provide a separate limitation on the foreign tax credit with respect to certain interest income. Under the amendment, (1) the foreign tax credit limitations are to be applied separately with respect to (A) certain interest income, and (B) income other than such interest income, and (2) the overall limitation is not to apply to such interest income. The interest income referred to is any interest other than—

(A) interest derived from any transaction which is directly related to the active conduct of a trade or business in a foreign country or a possession of the United States,

(B) interest derived in the conduct of a banking, financing, or similar business,

(C) interest received from a corporation in which the taxpayer owns at least 10 percent of the voting stock, and

(D) interest received on obligations acquired as a result of the disposition of a trade or business actively conducted by the taxpayer in a foreign country or a possession of the United States or as the result of the disposition of stock or obligations of a corporation in which the taxpayer owned at least 10 percent of the voting stock.

The amendment requires the Secretary of the Treasury or his delegate by regulations to prescribe the manner of applying foreign tax credit carrybacks and carryovers where the taxpayer elects the overall limitation as to other income and provides transitional rules (1) for foreign tax credit carrybacks from years to which the new provisions apply to years to which they do not apply, and (2) for foreign tax credit carryovers from years to which the new provisions do not apply to years to which they do apply. The new provisions are to apply with respect to taxable years beginning after the date of the enactment of the bill, but only with respect to interest resulting from transactions consummated after April 2, 1962. The House recedes.

EARNED INCOME FROM SOURCES WITHOUT THE UNITED STATES

Amendment No. 123: This amendment adds a new paragraph (6) to section 911(c) of the code as contained in the bill as passed by the House. Section 911(c) contains special rules for determining the amount of earned income from sources without the United States which is excludable from gross income. The new paragraph (6) provides that a statement by an individual who has earned income from sources within a foreign country to the authorities of that country that he is not a resident of that country, if he is held not subject as a resident of that country to the income tax of that country by its authorities with respect to such earnings, shall be conclusive evidence with respect to such earnings that he is not a bona fide resident of that country for purposes of section 911(a)(1). The House recedes.

Amendment No. 124: This amendment adds a new paragraph (7) to section 911(c) of the code as contained in the bill as passed by the

House. Under the new paragraph (7), if an individual who qualifies as a bona fide resident of a foreign country receives compensation from sources without the United States (except from the United States or any agency thereof) in the form of the right to use property or facilities, the \$20,000 or \$35,000 limitation applicable with respect to such individual (A) for a taxable year ending in 1963, is to be increased by an amount equal to the amount of such compensation so received during such taxable year; (B) for a taxable year ending in 1964, is to be increased by an amount equal to two-thirds of such compensation so received during such taxable year; and (C) for a taxable year ending in 1965, is to be increased by an amount equal to one-third of such compensation so received during such taxable year. The House recedes.

Amendment No. 125: The bill as passed by the House provided that the amendment made to section 911 of the code was to apply to taxable years ending after December 31, 1962, but only with respect to amounts received after December 31, 1962, which were attributable either to (A) services performed after December 31, 1962, or (B) services performed on or before December 31, 1962, but only if on March 12, 1962, there existed no right (whether forfeitable or nonforfeitable) to receive such amounts. Senate amendment No. 125 provides that the amendment made to section 911 of the code will apply to taxable years ending after September 4, 1962, but only with respect to (1) amounts received after March 12, 1962, which are attributable to services performed after December 31, 1962, or (2) amounts received after December 31, 1962, which are attributable to services performed on or before December 31, 1962, unless on March 12, 1962, there existed a right (whether forfeitable or nonforfeitable) to receive such amounts. The House recedes.

CONTROLLED FOREIGN CORPORATIONS

Amendment No. 126: The bill as passed by the House added a new subpart F to part III of subchapter N of chapter 1 of the code (relating to income from sources without the United States). The new subpart F (relating to controlled foreign corporations) provided rules under which a United States person who owns stock in a controlled foreign corporation would be required to include in his gross income a pro rata share of certain portions of the controlled foreign corporation's income. Senate amendment No. 126 struck out these provisions of the bill as passed by the House and inserted new text in the nature of a substitute which adds a new subpart F (relating to controlled foreign corporations) and a new subpart G (relating to export trade corporations). Under the conference agreement, the House recedes with amendments, which, except as discussed below in paragraph (m) relating to receipt of minimum distributions, are either technical or clerical. The more important differences between the bill as passed by the House and the Senate amendment as agreed to in conference are explained below.

(a) *Amounts included in gross income.*—The bill as passed by both the House and the Senate provides, in general, that a U.S. person who owns, or is considered to own, 10 percent or more of the total combined voting power of all classes of stock entitled to vote of a controlled foreign corporation is required to include in his gross income his pro rata share of (1) the subpart F income of the foreign corporation, (2)

previously excluded subpart F income withdrawn from investment in less developed countries, and (3) the increase in earnings of the foreign corporation invested in certain property ("nonqualified property" in the bill as passed by the House, and limited to "United States property" in the Senate amendment). Under the bill as passed by the House, this provision applied if the foreign corporation was a controlled foreign corporation on any one day of the taxable year. Senate amendment No. 126 requires that the foreign corporation be a controlled foreign corporation for an uninterrupted period of 30 days or more during its taxable year. The bill as passed by both the House and the Senate defines U.S. persons to mean, in general, citizens or residents of the United States, domestic partnerships and corporations, and any estate or trust (other than a foreign estate or trust). However, Senate amendment No. 126, in cases relating to certain corporations organized in the Commonwealth of Puerto Rico or possessions of the United States, excludes from the definition of U.S. persons certain individual citizens of the United States who are bona fide residents in the Commonwealth of Puerto Rico or the possession of the United States in which the corporation is created or organized.

(b) *Subpart F income.*—

(1) *Amounts included.*—The bill as passed by both the House and the Senate included within the term "subpart F income" the foreign base company income of a controlled foreign corporation and the income of a controlled foreign corporation derived from the insurance of U.S. risks. The bill as passed by the House also included in the subpart F income of a controlled foreign corporation income of such corporation derived from U.S. patents, copyrights, and exclusive formulas and processes if such properties were substantially developed, created, or produced in the United States or were acquired from a related U.S. person. Senate amendment No. 126 does not include such income in subpart F income. However, see amendment No. 161 for a provision that gain on the sale or exchange of such property to a foreign corporation controlled by the transferor is to be taxable as ordinary income.

(2) *Limitations on subpart F income.*—The bill as passed by both the House and Senate provided that the subpart F income of a controlled foreign corporation could not exceed the earnings and profits for the taxable year. Senate amendment No. 126 provides that, for purposes of this limitation, the earnings and profits for any taxable year is to be reduced by deficits in earnings and profits for taxable years of the controlled foreign corporation beginning after December 31, 1962 (and certain deficits in earnings and profits for taxable years beginning after December 31, 1959, and before January 1, 1963) and, under regulations prescribed by the Secretary of the Treasury or his delegate, by deficits in earnings and profits of other corporations in a chain of ownership which includes the controlled foreign corporation.

(c) *Income derived from insurance of U.S. risks.*—The bill as passed by both the House and the Senate provides that subpart F income includes income of a controlled foreign corporation derived from the insurance or reinsurance of property in the United States or of lives or health of residents of the United States. However, under Senate amendment No. 126 this provision applies only if the premiums or other consideration received or accrued in respect of such insurance or reinsurance by a controlled foreign corporation represents more than 5 percent of total premiums and other consideration.

(d) *Foreign base company income.*—The bill as passed by both the House and the Senate provides that the term “foreign base company income” means the sum of the foreign personal holding company income (discussed in paragraph (e) below) and the foreign base company sales income (discussed in paragraph (f) below) of a controlled foreign corporation. Senate amendment No. 126 also includes foreign base company services income (discussed in paragraph (g) below) within the defined term.

(e) *Foreign personal holding company income.*—The bill as passed by both the House and the Senate provides that subpart F income of a foreign corporation includes foreign personal holding company income, with certain modifications. The bill as passed by the House provided for an exclusion in the case of personal holding company income of certain banks. The Senate amendment provides for an exclusion from personal holding company income of: (i) rents and royalties derived from the active conduct of a trade or business, if received from an unrelated person; (ii) dividends, interest, and certain gains derived in the conduct of a banking, financing, or similar business, or derived by an insurance company on investments of unearned premiums or certain reserves, if received from an unrelated person; (iii) dividends and interest received from related persons if such persons are organized, and have a substantial part of their assets, within the country of incorporation of the controlled foreign corporation; (iv) interest received in the conduct of a banking, financing, or similar business from a related person also engaged in the conduct of a banking, financing, or similar business, if the businesses of both the recipient and payor are predominantly with unrelated persons; and (v) rents, royalties, and similar amounts received from a related person for the use of, or the privilege of using, property within the country of incorporation of the controlled foreign corporation.

(f) *Foreign base company sales income.*—The bill as passed by both the House and the Senate provides that subpart F income of a controlled foreign corporation includes income, whether in the form of profits, commissions, fees, or otherwise, derived by a controlled foreign corporation in connection with the purchase of property from a related person, or sale of property to a related person, when the property sold was neither manufactured in, nor sold for use, consumption, or disposition in, the country in which the controlled foreign corporation is organized. The Senate amendment provides that foreign branches of a controlled foreign corporation shall, under certain circumstances, be treated as wholly owned subsidiary corporations for purposes of determining the foreign base company sales income of the controlled foreign corporation, and treats foreign base company sales income of the branch as foreign base company sales income of the controlled foreign corporation.

The bill as passed by the House provided for a reduction of foreign base company sales income by an amount equal to the increase in qualified investments in less developed countries. Moreover, the bill as passed by the House provided that foreign base company sales income would be includible in subpart F income only if such income amounted to at least 20 percent of gross income (not including other foreign base company income). Senate amendment No. 126 contains neither provision. However, see the discussion below under paragraph (h) relating to exclusions from foreign base company income.

(g) *Foreign base company services income.*—Senate amendment No. 126 provides that subpart F income of a controlled foreign corporation includes income, whether in the form of compensation, commissions, fees, or otherwise, derived by a controlled foreign corporation in connection with the performance of technical, managerial, engineering, or like services if such services are performed for a related person and are performed outside the country of incorporation of the controlled foreign corporation, and if such income is not related to certain selling activities. The bill as passed by the House did not contain any similar provision.

(h) *Exclusions from foreign base company income.*—The bill as passed by the House provided that no part of the gross income of a controlled foreign corporation would be treated as foreign base company income if such income was less than 20 percent of gross income, and that the entire gross income of such a corporation would be treated as foreign base company income if such income exceeded 80 percent of gross income. Senate amendment No. 126 changes these percentages to 30 percent and 70 percent, respectively. The bill as passed by the House also provided, in general, that foreign base company income was to be reduced by an amount equal to the increased investment in certain less developed country properties, including stock of a foreign corporation engaged in business almost wholly within less developed countries if substantially all the property of such corporation was ordinary and necessary for the active conduct of such trade or business. Senate amendment No. 126 provides that foreign base company income does not include dividends and interest received from qualified investments in less developed countries, and net gain from the sale or exchange of such investments to the extent such dividends, interest, and gains do not exceed the increased investment of a controlled foreign corporation, for the taxable year, in qualified investments in less developed countries. The Senate amendment also provides that foreign base company income does not include income of a controlled foreign corporation derived from the use of any aircraft or vessel in foreign commerce, or from services directly related to such use.

(i) *Withdrawal of previously excluded subpart F income from qualified investments.*—As noted in paragraph (h) above, Senate amendment No. 126 provides that dividends, interest, and gains derived from qualified investments in less developed countries are excluded from foreign base company income to the extent of the increased investment for the taxable year, in qualified investments in less developed countries. Amounts once excluded from foreign base company income under this provision are, however, included in gross income of U.S. shareholders when there is a decrease in qualified investments in less developed countries.

(1) *Qualified investments in less developed countries.*—The Senate amendment defines the term “qualified investments in less developed countries” to mean (A) stock of a less developed country corporation, but only if the controlled foreign corporation which makes the investment owns 10 percent or more of the stock of such corporation, (B) an obligation of a less developed country corporation which at the time acquired by the controlled foreign corporation has a maturity of 1 year or more, but only if the controlled foreign corporation which makes the investment owns 10 percent or more of the stock of such corporation, and (C) obligations of a less developed country. How-

ever, if any such investment is disposed of within 6 months after the date of its acquisition, it is not to be treated as a qualified investment.

(2) *Less developed country corporations.*—Senate amendment No. 126 defines the term “less developed country corporation” to mean a foreign corporation engaged in the active conduct of a trade or business if (A) such corporation derives 80 percent or more of its gross income from sources within less developed countries, and (B) 80 percent or more of the assets of such corporation consists of (i) property located in less developed countries if used in an active trade or business, (ii) stock of any other less developed country corporation, (iii) obligations of less developed country corporations which at the time of their acquisition have a maturity of 1 year or more, (iv) obligations of a less developed country, and (v) certain other investments, including certain permissible investments in the United States. The Senate amendment also provides that the term “less developed country corporation” includes a foreign corporation (1) which, in general, derives 80 percent or more of its gross income (A) from the use in foreign commerce of aircraft or vessels registered under the laws of a less developed country, (B) from the performance of services directly related to such aircraft or vessels, (C) from the sale or exchange of such aircraft or vessels, and (D) from dividends and interest received from other less developed country corporations (within the meaning of this sentence) in which the recipient owns 10 percent or more of the voting stock, and from gain from the sale or exchange of stock or obligations of such other less developed country corporations, and (2) 80 percent or more of the assets of which consists of assets used in connection with the production of income described in (1) above, and of certain permissible investments in the United States.

(j) *Increase in investments in certain property.*—The bill as passed by the House provided for the inclusion in gross income of U.S. shareholders of earnings and profits of a controlled foreign corporation invested in nonqualified property to the extent of a shareholder's pro rata share of the increase in such investments for the taxable year. As defined in the bill as passed by the House, nonqualified property meant (1) property located in the United States, with certain exceptions, but including stock in a domestic corporation or an obligation of a U.S. person, and (2) property other than property ordinary and necessary for the active conduct of a trade or business (or for a substantially similar trade or business) carried on by the controlled foreign corporation outside the United States, if (A) the business had been carried on since December 31, 1962, or for a 5-year period ending at the close of the preceding taxable year, or (B) the business was carried on almost wholly within less developed countries. Senate amendment No. 126 includes only the first category of nonqualified property defined in the Senate amendment as “United States property”.

(k) *Controlled foreign corporations.*—The bill as passed by the House provided that a foreign corporation would be considered a controlled foreign corporation if more than 50 percent of the total combined voting power of all classes of its stock entitled to vote was owned by U.S. persons on any day during the taxable year of such corporation. Under Senate amendment No. 126, a foreign corporation is a controlled foreign corporation only if U.S. shareholders (defined as a U.S. person who owns, with the application of special rules of ownership continued in the Senate amendment, 10 percent or more of the stock

of a foreign corporation) on any day during the taxable year of such corporation owned more than 50 percent of the total combined voting power of all classes of stock entitled to vote of such corporation. Senate amendment No. 126 also provides that a corporation organized in the Commonwealth of Puerto Rico or a possession of the United States is excluded from the term "controlled foreign corporation" if the corporation is primarily engaged in the active conduct of specified trades or businesses in the Commonwealth of Puerto Rico or a possession of the United States and derives its income from specified sources.

(l) *Individuals subject to tax at corporate rates.*—Senate amendment No. 126 provides that a U.S. shareholder who is an individual may elect to limit his U.S. tax liability with respect to amounts which are includible in his gross income under the new subpart F by using the rates provided by section 11 of the code applicable in the case of a domestic corporation, and by applying the provisions of section 960 (relating to foreign tax credit). A U.S. shareholder who makes an election under this provision must, in the year of actual distribution of an amount previously taxed under subpart F, include an amount in gross income equal to the amount distributed reduced by U.S. tax previously paid with respect to such amount.

(m) *Receipt of minimum distributions.*—Senate amendment No. 126 provides that if a given percentage of the earnings and profits of a controlled foreign corporation is distributed, a domestic corporate shareholder may elect to exclude from its gross income its share of the amount of subpart F income of such controlled foreign corporation. A domestic corporate shareholder may elect to apply the minimum distribution provision on the basis of (1) any controlled foreign corporation in which it owns stock directly, (2) controlled foreign corporations in a chain of ownership, or (3) all controlled foreign corporations. In the case of an election with respect to all controlled foreign corporations, the domestic corporation may also elect (A) to exclude, under certain circumstances, less developed country corporations, and (B) to treat its foreign branches as controlled foreign corporations, for purposes of this provision. The required minimum distribution decreases as the effective foreign tax rate increases, with the result that the sum of the amount of foreign tax paid by the foreign corporations, and the U.S. tax paid by the shareholders on distributions of current earnings and profits of such corporations, produces an overall effective tax on current foreign profits equal to approximately 90 percent of the tax that would have been paid had the foreign corporations been taxable as domestic corporations. Under the conference agreement, a new table of minimum distributions, which permits less variation from this 90-percent requirement, is substituted for the table contained in Senate amendment No. 126. Under Senate amendment No. 126, an affiliated group of corporations eligible to file a consolidated return under section 1501 of the code could elect to be treated as a single corporation for purposes of applying the minimum distribution provision. Under the conference agreement, this election may be made only if the affiliated group actually files such a consolidated return for the taxable year.

(n) *Export trade corporations.*—Senate amendment No. 126, which adds a new subpart G to part III of subchapter N of chapter 1 of the code, provides that the subpart F income of a controlled foreign corporation which is an export trade corporation shall be reduced by the export trade income of such corporation which constitutes foreign

base company income. In general, this provision applies to controlled foreign corporations which derive more than 75 percent of their gross income from (1) the sale of property produced in the United States to unrelated persons for use outside the United States, (2) the performance of certain services outside the United States for unrelated persons, (3) the use of export property by unrelated persons, and (4) the receipt of interest on obligations which qualify as export trade assets. However, the amount of export trade income which reduces subpart F income is limited to the lesser of (1) an amount equal to $1\frac{1}{2}$ times certain export promotion expenses of the controlled foreign corporation, or (2) an amount equal to 10 percent of the gross receipts of such corporation from the transactions described above. In addition, the amount of export trade income which reduces subpart F income can in no event exceed an overall limitation based on the increase in investments in export trade assets.

(o) *Miscellaneous.*—The committee of conference was informed by the Treasury Department of the policy it plans to follow in the granting of rulings under section 367 of the Internal Revenue Code of 1954 in situations in which taxpayers seek to reorganize, during a reasonable period after the enactment of the bill, their foreign corporate structures in response to the enactment of section 12 of the bill as agreed to in conference.

The Treasury Department, for purposes of section 367, will not treat a transaction involving the reorganization of foreign corporate structures as being in pursuance of a plan having as one of its principal purposes the avoidance of Federal income taxes solely by reason of the fact that a principal purpose of the reorganization is to terminate a method of operation which would result in tax to U.S. shareholders under the provisions of section 12 of the bill. In such cases a favorable ruling under section 367 will generally not be denied by the Treasury Department in transactions in which earnings and profits of foreign corporations are carried over to other foreign corporations under circumstances in which there will be no reduction of the U.S. taxes (and foreign taxes) that would be payable on the eventual remittance of such earnings and profits to U.S. shareholders.

Under present administrative rules, where corporate shareholders are involved the Treasury Department generally does not issue rulings under section 367 which permit the tax-free remittance to the United States of earnings and profits of foreign corporations. However, under existing practice a ruling permitting a tax-free exchange is generally given subject to a condition that an appropriate amount be included in the income of the domestic shareholder (thus negating the existence of a principal purpose to avoid U.S. tax). Such rulings will continue to be given even though a principal purpose of the transaction is (1) to terminate the activities of a foreign corporation which would result in tax to U.S. shareholders under the provisions of section 12 of the bill, and (2) to carry on such activities in the future through a domestic corporation.

The conferees recognize that the problems in this area are complex and that particular aspects of the policy as explained above may require qualification and refinement as experience is gained in applying it to particular situations.

The conferees on the part of the Senate called attention to the colloquy in the Senate with respect to the amendment offered in the Senate relating to corporations engaged in producing or selling books

or other media of communications, etc. (see pp. 17511-17513 of the daily Congressional Record for Sept. 5, 1962). The conferees were advised that the substance of this amendment was not within the jurisdiction of the conference committee. However, the conferees have requested the Treasury Department to study this matter and report back next year to the Committees on Ways and Means and Finance.

GAIN FROM DISPOSITIONS OF CERTAIN DEPRECIABLE PROPERTY

Amendments Nos. 128, 129, 130, and 131: The bill as passed by both the House and the Senate adds a new section 1245 to the code. In general, the new section provides for the treatment as ordinary income of the gain from the disposition of certain depreciable property to the extent of depreciation deductions (taken in periods specified in the bill) which are reflected in the adjusted basis of the property.

Under the bill as passed by the House, the new section 1245 applied to property disposed of after the date of the enactment of the bill and to the extent of adjustments for depreciation and certain amortization for taxable years beginning after December 31, 1961. Under Senate amendment No. 128, the new section applies to property disposed of during a taxable year beginning after December 31, 1962. Under Senate amendments Nos. 129, 130, and 131, the adjustments taken into account are those attributable to periods after December 31, 1961. The House recedes.

Amendment No. 132: The bill as passed by both the House and the Senate amends section 167 of the code to permit a taxpayer to elect to change his method of depreciation in respect of section 1245 property from any declining balance or sum of the years-digits method to the straight line method. Under the bill as passed by the House, the election was required to be made within the period after the date of the enactment of the bill prescribed by the Secretary of the Treasury or his delegate. Under Senate amendment No. 132, the election must be made by the taxpayer on or before the last day prescribed by law (including extensions thereof) for filing his return for his first taxable year beginning after December 31, 1962. The House recedes.

Amendment No. 133: This amendment adds a new provision to the bill inserting a new sentence after the second sentence of section 613(a) of the code, relating to the general rule for computing percentage depletion. The new sentence, which does not affect the computation of the gross income from the property under the first sentence of section 613(a), provides that the allowable deductions taken into account with respect to expenses of mining in computing the taxable income from the property shall, for purposes of the 50-percent limitation contained in the second sentence of section 613(a), be decreased by an amount equal to so much of any gain which (1) is treated under new section 1245 of the code (relating to gain from disposition of certain depreciable property) as ordinary income, and (2) is properly allocable to the property. The House recedes.

Amendment No. 135: Under the bill as passed by the House, the amendments made by the bill relating to gain from dispositions of certain depreciable property (new sec. 1245), including the election to change the method of depreciation with respect to section 1245 property, the amount taken into account as salvage value, and the special rule for charitable contributions of section 1245 property, were to apply to taxable years beginning after December 31, 1961,

and ending after the date of the enactment of the bill. Under Senate amendment No. 135, the amendments (except the amendments with respect to salvage value, which take effect as provided by the bill as passed by the House) are to apply to taxable years beginning after December 31, 1962. The House recedes.

FOREIGN INVESTMENT COMPANIES

Amendments Nos. 140 and 141: The bill as passed by both the House and the Senate adds a new section 1246 to the code, relating to gain on foreign investment company stock.

Under the bill as passed by the House, a foreign investment company was defined as any foreign corporation which met one of two alternative tests. Under Senate amendment No. 140, either of these two tests must be met for any taxable year beginning after December 31, 1962. One test is registration under the Investment Company Act of 1940 either as a management company or as a unit investment trust. The second test (which must be met at a time when more than 50 percent of either the voting power or total value of the stock is held by U.S. persons) under the House bill was that the foreign corporation must be engaged (or holding itself out as being engaged) primarily in the business of investing, reinvesting, or trading in securities (within the meaning of section 3(a)(1) of the Investment Company Act of 1940). Senate amendment No. 141, in effect, excludes from the second test certain foreign corporations such as brokers, banks, and small loan companies. The House recedes on Senate amendments Nos. 140 and 141.

Amendment No. 143: Subsection (e)(1) of section 1246 added to the code by the bill provides that the basis of stock of a foreign investment company acquired from a decedent dying after December 31, 1962, is to be reduced by the amount of the decedent's ratable share of earnings and profits. Under the bill as passed by the House, the ratable share was of the accumulated earnings and profits of the company. Under Senate amendment No. 143, the ratable share is of the earnings and profits accumulated after December 31, 1962. The House recedes.

Amendment No. 145: This amendment adds a new subsection (g) to the new section 1246 of the code. The new subsection (g) provides that if a registered foreign investment company has made an election (under the new sec. 1247 added by the bill) to distribute income currently with respect to taxable years beginning after December 31, 1962, then section 367 of the code is not to apply in respect of such foreign investment company if the company is a party to a reorganization in which all of its properties are acquired before January 1, 1964, by a domestic corporation which is a regulated investment company under section 851 for its first taxable year ending after the reorganization. The committee of conference was informed by the Treasury Department that the proposed new subsection was not needed in view of the administrative practices under section 367 of the code, and might therefore imply that such practices are erroneous. The Senate recedes.

Amendment No. 147: New section 1247 added to the code by the bill provides that new section 1246 of the code (treating gain on sale or exchange of foreign investment company stock as ordinary income) is not to apply to the qualified shareholders of a registered foreign investment company if the company elects on or before December

31, 1962, with respect to each taxable year beginning after such date, to distribute 90 percent or more of its taxable income currently and to designate in a written notice to its shareholders the pro rata amount of the excess of the net long-term capital gain over the net short-term capital loss and the portion thereof which is being distributed. Under the bill as passed by the House, the notice must be mailed before the expiration of 30 days after the close of the taxable year. Under Senate amendment No. 147, the notice must be mailed before the expiration of 45 days after the close of the taxable year. The House recedes.

Amendment No. 153: This amendment strikes out subsection (d) of the new section 1247 added to the code by the bill and inserts subsections (d), (e), (f), and (g).

Under the Senate amendment the new subsection (d) requires each qualified shareholder of a foreign investment company with respect to which an election under section 1247 is in effect to compute his long-term capital gains by including his pro rata share of the distributed portion of the company's excess of net long-term capital gain over net short-term capital loss and his pro rata share of the undistributed portion of such excess. Subsection (e) is the same as subsection (d) as passed by the House in requiring proper adjustment in the earnings and profits of the company and in the adjusted basis of stock of such company held by such shareholder to reflect such shareholder's inclusion in gross income of undistributed capital gains, but also requires proper adjustment in a qualified shareholder's ratable share of the company's earnings and profits.

Subsections (f), (g), and (h) are new provisions relating to the election by a foreign investment company with respect to foreign taxes. Under subsection (f), a foreign investment company which has elected to distribute income currently and more than 50 percent of the value of whose total assets at the close of the taxable year consists of stock or securities in foreign corporations may elect (for such taxable year and for purposes of complying with its election to distribute 90 percent or more of its taxable income) to compute its taxable income without any deduction for income, etc., taxes paid to foreign countries or possessions of the United States and to treat the amount of such taxes as distributed to its shareholders. If the election is made each qualified shareholder of the company is required (1) to include in gross income and treat as paid by him his proportionate share of such taxes, and (2) for purposes of the foreign tax credit, to treat such share of taxes as having been paid to the country in which the company is incorporated and to treat as gross income from sources within such country such share of taxes and any dividend paid to him by the company. Subsection (g) provides for notice to the shareholders of their proportionate share of the taxes to be taken into account as provided in subsection (f). Subsection (h) provides that the election and notice are to be made in such manner as the Secretary of the Treasury or his delegate may prescribe by regulations. The House recedes.

GAIN FROM CERTAIN SALES OR EXCHANGES OF STOCK IN CERTAIN FOREIGN CORPORATIONS

Amendments Nos. 159 and 160: The bill as passed by the House added a new section 1248 to the code which provided, in general, that (1) if a U.S. person owned, or was considered to have owned, 10 per-

cent or more of the voting stock of a foreign corporation on the date he sells or exchanges stock in such corporation, or during the 5-year period ending on such date, and (2) the foreign corporation was a controlled foreign corporation on the date of the sale or exchange or during the 5-year period ending on such date, then (1) gain recognized on the sale or exchange, other than in redemption or liquidation of such stock, would, to the extent of the earnings and profits of the corporation attributable to the stock sold or exchanged, be considered gain from the sale of property which is not a capital asset, and (2) gain recognized on a distribution in redemption or liquidation of such corporation would, to the extent of the earnings and profits of the corporation attributable to the stock exchanged, be treated as a dividend. The new section 1248 provided for the reduction in the earnings and profits of a foreign corporation by amounts included in gross income of a U.S. person as subpart F income or as amounts invested in nonqualified property, but only to the extent such amounts did not result in an exclusion from gross income. The bill did not apply to distributions in redemption of stock to pay death taxes, consideration received in an exchange to which section 356 applied, or to amounts includible in gross income under any other provision of the code as a dividend, gain from the sale of an asset which is not a capital asset, or gain from the sale of an asset held for not more than 6 months.

Senate amendment No. 159 provides that (a) if a U.S. person sells or exchanges stock in a foreign corporation (including distributions in redemption or liquidation), and (b) such person owns, or is considered to own, 10 percent or more of the voting stock of such corporation at any time during the 5-year period ending on the date of sale or exchange on a date when such corporation was a controlled foreign corporation, then the gain shall be includible in the gross income of such U.S. person as a dividend, to the extent of the earnings and profits of the foreign corporation accumulated (1) in taxable years of the corporation beginning after December 31, 1962, (2) while the stock sold or exchanged was held by the U.S. person, and (3) while the foreign corporation was a controlled foreign corporation.

Senate amendment No. 159 provides that earnings and profits of a foreign corporation are to be determined according to rules substantially similar to those applicable to domestic corporations, except that the earnings and profits are to be reduced with respect to a U.S. person by amounts included in gross income under section 951, gain realized from the sale or exchange of property in pursuance of a plan of complete liquidation, income derived from sources within the United States of a foreign corporation engaged in trade or business within the United States, amounts included in gross income of a qualified shareholder of a foreign investment company, and, in some cases, by earnings and profits accumulated while the foreign corporation was a less developed country corporation.

Under Senate amendment No. 159, the earnings and profits of a foreign corporation whose stock is sold or exchanged is, under certain circumstances, deemed to include earnings and profits of foreign corporations in a chain of corporations. The Senate amendment also provides that if a domestic corporation was formed or availed of principally for the holding, directly or indirectly, of stock of one or more foreign corporations, the sale or exchange of the stock of the domestic corporation will be treated as a sale or exchange of the stock of the foreign corporation or corporations held by the domestic corporation.

The new section 1248, as amended by Senate amendment No. 159, provides a limitation on the tax imposed on an individual who is a U.S. person by reason of the application of the new section. In general, the tax so imposed is not to exceed the greater of (1) his pro rata share of the taxes which would have been imposed if the foreign corporation had been a domestic corporation during the period he held the stock sold or exchanged, or (2) the taxes which would have been imposed if the amounts to which the section applies had been received as dividends in the years in which earned by the foreign corporation. With respect to Senate amendment No. 159, the House recedes with amendments which (1) eliminate the second limitation described in the preceding sentence, and (2) make clerical and conforming changes.

Under the bill as passed by the House, the new section 1248 applied to sales or exchanges after the date of the enactment of the bill. Senate amendment No. 160 provides that the new section shall apply to sales or exchanges after December 31, 1962. The House recedes.

SALES AND EXCHANGES OF PATENTS, ETC., TO CERTAIN FOREIGN CORPORATIONS

Amendment No. 161: Senate amendment No. 161 adds a new section to the bill which adds a new section 1249 to the code, relating to gain of a U.S. person from the sale or exchange after December 31, 1962, of a patent, invention, model, or design (whether or not patented), copyright, secret formula or process, or similar property right to a foreign corporation which such person controls (within the meaning of the new sec. 1249). If such gain would (but for the new section) be gain from the sale or exchange of a capital asset or of property described in section 1231, then such gain is to be considered as gain from the sale or exchange of property which is neither a capital asset nor property described in section 1231. Under subsection (c) of the new section 1249, the new section would not apply, however, to gain realized from the sale or exchange for stock or contribution to capital of such property where it is established to the satisfaction of the Secretary of the Treasury or his delegate that the principal purpose of the transfer is to enable the foreign corporation to use the property in its own manufacturing operations. The new section 1249 applies to taxable years beginning after December 31, 1962.

Under the conference agreement, the House recedes with an amendment striking out subsection (c) of the new section 1249. With the deletion of subsection (c), the new section 1249 provides ordinary income treatment for all taxable sales or exchanges of patents (and other property covered by the provision) by a domestic corporation to a foreign corporation which it controls. The new section 1249 would not apply to nontaxable transactions such as those sales or exchanges to which (as the result of a ruling under sec. 367) section 351 of the code applies. Neither the enactment of section 1249 nor the deletion of the exception in subsection (c) is intended to have any implications with respect to the application of section 367 of the code to such nontaxable transactions.

The conferees requested the Treasury Department to study and report back on the proper tax treatment of the transfer of patents, etc., to foreign subsidiaries which use such property in their own manufacturing operations.

TAX TREATMENT OF COOPERATIVES AND PATRONS

Amendments Nos. 162, 163, 166, 167, and 168: The bill as passed by the House provides that, in computing the taxable income of a cooperative organization, certain distributions paid to patrons in the form of qualified written notices of allocation are to be treated as deductions from the cooperative's gross income. The recipients of such qualified written notices of allocation are required to include the stated dollar amount of such allocations in their gross income when received. A written notice of allocation is qualified only if (1) it is payable in cash within 90 days at the option of the patron, or (2) the patron has consented to include the stated dollar amount of this written notice of allocation in his gross income. Senate amendment No. 163 contains a further requirement which provides that a written notice of allocation is not a qualified one unless 20 percent or more of the distribution of which it is a part is paid in money or by qualified check.

The bill as passed by the House provides two methods by which a patron may consent to the inclusion in his gross income of the stated dollar amount of qualified written notices of allocation not redeemable in cash within the period provided in the bill. Senate amendments Nos. 162 and 166 provide a third method by which such consent may be made. Under this third method a patron may consent by endorsing and cashing (within the time prescribed by the amendment) a qualified check which is paid as a part of the same distribution as the written notice of allocation. Under Senate amendment No. 167, a qualified check is defined as a check (or other instrument redeemable in money) on which there is a clearly imprinted statement that the endorsement and cashing of the check (or other instrument) constitutes the consent of the payee to include in his gross income, as provided in the Federal income tax laws, the stated dollar amount of the written notice of allocation which is a part of the patronage dividend or payment of which such qualified check is also a part. Under Senate amendment No. 168, if a qualified check is not cashed on or before the 90th day after the close of the payment period for the taxable year with respect to which it is paid, such check becomes a non-qualified written notice of allocation. The House recedes on amendments Nos. 162, 163, 166, 167, and 168.

WITHHOLDING OF INCOME TAX AT SOURCE ON INTEREST, DIVIDENDS,
AND PATRONAGE DIVIDENDS; REPORTING OF INTEREST, DIVIDEND,
AND PATRONAGE DIVIDEND PAYMENTS OF \$10 OR MORE DURING A
YEAR

Amendment No. 173: Section 19 of the bill as passed by the House added to the Internal Revenue Code of 1954 provisions requiring the withholding of income tax at source on certain interest, dividend, and patronage dividend payments. The tax was to be withheld at the rate of 20 percent and was to apply to payments of interest, dividends, and patronage dividends as those terms were defined for withholding purposes. In addition, the bill as passed by the House provided for exemptions from withholding, quarterly refunds, and special credits. The tax withheld was to be allowed as a credit against the income tax of the recipients of the payments to the extent it had not been previously refunded to them or credited against other tax due from them.

Amendment No. 173 strikes out the provisions of section 19 of the bill as passed by the House and, in lieu thereof, adds to the Internal

Revenue Code of 1954 provisions requiring persons who make payments of dividends, patronage dividends, or interest (within the meaning of such terms as defined in the Senate amendment) aggregating \$10 or more to any other person in a calendar year to file an information return with the Secretary of the Treasury or his delegate with respect to such payments. The Senate amendment adds provisions requiring that payors of dividends, patronage dividends, and interest (as those terms are defined by the amendment) furnish to the recipients of these amounts annual statements showing the amounts paid to them as reported on the information returns filed with the Internal Revenue Service. New penalty provisions are provided by the Senate amendment for failure to file information returns with respect to payments of dividends, patronage dividends, or interest, and for failure to furnish to a recipient of such payments an annual statement of such payments.

The House recedes with clerical amendments. As a part of the agreement to the Senate amendment, the House and Senate conferees have requested the Treasury Department to make annual reports to the Committees on Ways and Means and Finance on the improvement in the reporting on tax returns of dividends, interest, and patronage dividends as a result of the Senate amendment, with the view that this matter will be reconsidered by the Committees on Ways and Means and Finance if it is determined that there has not been sufficient improvement in the reporting of such income.

INFORMATION WITH RESPECT TO CERTAIN FOREIGN ENTITIES

Amendment No. 176: Section 6038(b) of the code, as contained in the bill as passed by both the House and the Senate, provides for a reduction in foreign tax credit for each failure to furnish information with respect to a foreign corporation controlled by a U.S. person. Senate amendment No. 176 provides that such reduction is not to exceed whichever of the following amounts is greater: (A) \$10,000, or (B) the income of the foreign corporation for its annual accounting period with respect to which the failure occurs. The House recedes.

Amendment No. 179: Section 6038(d)(1) of the code as contained in the bill as passed by the House provided that, in applying the constructive ownership rules of section 318(a) of the code for purposes of determining control under section 6038 of the code, the rule which requires ownership of 50 percent of the stock of a corporation before stock owned by such corporation is attributed to its stockholders was to apply without regard to the 50-percent limitation. Senate amendment No. 179 substitutes a 10-percent limitation for the 50-percent limitation. Senate amendment No. 179 also provides that the rules of section 318(a)(2) of the code that stock owned by a partner or a beneficiary of an estate or trust will be considered as owned by the partnership, estate, or trust, are not to be applied so as to consider a U.S. person as owning stock which is owned by a person who is not a U.S. person, nor will a corporation be considered as owning stock owned by or for a 50 percent or more stockholder where the effect is to consider a U.S. person as owning stock which is owned by a person who is not a U.S. person. The House recedes.

Amendments Nos. 180 and 181: Section 6046 (a) and (b) of the code, as amended by the bill as passed by the House, required each U.S. citizen or resident who (on or after January 1, 1963) was or becomes an officer or director of a foreign corporation and each U.S. person who (on or after January 1, 1963) was or becomes an owner of 5 per-

cent or more in value of the stock of such a corporation to file an information return setting forth such information as the Secretary of the Treasury or his delegate prescribes by forms or regulations as necessary for carrying out the provisions of the income tax laws. Under Senate amendment No. 180, such an officer or director is required to file an information return only if 5 percent or more in value of the stock of the foreign corporation is owned by a U.S. person. Under Senate amendment No. 181, in the case of an officer or director of the foreign corporation, the information required is limited to furnishing the names and addresses of the U.S. persons who own 5 percent or more in value of the stock of such corporation. The House recedes on amendment No. 180 with a technical amendment. The House recedes on amendment No. 181.

Amendment No. 183: This amendment adds a new subsection (e) to section 6046 of the code. Under the new subsection, no information is to be required to be furnished under section 6046 with respect to any foreign corporation (1) if the liability of the U.S. citizen, resident, or person to file a return under section 6046(a) arises on or after January 1, 1963, and before March 1, 1963, unless such information is required to be furnished under regulations which have been in effect since January 1, 1963 (but only if such regulations were prescribed before December 1, 1962), or (2) if the liability of the U.S. citizen, resident, or person to file a return under section 6046(a) arises on or after March 1, 1963, unless such information is required to be furnished under regulations which have been in effect for at least 90 days.

Under the conference agreement, the House recedes with an amendment substituting a new subsection (e). Under the conference agreement, in the case of liability to file a return under section 6046 of the code arising on or after January 1, 1963, and before June 1, 1963—

(A) no information is to be required to be furnished under section 6046 with respect to any foreign corporation unless such information was required to be furnished under regulations in effect on or before March 1, 1963, and

(B) if the date on which such regulations become effective is later than the day on which such liability arises, any return required by section 6046(a) is required (in lieu of the time prescribed by sec. 6046(d)) to be filed on or before the 90th day after such date.

In the case of liability to file a return under section 6046(a) arising on or after June 1, 1963, no information is to be required to be furnished under section 6046 with respect to any foreign corporation unless such information was required to be furnished under regulations which have been in effect for at least 90 days before the date on which the U.S. citizen, resident, or person becomes liable to file a return required under section 6046(a).

EXPENDITURES BY FARMERS FOR CLEARING LAND

Amendment No. 189: This amendment adds a new section to the bill, adding a new section 182 to part VI of subchapter B of chapter 1 of the code (relating to itemized deductions for individuals and corporations). The new section 182 permits farmers to elect to treat as deductible expenses, rather than as nondeductible expenditures for capital improvements to property, expenditures for the clearing of land (including a reasonable allowance for depreciation with respect to depreciable property used in the clearing of land) if such expenditures are for the purpose of making the land suitable for use in farming.

The term "clearing of land" includes the eradication of trees, stumps, and brush, the treatment or moving of earth, and the diversion of streams and watercourses. The new section 182 limits the deduction for expenditures for the clearing of land for any taxable year to \$5,000 or to 25 percent of the taxable income derived from farming during the taxable year, whichever amount is the lesser. The new section applies to taxable years beginning after December 31, 1962. The House recedes with clerical and conforming amendments.

CHARITABLE CONTRIBUTIONS MADE FROM INCOME ATTRIBUTABLE TO
SEVERAL TAXABLE YEARS

Amendment No. 190: This amendment adds a new section to the bill, adding a new subsection (e) to section 1307 of the code, relating to rules applicable to part I of subchapter Q of chapter 1 of such code (which relates to income attributable to several taxable years).

When income attributable to several taxable years is received or accrued in a particular taxable year, part I of subchapter Q provides, under certain circumstances, that the tax attributable thereto for the taxable year in which it is received or accrued is, in general, not to be greater than the aggregate increases in taxes which would have resulted if the amount had been included in the taxpayer's income, on an allocated basis, over the period specified in the applicable section of such part I.

New subsection (e) provides that an individual who receives or accrues in a taxable year an amount to which part I of subchapter Q applies may elect (in such manner and at such time as the Secretary of the Treasury or his delegate prescribes by regulations) to apply the provisions of subsection (e) in computing his tax liability under such part. If the taxpayer so elects, the amount received or accrued shall be reduced, for the purposes of computing his tax liability under such part I with respect to such amount, by an amount (1) which bears the same ratio to the amount of his allowable charitable deduction for the taxable year in which the amount was received or accrued (computed without regard to pt. I of subch. Q) as (2) the amount received or accrued during the taxable year to which part I applies bears to the adjusted gross income for such year (computed without regard to pt. I of subch. Q).

New subsection (e) further provides that no portion of the amount received or accrued to which part I of subchapter Q applies shall (for purposes of computing the limitation on tax under such part) be taken into account for purposes of computing the limitation under section 170(b)(1) of the code for the taxable year in which the amount to which such part applies is received or accrued.

The House recedes with an amendment which is technical and clarifying in nature and is a substitute for the provision described in the preceding paragraph.

EFFECTIVE DATE OF SECTION 1371(C). OF THE INTERNAL REVENUE CODE
OF 1954

Amendment No. 191: The Senate amendment adds a new section to the bill as passed by the House which provides that section 1371(c) of the code (relating to the determination of the number of shareholders of a small business corporation where stock is owned by a husband and wife) is, subject to the provisions for filing of election and consents described below, to apply to taxable years beginning

after December 31, 1957, and before January 1, 1960. Under existing law, section 1371(c), which was added to the code by section 2(a) of Public Law 86-376 (approved September 23, 1959), applies only to taxable years beginning after December 31, 1959. The Senate amendment provides a 1-year period within which an otherwise qualifying small business corporation may make a special election to have the earlier effective date of section 1371(c) apply. For the special election to be valid, a corporation must have previously filed a timely election to have its income taxed directly to its shareholders, and each person who is a shareholder at the time of the special election (as well as each person who was a shareholder for any taxable year beginning after December 31, 1957, and ending before the date on which the special election is made) must give his consent. The amendment also provides that where a special election (and the requisite consents) has been made, the statute of limitations for assessing additional tax against the corporation or the shareholders attributable to the earlier effective date of section 1371(c) (and the statute of limitations for allowing a credit or refund of any overpayment of tax by the corporation or its shareholders attributable to the earlier effective date of section 1371(c)) is to remain open, or be opened, for 1 year following the date of the election. The House recedes.

CERTAIN LOSSES SUSTAINED IN CONVERTING FROM STREET RAILWAY
TO BUS OPERATIONS

Amendment No. 192: The Senate amendment adds a new section to the bill as passed by the House which provides that in the case of net operating losses incurred in the calendar years 1953 and 1954 principally as the result of conversion from street railway to bus operations, an additional 5 years, beginning with 1960, is to be allowed for the carryover of such losses. The Senate amendment applies only for years in which the taxpayer is engaged in the furnishing or sale of transportation (as defined in sec. 1503(c)(1)(A) of the 1954 code). The House recedes with a technical amendment.

PENSION PLAN OF LOCAL UNION NO. 435, INTERNATIONAL HOD CARRIERS'
BUILDING AND COMMON LABORERS' UNION OF AMERICA

Amendment No. 193: The Senate amendment adds a new section to the bill as passed by the House which provides that the pension plan of Local Union No. 435 of the International Hod Carriers' Building and Common Laborers' Union of America, which was negotiated to take effect May 1, 1960, pursuant to an agreement between such union and the Building Trades Employers Association of Rochester, N. Y., shall be held and considered to have been a qualified trust under section 401(a) of the code, and to have been exempt from taxation under section 501(a) of the code, for the period beginning May 1, 1960, and ending April 20, 1961, but only if it is shown to the satisfaction of the Secretary of the Treasury or his delegate that the trust has not in this period been operated in a manner which would jeopardize the interests of its beneficiaries. The House recedes.

CONTINUATION OF A PARTNERSHIP YEAR FOR SURVIVING PARTNER IN A
TWO-MAN PARTNERSHIP WHERE ONE DIES

Amendment No. 194: The Senate amendment adds a new section to the bill as passed by the House which amends section 188 of the

Internal Revenue Code of 1939 (relating to different taxable years of partner and partnership) to provide that for purposes of chapter 1 of the 1939 code, if the surviving partner so elects within 1 year after the date of enactment of this bill, the death of one of the partners of a partnership consisting of two members shall not result in the termination of the partnership or in the closing of the taxable year of the partnership with respect to the surviving partner prior to the time the partnership year would have closed if neither partner had died or disposed of his interest. The amendment is to apply to taxable years of a partnership beginning after December 31, 1946, to which the Internal Revenue Code of 1939 applies. The amendment further provides that if refund or credit of any overpayment resulting from the application of such amendment was prevented on the date of the enactment of the bill, or at any time within 1 year from such date by the operation of any law or rule of law (other than those relating to closing agreements and compromises), refund or credit of such overpayment may, nevertheless, be made or allowed if claim therefor is filed within 1 year after the date of enactment of the bill. No interest is to be allowed or paid on any overpayment resulting from the application of the amendment. The House recedes.

EXCLUSION FROM GROSS INCOME OF CERTAIN AWARDS MADE PURSUANT
TO EVACUATION CLAIMS OF JAPANESE-AMERICANS

Amendment No. 195: This amendment, which adds a new section to the bill, provides that awards received under the Japanese-American Evacuation Claims Act, as amended in 1951 and 1956 (50 U.S.C. App., secs. 1981-1987), are not to be included in gross income for purposes of chapter 1 of the Internal Revenue Code of 1939 or 1954. This treatment is to apply with respect to taxable years ending after July 2, 1948.

Any refund or credit of an overpayment of Federal income tax (including interest, additions to the tax, additional amounts, and penalties) resulting from this provision which is barred on the date of the enactment of this bill, or within 1 year from such date, by any law or rule of law may, nevertheless, be made, without interest, if a claim for such refund or credit is filed within 1 year after the date of enactment of the bill. In the case of any claim described in the preceding sentence, the amount to be refunded or credited as an overpayment is not to be diminished by any credit or setoff based on any item other than the amount of the award.

The House recedes with technical amendments.

DEDUCTION FOR BUSINESS DEPRECIATION BY TENANT-STOCKHOLDER OF
COOPERATIVE HOUSING CORPORATION

Amendment No. 196: This amendment adds a new section to the bill, adding a new subsection (c) to section 216 of the code (relating to amounts representing taxes and interest paid to a cooperative housing corporation).

The new subsection (c) provides that so much of the stock of a tenant-stockholder in a cooperative housing corporation as is allocable, under regulations prescribed by the Secretary of the Treasury or his delegate, to a proprietary lease or right of tenancy in property subject to the allowance for depreciation under section 167(a) shall, to the extent that such proprietary lease or right of tenancy is used by such

tenant-stockholder in a trade or business or for the production of income, be treated as property subject to the allowance for depreciation under section 167(a). The amendment is effective with respect to taxable years beginning after December 31, 1961. The House recedes with clerical amendments.

EXCLUSION FROM GROSS INCOME OF GAIN FROM SALE OF RESIDENCE
BY INDIVIDUAL AGE 65 OR OVER

Amendment No. 197: This amendment added a new section to the bill, adding a new section 121 to part III of subchapter B of chapter 1 of the code (relating to items specifically excluded from gross income). The new section 121, applicable only in the case of individuals, provided that gross income does not include gain from the sale, exchange, or involuntary conversion (within the meaning of sec. 121(e)) after December 31, 1962, of property used by the taxpayer as his principal residence, if (1) the taxpayer had attained the age of 65 years before the sale, exchange, or involuntary conversion, and (2) the property had been used by the taxpayer as his principal residence for a period of not less than 5 years at the time of its sale, exchange, or involuntary conversion. The Senate recedes.

DEDUCTION FOR INCOME TAX PURPOSES OF CONTRIBUTIONS TO CERTAIN
ORGANIZATIONS FOR JUDICIAL REFORM

Amendment No. 198: This amendment, which adds a new section to the bill, provides that a contribution or gift made after December 31, 1961, with respect to a referendum occurring during the calendar year 1962, shall be deductible as a charitable contribution under section 170 of the code if made to, or for the use of, an organization created and operated exclusively to consider proposals for the reorganization of the judicial branch of any State or local government and to provide information, make recommendations, and seek public support or opposition to such proposals. For contributions or gifts to be eligible for this treatment, no part of the net earnings of the organization may inure to the benefit of any private shareholder or individual and the organization must not participate in any political campaign in behalf of, or in opposition to, any candidate for public office. The House recedes with a clerical amendment.

AMENDMENT TO SOCIAL SECURITY ACT RELATING TO STATEMENT OF
FINANCIAL STATUS OF CLAIMANTS FOR MEDICAL ASSISTANCE FOR
THE AGED

Amendment No. 199: This amendment added to the bill a new section, amending section 2(a) of the Social Security Act so as to permit a State to provide in its State plan under title I of such act that any written statement required of a claimant for medical assistance for the aged under that title shall be presumed by the State agency administering the plan to be factually correct for purposes of determining eligibility for such assistance insofar as the statement relates to the claimant's financial status. The Senate recedes.

FOREIGN SUBSIDIARIES MANUFACTURING PRODUCTS ABROAD FOR SALE
IN THE UNITED STATES

Amendment No. 200: Senate amendment No. 200 added a new section to the bill to provide that foreign corporations to which the

proposed new section, section 885 of the code, applies are deemed to be engaged in trade or business within the United States, and their gross income from sources within the United States is deemed to be not less than their gross income from the sale of competitive articles sold for ultimate use, consumption, or disposition in the United States. The new section applied to a foreign corporation if at any time during the taxable year one or more domestic corporations own, directly or through one or more other corporations, 10 percent or more of the outstanding stock of the foreign corporation, and if for such taxable year the foreign corporation derives 10 percent or more of its gross income from the sale of competitive articles sold for ultimate use, consumption, or disposition in the United States. For such purpose a competitive article is any article mined, processed, or manufactured outside the United States for a foreign corporation which is the same as or similar to any article mined, processed, or manufactured in the United States (or formerly mined, processed, or manufactured in the United States) by any domestic corporation described in the preceding sentence with respect to the foreign corporation, or by any subsidiary of such domestic corporation. The new provision applied to taxable years beginning after December 31, 1962. The Senate recedes.

EFFECTIVE DATE OF AMENDMENT TO SECTION 1374(b) OF
INTERNAL REVENUE CODE OF 1954

Amendment No. 201: The Senate amendment adds a new section to the bill as passed by the House which makes the amendment to section 1374(b) of the code, which was added by section 2(b) of Public Law 86-376 (approved Sept. 23, 1959), effective on September 2, 1958. Under existing law, the amendment to section 1374(b), which permits the deduction of a deceased shareholder's pro rata share of the net operating loss of an electing small business corporation incurred in the year in which he dies, is effective only with respect to taxpayers who die after September 23, 1959. The House recedes with a clerical amendment.

TREATIES

Amendment No. 203: The bill as passed by the House provided that section 7852(d) of the code, relating to treaty obligations, was not to apply in respect of any amendment made by the Revenue Act of 1962. Senate amendment No. 203 provides that no provision of the Revenue Act of 1962 will apply in any case where its application would be contrary to any treaty obligation of the United States.

The Senate recedes. In this connection, the Treasury Department informed the committee of conference that it is its view that there are no conflicts between provisions of the bill and provisions of tax treaties, with one minor exception relating to the real estate clause of the Greek Estate Tax Treaty which the Treasury will seek to have renegotiated before July 1, 1964.

W. D. MILLS,
CECIL R. KING,
HALE BOGGS,
EUGENE J. KEOGH,
JOHN W. BYRNES,
HOWARD H. BAKER,

Managers on the Part of the House.

consent that the statement of the managers on the part of the House be read in lieu of the report.

The Clerk read the title of the bill.

The SPEAKER. Is there objection to the request of the gentleman from Michigan?

There was no objection.

The Clerk read the statement.

(For conference report and statement, see proceedings of the House of September 27, 1962.)

The SPEAKER. The question is on agreeing to the conference report.

The conference report was agreed to.

A motion to reconsider was laid on the table.

GENERAL LEAVE TO EXTEND REMARKS

Mr. ALBERT. Mr. Speaker, on behalf of the gentleman from North Carolina [Mr. BONNER], I ask unanimous consent that all Members may have 5 legislative days in which to extend their remarks on the following bills: H.R. 8151, H.R. 11587, S. 3389, S. 3396, and H.R. 12968.

The SPEAKER. Without objection, it is so ordered.

There was no objection.

REVENUE ACT OF 1962

Mr. MILLS submitted the following conference report and statement on the bill (H.R. 10650) to amend the Internal Revenue Code of 1954 to provide a credit for investment in certain depreciable property, to eliminate certain defects and inequities, and for other purposes:

CONFERENCE REPORT (H. REPT. NO. 2508)

The committee of conference on the disagreeing votes of the two Houses on the amendments of the Senate to the bill (H.R. 10650) to amend the Internal Revenue Code of 1954 to provide a credit for investment in certain depreciable property, to eliminate certain defects and inequities, and for other purposes, having met, after full and free conference, have agreed to recommend and do recommend to their respective Houses as follows:

That the Senate recede from its amendments numbered 11, 12, 13, 14, 28, 30, 50, 95, 145, 146, 197, 199, 200, and 203.

That the House recede from its disagreement to the amendments of the Senate numbered 2, 3, 4, 6, 7, 8, 10, 15, 16, 17, 18, 19, 20, 21, 22, 23, 24, 25, 26, 27, 32, 33, 34, 35, 36, 37, 38, 39, 40, 41, 42, 43, 44, 45, 46, 47, 49, 51, 52, 53, 55, 56, 57, 58, 59, 62, 63, 64, 65, 66, 67, 68, 70, 71, 72, 73, 74, 75, 76, 77, 78, 79, 80, 81, 82, 83, 84, 86, 88, 93, 94, 97, 98, 100, 101, 102, 103, 105, 106, 107, 108, 109, 110, 111, 112, 113, 114, 115, 116, 117, 118, 119, 120, 121, 122, 123, 124, 125, 127, 128, 129, 130, 131, 132, 133, 134, 135, 136, 137, 138, 139, 141, 142, 143, 144, 147, 148, 149, 150, 151, 152, 153, 154, 155, 156, 157, 158, 160, 162, 163, 164, 165, 166, 167, 168, 169, 170, 171, 172, 174, 175, 176, 177, 178, 179, 181, 182, 184, 185, 186, 188, 191, 193, and 194 and agree to the same.

Amendment numbered 1: That the House recede from its disagreement to the amendment of the Senate numbered 1, and agree to the same with amendments as follows:

Page 3, line 6, of the Senate engrossed amendments, strike out "date" and insert "dates".

Page 4 of the Senate engrossed amendments, strike out lines 27 and 28 and insert:

"(b) Conforming amendment.

"(c) Clerical amendment.

"(d) Effective date."

Page 5 of the Senate engrossed amendments, strike out lines 1 to 24, inclusive, and insert:

"Sec. 27. Exclusion from gross income of certain awards made pursuant to evacuation claims of Japanese-American persons.

(a) In general.

(b) Effective date, etc.

"Sec. 28. Deduction for depreciation by tenant-stockholder of cooperative housing corporation.

(a) Allowance of deduction.

(b) Clerical amendment.

(c) Effective date.

"Sec. 29. Deduction for income tax purposes of contributions to certain organizations for judicial reform.

"Sec. 30. Effective date of amendment to section 1374(b).

"Sec. 31. Treaties."

And the Senate agree to the same.

Amendment numbered 5: That the House recede from its disagreement to the amendment of the Senate numbered 5, and agree to the same with amendments as follows:

Page 6, line 13, of the Senate engrossed amendments, strike out "June 30, 1962" and insert "December 31, 1961".

Page 7 of the Senate engrossed amendments, strike out lines 14 to 22, inclusive, and insert:

"(4) TAXABLE YEAR BEGINNING BEFORE JANUARY 1, 1962.—For purposes of determining the amount of an investment credit carry-back that may be added under paragraph (1) for a taxable year beginning before January 1, 1962, and ending after December 31, 1961, the amount of the limitation provided by subsection (a)(2) is the amount which bears the same ratio to such limitation as the number of days in such year after December 31, 1961, bears to the total number of days in such year."

And the Senate agree to the same.

Amendment numbered 9: That the House recede from its disagreement to the amendment of the Senate numbered 9, and agree to the same with an amendment as follows:

Page 9, line 19, of the Senate engrossed amendments, after "is", insert "equal to or"; and the Senate agree to the same.

Amendment numbered 29: That the House recede from its disagreement to the amendment of Senate numbered 29, and agree to the same with an amendment as follows:

In lieu of the matter proposed to be inserted by the Senate amendment, insert the following: "or, in the case of an item directly preceding or following a substantial and bona fide business discussion (including business meetings at a convention or otherwise), that such item was associated with,".

And the Senate agree to the same.

Amendment numbered 31: That the House recede from its disagreement to the amendment of the Senate numbered 31, and agree to the same with an amendment as follows:

In lieu of the matter proposed to be inserted by the Senate amendment insert the following: "or, in the case of an item described in subparagraph (A) directly preceding or following a substantial and bona fide business discussion (including business meetings at a convention or otherwise), the portion of such item associated with,".

And the Senate agree to the same.

Amendment numbered 48: That the House recede from its disagreement to the amendment of the Senate numbered 48, and agree to the same with an amendment as follows: In lieu of the matter proposed to be inserted by the Senate amendment insert the following: "but the amount determined under this subparagraph shall in no case be greater than the larger of—

"(i) the amount determined under paragraph (4), or

"(ii) the amount which, when added to the amount determined under subparagraph (A), equals the amount by which 12 percent of the total deposits or withdrawable accounts of depositors of the taxpayer at the close of such year exceeds the sum of its surplus, undivided profits, and reserves at the beginning of such year (taking into account any portion thereof attributable to the period before the first taxable year beginning after December 31, 1951)".

And the Senate agree to the same.

Amendment numbered 54: That the House recede from its disagreement to the amendment of the Senate numbered 54, and agree to the same with an amendment as follows: Page 46, after line 4, of the House engrossed bill insert:

"(5) LIMITATION IN CASE OF CERTAIN DOMESTIC BUILDING AND LOAN ASSOCIATIONS.—If the percentage of the assets of a domestic building and loan association which are not assets described in section 7701 (a)(19)(D) (ii) exceeds 36 percent for the taxable year (as determined for purposes of section 7701 (a)(19) for such year), the amount determined under paragraph (2), and the amount determined under paragraph (3), shall in each case be the amount (determined without regard to this paragraph but with regard to the limits contained in paragraphs (2), (3), and (1)(B)) reduced by the amount determined under the following table:

"If the percentage exceeds—	but does not exceed—	the reduction shall be the following proportion of the amount so determined without regard to this paragraph—
36 percent.....	37 percent....	1/12
37 percent.....	38 percent....	1/6
38 percent.....	39 percent....	1/4
39 percent.....	40 percent....	1/3
40 percent.....	41 percent....	5/12"

And the Senate agree to the same.

Amendment numbered 60: That the House recede from its disagreement to the amendment of the Senate numbered 60, and agree to the same with amendments as follows:

Page 24, line 15, of the Senate engrossed amendments, strike out the parenthesis at the beginning of the line.

Page 25, line 23, of the Senate engrossed amendments, strike out "(i) and (ii)" and insert "(i), (ii), (iv), and (vi)".

Page 26, line 10, of the Senate engrossed amendments, strike out "(i) and (ii)" and insert "(i), (ii), (iv), and (vi)".

Page 27, after line 6, of the Senate engrossed amendments, insert: "The term 'domestic building and loan association' also includes any association which, for the taxable year, would satisfy the requirements of the first sentence of this paragraph if '41 percent' were substituted for '36 percent' in subparagraph (E). Except in the case of the taxpayer's first taxable year beginning after the date of the enactment of the Revenue Act of 1962, the second sentence of this paragraph shall not apply to an association for the taxable year unless such association (i) was a domestic building and loan association within the meaning of the first sentence of this paragraph for the first taxable year preceding the taxable year, or (ii) was a domestic building and loan association solely by reason of the second sentence of this paragraph for the first taxable year preceding the taxable year (but not for the second preceding taxable year)."

And the Senate agree to the same.

Amendment numbered 61: That the House recede from its disagreement to the amendment of the Senate numbered 61, and agree to the same with amendments as follows:

Page 27, line 13, of the Senate engrossed amendments, strike out "EXCISE".

Page 27, line 15, of the Senate engrossed amendments, after "ACT", insert "OF 1933".

Page 27, line 16, of the Senate engrossed amendments, after "Act", insert "of 1933".

Page 27, lines 19 and 20, of the Senate engrossed amendments, strike out "EXEMPTION FROM DISCRIMINATORY STATE AND LOCAL TAXATION.—".

And the Senate agree to the same.

Amendment numbered 69: That the House recede from its disagreement to the amendment of the Senate numbered 69, and agree to the same with amendments as follows:

Page 64, line 9, of the House engrossed bill, strike out "6047" and insert "6048".

Page 65, line 13, of the House engrossed bill, strike out "6047" and insert "6048".

Page 67, after line 6, of the House engrossed bill, strike out "6047" and insert "6048".

And the Senate agree to the same.

Amendment numbered 85: That the House recede from its disagreement to the amendment of the Senate numbered 85, and agree to the same with an amendment as follows: In lieu of the matter proposed to be inserted by the Senate amendment insert the following: "\$500,000"; and the Senate agree to the same.

Amendment numbered 87: That the House recede from its disagreement to the amendment of the Senate numbered 87, and agree to the same with an amendment as follows: In lieu of the matter proposed to be inserted by the Senate amendment insert the following:

"(F) SPECIAL TRANSITIONAL UNDERWRITING LOSS.—

"(1) COMPANIES TO WHICH SUBSECTION APPLIES.—This subsection shall apply to every mutual insurance company which has been subject to the tax imposed by this section (as in effect before the enactment of this subsection) for the 5 taxable years immediately preceding January 1, 1962, and has incurred an underwriting loss for each of such 5 taxable years.

"(2) REDUCTION OF STATUTORY UNDERWRITING INCOME.—For purposes of this part, the statutory underwriting income of a company described in paragraph (1) for the taxable year shall be the statutory underwriting income for the taxable year (determined without regard to this subsection) reduced by the amount by which—

"(A) the sum of the underwriting losses of such company for the 5 taxable years immediately preceding January 1, 1962, exceeds

"(B) the total amount by which the company's statutory underwriting income was reduced by reason of this subsection for prior taxable years.

"(3) UNDERWRITING LOSS DEFINED.—For purposes of this subsection, the term 'underwriting loss' means statutory underwriting loss, computed without any deduction under section 824(a) and without any deduction under section 832(c) (11).

"(4) YEARS TO WHICH SUBSECTION APPLIES.—This subsection shall apply with respect to any taxable year beginning after December 31, 1962, and before January 1, 1968, for which the taxpayer is subject to the tax imposed by subsection (a)."

And the Senate agree to the same.

Amendment numbered 89: That the House recede from its disagreement to the amendment of the Senate numbered 89, and agree to the same with an amendment as follows: In lieu of the matter proposed to be inserted by the Senate amendment insert the following: "\$1,100,000"; and the Senate agree to the same.

Amendment numbered 90: That the House recede from its disagreement to the amendment of the Senate numbered 90, and agree to the same with an amendment as follows: In lieu of the matter proposed to be inserted by the Senate amendment insert the

following: "\$1,100,000"; and the Senate agree to the same.

Amendment numbered 91: That the House recede from its disagreement to the amendment of the Senate numbered 91, and agree to the same with an amendment as follows: In lieu of the matter proposed to be inserted by the Senate amendment insert the following: "\$500,000"; and the Senate agree to the same.

Amendment numbered 92: That the House recede from its disagreement to the amendment of the Senate numbered 92, and agree to the same with an amendment as follows: In lieu of the matter proposed to be inserted by the Senate amendment insert the following: "\$1,100,000"; and the Senate agree to the same.

Amendment numbered 96: That the House recede from its disagreement to the amendment of the Senate numbered 96, and agree to the same with an amendment as follows: In lieu of the matter proposed to be inserted by the Senate amendment insert the following: arising, either in any one State or within "200 miles of any fixed point selected by the taxpayer,"; and the Senate agree to the same.

Amendment numbered 99: That the House recede from its disagreement to the amendment of the Senate numbered 99, and agree to the same with an amendment as follows: Page 85, line 4, of the House engrossed bill, after "insurance", insert "company"; and the Senate agree to the same.

Amendment numbered 104: That the House recede from its disagreement to the amendment of the Senate numbered 104, and agree to the same with amendments as follows:

Page 89, line 10, of the House engrossed bill, after "mutual fire", insert "or flood".

Page 89, line 19, of the House engrossed bill, after the period and before the quotation marks, insert "Premiums paid by the subscriber of a mutual flood insurance company referred to in paragraph (3) of section 831(a) shall be treated, for purposes of computing the taxable income of such subscriber, in the same manner as premiums paid by a policyholder to a mutual fire insurance company referred to in such paragraph (3)."

Page 90, line 18, of the House engrossed bill, after "mutual fire", insert "or flood". And the Senate agreed to the same.

Amendment numbered 126:

That the House recede from its disagreement to the amendment of the Senate numbered 126, and agree to the same with amendments as follows:

Page 62, line 7, of the Senate engrossed amendments, before "is", insert "income".

Page 64, line 24, of the Senate engrossed amendments, after "is", insert "created or".

Page 82, lines 6 and 7, of the Senate engrossed amendments, strike out "(computed without regard to section 931)".

Page 82, lines 14 and 15, of the Senate engrossed amendments, strike out "(computed without regard to section 931)".

Page 100 of the Senate engrossed amendments, strike out the table following line 10 and insert:

The required minimum distribution of earnings and profits is (percentage)—	
"If the effective foreign tax rate is (percentage)—	
Under 10.....	90
10 or over but less than 20.....	86
20 or over but less than 28.....	82
28 or over but less than 34.....	75
34 or over but less than 39.....	68
39 or over but less than 42.....	55
42 or over but less than 44.....	40
44 or over but less than 46.....	27
46 or over but less than 47.....	14
47 or over.....	0

Page 106, line 3, of the Senate engrossed amendments, strike out "total" and insert "consolidated".

Page 106, line 5, of the Senate engrossed amendments, strike out "total" and insert "consolidated".

Page 107, lines 20 and 21, of the Senate engrossed amendments, strike out "is eligible to make" and insert "makes".

And the Senate agree to the same.

Amendment numbered 140: That the House recede from its disagreement to the amendment of the Senate numbered 140, and agree to the same with an amendment, as follows: Page 123, line 14, of the Senate engrossed amendments, after "1962" insert a comma; and the Senate agree to the same.

Amendment numbered 159: That the House recede from its disagreement to the amendment of the Senate numbered 159, and agree to the same with amendments as follows: Page 130 of the Senate engrossed amendments, beginning with line 8, strike out all through page 131 and insert the following:

"(b) LIMITATION ON TAX APPLICABLE TO INDIVIDUALS.—In the case of an individual, if the stock sold or exchanged is a capital asset (within the meaning of section 1221) and has been held for more than 6 months, the tax attributable to an amount included in gross income as a dividend under subsection (a) shall not be greater than a tax equal to the sum of—

"(1) a pro rata share of the excess of—

"(A) the taxes that would have been paid by the foreign corporation with respect to its income had it been taxed under this chapter as a domestic corporation (but without allowance for deduction of, or credit for, taxes described in subparagraph (B), for the period or periods the stock sold or exchanged was held by the United States person in taxable years beginning after December 31, 1962, while the foreign corporation was a controlled foreign corporation, adjusted for distributions and amounts previously included in gross income of a United States shareholder under section 951, over

"(B) the income, war profits, or excess profits taxes paid by the foreign corporation with respect to such income; and

"(2) an amount equal to the tax that would result by including in gross income, as gain from the sale or exchange of a capital asset held for more than 6 months, an amount equal to the excess of (A) the amount included in gross income as a dividend under subsection (a), over (B) the amount determined under paragraph (1)."

Page 135, lines 9 and 10, of the Senate engrossed amendments, strike out "referred to in subparagraph (B)" and insert "ending on the date of the sale or exchange".

Page 137, line 25, of the Senate engrossed amendments, strike out "(2)".

And the Senate agree to the same.

Amendment numbered 161: That the House recede from its disagreement to the amendment of the Senate numbered 161, and agree to the same with amendments as follows: Page 139 of the Senate engrossed amendments, insert quotation marks after "apply." in line 7 and strike out lines 8 to 14, inclusive; and the Senate agree to the same.

Amendment numbered 173: That the House recede from its disagreement to the amendment of the Senate numbered 173, and agree to the same with amendments, as follows:

Page 150, line 4, of the Senate engrossed amendments, strike out "6047" and insert "6048".

Page 150, line 6, of the Senate engrossed amendments, strike out "6048" and insert "6049".

Page 154, line 13, of the Senate engrossed amendments strike out "6048(a) (1)" and insert "6049(a) (1)".

Page 155, line 4, of the Senate engrossed amendments, strike out "6048(a) (2)" and insert "6049(a) (2)".

Page 155, line 5, of the Senate engrossed amendments, strike out "6048(a)(3)" and insert "6049(a)(3)".

Page 156, line 5, of the Senate engrossed amendments, strike out "6048(c)" and insert "6049(c)".

Page 156, line 8, of the Senate engrossed amendments, strike out "6048(a)(1)" and insert "6049(a)(1)".

Page 156, line 22, of the Senate engrossed amendments, strike out "6048(a)(1)" and insert "6049(a)(1)".

Page 156, line 25, of the Senate engrossed amendments, strike out "6048(a)(2), or 6048(a)(3)" and insert "6049(a)(2), or 6049(a)(3)".

Page 157, line 19, of the Senate engrossed amendments, strike out "6048" and insert "6049"; and the Senate agree to the same.

Amendment numbered 180: That the House recede from its disagreement to the amendment of the Senate numbered 180, and agree to the same with an amendment as follows: Page 159, line 18, of the Senate engrossed amendments, after "person", insert "(as defined in section 7701(a)(30))".

And the Senate agree to the same.

Amendment numbered 183: That the House recede from its disagreement to the amendment of the Senate numbered 183, and agree to the same with an amendment as follows: In lieu of the matter proposed to be inserted by the Senate amendment insert the following:

"(e) LIMITATION.—

"(1) GENERAL RULE.—Except as provided in paragraph (2), no information shall be required to be furnished under this section with respect to any foreign corporation unless such information was required to be furnished under regulations which have been in effect for at least 90 days before the date on which the United States citizen, resident, or person becomes liable to file a return required under subsection (a).

"(2) EXCEPTION.—In the case of liability to file a return under subsection (a) arising on or after January 1, 1963, and before June 1, 1963—

"(A) no information shall be required to be furnished under this section with respect to any foreign corporation unless such information was required to be furnished under regulations in effect on or before March 1, 1963, and

"(B) if the date on which such regulations become effective is later than the day on which such liability arose, any return required by subsection (a) shall (in lieu of the time prescribed by subsection (d)) be filed on or before the 90th day after such date."

And the Senate agree to the same.

Amendment numbered 187: That the House recede from its disagreement to the amendment of the Senate numbered 187, and agree to the same with an amendment as follows: Page 239, after line 3, of the House engrossed bill, strike out "6038(d)(2)" and insert "6038(d)(1)"; and the Senate agree to the same.

Amendment numbered 189: That the House recede from its disagreement to the amendment of the Senate numbered 189, and agree to the same with amendments as follows: Page 163, after line 23, of the Senate engrossed amendments, insert:

"(b) CONFORMING AMENDMENT.—Section 263(a)(1) (relating to disallowance of deductions for capital expenditures) is amended by striking out 'or' at the end of subparagraph (C), by striking out the period at the end of subparagraph (D) and inserting ', or', and by adding at the end thereof the following new subparagraph:

"(E) expenditures by farmers for clearing land deductible under section 182."

Page 163, line 24, of the Senate engrossed amendments, strike out "(b)" and insert "(c)".

Page 164, line 4, of the Senate engrossed amendments, strike out "(c)" and insert "(d)".

And the Senate agree to the same.

Amendment numbered 190: That the House recede from its disagreement to the amendment of the Senate numbered 190, and agree to the same with an amendment as follows: Page 165 of the Senate engrossed amendments, strike out lines 4 through 10 and insert: "In any case in which the taxpayer elects to have the provisions of the preceding sentence apply, for purposes of computing the limitation on tax under this part—

"(1) only the same proportion of the amount to which this part applies shall be taken into account for purposes of computing the limitations under section 170(b)(1)(A) and (B) for taxable years before the taxable year in which such amount is received or accrued as (A) the excess of the maximum amount which could, if the taxpayer had made additional contributions described in clause (i), (ii), or (iii) of section 170(b)(1)(A), have been described in clause (1) of the preceding sentence over the amount described in such clause (1), bears to (B) such maximum amount, and

"(2) the portion of the amount of charitable contributions described in the preceding sentence shall not be taken into account in computing the tax for the taxable year in which the amount to which this part applies is received or accrued."

And the Senate agree to the same.

Amendment numbered 192: That the House recede from its disagreement to the amendment of the Senate numbered 192, and agree to the same with an amendment as follows: Page 168, of the Senate engrossed amendments, strike out lines 6 to 11, inclusive, and insert:

"(b) UNUSED CONVERSION LOSS DEFINED.—The amount of the unused conversion loss shall be the sum of the part of the net operating loss for each year described in subsection (a) which (without regard to this section) would be carried over to the sixth taxable year following the loss year if section 172(b) of the Internal Revenue Code of 1954 (or, where applicable, section 122(b)(2)(B) of the Internal Revenue Code of 1939) permitted such a carryover."

And the Senate agree to the same.

Amendment numbered 195: That the House recede from its disagreement to the amendment of the Senate numbered 195, and agree to the same with an amendment as follows: Page 171, line 19, of the Senate engrossed amendments, strike out "AMERICAN-JAPANESE INDIVIDUALS" and insert "JAPANESE-AMERICAN PERSONS"; and the Senate agree to the same.

Amendment numbered 196: That the House recede from its disagreement to the amendment of the Senate numbered 196, and agree to the same with amendments as follows: Page 173, line 9, of the Senate engrossed amendments, after "and", insert "BUSINESS".

Page 174, after line 2, of the Senate engrossed amendments, insert:

"(b) CLERICAL AMENDMENT.—The table of sections for part VII of subchapter B of chapter 1 is amended by striking out the item relating to section 216 and inserting in lieu thereof the following:

"Sec. 216. Deduction of taxes, interest, and business depreciation by cooperative housing corporation tenant-stockholder."

Page 174, line 3, of the Senate engrossed amendments, strike out "(b)" and insert "(c)".

And the Senate agree to the same.

Amendment numbered 198: That the House recede from its disagreement to the amendment of the Senate numbered 198, and agree to the same with an amendment as follows: Page 177, line 2, of the Senate

engrossed amendments, strike out "30" and insert "29"; and the Senate agree to the same.

Amendment numbered 201: That the House recede from its disagreement to the amendment of the Senate numbered 201, and agree to the same with an amendment as follows: Page 181, line 8, of the Senate engrossed amendments, strike out "33" and insert "30"; and the Senate agree to the same.

Amendment numbered 202: That the House recede from its disagreement to the amendment of the Senate numbered 202, and agree to the same with an amendment as follows: In lieu of the matter proposed to be inserted by the Senate amendment insert the following: "31"; and the Senate agree to the same.

WILBUR D. MILLS,
CECIL R. KING,
HALE BOGGS,
EUGENE J. KEOGH,
JOHN W. BYRNES,
HOWARD H. BAKER,

Managers on the Part of the House.

HARRY FLOOD BYRD,
ROBERT S. KERR,
RUSSELL B. LONG,
GEORGE A. SMATHERS,
JOHN J. WILLIAMS,
FRANK CARLSON,
WALLACE F. BENNETT,

Managers on the Part of the Senate.

STATEMENT

The managers on the part of the House at the conference on the disagreeing votes of the two Houses on the amendments of the Senate to the bill (H.R. 10650) to amend the Internal Revenue Code of 1954 to provide a credit for investment in certain depreciable property, to eliminate certain defects and inequities, and for other purposes, submit the following statement in explanation of the effect of the action agreed upon by the conferees and recommended in the accompanying conference report:

The following Senate amendments made technical, clerical, clarifying, or conforming changes: 1, 2, 3, 4, 7, 8, 15, 16, 20, 22, 24, 25, 26, 27, 34, 35, 36, 38, 39, 40, 44, 47, 49, 51, 53, 55, 57, 58, 59, 63, 66, 67, 68, 71, 72, 73, 74, 77, 78, 83, 86, 88, 89, 101, 103, 105, 106, 107, 108, 109, 110, 112, 114, 115, 116, 117, 118, 119, 120, 122, 127, 134, 136, 137, 138, 139, 142, 144, 146, 148, 149, 150, 151, 152, 154, 155, 156, 157, 158, 164, 165, 169, 170, 171, 172, 174, 175, 177, 178, 182, 184, 185, 186, 187, 188, and 202. With respect to these amendments (1) the House either recedes or recedes with amendments which are technical, clerical, clarifying, or conforming in nature, or (2) the Senate recedes in order to conform to other action agreed upon by the committee of conference.

CREDIT FOR INVESTMENT IN CERTAIN DEPRECIABLE PROPERTY

Amendments Nos. 5 and 23: Under the bill as passed by both the House and the Senate the amount of the investment credit which may be allowed for any taxable year may not exceed so much of the liability for tax for the taxable year as does not exceed \$25,000, plus 25 percent of so much of the liability for tax for the taxable year as exceeds \$25,000. Under the bill as passed by the House, any unused credit resulting from this limitation was to be carried forward to each of the 5 succeeding taxable years to the extent not taken into account in intervening years. Under Senate amendment No. 5, such unused credit is first carried back to the 3 preceding taxable years and then carried over to the 5 succeeding taxable years. This rule is subject to three exceptions: (1) The unused credit may be a carryback only to taxable years ending after June 30, 1962, (2) to the extent that an unused credit arises by reason of a net operating loss carryback, such unused credit is taken into account

only as a carryover and not as a carryback from such year; and (3) in the case of a taxable year beginning before July 1, 1962, and ending after June 30, 1962, the limitation on the credit allowable for such year for purposes of the carryback to such year is the amount which bears the same ratio to the limitation otherwise applicable as the number of days in such year after June 30, 1962, bears to the total number of days in such year. The House recedes with amendments conforming to the unused credit carryback provisions to the conference action on Senate amendment No. 28 (which provides that the investment credit is to apply to taxable years ending after December 31, 1961).

Senate amendment No. 23 amends the provisions of the code relating to periods of limitation and interest to conform to the Senate amendments providing for the unused credit carryback. The House recedes.

Amendments Nos. 6 and 9: The bill as passed by the House (sec. 46(c) of the code, as added by the bill) defined the qualified investment for purposes of the investment credit as the aggregate of (1) the applicable percentage of the basis of each new section 38 property placed in service during the taxable year, plus (2) the applicable percentage of the cost of each used section 38 property placed in service during the taxable year. These applicable percentages vary according to the useful life of the property. If any such property is disposed of, or otherwise ceases to be section 38 property with respect to the taxpayer, before the close of the useful life that was taken into account in computing the investment credit, then the income tax for the taxable year of the disposition is increased (sec. 47 of the code, as added by the bill) by an amount equal to the decrease in credits which would have resulted had the useful life used in determining the credit been the period beginning with the time the property was placed in service and ending with the time it ceased to be section 38 property.

The bill as passed by the Senate retains these rules except in cases where section 38 property is placed in service by the taxpayer to replace property which was stolen or was destroyed or damaged by fire, storm, shipwreck, or other casualty. Under Senate amendment No. 6, the basis (if new property) or cost (if used property) of the replacement section 38 property taken into account in determining qualified investment is required to be reduced by an amount equal to the amount received by the taxpayer as compensation (by insurance or otherwise) for the property destroyed, damaged, or stolen, or by an amount equal to the adjusted basis of such property, whichever is the lesser. This rule is not to apply if the reduction in qualified investment attributable to the substitution required by section 47(a)(1) of the code with respect to the property so destroyed, damaged, or stolen is greater than the reduction required under the new paragraph (4) added to section 46(c) by Senate amendment No. 6.

Senate amendment No. 9 adds a new paragraph (4) to section 47(a) of the code (relating to certain dispositions, etc., of sec. 38 property) to coordinate the provisions of such section 47(a) with the new rules provided under Senate amendment No. 6. In general, the new paragraph (4) of section 47(a) provides that paragraphs (1) and (3) of section 47(a) shall not apply to property which ceases to be section 38 property on account of its destruction or damage by fire, storm, shipwreck, or other casualty, or by reason of its theft, if such property is replaced by property to which the new paragraph (4) of section 46(c) (added by Senate amendment No. 6) applies, and if the reduction under that new paragraph is greater than the reduction in qualified investment under paragraph (1) of section 47(a).

The House recedes on Senate amendment No. 6 and recedes with a technical clarifying amendment on Senate amendment No. 9.

Amendment No. 10: This amendment adds a new paragraph (6) to new section 48(a) of the code (defining "section 38 property" for purposes of the investment credit) to provide that livestock is not to be treated as section 38 property. The House recedes.

Amendments Nos. 11, 12, 13, and 14: The bill as passed by the House defined the term "new section 38 property" as section 38 property (1) the construction, reconstruction, or erection of which is completed by the taxpayer after December 31, 1961, or (2) acquired after December 31, 1961, if the original use of such property commences with the taxpayer and commences after such date. In determining qualified investment described in clause (1) of the preceding sentence, only that portion of the basis which is properly attributable to construction, reconstruction, or erection after December 31, 1961, is to be taken into account. The bill as passed by the House also limited the definition of "used section 38 property" to property acquired by purchase after December 31, 1961. Senate amendments Nos. 11, 12, 13, and 14 changed these dates from December 31, 1961, to June 30, 1962. The Senate recedes.

Amendment No. 17: Under the bill as passed by the House, a person engaged in the business of leasing property would be permitted to elect with respect to any new section 38 property to treat the lessee as having acquired the property. Under Senate amendment No. 17, the lessor is not required to be engaged in the business of leasing property in order to make the election. The House recedes.

Amendments Nos. 18 and 19: Senate amendment No. 19 adds a new subsection (g) to new section 48 of the code (containing definitions and special rules relating to the investment credit). The new subsection requires that for purposes of subtitle A of the code (relating to income tax), other than for purposes of the investment credit, the basis of any section 38 property be reduced by an amount equal to 7 percent of the qualified investment with respect to such property. The new subsection provides, however, that if the tax under chapter 1 of the code is increased, or an adjustment in carrybacks or carryovers is made, under new section 47(a) of the code, the basis of the property is to be increased by an amount equal to the portion of the increase in tax and the portion of the adjustment attributable to such property. The House recedes.

It is the understanding of the conferees on the part of both the House and the Senate that the purpose of the credit for investment in certain depreciable property, in the case of both regulated and nonregulated industries, is to encourage modernization and expansion of the Nation's productive facilities and to improve its economic potential by reducing the net cost of acquiring new equipment, thereby increasing the earnings of the new facilities over their productive lives.

Senate amendment No. 18 provides that if a lessor makes an election to treat the lessee as having acquired the property then, under regulations prescribed by the Secretary of the Treasury or his delegate, the new subsection (g) added by amendment No. 19 is not to apply and the deductions otherwise allowable under section 162 of the code to the lessee for amounts paid to the lessor under the lease are to be adjusted in a manner consistent with the provisions of the new subsection (g). The House recedes.

Amendment No. 21: This amendment adds a new section 2(c) to the bill, adding a new section 181 to part VI of subchapter B of chapter 1 of the code (relating to itemized deductions for individuals and corporations). If after applying the carrybacks and carryovers of any unused investment credit

any amount thereof remains unused, this amount is to be allowed to the taxpayer as a deduction for the first taxable year following the last taxable year in which the unused amount could have been allowed as a credit. However, if a taxpayer dies or ceases to exist before such first taxable year, the amount described in the preceding sentence (or proper portion thereof) is, under regulations, to be allowed to the taxpayer as a deduction for the taxable year in which such death or cessation occurs. The House recedes.

Amendment No. 28: Under the bill as passed by the House, the amendments made by section 2 (relating to credit for investment in certain depreciable property) were to apply with respect to taxable years ending after December 31, 1961. Under Senate amendment No. 28, the amendments were to apply with respect to taxable years ending after June 30, 1962. The Senate recedes.

DISALLOWANCE OF CERTAIN ENTERTAINMENT, ETC., EXPENSES

Amendments Nos. 29, 30, and 31: The bill as passed by both the House and the Senate adds a new section 274 to the code (relating to disallowance of certain entertainment, etc., expenses). Section 274(a)(1) as passed by the House provided that no deduction otherwise allowable under chapter 1 of the code is to be allowed for any item—

(1) with respect to an activity which is of a type generally considered to constitute entertainment, amusement, or recreation, unless the taxpayer establishes that the item was directly related to the active conduct of the taxpayer's trade or business, or

(2) with respect to a facility used in connection with such an activity, unless the taxpayer establishes that the facility was used primarily for the furtherance of the taxpayer's trade or business and that the item was directly related to the active conduct of such trade or business,

and such deduction is in no event to exceed the portion of such item directly related to the active conduct of the taxpayer's trade or business.

Senate amendments Nos. 29, 30, and 31 inserted the words "or associated with" after the words "directly related to" each place they appeared in the new section 274(a)(1) as passed by the House.

Under the conference agreement the House recedes on Senate amendment No. 29 with an amendment providing that deductions otherwise allowable under chapter 1 of the code shall not be allowed for any item with respect to an entertainment type activity "unless the taxpayer establishes that the item was directly related to, or, in the case of an item directly preceding or following a substantial and bona fide business discussion (including business meetings at a convention or otherwise), that such item was associated with," the active conduct of the taxpayer's trade or business. Under the conference agreement, the Senate recedes on amendment No. 30, and the House recedes on amendment No. 31 with an amendment conforming to the action on amendment No. 29.

The rule of the House bill as described in the report of the Committee on Ways and Means is more strict than the "or associated with" rule of the Senate amendment. The rule of the House bill would not allow deduction of expenditures for entertainment occurring under circumstances where there is little or no possibility of conducting business affairs or carrying on negotiations or discussions relating thereto, such as where the group of persons entertained is large or the distractions substantial.

It is the understanding of the conferees, both on the part of the House and the Senate, that the alternative Senate "or associated with" test as described in the report of the Finance Committee would apply to cer-

tain entertaining primarily to encourage goodwill where the evidence of business connection is clear, whether or not business is actually transacted or discussed during the entertainment. The conference agreement would permit a deduction for the cost of an entertainment item, even though the item is not directly related to the active conduct of the taxpayer's trade or business, if the item is associated with it, so long as the entertainment activity directly precedes or follows a substantial and bona fide business discussion. The conditions under which an item is "associated with" the active conduct of a trade or business are contained in the report of the Committee on Finance. The deductibility of other items of entertainment expense, as well as items with respect to facilities, would be governed by the rule of the House bill.

Section 274(a) as agreed to by the conferees will allow as a deduction the cost of entertaining connected with what are primarily business meetings. For example, if the taxpayer conducts substantial negotiations with a group of business associates and that evening entertains the group and their wives at a restaurant, theater, concert, or sporting event, such entertainment expenses, if associated with the active conduct of the taxpayer's business, will be deductible even though the purpose of the entertainment is merely to promote goodwill in such business. Moreover, if a group of business associates with whom the taxpayer is conducting business meetings comes from out of town to the taxpayer's place of business to hold substantial business discussions, the entertainment of such business guests by the taxpayer the evening prior to the business discussions will be regarded as directly preceding the business discussions.

Similarly, if in between, or in the evenings after business meetings at a convention, the taxpayer entertains his business associates or prospective customers attending such meetings (and their wives), such entertainment will be considered as directly preceding or following a business discussion.

Any entertainment which is a part of substantial and bona fide business discussions, where the conduct of business is the principal activity during the combined entertainment and business time spent together by the taxpayer and the person or persons entertained, will be deductible if the expense is associated with the active conduct of the taxpayer's trade or business.

Also, the cost of banquets at meetings of professional and business associations would normally be deductible. As in the above cases, if the expense is associated with the active conduct of a trade or business, it would not be necessary for the person paying for the banquet to attend the banquet himself. For example, a dental equipment supplier would be able to deduct the cost of purchasing a table at a dental association banquet for dentists who are actual or prospective customers for his equipment.

Thus, under the business meal exception contained in proposed section 274(e)(1), and the conference agreement, the cost of providing food and beverages at most business meetings and banquets would be deductible, as well as almost all restaurant and most hotel entertaining. In neither of the situations covered by the conference agreement nor under the business meal exception is there a requirement that business must actually be discussed in order to get a deduction.

Amendment No. 32: Section 274(b), as added to the code by the bill as passed by both the House and the Senate, provides in effect that no deduction is to be allowed under section 162 or 212 of the code for any expense for gifts to any individual to the extent that the total expenses of the taxpayer for gifts to such individual during the same taxable year exceed \$25. For purposes

of the new section 274, the term "gift" is defined to mean any item excludable from gross income of the recipient under section 102 of the code which is not excludable from his gross income under any other provision of chapter 1 of the code. Senate amendment No. 32 adds a new provision providing that such terms does not include—

(1) an item having a cost to the taxpayer not in excess of \$4 on which the name of the taxpayer is clearly and permanently imprinted and which is one of a number of identical items distributed generally by the taxpayer.

(2) a sign, display rack, or other promotional material to be used on the business premises of the recipient, or

(3) an item of tangible personal property having a cost to the taxpayer not in excess of \$100 which is awarded to an employee by reason of length of service or for safety achievement.

The House recedes.

Amendment No. 33: This amendment adds a new subsection (c) to the new section 274 added to the code by the bill. The new subsection (c) provides that in the case of any individual who is traveling away from home in pursuit of a trade or business or in pursuit of an activity described in section 212 of the code (relating to expenses for production of income), no deduction is to be allowed under section 162 or 212 for that portion of the expenses of such travel otherwise allowable under such section which, under regulations prescribed by the Secretary of the Treasury or his delegate, is not allocable to such trade or business or to such activity. The new subsection (c) is not to apply to the expenses of any travel away from home which does not exceed 1 week or where the portion of the time away from home which is not attributable to the pursuit of the taxpayer's trade or business or an activity described in section 212 is less than 25 percent of the total time away from home on such travel. The House recedes.

Amendment No. 37: Under subsection (e) (6) of the new section 274 of the code, as added by the bill as passed by the House, section 274(a) (relating to disallowance of entertainment, amusement, or recreation expenses) was not to apply to expenses directly related to business meetings of employees or stockholders. Under Senate amendment No. 37, section 274(a) is not to apply to expenses incurred by a taxpayer which are directly related to business meetings of his employees, stockholders, agents, or directors. Under this provision, the members of a partnership are to be considered as agents. The House recedes.

Amendment No. 41: Section 162 of the code provides that there shall be allowed as a deduction all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, including "traveling expenses (including the entire amount expended for meals and lodging) while away from home in the pursuit of a trade or business." Under the bill as passed by the House, the parenthetical matter quoted in the preceding sentence would be changed to "(including a reasonable allowance for amounts expended for meals and lodging)". Under Senate amendment No. 41, such parenthetical matter would be changed to "(including amounts expended for meals and lodging other than amounts which are lavish or extravagant under the circumstances)". The House recedes.

Amendment No. 42: Under the bill as passed by the House, the amendments made by the bill with respect to the disallowance of certain entertainment, etc., expenses were to apply with respect to taxable years ending after June 30, 1962, but only in respect of periods after such date. Under Senate amendment No. 42, the amendments are to apply with respect to taxable years ending after December 31, 1962, but only in respect

of periods after such date. The House recedes.

AMOUNT OF DISTRIBUTION WHERE CERTAIN FOREIGN CORPORATIONS DISTRIBUTE PROPERTY IN KIND

Amendment No. 43: Subsection (d) of section 5 of the bill as passed by the House would amend section 902(a) of the code (relating to credit for foreign taxes) to provide that for purposes of section 902(a) and (b) the amount of any distribution in property other than money is to be determined under section 301(b)(1)(B) of the code. Under section 301(b)(1)(B) the amount of a distribution of property to a corporate shareholder is the lesser of (1) the fair market value of such property, or (2) the adjusted basis of such property (in the hands of the distributing corporation immediately before the distribution). Senate amendment No. 43 strikes out subsection (d) of section 5 of the bill. The House recedes.

AMENDMENT TO SECTION 482 OF THE INTERNAL REVENUE CODE

Amendment No. 45: Section 6 of the bill as passed by the House amended section 482 of the code (relating to allocation of income and deductions among taxpayers) by designating the existing text as subsection (a) and by adding a new subsection (b) to provide special rules for allocating taxable income, arising from sales of tangible property within a related group which includes a foreign organization, among the members of the group. The allocation was to be made by the Secretary of the Treasury or his delegate by taking into consideration that portion of the factors listed in the bill which is attributable to the United States and that portion which is not attributable to the United States. The bill also permitted consideration of other factors (including special risks, if any, of the market in which the property is sold). If the taxpayer established to the satisfaction of the Secretary or his delegate that an alternative method of allocation clearly reflects the income of each member of the group with respect to the property in question, the alternative method was required to be used.

Senate amendment No. 45 strikes out section 6 of the bill as passed by the House.

The House recedes. The conferees on the part of both the House and the Senate believe that the objectives of section 6 of the bill as passed by the House can be accomplished by amendment of the regulations under present section 482. Section 482 already contains broad authority to the Secretary of the Treasury or his delegate to allocate income and deductions. It is believed that the Treasury should explore the possibility of developing and promulgating regulations under this authority which would provide additional guidelines and formulas for the allocation of income and deductions in cases involving foreign income.

DISTRIBUTIONS OF FOREIGN PERSONAL HOLDING COMPANY INCOME

Amendment No. 46: Section 7 of the bill as passed by the House amended section 552 (a) of the code to substitute a 20-percent gross income requirement for the requirement now contained in the definition of a foreign personal holding company that more than 60 percent (or 50 percent in certain cases) of its gross income consist of foreign personal holding company income. Such section 7 also amended the definition of "undistributed foreign personal holding company income" contained in section 556(a) of the code to mean taxable income (adjusted as provided by existing law) if the foreign personal holding company income exceeds 80 percent of the company's gross income, and to mean a proportionate part of such taxable income if the foreign personal holding company income does not exceed 80 percent of its gross income.

Senate amendment No. 46 strikes out section 7 of the bill as passed by the House. The House recedes.

MUTUAL SAVINGS BANKS, ETC.

Amendment No. 48: The bill as passed by both the House and the Senate amends section 593 of the code to provide rules relating to reserves for losses on loans by mutual savings institutions listed in the bill. Subsection (b)(1) of the amended section 593 prescribes the method for determining the reasonable addition for the taxable year to the reserve for bad debts under section 166(c) of the code and also specifies the reserves to which such additions are to be made. Such reasonable addition is the sum of two amounts—(1) the amount determined under section 166(c) to be the reasonable addition to the reserve for losses on nonqualifying loans, plus (2) the amount determined by the taxpayer to be a reasonable addition to the reserve for losses on qualifying real property loans (but the amount so determined by the taxpayer is not to exceed the amount determined under pars. (2), (3), or (4) of sec. 593(b), whichever amount is the largest). Senate amendment No. 48 adds a further limitation providing that the amount of the addition for a taxable year to the reserve for losses on qualifying real property loans, when added to the amount of the addition to the reserve for losses on nonqualifying loans, shall in no case be greater than the amount by which 12 percent of the total deposits or withdrawable accounts of depositors of the taxpayer at the close of such year exceeds the sum of its surplus, undivided profits, and reserves at the beginning of such year (taking into account any portion thereof attributable to the period before the first taxable year beginning after December 31, 1951). The House recedes with a substitute for the Senate amendment which provides in effect, that the 12-percent ceiling is not to apply in the case of a taxpayer using the experience method for the taxable year.

Amendments Nos. 50 and 52: Under section 593(b)(2) of the code as amended by the bill as passed by the House, the amount of the reasonable addition to the reserve for losses on qualifying real property loans for a taxable year was limited to the excess of an amount equal to 60 percent of the taxable income for such year over the amount determined under section 166(c) to be a reasonable addition to the reserve for losses on nonqualifying loans. For purposes of this method, taxable income is determined without regard to any deduction for any additions to the reserves for bad debts, and also by excluding from gross income any amount included therein by reason of subsection (f) (relating to the treatment of certain distributions of property to stockholders by a domestic building and loan association).

Senate amendment No. 50 provided that, in the case of a domestic building and loan association having capital stock with respect to which any distribution of property is not allowable as a deduction under section 591 (relating to dividends paid on deposits), an amount equal to 50 percent of the taxable income is substituted for the 60 percent provided by the bill as passed by the House. The Senate recedes.

Senate amendment No. 52 provides that the amount of the addition determined under section 593(b)(2) is not to exceed the amount necessary to increase the balance (as of the close of the taxable year) of the reserve for losses on qualifying real property loans to 6 percent of such loans outstanding at such time. The House recedes.

Amendment No. 54: Under section 593(b)(3) of the code as amended by the bill as passed by the House, the amount of the reasonable addition to the reserve for losses on qualifying real property loans for a taxable year was limited to an amount equal to the

amount necessary to increase the balance (as of the close of the taxable year) of such reserve to 3 percent of such loans outstanding at such time. Senate amendment No. 54 permits the balance of the reserve for losses on qualifying real property loans to be increased to a larger amount in the case of a mutual savings institution which is a new company and which does not have capital stock with respect to which distributions of property are not allowable as a deduction under section 591 of the code. This larger amount is the sum of two amounts: (1) 3 percent of qualifying real property loans outstanding at the close of the taxable year, plus (2) an amount equal to 2 percent of so much of such loans as does not exceed \$4,000,000, reduced (but not below zero) by the amount, if any, of the balance (as of the close of such year) of the taxpayer's supplemental reserve for losses on loans. A taxpayer is a "new company" for any taxable year only if such taxable year begins not more than 10 years after the first day on which it (or any predecessor) was authorized to do business as a mutual savings institution described in section 593(a) of the code.

The House recedes with an amendment. Under the conference action the text of section 593(b)(3) of the code is the same as it is under Senate amendment numbered 54. In addition, under the conference action the new section 593(b)(5) of the code provides that in the case of certain domestic building and loan associations there will be a reduction in the amount determined under paragraph (2) (60 percent of taxable income method) and paragraph (3) (percentage of real property loans method) of section 593(b). For purposes of computing this reduction, the amount determined under paragraph (2), and the amount determined under paragraph (3), shall in each case be the amount determined without regard to the new section 593(b)(5), but with regard to the 12-percent ceiling added by Senate amendment numbered 48 and, in the case of the amount determined under paragraph (2), the 6-percent ceiling added by Senate amendment numbered 52. The reduction provided by the new section 593(b)(5) will apply only in the case of a domestic building and loan association which qualifies as such for the taxable year solely by reason of the second sentence of section 7701(a)(19) (see the discussion of Senate amendment numbered 60), which changes the 36-percent requirement of subparagraph (E) of the first sentence of section 7701(a)(19) to a 41-percent requirement. The reduction varies from one-twelfth to five-twelfths, depending on the number of percentage points (and fractions thereof) by which the association fails to satisfy the 36-percent requirement.

Amendment No. 56: Section 593(c) of the code, as amended by the bill as passed by the House provides for the allocation of pre-1963 reserves (that is, the net amount, determined as of December 31, 1962, accumulated in the reserve for bad debts for taxable years beginning after December 31, 1951)—

(1) first, to the reserve for losses on nonqualifying loans, to the extent such reserve is not increased above the amount which would be a reasonable addition under section 166(c) of the code for a period in which such loans increased from zero to the amount outstanding at the close of 1962,

(2) second, to the reserve for losses on qualifying real property loans, to the extent such reserve is not increased above the amount equal to 3 percent of the loans outstanding at the close of 1962 or, if larger, the amount which would be a reasonable addition under section 166(c) of the code for a period in which such loans increased from zero to the amount outstanding at the close of 1962, and

(3) then to a supplemental reserve for losses on loans.

Senate amendment No. 56 adds a new paragraph (5) to section 593(c) providing, in effect, that if the pre-1963 reserves are insufficient to bring the balance of the reserve for qualifying real property loans up to the amount referred to in paragraph (2) above then the term "pre-1963 reserves" includes so much of the surplus, undivided profits, and bad debt reserves (determined as of December 31, 1962) attributable to the period before the first taxable year beginning after December 31, 1951, as is necessary to bring the balance of the reserve for qualifying real property loans up to the amount referred to in paragraph (2) above. This rule is to apply only for the purpose of determining reasonable additions under the amended section 593 to such reserve, and for such purpose the amount so allocated is to be treated as remaining in such reserve. The House recedes.

Amendment No. 60: Section 7701(a)(19) of the code defines the term "domestic building and loan association" as a domestic building and loan association, a domestic savings and loan association, and a Federal savings and loan association, substantially all of the business of which is confined to making loans to members.

The bill as passed by the House amended section 7701(a)(19) to provide that the term "domestic building and loan association" means any domestic building and loan association, domestic savings and loan association, and Federal savings and loan association which met each of two requirements. The first requirement was that the association be either (i) an insured institution within the meaning of section 401(a) of the National Housing Act, or (ii) subject by law to supervision and examination by State or Federal authority having supervision over such associations. The second requirement was that substantially all of the business of the association must consist of accepting savings and investing the proceeds in (i) loans secured by an interest in real property which is, or from the proceeds of the loan will become, residential real property, and (ii) other loans to the extent they would be authorized to be made by a Federal savings and loan association under section 5(c) of the Home Owners' Loan Act of 1933.

Senate amendment No. 60 adopts without change the first requirement of the bill as passed by the House, but replaces the second requirement with six new requirements:

(1) Substantially all of the business of the association must consist of acquiring the savings of the public and investing in loans described in paragraph (2) below.

(2) At least 90 percent of the amount of the total assets (determined as of the close of the taxable year) of the association must consist of (i) cash, (ii) obligations of the United States, a State, or a political subdivision of a State, stock or obligations of a corporation which is an instrumentality of one of those governmental units, and certificates of deposit in, or obligations of, a corporation organized under a State law which specifically authorizes such corporation to insure the deposit or share accounts of member associations, (iii) loans secured by an interest in real property and loans made for the improvement of real property, (iv) loans secured by a deposit or share of a member, (v) property acquired through the liquidation of defaulted loans described in clause (iii) of this paragraph, and (vi) property used by the association in the conduct of the business described in paragraph (1) above.

(3) Of the assets taken in account as assets constituting the 90 percent of total assets, at least 80 percent of such 90 percent must consist of (i) assets of the types described in clauses (i) and (ii) of paragraph (2) above, and (ii) loans secured by an interest in real property which is, or

from the proceeds of the loan will become, residential real property or real property used primarily for church purposes, loans made for the improvement of residential real property or real property used primarily for church purposes, or property acquired through the liquidation of defaulted loans described in this paragraph.

(4) Of the assets taken into account as assets constituting the 90 percent of total assets, at least 60 percent of such 90 percent must consist of (i) assets of the types prescribed in clauses (1) and (ii) of paragraph (2) above, and (ii) loans secured by an interest in real property which is, or from the proceeds of the loan will become, residential real property containing four or fewer family units or real property used primarily for church purposes, loans made for the improvement of residential real property containing four or fewer family units or real property used primarily for church purposes, or property acquired through the liquidation of defaulted loans described in this paragraph.

(5) Not more than 18 percent of the amount of the total assets (determined as of the close of the taxable year) of the association may consist of assets other than those referred to in paragraph (3) above, and not more than 36 percent of the amount of such total assets may consist of assets other than those referred to in paragraph (4) above.

(6) Except for property described in paragraph (2) above, not more than 3 percent of the total assets of the association may consist of stock of any corporation.

Senate amendment No. 60 also provides that, at the election of the association, the percentages specified in paragraph (2) through (6) above shall be applied on the basis of the average assets outstanding during the taxable year, rather than at the close of the taxable year, as computed under regulations prescribed by the Secretary of the Treasury or his delegate.

The House recedes with amendments. Under the conference action, loans secured by a deposit or share of a member, and property used by the association in the conduct of its savings and loan business, are in effect to be taken into account (1) in the same manner as loans on residential real property for purposes of section 7701(a) (19) (D) (i), and (2) in the same manner as loans on residential real property for four or fewer family units for purposes of section 7701(a) (19) (D) (ii).

Under the conference action, a second sentence and a third sentence are added to section 7701(a) (19). The new second sentence provides that the term "domestic building and loan association" also includes any association which would satisfy the requirements of the first sentence if "41 percent" were substituted for "36 percent" in subparagraph (E) of the first sentence. The new third sentence provides in effect that, except in the case of the association's first taxable year (whenever occurring in the case of a new association) beginning after the date of the enactment of the bill, the modification of the 36-percent requirement is to be available to it for a taxable year only if—

(1) it met the requirements of the first sentence of section 7701(a) (19) for the immediately preceding taxable year, or

(2) it qualified as a domestic building and loan association for the immediately preceding taxable year solely by reason of the second sentence of section 7701(a) (19) and (if the taxable year is the third or any succeeding taxable year of the association beginning after the date of the enactment of the bill) it met the requirements of the first sentence of section 7701(a) (19) for the second preceding taxable year.

Amendment No. 61: The bill as passed by the House repealed the exemption of Federal

savings and loan associations from the taxes imposed by sections 4251 and 4261 of the code (relating, respectively, to the excise tax on communications and the excise tax on the transportation of persons). Senate amendment No. 61 amends section 5(h) of the Home Owners' Loan Act of 1933 (12 U.S.C., sec. 1464(h)) so as to eliminate entirely the exemptions from Federal taxes which that section now provides in the case of Federal savings and loan associations.

Under section 4382(a) (2) of the code, capital stock and certificates of indebtedness issued by domestic building and loan associations and cooperative banks are exempt from the documentary stamp taxes imposed by chapter 34 of the code. Senate amendment No. 61 amends section 4382(a) (2) so as to eliminate this exemption insofar as it extends (i) to all certificates of indebtedness issued by a domestic building and loan association or cooperative bank, and (ii) to shares or certificates of stock issued by such a domestic building and loan association or cooperative bank, to the extent that such shares or certificates of stock do not represent deposits or withdrawable accounts.

The House recedes with clerical and clarifying amendments.

Amendment No. 62: This Senate amendment adds a new provision to the bill as passed by the House which would amend section 591 of the code (relating to the deduction for dividends paid on deposits by mutual savings banks, cooperative banks, and domestic building and loan associations) so as to make clear that a deduction will be allowable under section 591 for (1) interest paid or credited to the accounts of depositors or holders of accounts on their deposits or withdrawable accounts by mutual savings banks, cooperative banks, and domestic building and loan associations, and (2) dividends and interest described in section 591 paid by a savings institution chartered and supervised as a savings and loan or similar association under Federal or State law. The House recedes.

Amendment No. 64: Under the bill as passed by the House, the change in the definition of the term "domestic building and loan association" would have taken effect on the enactment of the bill. Senate amendment No. 64 adds a new provision under which the new definition will apply to taxable years beginning after the date of the enactment of the bill. The House recedes.

Amendment No. 65: The bill as passed by the House provided an effective date of July 1, 1962, for the termination of the exemption of domestic building and loan associations from the excise taxes on communications and transportation of persons. Senate amendment No. 65 provides an effective date of January 1, 1963, for the termination of exemptions from Federal taxes. The House recedes.

DISTRIBUTIONS BY FOREIGN TRUSTS

Amendment No. 69: The bill as passed by the House defined the term "foreign trust created by a United States person" (for purposes of the provisions of the bill relating to distributions by foreign trusts) as, in general, a foreign trust to which money or property has been transferred directly or indirectly by a U.S. person, or under the will of a decedent who at the date of his death was a U.S. citizen or resident. Senate amendment No. 69 provides that such term means that portion of a foreign trust attributable to money or property transferred directly or indirectly by such a person or under the will of such a decedent. The House recedes with clerical amendments.

Amendment No. 70: Under the bill as passed by the House, the amendments to subchapter J of chapter 1 of the code with respect to distributions by foreign trusts were to apply with respect to distributions made in taxable years of trusts beginning

after the date of the enactment of the bill. Senate amendment No. 70 provides that these amendments are to apply with respect to distributions made after December 31, 1962. The House recedes.

MUTUAL INSURANCE COMPANIES (OTHER THAN LIFE, MARINE, AND CERTAIN FIRE OR FLOOD INSURANCE COMPANIES)

Amendments Nos. 75 and 76: These are amendments to conform, in the case of insurance companies subject to tax under part II of subchapter L of chapter 1 of the code, the normal tax rates on mutual insurance company taxable income and on taxable investment income to the action taken by the Congress in the Tax Rate Extension Act of 1962.

The House recedes.

Amendments Nos. 79, 80, 81, 82, and 102: Under existing law and under the bill as passed by the House, mutual insurance companies other than life or marine are exempt from income tax if the gross amount received from specified items does not exceed \$75,000. Under the bill as passed by the House, if this gross amount is over \$75,000 but less than \$125,000, the alternative tax imposed by the new section 821(c) (1) of the code on small companies is proportionately reduced. Under Senate amendment No. 102, a mutual insurance company other than life or marine is exempt from income tax if the gross amount does not exceed \$150,000. Senate amendments Nos. 79, 80, 81, and 82 provide for a proportionate decrease in the alternative tax if the gross amount is over \$150,000 but less than \$250,000. The House recedes.

Amendments Nos. 84 and 85: Under the bill as passed by the House, the alternative tax for certain small companies provided by the new section 821(c) of the code applied for a taxable year only if the gross amount referred to in section 821(c) (3) for the taxable year exceeded \$75,000 but did not exceed \$300,000. Under Senate amendments Nos. 84 and 85 the \$75,000 and \$300,000 amounts are changed to \$150,000 and \$600,000, respectively. The House recedes on Senate amendment No. 84. The House recedes on Senate amendment No. 85 with an amendment changing the \$600,000 amount provided by the Senate amendment to \$500,000.

Amendment No. 87: This amendment adds a new subsection (f) to section 821 of the code and provides a special transitional underwriting loss deduction for taxable years beginning after 1962 and before 1968 for mutual insurance companies which were subject to the tax imposed by existing section 821 for the 6 taxable years immediately preceding 1963 and which incurred an underwriting loss for at least 5 of such 6 years. The mutual insurance company taxable income with respect to such a company is reduced each year by the amount by which (1) the sum of the underwriting losses of such company for such 6 years, reduced by the underwriting gain for such years, exceeds (2) the total amount by which mutual insurance company taxable income was reduced under the new subsection (f) for prior taxable years. The House recedes with a substitute under which (1) the new subsection (f) applies only in the case of a company which has been subject to the tax imposed by section 821 for each of the 5 taxable years immediately preceding 1962, and has incurred an underwriting loss for each of such 5 taxable years, and (2) such losses are to be used as an offset only to statutory underwriting income.

Amendments Nos. 90, 91, and 92: Section 823(c) of the code, as added by the bill as passed by the House, provided a special deduction (not to exceed \$6,000 in amount) in determining the statutory underwriting income or loss for the taxable year if the gross amount received from the items speci-

fied in section 823(c) does not equal or exceed \$900,000. Under Senate amendments Nos. 90, 91, and 92 this special deduction decreases to zero when the gross amount equals \$1,200,000. The House recedes with an amendment under which the deduction decreases to zero when the gross amount equals \$1,100,000.

Amendments Nos. 93, 94, 95, and 96: Under the bill as passed by the House, paragraph (1) of the new section 824(a) added to the code (relating to deduction to provide protection against losses) provides that in determining the statutory underwriting income or loss for any taxable year there is to be allowed as a deduction the sum of—

- (1) an amount equal to 1 percent of the losses incurred during the taxable year, plus
- (2) an amount equal to 25 percent of the underwriting gain for the taxable year, plus
- (3) if the concentrated windstorm, etc., premium percentage (as defined in the bill) for the taxable year exceeds 50 percent, an amount determined by applying so much of such percentage as exceeds 50 percent to the underwriting gain for the taxable year.

Under the bill as passed by the House, paragraph (2) of the new section 824(a) defines the term "concentrated windstorm, etc., premium percentage" as the percentage obtained by dividing (A) premiums earned on insurance contracts during the taxable year, to the extent attributable to insuring against losses arising in any one State, from windstorm, hail, flood, earthquake, or similar hazards, by (B) premiums earned on insurance contracts during the taxable year.

Senate amendments Nos. 93 and 94 increase the scope of the coverage of paragraph (3) above and increase the amount of the deduction by striking out the references to 50 percent and inserting in lieu thereof 40 percent. The House recedes.

Senate amendment No. 96 changes the definition of "concentrated windstorm, etc., premium percentage" to permit the percentage to be determined by reference to premiums attributable to insuring against losses arising (1) in any one State, (2) if the taxpayer so elects, within 200 miles of any fixed point selected by the taxpayer, or (3) if the taxpayer so elects, within 400 miles of any fixed point selected by the taxpayer. Senate amendment No. 95 provides that, in the case of a taxpayer making the election described in clause (3) of the preceding sentence, the amount of the deduction allowable by reason of section 824(a)(1)(C) is to be one-half of the amount it would be but for this amendment. The House recedes on Senate amendment No. 96 with an amendment under which the percentage is to be determined by reference to premiums attributable to losses arising either (1) in any one State, or (2) within 200 miles of any fixed point selected by the taxpayer. The Senate recedes on Senate amendment No. 95.

Amendments Nos. 97, 98, and 99: Subsection (d) of the new section 824 of the code, as added by the bill, sets forth the amounts which are to be subtracted from the protection against loss account. These amounts are taken into account for purposes of determining mutual insurance company taxable income.

Under the bill as passed by the House, the first subtraction from the account was to be made for so much of the statutory underwriting loss as was generated either by the deduction for dividends to policyholders or by the deduction provided in section 824(a) for protection against losses. Thus, under the bill as passed by the House, any underwriting loss attributable to policy dividends could not be applied against taxable investment income unless the balance in the protection against loss account has first been reduced to zero.

The effect of Senate amendments Nos. 97, 98, and 99 is to permit any portion of the statutory underwriting loss attributable to

the deduction for dividends to policyholders to be first applied against taxable investment income. The House recedes on Senate amendments Nos. 97 and 98, and recedes on Senate amendment No. 99 with a clerical amendment.

Amendment No. 100: New section 826 of the code, as added by the bill, in effect permits a mutual insurance company which is an interinsurer or reciprocal underwriter to elect to combine certain income of its attorney-in-fact with its own underwriting income. If the company so elects, it is credited with so much of the tax paid by the attorney in fact as is attributable to such income of the attorney-in-fact. Under the bill as passed by the House, subsection (d) of section 826 provided, in effect, that the protection against loss deduction of the reciprocal making the election and the addition to its protection against loss account were to be computed without regard to the election. Senate amendment No. 100 strikes out this provision, thus permitting the protection against loss deduction, and the amount added to the protection against loss account, to reflect amounts attributable to such income of the attorney-in-fact. The amendment inserts a new subsection (d) providing, in effect, that no part of the amount added to the protection against loss account by reason of the election by the reciprocal may remain in the account (and thus be subject to tax deferral) for more than 5 years. The House recedes.

Amendment No. 104: Under this amendment (and Senate amendment No. 74) mutual flood insurance companies are to be taxed under part III of subchapter L of chapter 1 of the code (which imposes a tax on certain marine and mutual fire insurance companies and on certain stock insurance companies which are not life insurance companies).

The House recedes with technical conforming amendments making it clear that the taxation of these mutual flood insurance companies (and of their subscribers or policyholders) is to be the same as the present tax treatment of so-called factory mutuals (and of their policyholders).

DOMESTIC CORPORATIONS RECEIVING DIVIDENDS FROM FOREIGN CORPORATIONS

Amendments Nos. 111 and 113: These amendments deal with (1) the method to be used for determining the amount of foreign income tax deemed to have been paid by domestic corporations with respect to dividends received from foreign corporations for purposes of the allowance of a foreign tax credit under section 902 of the code, and (2) the amount to be treated as received as a dividend by reason of the tax so deemed paid. Under the bill as passed by the House, the entire amount of foreign income tax of the foreign corporation was to be taken into account in determining the foreign income tax deemed to be paid by the domestic corporation, and (under new sec. 78) an amount equal to the taxes deemed paid was required to be included in income as a dividend. Senate amendment No. 111 would (A) retain existing law with respect to dividends paid by a foreign corporation out of accumulated profits of a year for which it is a "less developed country corporation," and (B) provide, with respect to all other dividends paid by a foreign corporation, the same rules as were provided by the bill as passed by the House. Under Senate amendment No. 113, the new section 78 is amended to exclude from the application of the new section 78 dividends referred to in clause (A) above. The House recedes on Senate amendments Nos. 111 and 113.

SEPARATE LIMITATION ON FOREIGN TAX CREDIT WITH RESPECT TO CERTAIN INTEREST INCOME

Amendment No. 121: Section 904 of the code provides a per-country limitation on the amount of the foreign tax credit or (at

the election of the taxpayer) an overall limitation may be applied. Senate amendment No. 121 adds a new section to the bill to provide a separate limitation on the foreign tax credit with respect to certain interest income. Under the amendment, (1) the foreign tax credit limitations are to be applied separately with respect to (A) certain interest income, and (B) income other than such interest income, and (2) the overall limitation is not to apply to such interest income. The interest income referred to is any interest other than—

(A) interest derived from any transaction which is directly related to the active conduct of a trade or business in a foreign country or a possession of the United States,

(B) interest derived in the conduct of a banking, financing, or similar business,

(C) interest received from a corporation in which the taxpayer owns at least 10 percent of the voting stock, and

(D) interest received on obligations acquired as a result of the disposition of a trade or business actively conducted by the taxpayer in a foreign country or a possession of the United States or as the result of the disposition of stock or obligations of a corporation in which the taxpayer owned at least 10 percent of the voting stock.

The amendment requires the Secretary of the Treasury or his delegate by regulations to prescribe the manner of applying foreign tax credit carrybacks and carryovers where the taxpayer elects the overall limitation as to other income and provides transitional rules (1) for foreign tax credit carrybacks from years to which the new provisions apply to years to which they do not apply, and (2) for foreign tax credit carryovers from years to which the new provisions do not apply to years to which they do apply. The new provisions are to apply with respect to taxable years beginning after the date of the enactment of the bill, but only with respect to interest resulting from transactions consummated after April 2, 1962. The House recedes.

EARNED INCOME FROM SOURCES WITHOUT THE UNITED STATES

Amendment No. 123: This amendment adds a new paragraph (6) to section 911(c) of the code as contained in the bill as passed by the House. Section 911(c) contains special rules for determining the amount of earned income from sources without the United States which is excludable from gross income. The new paragraph (6) provides that a statement by an individual who has earned income from sources within a foreign country to the authorities of that country that he is not a resident of that country, if he is held not subject as a resident of that country to the income tax of that country by its authorities with respect to such earnings, shall be conclusive evidence with respect to such earnings that he is not a bona fide resident of that country for purposes of section 911(a)(1). The House recedes.

Amendment No. 124: This amendment adds a new paragraph (7) to section 911(c) of the code as contained in the bill as passed by the House. Under the new paragraph (7), if an individual who qualifies as a bona fide resident of a foreign country receives compensation from sources without the United States (except from the United States or any agency thereof) in the form of the right to use property or facilities, the \$20,000 or \$35,000 limitation applicable with respect to such individual (A) for a taxable year ending in 1963, is to be increased by an amount equal to the amount of such compensation so received during such taxable year; (B) for a taxable year ending in 1964, is to be increased by an amount equal to two-thirds of such compensation so received during such taxable year; and (C) for a taxable year ending in 1965, is to be increased by an amount equal to one-third of such compensation so

received during such taxable year. The House recedes.

Amendment No. 125: The bill as passed by the House provided that the amendment made to section 911 of the code was to apply to taxable years ending after December 31, 1962, but only with respect to amounts received after December 31, 1962, which were attributable either to (A) services performed after December 31, 1962, or (B) services performed on or before December 31, 1962, but only if on March 12, 1962, there existed no right (whether forfeitable or nonforfeitable) to receive such amounts. Senate amendment No. 125 provides that the amendment made to section 911 of the code will apply to taxable years ending after September 4, 1962, but only with respect to (1) amounts received after March 12, 1962, which are attributable to services performed after December 31, 1962, or (2) amounts received after December 31, 1962, which are attributable to services performed on or before December 31, 1962, unless on March 12, 1962, there existed a right (whether forfeitable or nonforfeitable) to receive such amounts. The House recedes.

CONTROLLED FOREIGN CORPORATIONS

Amendment No. 126: The bill as passed by the House added a new subpart F to part III of subchapter N of chapter 1 of the code (relating to income from sources without the United States). The new subpart F (relating to controlled foreign corporations) provided rules under which a U.S. person who owns stock in a controlled foreign corporation would be required to include in his gross income a pro rata share of certain portions of the controlled foreign corporation's income. Senate amendment No. 126 struck out these provisions of the bill as passed by the House and inserted new text in the nature of a substitute which adds a new subpart F (relating to controlled foreign corporations) and a new subpart G (relating to export trade corporations). Under the conference agreement, the House recedes with amendments, which, except as discussed below in paragraph (m) relating to receipt of minimum distributions, are either technical or clerical. The more important differences between the bill as passed by the House and the Senate amendment as agreed to in conference are explained below.

(a) Amounts included in gross income: The bill as passed by both the House and the Senate provides, in general, that a U.S. person who owns, or is considered to own, 10 percent or more of the total combined voting power of all classes of stock entitled to vote of a controlled foreign corporation is required to include in his gross income his pro rata share of (1) the subpart F income of the foreign corporation, (2) previously excluded subpart F income withdrawn from investment in less developed countries, and (3) the increase in earnings of the foreign corporation invested in certain property ("non-qualified property" in the bill as passed by the House, and limited to "United States property" in the Senate amendment). Under the bill as passed by the House, this provision applied if the foreign corporation was a controlled foreign corporation on any one day of the taxable year. Senate amendment No. 126 requires that the foreign corporation be a controlled foreign corporation for an uninterrupted period of 30 days or more during its taxable year. The bill as passed by both the House and the Senate defines U.S. persons to mean, in general, citizens or residents of the United States, domestic partnerships and corporations, and any estate or trust (other than a foreign estate or trust). However, Senate amendment No. 126, in cases relating to certain corporations organized in the Commonwealth of Puerto Rico or possessions of the United States, excludes from the definition of U.S. persons certain individual citizens of the United States who are

bona fide residents in the Commonwealth of Puerto Rico or the possessions of the United States in which the corporation is created or organized.

(b) Subpart F income:

(1) Amounts included: The bill as passed by both the House and the Senate included within the term "subpart F income" the foreign base company income of a controlled foreign corporation and the income of a controlled foreign corporation derived from the insurance of U.S. risks. The bill as passed by the House also included in the subpart F income of a controlled foreign corporation income of such corporation derived from U.S. patents, copyrights, and exclusive formulas and processes if such properties were substantially developed, created, or produced in the United States or were acquired from a related U.S. person. Senate amendment No. 126 does not include such income in subpart F income. However, see amendment No. 161 for a provision that gain on the sale or exchange of such property to a foreign corporation controlled by the transferor is to be taxable as ordinary income.

(2) Limitations on subpart F income: The bill as passed by both the House and Senate provided that the subpart F income of a controlled foreign corporation could not exceed the earnings and profits for the taxable year. Senate amendment No. 126 provides that, for purposes of this limitation, the earnings and profits for any taxable year is to be reduced by deficits in earnings and profits for taxable years of the controlled foreign corporation beginning after December 31, 1962 (and certain deficits in earnings and profits for taxable years beginning after December 31, 1959, and before January 1, 1963) and, under regulations prescribed by the Secretary of the Treasury or his delegate, by deficits in earnings and profits of other corporations in a chain of ownership which includes the controlled foreign corporation.

(c) Income derived from insurance of U.S. risks: The bill as passed by both the House and the Senate provides that subpart F income includes income of a controlled foreign corporation derived from the insurance or reinsurance of property in the United States or of lives or health of residents of the United States. However, under Senate amendment No. 126 this provision applies only if the premiums or other consideration received or accrued in respect of such insurance or reinsurance by a controlled foreign corporation represents more than 5 percent of total premiums and other consideration.

(d) Foreign base company income: The bill as passed by both the House and the Senate provides that the term "foreign base company income" means the sum of the foreign personal holding company income (discussed in paragraph (e) below) and the foreign base company sale income (discussed in paragraph (f) below) of a controlled foreign corporation. Senate amendment No. 126 also includes foreign base company services income (discussed in paragraph (g) below) within the defined term.

(e) Foreign personal holding company income: The bill as passed by both the House and the Senate provides that subpart F income of a foreign corporation includes foreign personal holding company income, with certain modifications. The bill as passed by the House provided for an exclusion in the case of personal holding company income of certain banks. The Senate amendment provides for an exclusion from personal holding company income of: (i) rents and royalties derived from the active conduct of a trade or business, if received from an unrelated person; (ii) dividends, interest, and certain gains derived in the conduct of a banking, financing, or similar business, or derived by an insurance company on investments of unearned premiums or certain reserves, if received from an unre-

lated person; (iii) dividends and interest received from related persons if such persons are organized, and have a substantial part of their assets, within the country of incorporation of the controlled foreign corporation; (iv) interest received in the conduct of a banking, financing, or similar business from a related person also engaged in the conduct of a banking, financing, or similar business, if the businesses of both the recipient and payor are predominantly with unrelated persons; and (v) rents, royalties, and similar amounts received from a related person for the use of, or the privilege of using, property within the country of incorporation of the controlled foreign corporation.

(f) Foreign base company sales income: The bill as passed by both the House and the Senate provides that subpart F income of a controlled foreign corporation includes income, whether in the form of profits, commissions, fees, or otherwise, derived by a controlled foreign corporation in connection with the purchase of property from a related person, or sale of property to a related person, when the property sold was neither manufactured in, nor sold for use, consumption, or disposition in, the country in which the controlled foreign corporation is organized. The Senate amendment provides that foreign branches of a controlled foreign corporation shall, under certain circumstances, be treated as wholly owned subsidiary corporations for purposes of determining the foreign base company sales income of the controlled foreign corporation, and treats foreign base company sales income of the branch as foreign base company sales income of the controlled foreign corporation.

The bill as passed by the House provided for a reduction of foreign base company sales income by an amount equal to the increase in qualified investments in less developed countries. Moreover, the bill as passed by the House provided that foreign base company sales income would be includible in subpart F income only if such income amounted to at least 20 percent of gross income (not including other foreign base company income). Senate amendment No. 126 contains neither provision. However, see the discussion below under paragraph (h) relating to exclusions from foreign base company income.

(g) Foreign base company services income: Senate amendment No. 126 provides that subpart F income of a controlled foreign corporation includes income, whether in the form of compensation, commissions, fees, or otherwise, derived by a controlled foreign corporation in connection with the performance of technical, managerial, engineering, or like services if such services are performed for a related person and are performed outside the country of incorporation of the controlled foreign corporation, and if such income is not related to certain selling activities. The bill as passed by the House did not contain any similar provision.

(h) Exclusions from foreign base company income: The bill as passed by the House provided that no part of the gross income of a controlled foreign corporation would be treated as foreign base company income if such income was less than 20 percent of gross income, and that the entire gross income of such a corporation would be treated as foreign base company income if such income exceeded 80 percent of gross income. Senate amendment No. 126 changes these percentages to 30 percent and 70 percent, respectively. The bill as passed by the House also provided, in general, that foreign base company income was to be reduced by an amount equal to the increased investment in certain less developed country properties, including stock of a foreign corporation engaged in business almost wholly within less developed countries if substantially all the property of such corporation

was ordinary and necessary for the active conduct of such trade or business. Senate amendment No. 126 provides that foreign base company income does not include dividends and interest received from qualified investments in less developed countries, and net gain from the sale or exchange of such investments to the extent such dividends, interest, and gains do not exceed the increased investment of a controlled foreign corporation, for the taxable year, in qualified investments in less developed countries. The Senate amendment also provides that foreign base company income does not include income of a controlled foreign corporation derived from the use of any aircraft or vessel in foreign commerce, or from services directly related to such use.

(1) Withdrawal of previously excluded subpart F income from qualified investments: As noted in paragraph (h) above, Senate amendment No. 126 provides that dividends, interest, and gains derived from qualified investments in less developed countries are excluded from foreign base company income to the extent of the increased investment for the taxable year, in qualified investments in less developed countries. Amounts once excluded from foreign base company income under this provision are, however, included in gross income of U.S. shareholders when there is a decrease in qualified investments in less developed countries.

(1) Qualified investments in less developed countries: The Senate amendment defines the term "qualified investments in less developed countries" to mean (A) stock of a less developed country corporation, but only if the controlled foreign corporation which makes the investment owns 10 percent or more of the stock of such corporation, (B) an obligation of a less developed country corporation which at the time acquired by the controlled foreign corporation has a maturity of 1 year or more, but only if the controlled foreign corporation which makes the investment owns 10 percent or more of the stock of such corporation, and (C) obligations of a less developed country. However, if any such investment is disposed of within 6 months after the date of its acquisition, it is not to be treated as a qualified investment.

(2) Less developed country corporations: Senate amendment No. 126 defines the term "less developed country corporation" to mean a foreign corporation engaged in the active conduct of a trade or business if (A) such corporation derives 80 percent or more of its gross income from sources within less developed countries, and (B) 80 percent or more of the assets of such corporation consists of (i) property located in less developed countries if used in an active trade or business, (ii) stock of any other less developed country corporation, (iii) obligations of less developed country corporations which at the time of their acquisition have a maturity of 1 year or more, (iv) obligations of a less developed country, and (v) certain other investments, including certain permissible investments in the United States. The Senate amendment also provides that the term "less developed country corporation" includes a foreign corporation (1) which, in general, derives 80 percent or more of its gross income (A) from the use in foreign commerce of aircraft or vessels registered under the laws of a less developed country, (B) from the performance of services directly related to such aircraft or vessels, (C) from the sale or exchange of such aircraft or vessels, and (D) from dividends and interest received from other less developed country corporations (within the meaning of this sentence) in which the recipient owns 10 percent or more of the voting stock, and from gain from the sale or exchange of stock or obligations of such other less developed country corporations, and (2) 80 percent or

more of the assets of which consists of assets used in connection with the production of income described in (1) above, and of certain permissible investments in the United States.

(j) Increase in investments in certain property: The bill as passed by the House provided for the inclusion in gross income of U.S. shareholders of earnings and profits of a controlled foreign corporation invested in nonqualified property to the extent of a shareholder's pro rata share of the increase in such investments for the taxable year. As defined in the bill as passed by the House, nonqualified property meant (1) property located in the United States, with certain exceptions, but including stock in a domestic corporation or an obligation of a U.S. person, and (2) property other than property ordinary and necessary for the active conduct of a trade or business (or for a substantially similar trade or business) carried on by the controlled foreign corporation outside the United States, if (A) the business had been carried on since December 31, 1962, or for a 5-year period ending at the close of the preceding taxable year, or (B) the business was carried on almost wholly within less developed countries. Senate amendment No. 126 includes only the first category of nonqualified property defined in the Senate amendment as "United States property."

(k) Controlled foreign corporations: The bill as passed by the House provided that a foreign corporation would be considered a controlled foreign corporation if more than 50 percent of the total combined voting power of all classes of its stock entitled to vote was owned by U.S. persons on any day during the taxable year of such corporation. Under Senate amendment No. 126, a foreign corporation is a controlled foreign corporation only if U.S. shareholders (defined as a U.S. person who owns, with the application of special rules of ownership continued in the Senate amendment, 10 percent or more of the stock of a foreign corporation) on any day during the taxable year of such corporation owned more than 50 percent of the total combined voting power of all classes of stock entitled to vote of such corporation. Senate amendment No. 126 also provides that a corporation organized in the Commonwealth of Puerto Rico or a possession of the United States is excluded from the term "controlled foreign corporation" if the corporation is primarily engaged in the active conduct of specified trades or businesses in the Commonwealth of Puerto Rico or a possession of the United States and derives its income from specified sources.

(l) Individuals subject to tax at corporate rates: Senate amendment No. 126 provides that a U.S. shareholder who is an individual may elect to limit his U.S. tax liability with respect to amounts which are includible in his gross income under the new subpart F by using the rates provided by section 11 of the code applicable in the case of a domestic corporation, and by applying the provisions of section 960 (relating to foreign tax credit). A U.S. shareholder who makes an election under this provision must, in the year of actual distribution of an amount previously taxed under subpart F, include an amount in gross income equal to the amount distributed reduced by U.S. tax previously paid with respect to such amount.

(m) Receipt of minimum distributions: Senate amendment No. 126 provides that if a given percentage of the earnings and profits of a controlled foreign corporation is distributed, a domestic corporate shareholder may elect to exclude from its gross income its share of the amount of subpart F income of such controlled foreign corporation. A domestic corporate shareholder may elect to apply the minimum distribution provision on the basis of (1) any controlled foreign corporation in which it owns stock directly, (2) controlled foreign corporations in a

chain of ownership, or (3) all controlled foreign corporations. In the case of an election with respect to all controlled foreign corporations, the domestic corporation may also elect (A) to exclude, under certain circumstances, less developed country corporations, and (B) to treat its foreign branches as controlled foreign corporations, for purposes of this provision. The required minimum distribution decreases as the effective foreign tax rate increases, with the result that the sum of the amount of foreign tax paid by the foreign corporations, and the U.S. tax paid by the shareholders on distributions of current earnings and profits of such corporations, produces an overall effective tax on current foreign profits equal to approximately 90 percent of the tax that would have been paid had the foreign corporations been taxable as domestic corporations. Under the conference agreement, a new table of minimum distributions, which permits less variation from this 90-percent requirement, is substituted for the table contained in Senate amendment No. 126. Under Senate amendment No. 126, an affiliated group of corporations eligible to file a consolidated return under section 1501 of the code could elect to be treated as a single corporation for purposes of applying the minimum distribution provision. Under the conference agreement, this election may be made only if the affiliated group actually files such a consolidated return for the taxable year.

(n) Export trade corporations: Senate amendment No. 126, which adds a new subpart G to part III of subchapter N of chapter 1 of the code, provides that the subpart F income of a controlled foreign corporation which is an export trade corporation shall be reduced by the export trade income of such corporation which constitutes foreign base company income. In general, this provision applies to controlled foreign corporations which derive more than 75 percent of their gross income from (1) the sale of property produced in the United States to unrelated persons for use outside the United States, (2) the performance of certain services outside the United States for unrelated persons, (3) the use of export property by unrelated persons, and (4) the receipt of interest on obligations which qualify as export trade assets. However, the amount of export trade income which reduces subpart F income is limited to the lesser of (1) an amount equal to 1½ times certain export promotion expenses of the controlled foreign corporation, or (2) an amount equal to 10 percent of the gross receipts of such corporation from the transactions described above. In addition, the amount of export trade income which reduces subpart F income can in no event exceed on overall limitation based on the increase in investments in export trade assets.

(o) Miscellaneous: The committee of conference was informed by the Treasury Department of the policy it plans to follow in the granting of rulings under section 367 of the Internal Revenue Code of 1954 in situations in which taxpayers seek to reorganize, during a reasonable period after the enactment of the bill, their foreign corporate structures in response to the enactment of section 12 of the bill as agreed to in conference.

The Treasury Department, for purposes of section 367, will not treat a transaction involving the reorganization of foreign corporate structures as being in pursuance of a plan having as one of its principal purposes the avoidance of Federal income taxes solely by reason of the fact that a principal purpose of the reorganization is to terminate a method of operation which would result in the tax to U.S. shareholders under the provisions of section 12 of the bill. In such cases a favorable ruling under section 367 will generally not be denied by the Treasury Department in transactions in which earnings and profits of foreign corporations are

carried over to other foreign corporations under circumstances in which there will be no reduction of the U.S. taxes (and foreign taxes) that would be payable on the eventual remittance of such earnings and profits to U.S. shareholders.

Under present administrative rules, where corporate shareholders are involved the Treasury Department generally does not issue rulings under section 367 which permit the tax-free remittance to the United States of earnings and profits of foreign corporations. However, under existing practice a ruling permitting a tax-free exchange is generally given a subject to a condition that an appropriate amount be included in the income of the domestic shareholder (thus negating the existence of a principal purpose to avoid U.S. tax). Such rulings will continue to be given each though a principal purpose of the transaction is (1) to terminate the activities of a foreign corporation which would result in tax to U.S. shareholders under the provisions of section 12 of the bill, and (2) to carry on such activities in the future through a domestic corporation.

The conferees recognize that the problems in this area are complex and that particular aspects of the policy as explained above may require qualification and refinement as experience is gained in applying it to particular situations.

The conferees on the part of the Senate called attention to the colloquy in the Senate with respect to the amendment offered in the Senate relating to corporations engaged in producing or selling books or other media of communications, etc. (see pp. 17511-17513 of the daily CONGRESSIONAL RECORD for Sept. 5, 1962). The conferees were advised that the substance of this amendment was not within the jurisdiction of the conference committee. However, the conferees have requested the Treasury Department to study this matter and report back next year to the Committees on Ways and Means and Finance.

GAIN FROM DISPOSITIONS OF CERTAIN DEPRECIABLE PROPERTY

Amendments Nos. 128, 129, 130, and 131: The bill as passed by both the House and the Senate adds a new section 1245 to the code. In general, the new section provides for the treatment as ordinary income of the gain from the disposition of certain depreciable property to the extent of depreciation deductions (taken in periods specified in the bill) which are reflected in the adjusted basis of the property.

Under the bill as passed by the House, the new section 1245 applied to property disposed of after the date of the enactment of the bill and to the extent of adjustments for depreciation and certain amortization for taxable years beginning after December 31, 1961. Under Senate amendment No. 128, the new section applies to property disposed of during a taxable year beginning after December 31, 1962. Under Senate amendments Nos. 129, 130, and 131, the adjustments taken into account are those attributable to periods after December 31, 1961. The House recedes.

Amendment No. 132: The bill as passed by both the House and the Senate amends section 167 of the code to permit a taxpayer to elect to change his method of depreciation in respect of section 1245 property from any declining balance or sum of the years-digits method to the straight line method. Under the bill as passed by the House, the election was required to be made within the period after the date of the enactment of the bill prescribed by the Secretary of the Treasury or his delegate. Under Senate amendment No. 132, the election must be made by the taxpayer on or before the last day prescribed by law (including extensions thereof) for filing his return for his first taxable year be-

ginning after December 31, 1962. The House recedes.

Amendment No. 133: This amendment adds a new provision to the bill inserting a new sentence after the second sentence of section 613(a) of the code, relating to the general rule for computing percentage depletion. The new sentence, which does not affect the computation of the gross income from the property under the first sentence of section 613(a), provides that the allowable deductions taken into account with respect to expenses of mining in computing the taxable income from the property shall, for purposes of the 50-percent limitation contained in the second sentence of section 613(a), be decreased by an amount equal to so much of any gain which (1) is treated under new section 1245 of the code (relating to gain from disposition of certain depreciable property) as ordinary income, and (2) is properly allocable to the property. The House recedes.

Amendment No. 135: Under the bill as passed by the House, the amendments made by the bill relating to gain from dispositions of certain depreciable property (new sec. 1245), including the election to change the method of depreciation with respect to section 1245 property, the amount taken into account as salvage value, and the special rule for charitable contributions of section 1245 property, were to apply to taxable years beginning after December 31, 1961, and ending after the date of the enactment of the bill. Under Senate amendment No. 135, the amendments (except the amendments with respect to salvage value, which take effect as provided by the bill as passed by the House) are to apply to taxable years beginning after December 31, 1962. The House recedes.

FOREIGN INVESTMENT COMPANIES

Amendments Nos. 140 and 141: The bill as passed by both the House and the Senate adds a new section 1246 to the code, relating to gain on foreign investment company stock.

Under the bill as passed by the House, a foreign investment company was defined as any foreign corporation which met one of two alternative tests. Under Senate amendment No. 140, either of these two tests must be met for any taxable year beginning after December 31, 1962. One test is registration under the Investment Company Act of 1940 either as a management company or as a unit investment trust. The second test (which must be met at a time when more than 50 percent of either the voting power or total value of the stock is held by U.S. persons) under the House bill was that the foreign corporation must be engaged (or holding itself out as being engaged) primarily in the business of investing, reinvesting, or trading in securities (within the meaning of section 3(a)(1) of the Investment Company Act of 1940). Senate amendment No. 141, in effect, excludes from the second test certain foreign corporations such as brokers, banks, and small loan companies. The House recedes on Senate amendments Nos. 140 and 141.

Amendment No. 143: Subsection (e)(1) of section 1246 added to the code by the bill provides that the basis of stock of a foreign investment company acquired from a decedent dying after December 31, 1962, is to be reduced by the amount of the decedent's ratable share of earnings and profits. Under the bill as passed by the House, the ratable share was of the accumulated earnings and profits of the company. Under Senate amendment No. 143, the ratable share is of the earnings and profits accumulated after December 31, 1962. The House recedes.

Amendment No. 145: This amendment adds a new subsection (g) to the new section 1246 of the code. The new subsection (g) provides that if a registered foreign in-

vestment company has made an election (under the new sec. 1247 added by the bill) to distribute income currently with respect to taxable years beginning after December 31, 1962, then section 367 of the code is not to apply in respect of such foreign investment company if the company is a party to a reorganization in which all of its properties are acquired before January 1, 1964, by a domestic corporation which is a regulated investment company under section 851 for this first taxable year ending after the reorganization. The committee of conference was informed by the Treasury Department that the proposed new subsection was not needed in view of the administrative practices under section 367 of the code, and might therefore imply that such practices are erroneous. The Senate recedes.

Amendment No. 147: New section 1247 added to the code by the bill provides that new section 1246 of the code (treating gain on sale or exchange of foreign investment company stock as ordinary income) is not to apply to the qualified shareholders of a registered foreign investment company if the company elects on or before December 31, 1962, with respect to each taxable year beginning after such date, to distribute 90 percent or more of its taxable income currently and to designate in a written notice to its shareholders the prorata amount of the excess of the net long-term capital gain over the net short-term capital loss and the portion thereof which is being distributed. Under the bill as passed by the House, the notice must be mailed before the expiration of 30 days after the close of the taxable year. Under Senate amendment No. 147, the notice must be mailed before the expiration of 45 days after the close of the taxable year. The House recedes.

Amendment No. 153: This amendment strikes out subsection (d) of the new section 1247 added to the code by the bill and inserts subsections (d), (e), (f), and (g).

Under the Senate amendment the new subsection (d) requires each qualified shareholder of a foreign investment company with respect to which an election under section 1247 is in effect to compute his long-term capital gains by including his pro rata share of the distributed portion of the company's excess of net long-term capital gain over net short-term capital loss and his pro rata share of the undistributed portion of such excess. Subsection (e) is the same as subsection (d) as passed by the House in requiring proper adjustment in the earnings and profits of the company and in the adjusted basis of stock of such company held by such shareholder to reflect such shareholder's inclusion in gross income of undistributed capital gains, but also requires proper adjustment in a qualified shareholder's ratable share of the company's earnings and profits.

Subsections (f), (g), and (h) are new provisions relating to the election by a foreign investment company with respect to foreign taxes. Under subsection (f), a foreign investment company which has elected to distribute income currently and more than 50 percent of the value of whose total assets at the close of the taxable year consists of stock or securities in foreign corporations may elect (for such taxable year and for purposes of complying with its election to distribute 90 percent or more of its taxable income) to compute its taxable income without any deduction for income, etc., taxes paid to foreign countries or possessions of the United States and to treat the amount of such taxes as distributed to its shareholders. If the election is made each qualified shareholder of the company is required (1) to include in gross income and treat as paid by him his proportionate share of such taxes, and (2) for purposes of the foreign tax credit, to treat such share of taxes as hav-

ing been paid to the country in which the company is incorporated and to treat as gross income from sources within such country such share of taxes and any dividend paid to him by the company. Subsection (g) provides for notice to the shareholders of their proportionate share of the taxes to be taken into account as provided in subsection (f). Subsection (h) provides that the election and notice are to be made in such manner as the Secretary of the Treasury or his delegate may prescribe by regulations. The House recedes.

GAIN FROM CERTAIN SALES OR EXCHANGES OF STOCK IN CERTAIN FOREIGN CORPORATIONS

Amendments Nos. 159 and 160: The bill as passed by the House added a new section 1248 to the code which provided, in general, that (1) if a U.S. person owned, or was considered to have owned, 10 percent or more of the voting stock of a foreign corporation on the date he sells or exchanges stock in such corporation or during the 5-year period ending on such date, and (2) the foreign corporation was a controlled foreign corporation on the date of the sale or exchange or during the 5-year period ending on such date, then (1) gain recognized on the sale or exchange, other than in redemption or liquidation of such stock, would, to the extent of the earnings and profits of the corporation attributable to the stock sold or exchanged, be considered gain from the sale of property which is not a capital asset, and (2) gain recognized on a distribution in redemption or liquidation of such corporation would, to the extent of the earnings and profits of the corporation attributable to the stock exchange, be treated as a dividend. The new section 1248 provided for the reduction in the earnings and profits of a foreign corporation by amounts included in gross income of a U.S. person as subpart F income or as amounts invested in nonqualified property, but only to the extent such amounts did not result in an exclusion from gross income. The bill did not apply to distributions in redemption of stock to pay death taxes, consideration received in an exchange to which section 366 applied, or to amounts includible in gross income under any other provision of the code as a dividend, gain from the sale of an asset which is not a capital asset, or gain from the sale of an asset held for not more than 6 months.

Senate amendment No. 159 provides that (a) if a U.S. person sells or exchanges stock in a foreign corporation (including distributions in redemption or liquidation), and (b) such person owns, or is considered to own, 10 percent or more of the voting stock of such corporation at any time during the 5-year period ending on the date of sale or exchange on a date when such corporation was a controlled foreign corporation, then the gain shall be includible in the gross income of such U.S. person as a dividend, to the extent of the earnings and profits of the foreign corporation accumulated (1) in taxable years of the corporation beginning after December 31, 1962, (2) while the stock sold or exchanged was held by the U.S. person, and (3) while the foreign corporation was a controlled foreign corporation.

Senate amendment No. 159 provides that earnings and profits of a foreign corporation are to be determined according to rules substantially similar to those applicable to domestic corporations, except that the earnings and profits are to be reduced with respect to a U.S. person by amounts included in gross income under section 951, gain realized from the sale or exchange of property in pursuance of a plan of complete liquidation, income derived from sources within the United States of a foreign corporation engaged in trade or business within the United States, amounts included in gross income of a qualified shareholder of a foreign investment company, and, in some cases, by earnings and profits accumulated

while the foreign corporation was a less developed country corporation.

Under Senate amendment No. 159, the earnings and profits of a foreign corporation whose stock is sold or exchanged is, under certain circumstances, deemed to include earnings and profits of foreign corporations in a chain of corporations. The Senate amendment also provides that if a domestic corporation was formed or availed of principally for the holding, directly or indirectly, of stock of one or more foreign corporations, the sale or exchange of the stock of the domestic corporation will be treated as a sale or exchange of the stock of the foreign corporation or corporations held by the domestic corporation.

The new section 1248, as amended by Senate amendment No. 159, provides a limitation on the tax imposed on an individual who is a U.S. person by reason of the application of the new section. In general, the tax so imposed is not to exceed the greater of (1) his pro rata share of the taxes which would have been imposed if the foreign corporation had been a domestic corporation during the period he held the stock sold or exchanged, or (2) the taxes which would have been imposed if the amounts to which the section applies had been received as dividends in the years in which earned by the foreign corporation. With respect to Senate amendment No. 159, the House recedes with amendments which (1) eliminate the second limitation described in the preceding sentence, and (2) make clerical and conforming changes.

Under the bill as passed by the House, the new section 1248 applied to sales or exchanges after the date of the enactment of the bill. Senate amendment No. 160 provides that the new section shall apply to sales or exchanges after December 31, 1962. The House recedes.

SALES AND EXCHANGES OF PATENTS, ETC., TO CERTAIN FOREIGN CORPORATIONS

Amendment No. 161: Senate amendment No. 161 adds a new section to the bill which adds a new section 1249 to the code, relating to gain of a U.S. person from the sale or exchange after December 31, 1962, of a patent, invention, model, or design (whether or not patented), copyright, secret formula or process, or similar property right to a foreign corporation which such person controls (within the meaning of the new sec. 1249). If such gain would (but for the new section) be gain from the sale or exchange of a capital asset or of property described in section 1231, then such gain is to be considered as gain from the sale or exchange of property which is neither a capital asset nor property described in section 1231. Under subsection (c) of the new section 1249, the new section would not apply, however, to gain realized from the sale or exchange for stock or contribution to capital of such property where it is established to the satisfaction of the Secretary of the Treasury or his delegate that the principal purpose of the transfer is to enable the foreign corporation to use the property in its own manufacturing operations. The new section 1249 applies to taxable years beginning after December 31, 1962.

Under the conference agreement, the House recedes with an amendment striking out subsection (c) of the new section 1249. With the deletion of subsection (c), the new section 1249 provides ordinary income treatment for all taxable sales or exchanges of patents (and other property covered by the provision) by a domestic corporation to a foreign corporation which it controls. The new section 1249 would not apply to nontaxable transactions such as those sales or exchanges to which (as the result of a ruling under sec. 367) section 351 of the code applies. Neither the enactment of section 1249 nor the deletion of the exception in subsection (c) is intended to have any implications with re-

spect to the application of section 367 of the code to such nontaxable transactions.

The conferees requested the Treasury Department to study and report back on the proper tax treatment of the transfer of patents, etc., to foreign subsidiaries which use such property in their own manufacturing operations.

TAX TREATMENT OF COOPERATIVES AND PATRONS

Amendments Nos. 162, 163, 166, 167, and 168: The bill as passed by the House provides that, in computing the taxable income of a cooperative organization, certain distributions paid to patrons in the form of qualified written notices of allocation are to be treated as deductions from the cooperative's gross income. The recipients of such qualified written notices of allocation are required to include the stated dollar amount of such allocations in their gross income when received. A written notice of allocation is qualified only if (1) it is payable in cash within 90 days at the option of the patron, or (2) the patron has consented to include the stated dollar amount of this written notice of allocation in his gross income. Senate amendment No. 163 contains a further requirement which provides that a written notice of allocation is not a qualified one unless 20 percent or more of the distribution of which it is a part is paid in money or by qualified check.

The bill as passed by the House provides two methods by which a patron may consent to the inclusion in his gross income of the stated dollar amount of qualified written notices of allocation not redeemable in cash within the period provided in the bill. Senate amendments Nos. 162 and 166 provide a third method by which such consent may be made. Under this third method a patron may consent by endorsing and cashing (within the time prescribed by the amendment) a qualified check which is paid as a part of the same distribution as the written notice of allocation. Under Senate amendment No. 167, a qualified check is defined as a check (or other instrument redeemable in money) on which there is a clearly imprinted statement that the endorsement and cashing of the check (or other instrument) constitutes the consent of the payee to include in his gross income, as provided in the Federal income tax laws, the stated dollar amount of the written notice of allocation which is a part of the patronage dividend or payment of which such qualified check is also a part. Under Senate amendment No. 168, if a qualified check is not cashed on or before the 90th day after the close of the payment period for the taxable year with respect to which it is paid, such check becomes a non-qualified written notice of allocation. The House recedes on amendments Nos. 162, 163, 166, 167, and 168.

WITHHOLDING OF INCOME TAX AT SOURCE ON INTEREST, DIVIDENDS, AND PATRONAGE DIVIDENDS; REPORTING OF INTEREST, DIVIDEND, AND PATRONAGE DIVIDEND PAYMENTS OF \$10 OR MORE DURING A YEAR

Amendment No. 173: Section 19 of the bill as passed by the House added to the Internal Revenue Code of 1954 provisions requiring the withholding of income tax at source on certain interest, dividend, and patronage dividend payments. The tax was to be withheld at the rate of 20 percent and was to apply to payments of interest, dividends, and patronage dividends as those terms were defined for withholding purposes. In addition, the bill as passed by the House provided for exemptions from withholding, quarterly refunds, and special credits. The tax withheld was to be allowed as a credit against the income tax of the recipients of the payments to the extent it had not been previously refunded to them or credited against other tax due from them.

Amendment No. 173 strikes out the provisions of section 19 of the bill as passed by

the House and, in lieu thereof, adds to the Internal Revenue Code of 1954 provisions requiring persons who make payments of dividends, patronage dividends, or interest (within the meaning of such terms as defined in the Senate amendments) aggregating \$10 or more to any other person in a calendar year to file an information return with the Secretary of the Treasury or his delegate with respect to such payments. The Senate amendment adds provisions requiring that payors of dividends, patronage dividends, and interest (as those terms are defined by the amendment) furnish to the recipients of these amounts annual statements showing the amounts paid to them as reported on the information returns filed with the Internal Revenue Service. New penalty provisions are provided by the Senate amendment for failure to file information returns with respect to payments of dividends, patronage dividends, or interest, and for failure to furnish to a recipient of such payments an annual statement of such payments.

The House recedes with clerical amendments. As a part of the agreement to the Senate amendment, the House and Senate conferees have requested the Treasury Department to make annual reports to the Committees on Ways and Means and Finance on the improvement in the reporting on tax returns of dividends, interest, and patronage dividends as a result of the Senate amendment, with the view that this matter will be reconsidered by the Committees on Ways and Means and Finance if it is determined that there has not been sufficient improvement in the reporting of such income.

INFORMATION WITH RESPECT TO CERTAIN FOREIGN ENTITIES

Amendment No. 176: Section 6038(b) of the code, as contained in the bill as passed by both the House and the Senate, provides for a reduction in foreign tax credit for each failure to furnish information with respect to a foreign corporation controlled by a U.S. person. Senate amendment No. 176 provides that such reduction is not to exceed whichever of the following amounts is greater: (A) \$10,000, or (B) the income of the foreign corporation for its annual accounting period with respect to which the failure occurs. The House recedes.

Amendment No. 179: Section 6038(d) (1) of the code as contained in the bill as passed by the House provided that, in applying the constructive ownership rules of section 318(a) of the code for purposes of determining control under section 6038 of the code, the rule which requires ownership of 50 percent of the stock of a corporation before stock owned by such corporation is attributed to its stockholders was to apply without regard to the 50-percent limitation. Senate amendment No. 179 substitutes a 10-percent limitation for the 50-percent limitation. Senate amendment No. 179 also provides that the rules of section 318(a) (2) of the code that stock owned by a partner or a beneficiary of an estate or trust will be considered as owned by the partnership, estate, or trust, are not to be applied so as to consider a U.S. person as owning stock which is owned by a person who is not a U.S. person, nor will a corporation be considered as owning stock owned by or for a 50 percent or more stockholder where the effect is to consider a U.S. person as owning stock which is owned by a person who is not a U.S. person. The House recedes.

Amendments Nos. 180 and 181: Section 6046 (a) and (b) of the code, as amended by the bill as passed by the House, required each U.S. citizen or resident who (on or after January 1, 1963) was or becomes an officer or director of a foreign corporation and each U.S. person who (on or after January 1, 1963) was or becomes an owner of 5 percent or more in value of the stock of such a corporation to file an information return setting forth such information as the Secretary

of the Treasury or his delegate prescribes by forms or regulations as necessary for carrying out the provisions of the income tax laws. Under Senate amendment No. 180, such an officer or director is required to file an information return only if 5 percent or more in value of the stock of the foreign corporation is owned by a U.S. person. Under Senate amendment No. 181, in the case of an officer or director of the foreign corporation, the information required is limited to furnishing the names and addresses of the U.S. persons who own 5 percent or more in value of the stock of such corporation. The House recedes on amendment No. 180 with a technical amendment. The House recedes on amendment No. 181.

Amendment No. 183: This amendment adds a new subsection (e) to section 6046 of the code. Under the new subsection, no information is to be required to be furnished under section 6046 with respect to any foreign corporation (1) if the liability of the U.S. citizen, resident, or person to file a return under section 6046(a) arises on or after January 1, 1963, and before March 1, 1963, unless such information is required to be furnished under regulations which have been in effect since January 1, 1963 (but only if such regulations were prescribed before December 1, 1962), or (2) if the liability of the U.S. citizen, resident, or person to file a return under section 6046(a) arises on or after March 1, 1963, unless such information is required to be furnished under regulations which have been in effect for at least 90 days.

Under the conference agreement, the House recedes with an amendment substituting a new subsection (e). Under the conference agreement, in the case of liability to file a return under section 6046 of the code arising on or after January 1, 1963, and before June 1, 1963—

(A) no information is to be required to be furnished under section 6046 with respect to any foreign corporation unless such information was required to be furnished under regulations in effect on or before March 1, 1963, and

(B) if the date on which such regulations become effective is later than the day on which such liability arises, any return required by section 6046(a) is required (in lieu of the time prescribed by sec. 6046(d)) to be filed on or before the 90th day after such date.

In the case of liability to file a return under section 6046(a) arising on or after June 1, 1963, no information is to be required to be furnished under section 6046 with respect to any foreign corporation unless such information was required to be furnished under regulations which have been in effect for at least 90 days before the date on which the U.S. citizen, resident, or person becomes liable to file a return required under section 6046(a).

EXPENDITURES BY FARMERS FOR CLEARING LAND

Amendment No. 189: This amendment adds a new section to the bill, adding a new section 182 to part VI of subchapter B of chapter 1 of the code (relating to itemized deductions for individuals and corporations). The new section 182 permits farmers to elect to treat as deductible expenses, rather than as nondeductible expenditures for capital improvements to property, expenditures for the clearing of land (including a reasonable allowance for depreciation with respect to depreciable property used in the clearing of land) if such expenditures are for the purpose of making the land suitable for use in farming. The term "clearing of land" includes the eradication of trees, stumps, and brush, the treatment or moving of earth, and the diversion of streams and watercourses. The new section 182 limits the deduction for expenditures for the clearing of land for any taxable year to \$5,000 or to 25 percent of the taxable income derived from farming during

the taxable year, whichever amount is the lesser. The new section applies to taxable years beginning after December 31, 1962. The House recedes with clerical and conforming amendments.

CHARITABLE CONTRIBUTIONS MADE FROM INCOME ATTRIBUTABLE TO SEVERAL TAXABLE YEARS

Amendment No. 190: This amendment adds a new section to the bill, adding a new subsection (e) to section 1307 of the code, relating to rules applicable to part I of subchapter Q of chapter 1 of such code (which relates to income attributable to several taxable years).

When income attributable to several taxable years is received or accrued in a particular taxable year, part I of subchapter Q provides, under certain circumstances, that the tax attributable thereto for the taxable year in which it is received or accrued is, in general, not to be greater than the aggregate increases in taxes which would have resulted if the amount had been included in the taxpayer's income, on an allocated basis, over the period specified in the applicable section of such part I.

New subsection (e) provides that an individual who receives or accrues in a taxable year an amount to which part I of subchapter Q applies may elect (in such manner and at such time as the Secretary of the Treasury or his delegate prescribes by regulations) to apply the provisions of subsection (e) in computing his tax liability under such part. If the taxpayer so elects, the amount received or accrued shall be reduced, for the purposes of computing his tax liability under such part I with respect to such amount, by an amount (1) which bears the same ratio to the amount of his allowable charitable deduction for the taxable year in which the amount was received or accrued (computed without regard to pt. I of subch. Q) as (2) the amount received or accrued during the taxable year to which part I applies bears to the adjusted gross income for such year (computed without regard to pt. I of subch. Q).

New subsection (e) further provides that no portion of the amount received or accrued to which part I of subchapter Q applies shall (for purposes of computing the limitation on tax under such part) be taken into account for purposes of computing the limitation under section 170(b)(1) of the code for the taxable year in which the amount to which such part applies is received or accrued.

The House recedes with an amendment which is technical and clarifying in nature and is a substitute for the provision described in the preceding paragraph.

EFFECTIVE DATE OF SECTION 1371(c) OF THE INTERNAL REVENUE CODE OF 1954

Amendment No. 191: The Senate amendment adds a new section to the bill as passed by the House which provides that section 1371(c) of the code (relating to the determination of the number of shareholders of a small business corporation where stock is owned by a husband and wife) is, subject to the provisions for filing of election and consents described below, to apply to taxable years beginning after December 31, 1957, and before January 1, 1960. Under existing law, section 1371(c), which was added to the code by section 2(a) of Public Law 86-376 (approved September 23, 1959), applies only to taxable years beginning after December 31, 1959. The Senate amendment provides a 1-year period within which an otherwise qualifying small business corporation may make a special election to have the earlier effective date of section 1371(c) apply. For the special election to be valid, a corporation must have previously filed a timely election to have its income taxed directly to its shareholders, and each person who is a shareholder at the time of the special election (as

well as each person who was a shareholder for any taxable year beginning after December 31, 1957, and ending before the date on which the special election is made) must give his consent. The amendment also provides that where a special election (and the requisite consents) has been made, the statute of limitations for assessing additional tax against the corporation or the shareholders attributable to the earlier effective date of section 1371(c) (and the statute of limitations for allowing a credit or refund of any overpayment of tax by the corporation or its shareholders attributable to the earlier effective date of section 1371(c)) is to remain open, or be opened, for 1 year following the date of the election. The House recedes.

CERTAIN LOSSES SUSTAINED IN CONVERTING FROM STREET RAILWAY TO BUS OPERATIONS

Amendment No. 192: The Senate amendment adds a new section to the bill as passed by the House which provides that in the case of net operating losses incurred in the calendar years 1953 and 1954 principally as the result of conversion from street railway to bus operations, an additional 5 years, beginning with 1960, is to be allowed for the carry-over of such losses. The Senate amendment applies only for years in which the taxpayer is engaged in the furnishing or sale of transportation (as defined in sec. 1503(c)(1)(A) of the 1954 code). The House recedes with a technical amendment.

PENSION PLAN OF LOCAL UNION NO. 435, INTERNATIONAL HOD CARRIERS' BUILDING AND COMMON LABORERS' UNION OF AMERICA

Amendment No. 193: The Senate amendment adds a new section to the bill as passed by the House which provides that the pension plan of Local Union No. 435 of the International Hod Carriers' Building and Common Laborers' Union of America, which was negotiated to take effect May 1, 1960, pursuant to an agreement between such union and the Building Trades Employers Association of Rochester, N.Y., shall be held and considered to have been a qualified trust under section 401(a) of the code, and to have been exempt from taxation under section 501(a) of the code, for the period beginning May 1, 1960, and ending April 20, 1961, but only if it is shown to the satisfaction of the Secretary of the Treasury or his delegate that the trust has not in this period been operated in a manner which would jeopardize the interests of its beneficiaries. The House recedes.

CONTINUATION OF A PARTNERSHIP YEAR FOR SURVIVING PARTNER IN A TWO-MAN PARTNERSHIP WHERE ONE DIES

Amendment No. 194: The Senate amendment adds a new section to the bill as passed by the House which amends section 188 of the Internal Revenue Code of 1939 (relating to different taxable years of partner and partnership) to provide that for purposes of chapter 1 of the 1939 code, if the surviving partner so elects within 1 year after the date of enactment of this bill, the death of one of the partners of a partnership consisting of two members shall not result in the termination of the partnership or in the closing of the taxable year of the partnership with respect to the surviving partner prior to the time the partnership year would have closed if neither partner had died or disposed of his interest. The amendment is to apply to taxable years of a partnership beginning after December 31, 1946, to which the Internal Revenue Code of 1939 applies. The amendment further provides that if refund or credit of any overpayment resulting from the application of such amendment was prevented on the date of the enactment of the bill, or at any time within 1 year from such date by the operation of any law or rule of law (other than those relating to closing agreements and compromises), refund or credit of such overpayment may, nevertheless, be made or

allowed if claim therefor is filed within 1 year after the date of enactment of the bill. No interest is to be allowed or paid on any overpayment resulting from the application of the amendment. The House recedes.

EXCLUSION FROM GROSS INCOME OF CERTAIN AWARDS MADE PURSUANT TO EVACUATION CLAIMS OF JAPANESE-AMERICANS

Amendment No. 195: This amendment, which adds a new section to the bill, provides that awards received under the Japanese-American Evacuation Claims Act, as amended in 1951 and 1956 (50 U.S.C. App., secs. 1981-1987), are not to be included in gross income for purposes of chapter 1 of the Internal Revenue Code of 1939 or 1954. This treatment is to apply with respect to taxable years ending after July 2, 1948.

Any refund or credit of an overpayment of Federal income tax (including interest, additions to the tax, additional amounts, and penalties) resulting from this provision which is barred on the date of the enactment of this bill, or within 1 year from such date, by any law or rule of law may, nevertheless, be made, without interest, if a claim for such refund or credit is filed within 1 year after the date of enactment of the bill. In the case of any claim described in the preceding sentence, the amount to be refunded or credited as an overpayment is not to be diminished by any credit or setoff based on any item other than the amount of the award.

The House recedes with technical amendments.

DEDUCTION FOR BUSINESS DEPRECIATION BY TENANT-STOCKHOLDER OF COOPERATIVE HOUSING CORPORATION

Amendment No. 196: This amendment adds a new section to the bill, adding a new subsection (c) to section 216 of the code (relating to amounts representing taxes and interest paid to a cooperative housing corporation).

The new subsection (c) provides that so much of the stock of a tenant-stockholder in a cooperative housing corporation as is allocable, under regulations prescribed by the Secretary of the Treasury or his delegate, to a proprietary lease or right of tenancy in property subject to the allowance for depreciation under section 167(a) shall, to the extent that such proprietary lease or right of tenancy is used by such tenant-stockholder in a trade or business or for the production of income, be treated as property subject to the allowance for depreciation under section 167(a). The amendment is effective with respect to taxable years beginning after December 31, 1961. The House recedes with clerical amendments.

EXCLUSION FROM GROSS INCOME OF GAIN FROM SALE OF RESIDENCE BY INDIVIDUAL AGE 65 OR OVER

Amendment No. 197: This amendment added a new section to the bill, adding a new section 121 to part III of subchapter E of chapter 1 of the code (relating to items specifically excluded from gross income). The new section 121, applicable only in the case of individuals, provided that gross income does not include gain from the sale, exchange, or involuntary conversion (within the meaning of sec. 121(e)) after December 31, 1962, of property used by the taxpayer as his principal residence, if (1) the taxpayer had attained the age of 65 years before the sale, exchange, or involuntary conversion, and (2) the property had been used by the taxpayer as his principal residence for a period of not less than 5 years at the time of its sale, exchange, or involuntary conversion. The Senate recedes.

DEDUCTION FOR INCOME TAX PURPOSES OF CONTRIBUTIONS TO CERTAIN ORGANIZATIONS FOR JUDICIAL REFORM

Amendment No. 198: This amendment, which adds a new section to the bill, provides that a contribution or gift made after

December 31, 1961, with respect to a referendum occurring during the calendar year 1962, shall be deductible as a charitable contribution under section 170 of the code if made to, or for the use of, an organization created and operated exclusively to consider proposals for the reorganization of the judicial branch of any State or local government and to provide information, make recommendations, and seek public support or opposition to such proposals. For contributions or gifts to be eligible for this treatment, no part of the net earnings of the organization may inure to the benefit of any private shareholder or individual and the organization must not participate in any political campaign in behalf of, or in opposition to, any candidate for public office. The House recedes with a clerical amendment.

AMENDMENT TO SOCIAL SECURITY ACT RELATING TO STATEMENT OF FINANCIAL STATUS OF CLAIMANTS FOR MEDICAL ASSISTANCE FOR THE AGED

Amendment No. 199: This amendment added to the bill a new section, amending section 2(a) of the Social Security Act so as to permit a State to provide in its State plan under title I of such act that any written statement required of a claimant for medical assistance for the aged under that title shall be presumed by the State agency administering the plan to be factually correct for purposes of determining eligibility for such assistance insofar as the statement relates to the claimant's financial status. The Senate recedes.

FOREIGN SUBSIDIARIES MANUFACTURING PRODUCTS ABROAD FOR SALE IN THE UNITED STATES

Amendment No. 200: Senate amendment No. 200 added a new section to the bill to provide that foreign corporations to which the proposed new section, section 885 of the code, applies are deemed to be engaged in trade or business within the United States, and their gross income from sources within the United States is deemed to be not less than their gross income from the sale of competitive articles sold for ultimate use, consumption, or disposition in the United States. The new section applied to a foreign corporation if at any time during the taxable year one or more domestic corporations own, directly or through one or more other corporations, 10 percent or more of the outstanding stock of the foreign corporation, and if for such taxable year the foreign corporation derives 10 percent or more of its gross income from the sale of competitive articles sold for ultimate use, consumption, or disposition in the United States. For such purpose a competitive article is any article mined, processed, or manufactured outside the United States for a foreign corporation which is the same as or similar to any article mined, processed, or manufactured in the United States (or formerly mined, processed, or manufactured in the United States) by any domestic corporation described in the preceding sentence with respect to the foreign corporation, or by any subsidiary of such domestic corporation. The new provision applied to taxable years beginning after December 31, 1962. The Senate recedes.

EFFECTIVE DATE OF AMENDMENT TO SECTION 1374(b) OF INTERNAL REVENUE CODE OF 1954

Amendment No. 201: The Senate amendment adds a new section to the bill as passed by the House which makes the amendment to section 1374(b) of the code, which was added by section 2(b) of Public Law 86-376 (approved Sept. 23, 1959), effective on September 2, 1958. Under existing law, the amendment to section 1374(b), which permits the deduction of a deceased shareholder's pro rata share of the net operating loss of an electing small business corporation incurred in the year in which he dies, is

effective only with respect to taxpayers who die after September 23, 1959. The House recedes with a clerical amendment.

TREATIES

Amendment No. 203: The bill as passed by the House provided that section 7852(d) of the code, relating to treaty obligations, was not to apply in respect of any amendment made by the Revenue Act of 1962. Senate amendment No. 203 provides that no provision of the Revenue Act of 1962 will apply in any case where its application would be contrary to any treaty obligation of the United States.

The Senate recedes. In this connection, the Treasury Department informed the committee of conference that it is its view that there are no conflicts between provisions of the bill and provisions of tax treaties, with one minor exception relating to the real estate clause of the Greek Estate Tax Treaty which the Treasury will seek to have renegotiated before July 1, 1964.

WILBUR D. MILLS,
CECIL R. KING,
HALE BOGGS,
EUGENE J. KEOGH,
JOHN W. BYRNES,
HOWARD H. BAKER,

Managers on the Part of the House.

FEDERAL AID FOR THE TRAINING OF HEALTH PERSONNEL

(Mr. MATHIAS (at the request of Mr. DEVINE) was granted permission to extend his remarks at this point in the RECORD and to include extraneous matter.)

Mr. MATHIAS. Mr. Speaker, this Congress has regrettably lost its opportunity to help meet the serious problems of higher education in this period of expanding enrollments and rising instructional costs. It is still not too late, however, to provide critically needed assistance to the schools which train our physicians, dentists, and public health specialists.

Whether we meet this responsibility will largely determine whether the Nation has an adequate supply of well-trained professional health personnel in the years ahead. H.R. 4999, which has been favorably reported by the Interstate and Foreign Commerce Committee, will help meet this responsibility. It provides for a 10-year program of matching grants for construction of medical teaching facilities, a 5-year program of loans to medical students, and a 3-year extension of the health research facilities construction program.

I am glad that the Rules Committee has granted a rule on this bill and I urge the Congress to act favorably on it before adjournment so that Americans may continue to receive the quality medical care of which we as a nation are so rightfully proud.

The need for Federal assistance in this area has long been recognized, and is long overdue. Such a program was first recommended by President Eisenhower in 1956: In a special health message in that year, he noted that:

The rate at which physicians are being graduated from the Nation's medical schools is barely keeping pace with the increase in population. There are serious shortages in such specialized fields as psychiatry, pediatrics, and in physical medicine and rehabilitation. Relative to population, the number of dentists and nurses is diminishing. The aging of our population and the increase in the incidence of chronic disease,

the anticipated continued growth of voluntary health insurance plans, and the general expansion of our economy—all will tend to increase the demand for health services.

Since that time the shortage of medical personnel has grown more acute. In 1960 the Surgeon General's Consultant Group on Medical Education estimated that by 1975 we must increase the annual output of our medical schools by 50 percent and our dental schools by 75 percent, simply to achieve the minimal national objective of maintaining the present ratio of physicians to population.

Furthermore, we are already a debtor nation in regard to our supply of young physicians: we are relying on an increasing number of foreign trained doctors to staff our hospitals and provide medical services in communities throughout the country. The United States should be in a position to export, rather than import, trained health personnel so that we may assist in meeting the needs of the international community.

The necessity for Federal aid in the solution of this problem has been recognized by all the professional associations. Such a program was pledged in the platforms of both the Republican and Democratic parties in 1960. It is time for us to redeem our pledges, and take action to meet our health manpower needs.

REVIEW OF FEDERAL PAY RATES

(Mr. MATHIAS (at the request of Mr. DEVINE) was granted permission to extend his remarks at this point in the RECORD and to include extraneous matter.)

Mr. MATHIAS. Mr. Speaker, provision for annual review of Federal pay rates should insure that employees of the Federal Government will not experience in the future the deceleration in pay scales relative to industry that has gone on over a long period of time. The fact that employees of the Government stand willing, almost to a man, to make financial sacrifices to remain in the service should not be license to either take advantage of them or to forget them.

Federal employees are a popular target because they are not provided with the means by which they can defend themselves. I continue to be impressed with their competence, their loyalty, and their dedication to service. Happily, the time appears near when they will be put on equal financial footing with their counterparts outside of Government.

I urge that this legislation be sent to conference without further delay.

CONSTITUTIONAL CRISIS IN MISSISSIPPI

(Mr. ALFORD was granted permission to extend his remarks in the body of the RECORD and include extraneous matter.)

Mr. ALFORD. Mr. Speaker, for the second time in my life I have seen the unbelievable and unwarranted defiance of the Constitution of the United States by the use of armed force to impose the will of a minority on a sovereign State.

If the reports of harsh and brutal treatment of citizens by armed soldiers and Federal marshals are true, the epi-

sode in my home city, Little Rock, 5 years ago, pales into a tragic memory. Already, according to these reports, lives have been lost and scores have been wounded and injured.

I have seen the bayonets of illegal interventionists glistening in the sun. It is a sight to strike terror into the hearts of all those who love America and cherish its traditions.

The basic issues in this struggle have not been clearly defined and brought into focus. In an effort to accomplish this, I have today sent a telegram to the President of the United States who must bear the full responsibility for this unhappy trend of events.

Under leave to extend my remarks, I include a copy of that telegram dispatched to the White House this morning:

The Honorable JOHN F. KENNEDY,
The White House,
Washington, D.C.

Mr. PRESIDENT: In the name of the American Republic, I deplore that you have made the same tragic mistake as did your predecessor in sending Armed Forces into a sovereign State in complete violation of the rights reserved to the States under our Constitution. Relative to the intervention of the Federal Government in affairs that are prerogatives of a sovereign State under the Constitution, in all sincerity and with the highest purpose to preserve the Republic, all of us should be reminded that the Constitution is not plastic. It cannot be molded or twisted to suit the political designs of a few. The Supreme Court's decision is not "the law of the land" even though in a case the Court may soundly define the meaning of particular words of the Constitution. It is the Constitution which remains "the supreme law of the land" art. VI, and which you and I are under oath to uphold and defend. Under the Constitution the judiciary has no power to make general rules bearing upon the people and governments of the sovereign States. In short, Federal courts cannot amend the Constitution. The present action of the Court toward the State of Mississippi through its orders are in direct conflict with the Constitution, according to the interpretation clearly stated by the framers and adopters of the Constitution, our Founding Fathers. The great moral issue in Mississippi today, therefore, is not segregation versus integration of the schools; it is, instead, the issue of the sovereign people and the Constitution versus defaulting public trustees as oath-breaking usurpers. Shall we have limited government and rule by law as interpreted by the framers and adopters of the Constitution or shall we have usurpers supreme with unlimited powers? Mr. President, shall the American Republic endure or shall we sacrifice our State sovereignty to an all-powerful superstate acting in direct opposition to the will of the majority of the people of a sovereign State and therefore in opposition to the Constitution? I respectfully submit with malice toward no one, but with the love of the American Republic above all political expediency that the use of force in any form convinces even the most intellectually uninformed that our values of patriotism are radically confused. If force is to be used by our National Government, let it be used against our enemy, international communism, Cuba in particular, and not against loyal patriotic Americans who are upholding their rights as guaranteed to them by the Constitution. Listen, well, Mr. President, to what Hamilton, Madison, and Jay, who wrote in the Federalist about the distribution of powers between the Federal Government and the States:

"The powers delegated by the Constitution to the Federal Government are few and defined. Those which are to remain in the

State governments are numerous and indefinite. The former will be exercised principally on external objects as war, peace, negotiation, and foreign commerce. The powers reserved to the several States will extend to all objects, which, in the ordinary course of affairs, concern the internal order and prosperity of the State."

In our beloved country, Mr. President, the people are sovereign.

DALE ALFORD,
Member of Congress.

CHARITABLE CONTRIBUTION CARRYOVER

(Mr. CURTIS of Missouri (at the request of Mr. DEVINE), was given permission to extend his remarks at this point in the RECORD.)

Mr. CURTIS of Missouri. Mr. Speaker, one of the important, if secondary, functions of our Internal Revenue Code is to encourage the allocation of funds by individuals and corporations in this country to purposes which are consistent with our overall national goals. Probably the outstanding example of this operation of the Internal Revenue Code is the deduction given for charitable contributions by taxpayers.

Limitations have been set on the amount of the deductions which one might take for his contributions of this nature. Basically, the upper deduction limit is 20 percent. I am proud to have had a leading role in extending this by an extra 10 percent for contributions made to religious, educational, and medical charities and I have offered legislation seeking to extend this extra 10-percent provision to other contributions, those to libraries and museums (H.R. 7478).

I have today offered another bill in this area of the Internal Revenue Code. This would permit individual taxpayers a 2-year carryover for charitable contribution deductions, just as corporate taxpayers are now allowed. This would further encourage the social use of an individual's funds, turning money into areas in which it can help the entire society—areas such as education and health—and at the same time leaving in the hands of the people, each individual taxpayer, exactly which charity will receive support. This encouragement comes through permitting those whose contributions exceed the current upper limits to carry the amount not absorbed by one year's deduction forward into later years.

I believe this deserves the considered attention of the Congress and, although I am aware no action could be taken on it this session, I hope this bill will help stir thoughts in this area.

MODERNIZING WELFARE

(Mr. CURTIS of Missouri (at the request of Mr. DEVINE), was given permission to extend his remarks at this point in the RECORD.)

Mr. CURTIS of Missouri. Mr. Speaker, our laws reflect many of the prejudices and fears of an earlier day. We, along with moving ahead into new areas of legislative interest, must, at the same

time, weed out these dead remnants of the past and bring the laws of yesterday more into harmony with our society of today.

I have today introduced a bill to do just that. It is an amendment to the Social Security Act and is designed to secure the same treatment under our social security laws for those afflicted with tuberculosis and mental disease as is given those suffering from other types of illness. Several sections of the Social Security Act now specifically except the tubercular and mental patients from the benefits of the law which are given to others having other infirmities. Our medical science has advanced and we now recognize these afflictions as similar in kind to the others to which man falls prey.

There is no basis in reason why the treatment under the welfare sections of our laws should differentiate between these afflictions and others. I hope that the Congress will act to modernize our welfare laws.

FRAUDULENT USE OF CREDIT CARDS

(Mrs. BOLTON (at the request of Mr. DEVINE), was given permission to extend her remarks at this point in the RECORD.)

Mrs. BOLTON. Mr. Speaker, I am introducing a bill today to amend title 18 of the United States Code to prohibit the fraudulent or unlawful use of credit cards that have been lost or stolen.

Credit card frauds have increased at a phenomenal rate in recent years. From 1955 through 1961, it is estimated that they have increased 1,100 percent. These crimes affect many millions of people in this country to whom credit cards have been issued as they are liable for the use of such cards prior to notifying the issuing companies in the event they are lost or stolen. Federal legislation should help to act as a deterrent to the fraudulent use of such credit cards.

A number of State legislatures, including that of Ohio, have recognized the need for legislation to cover the fraudulent use of credit cards. However, because of the fact that oil company credit cards are used in connection with automobiles, the matter is appropriately a Federal interstate one. In the period of a month a person committing a credit card fraud can travel through many States prior to the time that the person to whom the card has been issued may be aware that the card is being misused. Further, because of the mobile character of the person committing the fraud and its interstate character, it is virtually impossible to apprehend the wrongdoer without the assistance of the Federal Bureau of Investigation.

Probably it will be impossible for the Congress to act on this matter in the short time remaining but I am hopeful that by introducing the bill at this time, the reports of the Federal agencies involved will be worked out during the adjournment period, and that we can pass the bill early in the 88th Congress.

ONE HUNDREDTH ANNIVERSARY OF THE EMANCIPATION PROCLAMATION

(Mr. SCHWENGEL (at the request of Mr. DEVINE) was given permission to extend his remarks at this point in the RECORD.)

Mr. SCHWENGEL. Mr. Speaker, on the 22d of September 1962, the Civil War Centennial Commission—a creature of the Congress—with the help and support of the Lincoln group of the District of Columbia, the D.C. Civil War Centennial Commission and the National Park Service, commemorated the 100th anniversary of the issuance of what I have called America's most phenomenal document, the Proclamation of Emancipation. The ceremonies were held on the steps of the Lincoln Memorial in Washington, D.C.

Those who were present were unanimous in their agreement that this was both appropriate and a moving event. It sought to, and I believe did, reveal some of the greatness that has been and is a part of our heritage.

The program recognized and featured the arts of America which inform, inspire, and instill in us a desire to move further and with greater rapidity in the direction of those goals established by our forefathers when they brought forth such documents as the Declaration of Independence, the Constitution, and the Proclamation of Emancipation authored by America's most American American—Abraham Lincoln.

It was appropriate and desirable that we have Miss Mahalia Jackson, one of America's most loved singers, appear, and perform on our program. And, she did perform magnificently. Singing with a feeling that was contagious and encompassing, she thrilled beyond measure those in our presence and the millions who heard her on television and radio that day as she sang the National Anthem, that beautiful song, "America," and then thrilled us as she was escorted to the podium for an impromptu singing "The Battle Hymn of the Republic." She brought forth our most noble sentiments, she thrilled us and all who heard and saw her supremely.

Mr. Speaker, in 1922 the committee of the Congress responsible for dedicating the Lincoln Memorial invited Edwin Markham to recite his poem, "Lincoln the Man." Reports of that occasion indicate that one of the high points of that program was Edwin Markham's personal presentation of this beautiful poem Lincoln. Last Saturday, again, we who were there were thrilled to hear Archibald MacLeish recite a poem entitled, "At the Lincoln Memorial: A Poem for the Centennial of the Emancipation Proclamation," which he wrote especially for the centennial commemoration. It was obvious that he reflected much and deeply on the occasion and the opportunity this presented before he wrote the poem. His personal presentation was superb and challenged our thinking toward the higher goals that the author of the Proclamation and occasion suggest. Somehow, too, it was a prayer as well as a hope as

Digest of CONGRESSIONAL PROCEEDINGS

OF INTEREST TO THE DEPARTMENT OF AGRICULTURE

OFFICE OF
BUDGET AND FINANCE

(For information only,
should not be quoted
or cited)

Issued Oct. 3, 1962
For actions of Oct. 2, 1962
87th-2d, No. 179

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HIGHLIGHTS: House received conference report on agricultural appropriation bill. House received conference report on foreign trade bill. Both Houses agreed to conference report on tax bill. Conferees agreed to file report on pay bill. Senate passed bills to: Amend Food and Agriculture Act re 15-acre wheat exemption for 1963 crop; Increase limitation on FHA loans. Both Houses received and Senate agreed to conference report on school lunch fund apportionment bill. Senate passed foreign aid appropriation bill. Senate committee reported bill for holding World Food Congress.

HOUSE

1. **AGRICULTURAL APPROPRIATION BILL, 1963.** Received the further conference report on amendments in disagreement on this bill, H. R. 12648 (H. Rept. 2514). All amendments previously reported in disagreement were still reported in disagreement (pp. 20596, 20650). Attached to this Digest is a copy of the conference committee report.
2. **APPROPRIATIONS.** Conferees were appointed on H. R. 12900, the public works appropriation bill. Senate conferees have already been appointed. p. 20568
The Appropriations Committee was granted permission to file conference reports at any time. p. 20568

3. PUBLIC WORKS. The Rules Committee reported a resolution for the consideration of H. R. 13273, the public works authorization bill. p. 20650

4. PERSONNEL. The "Daily Digest" states that "Conferees, in executive session, agreed to file a conference report on the differences between the Senate- and House-passed versions of H. R. 7927, providing for postal rate increases and increases in Federal employees' salaries." p. D929

The Post Office and Civil Service Committee reported with amendment H. R. 9531, to amend the law relating to pay for postal employees (H. Rept. 2509). p. 20650

Concurred in the Senate amendment to the House amendment to S. 2697, to amend title 38, U.S.C., to provide an extension of the period within which certain educational programs must be begun and completed in the case of persons called to active duty during the Berlin crisis. This bill will now be sent to the President. p. 20569

Received from Treasury a report of the operations by Federal departments and establishments in connection with the bonding of officers and employees. p. 20650.

5. WATERSHEDS. The Agriculture Committee approved the work plans for the following watersheds: Anasco River, P. R.; Bayou Folse, La.; Bee Creek, Kan.; Big Indian Creek, Neb.; Big Muddy Creek, Ky.; Big Wyacondah, Iowa; Crooked Bayou, Ark.; Duncan Creek, S. C.; Hardin Creek, Tenn.; Kaercher Creek, Penn.; Lattas Creek, Ind.; Line Creek, Tenn.; Lower Forest River, N. Dak.; Middle Caney, Kan.; Neshobe River, Vt.; Saltlick Creek, W. Va.; Stucker Fork, Ind.; Upper Bogue Phalia, Miss.; Upper Quaboag River, Mass.; West Fork of Pine River, Ky.; and Silver Creek, Kan. p. 20571

6. TAXATION. Both Houses agreed to the conference report on H. R. 10650, the proposed Revenue Act of 1962. This bill will now be sent to the President. See Digest No. 150 for items of interest. pp. 20547-65, 20580-92

7. FOREIGN TRADE. Received the conference report on H. R. 11970, the proposed Trade Expansion Act of 1962 (H. Rept. 2518). pp. 20597-601, 20650

The Ways and Means Committee reported with amendment H. R. 12109, to amend the Tariff Act of 1930 to permit certain natural grasses and other natural materials to be imported free of duty (H. Rept. 2516). p. 20650

8. DRUGS. The "Daily Digest" states that "Conferees, in executive session, agreed to file a conference report on the differences between the Senate- and House-passed versions of S. 1552, proposed Drug Industry Antitrust Act." p. D929

9. LEGISLATIVE PROGRAM. Rep. Albert announced that the following bills will be considered on Wed.: H. R. 13290, the supplemental appropriation bill; H. R. 13273, the public works authorization bill; S. 1123, to extend certain child labor provisions of the Fair Labor Standards Act to children employed in agriculture; and the conference report on H. R. 11665, the school lunch fund apportionment bill. He further announced that the conference report on the proposed Trade Expansion Act of 1962 will be considered on Thurs. p. 20616

SENATE

10. WHEAT. Passed without amendment H. R. 13241, to amend Sec. 309 of the Food and Agriculture Act of 1962 so as to provide that a farm marketing quota on the 1963 crop of wheat shall be applicable to any farm on which acreage of wheat planted exceeds the smaller of 15 acres or the highest number of acres planted to wheat on the farm in calendar years 1959, 1960, 1961, or 1963, (instead of 1959, 1960, or 1961). This bill will now be sent to the President. p. 20492

agency would then hold a hearing and if it finds affirmatively, the Interstate Commerce Commission would grant the registration unless there is a protest requesting the Commission to reverse or modify the State determination. If there is such a protest, the ICC would make an independent determination on the basis of the hearing record developed before the State commission.

The House of Representatives adopted a series of amendments to the version that passed the Senate. Many are technical—changing, for example, the effective date of the bill from December 31, 1961, to the date of enactment. However, there were four amendments added by the House at the request of Congressman Sisk that have substantive consequences. Three of these were adopted unanimously:

First. A provision preserving rights for a carrier who has been unable to file his intrastate certificate under the second proviso and to operate in interstate commerce because of pending litigation concerning the validity of his intrastate operations;

Second. A provision changing the standard of proof from "prima facie" to "conclusive" which would require the Commission to issue certificates of registration embracing all of the operating authority contained in State certificates; and

Third. A provision which would give a so-called "second proviso operator" a grace period of 6 months on the interstate portion of his rights in event that the underlying State certificate was suspended or revoked. The change that would be effected is this: Instead of the interstate right expiring at the same time the State right expires, an operator whose State right was suspended or revoked would have 6 months in which to get his State right reinstated. Thus the interstate right would have now a longer life term than the State right.

The fourth amendment offered by Congressman Sisk and the one that became known as the Sisk amendment after it was added on a division vote in the House is the one the House-Senate conferees, after two meetings, agreed to eliminate. This provision would have created an indefinite interstate right unless and until the Commission conducted a hearing for the purpose of revocation. The Interstate Commerce Commission and the National Association of Railroad and Utility Commissioners—composed of members from the State regulatory agencies—opposed the Sisk amendment.

In summary, the conference agreed to accept three of the four Sisk amendments. The fourth, which was not accepted, represented a sharp departure from the purposes for which the bill was enacted by the Senate originally—see page 5 of the Commission's letter.

The PRESIDING OFFICER. The question is on agreeing to the conference report.

The report was agreed to.

MESSAGE FROM THE HOUSE

A message from the House of Representatives, by Mr. Maurer, one of its

reading clerks, announced that the House had passed, without amendment, the following bills of the Senate:

- S. 136. An act for the relief of Dinko Dorcic;
- S. 453. An act for the relief of Robert J. Scanlan;
- S. 689. An act for the relief of Karl Heinz Agar;
- S. 1263. An act for the relief of Marie Margaret Arvanetes;
- S. 1999. An act for the relief of Anna Marie Erdelyi;
- S. 2667. An act for the relief of Sebastiana Santoro;
- S. 2687. An act for the relief of Robert D. Barbee;
- S. 2690. An act for the relief of Mona McIsaac Downey;
- S. 2711. An act for the relief of Tasia Deme-tropoulou (Dimitropoulos);
- S. 2753. An act for the relief of Duk Man Lee and Soon Mal Lee;
- S. 2777. An act for the relief of Arild Erick-sen Sandli;
- S. 2836. An act for the relief of Carmelo Rafala;
- S. 2902. An act for the relief of Sumiko Takahashi;
- S. 2908. An act for the relief of Rosa Fu-marola Balice;
- S. 2922. An act for the relief of Raymond Chester Hendon;
- S. 2950. An act for the relief of Dwijendra Kumar Misra;
- S. 2992. An act for the relief of Michelan-gelo Comito (Nati);
- S. 3085. An act for the relief of Paul Huyge-len and Duba A. Huygelen;
- S. 3177. An act for the relief of Michael (Mike) Bessler;
- S. 3265. An act for the relief of Despina Anastos (Psychopeda);
- S. 3267. An act for the relief of Gunter Heinz Hillebrand;
- S. 3275. An act for the relief of Anna Sci-amanna Misticoni;
- S. 3295. An act for the relief of Mathew Lengyel (also known as Brother Paul, S.V.D.);
- S. 3336. An act for the relief of Lazaro Loyola Arinque, Jr.;
- S. 3390. An act for the relief of Naife Kahl;
- S. 3452. An act for the relief of Dr. Has-san M. Nouri;
- S. 3557. An act for the relief of Betty San-dra Fagan; and
- S. 3600. An act for the relief of Chao Hua-Hsin.

The message also announced that the House had agreed to the amendments of the Senate to each of the following bills of the House:

H.R. 8181. An act to authorize the construction of a National Fisheries Center and Aquarium in the District of Columbia and to provide for its operation; and

H.R. 12080. An act to permit domestic banks to pay interest on time deposits of foreign governments at rates differing from those applicable to domestic depositors.

REVENUE ACT OF 1962—CONFER- ENCE REPORT

Mr. KERR. Mr. President, I submit a report of the committee of conference on the disagreeing votes of the two Houses on the amendments of the Senate to the bill (H.R. 10650) to amend the Internal Revenue Code of 1954 to provide a credit for investment in certain depreciable property, to eliminate certain defects and inequities, and for other purposes. I ask unanimous consent for the present consideration of the report.

The PRESIDING OFFICER. The report will be read for the information of the Senate.

The legislative clerk read the report. (For conference report, see House proceedings of October 1, 1962, pp. 20413-20415, CONGRESSIONAL RECORD.)

The PRESIDING OFFICER. Is there objection to the present consideration of the report?

There being no objection, the Senate proceeded to consider the report.

The PRESIDING OFFICER. The question is on agreeing to the conference report. (Putting the question).

Mr. MILLER. Mr. President, a parliamentary inquiry.

The PRESIDING OFFICER. The Senator will state it.

Mr. MILLER. Is this the vote on the adoption of the conference report?

The PRESIDING OFFICER. The Senator is correct.

Mr. MILLER. There will be no further vote on the tax bill after this vote?

The PRESIDING OFFICER. The Senator is correct. When the report is agreed to, that concludes the matter.

Mr. MILLER. It seems to me that we should know what the conference report contains. May we have a brief statement from the Senator who was in charge of the bill on the floor?

Mr. KERR. Mr. President, is it the desire of the acting majority leader that I make a statement on the action of the conferees?

Mr. HUMPHREY. Yes; it would be helpful if the Senator were to do so.

Mr. KERR. Mr. President, the proposed Revenue Act of 1962, as passed by the Senate, contained 203 amendments. While it is true that many of these were technical or conforming amendments, nevertheless, approximately 100 of these represented substantive changes in the bill. It is, of course, not easy to reconcile this many differences, particularly on a subject matter as complex as tax revision measures are. Nevertheless, the conference committee has reached agreement.

I am glad to be able to say that in very large measure the bill as agreed to by the conferees very closely resembles the bill as passed by the Senate. Thus, in the case of the investment credit, the so-called Long amendment requiring an adjustment to basis has been retained. The reporting system for dividends and interest and patronage dividends rather than the House provision for withholding has also been retained. Moreover, the foreign-income provisions also with only very slight modifications are the same as passed by the Senate. It is in no small part due to the leadership furnished the Senate conferees by their great chairman that it was possible for us to bring back the Senate bill largely in its original form.

The action taken by the conferees will increase somewhat the revenue loss in the fiscal year 1963. The Treasury has estimated that the loss is increased by \$490 million if no effect is given to the stimulative effect of the bill. The joint committee staff has estimated that this loss is increased by \$615 million on the same basis. This increase in loss occurs almost wholly because the House conferees insisted on making the investment credit effective as of January 1, 1963 rather than July 1, 1963.

On a full year basis the Treasury estimates that the bill will result in a reve-

nue loss of \$170 million with no effect being given to the stimulative effect. With this effect the bill would result in a surplus. The joint committee staff estimate comparable to the Treasury loss of \$170 million is \$550 million.

Mr. President, I ask to have inserted in the RECORD at this point two tables showing the Treasury and joint committee staff estimates on the bill as agreed by by the conferees.

There being no objection, the tables were ordered to be printed in the RECORD, as follows:

Estimated full-year revenue effect of H.R. 10650 as agreed to by the conferees
[Millions of dollars]

	As estimated by the staff of the Joint Committee on Internal Revenue Taxation	As estimated by the staff of the Treasury Department
Investment tax credit.....	-1,340	-1,020
Reporting of dividend and interest payments.....	+275	+240
Mutual banks and savings and loan associations.....	+170	+200
Entertainment, etc., expenses.....	+100	+100
Capital gains on depreciable property.....	+105	+100
Mutual fire and casualty companies.....	+25	+40
Cooperatives.....	+30	+35
Foreign items:		
Controlled foreign corporations.....	+50	+85
Gross-up of dividends.....	+15	+25
All other foreign items.....	+25	+30
Secs. 21-26.....	-5	-5
Secs. 27, 28, 30, and 33.....	(1)-	(1)-
Total.....	-550	-170

¹ Less than \$2,500,000.

Estimated revenue effect of H.R. 10650 for the fiscal year 1963 as agreed to by the conferees
[Millions of dollars]

	As estimated by the staff of the Joint Committee on Internal Revenue Taxation	As estimated by the staff of the Treasury Department
Investment tax credit.....	-1,265	-985
Reporting of dividend and interest payments.....	0	0
Mutual banks and savings and loan associations.....	+10	+5
Entertainment, etc., expenses.....	(1)+	+5
Capital gains on depreciable property.....	0	0
Mutual fire and casualty companies.....	0	0
Cooperatives.....	0	0
Foreign items:		
Controlled foreign corporations.....	0	0
Gross-up of dividends.....	0	0
All other foreign items.....	+10	+5
Secs. 21-26.....	(1)-	0
Secs. 27, 28, 30, and 33.....	(1)-	0
Total.....	-1,245	-970

¹ Less than \$2,500,000.

Mr. KERR. Mr. President the material I shall present next is a summary of the changes made by the conferees in the actions taken by the Senate. If I make no comment on a Senate amendment this means that it was accepted by the conferees and is in the final bill.

Mr. President, in order that my references to the pages and the amendment numbers may be clearly understood and included in the RECORD, I ask unani-

mous consent to have printed in the RECORD at the conclusion of my remarks a pamphlet entitled "Summary of Senate Amendments to H.R. 10650, Revenue Bill of 1962." This pamphlet summarizes the Senate amendments by number. The pages I refer to are pages in this pamphlet and the numbers are to Senate amendment numbers.

The PRESIDING OFFICER. Without objection, it is so ordered.

(See exhibit 1.)

Mr. KERR. Mr. President, the provisions of the bill as approved by the Senate were retained with the following substantive exceptions and modifications.

PAGE 1, AMENDMENT 11-14—INVESTMENT CREDIT

The conferees rejected the Senate amendment which would have made the investment credit available only with respect to property acquired or constructed after June 30, 1962. Under the conference agreement, this credit will be available with respect to property acquired or constructed after December 31, 1961, as provided in the House bill.

It is the understanding of the conferees on the part of both the House and the Senate that the purpose of the credit for investment in certain depreciable property, in the case of both regulated and nonregulated industries, is to encourage modernization and expansion of the Nation's productive facilities and to improve its economic potential by reducing the net cost of acquiring new equipment, thereby increasing the earnings of the new facilities over their productive lives.

PAGE 2, AMENDMENTS 29 AND 31—ENTERTAINMENT EXPENSES

The conferees rejected the Senate amendment which would have permitted a deduction for entertainment-type expenses which were "associated with" a taxpayer's trade or business and substituted a provision which would allow a deduction for such expense items which directly precede or follow a substantial and bona fide business discussion (including business meetings at a convention) if the taxpayer establishes that such items are associated with the active conduct of his trade or business. The House provision relating to entertainment-type facilities was retained.

The rule of the House bill as described in the report of the Committee on Ways and Means is more strict than the "or associated with" rule of the Senate amendment. The rule of the House bill would not allow deduction of expenditures for entertainment occurring under circumstances where there is little or no possibility of conducting business affairs or carrying on negotiations or discussions relating thereto, such as where the group of persons entertained is large or the distractions substantial.

It is the understanding of the conferees, both on the part of the House and the Senate, that the alternative Senate "or associated with" test as described in the report of the Finance Committee would apply to certain entertaining primarily to encourage goodwill where the evidence of business connection is clear, whether or not business is actually trans-

acted or discussed during the entertainment. The conference agreement would permit a deduction for the cost of an entertainment item, even though the item is not directly related to the active conduct of the taxpayer's trade or business, if the item is associated with it, so long as the entertainment activity directly precedes or follows a substantial and bona fide business discussion. The conditions under which an item is "associated with" the active conduct of a trade or business are contained in the report of the Committee on Finance. The deductibility of other items of entertainment expense, as well as items with respect to facilities, would be governed by the rule of the House bill.

Section 274(a) as agreed to by the conferees will allow as a deduction the cost of entertaining connected with what are primarily business meetings. For example, if the taxpayer conducts substantial negotiations with a group of business associates and that evening entertains the group and their wives at a restaurant, theater, concert, or sporting event, such entertainment expenses, if associated with the active conduct of the taxpayer's business, will be deductible even though the purpose of the entertainment is merely to promote goodwill in such business. Moreover, if a group of business associates with whom the taxpayer is conducting business meetings comes from out of town to the taxpayer's place of business to hold substantial business discussions, the entertainment of such business guests by the taxpayer the evening prior to the business discussions will be regarded as directly preceding the business discussions.

Similarly, if in between, or in the evenings after, business meetings at a convention, the taxpayer entertains his business associates or prospective customers attending such meetings (and their wives), such entertainment will be considered as directly preceding or following a business discussion.

Any entertainment which is a part of substantial and bona fide business discussions, where the conduct of business is the principal activity during combined entertainment and business time spent together by the taxpayer and the person or persons entertained, will be deductible if the expense is associated with the active conduct of the taxpayer's trade or business.

Also, the cost of banquets at meetings of professional and business associations would normally be deductible. As in the above cases, if the expense is associated with the active conduct of a trade or business, it would not be necessary for the person paying for the banquet to attend the banquet himself. For example, a dental equipment supplier would be able to deduct the cost of purchasing a table at a dental association banquet for dentists who are actual or prospective customers for his equipment.

Thus, under the business meal exception contained in proposed section 274 (e)(1), and the conference agreement, the cost of providing food and beverages at most business meetings and banquets would be deductible, as well as almost all restaurant and most hotel entertaining.

In neither of the situations covered by the conference agreement nor under the business meal exception is there a requirement that business must actually be discussed in order to get a deduction.

Senators will recall that on the floor of the Senate I indicated that the principal difference between the House entertainment and the Senate entertainment provisions was the description of these provisions in the House Ways and Means Committee report and in the Senate Finance Committee's report. In my judgment the conferees, in the provision they have worked out, have just about split the difference between the House and Senate versions of this provision. I will illustrate that by saying our staff estimates that under the House version, this provision would have raised about \$125 million in additional taxes. Under the Senate version our staff estimated that the entertainment provision would raise about \$85 million. It was the estimate of the staff that under the language of the report adopted by the conferees, the entertainment provision will raise about \$105 million. Therefore, the difference between the two versions of this provision was split as nearly equally as the conferees were able to do it.

AMENDMENT TO SECTION 482 (HOUSE BILL ONLY)

The House receded in this case because the conferees on the part of both the House and the Senate believe that the objectives of section 6 of the bill as passed by the House can be accomplished by amendment of the regulations under present section 482. Section 482 already contains broad authority to the Secretary of the Treasury or his delegate to allocate income and deductions. It is believed that the Treasury should explore the possibility of developing and promulgating regulations under this authority which would provide additional guidelines and formulas for the allocation of income and deductions in cases involving foreign income.

PAGE 4, AMENDMENT 48—MUTUAL SAVINGS BANKS, ETC.

The conferees modified the Senate amendment which limited the deductibility of additions to reserves by mutual savings banks, and other thrift organizations to 12 percent of deposits (the limitation that exists under present law) by providing that this limitation would not apply to taxpayers who computed their deduction for additions to bad debt reserves on the experience method.

PAGE 5, AMENDMENT 50

The conferees rejected the Senate amendment which would have permitted stockholder-owned savings and loan associations to deduct only 50 percent of taxable income as a reasonable addition to their bad debt reserves, thereby equating them with mutual savings institutions by permitting them to deduct 60 percent of taxable income for such additions.

PAGE 5, AMENDMENT 60

The conferees modified the Senate action taken on the definition of a "domestic building and loan association" by

revising certain limitations on the investment of assets in a manner which would provide for a proportionate cut-back in the otherwise allowable deduction for additions to reserves for losses on qualifying real property loans so long as the Senate bill's 36 percent limitation with respect to other than 1- to 4-unit residential housing and certain other investments is not increased to more than 41 percent. If other investments exceed this 41-percent limitation, the institution will not be treated as a building and loan association. For purposes of these investment limitations, passbook loans and investments in home office buildings would be treated the same as investments in 1- to 4-unit residential property.

PAGE 7, AMENDMENT 85—MUTUAL FIRE AND CASUALTY INSURANCE COMPANIES

The conferees modified the provision exempting underwriting income from tax to make it applicable only to mutual fire and casualty insurance companies receiving gross amounts under \$500,000 rather than \$600,000 as provided in the Senate bill.

It had been \$300,000 as passed by the House.

PAGE 7, AMENDMENT 87

The conferees modified the Senate amendment applicable to mutual companies experiencing underwriting losses to make it applicable only to those companies that experience such losses in each of the 5 years immediately preceding 1962 and by permitting such losses to be carried over and offset only against statutory underwriting gains during the next 5 years.

PAGE 8, AMENDMENT 95-6

The conferees eliminated the Senate amendment which would have provided a special alternative coverage area rule applicable to concentrated risk companies where the risks involved arose within 400 miles of any fixed point selected by the taxpayer.

They retained the 200 miles limit for concentrated risks, however, which also was added by the Senate.

PAGE 9, AMENDMENT 104

The conferees modified the Senate amendment which would treat mutual flood insurance companies substantially the same as factory mutual companies by providing amendments to insure that these companies and their subscribers would be treated identically.

The bill as agreed to by the conferees treats the subscriber of a mutual flood insurance company in the same manner as a policyholder of a factory mutual is treated under existing law—and under the bill. Accordingly, the subscriber of a mutual flood insurance company may only deduct—assuming the payment of the premium constitutes a business expense—so much of the premium as the company absorbs.

PAGE 11, AMENDMENT 126—CONTROLLED FOREIGN CORPORATIONS

The conferees modified the provisions of the Senate bill relating to the tax treatment of controlled foreign corporations only slightly. It refined the schedule of minimum distributions required by such corporations for varying effec-

tive foreign tax rates. Compliance with this minimum distribution rule as under the Senate version will avoid the application of the new rules generally applicable to controlled foreign corporations.

The committee of conference was informed by the Treasury Department of the policy it plans to follow in the granting of rulings under section 367 of the Internal Revenue Code of 1954 in situations in which taxpayers seek to reorganize, during a reasonable period after the enactment of the bill, their foreign corporate structures in response to the enactment of section 12 of the bill as agreed to in conference.

The Treasury Department, for purposes of section 367, will not treat a transaction involving the reorganization of foreign corporate structures as being in pursuance of a plan having as one of its principal purposes the avoidance of Federal income taxes solely by reason of the fact that a principal purpose of the reorganization is to terminate a method of operation which would result in tax to U.S. shareholders under the provisions of section 12 of the bill. In such cases a favorable ruling under section 367 will generally not be denied by the Treasury Department in transactions in which earnings and profits of foreign corporations are carried over to other foreign corporations under circumstances in which there will be no reduction of the U.S. taxes (and foreign taxes) that would be payable on the eventual remittance of such earnings and profits to U.S. shareholders.

Under present administrative rules, where corporate shareholders are involved the Treasury Department generally does not issue rulings under section 367 which permit the tax-free remittance to the United States of earnings and profits of foreign corporations. However, under existing practice a ruling permitting a tax-free exchange is generally given subject to a condition that an appropriate amount be included in the income of the domestic shareholder (thus negating the existence of a principal purpose to avoid U.S. tax). Such rulings will continue to be given even though a principal purpose of the transaction is (1) to terminate the activities of a foreign corporation which would result in tax to U.S. shareholders under the provisions of section 12 of the bill, and (2) to carry on such activities in the future through a domestic corporation.

The conferees recognize that the problems in this area are complex and that particular aspects of the policy as explained above may require qualification and refinement as experience is gained in applying it to particular situations.

The conferees on the part of the Senate called attention to the colloquy in the Senate with respect to the amendment offered in the Senate relating to corporations engaged in producing or selling books or other media of communications, and so forth (see pp. 17511-17513 of the daily CONGRESSIONAL RECORD for September 5, 1962). The conferees were advised that the substance of this amendment was not within the jurisdic-

tion of the conference committee. However, the conferees have requested the Treasury Department to study this matter and report back next year to the Committees on Ways and Means and Finance.

Mr. President, I continue to summarize the conference report.

PAGE 13, AMENDMENT 145—FOREIGN INVESTMENT COMPANIES

The conferees eliminated the Senate amendment which would have provided that clearance from the Internal Revenue Service under section 367 need not be obtained in the case of a foreign investment company registered with the Securities and Exchange Commission if it is a party to a reorganization in which all of its properties are acquired by a domestic regulated investment company before January 1964. The committee of conference was informed by the Treasury Department that the proposed new subsection was not needed in view of the administrative practices under section 367 of the code, and might therefore imply that such practices are erroneous.

PAGE 15, AMENDMENT 159—GAIN FROM SALES OR EXCHANGES OF STOCK IN FOREIGN CORPORATIONS

The conferees rejected the alternative averaging ceiling limitation applicable to the tax on individual shareholders who sell or exchange stock in foreign corporations.

PAGE 15, AMENDMENT 161—SALES AND EXCHANGES OF PATENTS, ETC., TO FOREIGN CORPORATIONS

The conferees rejected the Senate amendment which would have provided an exception from the general rule that gain on sale of patents to a controlled foreign corporation would be treated as ordinary income rather than as capital gain in the case of transfers of such patents to a foreign subsidiary for use in manufacturing operations of the subsidiary.

The conferees requested the Treasury Department to study and report back on the proper tax treatment of the transfer of patents, and so forth, to foreign subsidiaries which use such property in their own manufacturing operations.

PAGE 16, AMENDMENT 173—REPORTING ON INTEREST, DIVIDENDS, AND PATRONAGE DIVIDENDS OF 10 OR MORE A YEAR

The House receded with only clerical amendments but as a part of the agreement to the Senate amendment, the House and Senate conferees have requested the Treasury Department to make annual reports to the Committees on Ways and Means and Finance on the improvement in the reporting on tax returns of dividends, interest, and patronage dividends as a result of the Senate amendment, with the view that this matter will be reconsidered by the Committees on Ways and Means and Finance if it is determined that there has not been sufficient improvement in the reporting of such income.

PAGE 20, AMENDMENT 197—EXCLUSION FROM GROSS INCOME OF GAIN FROM SALE OF RESIDENCE BY INDIVIDUALS AGED 65 OR OVER

The conferees rejected the Senate amendment which would have excluded

from gross income gain realized by a taxpayer aged 65 or over from the sale or disposition of his principal residence which he had occupied for 5 years at the time of sale.

PAGE 21, AMENDMENT 199—SOCIAL SECURITY AMENDMENT RELATING TO STATEMENT OF CLAIMANTS FOR MEDICAL ASSISTANCE FOR THE AGED

The conferees rejected the Senate amendment which would have permitted States to accept as presumptively correct any written statement as to the financial status of a claimant of medical assistance for the aged.

PAGE 21, AMENDMENT 200—FOREIGN SUBSIDIARIES MANUFACTURING PRODUCTS ABROAD FOR SALE IN THE UNITED STATES

The conferees rejected the Senate amendment which would have provided that under certain conditions a foreign corporation would be deemed to be engaged in business in the United States if such foreign corporation were 10 percent U.S. owned and derived more than 10 percent of its gross income from the sale of competitively mined, manufactured, or processed articles which were sold by the foreign corporation for ultimate U.S. consumption or disposition in the United States.

PAGE 22, AMENDMENT 203—TREATIES

The conferees rejected the Senate provision that would have provided that any provision in this bill that contravened an existing tax treaty was not to have precedence over the treaty obligation.

In this connection, the Treasury Department informed the committee of conference that it is its view that there are no conflicts between provisions of the bill and provisions of tax treaties, with one minor exception relating to the real estate clause of the Greek Estate Tax Treaty which the Treasury will seek to have renegotiated before July 1, 1964.

Mr. JAVITS. Mr. President, will the Senator from Oklahoma yield for questions?

Mr. KERR. I yield.

Mr. JAVITS. First, I think it would not have been quite right to allow the conference report to be agreed to without some analysis and discussion of it. A measure which involved many days of debate and exercised the business community of the country should certainly not go through the Senate in 5 minutes. That was the purpose the Senator from Iowa [Mr. MILLER] sought to serve and which I sought to serve in interrupting the proceeding.

I do not ask these questions with any hostile or adverse intent. I intend to support the conference report. However, I think it is important to pinpoint certain of the critical items in it.

First, taking the items in series as reported by the conference, the Senator from Oklahoma said there will be a net gain in revenue by the enactment of the bill. Will that gain be attributable to an excess from the closing of loopholes?

Mr. KERR. Will the Senator show me the statement to which he has just referred?

Mr. JAVITS. It was only my impression of what the Senator said.

Mr. KERR. I don't believe the Senator from Oklahoma made any such statement unless it was with respect to the Treasury full-year effect of the bill taking into account its stimulative effect.

Mr. JAVITS. I thought I heard the Senator use the figure "\$105 million."

Mr. KERR. That was in connection with only one amendment to the bill, the provision concerned with entertainment expenses.

The language in the bill which was agreed upon in conference will result in the collection of approximately \$20 million more revenue a year than would have the language in the bill as passed by the Senate.

Mr. JAVITS. Is the Senator from Oklahoma prepared to give an estimate of the revenue gain as against revenue diminution by virtue of the passage of the bill?

Mr. KERR. The overall passage of the bill?

Mr. JAVITS. Yes.

Mr. KERR. Nearly everyone connected with our committee and the Committee on Ways and Means, the staff of the Joint Committee on Internal Revenue Taxation, the individual members of the Committee on Finance, and the personnel in the Treasury have come forward with an estimate as to what the revenue result will be by reason of the passage of the bill. I have placed the revenue estimates of the two staffs in the record.

When the bill was before the Senate, the Senator from Oklahoma took the position that in the first year there would be a loss, under the bill, of \$200 million; that, in his judgment, thereafter there would be a net gain from the bill.

The latter statement is still the opinion of the Senator from Oklahoma as to the longrun effect.

In view of the fact that the Senate conferees were unable to retain in conference the Senate amendment which made investment credit effective July 1, 1962, instead of January 1, 1962, there will be an additional loss in fiscal 1963 of approximately \$500 million.

However, as I said a while ago, in the judgment of the Senator from Oklahoma, after fiscal 1963, because of its stimulative effect, the bill will produce a net revenue.

Mr. JAVITS. Speaking for myself, I shall support the conference report with this estimate, which I gather is in the neighborhood of \$650 million to \$750 million for the first year.

Mr. KERR. I think it would not be in excess of \$970 million for the first year; my judgment is that it would be less.

Mr. JAVITS. I feel, as does the Senator from Oklahoma, that the stimulus of the economy which is represented by the bill is very much worthwhile and will pay us back handsomely.

Mr. KERR. I thank the Senator from New York for his statement. I agree with him.

Mr. JAVITS. I thought it important to pinpoint that item so that there would be no lack of explanation.

In regard to entertainment expenses, I gather that the fundamental thrust of the change was not to use the words "di-

rectly related to the conduct of the taxpayer's trade or business exclusively" or the words "associated exclusively", but to do what we lawyers often do—namely, to relate the propriety of the entertainment expense deduction to the fact that the expense was in connection with—whether before or after—income, and so forth, which would be earned. I think that is a fair compromise, in view of the desire to tighten the definition, which those in some quarters felt had been abused; and I do not believe it would materially change the decisions of the Internal Revenue authorities in regard to the deductions claimed by those who have pursued a reasonable course of conduct in making deductions for the expenses of entertainment with fair relationship to their earning of income or engaging in business.

Let me ask to what extent the conference report allows the deduction of expenses of entertainment in connection with good will.

Mr. KERR. This was the principal work of the conferees, I say to the Senator from New York with respect to entertainment expenses. Expenses connected with the development of good will can be appropriately and legally deducted under the language agreed to by the conferees, provided the expenditure is directly preceding or following a substantial and bona fide business discussion. This includes business meetings at a convention. In such cases the entertainment goodwill is deductible if it is associated with business. Otherwise the expense must be directly related to business.

Mr. JAVITS. Therefore, would the Senator say we are dealing with a matter of hours or minutes or days or with a bracket of time, as it relates to a business deal?

Mr. KERR. I would say that if a business representative is engaged in an effort to expand or further his business or make sales, and if there is a goodwill expenditure at the time of the effort—or I believe the language of the conference report is "directly preceding in following a substantial and bona fide business discussion."

Mr. JAVITS. I notice in the report, the words "directly precede or follow." I am trying to ascertain from the Senator whether there is to be reasonable latitude in terms of a duration of time, provided the taxpayer can show it is directly related to being immediately after or immediately before a discussion.

Mr. KERR. In my opinion that is an accurate statement if the business discussion is substantial and bona fide.

Mr. JAVITS. Men might take a 3-hour or 4-hour automobile ride or train ride before they reached the situs of the entertainment.

Mr. KERR. Yes.

Mr. SMATHERS. Mr. President, will the Senator from Oklahoma yield?

Mr. KERR. I yield.

Mr. SMATHERS. So, as the Senator from New York has said, if the expense is "directly related to," there is no limitation, as I understand, as to hours or minutes, or anything of the sort.

Mr. JAVITS. I am speaking of the way a lawyer would consider this matter; and I wonder whether we are dealing with an event bracket or with a time bracket.

Mr. SMATHERS. It is an event bracket.

Mr. JAVITS. So I believe it will be necessary to prove contiguity with the event, not as regards time.

Mr. SMATHERS. Yes.

Mr. KERR. I believe the report uses the words "directly preceding or following a substantial and bona fide business discussion."

Mr. JAVITS. And that refers to an event, and shows that we are dealing with an event bracket.

Mr. KERR. The interpretation of the Internal Revenue authorities in this regard will be reasonable.

Mr. JAVITS. I thank the Senator.

I notice that the conference report, in dealing with building and loan associations, a matter of great controversy—is rather heavily weighted on the side taken by the Senate, and that the definition voted by the House, which was considerably restricted, has been considerably yielded in favor of the position taken by the Senate. Is it fair to say that, generally speaking, the Senate view in that regard has prevailed?

Mr. KERR. I would say the definition included by the House was both vague and at the same time relatively severe. The Senator from New York was on the floor of the Senate when the definition which had been written by the Finance Committee was further modified. The conferees further changed the definition, as contained in the Senate amendment dealt with on the floor. The effect of the change was to make it slightly more generous. Also, it provided a reduced deduction for those who did not quite meet the definition but nearly did so. This "near miss" category, however, can only be retained for 2 years at most, for any consecutive period.

Mr. JAVITS. I thank the Senator.

I have two further questions to ask. One of them relates to the problem of controlled foreign corporations under American ownership, and the attempt to include a provision which would be such that American concerns would not thus find themselves at a disadvantage when competing with foreign corporations which would not come under the provisions imposed by this tax bill.

Of course it is impossible for me to deal with all the nuances of this matter; but we have great confidence in the Senator from Oklahoma, and therefore I wish to ask him this question: Was the competitive situation of such American firms in competition with foreign firms reasonably taken into consideration in determining the tax base upon which the controlled foreign corporations should operate?

Mr. KERR. This measure does not touch, taxwise, the operations of a legitimate manufacturing or similar operating corporation in another country which is a subsidiary of a company in the United States. It does, however,

tax to U.S. shareholders income from tax haven operations.

Mr. JAVITS. As I have said, we have great confidence in the Senator from Oklahoma, and we accept that assurance. But he will remember that was the principal matter about which the Senator from Minnesota [Mr. McCARTHY] and I and other Senators made our fight—namely, the competitive aspect.

From a quick reading of the report, I gained the impression that that is the general thrust of this portion of the conference report.

Mr. KERR. The Senate amendments I offered were intended to enable our concerns abroad to be competitive and the House agreed to these amendments.

Mr. JAVITS. In connection with my last question, I must say that, being the author of the compromise in regard to reporting, I have been quite dismayed by the many protests which have been made by credit unions, which have sent to me, and I am sure, to many other Members of the Senate, telegrams in which they have strongly urged that the reporting provisions which we substituted for the withholding provisions—and I am glad to say that the latter have been deleted from the bill—would be very onerous on the credit unions.

Will the Senator state whether that question was considered by the conferees, and will he state their point of view in that regard?

Mr. KERR. I understand this controversy arose by reason of the provision of the bill, as passed by the House, calling for withholding by the payors of dividends and of interest. I worked out a number of amendments which, in my judgment, would have alleviated any injustice or inconvenience to any taxpayer with reference to whom such dividends or interest earnings did not result in further tax.

That effort, however, availed nothing. Those in opposition to the withholding measure came forward with a reporting requirement providing for the submission by payors of information returns to the Government for interest, dividends, and patronage dividends of \$10 or more per person per year, and providing that this same information must also be submitted by the payors to the recipients of interest, dividends, or patronage dividends on an annual basis. Penalties of \$10 per return on statement, but not to exceed \$25,000 per payor, are provided for failures to file returns with the Government and penalties of \$10 per statement but not over \$25,000 are provided for failures to submit statements to payees.

Those who had opposed withholding, both as members of the committee and as representatives of industry, who appeared before the committee as witnesses, advocated adoption of an adequate reporting requirement in lieu of the withholding provisions in the bill, and that was done.

I will say to my friend from the great State of New York that, in my judgment, if I had been in the building and loan business, or in the banking business, or

in any business paying dividends, or in the regulated investment company business, or in the credit union business, I would have been before the Finance Committee favoring the liberalized withholding provisions, rather than this reporting requirement. But such was not the case.

There were not sufficient votes on the committee to retain the withholding provisions, and there were not sufficient votes in the Senate to retain the withholding provisions.

When the withholding provisions were eliminated, the Senator from Oklahoma supported the amendment offered by the distinguished chairman of the committee, the Senator from Virginia [Mr. BYRD], who had the support of the majority of the members of the committee.

It may well be a burdensome provision for the payors of dividends and interest. But when the question came to a vote, in committee the withholding amendments were defeated and the committee instead adopted the reporting provisions.

Mr. JAVITS. I, too, opposed the withholding, but is it fair to say that, having accepted an alternative rather than withholding, which the savings institutions and credit unions considered the least worse of the two alternatives, they must live with it? I notice the Treasury has been asked to carefully watch the operation—

Mr. KERR. Yes. I would like to read that language into the Record.

Mr. JAVITS. I think it might help if the Senator heard my question first.

Mr. KERR. Very well.

Mr. JAVITS. I will not read it. I will let the Senator from Oklahoma read it. The Treasury is to watch the operation to see if it wishes any improvement in the reporting of dividend and interest income.

Would the Senator, as a matter of legislative record, be willing to have the Treasury watch it from the point of view of the onerousness of the reporting on the part of segments of the savings industry, including thrift industries, to see what additional revenue has been produced by this provision, and also report if it finds that the reporting requirements which the bill carries bear particularly heavy on any particular section of the thrift industry, and if so, to make recommendations?

Mr. KERR. There is no provision in the conference report for that.

Mr. JAVITS. No, there is not.

Mr. KERR. As the Senator from New York has just indicated, the House and Senate conferees have requested the Treasury Department to make annual reports to the House Committees on Ways and Means and the Senate Committee on Finance on the improvement in the reporting on tax returns of dividends, interest, and patronage dividends as a result of the Senate amendment, with the view that this matter will be reconsidered by the Committees on Ways and Means and Finance if it is determined that there has not been sufficient improvement in the reporting of such income.

In further answer to the question, I think that this subject will be brought before the Congress after this law goes into effect and the payors have had to operate under it. The Senator from Oklahoma accepted the thesis of the chairman of the Finance Committee, that this reporting requirement would produce as much revenue as the withholding requirement. Whether it does or not, I believe it will be more burdensome to those who pay interest and dividends. There is no doubt in the mind of the Senator from Oklahoma that those affected will be before Congress in the next 12 or 18 months, as soon as they have to make the reports once, and will ask Congress to reconsider this decision.

So far as the Senator from Oklahoma knows, the witnesses who appeared before the committee representing the savings and thrift industries and financial institutions and corporations paying dividends, who opposed the withholding tax, generally supported the provision requiring this additional reporting. I talked with a number of the witnesses. I frankly told them that I thought they were getting out of a very comfortable couch into the fire, and not out of the frying pan into the fire; but they assured the Senator from Oklahoma that is what they wanted. If the committee report is adopted and the bill is signed, that is what they are going to get.

Mr. JAVITS. I happen to be one of those who believed that the reporting was superior to the withholding requirement. I thought the withholding requirement, considering our general situation, was not wise. But we are now considering the report. I have no doubt it will be approved. I myself intend to support it.

Will the Senator join with me in the suggestion that the Treasury, at the same time it reports on revenue production, report on the way the reporting system is operating and the way it affects different segments of the thrift industry?

Mr. KERR. I shall be glad to bring it to the attention of the Finance Committee, because I think the suggestion has merit.

Mr. JAVITS. I thank the Senator.

Mr. YARBOROUGH. Mr. President, will the Senator yield for a question?

Mr. KERR. I yield.

Mr. YARBOROUGH. Was any change made by the conference committee in the sections relating to lobbying deductions?

Mr. KERR. No changes were made. That question was not in conference, because after adoption of the amendment of the Senator from Kentucky deleting from the bill, the Finance Committee amendment, the language retained was identical with that passed by the House. So there was no matter in conference with reference to that question.

Mr. YARBOROUGH. Did I correctly understand the distinguished Senator from Oklahoma to say that the first year of the operation under the bill the re-

sult probably would show a net loss of about \$600 million?

Mr. KERR. That is my judgment. That would be for fiscal year 1963.

Mr. YARBOROUGH. I thank the distinguished Senator.

Mr. KUCHEL. Mr. President will the Senator yield?

Mr. KERR. I yield to the Senator from California.

Mr. KUCHEL. First I wish to congratulate my able friend from Oklahoma, who has assumed a very great responsibility with respect to this proposed legislation and who has performed it in the usual excellent manner which characterizes his work.

Was the text of the amendment which I offered with respect to the Japanese-American problem retained in the bill as the Senate approved it?

Mr. KERR. I say to the distinguished Senator from California with the realization that it will come to him within an impact of pleasure, joy and pride, that the answer is "Yes."

Mr. KUCHEL. I thank my able friend.

The PRESIDING OFFICER. The question is on agreeing to the conference report.

SO-CALLED TAX RELIEF BILL NOT GOOD FOR AMERICA

Mr. YARBOROUGH. Mr. President, the original purpose of this tax bill was to eliminate undesirable loopholes. At the same time, it was felt by the administration proponents that the sluggish performance of the economy could be stimulated by creating new tax incentives; thus, the investment credit. But what has happened is that many of the loophole-closing provisions have been rendered impotent, and the investment credit provision has been so altered that it will not fulfill its original purpose. President Kennedy asked for a provision that would induce new investment, investment that would not be made in the absence of such a credit. Therefore, the President proposed a 15-percent tax credit on new investment; that is, investment in excess of depreciation. Such a provision was properly designed to provide an incentive to net investment, and thus encourage economic growth, providing that other important factors were favorable.

The President's original proposal has been greatly altered. The investment credit provision, as amended, provides no incentive to net investment. Rather than affording a strong investment-inducing tax credit of 15 percent on net investment, the bill now will give a 7-percent tax credit to gross investment. Business will be given a windfall tax deduction for investment that would have been made even in the absence of a tax credit. This is a windfall that business did not ask for. To their credit, potential large beneficiaries said they did not want it.

The National Industrial Conference Board, reporting on a survey to determine what effect the 7-percent investment credit would have upon capital investment, states:

Overall, the increase in 1963 outlays expected on account of the investment tax credit may be small in relation to its potential. In more than half of the industries covered, moreover, the imputed difference was less than 1 percent.

Mr. President, there is a need at the present time to stimulate the economy. The recovery from each succeeding postwar recession has been weaker than the one before. But, Mr. President, the economic growth equation is comprised of two equal parts: supply and demand. The most pressing economic growth problem facing the American economy is insuring effective demand. A study by the staff of the Joint Economic Committee makes the following two points:

First. The growth rate in the postwar period tapered off substantially after 1953. Not only was recent history marred by two recessions, a period of low growth during prosperity also occurred. This low growth during prosperity was due primarily to the slowing down of the rate of growth of demand, particularly the demand for goods.

Second. That a lack of labor and capital did not limit growth during this period is revealed by: (a) Higher unemployment rates, even during the prosperity phase 1956-57; (b) the higher percentage of the labor force which was working part time; and (c) the low and falling rates of capital utilization. The McGraw-Hill index of plant utilization is now at approximately 85 percent. Certain key industries such as steel are even lower.

There is a shortage of investment funds; in 1961 American corporations accumulated nearly \$12 billion in liquid assets. In the face of this overwhelming evidence, can we come to any conclusion other than that the problem we must conquer is one of insufficient demand? The investment credit operates on the supply side of the equation. We are treating the healthy patient and ignoring the sick one. What sense does it make to give a business firm an incentive to enlarge or modernize its productive capacity, when there is not enough demand for its product to warrant full use of the capacity it already has?

Increased demand will give business a healthy, natural incentive to expand. Therefore, we should be looking to the lower economic brackets when we consider who should get a tax deduction. In the past 8 years accelerated depreciation allowances and other tax changes have reduced the tax load of corporations by \$4 billion a year. During this same period virtually no tax cuts have been given to low- and middle-income groups. The biggest impact upon consumption from a tax reduction comes from these bottom income groups, since these people spend a larger proportion of their incomes than do those in any other category. Almost all of a tax cut for our lowest bracket taxpayer will result in increased spending.

It is utter folly to think about giving an investment credit to business at a time when corporations are increasing their liquidity and are not finding enough demand to use even the capacity they already have. Rather we should attack

the source of our problem—insufficient demand, and that can best be accomplished by tax relief for lower bracket individuals.

Mr. President, the bill before the Senate is the very antithesis of that. The bill would worsen the situation instead of help to solve the problem.

We are all hopeful of giving some tax relief next year on the bottom end of the scale, but we must realize now that what tax cuts we give this year will reduce the amount of tax cuts we can make next year for the benefit of the public at large. This year we are frittering away the badly needed tax cut for the people for the benefit of a few groups who do not really need tax relief.

Mr. GORE. Mr. President, will the Senator yield?

Mr. YARBOROUGH. I yield to the distinguished Senator from Tennessee.

Mr. GORE. I wonder what incentive for modernization would be involved in a retroactive tax gift of the investment credit to January 1, 1962.

Mr. YARBOROUGH. I confess that that is a question I am unable to answer. The distinguished Senator from Tennessee will have to find some other source. He could not do it by clairvoyance, because it could not be done by projecting into the future, since the capital improvement would already have been made prior to the time the bill was passed.

The purported object is an incentive to cause capital improvements in the future. As already pointed out, the purchasing power of the people is not high enough to utilize the productive capacity now available.

We will be making a tax cut in the wrong place, in the wrong brackets.

By further illustration, I cite the really horrible example: the provision in the bill allowing a tax deduction for lobbying expenditures.

At the present time the tax laws are neutral with respect to the expenses incurred by the different groups which engage in lobbying activities. This is as it should be; groups which lobby for the purpose of advancing their own self-interest should pay for these activities themselves. They have no right to ask for the financial support of the rest of the economy.

That is what happens when we provide a tax credit for some businesses to send representatives to lobby the Congress. We make the other citizens pay the expense of their lobbying for their own selfish ends.

Section 3 would change all that. Section 3 would give a tax deduction to business concerns for lobbying activities. This tax deduction would be given only to business concerns. The revenue lost from these deductions will have to be made up by the rest of the economy. The average citizen will be forced to pay for the lobbying activities of big business, and further, cannot even take advantage of the deduction himself.

We would deny the deduction to a citizen who wished to write or telephone to a Senator or his Representative about pending legislation—legislation which would quite probably hit the citizen in

the pocketbook. We would deny that deduction, and yet allow such an expense to be made tax free by a business that was lobbying. That section of the bill is completely unconscionable.

Those two sections alone—the investment credit and the lobbying deduction—unfortunately vitiate any public interest to be gained by passage of the other provisions of the bill. For the sake of having a reasonably just tax relief bill next year, the conference report should be killed now. Next year, when the public comes clamoring, "Where is the tax cut you promised us in 1962?" I do not desire to be one who will have to say, "We gave it away last year. We gave it away last year to someone who did not need it."

In my opinion, the bill is not a tax reform. It is the opposite. It is tax regression. It would create greater inequities in our tax structure. In effect, it would give tax cuts to the larger financial interests which are not using their productive capacity now, and deny tax cuts to the great body of American citizens.

It has been stated by the chairman of the conference that the bill would result in a net loss of revenue of \$600 million in fiscal year 1963.

The bill is not a tax reform bill. It is a bill that would put us \$600 million further in the hole for the relief of those who do not need it.

I see no good, no public benefits in the bill to compensate for the loss of revenue and the greater inequity in the tax structure which would result by giving no relief to those in the lower income brackets, but giving more tax cuts to those in the higher brackets. It would not give a tax cut to the buying public. It is based upon a trickle-down theory which is an archaic and outmoded economic theory, not leading to a generally prosperous economy.

Mr. President, I hope that the conference report is rejected. I ask for the yeas and nays.

The yeas and nays were not ordered.

Mr. YARBOROUGH. Mr. President, I suggest the absence of a quorum.

Mr. MANSFIELD. Mr. President, will the Senator withhold his request until we determine whether it is possible to arrive at a time at which to vote?

Mr. YARBOROUGH. I withhold my request. I have no further statement to make.

Mr. MANSFIELD. Would it be satisfactory if we can arrange to vote at or before 5 o'clock?

Mr. YARBOROUGH. Whatever hour is satisfactory to the majority leader is satisfactory to me.

Mr. MANSFIELD. Mr. President, I ask unanimous consent that there be a vote on the conference report at or before 5 o'clock.

Mr. SMATHERS. If no Senator wishes to speak further, perhaps the vote could be taken sooner.

Mr. MANSFIELD. I suggested any time before 5 o'clock.

Mr. SMATHERS. Very well.

The PRESIDING OFFICER. Is there objection to the request of the Senator

from Montana? The Chair hears none, and it is so ordered.

Mr. MANSFIELD. Mr. President, I ask for the yeas and nays on the question of agreeing to the conference report.

The PRESIDING OFFICER. Is there a sufficient second?

The yeas and nays were ordered.

Mrs. NEUBERGER obtained the floor.

Mr. MANSFIELD. Mr. President, will the Senator from Oregon yield?

Mrs. NEUBERGER. I yield.

Mr. MANSFIELD. May I ask how long the Senator believes she will speak?

Mrs. NEUBERGER. Not more than 5 minutes.

Mr. MANSFIELD. Mr. President, will the Senator yield for the purpose of my suggesting the absence of a quorum, without losing her right to the floor?

Mrs. NEUBERGER. I yield with that understanding.

Mr. MANSFIELD. Mr. President, I suggest the absence of a quorum.

The PRESIDING OFFICER. The clerk will call the roll.

The legislative clerk proceeded to call the roll.

Mr. MANSFIELD. Mr. President, I ask unanimous consent that the order for the quorum call be rescinded.

The PRESIDING OFFICER. Without objection, it is so ordered.

Mr. MANSFIELD. With the consent of the Senator from Oregon, I should like to ask the attachés of the Senate to notify Senators that there will be a vote between now and 5 o'clock on the conference report on the tax bill.

The PRESIDING OFFICER. The attachés will take note.

Mrs. NEUBERGER. Mr. President, during the initial debate on section 3 of the tax bill, the lobbying expense deduction was sharply challenged by the Senators from Illinois and Tennessee. At that time I was particularly impressed and disturbed by their argument that the deduction would benefit only those private commercial interests which already exercise a disproportionate voice in the legislative process. During the present session, we have had ample opportunity to witness the voice of the consumer struggling to be heard against the broadly financed campaigns of the business giants. The lobbying deduction will only amplify the advantage already enjoyed by the business interests.

Unfortunately, the counsel of my dissenting colleagues remained unheeded and the lobbying deduction is entrenched in the conference report now before us. The deduction is, however, expressly limited to direct lobbying. It is, therefore, important that the legislative history clearly indicate that section 3 disallows deductions for efforts "to influence the general public, or segments thereof."

I have before me a copy of the detailed and exhaustive minutes of a meeting of the timber policy implementation committee of the National Lumber Manufacturers Association held in Chicago on June 14 of this year. These minutes describe the committee's launching of a program of "massive" public indoctrination in the goals of the National Lumber Manufacturers Association.

After preliminary discussion, the committee unanimously adopted the following statement of purpose:

It shall be the purpose of the timber policy implementation committee to develop widespread support for Federal forest management policies that produce jobs, income, industry stability and prosperous communities by—

(a) Organizing and activating local citizen groups to aid in finding solutions to Federal timber supply problems;

(b) Informing Federal forest dependent communities of the problems of Federal forest management;

(c) Developing community understanding of how such problems affect the well-being of dependent communities;

(d) Encouraging community leaders to inform the government of their interest in such problems by bringing an informed opinion to bear on public land management policies and decisions;

(e) Encouraging other forest industry associations and other organizations interested in the timber policy problems of the industry to cooperate in carrying forward the committee's program and to undertake such other activities and programs in the interest of purchasers and processors of Federal timber and communities dependent upon Federal timber as may be helpful in maintaining stability for those who buy and process timber from Federal forests, and the communities dependent thereon;

(f) By discussing such problems with Government agencies involved.

The committee also appropriated for the implementation of its program the sum of \$55,000.

I am not concerned today with the merits of the National Lumber Manufacturers Association's case. There are, however, significant groups, particularly conservation groups, which take a view of timber policies diametrically opposed to that of the National Lumber Manufacturers Association. It is certain that any expenditures made by these groups in disseminating their views will not be tax deductible, and I should like to make certain that the contributions of individual lumber companies to the timber policy implementation committee's program will be equally nondeductible.

I am probably particularly sensitive about this issue because in my State of Oregon there is a very active group, conservation minded, and interested in having the Oregon dunes established as a national seashore park. Contributions to the support of this avowed lobbying group are non-tax-deductible. The activities of the committee supporting the Oregon dunes are non-tax-deductible. I see an opportunity here for this massive program, which I will ask to have inserted in the RECORD.

It is planned in every detail as a tax deductible item.

I quote a few paragraphs from this plan:

It sets out the scale of contributions, and how the members of the NMLA will contribute according to the number of board feet they produce. It states:

It will be possible to begin operations with the funds in hand, but accomplishment of the long-range purposes of the program will depend upon the voluntary subscription of several hundreds of thousands of dollars over a period of several years.

All of this will be tax deductible under our new tax law.

In another place the plan states:

The series of speeches at service clubs will pave the way for a communitywide rally to which all members of all organizations in the community will be invited by either a telephone squad or a direct mail campaign. It is likely that for an organization such as FACTS where there is no profit motive, arrangements could be made for free use of a grange hall, a lodge hall, or even a high school auditorium.

In another section it states that the implementation of one of the points has assumed greater urgency "because the Secretary, and the Chief of the Forest Service, had failed to take any recognition of the needs of dependent communities."

The assumption is that they must lobby them further.

Then it states:

The committee members concluded that an intense interest in the industry's problems had been sparked in Congress and the Forest Service had been made acutely aware of the dissatisfaction with its policies and procedures; that the industry had laid effective groundwork and built up a momentum which should not be allowed to die down; and that a program was needed to build up public support which, when added to the industry's efforts, would eventually lead to solution of the problems.

I could go on and on and cite details which the lumber manufacturers have available for presenting their cause before communities and before Members of Congress, before members of the Cabinet, and so forth. My point is that all of this grandiose effort is a tax deductible item under the new bill.

I ask unanimous consent to have the minutes of this meeting are the prospectus inserted in the RECORD, at this point.

There being no objection, the material was ordered to be printed in the RECORD, as follows:

MINUTES OF THE MEETING OF THE TIMBER POLICY IMPLEMENTATION COMMITTEE, WATER TOWER INN, CHICAGO, ILL., JUNE 14, 1962

A meeting of the timber policy implementation committee was held at the Water Tower Inn, Chicago, Ill., June 14, 1962, in accordance with due notice of call. The meeting was called to order at 9:30 a.m. by Chairman, N. B. Giustina, and upon call of the roll, the following members, a quorum, were present:

Representing Western Pine Association, E. C. Rettig, C. T. Gray, Walter W. Black; representing West Coast Lumbermen's Association, Niles B. Hult, R. W. Middleton; representing Southern Pine Association, J. F. Muller, Ralph S. Taggart, Warren Briggs; at large, B. L. Orell, J. D. Bronson, C. M. Hines, N. B. Giustina, Douglas M. Miller.

Others present included Robert Keck and W. E. Griffie. Absent members were Abbott M. Fox and L. L. Stewart.

OPENING REMARKS OF CHAIRMAN

Chairman Giustina briefly outlined the appointment of the committee by NLMA President Arthur Temple, Jr., and stated the purpose of the meeting. He explained that the committee had been requested to implement a public relations program through a "grassroots" organization to activate broad public support of the four points which the industry felt would solve its Federal timber problems. These four points, he added, dealt with allowable cut, timber appraisal procedures, appeals procedures, and proposals for study and revision of Government timber sales contract forms.

After concluding his remarks, Chairman Giustina called upon Mortimer B. Doyle, executive vice president of the National Lumber Manufacturers Association, to give the background of the problem which had led to the appointment of the committee.

BACKGROUND OF INDUSTRY'S FEDERAL TIMBER POLICY PROGRAM

Mr. Doyle recounted the numerous efforts made in the past by various industry groups to bring about parity in bargaining between Federal administrators and members of the industry dependent of Federal timber. All of these efforts, he stated, had been fruitless and the situation had progressively deteriorated.

Not succeeding in correcting the policies and practices of the Federal timber management agencies which were leading to industry instability and economic distress for the companies and communities dependent upon Federal timber, the National Lumber Manufacturers Association Forest Management Committee, Mr. Doyle said, had studied the matter in detail. The committee, he added, had concluded that industry and community forces must be combined to develop enough strength and influence to impress the Federal agencies of the urgency of the problem. To accomplish this, he said, the forest management committee recommended, and the board of directors at the November 1961 meeting authorized the appointment of an executive council on Federal timber supply.

The council met in December 1961 and developed a five-point program, Mr. Doyle stated. The first four points the chairman had already outlined, he said, and the fifth called for the establishment of a citizens' public information organization to build up grassroots support for the solution of the industry's Federal timber policy problems.

Mr. Doyle then enumerated the developments and actions taken since that meeting of the council which included—

(a) January 19, 1962: National Lumber Manufacturers Association executive committee approved in principle council's first four points and authorized National Lumber Manufacturers Association participation and support of fifth point, if such action were requested by affected regional associations.

(b) February 21, 1962: Four points presented to Secretary of Agriculture and 45 Members of Congress.

(c) Letters from hundreds of lumbermen written to Members of Congress emphasizing seriousness of situation.

(d) March 1962: Western Pine Association authorized \$25,000 for point 5, providing National Lumber Manufacturers Association developed an acceptable program within 90 days.

(e) March 12, 1962: National Lumber Manufacturers Association executive committee authorized expenditure of \$25,000 for point 5, providing comparable financial cooperation was sought from other groups.

(f) Series of meetings held by National Lumber Manufacturers Association and Congressmen and Senators: April 11, 1962; April 12, 1962; and June 4, 1962.

(g) March 3, 1962: Nine western Senators wrote Secretary of Agriculture supporting industry's position and urging prompt consideration. Secretary replied on April 17, 1962.

(h) May 9, 1962: Having received no reply from the Secretary of Agriculture regarding its February 21 presentation, NLMA board of directors at its 1962 spring meeting reaffirmed its position and instructed President Temple to telegraph President Kennedy urging prompt action on the industry's problems. A reply was received 10 days later from a Deputy Assistant Secretary of Commerce stating that the Department of Commerce and other agencies would conduct a

complete study of industry problems and make recommendations for Government consideration and action.

(i) May 24, 1962: Eight Members of Congress spoke on industry's situation on floor of House of Representatives.

(j) June 4, 1962: Major portion of testimony and discussion at hearings before Senate Commerce Committee in Portland, Oreg., was on National Forest Management problems.

(k) June 11, 1962: Secretary of Agriculture replied to industry's point 4 program.

Mr. Doyle summarized by stating that the industry had made some progress on all four points, but had failed to achieve its main objectives. In view of this, he said, implementation of point 5 had assumed even greater urgency because the Secretary, and the Chief of the Forest Service, had failed to take any recognition of the needs of dependent communities.

He then outlined the task of the committee which, he said, included the following three fundamental steps:

(a) Development and acceptance of a statement of objectives.

(b) Adoption of a comprehensive plan of operation.

(c) Adoption of a preliminary budget to accomplish the objectives of the program in line with the operation plan.

After elaborating on the details of each of these points, Mr. Doyle concluded by stating that if the program were well-conceived, well-financed, and well-executed, it would stimulate action at the local level which inevitably would attain the objectives the industry was seeking.

Following Mr. Doyle's summary of the background of the industry's Federal timber policy program, the committee discussed the resolution adopted by the NLMA Board of Directors on May 9, 1962, authorizing the program. Question was raised as to the interpretation of the provision that the "committee will cooperate with the regional associations, their members and others to secure broad public support for the program." The members concluded that they should first approve and detail a program and then decide how it should be implemented.

GENERAL DISCUSSION OF PROPOSED PROGRAM

Before taking up specific aspects of the proposed program, the committee read the material in the meeting book which had been prepared by the NLMA staff and informally discussed the suggested statement of purpose, methods of accomplishing objectives, operating policies and procedures and preliminary budget.

The committee members concluded that an intense interest in the industry's problems had been sparked in Congress and the Forest Service had been made acutely aware of the dissatisfaction with its policies and procedures; that the industry had laid effective groundwork and built up a momentum which should not be allowed to die down; that they should take advantage of what had been done; and that a program was needed to build up public support which, when added to the industry's efforts, would eventually lead to solution of the problems.

The committee agreed that it should—

(a) Determine the general approach to the problem.

(b) Decide if the approach should be long range or short range.

(c) Decide if they could develop a program which would produce the desired results.

(d) Determine if they could get adequate financing to carry forward such a program.

(e) Determine the organization and administration of such a program.

Following the general discussion, the committee took up each point of the program in detail.

STATEMENT OF PURPOSE

The committee discussed the purpose of the timber policy implementation committee and the need for a clear-cut statement to serve as a guide in its future operations. During the discussion it was brought out that the whole program should be aimed at securing equity from the Federal Government on timber policies and the purposes and objectives should clearly state and foster this aim.

After detailed discussion of the purposes of the timber policy implementation committee, on motion by Mr. Middleton, seconded by Mr. Rettig, the following statement of purpose was unanimously approved:

"It shall be the purpose of the timber policy implementation committee to develop widespread support for Federal forest management policies that produce jobs, income, industry stability and prosperous communities by—

"(a) Organizing and activating local citizen groups to aid in finding solutions to Federal timber supply problems;

"(b) Informing Federal forest dependent communities of the problems of Federal forest management;

"(c) Developing community understanding of how such problems affect the well-being of dependent communities;

"(d) Encouraging community leaders to inform the Government of their interest in such problems by bringing an informed opinion to bear on public land management policies and decisions;

"(e) Encouraging other forest industry associations and other organizations interested in the timber policy problems of the industry to cooperate in carrying forward the committee's program, and to undertake such other activities and programs in the interest of purchasers and processors of Federal timber and communities dependent upon Federal timber as may be helpful in maintaining stability for those who buy and process timber from Federal forests, and the communities dependent thereon;

"(f) By discussing such problems with Government agencies involved.

"The immediate objectives of the committee shall be the implementation of the four lumber industry recommendations to the Secretary of Agriculture which are: (1) an annual statement of performance standards; (2) a fair appraisal method; (3) a practical and workable appeals procedure; and (4) contract revision, as well as other current timber policy problems, such as ingress and egress, land acquisition by public agencies and other similar matters."

METHOD OF ACCOMPLISHING OBJECTIVE

The committee next discussed how to proceed to carry out its responsibilities and what method for financing the program should be approved. Three alternatives were discussed:

(a) Providing required funds from the National Lumber Manufacturers Association budget.

(b) Additional contributions from the federated regional associations.

(c) Support from individual companies whose future is dependent on a prompt solution of the problem.

During the discussion it was brought out that the National Lumber Manufacturers Association could only finance the program at the expense of other approved activities and projects and that, similarly the regional associations had indicated their budgets were not flexible enough to accommodate additional budgetary expenses at the present time.

The committee, after discussing the matter in detail, concluded that the program should be launched with the funds already available and that continuing support should be on the basis of individual company con-

tributions, and continued support of interested associations. Following discussion of the exact wording of the resolution, including amendments, on motion by Mr. Hines, seconded by Mr. Rettig, the following resolution was unanimously approved:

"In view of the importance of carrying forward promptly and intensively the Federal timber policy program, the Timber Policy Implementation Committee approves the establishment and carrying forward of the program on the basis of individual company contributions, together with continued support of interested associations."

OPERATING POLICIES AND PROCEDURES

The committee then discussed what operating policies and procedures would be appropriate to the successful carrying forward of the program. During the discussion it was brought out that although the industry had on many occasions in the past presented its timber management problems to the Congress and the administrative agencies of the Government, it had met with little success in securing solutions to those problems.

Another point made was that it was now apparent that the industry must muster the massive support of the general public in those communities dependent upon the forest based industries. To do this the grass roots strength necessary to achieve policy revisions essential to community and industry survival must be organized and once organized this strength must be exerted at the local level toward apprising elected representatives and Federal administrators of the urgency of prompt and effective action to correct the economic effects of adherence to existing policies.

There was considerable discussion of where the program would be initiated—which areas would be given priority. It was brought out that this program should lead to an approach to the Forest Service which might not directly bear on the four points, but would have important reactions on any future operations in association with the Forest Service. In this connection, it was brought out that if any policy determinations were effected at the national level, every region would benefit, and each local area would feel the results. Therefore, the determination of "priority areas" was not essential to the effectiveness of the program.

Following discussion of the various points which should be included in a statement of operating policies and procedures, on motion by Mr. Bronson, seconded by Mr. Muller, the following resolution was unanimously approved:

"The solution of the industry's problems with Federal agencies is a matter of paramount importance to the companies and communities dependent upon Federal timber. To effectively carry out its responsibility in this connection, the timber policy implementation committee hereby established the following statement of operating policies and procedures:

"1. The industry must assume fundamental responsibility for solicitation and provision of adequate financial support from principals and companies concerned with Federal timber policy problems.

"2. The committee will provide guidance in the selection of communities in which basic organizational activities are to be carried forward by the staff and nominate for enlistment in the program citizens in each community who are aware of the correlation between forest-industry operations and community prosperity.

"3. The committee will undertake, within the policies and directions of the National Lumber Manufacturers Association board of directors, to guide the evolution of the program, determine its scope and emphasis and to provide such other direction as may be requested by the executive vice president of National Lumber Manufacturers Association.

"4. It will be the responsibility of the staff to carry out, under the direction of the executive vice president, programs and activities approved by the committee as contributive to the principal objectives of the committee and to develop additional projects and associated efforts for consideration by the committee. In this connection, the staff will be charged with conceiving, developing, and executing programs designed to establish, as rapidly as possible, in key areas, strong local groups comprised of business, professional, and other community leaders and providing such groups with printed and visual materials enabling them to conduct effective action programs among their fellow citizens. Such organizations, programs, and instructional materials shall be aimed specifically at informing the general public of its stake in Federal timber policies.

"5. In accordance with its bylaws and the authorization of the board of directors, National Lumber Manufacturers Association will furnish, at cost, the services and facilities required in the program.

"6. To carry forward its program speedily and effectively, the timber policy implementation committee solicits the active cooperation, support and assistance of the federated associations, all producers and other organizations, companies, and individuals susceptible wholly or in part to the influence of the Federal timber policy programs with which the timber policy implementation program is concerned."

ADMINISTRATION OF THE PROGRAM

The committee discussed the administration of the program and the most practical way of accomplishing the job to be done. It was suggested that the program be handled as a special project under the auspices of the National Lumber Manufacturers Association.

During discussion it was brought out that establishing the program as a special project under NLMA in no way precluded solicitation of funds from nonmember companies nor contributions from affiliated or other associations or groups. It was also pointed out that setting up the program in this manner put the committee in the clear position of moving in any direction it desired without having to go through formal approval by another group, just so long as its activities did not conflict with National Lumber Manufacturers Association approved policies.

Following discussion, on motion by Mr. Rettig, seconded by Mr. Hines, the following resolution was unanimously approved:

"The administration of the timber policy implementation committee shall be a special project of the National Lumber Manufacturers Association."

BUDGET

The committee discussed what budget should be provided for the timber policy implementation program. Mr. Doyle outlined a preliminary budget for the committee, which he said would provide the maximum program activities and require the services of five full-time and four part-time employees.

During the discussion which followed, it became evident that members of the committee were agreed that it would be better to start the program off modestly. In discussing the details of the National Lumber Manufacturers Association accounting procedures, it was pointed out that the association's fiscal year runs from December 1 to November 30 of the following year, and establishing a June-to-May fiscal period for the committee would create some difficulties as far as the National Lumber Manufacturers Association bookkeeping was concerned.

The following suggestions were offered for the committee's consideration:

(a) That a preliminary first budget for 6 months (to November 30, 1962) of \$30,000 be approved to get the program underway.

(b) That the committee schedule a meeting at the time of the National Lumber Manufacturers Association annual meeting (November 1962) to consider next year's operations, including a 1963 budget.

(c) In the interim, ascertain the probable amount of support available from individual companies, associations and others.

(d) Members of the committee in the meantime study and digest the full recommended program so they would be informed of its proposed activities and could make suggestions at the November meeting.

After discussion of the budget requirements of the program, on motion by Mr. Taggart, seconded by Mr. Hines, the following resolution was unanimously approved:

"That the program be inaugurated with the understanding that there is now available the sum of \$55,000 for the expenditure; that expenditures between now and November 30, 1962, not exceed \$30,000; that a program and funding effort be developed within 30 days and presented to the industry for consideration and attitude; and that, based on such industry attitude toward funding on a yearly basis, a final yearly budget be formalized at the time of the National Lumber Manufacturers Association annual meeting in November 1962."

Members of the committee expressed the desire that the experienced National Lumber Manufacturers Association personnel who had been working on this program be made available for advising and counseling the committee, consistent with their other duties and responsibilities and with appropriate costs charged to the committee. Mr. Doyle assured the committee that this would be done.

Following approval of the budget, each member of the committee expressed satisfaction with the program. There was general agreement that the program, as approved would be acceptable to the federated associations and the industry.

ADJOURNMENT

There being no other business, the meeting was adjourned at 5 p.m.

MORTIMER B. DOYLE,
Committee Executive.

PROSPECTUS FOR TIMBER POLICY IMPLEMENTATION COMMITTEE PROGRAM

THE OBJECTIVE

The timber policy implementation program is designed to acquaint forest-based communities with the economic and regulatory factors affecting the lives and futures of their citizens and to influence them to insist that the executive branch of Government bring about parity in industry-Government bargaining, particularly with respect to industry proposals involving (1) sale of the allowable cut from the national forests; (2) realistic timber appraisals; (3) administrative and judicial appeals procedures; (4) timber sales contract form.

In addition, the committee will undertake to explain the impact on communities of other timber policy problems, such as ingress and egress, land acquisition by public agencies and other similar matters.

Communities dependent upon Federal timber for fundamental industrial employment must be made aware of their own stake in the continued operations of firms engaged in logging and the production of lumber and wood fibers.

Present Federal timber sales policies exert an influence on the lives of every man, woman and child in each such community. If responsible citizens of those communities are made conscious of the threat to community existence by Federal Government adherence to unsound policies they will, at the local level, tend to demand corrective action by their elected representatives.

In the past there has been no continuous, nationwide, coordinated effect on the part of the forest industries to acquaint residents

of dependent communities of these facts nor to solicit their support of industry programs for correction.

The increasing unemployment in the forest industries and the advantage of discussing the issues in terms of continued employment give the overall effort a sense of urgency which should not be underrated. Similarly, since most of the communities involved derive their principal revenues for all their goods and services directly or indirectly from the forest it will be possible to arouse positive action by all citizens and not only those directly employed by the forest industries. Local press, radio and television outlets, local elected officials, service clubs and other community spirited organizations and citizens should react positively to an effort which is designed to strengthen the economic base for their own community.

THE BASIC PLAN

It is planned to conduct the timber policy implementation program on a national basis, concentrating initially on the creation of a network of local action committees in communities which depend heavily upon Federal timber for their economic stability.

DETERMINING THE ORGANIZATIONAL TARGETS

There are two fundamental ways to proceed in organizing the local committees. The first envisions the establishment of citizens committees in cities and towns which are largely dependent upon Federal timber and upon the payrolls resulting from the logging and conversion of logs into manufactured items. The second contemplates the analysis of political geographic units which derive direct benefits from the sale of Federal timber and which afford a primary opportunity for direct assistance to Government representatives while, at the same time, reducing the organizational burden.

In the first instance, where sawmill towns are principally involved, the community leaders, in most instances, may be directly identified with the logging or sawmill operators. If such individuals assume fundamental leadership for the campaign, the project may be attacked by the opposition on the basis that it is self-serving and is a means for the operators to strengthen their own position by using the community. Such opposition would reduce the basic effectiveness of the program since much time and effort would be spent in defending the integrity of the program while its main objectives would suffer. In the second instance, however, using county seats in Federal timber areas as the basic organizational unit it would be possible to identify with the public interest from the outset and win the support of elected county officials as well as teachers, lawyers, doctors, and other professional people with the mill operators participating as interested local citizens with special knowledge of the problem.

The county is the basic Government unit which derives direct financial return from Federal timber sales which is earmarked for building roads and for public education. Similarly, county seats afford an opportunity to make use of such newspaper, radio, and TV facilities which may exist in forested areas. It appears logical on that basis to concentrate on the county seats in forested areas as the first places in which to organize local action committees.

While there are approximately 6,000 communities in the United States having a population of 2,500 or more (based on the 1960 census) there are only 3,072 counties in the United States plus 24 election districts in Alaska. These latter 3,000 political units would require screening against Federal timber involvement to determine areas of initial concentration for organization. Taking the Pacific Coast States as an example, California has 58 counties; Oregon, 36; and

Washington, 39. By concentrating organizational work initially on county seats, it would be possible to establish basic units in only those communities having a direct relationship to timber sales among the 133 potential communities. Similar examples can be found in the South and Midwest. If, on the other hand, a decision were made to establish action groups in forest-based communities having 2,500 or more population in those three States, California would require screening of 386 potential communities, Oregon, 61, and Washington, 84, for a total of 531, or nearly four times the number of county seats.

There is an interesting political phenomenon concerning county seats which may have a direct bearing on the success of concentrating the organizational effort in those communities. All seven Members of the Washington delegation in the House of Representatives and both Senators from that State reside in six communities which are county seats. Three of the four Oregon Congressmen and both Senators from Oregon also reside in county seats. Eighty percent of the present Members of the U.S. Senate reside in county seats.

Step one of organizing the implementation program must be to analyze the counties of the United States to identify those counties which have a substantial interest in Federal timber sales. Then the place of residence of each Congressman representing such a district would be checked against the county seats of those counties, and the residences of all Senators would be checked against county seats within forested States. The final determination of county seats meeting any of these criteria would provide the community list for initial organization. It would be desirable, of course, to ascertain simultaneously the counties where all Congressmen live as a basis for phase 2 of the organizational effort.

Those communities dependent upon the forests in which national legislators reside would receive top priority for the initial organization. It follows then that attempts would be made to organize all county seats in areas having Federal forests.

As each local group is formed in a county seat it would be assigned the responsibility of establishing similar groups at other cities, towns, and villages within the boundaries of the county with the presidents of all groups comprising a county action committee.

ADOPTING AN IDENTITY

Although the overall project will be identified by the name of the responsible committee within the National Lumber Manufacturers Association, the timber policy implementation committee, it will be essential to adopt an identifying name for local action groups which has the threefold advantage of being significant when written in its entirety, meaningful when abbreviated to its key initials, and easy to remember once it has been heard or seen and established in the minds of both people in the community and the elected officials who will be the ultimate targets of the group's action.

Many current successful action groups have one-word abbreviations for longer titles such as COPE, MEDIC, CARE, HELP, AID, and ACTION.

The local action groups of the timber policy implementation committee will be known as the committee on Federal and community timber supply. The short form will be FACTS.

This designation will serve to remind the community that the actions of the group will provide FACTS with respects to the local economy; that the function of the group is in the interest of community information without being either politically or selfishly inspired; and that identification with the

program will enable the entire community to improve its outlook and opportunity.

An easy-to-remember designator which has significance when related to the basic name of any organization is a great asset in making the general public aware of the organization and what it is doing.

LAUNCHING THE PROGRAM

Basic to undertaking a community action program of any kind is adequate funding.

When it has been determined what the communities are which can yield the greatest potential results from being organized, it will be necessary to alert forest-based industries having a need for Federal timber in those areas and solicit their financial support as well as advice with respect to local leadership.

Consideration must be given in each community situation to the advantages and disadvantages of having local committees directed by forest industry managers. In some communities direct leadership of the program by officials of lumber companies, for instance, might be misconstrued by the very people it is desired to enlist. In other communities such lumber leadership would be absolutely essential. Each community must be studied to determine the best leadership approach. In general it is considered that the program would be best served by having forest industry firms provide nominations of doctors, lawyers, teachers, clergymen, club men and women, elected officials, and other community opinion leaders who have demonstrated an understanding of the correlation between community economic health and a strong forest industry. Direct contacts with these people will be conducted personally by timber policy implementation committee program staff representatives during the active organizational phase.

FUNDING THE CAMPAIGN

The board of directors of National Lumber Manufacturers Association, in adopting the resolution relative to the Timber Policy Committee of National Lumber Manufacturers Association made available to the Committee the funds subscribed in support of its activities and authorized solicitation of funds from the regional and other interested associations and individual companies when the committee has prepared and submitted an acceptable plan, including a budget.

Current National Lumber Manufacturers Association funds available total \$25,000, but the Western Pine Association Directors have authorized expenditures of \$25,000 and the Southern Pine Association, \$5,000 to support an acceptable Federal timber policy implementation program.

It is contemplated that direct solicitation of funds from purchasers and processors of Federal stumpage, including all segments of the forest products industry, pulp and paper, plywood, railway ties, and other forest manufacturers, and lumber manufacturers will be undertaken with rates established on the basis of volume of Federal timber purchased last year by each supporter.

The scale of contributions recommended is as follows:

	Annual dues
Quantity of Federal timber purchased:	
Less than 5,000,000 board feet.....	\$100
5 to 10,000,000 board feet.....	500
10 to 25,000,000 board feet.....	1,000
25 to 50,000,000 board feet.....	2,500
50 to 100,000,000 board feet.....	5,500
Over 100,000,000 board feet.....	10,000

Based upon an analysis of purchases of Forest Service stumpage by the 200 largest buyers, the scale of contributions would provide with good support of those buyers, the necessary annual budget of \$145,000.

Funds such as those required to support this venture will not be obtained by direct mail solicitation alone. It will be necessary for principals, who themselves are contributors, to arrange personal or phone interviews with the principals of prospective donors and sell both the concept and the program. Large sums cannot be obtained through solicitation by members of the staff.

A fund solicitation committee of five industry principals will be established for each volume category of Federal timber purchasers and will conduct direct solicitation personally, by telephone, and by mail among firms purchasing Federal timber in the same volume as the individuals soliciting the contributions. This technique will assure that small, medium, and large operators will be reached by businessmen who share similar problems with respect to Forest Service timber policies and who will thus be more convincing salesmen of the concept of participation.

It will be possible to begin operations with the funds in hand, but accomplishment of the long-range purposes of the program will depend upon the voluntary subscription of several hundreds of thousands of dollars over a period of several years.

THE CAMPAIGN

Essentially the function of the staff will be to provide community leaders, and through them the public at large in forest-based communities, with information and guidance with respect to the effect of forest service timber policies on the economic well-being of their communities and of their fellow citizens. The means for accomplishing this task are limited only by the available funds and staff.

A fundamental program is that of organization within key communities to provide the timber policy implementation committee and the staff with a leadership of hardworking, knowledgeable people to represent the community's point of view in public forums, community meetings, and various sessions with local, State, and national officials and lawmakers.

As indicated, it will be necessary to assemble the names, interests, and capability factors of key residents of affected communities and to determine an itinerary for a staff member to methodically tour the regions and undertake the establishment of local action committees.

The staff representative will be armed with a well-conceived simple visual presentation, supported by reading material so that he can make a presentation to key leaders in a small, informal session designed to acquaint them with the facts. A more elaborate, sound-color filmagraph or motion picture should be developed to explain the issues, demand the action, and describe the results of success or of failure to larger audiences. The organization of a local conference on the subject should be the obligation of the local committee with a staff member arriving to conduct the session and describe the work of the group.

The staff will be obliged to develop a series of patterned speeches, news stories, radio scripts, and television materials for use by the local group in arousing community interest in a mass meeting to consider the problem. Sample kits of this material will be available at the first meeting of each local organizing group and will be prepared in such a way that it can easily be converted for use in each locality.

It is essential that the local chamber of commerce, which has ready access to local statistics with respect to employment, payrolls, industry, and other community economic and population statistics, be approached immediately after the local group has agreed to undertake the local program. Basic information of this kind, carefully melded into the basic news and feature ma-

terial for all media will help materially in alerting local citizens to their dependency on forest industries and spur their interest in supporting the efforts of the local committee.

Immediately after announcing the creation of the local committee, the fact that it has met, and the outline of the program it proposes to carry forward for the local community, it will be essential to involve the local radio, TV, and newspaper outlets in a planned sequence of editorials, feature articles, TV panel shows, radio interviews, and similar public service activities acquainting the general public with the facts and recommending that they interest themselves in the battle being fought in their behalf.

On a predetermined time schedule, probably a month following the initial meeting, arrangements should be made for a speech bureau which will provide qualified speakers on each of the four points who can explain the ramifications of each and relate it to the needs of the immediate community.

Once again, the local committee should take the lead in providing opportunities for the speakers to make appearances through the service clubs of the area. Speaking dates before service clubs in smaller communities provide a potential three-way impact: To the captive audience at luncheon or dinner; to the reading public where detailed accounts of such addresses are frequently published, when a text is provided the editor in advance; and through radio which frequently carries live remote broadcasts or tapes the speech and plays it over the air in prime time.

The series of speeches at service clubs will pave the way for a communitywide rally to which all members of all organizations in the community will be invited by either a telephone squad or a direct mail campaign. It is likely that for an organization such as FACTS where there is no profit motive, arrangements could be made for free use of a Grange hall, a lodge hall, or even a high school auditorium.

It will be necessary for a staffman to arrive in the community several days in advance of community rally to assist local leaders to develop an audience. Where possible, it would be desirable to have congressional representatives on hand to speak in favor of the overall program. It will be equally desirable to invite the chairmen of both the county Democratic and Republican committees to sit on the platform and thus demonstrate the nonpartisan nature of the issue. The image of community solidarity would then become apparent. Sufficient advance notice of this kind of ideal situation would enable the staff to alert national news magazines and picture magazines in addition to the wire services for a full-scale "grassroots" economics story, which are few and far between.

Immediate attention will be given to the development of a leadership manual for use in the local committees to provide detailed discussions of each of the four points, and other timber policy issues, questions and answers, membership campaign information and techniques, fund solicitation information for local projects and programs, and outline for the local campaign and how-to-do-it information, a description of methods for influencing community opinion molders, and a primer concerning community programs and how they should be operated for maximum success.

Basic issue pamphlets will be prepared and will be designed to provide for imprinting of the name of the local committee and localization to as great an extent as possible.

In addition, more comprehensive discussions of each point at issue will be developed for use of community discussion group leaders and others who desire more detailed information.

It is essential in any national campaign, involving local action groups, that local workers be identified with a nationwide effort and share, if only vicariously, in the limelight of national identity. For that reason, it might be desirable at a later time to establish a clipsheet to appear monthly with photos and to be distributed in bulk to local committees for distribution. Each editor in participating communities will be included on the mailing list, not only for the newspaper but for all releases originating from the national organization.

A clipping service should be hired to provide measurement of coverage throughout the campaign. Not only will such clippings provide a valuable historical record, but much of the editorial content for the organization clipsheet could be based on the stories occurring at widely separated locations in the United States. Nothing makes a volunteer organization work harder than knowledge that its efforts are being given national recognition and a spirit of competition, created through this means, spurs the entire program.

Consideration should be given eventually to a countywide rally, a statewide rally, and a national rally of individuals representing the organization throughout the country. It would be appropriate at such a national event to have prominent industrialists and public officials recognize the impact of the program and measure its effects.

In addition to the monthly clipsheet, it is considered desirable to undertake publication of a weekly newsletter which will be published on a limited basis for the information and guidance of leaders in each community. It will consist largely of up-to-date information of negotiations with public officials in Washington, quotable quotes from congressional sources, advice on procedures, and a catalog of available materials such as pamphlets, brochures, feature articles, and similar material.

CHRONOLOGICAL ACTIVATION PLAN

1. Approve basic plan, budget, and organization.
2. Employ basic staff.
3. Prepare prospectus.
4. Distribute prospectus, solicit and obtain funds.
5. Determine target communities.
6. Build list of prospective community leaders.
7. Prepare leadership manual, visual presentation, and associated scripts, news stories, pamphlets, and brochures for initial group meetings.
8. Acquire western regional manager.
9. Prepare itinerary for organizational meetings.
10. Develop sound-color filmagraph or motion picture providing detailed information concerning program and community involvement.
11. Develop pamphlet to be distributed to all seeing film.
12. Announce national organization in all media.
13. Arrange first group meetings.
14. Concentrate on development of materials for speakers bureau.
15. Initiate weekly newsletter.
16. Organize initial community rallies.
17. Contact national officials of employee groups, enlist their endorsement of program and participation by locals. Follow on with Grange, Farm Bureau Federation, Hoo-Hoo, and similar groups.
18. Sustain program in all aspects providing new and different material on a regular basis to each organized community.

Staff Organization and Functions

The timber policy implementation committee will be staffed and administered under the existing industry relations division of the National Lumber Manufacturers Association, with separate accounting and financ-

ing, but bearing its appropriate share of administrative and services costs.

The timber policy implementation committee program will be coordinated with present programs conducted by the industry relations division, benefiting from the staff personnel already available but retaining a separate and distinct identity.

The chief forester of NLMA will serve as a special adviser to the committee.

Staff personnel—timber policy implementation committee. Director for community programs and manager, eastern region: Under the direct supervision of the director, industry relations division, he will conceive and execute projects and programs to achieve the purpose of timber policy implementation, will directly supervise the personnel under his jurisdiction, and will conduct organizational activities within the States east of the Mississippi River.

Secretary to the assistant director for community programs will perform all duties appropriate to the position including the maintaining of appropriate files, records, and procedures as required.

Manager, Pacific coast region will conduct organizational activities within the States of California, Oregon, and Washington and will operate from a city centrally located in the region under his jurisdiction.

Manager, Rocky Mountain region, will conduct organizational activities in the States of Idaho, Montana, Arizona, New Mexico, Colorado, Wyoming, Utah, South Dakota, and Nevada, and will operate from a city centrally located in the region under his jurisdiction.

Manager, editorial services department will provide all written materials required for accomplishment of the programs and projects undertaken by the timber policy implementation project including, but not limited to, editorials, pamphlets, brochures, news stories, feature articles, speeches, manuals, scripts, and photographic materials.

Secretary to manager, editorial services department will perform all duties appropriate to the position including maintenance of appropriate files, records, and procedures, including the historical records of accomplishments.

National Lumber Manufacturers Association will provide the balance of timber policy implementation committee staff activities with appropriate charges to the timber policy implementation committee.

The PRESIDING OFFICER. The question is on agreeing to the conference report on the tax bill.

Mr. KERR. Mr. President, I wish to read from the letter of the Secretary of the Treasury with reference to the investment credit provision in the bill before the Senate:

The central element of the President's recommendations was the need for an incentive for investment in machinery and equipment that would stimulate a higher rate of economic growth and better enable our industry to compete in markets at home and abroad. The investment credit contained in this bill will operate as a powerful stimulus to investment. In combination with the Treasury's recent administrative reform of depreciation, the credit will, at long last, give to American business tax treatment on new investment in machinery and equipment approaching that of its chief competitors in Western Europe, Canada, and Japan. Its adoption will constitute a major advance toward our national goals of greater economic growth and the increased productive efficiency and competitiveness necessary to a solution of our balance-of-payments problem.

Mr. President, it is the opinion of the Senator from Oklahoma that those who

take the position that the investment credit provision in the bill will not result in a great stimulant to our economy, that it will not result in the encouragement of expansion and modernization, and thus make a more efficient productive complex of our industrial structure, either have not read the bill or do not understand it.

We have listened to many who talked about a recession which was to have begun in August or September. The fact is that every economic indicator now coming to public attention shows that our production is running ahead of a year ago; that our construction outlays are at an all-time high; that the production of steel increased 3 percent last week over the preceding week and that it was the third consecutive weekly increase; that the production of automobiles is 30 percent above what it was a year ago.

Also, I noticed a statement by the chairman of the board of the American Telephone & Telegraph Co. to the effect that new telephone installations were running 7½ percent ahead of a year ago.

In the judgment of the Senator from Oklahoma, a substantial part of the evident increase in our economic production, a substantial part of the improvement in our economic structure in the last 6 to 10 weeks—as related to the time immediately preceding that and as compared with a year ago—is directly attributable to the investment credit.

Mr. GORE. Mr. President, will the Senator from Oklahoma yield?

Mr. KERR. I yield to the Senator from Tennessee.

Mr. GORE. To what would the Senator attribute an incentive to investment? How would the application of the investment credit, which is tax reduction, to January 1, 1962, provide incentive for improvement?

Mr. KERR. There is no Member of the Senate better qualified to answer that question than the Senator who asked it. He is just as aware as is the American industrial and economic community of the fact that the House held hearings on this proposal much of last year; that the House passed a bill early this year which included the investment credit provision; that the House-passed bill provided an effective date of January 1, 1962, for the application of investment credit.

It is the opinion of the Senator from Oklahoma, substantiated by the evidence from countless numbers of representatives of industry, that they had proceeded throughout the year in the development and expansion of their investments with the expectation that the investment credit would be available.

Rather than this provision being in the posture of creating an impetus retroactively, it is but carrying out the expectation of the American industrial workshop throughout the year, as to the result, and the treatment, of their expenditures for new equipment and modernization of old equipment.

Mr. GORE. Mr. President, will the Senator further yield?

Mr. KERR. I yield for a question.

Mr. GORE. Is it a correct understanding of the Senator's answer that the retroactive application of the investment credit is not, in fact, an incentive, but is a reward for what has already been done?

Mr. KERR. The providing of a proposed incentive which is acted upon affirmatively by the beneficiary of it, by reason of its having been proffered, might well be interpreted as being a reward when it materializes; but that is a result after the fact. The stimulant was the productive cause before the fact.

The Senator from Oklahoma, believing in the investment credit provision, and believing that it is a stimulant, certainly would be the first to acknowledge and the last to deny that the receipt by the investor of the investment credit comes as a reward. A reward for what? For having responded to the stimulant of the promise of the credit by moving to expand his productive facilities or to modernize them in response to the stimulant that was offered.

So I say to my good friend from Tennessee, if he succeeds in establishing that this investment credit is a reward to those who have expanded their productive facilities, he will have proved the case that it is effective in bringing about such expansion and such modernization.

Mr. GORE. Mr. President, will the Senator further yield?

Mr. KERR. I yield for a question.

Mr. GORE. If the reward or windfall goes to those who did not make such an investment because of the proposed investment credit, would the Senator give the same answer with respect to them?

Mr. KERR. The Senator from Oklahoma does not care to discuss or speculate on a legislative impossibility. The Senator from Tennessee is an authority on the Constitution. He knows that legislation must be general in application in order to conform to the Constitution.

The Senator knows—being a student of the Bible—that it rains on the just as well as on the unjust; and certainly some of those who will benefit from the investment credit might have made their investments without the credit. The legislation cannot be made applicable only to those who made their investments by reason of the credit, since this is general legislation, and must be made applicable to all who make investments. Moreover, we cannot look into their minds to see what they would have done in the absence of a credit.

SUMMARY OF SENATE AMENDMENTS TO H.R. 10650 REVENUE BILL OF 1962

(Prepared for the use of the House and Senate conferees on the revenue bill of 1962 by the staff of the Joint Committee on Internal Revenue Taxation, September 20, 1962)

[Number of Senate amendment and description]

1. Clerical conforming change.
2. Technical drafting change.

II. INVESTMENT CREDIT

3. Clerical conforming change.
4. Conforming change to No. 5 below.
5. This provides a 3-year carryback of any investment credit which because of the limitation cannot be used in the current year. The 5-year carryforward which was in the

House bill is retained. The credit may not be carried back to a year ending before June 30, 1962, and for years beginning before that date a proration rule in effect limits the carryback privilege to the portion of the year occurring after June 30, 1962. The revenue effect of this amendment is believed to be negligible. This is a committee amendment.

6. This provides that where property is lost or destroyed as the result of a casualty or is stolen and is insured, reinvestment of the insurance proceeds in replacement property is not to be eligible for the investment credit. This is designed to eliminate the allowance of a credit where the taxpayer has made no contribution of additional funds toward the acquisition of new property. This reduces the revenue cost of the credit by \$25 million. This is a committee amendment.

7. Conforming amendment to No. 5 above.

8. Conforming amendment to No. 5 above.

9. Conforming amendment to No. 6 above.

10. This provides that the purchase of livestock is not to be eligible for the investment credit. This was provided because they are not included in the category of property resulting in ordinary income (to the extent of depreciation deductions) at the time of sale. This is expected to result in a revenue gain of less than \$5 million a year. This is a committee amendment.

11, 12, 13, and 14. This provides that the investment credit is to be available only with respect to property acquired or constructed after June 30, 1962, rather than on or after January 1, 1962. This has no full-year revenue effect but reduces the cost of the credit in the first fiscal year by \$650 million. This is a committee amendment.

15. Conforming amendment to No. 6 above.

16. Conforming amendment to No. 5 above.

17. This deletes the requirement of the House bill that in order to shift the benefit of the investment credit from the lessor to the lessee the lessor must be engaged in the business of leasing property. This is intended to avoid the problem of having to determine whether a lessor is engaged in the business of leasing. This change has no significant effect on revenues. This is a committee amendment.

18. Technical drafting change.

19, 20, and 21. This change, known as the Long amendment, provides for the reduction of the amount on which depreciation may be taken in the case of assets eligible for the investment credit by the amount of the investment credit allowable. Where a taxpayer purchases a \$100 asset, for example, \$7 of this may be allowable as a reduction in tax in the form of a credit. In such a case, this provision limits the depreciation which may be taken with respect to this \$100 asset to \$93 instead of the \$100 presently available. If because of the limitation on the credit, this full \$7 cannot be taken as a credit in either the current year or in any of the years in which this may be carried, then the taxpayer is allowed a deduction to the extent this credit is not used in computing his income to compensate him for the depreciation deduction lost. In the fiscal year 1963 it is estimated that this will result in an increase in revenue of \$25 million and in a full year in the immediate future a revenue gain of \$95 million. If it were assumed that there were no growth in investments, however (and apart from the advantage gained by the taxpayer in recovering his cost more quickly), this provision would ultimately reduce the revenue cost of the investment credit by one-half. This is a committee amendment.

22. Clerical conforming change.

23. Conforming amendment to No. 5 above.

24. Conforming amendment to Nos. 19, 20, and 21.

25. Clerical conforming amendment.

26. Clerical conforming amendment.

27. Clerical conforming amendment.

28. Conforming amendment to Nos. 11, 12, 13, and 14 above.

IV. ENTERTAINMENT EXPENSES

29, 30, and 31. The amendment, by adding the words "or associated with" modified the House bill as reflected in the report to permit the deduction of certain expenses for goodwill.

The House report interprets the words "directly related to the active conduct of a trade or business" as limiting entertainment expenses (1) to those cases where there is more than a general expectation of deriving income at some future time; (2) to those expenses which occur under circumstances where there is at least some possibility of conducting business affairs or negotiations or discussions; (3) to those where the taxpayer or his representative is present at the entertainment activity; and (4) to those cases where the group of persons entertained is not large or the distraction is not substantial. Reference to the allowance of goodwill expenditures in the House report (except in the case of specific exceptions) is limited to goodwill expenditures in a hospitality room at a convention.

The Senate report indicates that expenses are not to be disallowed merely because they are incurred for the purpose of generating business goodwill. The Senate report indicates that no deductions for entertainment expenses would be allowed for (1) expenses attributable to the wife or family of a client or customer; (2) for expenses where there is a big backlog of orders showing entertainment is not necessary to produce income; (3) for expenses which are against public policy or public conscience; and (4) expenses which are lavish or extravagant.

The joint committee staff estimates that the Senate version will bring in \$40 million less than the House version; the Treasury Department estimates it will bring in \$65 million less. This is a committee amendment.

32. As under the House bill, the Senate disallows the deduction of gifts in excess of \$25 per recipient. It has modified the House provision, however, to provide for the exclusion from this provision of (1) items costing not over \$4 which have the taxpayer's name imprinted, and which are one of a number of identical items distributed; (2) signs, display racks, etc., to be used on business premises of recipient; and (3) tangible personal property costing not over \$100 awarded to an employee for long service or for safety achievements. This is a committee amendment.

33. In the case of a combined business and personal trip away from home, the travel cost is to be allocated to the business and personal aspect (and denied as a deduction to the extent allocated to the personal aspect) where the time away from home is for more than 1 week and the portion of the time spent for personal purposes constitutes 25 percent or more of the total time away from home. There would be a small revenue increase under this change. This is a committee amendment.

34, 35, and 36. Conforming clerical changes.

37. Permits deduction of expenses by taxpayer which are related to business meetings of agents or directors as well as employees and stockholders as provided under the House bill. This is a committee amendment.

38, 39, and 40. Conforming clerical changes.

41. In the case of expenses for meals and lodging incurred while traveling, the Senate amendment provides that to be deductible these meals or lodging must not be lavish or extravagant under the circumstances. The House version permits a reasonable allowance for amounts spent for meals and lodging. This is a committee amendment.

42. This makes the entertainment provisions effective for taxable years ending after December 31, 1962, rather than taxable years

ending after June 30, 1962, with respect to periods after the dates specified. This is a committee amendment.

V. DISTRIBUTIONS IN KIND BY FOREIGN CORPORATIONS

43. The amendment provides that the share of the foreign tax is to be credited with respect to a distribution in kind from a foreign corporation and is to be determined on the basis of the fair market value of the distribution, rather than on the basis of the adjusted basis of the property as under the House bill. This is a committee amendment.

44. Conforming clerical amendment.

VI. AMENDMENT TO SECTION 482—HOUSE BILL ONLY

45. This deletes section 6 of the House bill providing an amendment to section 482 of the code. In general, the House provision provided that where goods are purchased or sold by a domestic corporation to a related foreign corporation, the income arising from these transactions is to be allocated between the parties on the basis of the location of the assets used in the operations, the payroll attributable to them, and the related selling expenses. This rule would not apply where an arm's-length price could be established for the purchase or sales. This is a committee amendment.

VII. DISTRIBUTIONS OF FOREIGN PERSONAL HOLDING COMPANY INCOME—HOUSE BILL ONLY

46. The amendment deletes section 7 of the House bill relating to distributions of foreign personal holding company income. In general, the House provision provides that the passive income of a foreign personal holding company is to be taxed to the U.S. shareholders if 20 percent or more of its income is "foreign personal holding company income," and if 80 percent or more of its income is of this type, then the remaining income of the company also is to be taxed to the shareholders. Under present law all of the income is taxed to the shareholders in the case of such companies if 50 or 60 percent of the company's income is foreign personal holding company income. This is a committee amendment.

VIII. MUTUAL SAVINGS BANKS, ETC.

47. Conforming clerical change.

48. This puts a ceiling on the deduction which may be taken by mutual savings banks, etc. The deduction may not increase reserves for losses to an amount equal to more than 12 percent of total deposits. In general, this is the same as the ceiling under present law. The revenue increase is expected to be small. This is a committee amendment.

49. Clerical conforming change.

50. Generally, mutual savings banks and savings and loan associations may deduct, and add to their loss reserves, 60 percent of what would otherwise be their taxable income. This amendment limits the deduction which may be taken in the case of stock savings and loan associations to 50 percent of taxable income. This is expected to increase revenues by about \$10 million a year. This is a committee amendment.

51. Clerical conforming change.

52. Generally, mutual savings banks, etc., can deduct 60 percent of taxable income, or an amount which brings the reserve on losses on qualifying real property loans to 3 percent (plus a reasonable amount for the reserve for other losses). This amendment places a ceiling on the reserve for losses on qualified real property loans where the deduction taken is 60 percent of taxable income. In such a case, this deduction may not increase the balance in the reserve for losses on qualified real property loans to more than 6 percent of these loans. This will result in a very small increase in revenue. This is a committee amendment.

53. Clerical conforming change.

54. This amendment increases the 3-percent level of reserves previously referred to for which a deduction may be taken to 5 percent for the first \$4 million of loans (a maximum increase in reserves of \$80,000) during the first 10 years of mutual savings institutions' existence. The revenue loss is not significant. This is a committee amendment.

55. Clerical conforming change.

56. The House bill provided that the reserve for losses on qualified real property loans at the end of 1962 was to be established out of existing reserves attributable to years beginning after December 31, 1951 (the year these institutions became taxable), up to a level of 3 percent of qualifying loans. This amendment takes into account pre-1952 reserves to the extent necessary to obtain the 3 percent beginning reserve. No revenue estimates are available. This is a committee amendment.

57. Clerical conforming change.

58 and 59. Clerical conforming change.

60. The definition of a domestic building and loan association in the House bill in general provides that substantially all of the business of the institution must consist of accepting savings and investing the proceeds in loans secured by residential real property and other loans to the extent authorized for a Federal savings and loan association under the Home Owners' Loan Act. The definition in the Senate amendment requires that the institution be one which is federally insured or subject to State or Federal supervision, one substantially all of whose business consists of acquiring savings from the public and investing in real estate loans, and one whose assets are invested as specified below.

In general, 90 percent of the total assets of the institution must be invested in loans secured by real property (or closely associated uses). Of this 90 percent of total assets, at least 80 percent (72 percent of total assets) must be invested in residential real property or closely associated uses. Moreover, 60 percent of this 90 percent (54 percent of total assets) must be invested in residential real property containing four or fewer family units or in closely associated uses. Cash and Government obligations may also qualify under any of the percentage requirements specified above.

However, to prevent the cash or Government obligations from being used as a means of expanding nonresidential loans beyond the difference between 72 and 90 percent of total assets and to prevent the expansion of other than one- to four-family residential loans beyond the difference between the 54 and 90 percent of total assets, it is provided that not more than 18 percent of total assets may be invested in other than residential loans, cash, and Government obligations and not more than 36 percent of total assets in other than one- to four-family residential unit loans and cash and Government obligations.

It is also provided that not more than 3 percent of the assets of the association may consist of stock in any private corporation. This definition is not believed to have any significant revenue consequences. This is a committee amendment which was modified by a floor amendment made by Senator SPARKMAN.

61. The House bill repealed exemptions granted Federal savings and loan associations from excise taxes on communications and on transportation of persons. The Senate, in addition, repealed the exemptions for these savings institutions in the case of documentary stamp taxes. The revenue gain is expected to be negligible. This is a committee amendment.

62. This provides that dividends and interest paid by savings institutions which are chartered and supervised as savings and loan

under Federal or State law are to be deductible to the institution for tax purposes in the same way as interest on deposits is for commercial banks. This is to be true whether or not the savings institution meets the definition of a "domestic building and loan association." No revenue effect is anticipated. This is a committee amendment.

63. Clerical conforming change.

64. The Senate definition of a domestic savings and loan association is to be effective for taxable years after the date of enactment of the bill rather than on the date of enactment. This is a committee change.

65. The effective date for the excise tax changes is postponed from June 30, 1962, to January 1, 1963. This is a committee amendment.

VII. DISTRIBUTIONS BY FOREIGN TRUSTS

66. Clerical conforming change.

67. Clerical change.

68. Clerical change.

69. Under the House bill where there was a foreign trust to which both U.S. persons and foreign persons contributed money or property, a U.S. beneficiary receiving a distribution from such a trust would be taxable on the entire amount of accumulated income. The amendment provides that the U.S. beneficiary is to be taxable only on the portion of the distributions made to him attributable to contributions by U.S. persons. The revenue loss is believed to be negligible. This is a committee amendment.

70. Under the House bill this provision would apply to distributions made in taxable years of trusts beginning after the date of enactment of the bill. Under the Senate amendment the provision is to apply to distributions made after December 31, 1962. This is a committee amendment which was modified on the floor by a compromise worked out with Senator McCARTHY.

VIII. MUTUAL FIRE AND CASUALTY INSURANCE COMPANIES

71, 72, 73, and 74. Clerical conforming amendments.

75 and 76. Technical changes.

77, 78, 79, 80, 81, and 82. Under existing law and the House bill companies with total receipts from all sources (including premiums) not in excess of \$75,000 are exempt from tax. The Senate amendment raises this exemption level to \$150,000. This is expected to result in a revenue loss of less than a half million dollars a year. This is a committee amendment.

83. Conforming amendment.

84. Conforming to Nos. 77-82 above.

85. The House bill provided that companies with total receipts above the exemption level but not in excess of \$300,000 were to be taxed only on investment income (similar to present law except for the omission of the 1-percent alternative premiums tax). The Senate raised this \$300,000 to \$600,000, thereby taxing only companies with incomes above this level or underwriting income. This also is expected to result in a revenue loss of less than half a million dollars a year. This is a committee amendment.

86. Technical amendment.

87. This amendment provides that a mutual company experiencing underwriting losses in each of 5 out of the 6 years immediately preceding 1963 is to have a special 5-year carryover of the excess of underwriting losses over underwriting gains during the 6-year period. The term "underwriting loss" in this case is computed without any deduction for dividends to policyholders. The revenue loss under this provision is estimated to be small, in the neighborhood of \$1 or \$2 million. This is a committee amendment which was modified by a floor amendment by Senator McCarthy.

88. Clerical conforming change.

89, 90, 91, and 92. Conforming changes to No. 85 above.

93 and 94. Under the House bill a concentrated risk company is one deriving more than 50 percent of its premium income from insuring in one State against losses arising from wind, hail, floods, and so forth. The Senate provided that a company met this requirement when 40 percent of its premium income was concentrated rather than 50 percent. This will result in a small revenue loss. This is a committee amendment.

95 and 96. Under the House bill, to be eligible for a special deduction for concentrated risk 50 percent of the premium income from wind, hail, flood, etc., must be derived from one State. Under the Senate amendment for the special deduction to be available, the taxpayer could count as an alternative to concentration of premium income from one State the concentration of premium income from an area within 200 miles of any six points selected by the taxpayer. In either of such cases, to the extent the concentration exceeded 40 percent of the premium income there was to be a similar percentage increase in the proportion of underwriting income which could be set aside for up to a 5-year period in the PAL account. The Senate amendment also provides as an alternative that the taxpayer can elect to make his determination on the basis of a 400-mile radius from any six points but in this case set aside only one-half of the excess of his concentration over 40 percent in that area. There will be a revenue loss under this provision which is believed to be small. Provision for the 200-mile radius alternative is a committee amendment while provision for the 400-mile radius was an alternative worked out with Senator HICKENLOOPER.

97 and 98. Under the House bill, underwriting losses to the extent attributable to the deduction for policyholder dividends had first to be charged against the PAL account and only to the extent of any excess against investment income. Under the Senate amendment losses arising from policyholder dividends, as well as from other sources (except the PAL deduction itself) is charged first against investment income and then only to the extent of any loss still remaining against the amount in the PAL account. It has been estimated that the annual revenue loss from this amendment may build up to about \$5 million in the fifth year but most of this loss will be recaptured in later years. This is a committee amendment.

99. Conforming to Nos. 97 and 98 above.

100. The House taxes reciprocal underwriters and interinsurers under the same rules that apply to ordinary mutuals except that it permits them in effect to combine the underwriting income of the attorney-in-fact with their own for purposes of offsetting losses. The Senate amendment also permits the reciprocal to use the combined underwriting income as the basis for setting aside the deduction of 25 percent of underwriting income in the P.A.L. account. However, any additional amount set aside in this manner attributable to the attorney-in-fact may be only deferred for 5 years and not retained permanently in this account. It is expected that this will result in a negligible revenue loss. This is a committee amendment.

101. This is a conforming change to No. 100.

102. This is a conforming change to Nos. 77-82.

103. Clerical conforming change.

104. This treats mutual flood insurance companies (including reciprocal exchanges) operating on a premium deposit system in the same manner as factory mutual fire insurance companies. As a result, these flood insurance companies are to determine their underwriting income on the basis of their schedule of premium absorptions. However, the companies will also be required to in-

crease their absorbed premiums by 2 percent of the amount actually absorbed. This will result in a negligible revenue loss. This is a committee amendment.

105, 106, 107, 108, and 109. Clerical conforming changes.

IX. DOMESTIC CORPORATIONS RECEIVING DIVIDENDS FROM FOREIGN CORPORATIONS

110. Clerical conforming amendment.

111. The House bill "grosses up" dividends received from all foreign corporations. The Senate amendment provides for the same grossup in the case of dividends received from other than "less developed country corporations." A less developed country corporation has the same definition as in section 12, but here also includes certain holding companies. In general terms, a less developed country corporation is one which is engaged in the active conduct of a trade or business which derives 80 percent or more of its gross income from sources within less developed countries and which has 80 percent in value of its assets invested in a trade or business in a less developed country and certain other assets consistent with carrying on this trade or business. Certain shipping and aircraft corporations also qualify. A third category, which for purposes of this one provision also qualifies, is a foreign holding company which owns 10 percent or more of the stock in less developed country corporations, which receive 80 percent or more of their income from sources within less developed countries and have 80 percent or more of their assets invested in the same manner as other less developed country corporations. It is estimated this amendment will lose \$10 million a year. This is a committee amendment.

112, 113, 114, 115, 116, 117, 118, 119, and 120. Clerical conforming amendments.

X. SEPARATE LIMITATIONS ON FOREIGN TAX CREDIT WITH RESPECT TO CERTAIN INTEREST INCOME

121. This is a new section. It provides that the foreign tax credit limitation for certain interest income is to be computed separately from the limitation for other types of income. The interest income referred to does not include that derived from the active conduct of a trade or business, from a banking or similar business, or from a corporation in which the taxpayer has a 10-percent voting interest. No revenue estimate is available. This is a committee amendment.

XI. EARNED INCOME FROM SOURCES OUTSIDE THE UNITED STATES

122. Clerical conforming amendment.

123. This denies an exclusion to an individual as a "bona fide resident of a foreign country" if the individual (1) has earned income from sources within that foreign country; (2) has filed a statement with the authorities of that country that he is not a resident of it; and (3) has been held not to be subject to income tax as a resident of that country. This will result in a negligible revenue gain. This is a committee amendment.

124. This provides that the \$20,000 or \$35,000 ceiling on the exclusion, for a limited period of time, is not to apply to certain fringe benefits. These are noncash compensation, such as provision for a home or a car. These fringe benefits are entirely excluded from taxable income in 1963, are excluded to the extent of two-thirds in 1964, and excluded to the extent of one-third in 1965. This will result in a negligible revenue loss. This is a committee amendment.

125. In general, the House bill applied to taxable years ending after December 31, 1962, with respect to amounts received after that date for services performed after that date, or for services performed before that date. The Senate amendment applies to taxable years ending after September 4, 1962,

but only with respect to amounts received after March 12, 1962, for services performed after December 31, 1962, or received after December 31, 1962, for services after that date. The amendments relative to pensions and annuities applies to taxable years ending after December 31, 1962. This is a floor amendment offered by Senator Kerr.

XII. CONTROLLED FOREIGN CORPORATIONS

126. Both the House and Senate versions of this provision are concerned primarily with tax-haven devices. However, the versions of the bill differ considerably. The House and Senate features can be compared as follows:

1. Both versions tax to U.S. shareholders income arising from insurance of U.S. risks. However, the Senate version does not tax such income to the shareholders unless this income represents more than 5 percent of total premiums and other consideration.

2. Both versions tax passive investment income under certain conditions to the U.S. shareholders. The Senate version, however, includes in this category all rental income. It also provides that rents and royalties received from an unrelated person and derived from a trade or business are not to be included. Also excluded are dividends, interest, and gains from the sale of securities derived from a financial business or from investments made by an insurance company attributable to its insurance business. Finally, dividends and interest received from a related corporation located in the same foreign country are not included. Also, rents, royalties, and similar amounts are excluded if received for the use of property in the same country.

3. Foreign base company sales income is taxed under both versions. However, it and the investment income described above are taken into account under the House version only if representing 20 percent of gross income, and if they represent 80 percent, all income of the corporation is taxed to the U.S. shareholders. Under the Senate version, the income is taxed only if it represents 30 percent of gross income, and if it represents 70 percent or more, all of the income is taxed to the U.S. shareholders.

4. The Senate version alone taxes foreign base company service income derived from the performance of technical, managerial, engineering, etc., services for a related person outside of a country in which the controlled foreign corporation is organized. This income under the Senate version is taken into account in applying the 30-percent test referred to above.

5. Under the Senate version, tax on dividends and interest derived from a less developed country may be avoided if reinvested in a less developed country. Under the House version, the reinvestment provisions applied not only to dividends and interest but also to other forms of passive income and base company sales income. In addition, it was not necessary that they be derived from a less developed country. However, the reinvestment had to be made in a corporation in a less developed country in which the taxpayer and no more than four other Americans had an interest of more than 50 percent.

6. The Senate version does not contain the provision of the House bill which taxed to the U.S. shareholders, income not reasonably needed in the taxpayer's trade or business, nor does it include the provision that such earnings be reinvested in the same trade or business in which the taxpayer was engaged for the last 5 years, or before December 31, 1962.

7. The House version provided that U.S. shareholders were to be taxed on income from, or attributable to, patents, copyrights, formulas, and processes developed or acquired in the United States. The Senate version does not tax such income to the U.S. shareholders but in a separate section (sec.

16) provides that gains from any of these patents, copyrights, etc., are to be taxed as ordinary income in most cases at the time of the transfer of the patent or other rights from the domestic corporation to the foreign subsidiary.

8. Both versions tax in substantially the same manner to the U.S. shareholders earnings which are reinvested in the United States although not distributed to the U.S. shareholders.

9. The Senate version makes this section inoperative where the overall foreign and U.S. taxes paid with respect to the foreign operations are not substantially below what the U.S. taxes would have been on this income. This is known as the minimum distribution provision. It provides a schedule of effective foreign tax rates and corresponding percentages of distribution which, if complied with, make this section inoperative. There is no such provision in the House bill.

10. The Senate version provides that this provision is not to apply to the export-trade income of export-trade corporations. In general, this provides that where the products sold are those produced or grown in the United States and where the profit attributable to these operations complies with certain specified limitations, then this export-trade income is not to be subject to this provision if the earnings are reinvested in an export-trade business.

It is estimated that the House and Senate versions will bring in about the same amount of revenue; namely, \$50 million a year. This is a committee amendment.

XIII. GAIN FROM DISPOSITION OF CERTAIN DEPRECIABLE PROPERTY

127. Clerical conforming amendment.

128, 129, 130, 131, and 132. Conforming changes to No. 135.

133. The amendment provides that an adjustment is to be made in the computation of the 50-percent limitation applicable in the case of percentage depletion deductions. It is provided that deductions taken into account in determining the expenses of mining in computing "taxable income from the property" are to be decreased by any gain properly allocable to the mining property which under this provision is treated as ordinary income rather than capital gain. This is expected to result in an annual revenue loss of \$5 million. This is a committee amendment.

134. Clerical conforming amendment.

135. The House bill applied to property disposed of after the date of enactment of the bill and provided that the only gain which would be treated as ordinary income generally was to be depreciation occurring in 1962 and subsequent years. The Senate amendment provides that the provision is to apply to property disposed of in taxable years beginning after December 31, 1962. However, as under the House bill, depreciation occurring in 1962 and subsequent years will still result in ordinary income if the property is disposed of in a taxable year beginning after December 31, 1962. This is a committee amendment.

XIV. FOREIGN INVESTMENT COMPANIES

136 and 137. Clerical conforming amendments.

138, 139, 140, and 141. Technical amendments.

142. Clerical conforming change.

143. Technical amendment.

144. Clerical conforming amendment.

145. This amendment provides that clearance from the Internal Revenue Service under section 367 need not be obtained in the case of a foreign investment company registered with the SEC if it is a party to a reorganization in which all of its properties are acquired by a domestic regulated investment company before January 1, 1964. However, for this treatment to be available, the

corporation for the year 1963 must have elected to distribute at least 90 percent of its ordinary income and to have distributed, or treated as distributed, any excess of its net long-term capital gains over its net short-term capital losses. This is a committee amendment.

146. Clerical conforming change.

147. The Senate extended from 30 to 45 days the period of time elapsing after the end of the taxable year before the investment companies must report to the shareholders their share of the undistributed capital gains which they must take into account for tax purposes. This is a committee amendment.

148, 149, 150, 151, and 152. These are technical amendments.

153. Under present law where domestic regulated investment companies have more than 50 percent of their assets invested in foreign securities, any foreign tax credits available to the company in such a case may be passed through to the shareholders of the regulated investment company. The Senate amendment makes this same treatment available in the case of foreign investment companies which distribute most of their ordinary income currently and require their shareholders to report the company's capital gains whether or not distributed. This is a committee amendment.

154, 155, and 156. Clerical conforming amendments.

XV. GAIN FROM SALES OR EXCHANGES OF STOCK IN FOREIGN CORPORATIONS

157 and 158. Clerical conforming changes.

159. The Senate amendment, while retaining the basic structure of the House provision, made a number of important modifications:

1. Under the House version amounts received on the sale of stock, as distinguished from a redemption, were treated as ordinary income and not as dividends. This meant that the foreign tax credit would not be available in such cases. The Senate version treats the appropriate portion of the gain on a sale as a dividend.

2. Under the House version, individual shareholders were required to treat the gain as ordinary income in the year of the sale. Under the Senate version the tax of an individual shareholder (on either a redemption or sale) is to be no greater than would be provided under the lower of two ceilings. The first provides that the individual's tax is to be no greater than if the foreign corporation had been a domestic corporation paying the regular corporate tax (offset by available foreign tax credits) which then made a liquidating distribution of the balance to the U.S. shareholder and that this balance was subject to a capital gains tax. This is a tax of no more than 52 percent (less any foreign tax credits available) plus a capital gains tax on the remaining 48 percent at not more than a 25 percent rate. The aggregate tax in such a case is 64 percent (52 percent plus 25 percent of 48 percent). The second ceiling provides that the tax is not to exceed the amount which would have resulted had the earnings and profits been distributed to the shareholder in the years they were earned.

3. The Senate version also provides that earnings and profits are not to include profits on sales if the corporation could have qualified for a tax-free sale on liquidations had it been a domestic corporation.

4. The Senate provision does not apply to earnings and profits accumulated by a foreign corporation while it was a less developed country corporation if the stock sold was owned for at least 10 years before that time by the U.S. shareholder.

5. The Senate version provides that the ordinary income treatment in this section is not to apply to earnings and profits accumulated in taxable years before Janu-

ary 1, 1963. Under the House bill the ordinary income treatment could have applied to earnings and profits accumulated since February 28, 1913.

This is a committee amendment.

160. The House provision is effective for sales or exchanges occurring after the date of enactment of the bill. The Senate version applies to sales or exchanges occurring after December 31, 1962. This is a committee amendment.

XVI. SALES AND EXCHANGES OF PATENTS, ETC., TO FOREIGN CORPORATIONS

161. The House bill in section 13 (sec. 12 of the Senate amendments) would have taxed income attributable to patents, copyrights, and exclusive formulas and processes substantially developed, created, or produced in the United States or acquired from related U.S. persons as giving rise to income (whether distributed or not) which was taxable to the U.S. shareholders of controlled foreign corporations. The Senate substituted for this a new provision which treats gains from the transfers of patents, copyrights, etc., as ordinary income rather than capital gain when transferred by a U.S. person to a foreign corporation which it controls. An exception is provided for transfers for use in the subsidiary's own manufacturing business. This is a committee amendment.

XVII. TAX TREATMENT OF COOPERATIVES AND PATRONS

162. Conforming amendment to Nos. 164-168 below.

163. The House bill provided for withholding at a 20-percent rate on patronage dividends. The Senate amendments delete the withholding provision and, as indicated in section 19 below, substitute certain reporting requirements. In addition, they provide that for a cooperative to receive any deduction for noncash allocations, it must pay out at least 20 percent of the patronage dividends in cash. This applies both in the case where the patron has given his consent to receiving allocations and where he has had the option for a 90-day period to receive cash or scrip. This is a committee amendment.

164, 165, 166, 167, and 168. Under the House bill a patron gives his consent to being taxed on noncash patronage dividends either by providing this consent in writing or by being a member of the cooperative when its bylaws provided for this consent. The Senate version adds a new procedure for giving consent. This consent may be supplied by endorsing and cashing a qualified check. The check must indicate that by endorsing and cashing it, the patron is consenting to taking the remainder of the patronage dividends into account in computing his income. For the cooperative to omit a patronage dividend under this procedure from its income for the year in which the patronage occurs, the qualified check must be endorsed and cashed within 90 days after the payment period for the cooperative. This is a committee amendment.

169, 170, 171, and 172. Clerical conforming amendments.

XIX. REPORTING ON INTEREST, DIVIDENDS, AND PATRONAGE DIVIDENDS OF \$10 OR MORE A YEAR

173. The House bill provided for withholding at a rate of 20 percent with respect to most interest, dividends, and patronage dividends payments. In this system, provision was made for the use of exemption certificates for individuals expecting to have no tax liability and a system of quarterly refunds for those having a tax liability but subject to overwithholding. The Senate amendments in lieu of this provided for the submission by payors of information returns to the Government for interest, dividends, and patronage dividends of \$10 or more per

person per year. This same information must also be submitted by the payors to the recipients of interest, dividends, or patronage dividends on an annual basis. Penalties of \$10 per return on statement, but not to exceed \$25,000 per payor, for failures to file returns with the Government and \$25,000 for failures to submit statements to payees, are provided. The joint committee staff estimated that the withholding provision in the House bill would result in a revenue increase of \$550 million. The Treasury Department estimated the revenue increase to be \$780 million. The joint committee staff estimates that the reporting system will result in a revenue increase of \$275 million a year, while the Treasury Department estimates it will increase revenues by \$240 million a year. This is a committee amendment.

XX. INFORMATION WITH RESPECT TO FOREIGN CORPORATIONS

174 and 175. Clerical conforming changes.

176. With respect to the annual information return, the Senate has provided a ceiling on the penalty which may be imposed where the information is not supplied. Under present law, a failure to supply the required information results in a decrease of 10 percent in the foreign tax credit allowed a domestic corporation, plus an additional 5 percent for each 3-month period of non-compliance. The Senate amendment provides that in no event is this penalty to exceed \$10,000 or the income of the foreign corporation with respect to which the penalty occurred, whichever is the greater. This is a committee amendment.

177 and 178. Clerical conforming changes.

179. In the case of the annual information return in determining whether or not 50-percent control exists and, therefore, whether or not the information must be supplied, the Senate amendment has narrowed somewhat the constructive ownership rules applied under the House bill. Stock owned by a partner, an estate, trust, or corporation will not be treated as owned by the partnership, estate, trust, or corporation if this treats a U.S. person as owning stock owned by a person who is not actually a U.S. person. Also, a person is not to be considered as owning stock held by a corporation if his stock interest is not more than 10 percent. This is a committee amendment.

180 and 181. In the case of information required with respect to organizations, reorganizations, etc., the Senate bill provides that officers or directors who are U.S. citizens need supply information only if there are 5 percent U.S. shareholders and the information they submit is to be only the names and addresses of these shareholders. This is a committee amendment.

182. Clerical conforming change.

183. The Senate amendment provides that no information is to be required to be furnished with respect to a foreign corporation which is organized, reorganized, etc., unless that information was required under regulations in effect 90 days prior (30 days prior at the beginning of the first year) to the date on which the U.S. persons became liable to file the return with respect to the information. This is a committee amendment.

184, 185, 186, 187, and 188. Clerical conforming changes.

XXI. EXPENDITURES BY FARMERS FOR CLEARING LAND

189. This permits taxpayers engaged in the business of farming to deduct, in computing their tax, expenditures they incur in clearing land of brush and trees, in leveling the land and in diverting streams to make the land suitable for farming. This deduction may not exceed \$5,000 in any year or, if less, 25 percent of the taxpayer's income from farming. There is no comparable House provision. This is a committee amendment.

XXII. CHARITABLE CONTRIBUTIONS MADE FROM INCOME ATTRIBUTABLE TO SEVERAL TAXABLE YEARS

190. Under present law where charitable contributions are made in a year and an averaging device permits the spreading of income received in that year over several years, the charitable limitation is applied after the averaging of the income occurs. Under the Senate amendment the limitation on charitable contributions made at the election of the taxpayer is to be applied before the income is spread over the years to which it is attributable, for purposes of determining the application of the 20- or 30-percent charitable limitation. There is no comparable House provision. This is a committee amendment.

XXII. EFFECT DATE OF SECTION 1371 (C) OF THE CODE

191. This amendment provides for the years 1958 and 1959 that in determining the number of shareholders of a small business corporation for purposes of the election provided by subchapter S of the code (under which shareholders are taxed directly on their corporate earnings), spouses who hold stock of such a corporation jointly or under community property laws are to be treated as one shareholder. There is no comparable House provision. This is a committee amendment.

XXIV. LOSSES SUSTAINED IN CONVERTING FROM STREET RAILWAY TO BUS OPERATIONS

192. The Senate amendment provides that net operating losses incurred in 1953 and 1954 by a street railway company in converting from streetcar to bus service, which are not absorbed in the normal carryover period, are to be treated as a net loss occurring in 1959. This permits these losses to be carried forward to the years 1960 through 1964. There is no comparable House provision. This is a committee amendment.

XXV. PENSION PLAN OF INTERNATIONAL HOD CARRIERS' BUILDING AND COMMON LABORERS' UNION

193. The Senate amendment provides that the union-negotiated pension plan of Local Union No. 435 of the International Hod Carriers' Building and Common Laborers' Union of America is to be treated as a qualified tax-exempt trust for the period from May 1, 1960, to April 20, 1961, if the trust was not operated during this period in a manner to jeopardize the interests of its beneficiaries. This also permits employers to deduct contributions made to the trust in this period. There is no comparable House provision. This is a committee amendment.

XXVI. PARTNERSHIP YEAR OF SURVIVING PARTNER IN TWO-MAN PARTNERSHIP

194. The Senate amends the 1939 Code (years after 1946) to provide that where one partner in a two-man partnership dies, the partnership year for the surviving partner is not to close prior to the time the partnership year would have closed had neither partner died nor otherwise disposed of his interest. There is no comparable House provision. This is a committee amendment.

XXVII. EXCLUSION FROM GROSS INCOME OF AWARDS MADE PURSUANT TO EVACUATION CLAIMS OF AMERICAN-JAPANESE INDIVIDUALS

195. The Senate amendment provides that amounts received as awards made under the Japanese-American Evacuation Claims Act to persons of Japanese ancestry who were evacuated from the west coast in 1942 during World War II are not to be subject to Federal income tax. There is no comparable House provision in the bill but this provision is identical to a bill passed by the House on August 30, 1962. This is a floor amendment by Senator KUCHEL.

XXVIII. DEDUCTION FOR DEPRECIATION BY TENANT STOCKHOLDER OF COOPERATIVE HOUSING CORPORATION

196. The Senate amendment provides that a depreciation deduction is to be allowed a tenant stockholder in a cooperative housing corporation to the extent this deduction is a business deduction and is properly allocable to his proprietary lease or his right of tenancy and his stock. There is no comparable House provision. This is a floor amendment made by Senator SPARKMAN.

XXIX. EXCLUSION FROM GROSS INCOME OF GAIN FROM SALE OF RESIDENCE BY INDIVIDUALS AGE 65 OR OVER

197. The Senate amendment excludes from a taxpayer's gross income any gain realized by him from the sale or disposition of his principal residence after he or his spouse has reached the age of 65. The exemption applies only if the property has been used by the taxpayer as his principal residence for at least 5 years prior to the sale and if the sales price exceeds \$30,000 the exclusion is to be limited to the same proportion of the gain which \$30,000 is of the sales price. There is no comparable House provision. The Treasury Department has estimated that this amendment will cost \$30 million a year. This is a floor amendment made by Senator DIRKSEN.

XXX. DEDUCTION FOR INCOME TAX PURPOSES OF CONTRIBUTIONS FOR JUDICIAL REFORM

198. The Senate amendment provides that gifts made after December 31, 1961, to nonprofit organizations supporting or opposing the reorganization of the judicial branch of a State government, where referendums are occurring in 1962, are to be deductible as charitable contributions. The nonprofit organizations must be created and operated exclusively to consider such proposals and to provide information, make recommendations, and seek public support or opposition to them. In addition, no part of the earnings of the organization may inure to the benefit of any private individual and the organization must not participate in any political campaign of any candidate for public office. There is no comparable House provision but an identical bill was recently passed by the House. This is a floor amendment made by Senator DIRKSEN.

XXXI. SOCIAL SECURITY AMENDMENT RELATING TO STATEMENT OF FINANCIAL STATUS OF CLAIMANTS FOR MEDICAL ASSISTANCE FOR THE AGED

199. Under present law a State plan must include standards limiting eligibility to those aged persons who lack means to pay for medical services. This amendment would expressly permit a State to accept as presumptively correct any written statement by an applicant as to his financial status. Such a statement can be accepted without investigation if a State desires to do so under present law. There is no comparable House provision. This is a floor amendment offered by Senator DIRKSEN.

XXXII. FOREIGN SUBSIDIARIES MANUFACTURING PRODUCTS ABROAD FOR SALE IN THE UNITED STATES

200. This amendment provides that under certain conditions a foreign corporation is to be deemed to be engaged in a trade or business within the United States and its gross income from sources within the United States is to be deemed to be not less than the gross income it derives from the sale of competitive articles which are sold by it for ultimate use, consumption, or disposition in the United States. This section is to apply to a foreign corporation only if 10 percent or more of its stock is held by a domestic corporation and the foreign corporation derives 10 percent or more of its

gross income from the sale of competitive articles which are sold by it for ultimate use, consumption, or disposition in the United States.

A competitive article for purposes of this section is one which is mined, processed, or manufactured outside of the United States for a foreign corporation which is the same as or similar to presently or formerly mined, processed, or manufactured in the United States by the corporation holding 10 percent or more of the foreign corporation's stock or any subsidiary of such domestic corporation. There is no comparable House provision. It has been estimated that if corporations continue their present imports into the United States without regard to this provision, this provision might result in a revenue increase of \$50 million. This is a floor amendment offered by Senator MCCARTHY.

XXXIII. EFFECTIVE DATE OF AMENDMENT TO SECTION 1374 (b)

201. Shareholders of a small business corporation electing to be taxed under subchapter S generally may deduct their proportionate share of the corporation's net operating loss. This "passthrough" of the net operating loss, however, initially was available only with respect to shareholders who were living at the end of the corporation's taxable year. Public Law 86-376 removed this requirement that the taxpayer be living at the end of the corporation's year for this passthrough of the loss to be available. This was made effective as of October 24, 1959. The Senate amendment would make this change effective retroactively to September 2, 1958. There is no comparable House provision. This is a floor amendment offered by Senator COTTON.

XXXIV. TREATIES

202. Clerical conforming amendment.

203. The House bill provided that if any provision in this bill contravened any existing tax treaty then the new statutory law was to have precedence over the prior tax treaty. The Senate amended this to provide that no provision of this bill was to apply in any case where its application would be contrary to any treaty obligation of the United States. This is a committee amendment.

The VICE PRESIDENT. The hour of 5 o'clock having arrived, the question is on agreeing to the conference report on the tax bill, H.R. 10650.

On this vote, the yeas and nays have been ordered; and the clerk will call the roll.

The Chief Clerk called the roll.

Mr. HUMPHREY. I announce that the Senator from New Mexico [Mr. CHAVEZ], the Senator from Pennsylvania [Mr. CLARK], the Senator from Mississippi [Mr. EASTLAND], the Senator from Ohio [Mr. LAUSCHE], the Senator from Washington [Mr. MAGNUSON], and the Senator from Arkansas [Mr. McCLELLAN] are absent on official business.

I further announce that the Senator from New Mexico [Mr. ANDERSON], the Senator from Arkansas [Mr. FULBRIGHT], the Senator from Alaska [Mr. GRUENING], the Senator from Wyoming [Mr. HICKEY] are necessarily absent.

On this vote, the Senator from Alaska [Mr. GRUENING] is paired with the Senator from New Mexico [Mr. CHAVEZ]. If present and voting, the Senator from Alaska would vote "nay," and the Senator from New Mexico would vote "yea."

On this vote, the Senator from Pennsylvania [Mr. CLARK] is paired with the

Senator from Mississippi [Mr. EASTLAND]. If present and voting, the Senator from Pennsylvania would vote "nay," and the Senator from Mississippi would vote "yea."

Mr. KUCHEL. I announce that the Senators from Vermont [Mr. AIKEN and Mr. PROUTY, the Senator from Maryland [Mr. BEALL], the Senator from Utah [Mr. BENNETT], the Senator from South Dakota [Mr. BOTTRUM], the Senator from Connecticut [Mr. BUSH], the Senator from Indiana [Mr. CAPEHART], the Senator from Nebraska [Mr. HRUSKA], the Senator from Kentucky [Mr. MORTON], the Senator from Texas [Mr. TOWER], and the Senator from Massachusetts [Mr. SALTONSTALL] are necessarily absent.

If present and voting, the Senator from Vermont [Mr. AIKEN], and the Senator from Maryland [Mr. BEALL], would each vote "yea."

On this vote, the Senator from Utah [Mr. BENNETT] is paired with the Senator from Nebraska [Mr. HRUSKA]. If present and voting, the Senator from Utah would vote "yea," and the Senator from Nebraska would vote "nay."

On this vote, the Senator from South Dakota [Mr. BOTTRUM] is paired with the Senator from Connecticut [Mr. BUSH]. If present and voting, the Senator from South Dakota would vote "yea," and the Senator from Connecticut would vote "nay."

On this vote, the Senator from Indiana [Mr. CAPEHART] is paired with the Senator from Texas [Mr. TOWER]. If present and voting, the Senator from Indiana would vote "yea," and the Senator from Texas would vote "nay."

On this vote, the Senator from Kentucky [Mr. MORTON] is paired with the Senator from Massachusetts [Mr. SALTONSTALL]. If present and voting, the Senator from Kentucky would vote "yea," and the Senator from Massachusetts would vote "nay."

The result was announced—yeas 56, nays 22, as follows:

[No. 303 Leg.]
YEAS—56

Allott	Hayden	Mundt
Bible	Hill	Murphy
Butler	Holland	Muskie
Byrd, Va.	Humphrey	Pastore
Byrd, W. Va.	Jackson	Pearson
Cannon	Javits	Randolph
Carlson	Johnston	Robertson
Carroll	Jordan, N.C.	Scott
Case	Kerr	Smathers
Church	Kuchel	Smith, Mass.
Cooper	Long, Mo.	Smith, Maine
Cotton	Long, Hawaii	Sparkman
Dirksen	Long, La.	Symington
Dodd	Mansfield	Talmadge
Ellender	McCarthy	Wiley
Engle	McGee	Williams, N.J.
Ervin	Metcalfe	Young, N. Dak.
Fong	Monroney	Young, Ohio
Hartke	Moss	

NAYS—22

Bartlett	Hickenlooper	Proxmire
Boggs	Jordan, Idaho	Russell
Burdick	Keating	Stennis
Curtis	Kefauver	Thurmond
Douglas	McNamara	Williams, Del.
Goldwater	Miller	Yarborough
Gore	Morse	
Hart	Neuberger	

NOT VOTING—22

Aiken	Clark	McClellan
Anderson	Eastland	Morton
Beall	Fulbright	Pell
Bennett	Gruening	Prouty
Bottrum	Hickey	Saltonstall
Bush	Hruska	Tower
Capehart	Lausche	
Chavez	Magnuson	

So the report was agreed to.

Mr. KERR. Mr. President, I move that the vote by which the conference report was adopted be reconsidered.

Mr. HUMPHREY. Mr. President, I move to lay that motion on the table.

The VICE PRESIDENT. The question is on agreeing to the motion to lay on the table.

The motion to lay on the table was agreed to.

AUTHORIZING THE CLERK OF THE HOUSE TO MAKE A CORRECTION IN THE ENROLLMENT OF H.R. 8567

The PRESIDING OFFICER (Mr. HART in the chair) laid before the Senate, House Concurrent Resolution No. 581, which was read as follows:

Resolved by the House of Representatives (the Senate concurring), That in the enrollment of the bill (H.R. 8567) to authorize the Secretary of the Interior to create trial boards for the United States Park Police, and for other purposes, the Clerk of the House is authorized and directed to make the following correction:

In Senate amendment numbered 3, strike out "discharges" and insert in lieu thereof "charges".

Mr. MANSFIELD. Mr. President, I move that the Senate concur in the concurrent resolution. Its purpose is to correct an error in H.R. 8567.

The PRESIDING OFFICER. The question is on agreeing to the motion of the Senator from Montana.

The motion was agreed to.

THE 85TH BIRTHDAY ANNIVERSARY OF SENATOR HAYDEN, OF ARIZONA

Mr. MANSFIELD. Mr. President, it is my pleasure and privilege to call to the attention of the Senate the fact that today is the birth anniversary of a great man, the senior Senator of the United States, the President pro tempore of this body, a man whom, regardless of our political affiliations, we respect, admire, and love.

On this occasion I want to extend, on my behalf—and I hope all other Senators will join me—my felicitations and congratulations to the senior Senator from Arizona on his birth anniversary.

[Prolonged applause, Senators rising.]

Mr. HAYDEN. Mr. President, what the majority leader says makes me very happy to be 85 years young.

ORDER FOR ADJOURNMENT TO 10 A.M. TOMORROW

Mr. MANSFIELD. Mr. President, I ask unanimous consent that when the Senate adjourns tonight it adjourn to meet at 10 o'clock tomorrow morning.

The VICE PRESIDENT. Without objection, it is so ordered.

LEGISLATIVE PROGRAM

Mr. MANSFIELD obtained the floor. Mr. DIRKSEN. Mr. President, will the Senator yield?

Mr. MANSFIELD. I yield.

Mr. DIRKSEN. I wish to ask the majority leader about the schedule for the remainder of the day.

Mr. MANSFIELD. In response to the question raised by the distinguished minority leader—whom we are all glad to see back in the Chamber and in such obviously good health—

Mr. DIRKSEN. I thank the Senator. [Applause.]

Mr. MANSFIELD. There will be no further business tonight except for a couple of bills which seem to be without opposition and which have cleared both sides.

Mr. President, it is the intention, at the conclusion of the morning hour tomorrow, to take up Calendar No. 2176, H.R. 8140, a bill to strengthen the criminal laws relating to bribery, graft, and conflict of interest, and for other purposes.

It is my understanding that the Senator from New York [Mr. KEATING] has several amendments, and that he is agreeable to a time limitation of very short duration on those amendments.

Then it is contemplated that the Senate will take up the State, Justice, and Commerce appropriation bill; the conference report on the drug bill; possibly the conference report on the trade bill, in the event the House has acted, possibly tomorrow, more likely on Thursday; the conference report on H.R. 7283, the war claims bill, in the event the House has acted Wednesday or Thursday.

For the remainder of the week, on Thursday and possibly Friday, there will be the supplemental appropriation bill; the conference report on the District of Columbia Appropriation bill; the conference report on the State, Justice, Commerce, Judiciary appropriation bill; the conference report on the Agriculture Department appropriation bill; the conference report on the public works appropriation bill; the conference report on the foreign-aid appropriation bill; the conference report on the supplemental appropriation bill; and other odds and ends as they come in.

Mr. MORSE. Mr. President, will the Senator yield?

Mr. MANSFIELD. I yield.

Mr. MORSE. Speaking about odds and ends, does the Senator have any recommendation to make to me as to the bill to which I should attach the Senate "prohibition" bill?

Mr. MANSFIELD. I would say any bill.

OATH OF APPLICANT FOR PATENT

Mr. MANSFIELD. Mr. President, I ask unanimous consent that the Senate

proceed to the consideration of Calendar No. 2132, S. 2639.

The VICE PRESIDENT. The bill will be stated by title for the information of the Senate.

The LEGISLATIVE CLERK. A bill (S. 2639) to amend the provisions of title 35 of the United States Code relating to the oath of applicant for patent, and the provisions of the Trademark Act of July 5, 1946, relating to verification by the applicant of application for trademark registration, and for other purposes.

The VICE PRESIDENT. Is there objection to the request of the Senator from Montana?

There being no objection, the Senate proceeded to consider the bill, which had been reported from the Committee on the Judiciary, with an amendment to strike out all after the enacting clause and insert:

That title 35, United States Code, is amended by adding the following new sections after section 24:

"§ 25. Declaration in lieu of oath

"(a) The Commissioner may by rule prescribe that any document to be filed in the Patent Office and which is required by any law, rule, or other regulation to be under oath may be subscribed to by a written declaration in such form as the Commissioner may prescribe, such declaration to be in lieu of the oath otherwise required.

"(b) Whenever such written declaration is used, the document must contain a warning that willful false statements and the like are punishable by fine or imprisonment, or both, under section 1001, title 18, United States Code.

"§ 26. Effect of defective execution

"Any document to be filed in the Patent Office and which is required by any law, rule, or other regulation to be executed in a specified manner may be provisionally accepted by the Commissioner despite a defective execution, provided a properly executed document is submitted within such time as may be prescribed."

SEC. 2. The analysis of chapter 2 of title 35, United States Code, immediately preceding section 21, is amended to read as follows:

- "Sec.
 "21. Day for taking action falling on Saturday, Sunday, or holiday.
 "22. Printing of papers filed.
 "23. Testimony in Patent Office cases.
 "24. Subpenas, witnesses.
 "25. Declaration in lieu of oath.
 "26. Effect of defective execution."

The VICE PRESIDENT. The question is on agreeing to the committee amendment.

The amendment was agreed to.

The bill (S. 2639) was ordered to be engrossed for a third reading, read the third time, and passed.

The title was amended, so as to read: "A bill to amend title 35 of the United States Code to permit a written declaration to be accepted in lieu of an oath, and for other purposes."

PUBLIC NOTICE OF SETTLEMENTS IN PATENT INTERFERENCES

Mr. MANSFIELD. Mr. President, I move that the Senate proceed to the consideration of calendar No. 2133, H.R. 12513.

The VICE PRESIDENT. The bill will be stated by title for the information of the Senate.

The LEGISLATIVE CLERK. A bill (H.R. 12513) to provide for public notice of settlements in patent interferences, and for other purposes.

The VICE PRESIDENT. The question is on agreeing to the motion of the Senator from Montana.

The motion was agreed to; and the Senate proceeded to consider the bill, which had been reported from the Committee on the Judiciary, with an amendment, to strike out all after the enacting clause and insert:

That section 135 of title 35, United States Code, is amended by designating the first and second paragraphs thereof as subsections (a) and (b), respectively, and by adding thereto the following subsection:

"(c) Any agreement or understanding between parties to an interference, including any collateral agreements referred to therein, made in connection with or in contemplation of the termination of the interference, shall be in writing and a true copy thereof filed in the Patent Office before the termination of the interference as between the said parties to the agreement or understanding. If any party filing the same so requests, the copy shall be kept separate from the file of the interference, and made available only to Government agencies on written request, or to any person on a showing of good cause. Failure to file the copy of such agreement or understanding shall render permanently unenforceable such agreement or understanding and any patent of such parties involved in the interference or any patent subsequently issued on any application of such parties so involved. The Commissioner may, however, on a showing of good cause for failure to file within the time prescribed, permit the filing of the agreement or understanding during the six-month period subsequent to the termination of the interference as between the parties to the agreement or understanding.

"The Commissioner shall give notice to the parties or their attorneys of record, a reasonable time prior to said termination, of the filing requirement of this section. If the Commissioner gives such notice at a later time, irrespective of the right to file such agreement or understanding within the six-month period on a showing of good cause, the parties may file such agreement or understanding within sixty days of the receipt of such notice.

"Any discretionary action of the Commissioner under this subsection shall be reviewable under section 10 of the Administrative Procedure Act."

The VICE PRESIDENT. The question is on agreeing to the committee amendment.

The amendment was agreed to.

The amendment was ordered to be engrossed and the bill to be read a third time.

The bill (H.R. 12513) was read the third time and passed.

EXTENSION OF REGULATORY AUTHORITY UNDER CONVENTION FOR ESTABLISHMENT OF INTER-AMERICAN TROPICAL TUNA COMMISSION

Mr. BARTLETT. Mr. President, I ask the Presiding Officer to lay before the Senate the amendments of the House of

Representatives to the bill, S. 2568, to amend the act of September 7, 1950, to extend the regulatory authority of the Federal and State agencies concerned under the terms of the Convention for the Establishment of an Inter-American Tropical Tuna Commission, signed at Washington May 31, 1949, and for other purposes.

The VICE PRESIDENT laid before the Senate the amendments of the House of Representatives to the bill from the Senate (S. 2568) entitled to amend the act of September 7, 1950, to extend the regulatory authority of the Federal and State agencies concerned under the terms of the Convention for the Establishment of an Inter-American Tropical Tuna Commission, signed at Washington May 31, 1949, and for other purposes, which were, on page 1, strike out lines 7 and 8, and insert:

(e) "United States" shall include all areas under the sovereignty of the United States, the Trust Territory of the Pacific Islands, and the Canal Zone.

On page 5, line 4, strike out "any" and insert "such", and on page 5, strike out lines 7 through 13, inclusive, and insert "The aforesaid prohibitions shall continue until the Secretary of the Interior is satisfied that the condition warranting the prohibition no longer exists, except that all fish in any form of the species under regulation which were previously prohibited from entry shall continue to be prohibited from entry."

Mr. BARTLETT. Mr. President, the House amendments were suggested by the Department of State and are of a technical and clarifying nature. They do not alter the substance of the bill. They were worked out after consultation with the American tuna industry, which has a deep interest in this subject.

I move that the Senate concur in the House amendments to S. 2568.

The VICE PRESIDENT. The question is on agreeing to the motion of the Senator from Alaska.

The motion was agreed to.

Mr. BARTLETT. Mr. President, I move that the vote by which the Senate concurred in the House amendments to S. 2568 be reconsidered.

Mr. McCARTHY. Mr. President, I move to lay that motion on the table.

The VICE PRESIDENT. The question is on agreeing to the motion to lay on the table the motion to reconsider.

The motion to lay on the table was agreed to.

AMENDMENT OF COMMUNICATIONS ACT OF 1934

Mr. MANSFIELD. Mr. President, I move that the Senate proceed to the consideration of Calendar No. 2187, H.R. 11732.

The VICE PRESIDENT. The bill will be stated by title for the information of the Senate.

The LEGISLATIVE CLERK. A bill (H.R. 11732) to amend section 305 of the Communications Act of 1934, as amended.

The VICE PRESIDENT. The question is on agreeing to the motion by the Senator from Montana.

The Clerk read as follows:

Amendment offered by Mr. LANE: Add the following sections at the end of the bill:

"SEC. 2. The Secretary of the Treasury is authorized and directed to pay, out of any money in the Treasury not otherwise appropriated, to Lieutenant Claude V. Wells an amount equal to the aggregate of the amounts paid by him, or withheld from sums otherwise due him, in complete or partial satisfaction of the liability to the United States specified in the first section.

"SEC. 3. No part of the amount appropriated in this Act shall be paid or delivered to or received by any agent or attorney on account of services rendered in connection with this claim, and the same shall be unlawful, any contract to the contrary notwithstanding. Any person violating the provisions of this Act shall be deemed guilty of a misdemeanor and upon conviction thereof shall be fined in any sum not exceeding \$1,000."

The amendment was agreed to.

The bill was ordered to be engrossed and read a third time, was read the third time, and passed, and a motion to reconsider was laid on the table.

DR. OLGA MARIE FERRER

The Clerk called the bill (H.R. 12886) for the relief of Dr. Olga Marie Ferrer.

There being no objection, the Clerk read the bill, as follows:

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That for the purposes of title III of the Immigration and Nationality Act, Doctor Olga Marie Ferrer (A12539965) shall be held and considered to have been admitted to the United States for permanent residence on May 17, 1947, and to have complied with the residential and physical presence requirements of section 316 of the said Act.

The bill was ordered to be engrossed and read a third time, was read the third time, and passed, and a motion to reconsider was laid on the table.

CHAO HUA-HSIN

The clerk called the bill (S. 3600) for the relief of Chao Hua-Hsin. There being no objection, the clerk read the bill, as follows:

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That, for the purposes of sections 101(a) (27) (A) and 205 of the Immigration and Nationality Act, the minor child, Chao Hua-Hsin, shall be held and considered to be the natural-born alien child of Arthur E. Link, a citizen of the United States: *Provided,* That the natural parents of the said Chao Hua-Hsin shall not, by virtue of such parentage, be accorded any right, privilege, or status under the Immigration and Nationality Act.

The bill was ordered to be read a third time, was read the third time, and passed, and a motion to reconsider was laid on the table.

JANE FROMAN, GYPSY MARKOFF, AND JEAN ROSEN

Mr. MULTER. Mr. Speaker, I ask unanimous consent to return to Calendar No. 770, H.R. 12313, for the relief of Jane Froman, Gypsy Markoff, and Jean Rosen, and ask for its immediate consideration.

The clerk read the title of the bill. The SPEAKER pro tempore. Is there objection to the request of the gentleman from New York?

There being no objection, the clerk read the bill, as follows:

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That the Secretary of the Treasury is authorized and directed to pay, out of any money in the Treasury not otherwise appropriated, (1) to Jane Froman, the sum of \$217,263.56, (2) to Gypsy Markoff, the sum of \$142,230.42, and (3) to Jean Rosen, the sum of \$149,175.46. The payment of such sums shall be in full satisfaction of the respective claims of the said Jane Froman, Gypsy Markoff, and Jean Rosen arising out of an accident which occurred on or about February 22, 1943, when the Pan American Airways seaplane Yankee Clipper, on which they were traveling to entertain members of the Armed Forces of the United States, crashed in the Tagus River in the Port of Lisbon, Portugal: *Provided,* That no part of the amounts appropriated in this Act in excess of 10 per centum thereof shall be paid or delivered to, or received by, any agent or attorney on account of services rendered in connection with the claims referred to herein, and the same shall be unlawful, any contract to the contrary notwithstanding.

With the following committee amendment:

Page 1 strike all after the enacting clause and insert the following: "That the Secretary of the Treasury is authorized and directed to pay, out of any money in the Treasury not otherwise appropriated, (1) to Jane Froman, the sum of \$20,000.00, (2) to Gypsy Markoff, the sum of \$20,000.00, and (3) to Jean Rosen, the sum of \$20,000.00, in accordance with the recommendations of the United States Court of Claims in its opinion in congressional reference case numbered 20-58, Jane Froman, Gypsy Markoff and Jean Rosen against The United States, decided June 6, 1962. The amounts paid under the authority of this Act shall be in full and final settlement of the respective claims of the said Jane Froman, Gypsy Markoff, and Jean Rosen against the United States arising out of an accident which occurred on or about February 22, 1943, when the Pan American Airways seaplane Yankee Clipper, on which they were traveling as entertainers engaged by Camp Shows, Incorporated, to provide entertainment to members of the Armed Forces of the United States, crashed in the Tagus River in the Port of Lisbon, Portugal: *Provided,* That no part of the amount appropriated in this Act in excess of 10 per centum thereof shall be paid or delivered to or received by any agent or attorney on account of services rendered in connection with this claim, and the same shall be unlawful, any contract to the contrary notwithstanding. Any person violating the provisions of this Act shall be deemed guilty of a misdemeanor and upon conviction thereof shall be fined in any sum not exceeding \$1,000."

The amendment was agreed to.

The bill was ordered to be engrossed and read a third time, was read the third time, and passed, and a motion to reconsider was laid on the table.

The SPEAKER pro tempore. This concludes the call of the Private Calendar.

CALL OF THE HOUSE

Mr. CURTIS of Missouri. Mr. Speaker, I make the point of order that a quorum is not present.

The SPEAKER pro tempore (Mr. ALBERT). Evidently a quorum is not present.

Mr. MILLS. Mr. Speaker, I move a call of the House.

A call of the House was ordered.

The Clerk called the roll, and the following Members failed to answer to their names:

[Roll No. 262]

Alexander	Hébert	Rogers, Tex.
Anfuso	Hiestand	Rousselot
Arends	Hoffman, Mich.	Santangelo
Aspinall	Hull	Saund
Barrett, Pa.	Jarman	Saylor
Bass, N.H.	Karth	Schadeberg
Bates	Kearns	Scherer
Belcher	Kee	Scott
Bennett, Mich.	Kjburn	Scranton
Berry	Kirwan	Seely-Brown
Blich	Kowalski	Selden
Bolling	Laird	Shelley
Boykin	Latta	Sheppard
Breeding	McDonough	Shipley
Brown	McDowell	Short
Buckley	McIntire	Sibal
Burke, Ky.	McSween	Siler
Celler	McVey	Smith, Miss.
Chamberlain	MacGregor	Springer
Curtin	Magnuson	Thompson, La.
Diggs	Martin, Nebr.	Tollefson
Dominick	Mason	Ullman
Dooley	Morrow	Utt
Evins	Michel	Van Pelt
Frazier	Miller,	Vinson
Garland	George P.	Watts
Goodell	Moorehead,	Weis
Gray	Ohio	Whalley
Hall	Moulder	Wickersham
Halleck	O'Brien, Ill.	Willis
Hansen	Powell	Winstead
Harris	Rains	Yates
Harrison, Va.	Reifel	Zelenko
Harvey, Ind.	Riley	

The SPEAKER pro tempore (Mr. ALBERT). On this rollcall, 337 Members have answered to their names, a quorum.

By unanimous consent, further proceedings under the call were dispensed with.

HON. CLARE E. HOFFMAN

(Mr. MEADER asked and was given permission to address the House for 1 minute and to revise and extend his remarks and to include a resolution.)

Mr. MEADER. Mr. Speaker, I believe Members will be interested in knowing that today the chairman of the Committee on Government Operations, the gentleman from Illinois, Hon. WILLIAM L. DAWSON, is sending to the ranking minority member of the committee, our colleague, the gentleman from Michigan, Hon. CLARE E. HOFFMAN, a letter enclosing a copy of a resolution adopted by the House Committee on Government Operations on September 19, 1962. That resolution was adopted unanimously on that date and subsequently was signed by all 19 majority members and all 10 minority members of the committee.

I will include a copy of the letter of the gentleman from Illinois and the entire text of the resolution in my remarks, but I just want to read the resolving clause of the resolution which is as follows:

Resolved, That the Committee on Government Operations of the House of Representatives of the United States express its gratitude and appreciation for the distinguished service of the Honorable CLARE E. HOFFMAN, and extend its best wishes for many happy years of well-earned retirement.

The letter and the text of the resolution are as follows:

OCTOBER 1, 1962.

HON. CLARE E. HOFFMAN,
House of Representatives,
Washington, D.C.

DEAR COLLEAGUE: On behalf of the membership of the Committee on Government Operations, I am happy to enclose herewith a resolution adopted by the full committee at its meeting on Wednesday, September 19, 1962.

You have my personal wishes for good health and happiness in your retirement.

Sincerely,

WILLIAM L. DAWSON,
Chairman.

RESOLUTION OF THE GOVERNMENT OPERATIONS COMMITTEE

Whereas the Honorable CLARE E. HOFFMAN, having represented the Fourth Congressional District of Michigan in the U.S. House of Representatives since 1935, has announced his decision to retire at the end of the 87th Congress; and

Whereas Representative HOFFMAN served as chairman of the Committee on Government Operations of the House of Representatives in the 80th and 83d Congresses, and as ranking minority member in the 81st, 82d, 84th, 85th, 86th, and 87th Congresses; and

Whereas Representative HOFFMAN's leadership, determination, diligence, and devotion to his principles have contributed substantially to the record of performance of the committee: Now, therefore, be it

Resolved, That the Committee on Government Operations of the House of Representatives of the United States express its gratitude and appreciation for the distinguished service of the Honorable CLARE E. HOFFMAN, and extend its best wishes for many happy years of well-earned retirement.

WILLIAM L. DAWSON, of Illinois, Chairman; CHET HOLIFIELD, of California; JACK BROOKS, of Texas; L. H. FOUNTAIN, of North Carolina; PORTER HARDY, Jr., of Virginia; JOHN A. BLATNIK, of Minnesota; ROBERT E. JONES, of Alabama; EDWARD A. GARMATZ, of Maryland; JOHN E. MOSS, of California; JOE M. KILGORE, of Texas; DANTE B. FASCELL, of Florida; HENRY S. REUSS, of Wisconsin; ELIZABETH KEE, of West Virginia; KATHRYN E. GRANAHAN, of Pennsylvania; JOHN S. MONAGAN, of Connecticut; NEAL SMITH, of Iowa; RICHARD E. LANKFORD, of Maryland; ROSS BASS, of Tennessee; LUCIEN N. NEDZI, of Michigan; R. WALTER RIEHLMAN, of New York; GEORGE MEADER, of Michigan; CLARENCE J. BROWN, of Ohio; FLORENCE P. DWYER, of New Jersey; ROBERT P. GRIFFIN, of Michigan; GEORGE M. WALLHAUSER, of New Jersey; ODIN LANGEN, of Minnesota; JOHN B. ANDERSON, of Illinois; RICHARD S. SCHWEIKER, of Pennsylvania; F. BRADFORD MORSE, of Massachusetts.

SEPTEMBER 19, 1962.

REVENUE ACT OF 1962

Mr. MILLS. Mr. Speaker, I call up the conference report on the bill (H.R. 10650) to amend the Internal Revenue Code of 1954 to provide a credit for investment in certain depreciable property, to eliminate certain defects and inequities, and for other purposes, and ask unanimous consent that the statement of the managers on the part of the House be read in lieu of the report.

The Clerk read the title of the bill.

The SPEAKER pro tempore. Is there objection to the request of the gentleman from Arkansas?

There was no objection.

The Clerk read the statement.

Mr. MILLS (during the reading of the statement). Mr. Speaker, I ask unanimous consent to dispense with the further reading of the statement.

The SPEAKER pro tempore. Without objection, it is so ordered.

There was no objection.

(For conference report and statement, see proceedings of the House of October 1, 1962.)

The SPEAKER pro tempore. The Chair recognizes the gentleman from Arkansas [Mr. MILLS].

Mr. MILLS. Mr. Speaker I yield myself 10 minutes.

Mr. Speaker, you will recall the House passed H.R. 10650 in March of this session of the Congress after several weeks of consideration in the Ways and Means Committee. The bill was sent over to the Senate. In the Finance Committee and on the floor of the Senate there were 203 amendments adopted.

When your conferees on the part of the House met with the conferees on the part of the Senate many of us had the impression that perhaps in the process of amending H.R. 10650 to this extent, the Senate had actually performed a major operation. That is not the case, Mr. Speaker; the majority of the 203 amendments which were adopted by the other body are technical, clarifying, or conforming, and were not amendments of substance. I do not mean however, Mr. Speaker, to minimize the fact that the other body made a number of rather substantial changes in H.R. 10650 while that body was considering the bill, but many of these 203 amendments could be accepted by the conferees on the part of the House with the full recommendation of the Treasury Department and the advice of the technicians of the Department as well as the technicians working with the Ways and Means Committee. In many instances—and we on this side prefer not to make this admission—somewhere along the line somebody came up with language that carried out the objectives which the House sought better than did the language in the House bill itself. Of course, they had the advantage of all our preliminary work we feel.

One of the fundamental changes with respect to this bill in the Senate was with respect to the investment credit.

The investment credit had been worked out in the Ways and Means Committee. As passed by the Senate there were only two really major points that were in disagreement and in conference: First, the Senate had changed the effective date of this provision from January 1 of this year, as provided in the House bill, to July 1 of this year; and, second, the Senate saw fit to adopt an amendment which reduced the basis of an asset for purposes of depreciation by the amount of the investment credit. If the taxpayer received 7 percent of the cost of this asset as an investment credit then the basis for depreciation is, under the conference report, reduced from 100 cents to 93 cents, for each dollar of cost.

Actually, Mr. Speaker, that was a rather basic change in the investment credit provision, but it was accepted by

the House conferees among other things for the reason that it will reduce the revenue loss otherwise resulting from the investment credit over a 10-year period by some 4½ or 5 billion dollars, and it will, I must say—and I think my friend from Wisconsin would not mind my saying this, provides for the very result that he had urged when the matter was in the Ways and Means Committee.

In other words, as amended by the other body, the investment credit served to reduce the amount of the basis of the asset for depreciation purposes and therefore did not provide a tax benefit in addition to depreciation. What this does is not to this exact percentage but almost to it. In combination it is less effective as an incentive under the conference agreement as the House provision would have made it. In other words the 7-percent investment credit is worth about 14 percent for depreciation purposes at the full corporate rate. Adding this to the 7-percent reduction in the depreciation basis under the conference agreement you reach a total of 107 cents in equivalent depreciation to the taxpayer for each dollar of investment as a result of this investment credit. Under the House bill he would have obtained \$1.14 of depreciation for each dollar of his investment.

So you see there is a reduction of approximately 50 percent in the tax benefit over this period of time of his investment credit.

Actually this often used comparison of the credit with depreciation ignores the fact that the credit is available when the investment is made and the adjustment in the depreciation basis will result in lower deductions only in future years. When this is taken into account it is fair to say that as modified the investment credit is about 70 percent as effective as an incentive as it was under the House bill.

Mr. CURTIS of Missouri. Mr. Speaker, will the gentleman yield for an inquiry?

Mr. MILLS. I yield to the gentleman from Missouri.

Mr. CURTIS of Missouri. The reason this works out to about 7 is because of the 52-percent corporate tax?

Mr. MILLS. Yes.

Mr. CURTIS of Missouri. I want to make this point: For your smaller concerns, if you have 30 percent, it would mean more?

Mr. MILLS. It would mean more. I was taking the 52-percent rate.

The Senate receded from its amendment which provided for this program to go into effect as outlined in the House bill on January 1 of this year rather than on July 1 as provided by the Senate.

It will be recalled that the investment credit and withholding of the tax on interest and dividends were the subject matter of a motion to recommit the bill when it was passed by the House, therefore I will turn now to the change made by the Senate with respect to the collection of the tax due on interest and dividends. It will be recalled that under the provisions of existing law, it is necessary for an institution paying dividends

to report annually, to the Internal Revenue Service, the name of each recipient of a dividend of \$10 or more. The Senate decided in its wisdom, after having had two votes on the question of withholding—I think 20 voted for the proposition on one occasion and maybe less on the other occasion—to strike out the House passed provision for withholding and to substitute a reporting system that was worked out in conjunction with the staff of the Joint Committee on Internal Revenue taxation, as well as the staff of the Treasury Department.

Therefore, the withholding provision that some Members of the House found objectionable in March is out of the bill as we bring it back to the House from the conference. In lieu of it is this provision that has been developed and which calls for a reporting system.

The SPEAKER *pro tempore*. The time of the gentleman from Arkansas has expired.

Mr. MILLS. Mr. Speaker, I yield myself 5 additional minutes.

Mr. Speaker, this reporting system in my opinion may develop to be more onerous upon the institutions that are paying interest and dividends than would the withholding system have been. Let us take an example of a savings and loan association in your district which pays to 1,000 depositors \$10 in interest or more each year. It is necessary for that institution to prepare a slip of paper with the taxpayer's name, the taxpayer's address, the taxpayer's tax number, which we passed under legislation earlier in this Congress, with the amount of interest actually disbursed to him, and transmit that to the Internal Revenue Service.

Then it must give the recipient another piece of paper which will indicate to that individual that the institution has reported to the Internal Revenue Service the fact that it has paid to that individual whatever this amount of interest is.

Mr. Speaker, it was thought in the conference that it would be desirable to try this system, because everyone in the conference was, I think, in agreement that every effort should be made to assist the Internal Revenue Service to collect the taxes due and owing from all people alike on the basis of the provisions of existing law.

Mr. BYRNES of Wisconsin. Mr. Speaker, will the gentleman yield?

Mr. MILLS. I would be glad to yield to the gentleman from Wisconsin.

Mr. BYRNES of Wisconsin. The gentleman has said that this reporting system may prove to be more onerous than the withholding system. However, I would call to the attention of the gentleman the fact that the withholding system that passed this House, and practically any withholding system that had been suggested other than the original one of the administration, required some reporting.

Mr. MILLS. The House bill did not require the reporting involved in the Senate amendment. The House bill did require some handling of exemption certificates. I was coming to the point of

saying that even though it was my own private opinion that the reporting system might turn out to be more onerous, some of the institutions which are charged with the responsibility under this provision of being reporting agents to the Internal Revenue Service, apparently feel, based upon what they tell me, that this will be more workable from their point of view and that it is far more acceptable to them than the provision for withholding. They also state that they question it will be more onerous to them.

Mr. BYRNES of Wisconsin. If the gentleman will yield further, the main point I wanted to make was—and I think the gentleman will agree—that under the bill as it passed the House the withholding would also have involved reporting.

Mr. MILLS. The required information under the House bill would not have been voluminous.

It may turn out that this reporting system will do the job. It was our thought when we were in the Ways and Means Committee and considered this entire matter, that the only really sound way to collect the amount of money that is not being collected now from interest and dividends was through a system of withholding. We explored this. But we have been here long enough to know that it is not always the will of the House that prevails. Sometimes compromises have to be worked out. We took this reporting provision with an addition to it requiring the Treasury to report back at the end of each year, providing us with information as to the effectiveness of the system of reporting.

Mr. Speaker, this provision, it is anticipated, will bring in additional money. I doubt that anyone can assure us with any degree of certainty that it will bring in \$300 million, \$100 million, \$200 million, or any other fixed amount. It is estimated by the staff of the Joint Committee on Internal Revenue Taxation that whereas \$550 million, they say, would have been collected under withholding, this system will collect around \$275 million.

It is said by the Treasury that it probably will enable a collection of around \$240 or \$250 million. The Treasury at the same time said that the method of withholding that we had, based upon more recent data than they had when the matter was before the House would produce \$780 million of revenue.

There is a large difference, Mr. Speaker, in the revenue effect of the conference report compared to the House bill. That revenue effect is not with respect to this fiscal year; it is not with respect to the past fiscal year; because the situation is approximately the same in that respect between the conference report and the House bill. The difference, if any, Mr. Speaker, would develop in the course of the first full year of the operation of this conference report compared to the House bill.

The major difference in revenue effect is the amount that will be developed on the plus side through reporting compared to the amount that would be de-

veloped on the plus side through withholding.

The staff of the joint committee says that this bill, contrary to the bill as it passed the House, will create a deficit in a full year of operation of \$550 million. The same group said that the bill as it passed the House would create a deficit in the first full year of \$285 million. The Treasury people on the other hand said that in a full year of operation as the bill passed the House there was a revenue gain in the bill of \$325 million. They say that as a result of the action taken in the conference, in the same full year, that revenue gain of \$325 million has been changed to a loss of \$170 million on a gross basis. On a net basis there is a gain of \$10 million. So, Mr. Speaker, I say that on this question of the revenue effect of the conference report in a full year of operation, it is not certain as between the two staffs.

The membership may take, if they desire, the figures of the staff of the joint committee or they may take the figures of the Treasury Department. I think, frankly, that it is probably correct that the revenue effect of this will be somewhere in between the two estimates of these two staffs.

Mr. Speaker, there are many other provisions of the bill that I hope others will take time to discuss. I want to yield to the gentleman from Wisconsin when I conclude my remarks. I hope that he will take up other provisions. I would call attention to the fact that this conference report was signed by all of the conferees on the part of the House with the exception of the gentleman from Illinois [Mr. MASON]. All of the conferees on the part of the Senate signed the conference report.

I suggest, Mr. Speaker, that this is about the best job that your conferees on the part of the House could do.

Mr. BAILEY. Mr. Speaker, will the gentleman yield?

Mr. MILLS. I yield.

Mr. BAILEY. I would like to ask the distinguished chairman of the committee if the Members of the House are to understand that the withholding tax as such is not a part of the bill.

Mr. MILLS. It is not a part of the bill. I must suggest to those who voted for the bill as it passed the House that the primary difference is the difference between withholding and reporting.

If a Member who voted for this bill to pass last March now should vote against the conference report, I am not saying that it would be, but it could be interpreted by someone to mean that that Member was casting that vote because he did not want the tax bill to go through without the withholding provision in it. I say that could be an interpretation placed upon it, and I wanted to advise my friends of that possibility.

Mr. SMITH of Virginia. Mr. Speaker, will the gentleman yield?

Mr. MILLS. I yield.

Mr. SMITH of Virginia. I should like to ask this question: As the result of all this hard work done by the Senate and the House and the committee of

conference, is the net result a loss to the Treasury or is it a gain to the Treasury? I understand that your own estimate is that it will be a loss of some probably \$200 million. The joint staff of the House and Senate estimates that it will be some \$300 million.

Mr. MILLS. Actually, as I pointed out it depends upon whose estimate you take. We have the Treasury estimate, which I shall include as part of my remarks along with a further explanation of other provisions of the bill. Then we have the estimates of the staff of the joint committee. As I pointed out, as far as this present fiscal year we are in is concerned, I doubt there is any significant difference in revenue effect in this fiscal year between the House-passed bill and the conference report. There are significant differences in the estimates of revenue loss in a full year of operation, when all these provisions are in effect.

My own guess is, and it is only a guess, that these estimates at that time, perhaps one high, one low, would lead us to the conclusion that there might be some loss in that year somewhere in between these two estimates. The Treasury says there would be a gain of \$10 million on a net basis. The joint staff says there would be a loss of some \$550 million on a gross basis. My own thought is that the figure would be somewhere in between.

Mr. SMITH of Virginia. Would the gentleman say that the Treasury then instead of gaining by this bill would lose perhaps \$250 million a year?

Mr. MILLS. Somewhere in between these two figures would be my best guess. That would depend entirely on how well this investment credit works. If it does what the experts and the Treasury say it is going to do, if it creates additional impetus for investment and brings about modernization of facilities within plants that are going to be competing, that is desired and that is thought will be the case, then in all probability there would be more money developed under the income tax from corporations and other business operations. So that I am not certain as to what the revenue implication would be 2 or 3 years in advance. But as far as the present is concerned, there is not, in my opinion, any difference in effect.

Mr. COLLIER. Mr. Speaker, will the gentleman yield?

Mr. MILLS. I yield to the gentleman from Illinois.

Mr. COLLIER. I wonder if the distinguished chairman of the committee can tell us if there is any estimate of the number of accountants that would be needed in the various financial institutions where the duplicate reports to the savers and the Internal Revenue Bureau are involved?

Mr. MILLS. There would not be any duplicate reporting except where a depositor in one institution might have a deposit in half a dozen other institutions. Those would not be basic duplications. They would be duplicates of a report with respect to the same individual, but upon different accounts.

Mr. COLLIER. How many savings accounts are involved?

Mr. MILLS. I am uncertain as to how many savings accounts are involved. Does the gentleman from Wisconsin have the figures?

Mr. BYRNES of Wisconsin. My understanding, may I say to my chairman, is that with the \$10 limitation there are about 350 million accounts.

Mr. MILLS. That may be correct.

Mr. BYRNES of Wisconsin. And as to all accounts, there are about 500 million.

Mr. COLLIER. What would be involved in personnel to handle this function and the increase in administrative costs?

Mr. MILLS. There may be some additional personnel in the Internal Revenue Service but we do not have the figures with respect to them. Many of the paying institutions were anxious to have this method enacted in lieu of the withholding method, as I pointed out earlier. They said they could live with it and that it would be acceptable to them. It was on that basis largely that I think the other body went along with the reporting system.

Mr. COLLIER. So there would be no real increase in administrative costs?

Mr. MILLS. There will be some increase compared to withholding. I cannot say that this will do the job without some additional personnel to check returns and do what would have been done under a withholding system with less personnel—I cannot say that. There would be, if all of these returns are checked, in all probability some requirements for additional people. But bear in mind this, that if this provision does collect in the first year of its operation the amount that the staff of the joint committee says, \$275 million, we will be making money even if we have to put up even as much as \$10 million for additional personnel.

Mr. KYL. Mr. Speaker, will the gentleman yield?

Mr. MILLS. I yield to the gentleman.

Mr. KYL. Is it not true that the proposed data processing system of the Internal Revenue Service with its assigned taxpayer numbers, anticipates a reporting method similar to the one under discussion?

Mr. MILLS. This reporting system will be more effective in 1966 or whenever it is when this entire data processing plan is in effect. It is in effect in some areas. To the extent that it is, can be used within a section of this program.

Mr. LINDSAY. Mr. Speaker, will the gentleman yield?

Mr. MILLS. I yield to the gentleman.

Mr. LINDSAY. I am curious as to why the distinguished chairman of the committee did not touch on the international features of the bill. One of the aspects of the House bill that gave me the most trouble was the taxation of foreign subsidiaries. Was the gentleman going to cover that point?

Mr. MILLS. My understanding is that this provision meets the objection that the gentleman from New York, as

I recall, registered on the floor, in that, under the pending bill, we are confining this operation of penetrating the veil of foreign corporations owned by American corporations for the purpose of getting at what is described as tax haven income. We are not going beyond that as we did in the House version. By the same token, the Senate version in this respect, which we accepted, does not permit, under circumstances that were permitted by the House bill, a deferral of that income from the American tax depending on its investment in certain areas, and so on. So that as the Senate confined the effect of it, the Senate also limited the opportunity within that confinement for any escape by reinvestment in certain sections of the world. So the provision brings in, I think, in a better way the same \$85 million that would have been brought in by the House bill, according to the statement of the Treasury.

Mr. LINDSAY. I thank the gentleman.

Mr. MILLS. I think the gentleman will be satisfied with this version.

Mr. DERWINSKI. Mr. Speaker, will the gentleman yield?

Mr. MILLS. I yield to the gentleman.

Mr. DERWINSKI. Could the gentleman clarify the Senate provision that would have offered capital gains tax relief for persons over 65 who were selling their home?

Mr. MILLS. That was deleted in conference along with other provisions written in on the floor of the Senate. Legislation of this nature is a matter, of course, that is of interest to all of us. It is a matter, however, that the Committee on Ways and Means had not had an opportunity to consider and we thought it would be better to have it carried over so that we could have hearings on it at some time in the future.

Mr. DERWINSKI. I thank the gentleman.

Mr. MILLS. Mr. Speaker, under leave to extend my remarks, I would like to include a more detailed comment on the conference agreement along with the revenue estimates I have referred to.

The proposed Revenue Act of 1962, as agreed to by your conferees, still retains the basic approach that was embodied in H.R. 10650 as passed by the House, but it, of course, represents a compromise as is always true of conference agreements. This tax bill presents a program of changes designed to stimulate business activity and to eliminate various preferential provisions of present tax law. Permit me to first give you the principal highlights.

The part of the program designed to provide a business incentive is the investment credit. The general provisions of the investment credit have been maintained close to the provisions in the House bill. Your conferees did accept an amendment which requires the taxpayer to reduce the basis of business property for depreciation purposes by the amount of the investment credit taken. This will in the long run lessen the revenue loss from the investment credit although it will also lessen the incentive effect of

the credit. Your conferees succeeded in retaining the effective date of January 1 of this year as provided in the House bill in order to make the credit applicable to investors who proceeded with their business plans relying on the provisions of the bill as it passed the House.

Your conferees were forced to accept the deletion of the provision for withholding on dividends and interest in favor of the plan for more detailed reporting of payments. Whether or not this reporting will be a satisfactory substitute for withholding will be finally proved one way or the other by experience. The Members of the House should realize that the reporting approach requires a good deal more paperwork, particularly on the part of banks and savings and loan associations. It will also be more expensive for the Internal Revenue Service to actually collect the money when the reports of payments are received and reconciled with individual tax returns. The reconciliation job will be enormous even with continued heavy outlays on automatic data processing equipment and once discrepancies are discovered between the reports of payments and the reports of receipts, activity of revenue agents will be called for. This will require considerable outlays by the Internal Revenue Service if the tax evasion on nonreporting of dividends and interest is to be substantially reduced by means of information returns.

In the matter of the business entertainment expense deduction, your conferees reach agreement on the rule between the relatively strict rule of the House and the milder rule adopted by the other body. In general, the House bill will prevail in that entertainment expenses to be deductible must be directly related to the active conduct of the trade or business. An exception is provided for business entertainment directly preceding or following a substantial business discussion. Entertainment of a good will character is to be allowed as deductible if it is associated with the active conduct of the trade or business.

The provisions of the House bill with respect to gain from the sale of depreciable property are substantially unchanged in the final bill.

The various provisions of the House bill which reduce or eliminate the tax differences on special provisions applicable to certain classes of domestic taxpayers have been largely retained in the final bill. These include mutual savings banks, savings and loan associations, mutual fire and casualty insurance companies, and cooperatives. Your conferees accepted various amendments introduced in these areas by the other body designed to eliminate particular cases of hardship that might have developed under the House bill. In the mutual savings area, a more specific provision was adopted relating to the definition of a savings and loan association. In the cooperative area, in view of the elimination of withholding, your conferees accepted an amendment requiring cooperatives to distribute at least 20 percent of patronage refunds in

the form of cash as a condition for obtaining a tax deduction with respect to noncash dividends. This will obtain the results sought in the House bill of assuring the patron of the ability to meet at least the first bracket tax liability on his entire patronage dividend.

In the area of taxation of foreign income, your conferees have accepted, in the main, the modifications of the House bill adopted in the other body. On the matter of the deferred income of controlled foreign corporations, the direction of these amendments was to apply the provisions more particularly with respect to tax-haven income, that is, situations where the whole foreign corporation arrangement exists more for tax purposes than for business purposes. On the other hand, the provisions as modified would have less impact than might have occurred under the House bill on other business operations. Your conferees accepted the exception to the requirement for "gross-up" in connection with the foreign tax credit on dividends for dividends received from less developed country corporations. With the exception of these modifications, the foreign tax provisions in the final bill are substantially like those contained in the House bill.

I will now briefly describe the other substantive amendments adopted in the other body which are in addition to the matters I have already mentioned.

INVESTMENT CREDIT

As accepted by your conferees, the bill includes several improvements in the operation of the investment credit. One of these has to do with the carryback of credits that cannot be used because they are too large in relation to the current tax. Under the House bill the taxpayer would have to carry forward the unused credit to be used against taxes of the following 5 years. Under an amendment accepted by your conferees, the taxpayer may first carry back the unused credit against tax during the prior 3 years.

This will permit the credit to operate as a current investment incentive even when many taxpayers might have little or no current tax liability.

Another amendment to the investment credit provision provides that no credit would be allowed with respect to reinvestment of insurance proceeds where property has been stolen or destroyed or damaged by fire, storm, shipwreck or other casualty. Since replacement is fairly automatic in these situations, it is believed that no incentive is necessary.

Another amendment in this area provides that the investment credit shall not apply to investment in livestock. Under the House bill, livestock, like buildings, was exempted from the provisions for ordinary income treatment on sale, to the extent of prior depreciation. It was agreed that since livestock is excluded for this purpose it should, like buildings, be excluded from the investment credit.

Mr. Speaker, as passed by the House, the bill also provided that a person engaged in the business of leasing property could elect to give the benefit of the investment credit to his lessee. Your conferees accepted an amendment which

made this election available also where the lessor was not in the business of leasing property.

As I explained earlier, the conferees accepted amendments made by the other body to the investment credit provisions as passed by the House which provided that the cost of property for depreciation purposes was to be reduced by the amount of the investment credit allowed with respect to such property. This reduction on the depreciation base will be restored if it develops that the taxpayer gets no benefit from the investment credit.

ENTERTAINMENT EXPENSES

Mr. Speaker, under the House bill no deduction would have been allowed for any business entertainment unless the expense item was directly related to the active conduct of the trade or business. Similarly, the House bill provided that no deduction would be allowed for expense items with respect to a facility, such as a yacht, used in connection with business entertainment unless the facility is used primarily for the furtherance of the trade or business and that the expense item was directly related to the active conduct of the trade or business. The amendment adopted in the other body provided that these items could be deducted if they were "associated with" as well as "directly related to" the business. The committee report of the other body indicated that the words "or associated with" were to cover a range of goodwill expenditures.

Under the conference agreement, the words "or associated with" were made applicable only to items directly preceding or following a substantial and bona fide business discussion—including a business meeting at a convention. The concept of the House bill was retained so far as entertainment facilities are concerned.

Mr. Speaker, the other body also amended the entertainment expense provisions of the House bill by carving out certain exceptions from the application of the general rule contained therein that business gifts would be deductible only to the extent that they did not exceed \$25 a year for each donee. In general, these exceptions relate to advertising and promotional material and to employee service or safety achievement awards, subject to reasonable dollar limitations.

Another amendment made by the other body to the provisions of the House bill had to do with the deductibility of traveling expenses in the case of a taxpayer who is away from home on business or in pursuit of an income-producing activity. Under this amendment the deduction for business travel is cut down in certain cases where there are major nonbusiness as well as business reasons for the trip. There is to be no cutdown where the trip lasts less than a week, nor where the time spent on other than business is less than 25 percent. Your conferees accepted this amendment.

Mr. Speaker, as passed by the House, the bill provided for the deduction of traveling expenses which were to include a reasonable allowance for amounts expended for meals and lodging.

Under the amendment made by the other body, only those expenses for meals and lodging while traveling, which are not lavish or extravagant under the circumstances, would be deductible. Under the conference agreement, this amendment was retained.

Mr. Speaker, your conferees also accepted the amendment made by the other body which updates the effective date of these new entertainment expense provisions from the June 30, 1962 date specified in the House bill to December 31, 1962.

MUTUAL SAVINGS BANKS, ETC.

The major change from the House bill provision relating to mutual savings banks and savings and loan institutions was an amendment which would have provided a lower reserve deduction for those institutions which had capital stock. Under the conference agreement this change from the House bill was eliminated.

Your conferees accepted several amendments which provided certain ceilings on the loss reserves. One was the 12 percent ceiling of previous law. Another ceiling is provided by the rule that the reserve for losses in qualifying real property loans cannot exceed 6 percent of those loans. An amendment which would require that pre-1952 reserves would be taken into account for certain purposes was also adopted. The remaining amendment related to the reserve computation was an alternative formula for new institutions. This was also accepted.

Another amendment adopted in the other body went to the definition of a building and loan, or savings and loan association. Generally the amendment went in the direction of replacing the qualitative tests of the House bill with a specific formula. The formula carried out the general thrust of the House bill so far as limiting commercial and non-residential loans is concerned. The amendment introduced in addition a limitation on the amount of lending on multifamily residential property. Under the conference agreement the formula approach of the amendment was retained with the clarification that assets used in the trade or business and pass-book loans would be treated in the same manner as investments in one- to four-unit residential property. In addition, under the conference agreement, the formula was modified to allow institutions to exceed the percentage limitation on investments in other than one- to four-unit residential property but by no more than 5 percentage points and for not over 2 years. If the institution is within this 5 percent range over the allowable investment, the special reserve deductions are reduced by one-twelfth of each 1 percentage point of the excess on the basis of the formula contained in the amendment.

The matter of the definition of a savings and loan association has been a matter of considerable uncertainty in the last few weeks. I would like to make several points to clarify questions that might be in Members' minds on this matter. In the first place we have been assured by the Treasury technicians that if, in some future year, a savings

and loan association ceases to qualify under the new definition, this fact by itself will not result in imposition of tax on the reserves accumulated in prior years. In addition, the operation of the new definition will not impede the participation loan program endorsed by the Congress in 1959. An institution will be able to treat as a residential property loan a participation in such a loan or the portion remaining after the sale of a participation to another institution so long as the taxpayer continues to meet the principal requirements of the new statute that substantially all of the business of the institution consists of acquiring the savings of the public and investing them in loans. In such cases, sales of participations, with an agreement to continue servicing the loans on which participations are sold, as well as occasional sales of loans, would not cause the institution to lose its status as a building and loan association provided, this principal requirement of the statute is met.

MUTUAL FIRE AND CASUALTY INSURANCE COMPANIES

Mr. Speaker, your conferees accepted several amendments dealing with the tax treatment of mutual fire and casualty insurance companies that were designed to modify the application of the House bill in special circumstances. The general provision of the House bill in this area was retained.

A group of amendments were intended to provide additional exemptions from the new provision for small insurance companies. These amendments were accepted by your conferees with two minor modifications.

Your conferees accepted an amendment which would provide that underwriting losses generated by policyholder dividends could be deducted first against investment income before being charged against the deferred income account. Under the House bill, these underwriting losses attributable to policyholder dividends had to be charged first against the deferred income account. This modification was accepted in order to prevent the bill from discriminating against ordinary mutuals in favor of the so-called deviating companies.

The other body adopted an amendment dealing with certain companies having underwriting losses for a series of years prior to 1962. The principal of this amendment was accepted by the conferees but the scope of the amendment was substantially narrowed. Another amendment liberalized the provisions of the House bill dealing with certain companies insuring against natural disasters and having concentrated risks. The alternative rules for measuring this concentration adopted in the other body were accepted with one modification.

Your conferees accepted an amendment dealing with the treatment of reciprocal companies which would modify the application of the rule of the House bill which permits the reciprocal to take into account the income and the tax paid by a corporate attorney in fact. Under the amendment, this is permitted to increase the amount of the deferred income.

Finally, your conferees accepted a provision that would allow certain mutual flood insurance companies to be treated in the same manner as the so-called factory mutuals. The amendment in this regard was modified so as to insure that subscribers in such a flood insurance company would be treated in the same manner as policyholders in a factory mutual in determining their current deduction for business insurance. Under present practice, a policyholder in a factory mutual is permitted to deduct only the absorbed premium.

FOREIGN TAX PROVISIONS

1. FOREIGN TAX CREDIT

The House bill provided the so-called gross-up in the foreign tax credit for an American corporation receiving dividends from a foreign corporation. Your conferees accepted the amendment which exempts from the new gross-up provision dividends from a foreign corporation which derives substantially all of its income from sources within a less-developed country. A shipping company whose vessels are registered in a less-developed country might also qualify for this exception to the gross-up procedure. This amendment will reduce the estimated revenue gain from the gross-up provision as contained in the House bill from \$30 million to \$20 million.

Your conferees accepted a new provision for a separate foreign tax credit limitation for certain interest income, not derived directly in connection with a trade or business. This provision will discourage the use of short-term investments in foreign securities in order to take advantage of a potentially unusable foreign tax credit on other income, and thus will tend to improve our balance of payments.

2. FOREIGN EARNED INCOME

The report contains substantially the same provisions as the House bill in limiting the exclusion from income of foreign earned income of American citizens permanently residing abroad beginning in 1963. Several amendments were accepted. One prevented a taxpayer from simultaneously claiming to be a foreign resident for U.S. tax purposes and a U.S. resident for foreign tax purposes and thereby avoid U.S. tax. Another provides a 3-year transition rule for including in the tax base income received in the form of the right to use property. Another amendment prevents evasion of the new limitations by prepayments of income in 1962 for services to be performed after 1962.

3. CONTROLLED FOREIGN CORPORATIONS

The basic section dealing with controlled foreign corporations, as contained in the conference agreement, is substantially similar to the provision adopted in the other body. Generally, the revision from the House bill directed the section more explicitly at the so-called tax haven corporation. In this area, the final bill is in many respects tighter than the House bill. The final bill has a more limited application than did the House bill.

Under the House bill the profits of a controlled foreign corporation might be taxable to principal U.S. shareholders

whatever the source of the profit if reinvestment is not in substantially the same trade or business as one in which the company was already engaged or in a less developed country. The revised provisions concentrate on relatively passive forms of income where there is reason to believe that the incomes are being diverted to the foreign corporation principally for tax advantage.

The two bills are substantially the same with respect to income earned from insurance of U.S. risks except that the Senate and conference bill provide a de minimis provision. The two bills were substantially similar with respect to passive investment incomes such as dividends, interest, rents, and royalties except that the final bill provides various exceptions for these incomes earned in connection with an active trade or business conducted by the foreign corporation or certain subsidiaries of the foreign corporation.

Under the original House bill, passive investment income could avoid the special tax provision, however, by being reinvested in a less developed country. The conference bill narrows this exception by limiting it to dividends, interest, and gains on investments in less developed countries. The bill does not now have a special provision within the section on controlled foreign corporations to deal with the income earned on U.S. patents, copyrights, and so forth, as was contained in the House bill. This problem is dealt with here through a single tax imposed at the time that a patent is transferred to a foreign subsidiary.

Both the House bill and the final bill apply the new tax provisions to certain sales income, where sales involving one foreign country are channeled through a tax haven corporation in another foreign country in order to minimize the tax. The principal change here reduced the allowable minimum income of this sort that could be received by combining the minimum with respect to foreign base company sales income with the minimum provided for passive investment income. These were two separate minimum 20-percent figures in the House bill and have now been combined into a single 30-percent minimum provision. Your conferees accepted another feature of the amendment which extended this principle to certain types of service income where the income arising from services performed in one country might be diverted to a tax haven corporation in another foreign country in order to minimize taxes.

The House bill, as well as the pending bill, makes the new tax provisions apply in certain cases where the controlled foreign corporation invests part of its profits in U.S. assets as a device for bringing the profits home without actually paying dividends. The provision in this regard is substantially the same as it was in the House bill.

The amendment adopted in the other body provided several relief provisions consistent with preventing tax avoidance. These provisions have been accepted with slight modification by your conferees. One of the relief measures provides that the tax imposed by reason

of this section on an individual U.S. shareholder will not be greater than the tax that would be imposed if the income had been earned through a corporation organized in the United States.

It is also provided that the new tax provisions will not be operative if the controlled foreign corporation makes a sufficiently large distribution of its current earnings and profits to assure the result that the aggregate tax imposed by the foreign government on these earnings and profits and by the United States on the dividends distributed will be about 90 percent of the 52 percent U.S. corporate tax rate.

The conference agreement also provided that corporations organized in and principally doing business in Puerto Rico, the Virgin Islands, or other possessions of the United States will generally be excluded from the category of controlled foreign corporations. In addition, certain persons who are residents of Puerto Rico, the Virgin Islands, or other possessions of the United States will not be treated as U.S. persons for purposes of determining U.S. control.

The final revision in this provision accepted by your conferees was a limited exception for export trade corporations as defined in the bill. The general effect of this provision is to specify that where a foreign corporation is engaged in exporting U.S. goods for foreign sale, its income up to a limit of certain normal trade markups will be excepted from the new tax provisions if this income is reinvested in export trade assets. The inclusion of this provision is desirable in order to permit reasonable corporate structures designed to increase the level of U.S. exports.

4. SALES OF PATENTS, AND SO FORTH, TO FOREIGN CORPORATIONS

Under the bill approved by the House, income realized by a controlled foreign corporation which was attributable to patents, and so forth, created or produced in the United States would be currently taxable to U.S. shareholders, whether distributed or not. The other body substituted for this treatment a provision under which gain on the sale or exchange of patents, and so forth, to a controlled foreign corporation by a U.S. person in control of such corporation would be treated as ordinary income unless it was established that such property was to be used by the foreign subsidiary in its own manufacturing operations.

Under the conference agreement, the amendment made by the other body was retained but the exception of transfers to a foreign subsidiary for use in its manufacturing operations was deleted.

5. OTHER FOREIGN TAX PROVISIONS

The remaining foreign tax provisions may be referred to briefly. Your conferees accepted an amendment deleting the House provisions changing present law with regard to foreign personal holding companies. This amendment was regarded as unnecessary in view of the changes with regard to controlled foreign corporations. We also accepted the deletion of the amendment in the House bill to Section 482 of present law. The

House bill provided a specific formula for allocating sales income between related domestic and foreign companies. This deletion was accepted with the understanding that the Treasury would seek to carry out the intent of the House bill provision through its broad regulatory power under section 482 in present law.

Your conferees accepted an amendment to the new rule of the House bill relating to the valuation of property distributed with respect to stock by a foreign corporation to a domestic corporate shareholder. The amendment provides a consistent rule for computing the foreign tax credit.

Your conferees accepted two minor amendments to the new provision added by the House bill with respect to distributions by foreign trusts with U.S. grantors. The amendments limit the new provisions to the portion allocable to property contributed by U.S. persons and make the effective date uniformly December 31, 1962.

The conference agreement contains substantially unchanged the House bill provision eliminating certain abuses under present law in regard to foreign investment companies. An amendment was adopted to the provision allowing these companies to elect to be taxed substantially like domestic investment companies. Under the amendment, companies making this election would get the same treatment as domestic regulated investment companies on foreign tax credits. Another amendment dealing with the application of section 367 to the domestication of a foreign investment company was rejected as unnecessary.

Mr. Speaker, as passed by the House, the bill provided that certain gains realized on redemption or sale of stock in a controlled foreign corporation by a 10 percent or more U.S. shareholder would be treated as a dividend to the extent of the shareholder's share of the corporation's earnings and profits.

Your conferees accepted an amendment limiting the new rules to transactions occurring after December 31, 1962, and then treating as ordinary income only earnings and profits accumulated after that date. The final version also provides other exceptions to the new rules and provides a limitation on the tax payable by individual shareholders, based upon the tax that would be paid by a corporate shareholder.

6. INFORMATION AS TO FOREIGN ORGANIZATIONS

Your conferees accepted the amendment made by the other body to the provisions of the House bill requiring the submission of information with respect to foreign organizations, with one minor modification having to do with the date the new reporting requirements go into effect. In general these amendments liberalized the reporting requirements specified in the House bill and reduced the penalty for noncompliance with these provisions.

GAIN FROM THE DISPOSITION OF CERTAIN DEPRECIABLE PROPERTY

Under the House bill, gain on the disposition of certain depreciable property

after enactment would be treated as ordinary income to the extent of depreciation taken with respect to the property for taxable years beginning after December 31, 1961. The other body amended this provision to make it applicable only to dispositions made in taxable years beginning after December 31, 1962, and only with respect to depreciation taken in periods after December 31, 1961. Under the conference agreement, the amendments made by the other body are retained.

The other body also amended the provisions of the House bill to take account of the interaction of the effect of this new provision upon the computation of the taxable income base to which the 50-percent limitation on allowable depletion deductions is applied. Under this amendment, this taxable income base would, in effect, be increased by the amount of ordinary income realized by virtue of this new provision, thereby increasing the base to which the 50-percent depletion limitation applies. Your conferees accepted this amendment.

COOPERATIVES

Under the House bill, patronage dividends paid in cash or qualified written notices of allocation would be deductible by a cooperative and taxable to patrons. Written notices of allocation would qualify only if they were redeemable in cash within 90 days after issuance or were those with respect to which the patrons had consented to include the stated value thereof in income. The other body amended this provision of the House bill to provide that a written notice of allocation would not qualify unless 20 percent or more of the stated amount of the written notice of allocation was paid in cash or by qualified check. Under the conference agreement, this amendment was retained.

Your conferees also accepted an amendment made by the other body which permits member and nonmember patrons to consent to the inclusion of the stated value of a patronage allocation in their income by endorsing and cashing a qualified check within 90 days after the close of the cooperative's payment period for which the check is paid. This method of giving consent is in addition to the other methods that were provided in the House bill.

REPORTING OF INTEREST, DIVIDENDS, AND PATRONAGE DIVIDENDS

As passed by the House the bill contained provisions which would have instituted a system of withholding of tax at source on payments of interest, dividends, and patronage dividends. These provisions were deleted by the other body and, in lieu thereof, provisions were substituted which would require paying agents, after January 1, 1963, to report to the Government and to provide payees with annual statements of, all payments of these items which amount to \$10 or more per year. The other body also provided penalties for the failure to timely report these items and to provide statements for payees.

Under the conference agreement, the reporting provisions approved by the other body are retained.

PROVISIONS ADDED BY THE OTHER BODY NOT IN HOUSE BILL

(1) EXPENDITURES BY FARMERS FOR CLEARING LAND

Your conferees accepted a provision which would permit taxpayers engaged in farming to deduct, currently, rather than capitalize, expenditures incurred in clearing and levelling land, and in diverting streams, to make the land suitable for farming. This deduction is limited to \$5,000 or 25 percent of the taxpayer's income from farming, whichever is the lesser.

(2) CERTAIN CHARITABLE CONTRIBUTIONS

An amendment was accepted to modify the operation of the charitable contribution deduction where a taxpayer spreads back a lump sum receipt of income over the years to which it is attributable for the purpose of determining the amount of tax he must pay on such income. Under the conference agreement, the amendment was modified to more closely carry out the intent, to permit the deductibility of contributions to be determined as closely as possible to what it would have been in the absence of the bunching.

(3) EFFECTIVE DATE OF SECTION 1371(C)

Your conferees accepted an amendment making applicable to 1958 and 1959 the rule that spouses who hold stock in a "Subchapter's corporation" jointly or under community property laws would be treated as one shareholder for the purpose of applying the 10 shareholder rule.

(4) LOSSES SUSTAINED BY CERTAIN STREET RAILWAY COMPANIES

Your conferees accepted an amendment providing that certain losses incurred in 1953 and 1954 by a street railway company not heretofore used against taxable income could be carried forward and offset against income in the years 1960 through 1964. This amendment is comparable to the bill passed by the House last year.

(5) EXEMPTION FOR PENSION TRUSTS

The conference agreement contains an amendment to provide that the union negotiated plan of a local of the International Hod Carriers', Building & Common Laborers' Union of America is to be treated as a qualified tax-exempt trust for the period beginning May 1, 1960, to April 29, 1961. A number of similar bills have been approved by the House in recent years and this amendment contains the same safeguards that were in prior legislation.

(6) CONTINUATION OF PARTNERSHIP YEAR IN CERTAIN CASES

Your conferees accepted an amendment which would provide, under the code of 1939, that where one of two partners dies, the partnership year for the surviving partner would not have to terminate at that time. This amendment is designed to provide relief from the inadvertent "bunching" of income that occurred under prior law.

(7) EXCLUSION OF CERTAIN AWARDS

An amendment made by the other body provided that awards made pursuant to the Japanese-American Evacuation Claims Act of 1948 would be ex-

cluded from gross income of recipients. Although no comparable provision was contained in the House bill, legislation sponsored by our colleague, Mr. KING of California, identical to this bill was passed by the House recently. Under the conference agreement, this amendment is retained.

(8) COOPERATIVE HOUSING DEPRECIATION

Your conferees accepted an amendment to provide that a tenant-stockholder in a cooperative housing corporation can take depreciation on the portion of his basis in the stock to the extent that the deduction represents a business deduction and is properly allocable to his proprietary lease or right of tenancy.

(9) PERSONS 65 OR OLDER SELLING PERSONAL RESIDENCES

An amendment made by the other body which was rejected under the conference action would have provided that gain realized from the sale or disposition of his personal residence by a taxpayer aged 65 or over would be excluded from gross income provided the taxpayer or his spouse used such residence for 5 years before such sale or exchange. However, the amount so excluded would not be permitted to exceed that portion of the gain corresponding to the ratio of \$30,000 to the sales price.

(10) CONTRIBUTIONS TO JUDICIAL REFORM ORGANIZATIONS

Mr. Speaker, one of the amendments which was accepted provides deduction for gifts made after December 31, 1961, to nonprofit organizations created and operated exclusively to advance State and local judicial reform proposals which are the subject of referendums in 1962, as charitable contributions. No part of the net earnings of the organization may inure to the benefit of any private individual nor may the organization participate in any political campaign in behalf of or in opposition to any candidate for public office. An identical bill on this subject by our colleague, the gentleman from Illinois [Mr. YATES] was recently passed by the House.

(11) SOCIAL SECURITY AMENDMENT

Under the conference agreement, an amendment to the Social Security Act was deleted. This amendment would have permitted the States to accept as presumptively correct any written statement as to financial status made by an applicant for medical assistance for the aged under the Kerr-Mills Act.

(12) FOREIGN SUBSIDIARIES MANUFACTURING PRODUCTS ABROAD FOR SALE IN THE UNITED STATES

The other body added a provision to the House bill which would have taxed as U.S. source income the income realized by a 10 percent U.S.-owned foreign corporation from the sale for use, consumption, or disposition in the United States of competitive articles mined, processed, or manufactured abroad. This treatment would apply if 10 percent or more of the gross income of such foreign corporation was derived from such sales. Under the conference agreement, this amendment was eliminated from the bill.

(13) EFFECTIVE DATE OF AMENDMENT TO SECTION
1374 (b)

Your conferees accepted a provision changing the effective date of a 1959 amendment to subchapter S of the Internal Revenue Code. This 1959 amendment permitted shareholders in such corporations who died before the end of the corporation's taxable year to deduct

their share of any net operating loss sustained by the corporation. The amendment changes the effective date of the 1959 provision from September 23, 1959 to September 2, 1958.

TREATIES

Mr. Speaker, the House bill provided, in effect, that the provisions of the bill

were to have precedence over any conflicting treaty obligation. The bill approved by the other body provided that the bill's provisions were not to take precedence over conflicting treaty obligations. Under the conference agreement, the provisions of the House bill would be retained.

Estimated full-year revenue effect of H.R. 10650,¹ as passed by the House of Representatives, as amended by the Senate Committee on Finance, as amended by the Senate and as agreed to by the conferees

[Millions of dollars]

	As passed by the House of Representatives	As amended by the Committee on Finance	As amended by the Senate	As agreed to by conference		As passed by the House of Representatives	As amended by the Committee on Finance	As amended by the Senate	As agreed to by conference
Investment tax credit.....	-1,395	-1,340	-1,340	-1,340	Foreign items:				
Withholding on dividends and interest.....	+550				Controlled foreign corporations.....	+50	+50	+50	+50
Reporting of dividend and interest payments.....		+275	+275	+275	Grossup of dividends.....	+25	+15	+15	+15
Mutual banks, and savings and loan associations.....	² +170	² +180	² +180	² +170	All other foreign items.....	+25	+25	+25	+25
Entertainment, etc., expenses.....	+125	+85	+85	+100	Products of foreign subsidiaries sold in United States.....			+50	
Capital gains on depreciable property.....	+110	+105	+105	+105	Secs. 21-26.....		-5	-5	-5
Mutual fire and casualty companies.....	³ +25	³ +25	³ +25	³ +25	Secs. 27, 28, 30, and 31.....			-(⁴)	-(⁴)
Cooperatives.....	+30	+30	+30	+30	Secs. 29 and 31.....			-30	
					Total.....	-285	-555	-535	-550

¹ At levels of income and investment estimated for the calendar year 1962, without taking into account effect of provisions on the economy; estimates are rounded to nearest \$5,000,000.

² The level of income for these thrift institutions in 1962 has been revised upward since the preparation of the revenue estimates for the House bill.

³ Revenue gain which would result if this provision were in effect for 1962 and had

been in effect for the 5 preceding years, so that amounts added to the protection against loss account in the 1st year and not offset by losses would be brought into taxable income in 1962.

⁴ Less than \$2,500,000.

Source: Staff of the Joint Committee on Internal Revenue Taxation.

Estimated revenue effect of H.R. 10650 for the fiscal year 1963,¹ as passed by the House of Representatives, as amended by the Senate Committee on Finance, as amended by the Senate, and as agreed to by the conferees

[Millions of dollars]

	As passed by the House of Representatives	As amended by the Committee on Finance	As amended by the Senate	As agreed to by conference		As passed by the House of Representatives	As amended by the Committee on Finance	As amended by the Senate	As agreed to by conference
Investment tax credit.....	-1,340	-650	-650	-1,265	Foreign items:				
Withholding on dividends and interest.....	+170				Controlled foreign corporations.....	0	0	0	0
Reporting of dividend and interest payments.....		0	0	0	Gross-up of dividends.....	0	0	0	0
Mutual banks and savings and loan associations.....	+10	+10	+10	+10	All other foreign items.....	+10	+10	+10	+10
Entertainment, etc., expenses.....	+60	(²) +	(²) +	(²) +	Products of foreign subsidiaries sold in the United States.....			0	
Capital gains on depreciable property.....	0	0	0	0	Secs. 21-26.....		(² -)	(² -)	(² -)
Mutual fire and casualty companies.....	0	0	0	0	Secs. 27, 28, 30, and 31.....			(² -)	(² -)
Cooperatives.....	0	0	0	0	Secs. 29 and 31.....			(² -)	
					Total.....	-1,090	-630	-630	-1,245

¹ Estimates are rounded to nearest \$5,000,000.

² Less than \$2,500,000.

Source: Staff of the Joint Committee on Internal Revenue Taxation.

Estimated full-year revenue effect of H.R. 10650

[In millions of dollars]

	Gross effect ¹			Net effect ²				Gross effect ¹			Net effect ²		
	House	Senate	Conference	House	Senate	Conference		House	Senate	Conference	House	Senate	Conference
Investment tax credit ³	-1,105	-1,020	-1,020	-555	-580	-580	Foreign items:						
Capital gains on depreciable property.....	+100	+100	+100	+50	+50	+50	Controlled foreign corporations.....	+35	+35	+35	+35	+35	+35
Withholding on dividends and interest.....	+780	⁴ +240	⁴ +240	+520	⁴ +155	⁴ +155	Grossup of dividends.....	+35	+25	+25	+35	+25	+25
Expense accounts.....	+125	+60	+100	+80	+40	+65	All other foreign items.....	+30	⁴ +30	+30	⁴ +30	+30	+30
Mutual savings banks and savings and loan associations.....	+200	+205	+200	+135	+140	+135	Miscellaneous provisions.....	-35	-5	-5	-25	-5	-5
Mutual fire and casualty companies.....	+40	+35	+40	+25	+20	+25	Total.....	+325	-240	-170	+430	-35	+10
Cooperatives.....	+35	+35	+35	+25	+25	+25							

¹ Without taking into account the effect on the economy of the provisions.

² After taking into account the estimated effect on the economy of the provisions.

³ At levels of income and investment estimated for 1962. In estimating the net revenue cost of the investment credit, its favorable effects on the level of investment were computed from statistical relationships in the past years between investment and gradual changes in the cost of capital goods (profitability) and cash flow. This procedure thus does not take into account the especially favorable impact on businessmen's decisions to invest of the sudden major improvements in these factors resulting from the enactment of the credit. Taking this into account should produce more favorable effects than those shown in the table.

⁴ Estimated gain from increased compliance because of reporting requirements.

⁵ Because of difficulty of interpretation, no estimate has been made of amendment taxing income derived from imports of goods manufactured abroad by foreign subsidiaries.

Source: Office of the Secretary of the Treasury, Office of Tax Analysis, Sept. 27, 1962.

Estimated revenue effect of H.R. 10650, fiscal year 1963

[In millions of dollars]

	Gross effect ¹			Net effect ²				Gross effect ¹			Net effect ²		
	House	Senate	Conference	House	Senate	Conference		House	Senate	Conference	House	Senate	Conference
Investment tax credit ³	-1,040	-520	-985	-525	-235	-530	Cooperatives.....						
Capital gains on depreciable property.....							Foreign items:						
Withholding on dividends and interest.....	+245			+235			Controlled foreign corporations.....						
Expense accounts.....	+65	+5	+5	+40	+5	+5	Gross-up of dividends.....						
Mutual savings banks and savings and loan associations.....	+5	+5	+5	+5	+5	+5	All other foreign items.....	+5	+5	+5	+5	+5	+5
Mutual fire and casualty companies.....							Miscellaneous provisions.....						
							Total.....	-720	-505	-970	-240	-220	-515

¹ Without taking into account the effect on the economy of the provisions.² After taking into account the estimated effect on the economy of the provisions.³ At levels of income and investment estimated for 1962. In estimating the net revenue cost of the investment credit, its favorable effects on the level of investment were computed from statistical relationships in the past years between investment and gradual changes in the cost of capital goods (profitability) and cash flow. This

procedure thus does not take into account the especially favorable impact on businessmen's decisions to invest of the sudden major improvements in these factors resulting from the enactment of the credit. Taking this into account should produce more favorable effects than those shown in the table.

Source: Office of the Secretary of the Treasury, Office of Tax Analysis, Sept. 26, 1962.

(Mr. MILLS asked and was given permission to revise and extend his remarks and include extraneous matter and tables.)

Mr. MILLS. Mr. Speaker, I yield 20 minutes to the gentleman from Wisconsin [Mr. BYRNES].

Mr. BYRNES of Wisconsin. Mr. Speaker, I would like to bring your attention back to March 29 when this bill was before the House of Representatives. At that time I opposed this bill. I offered a motion to recommit with instructions to make certain changes in it. One hundred and ninety Members of the House of Representatives at that time voted that those changes should be made. Then on the vote on final passage I joined with 196 Members of this House to oppose the bill.

I appear here today, however, in view of the changes that have been made, in support of this legislation.

My objections to H.R. 10650 as it passed the House were directed primarily to three parts of the bill:

First. The withholding on interest and dividends;

Second. The windfall provision—the so-called investment credit—for expenditures made for the acquisition of machinery, equipment, livestock, or any other movable property used in a trade or business;

Third. The foreign income provisions—seeking to build a Berlin wall in the tax laws to prevent American business from going abroad.

I am very happy to report to the House—and particularly to those Members who voted for the motion to recommit and against the bill—that these provisions have been either completely deleted—or have been amended so as to reflect more nearly the minority views in the House.

I would like to refresh your memory on another point. When this bill was before the House on March 27 the President saw fit to have a press conference at which he took note of the position of the Republican minority and charged us

with an obstructionist effort to kill the bill. My colleagues on the other side of the aisle took the floor and charged that the amendments offered by the Republican minority were designed to gut the bill.

When I took the floor of the House on March 29 I suggested that he get his facts straight, that we were not attempting to gut the bill, we were attempting to improve it. There were some 21 sections of the bill. Eighteen of them had our general approval on the minority side. But there were three sections to which we objected. We were trying to improve the bill.

Mr. Speaker, we now have a bill with one of these sections eliminated, and the other two vastly improved. Did this gut the bill? I would like to read you the concluding paragraph of a letter which Mr. Stanley S. Surrey, Assistant Secretary of the Treasury, addressed to the New York Times, on September 12, 1962. Mr. Surrey, talking about the Senate bill which contained these changes, said:

As a longtime tax lawyer with years of experience both in and out of Government, I believe the present tax bill makes advances in more broad areas of income taxation than any tax legislation since 1942.

In quoting Mr. Surrey I do not mean to infer agreement with all he says. I just point out, Mr. Speaker, that we were not trying to gut the bill, we were trying to improve it, and I am here now to support the bill, because the changes we asked for but which were refused by this body were adopted in the Senate and were finally agreed to in conference.

This bill, which the administration describes as the most advanced in broad areas of income taxation than any tax legislation since 1942, embodies the same proposals which, when advanced by the Republicans in this House, were greeted with the claim that we were gutting the tax bill.

Had these provisions been adopted in the committee or on the House floor, we would not be here discussing this because

it would have been law months before now due to the fact the controversy would have been eliminated, and we would have had had a sound bill, in my judgment.

Let me say just a few things about certain of the provisions that are left, and I would like to address myself for a moment particularly to the withholding provision.

I know that most Members—regardless of party—were relieved to learn that the section in the House bill—which provided for withholding on dividends and interest—was completely deleted.

There was substituted a provision requiring dividend and interest paying companies to report the amount of dividends paid both to the Treasury Department and to the payee. This was a suggestion made by Republicans on the committee.

With the new automatic record-processing equipment, which the Internal Revenue Service is installing, it will soon be possible for the Service automatically to check the returns of taxpayers against these reports.

Most important, the paying agent will be required to furnish each taxpayer annually with a report of the amount of dividends and interest paid to that taxpayer. When he gets ready to file his return, the taxpayer will have a record of the amounts paid to him throughout the year. This should eliminate the loss of revenue resulting from forgetfulness on the part of taxpayers.

We are giving the Treasury Department the tools which are needed to collect any taxes due on interest and dividends.

I would caution only that I think the temptation will be great for those die-hard exponents of an across-the-board withholding in the Treasury to sit on their hands in the next few years, and then claim that the returns are not resulting in adequate compliance. We must make every effort to see that the Internal Revenue Service makes use of these tools which we have given them;

otherwise you can be sure they will be back here in a year or two telling us there is some fantastic amount of income escaping taxation which cannot be discovered and collected without an arbitrary across-the-board system of withholding. So much for withholding.

As passed by the House, upon the insistence of the administration, investment credit was the greatest loophole of all time. I repeat again, briefly, how that worked:

The taxpayer might purchase a new machine costing \$1,000. The taxpayer would receive a tax credit of \$70. In other words, he would get back \$70 from the Government in the form of a credit or reduction of his tax liability, merely because he purchased the machine. The taxpayer, however, would set up the machine on his books at a cost of \$1,000. He would then deduct that amount over the life of the property in the form of depreciation. Thus, the taxpayer was getting a deduction for \$70 of the cost of the machine for which he had already been reimbursed by the Government in the form of the investment tax credit.

Mr. Speaker, the amendment which was adopted in the Senate is the same as an amendment which I proposed in the committee. The taxpayer is now required to reduce the cost of the machine for depreciation purposes by the amount of the subsidy or the investment credit. For example, if the taxpayer under the bill as is before us now received an investment credit of \$70 on the purchase of a \$1,000 machine, the taxpayer can only deduct \$930 of the cost of the machine for depreciation purposes over the life of the property. With this Senate amendment, the investment credit is only half as bad as it was in the House bill. The taxpayer still gets a subsidy, but does not get it tax free. He cannot have the subsidy and depreciate the amount at the same time.

I am not suggesting that the investment credit is now good tax law. I am not doing that. I am only saying they have eliminated a great share of the windfall and the loophole and the bonanza. I still believe we should have approached this question through a change in depreciation.

This change in the investment credit was bitterly fought by the Kennedy administration. It is not significant in its immediate revenue effect, but it has a very significant long-term effect. Over the next 10 years this amendment results in savings in the Federal revenues aggregating some \$5 billion.

At this point I ask permission to insert in my remarks a schedule prepared by the staff of the Joint Committee on Internal Revenue Taxation showing the difference between the investment credit as provided for in the House bill and the investment credit as amended by the Senate and accepted by your conferees.

The SPEAKER pro tempore. Is there objection to the request of the gentleman from Wisconsin?

There was no objection.

The schedule referred to follows:

Estimated revenue loss under investment tax credit provision of H.R. 10650 as agreed to by the conferees and without Senate amendment 19, which reduces depreciation base by amount of tax credit, 1962-72, assuming an annual increase of 5 percent in investment in eligible assets¹

[In millions]

Calendar year	Revenue loss attributable to investment tax credit on eligible assets acquired or constructed in calendar year ²		
	Under provision as agreed to by the conferees (including Senate amendment 19)	Decrease in revenue loss ascribable to Senate amendment 19	Under provision without Senate amendment 19
1962-----	\$1,320	\$50	\$1,370
1963-----	1,350	140	1,490
1964-----	1,385	230	1,615
1965-----	1,400	310	1,710
1966-----	1,390	390	1,780
1967-----	1,435	465	1,900
1968-----	1,470	535	2,005
1969-----	1,505	605	2,110
1970-----	1,545	670	2,215
1971-----	1,575	730	2,305
1972-----	1,630	790	2,420
1962-66-----	6,845	1,120	7,965
1962-72-----	16,005	4,915	20,920

¹ This is the rate of increase assumed by the Secretary of the Treasury before Senate Committee on Finance on Apr. 2, 1962.

² Except that carryforwards are allocated to years to which they are carried; tax effects of reduced depreciation base are allocated to years in which depreciation is taken on the relevant assets, that is, assets acquired in the designated year and in designated years preceding that year; and tax effects of deductions for unused investment credit are allocated to years in which the deductions are taken. Carrybacks are allocated to years from which they are carried. Estimates are rounded to nearest \$5,000,000.

Source: Staff of the Joint Committee on Internal Revenue Taxation, Sept. 27, 1962.

Mr. BYRNES of Wisconsin. Mr. Speaker, I am still opposed to the investment credit. I do not think that it makes any sense. This form of so-called tax incentive will result in an immediate revenue loss of \$1.3 billion. It has been rammed down the throat of the business community—notwithstanding that business would prefer that any incentive for investment in machinery and equipment take the form of accelerated depreciation. If we are going to provide for a tax incentive of \$1.3 billion to business, we should give business what it needs and wants—not waste our tax revenues on some new gimmick.

In the House bill, the investment credit was applied to any property put into use after January 1, 1962. The Senate moved this date up to July 1, 1962, thereby cutting in half the revenue loss. In conference, however, the Senate receded.

Faced with a deficit of at least \$5 billion for fiscal 1963, I do not find any justification for providing a retroactive investment credit at a revenue loss of some \$1.3 billion. There can be no justification for giving a taxpayer an incentive to do something which he has already done, and would have done in any event. By making the investment credit retroactive to January 1, 1962, that is what this bill will do.

I would have preferred to make the provision prospective, and if the provi-

sion had been made effective as of October 1, 1962, for instance, the date on which we are passing this bill, the revenue loss for fiscal 1963 would have been reduced by about \$1 billion and we would have had practically a balanced revenue bill today.

Mr. Speaker, I think it is most unfortunate that we did not bring out a balanced bill, when it was so easy to do so, simply by changing the effective date of this provision. But I must say to the Members of the House as one of the House conferees and charged with trying to hold the House position, when the motion was made on our side that we recede and hold to the January 1st date, there was no parliamentary device whereby that could even be insisted upon.

Mr. Speaker, just a word about the taxation of income earned abroad by foreign corporations in which there is an American ownership. I concur in the provisions of the conference report as I concurred in the provisions of the House bill which sought to tax the income of American-owned "paper" companies, those set up in tax-haven countries for the sole purpose of avoiding U.S. income taxes on transactions which would otherwise have been taxable in the United States. But, as I pointed out in March 29 when this bill was before the House, the House bill did not stop at that point.

As originally passed by this House, H.R. 10650 attempted to tax to the American shareholder the income of all foreign corporations—whether tax haven or otherwise—in which the American shareholder might be said to have had a substantial interest. It would no longer have been possible for an American-owned company in Germany to compete in the same markets with another German corporation, the stock of which was owned by other than American nationals. This is what I objected to in the House bill.

Where the House used a shotgun to get at the problem involved here the Senate, to their credit, used a rifle. The foreign income provisions of this bill as rewritten by the Senate, and as it comes to us from the conference, are immeasurably better than the bill passed by the House. For the most part the bill no longer will seriously impede the ability of an American-owned business located abroad to meet its foreign competition.

The final version of this bill is still incompatible with the stated policy of the administration—to encourage private investment in the less developed countries. The bill provides for the deferral of U.S. tax on certain types of income earned abroad which is reinvested in a less developed country. However, the only income to which the exception applies is that which was derived from the same or another less developed country.

As I interpret this restriction, the administration is saying that if a foreign subsidiary of an American corporation has earnings in Brazil, it can invest those earnings in Latin America with-

out the equivalent of first repatriating the earnings and paying the full U.S. income tax. However, it cannot do this if the earnings come from Western Europe.

The likelihood of generating reinvestment funds in the less developed countries is exceedingly remote. There will be none. What is going to happen? The answer should be obvious.

The U.S. corporation is not going to subject the earnings of its German manufacturing subsidiary to the full U.S. income tax for the privilege of reinvesting those earnings in a less developed country. It will reinvest the earnings in Germany or in the Common Market. This is can do without any U.S. tax.

The House bill, bad as it was, did permit greater latitude for reinvestment in less developed countries than the Senate bill or the conference report that is before you. In the conference I tried to insist on the House provision which would have permitted the international trading or export corporation to reinvest its earnings in a less developed country regardless of the source of such earnings.

In my opinion, regardless of statements to the contrary, the administration is not really seeking to encourage private investment in the less-developed countries. The administration's basic philosophy is that the public sector—the Federal Government—should take over the initiative and control of the investment of American funds both at home and abroad. The administration really does not have sufficient confidence in American business to let it operate under the free enterprise system. That is what is lacking in this administration.

Mr. Speaker, let me say in conclusion that when considered in the light of the changes which the other body saw fit to adopt and your conference is bringing to you, when we weigh it all in the balance, I think that we have some features of this bill that are sound and good and, over all we have a balanced bill. That is not to say that I agree with all parts of it. Even though the bill will result, frankly, in a \$1.3 billion loss for fiscal 1963—and that is the part I object to mostly as far as this conference report is concerned—there are other provisions of the bill which will ultimately yield about \$790 million to \$1 billion additional revenue each year. It is that aspect that from the fiscal standpoint brings me to the conclusion that revenue-wise and equity-wise the country is generally better with this bill than without it, in spite of the \$1.3 billion loss in the fiscal year 1963.

We do pick up, I emphasize again, somewhere between \$700 million and \$1 billion a year when the other sections of the bill other than the investment credit go into operation, which is what happens in January 1963.

On the whole, therefore, I come to the conclusion that we should support the bill.

I am hopeful that the experience of the administration in presenting this legislation will serve as a lesson for next year.

The responsibility for tax legislation rests with the Ways and Means Committee—not downtown. I am always prepared to listen to the representatives from the Treasury Department. However, neither I, nor any other member of the Ways and Means Committee, should be asked to accept without question a dictatorial tax policy conceived outside of the Congress and without any regard to its practical effect upon the economy.

If the administration comes up here next year with the same attitude that was exhibited with respect to this bill, it will be impossible to evolve a sound program of tax reform.

(Mr. BYRNES of Wisconsin asked and was given permission to revise and extend his remarks.)

Mr. MILLS. Mr. Speaker, I yield 2 minutes to the gentleman from Tennessee [Mr. BAKER].

Mr. BAKER. Mr. Speaker, as one of the managers on the part of the House, I urge your support of the conference report on H.R. 10650. I do so with some misgivings, because after we have struggled for more than 18 months, we bring forth a tax bill without facing up to the real problem; that is, the existing high and confiscatory rate structure. We should attack that problem first.

I have long urged the need for rate reform. The gentleman from Florida [Mr. HERLONG] and I have identical bills pending. As introduced early in this Congress our bills, H.R. 2030 and H.R. 2031, covered both rate reform as well as depreciation. When the great demand for tax reduction was at its height over the Nation, we introduced identical bills, H.R. 12632 and H.R. 12633, dealing solely with rate reform, and rate reduction, all tied to a balanced budget after the first year.

Over a 5-year period, the first bracket individual rate would be reduced from 20 to 15 percent; the \$4,000 to \$6,000 taxable income bracket from 26 percent to 17 percent, and corresponding reductions in all brackets bringing the top rates, both individual and corporate, down to 42 percent. Nearly 60 percent of the reduction would fall in taxable income brackets below \$6,000.

It was estimated that this rate reduction would result in a loss of revenue of about \$1 billion for fiscal 1963. After fiscal 1963, the full year effect of the 1964 reductions would be about \$3.7 billion—\$2.7 billion to individuals and \$1 billion to corporations, with the express power in the President to defer any annual reduction which would result in unbalancing the budget.

I urge that the approach and rationale of the Herlong-Baker bills be adopted and enacted in the 88th Congress.

H.R. 10650 accomplishes many desirable objectives.

Withholding on interest and dividends was stricken in conference, and a fair and sensible method of reporting of dividends and interest in excess of \$10 both to the Treasury Department and to the recipient was adopted.

This bill closes many loopholes and tax evasion devices in the field of tax

haven corporations and expense accounts.

We have provided new rules for the taxation of mutual banks and savings and loan associations, for the taxation of mutual fire and casualty insurance companies and for the taxation of cooperatives, all in the interest of fairness and equity to all taxpayers.

The bill as agreed to in conference provides a more rational basis for taxing to the U.S. shareholders the income earned abroad by foreign corporations.

There is a great deal more to be done in the field of tax reform and tax revision. I believe that H.R. 10650 will stimulate business activity, and I urge the adoption of the conference report.

(Mr. BAKER asked and was given permission to revise and extend his remarks.)

Mr. MILLS. Mr. Speaker, I ask that all Members desiring to do so may have 5 legislative days to extend their remarks at this point in the RECORD on the conference report.

The SPEAKER pro tempore. Is there objection to the request of the gentleman from Arkansas?

There was no objection.

Mr. ALGER. Mr. Speaker, while there is still much to be desired in this bill it has been greatly improved over the way it was passed by the House and comes nearer to the position I supported when we debated this legislation in this body. The withholding tax on interest and dividends, to which I was opposed, has been eliminated. Investment credit has been cut from a total of 107 to 100 percent and, while my own feeling is that realistic depreciation reform is better, this is a decided improvement. The provisions affecting foreign investment have also been greatly improved. While I would have preferred that the investment credit would become effective on enactment of the measure instead of being made retroactive to January 1, 1962, so that the deficit of this bill would be cut in half, I believe we have taken a decidedly improved position.

I think it is only right to point out that the loss of revenue through the enactment of this bill will amount to \$1.25 billion in fiscal 1963 and \$550 million in fiscal 1964 and thereafter. I deplore the loss of revenue to the Government which cannot help but contribute to further deficits. I am for a balanced budget as the only responsible approach to fiscal policy, but I firmly believe that tax cuts are needed to stimulate business and when tax inequities are found, that is the time to correct them. This is the position I took last year when the Korean war excise taxes were up for renewal. For the first time in 7 years I voted for a tax cut before cutting spending because I stated then, and I state now, I am not picking up the tab any further for the big spenders, wherever they may be or whoever they may be politically. In this my voting record is consistent—I am for reduced spending and on that basis for reduced taxes. Therefore, while not entirely satisfied, I support the conference report on the tax bill.

Mr. BETTS. Mr. Speaker, I support the adoption of the conference report on H.R. 10650. My action in this regard should not be construed as wholehearted approval of all the provisions of this battered and bruised legislation, but instead indicates my conclusion that the bill on balance as it emerged from conference makes some modest contribution to the improvement of our Federal tax structure.

The Senate in acting on H.R. 10650 corrected or ameliorated many of the shortcomings and objectionable features of the House-passed version of the Treasury Department's tax recommendations. Examples of improvements made by the Senate include the following:

The investment credit was improved by providing a 3-year carryback of any investment credit which could not be used in the current taxable year. I might say, Mr. Speaker, that the investment credit as approved by the Congress is a total departure from the unwise, unworkable, and unfair investment credit proposal originally urged by the administration. As the investment credit emerges from the conference committee, it essentially becomes the equivalent of a first year writeoff of a portion of the costs of acquisition of a capital asset. It in effect becomes liberalized depreciation and this is what the Republican membership of the House Committee on Ways and Means originally urged at the time the Treasury Department proposal provoked such controversy.

Mr. Speaker, another improvement in the conference approved bill is the deletion of withholding on dividends and interest. As was stated in the Senate committee report the provision of the House-passed bill for withholding on dividends and interest was neither simple in operation nor free of substantial hardship for broad groups of taxpayers. The report went on to say the proposal represents a heavy administrative burden for the businesses which would have to perform the withholding and collection functions for the Government. It also appears that there are numerous tax avoidance possibilities in a system providing exemption certificates and intra-annual refunds. This accurate condemnation of the House withholding provision made it inescapable that the other body would act to delete this House provision. I regret that the Senate has seen fit to substitute for the withholding requirement a so-called compromise measure introducing added complexity in the area of tax administration. I think it fair to say that no Member of the Congress favors either tax loopholes or tax avoidances. There are, however, different approaches to solving existing problems. In the case of under reporting of interest and dividends, I think a major corrective stride can be accomplished through improved enforcement procedures possible under existing law and through the effective utilization of the new automatic data processing system in conjunction with the program for introducing taxpayer account numbers.

Mr. Speaker, improvement is also found in the bill as it emerged from conference over the House-passed ver-

sion in regard to the complex, confused, and confiscatory provisions dealing with the taxation of income derived from abroad. In my judgment, the House version of H.R. 10650 established tax rules for the taxation of income arbitrarily attributed to U.S. taxpayers which would have substantially lessened the ability of American free enterprise to participate in an expanding level of international trade. While I find this fault to be also true of the bill as agreed to in conference, the extent of this hardship on the endeavors of American free enterprise in the world markets will be reduced.

For the most part, I frankly do not find a good legal or economic basis of justification for the tax changes which are to be made under the conference agreement in the foreign income area. The tax haven abuse situation which cries for correction could have been dealt with on the basis of less sweeping change imposing less stringent conditions.

As it is, the conference version of the foreign income provisions in H.R. 10650 will impose greater tax burdens and infinitely greater tax complexity on the American entrepreneur engaged in international trade and commerce.

This will be occurring at the very time our Nation is ostensibly urging private enterprise to assist in the development of the underdeveloped countries and at the very time our Nation is about to assume leadership in urging the reduction of trade and tariff barriers among the nations of the free world. Mr. Speaker, the conference report fails to deal adequately with our real needs in the way in which our American tax laws apply to overseas income but the measure again represents a substantial improvement over the House-passed bill.

In closing, Mr. Speaker, let me make it clear that I do not mean to sound critical of my able and diligent colleagues who serve with me on the Committee on Ways and Means nor my colleagues who serve with distinction in the House of Representatives. The truth of the matter is that when the Treasury Department came forward with its controversial and complex proposals for amending our Federal tax structure, these proposals were described only in the most general terms and there were no drafts of statutory language available. We made repeated efforts to obtain drafts of such language from the Treasury to no avail. Thus, the committee had to develop a bill virtually from scratch and scratch we did. I urge my colleagues to support the adoption of the conference report.

Mr. SCHNEEBELI. Mr. Speaker, this bill is a substantial improvement over the bill first proposed by the President on April 20, 1961. It is much better than the bill as passed by this body earlier this year. As my colleagues preceding me have said, the bill as agreed to in conference conforms in most respects to the views of the Republican members of the Ways and Means Committee.

I would say that the Revenue Act of 1962 is in better form today than at any other time during the last 17 months. This is not to say that I have no reserva-

tions about the bill. I still do. Nevertheless, I will say that this is a much improved piece of legislation.

When I addressed this body on March 28 of this year, I expressed grave concern over what the administration was attempting to do in the withholding of interest and dividends sections of H.R. 10650. Since that time this unrealistic scheme has been removed entirely from the bill.

I know all my colleagues are relieved. I am certain that the vast majority of the electorate—who made their views known on this issue—will be equally gratified.

Since the beginning I have maintained that the withholding of 20 percent of the income arising from interest and dividends was both unworkable and unsound.

The exemptions for those under age 18 and for those expecting to pay no tax, plus the quickie refund provisions were nothing more than sweeteners designed to soft-pedal unpopular legislation. They did nothing to alleviate the obvious complications and complexities surrounding the procedure. At most, they merely added confusion to chaos.

When we stop to consider the massive overwithholding that would have occurred—the turmoil and paperwork between individuals and the Internal Revenue Service with its resultant confusion—and the effect on tax-exempt institutions, we can see why it had to be eliminated from the bill.

My support of the Senate provision providing for the reporting on interest and dividends is not of recent origin. I supported this approach on the vote to recommit in order that the withholding feature of the bill be eliminated. This was back in March. I supported reporting as a proper remedy even before then.

This year the national processing center at Morgantown, W. Va., will be fully in use. It will be using the latest in electronic-processing machinery known as automatic data processing. Also this year, the first of nine Internal Revenue district centers at Atlanta, Ga., will be equipped with automatic data processing. Next year Philadelphia will be fully implemented. By 1966, at the latest, all nine districts will have complete facilities for this project.

The reports received from financial institutions on interest and dividends of \$10 or more a year per recipient will be fed into these machines. These reports can be matched against the numbered accounts of the various taxpayers concerned. Any taxpayer not reporting such income on his individual return can be quickly discovered.

At the same time, all this will not be going on behind the taxpayer's back. These same financial institutions will be required to send reports to the taxpayers to whom they have paid interest or dividends. The taxpayer will have the benefit of the identical information when making out his return, as the Internal Revenue Service will have when checking his account.

Both the taxpayers and financial institutions have expressed interest in this approach to a very serious problem. Both realize that millions of dollars in

revenues are lost each year because some fail to report and pay the tax on this income. Those who do comply with the letter of the law are desirous of working toward a practical solution of this problem.

All parties concerned have a year to prepare for this reporting approach. It will become effective in 1964 on 1963 income. In that time everyone will have a chance to get his house in order. Hardship should be minimized because of the prospective features of the new system.

I sincerely hope that the Treasury Department and the Internal Revenue Service will make the proper use of the information to be gained from the reporting. I hope they will consider this legislation in the spirit in which it has been offered—not as a scheme designed to further avoid the payment of taxes on income from interest and dividends, but as a workable and practical method for correcting a widely recognized abuse of our tax laws. I hope they have a willingness to make this reporting system work, and will not immediately throw in the towel in disgust and again ask for withholding in this tax reform and reduction package that they are planning for next year—or even the year after, for that matter.

The elimination of withholding and the substitute of a reporting system is the will of the people and of this Congress.

Mr. Speaker, again let me say that this is a much-improved bill and, in conclusion, I urge its support.

Mr. VANIK. Mr. Speaker, I want to set forth my opposition to this conference report on the Revenue Act of 1962. This legislation will constitute a tax drain on the Treasury vastly disproportionate to any stimulation to the economy which it may bring about. The passage of this monstrous proposal, with its overwhelming advantages to the business community, will make it increasingly difficult to pass a fair and equitable and comprehensive tax revision act next year. At that time, the industrial and business sector will insist on added concessions as a condition of support for any large-scale tax revision legislation.

While the tax credit principle may serve as an accelerator toward boom, it also has a potential of serving as an accelerator toward recession. It cannot be expected to serve as a constant stimulus to growth in our economy. As an accelerator, it may serve as an impetus to higher investment spending in periods of higher profits in order to conserve tax liability, and correspondingly slow down investment in periods of recession and low profits when there will be less tax liability toward which to apply the credit.

As adopted in the conference report, the investment credit is made to apply on the first dollar of investment including such new investment as the taxpayer would undertake in the normal course of events. This serves to provide a taxpayer with a bonus for doing something he would do without the stimulant of tax credit. It would seem more prudent to reward a taxpayer for such new investment as he may make beyond that

required in the normal course of business.

It seems unfair to extend this tax bonanza to industrial activity generated by defense procurement. The defense contract producers who are already the recipients of Government aid in the form of defense contracts, many of which are noncompetitive, will receive a special tax windfall through the tax credit.

Perhaps the most unjust feature of all in this law are the provisions which extend the benefits of tax credit to investment in procurement abroad. Thus the purchase of a generator abroad by an American concern for use in this country creates an entitlement for tax credit on taxes due the U.S. Treasury. This Treasury loss cannot help the domestic economy.

In my judgment the enactment of the tax credit provisions will provide a one-shot stimulus to the economy which will soon lose its effect. In computing the revenue loss to the Treasury, the long range effect must be computed. The Joint Committee on Internal Revenue has estimated a \$10 billion tax loss for the period 1962-66 and approximately \$26 billion for the next 10-year period.

This legislation is utterly indefensible. Mr. MILLS. Mr. Speaker, I move the previous question on the conference report.

The previous question was ordered.

The conference report was agreed to.

A motion to reconsider was laid on the table.

NATIONAL FISHERIES CENTER AND AQUARIUM, DISTRICT OF COLUMBIA

Mr. O'NEILL. Mr. Speaker, by direction of the Committee on Rules, I call up House Resolution 822 and ask for its immediate consideration.

The Clerk read as follows:

Resolved, That immediately upon the adoption of this resolution the bill H.R. 8181, with the Senate amendments thereto, be, and the same hereby is, taken from the Speaker's table, to the end that the Senate amendments be, and the same are hereby, agreed to.

Mr. O'NEILL. Mr. Speaker, I yield myself 30 minutes.

Mr. Speaker, this is a resolution relating to the bill (H.R. 8181) to authorize the construction of a National Fisheries Center and Aquarium in the District of Columbia and to provide for its operation. This bill was introduced by the gentleman from Ohio [Mr. KIRWAN]. It passed the House the last day of the session last year by 75 votes.

It went to the Senate where it lingered for some time. The Senate passed the bill with an amendment cutting our original authorization from \$20 million to \$10 million. It came back with the motion that we concur with the Senate amendment. I hope we concur with the Senate amendment.

Mr. Speaker, I now yield to the gentleman from Kansas.

Mr. AVERY. Mr. Speaker, I yield 5 minutes to the gentleman from Iowa [Mr. Gross].

Mr. GROSS. Mr. Speaker, with hope, if not a song in our hearts, we look forward today to an end to the 87th Congress—a Congress that has inched and limped its way through 9 weary months serving well the T. & T. Club. And what more fitting epitaph could be written on the tomb of this deceased than the procedure here today by which the House approves a \$10 million platinum-lined fish bowl.

It is not to be built on the Mississippi, the Maumee, the Katoohochee, or the banks of the Wabash far away. Although the bill hints that individuals of any nation will be encouraged to use it, there is no evidence that Foggy Bottom, watering place of the promoters of an independent, interdependent one world, is even being considered.

There was some talk that members of the finny tribe might be offered the opportunity to share the swimming pool in the \$100 million new, New House Office Building but this is understood to have been given the thumbs-down treatment and for two reasons: First, the shark and barracuda might find something edible about their swimming companions; and second, tourists, paying out their hard-earned cash for admissions which this bill provides, might get a different and startling perspective of House Members when attired in abbreviated bathing apparel.

Although the bill is silent on the subject, the best guess is that this gilt-edged fish bowl will be located on the banks of the Potomac where the flotsam and jetsam goes drifting by when the tide is running. And on a quiet summer night, when the tide is in, one sniff of the air is all that is needed to inform one and all that the Potomac is close by. Here then is our setting for this \$10 million dream attraction that is to bring paying tourists from every nook and crevice of the world, and way points between.

I labor under no illusions about the passage of this bill. The author, the genial gentleman from Ohio [Mr. KIRWAN] is persuasive. He would not be the veteran Member of Congress that he is, neither would he be the chairman of the Democrat congressional campaign committee if that were not true.

As a member of the Appropriations Committee he knows there is nothing easier to spend than public money for it does not appear to belong to anybody. As a Member of Congress for many more years than the gentleman from Iowa, he needs no reminder of the barrenness of the Federal Treasury, of the debts that have been piled high on the generations yet to come.

Appearing before the Rules Committee yesterday, he is reported to have said in justification for his glorified fish tank that "families that fish together, stay together." I would like to tell the gentleman from Ohio that a fishing pole is standard equipment in my car; that it is my earnest hope there will come a year, any year, when the Democratic leadership, of which he is a part, will bring an end to a session of Congress before the rivers and streams freeze over in Iowa.



Public Law 87-834
87th Congress, H. R. 10650
October 16, 1962

An Act

76 STAT. 960.

To amend the Internal Revenue Code of 1954 to provide a credit for investment in certain depreciable property, to eliminate certain defects and inequities, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. SHORT TITLE, ETC.

(a) **SHORT TITLE.**—This Act may be cited as the “Revenue Act of 1962”. Revenue Act of 1962.

(b) **TABLE OF CONTENTS.**—

Sec. 1. Short title, etc.

- (a) Short title.
- (b) Table of contents.
- (c) Amendment of 1954 code.

Sec. 2. Credit for investment in certain depreciable property.

- (a) Allowance of credit.
- (b) Rules for computing credit.
- (c) Deduction for unused credit.
- (d) Certain corporate acquisitions.
- (e) Statutes of limitations and interest relating to investment credit carrybacks.
- (f) Technical amendment.
- (g) Clerical amendments.
- (h) Effective date.

Sec. 3. Appearances, etc., with respect to legislation.

- (a) In general.
- (b) Effective date.

Sec. 4. Disallowance of certain entertainment, etc., expenses.

- (a) Denial of deduction.
- (b) Traveling expenses.
- (c) Effective date.

Sec. 5. Amount of distribution where certain foreign corporations distribute property in kind.

- (a) Amount distributed.
- (b) Basis.
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(c) AMENDMENT OF 1954 CODE.—Except as otherwise expressly provided, whenever in this Act an amendment or repeal is expressed in terms of an amendment to, or repeal of, a section or other provision, the reference shall be considered to be made to a section or other provision of the Internal Revenue Code of 1954.

SEC. 2. CREDIT FOR INVESTMENT IN CERTAIN DEPRECIABLE PROPERTY.

(a) ALLOWANCE OF CREDIT.—Part IV of subchapter A of chapter 1 (relating to credits against tax) is amended by redesignating section 38 as section 39 and by inserting after section 37 the following new section:

“SEC. 38. INVESTMENT IN CERTAIN DEPRECIABLE PROPERTY.

“(a) GENERAL RULE.—There shall be allowed, as a credit against the tax imposed by this chapter, the amount determined under subpart B of this part.

26 USC 1
et seq.

26 USC 31-38.

Post, pp. 967,
968.

Post, p. 963.

“(b) REGULATIONS.—The Secretary or his delegate shall prescribe such regulations as may be necessary to carry out the purposes of this section and subpart B.”

26 USC 31-38.

(b) RULES FOR COMPUTING CREDIT.—Part IV of subchapter A of chapter 1 is amended by adding at the end thereof the following new subpart:

“Subpart B—Rules for Computing Credit for Investment in Certain Depreciable Property

“Sec. 46. Amount of credit.

“Sec. 47. Certain dispositions, etc., of section 38 property.

“Sec. 48. Definitions; special rules.

“SEC. 46. AMOUNT OF CREDIT.

“(a) DETERMINATION OF AMOUNT.—

Ante, p. 962.

“(1) GENERAL RULE.—The amount of the credit allowed by section 38 for the taxable year shall be equal to 7 percent of the qualified investment (as defined in subsection (c)).

“(2) LIMITATION BASED ON AMOUNT OF TAX.—Notwithstanding paragraph (1), the credit allowed by section 38 for the taxable year shall not exceed—

“(A) so much of the liability for tax for the taxable year as does not exceed \$25,000, plus

“(B) 25 percent of so much of the liability for tax for the taxable year as exceeds \$25,000.

“(3) LIABILITY FOR TAX.—For purposes of paragraph (2), the liability for tax for the taxable year shall be the tax imposed by this chapter for such year, reduced by the sum of the credits allowable under—

26 USC 33.

“(A) section 33 (relating to foreign tax credit),

“(B) section 34 (relating to dividends received by individuals),

“(C) section 35 (relating to partially tax-exempt interest), and

“(D) section 37 (relating to retirement income).

For purposes of this paragraph, any tax imposed for the taxable year by section 531 (relating to accumulated earnings tax) or by section 541 (relating to personal holding company tax) shall not be considered tax imposed by this chapter for such year.

“(4) MARRIED INDIVIDUALS.—In the case of a husband or wife who files a separate return, the amount specified under subparagraphs (A) and (B) of paragraph (2) shall be \$12,500 in lieu of \$25,000. This paragraph shall not apply if the spouse of the taxpayer has no qualified investment for, and no unused credit carryback or carryover to, the taxable year of such spouse which ends within or with the taxpayer's taxable year.

“(5) AFFILIATED GROUPS.—In the case of an affiliated group, the \$25,000 amount specified under subparagraphs (A) and (B) of paragraph (2) shall be reduced for each member of the group by apportioning \$25,000 among the members of such group in such manner as the Secretary or his delegate shall by regulations prescribe. For purposes of the preceding sentence, the term ‘affiliated group’ has the meaning assigned to such term by section 1504(a), except that all corporations shall be treated as includible corporations (without any exclusion under section 1504(b)).

“(b) CARRYBACK AND CARRYOVER OF UNUSED CREDITS.—

“(1) ALLOWANCE OF CREDIT.—If the amount of the credit determined under subsection (a)(1) for any taxable year exceeds the limitation provided by subsection (a)(2) for such taxable year

(hereinafter in this subsection referred to as 'unused credit year'), such excess shall be—

“(A) an investment credit carryback to each of the 3 taxable years preceding the unused credit year, and

“(B) an investment credit carryover to each of the 5 taxable years following the unused credit year, and shall be added to the amount allowable as a credit by section 38 for such years, except that such excess may be a carryback only to a taxable year ending after December 31, 1961. The entire amount of the unused credit for an unused credit year shall be carried to the earliest of the 8 taxable years to which (by reason of subparagraphs (A) and (B)) such credit may be carried, and then to each of the other 7 taxable years to the extent that, because of the limitation contained in paragraph (2), such unused credit may not be added for a prior taxable year to which such unused credit may be carried.

Ante, p. 962.

“(2) LIMITATION.—The amount of the unused credit which may be added under paragraph (1) for any preceding or succeeding taxable year shall not exceed the amount by which the limitation provided by subsection (a)(2) for such taxable year exceeds the sum of—

“(A) the credit allowable under subsection (a)(1) for such taxable year, and

“(B) the amounts which, by reason of this subsection, are added to the amount allowable for such taxable year and attributable to taxable years preceding the unused credit year.

“(3) EFFECT OF NET OPERATING LOSS CARRYBACK.—To the extent that the excess described in paragraph (1) arises by reason of a net operating loss carryback, subparagraph (A) of paragraph (1) shall not apply.

“(4) TAXABLE YEAR BEGINNING BEFORE JANUARY 1, 1962.—For purposes of determining the amount of an investment credit carryback that may be added under paragraph (1) for a taxable year beginning before January 1, 1962, and ending after December 31, 1961, the amount of the limitation provided by subsection (a)(2) is the amount which bears the same ratio to such limitation as the number of days in such year after December 31, 1961, bears to the total number of days in such year.

“(c) QUALIFIED INVESTMENT.—

“(1) IN GENERAL.—For purposes of this subpart, the term 'qualified investment' means, with respect to any taxable year, the aggregate of—

“(A) the applicable percentage of the basis of each new section 38 property (as defined in section 48(b)) placed in service by the taxpayer during such taxable year, plus

Post, p. 968.

“(B) the applicable percentage of the cost of each used section 38 property (as defined in section 48(c)(1)) placed in service by the taxpayer during such taxable year.

Post, p. 968.

“(2) APPLICABLE PERCENTAGE.—For purposes of paragraph (1), the applicable percentage for any property shall be determined under the following table:

"If the useful life is—	The applicable percentage is—
4 years or more but less than 6 years.....	33½
6 years or more but less than 8 years.....	66½
8 years or more.....	100

For purposes of this paragraph, the useful life of any property shall be determined as of the time such property is placed in service by the taxpayer.

“(3) PUBLIC UTILITY PROPERTY.—

Ante, p. 962.

“(A) In the case of section 38 property which is public utility property, the amount of the qualified investment shall be $\frac{3}{7}$ of the amount determined under paragraph (1).

“(B) For purposes of subparagraph (A), the term ‘public utility property’ means property used predominantly in the trade or business of the furnishing or sale of—

“(i) electrical energy, water, or sewage disposal services,

“(ii) gas through a local distribution system,

“(iii) telephone service, or

“(iv) telegraph service by means of domestic telegraph operations (as defined in section 222(a)(5) of the Communications Act of 1934, as amended; 47 U.S.C., sec. 222(a)(5)),

57 Stat. 5.

if the rates for such furnishing or sale, as the case may be, have been established or approved by a State or political subdivision thereof, by an agency or instrumentality of the United States, or by a public service or public utility commission or other similar body of any State or political subdivision thereof.

“(4) CERTAIN REPLACEMENT PROPERTY.—For purposes of paragraph (1), if section 38 property is placed in service by the taxpayer to replace property which was—

“(A) destroyed or damaged by fire, storm, shipwreck, or other casualty, or

“(B) stolen,

the basis of such section 38 property (in the case of new section 38 property), or the cost of such section 38 property (in the case of used section 38 property), which (but for this paragraph) would be taken into account under paragraph (1) shall be reduced by an amount equal to the amount received by the taxpayer as compensation, by insurance or otherwise, for the property so destroyed, damaged, or stolen, or to the adjusted basis of such property, whichever is the lesser. No reduction in basis or cost shall be made under the preceding sentence in any case in which the reduction in qualified investment attributable to the substitution required by section 47(a)(1) with respect to the property so destroyed, damaged, or stolen (determined without regard to section 47(a)(4)) is greater than the reduction described in the preceding sentence.

Post, p. 966.

“(d) LIMITATIONS WITH RESPECT TO CERTAIN PERSONS.—

“(1) IN GENERAL.—In the case of—

Post, p. 977.

“(A) an organization to which section 593 applies,

“(B) a regulated investment company or a real estate investment trust subject to taxation under subchapter M (sec. 851 and following), and

“(C) a cooperative organization described in section 1381(a),

the qualified investment and the \$25,000 amount specified under subparagraphs (A) and (B) of subsection (a)(2) shall equal such person's ratable share of such items.

“(2) RATABLE SHARE.—For purposes of paragraph (1), the ratable share of any person for any taxable year of the items described therein shall be—

“(A) in the case of an organization referred to in paragraph (1)(A), 50 percent thereof,

"(B) in the case of a regulated investment company or a real estate investment trust, the ratio (i) the numerator of which is its taxable income and (ii) the denominator of which is its taxable income computed without regard to the deduction for dividends paid provided by section 852(b) (2) (D) or 857(b) (2) (C), as the case may be, and 26 USC 852.

"(C) in the case of a cooperative organization, the ratio (i) the numerator of which is its taxable income and (ii) the denominator of which is its taxable income increased by amounts to which section 1382(b) or (c) applies and similar amounts the tax treatment of which is determined without regard to subchapter T (sec. 1381 and following).

Post, p. 1046.

Post, p. 1045.

For purposes of subparagraph (B) of the preceding sentence, the term 'taxable income' means in the case of a regulated investment company its investment company taxable income (within the meaning of section 852(b) (2)), and in the case of a real estate investment trust its real estate investment trust taxable income (within the meaning of section 857(b) (2)).

SEC. 47. CERTAIN DISPOSITIONS, ETC., OF SECTION 38 PROPERTY. Ante, p. 962.

"(a) **GENERAL RULE.**—Under regulations prescribed by the Secretary or his delegate—

"(1) **EARLY DISPOSITION, ETC.**—If during any taxable year any property is disposed of, or otherwise ceases to be section 38 property with respect to the taxpayer, before the close of the useful life which was taken into account in computing the credit under section 38, then the tax under this chapter for such taxable year shall be increased by an amount equal to the aggregate decrease in the credits allowed under section 38 for all prior taxable years which would have resulted solely from substituting, in determining qualified investment, for such useful life the period beginning with the time such property was placed in service by the taxpayer and ending with the time such property ceased to be section 38 property.

"(2) **PROPERTY BECOMES PUBLIC UTILITY PROPERTY.**—If during any taxable year any property taken into account in determining qualified investment becomes public utility property (within the meaning of section 46(c) (3) (B)), then the tax under this chapter for such taxable year shall be increased by an amount equal to the aggregate decrease in the credits allowed under section 38 for all prior taxable years which would have resulted solely from treating the property, for purposes of determining qualified investment, as public utility property (after giving due regard to the period before such change in use). If the application of this paragraph to any property is followed by the application of paragraph (1) to such property, proper adjustment shall be made in applying paragraph (1).

Ante, p. 965.

"(3) **CARRYBACKS AND CARRYOVERS ADJUSTED.**—In the case of any cessation described in paragraph (1) or any change in use described in paragraph (2), the carrybacks and carryovers under section 46(b) shall be adjusted by reason of such cessation (or change in use).

"(4) **PROPERTY DESTROYED BY CASUALTY, ETC.**—No increase shall be made under paragraph (1) and no adjustment shall be made under paragraph (3) in any case in which—

"(A) any property is disposed of, or otherwise ceases to be section 38 property with respect to the taxpayer, on account of its destruction or damage by fire, storm, shipwreck, or other casualty, or by reason of its theft,

Ante, p. 962.

“(B) section 38 property is placed in service by the taxpayer to replace the property described in subparagraph (A), and

Ante, p. 965.

“(C) the reduction in basis or cost of such section 38 property described in the first sentence of section 46(c)(4) is equal to or; greater than the reduction in qualified investment which (but for this paragraph) would be made by reason of the substitution required by paragraph (1) with respect to the property described in subparagraph (A).

“(b) SECTION NOT TO APPLY IN CERTAIN CASES.—Subsection (a) shall not apply to—

26 USC 381.

“(1) a transfer by reason of death, or

“(2) a transaction to which section 381(a) applies.

For purposes of subsection (a), property shall not be treated as ceasing to be section 38 property with respect to the taxpayer by reason of a mere change in the form of conducting the trade or business so long as the property is retained in such trade or business as section 38 property and the taxpayer retains a substantial interest in such trade or business.

“(c) SPECIAL RULE.—Any increase in tax under subsection (a) shall not be treated as tax imposed by this chapter for purposes of determining the amount of any credit allowable under subpart A.

“SEC. 48. DEFINITIONS; SPECIAL RULES.

“(a) SECTION 38 PROPERTY.—

“(1) IN GENERAL.—Except as provided in this subsection, the term ‘section 38 property’ means—

“(A) tangible personal property, or

“(B) other tangible property (not including a building and its structural components) but only if such property—

“(i) is used as an integral part of manufacturing, production, or extraction or of furnishing transportation, communications, electrical energy, gas, water, or sewage disposal services, or

“(ii) constitutes a research or storage facility used in connection with any of the activities referred to in clause (i).

Such term includes only property with respect to which depreciation (or amortization in lieu of depreciation) is allowable and having a useful life (determined as of the time such property is placed in service) of 4 years or more.

“(2) PROPERTY USED OUTSIDE THE UNITED STATES.—

“(A) IN GENERAL.—Except as provided in subparagraph (B), the term ‘section 38 property’ does not include property which is used predominantly outside the United States.

“(B) EXCEPTIONS.—Subparagraph (A) shall not apply to—

“(i) any aircraft which is registered by the Administrator of the Federal Aviation Agency and which is operated to and from the United States;

“(ii) rolling stock, of a domestic railroad corporation subject to part I of the Interstate Commerce Act, which is used within and without the United States;

“(iii) any vessel documented under the laws of the United States which is operated in the foreign or domestic commerce of the United States;

“(iv) any motor vehicle of a United States person (as defined in section 7701(a)(30)) which is operated to and from the United States;

24 Stat. 379.

49 USC 1

et seq.

Post, p. 988.

“(v) any container of a United States person which is used in the transportation of property to and from the United States; and

“(vi) any property (other than a vessel or an aircraft) of a United States person which is used for the purpose of exploring for, developing, removing, or transporting resources from the outer Continental Shelf (within the meaning of section 2 of the Outer Continental Shelf Lands Act, as amended and supplemented; 43 U.S.C., sec. 1331).

67 Stat. 462.

“(3) **PROPERTY USED FOR LODGING.**—Property which is used predominantly to furnish lodging or in connection with the furnishing of lodging shall not be treated as section 38 property. The preceding sentence shall not apply to—

Ante, p. 962.

“(A) nonlodging commercial facilities which are available to persons not using the lodging facilities on the same basis as they are available to persons using the lodging facilities, and

“(B) property used by a hotel or motel in connection with the trade or business of furnishing lodging where the predominant portion of the accommodations is used by transients.

“(4) **PROPERTY USED BY CERTAIN TAX-EXEMPT ORGANIZATIONS.**—Property used by an organization (other than a cooperative described in section 521) which is exempt from the tax imposed by this chapter shall be treated as section 38 property only if such property is used predominantly in an unrelated trade or business the income of which is subject to tax under section 511.

26 USC 521.

“(5) **PROPERTY USED BY GOVERNMENTAL UNITS.**—Property used by the United States, any State or political subdivision thereof, any international organization, or any agency or instrumentality of any of the foregoing shall not be treated as section 38 property.

“(6) **LIVESTOCK.**—Livestock shall not be treated as section 38 property.

“(b) **NEW SECTION 38 PROPERTY.**—For purposes of this subpart, the term ‘new section 38 property’ means section 38 property—

“(1) the construction, reconstruction, or erection of which is completed by the taxpayer after December 31, 1961, or

“(2) acquired after December 31, 1961, if the original use of such property commences with the taxpayer and commences after such date.

In applying section 46(c) (1) (A) in the case of property described in paragraph (1), there shall be taken into account only that portion of the basis which is properly attributable to construction, reconstruction, or erection after December 31, 1961.

Ante, p. 964.

“(c) **USED SECTION 38 PROPERTY.**—

“(1) **IN GENERAL.**—For purposes of this subpart, the term ‘used section 38 property’ means section 38 property acquired by purchase after December 31, 1961, which is not new section 38 property. Property shall not be treated as ‘used section 38 property’ if, after its acquisition by the taxpayer, it is used by a person who used such property before such acquisition (or by a person who bears a relationship described in section 179(d) (2) (A) or (B) to a person who used such property before such acquisition).

26 USC 179.

“(2) **DOLLAR LIMITATION.**—

“(A) **IN GENERAL.**—The cost of used section 38 property taken into account under section 46(c) (1) (B) for any taxable year shall not exceed \$50,000. If such cost exceeds \$50,000, the taxpayer shall select (at such time and in such manner as the Secretary or his delegate shall by regulations prescribe) the

items to be taken into account, but only to the extent of an aggregate cost of \$50,000. Such a selection, once made, may be changed only in the manner, and to the extent, provided by such regulations.

“(B) MARRIED INDIVIDUALS.—In the case of a husband or wife who files a separate return, the limitation under subparagraph (A) shall be \$25,000 in lieu of \$50,000. This subparagraph shall not apply if the spouse of the taxpayer has no used section 38 property which may be taken into account as qualified investment for the taxable year of such spouse which ends within or with the taxpayer's taxable year.

“(C) AFFILIATED GROUPS.—In the case of an affiliated group, the \$50,000 amount specified under subparagraph (A) shall be reduced for each member of the group by apportioning \$50,000 among the members of such group in accordance with their respective amounts of used section 38 property which may be taken into account.

“(D) PARTNERSHIPS.—In the case of a partnership, the limitation contained in subparagraph (A) shall apply with respect to the partnership and with respect to each partner.

“(3) DEFINITIONS.—For purposes of this subsection—

“(A) PURCHASE.—The term ‘purchase’ has the meaning assigned to such term by section 179(d)(2).

“(B) COST.—The cost of used section 38 property does not include so much of the basis of such property as is determined by reference to the adjusted basis of other property held at any time by the person acquiring such property. If property is disposed of (other than by reason of its destruction or damage by fire, storm, shipwreck, or other casualty, or its theft) and used section 38 property similar or related in service or use is acquired as a replacement therefor in a transaction to which the preceding sentence does not apply, the cost of the used section 38 property acquired shall be its basis reduced by the adjusted basis of the property replaced. The cost of used section 38 property shall not be reduced with respect to the adjusted basis of any property disposed of if, by reason of section 47, such disposition involved an increase of tax or a reduction of the unused credit carrybacks or carryovers described in section 46(b).

“(C) AFFILIATED GROUP.—The term ‘affiliated group’ has the meaning assigned to such term by section 1504(a), except that—

“(i) the phrase ‘more than 50 percent’ shall be substituted for the phrase ‘at least 80 percent’ each place it appears in section 1504(a), and

“(ii) all corporations shall be treated as includible corporations (without any exclusion under section 1504(b)).

“(d) CERTAIN LEASED PROPERTY.—A person (other than a person referred to in section 46(d)) who is a lessor of property may (at such time, in such manner, and subject to such conditions as are provided by regulations prescribed by the Secretary or his delegate) elect with respect to any new section 38 property to treat the lessee as having acquired such property for an amount equal to—

“(1) if such property was constructed by the lessor (or by a corporation which controls or is controlled by the lessor within the meaning of section 368(c)), the fair market value of such property, or

“(2) if paragraph (1) does not apply, the basis of such property to the lessor.

Ante, p. 968.

Ante, pp. 962,
968.

26 USC 179.

Ante, p. 966.

Ante, p. 963.

26 USC 1504.

Ante, p. 965.

26 USC 368.

The election provided by the preceding sentence may be made only with respect to property which would be new section 38 property if acquired by the lessee. For purposes of the preceding sentence and section 46(c), the useful life of property in the hands of the lessee is the useful life of such property in the hands of the lessor. If a lessor makes the election provided by this subsection with respect to any property, the lessee shall be treated for all purposes of this subpart as having acquired such property. If a lessor makes the election provided by this subsection with respect to any property, then, under regulations prescribed by the Secretary or his delegate, subsection (g) shall not apply with respect to such property and the deductions otherwise allowable under section 162 to the lessee for amounts paid to the lessor under the lease shall be adjusted in a manner consistent with the provisions of subsection (g).

Ante, p. 968.

Ante, p. 964.

26 USC 162;

Post, p. 973.

“(e) **SUBCHAPTER S CORPORATIONS.**—In the case of an electing small business corporation (as defined in section 1371)—

“(1) the qualified investment for each taxable year shall be apportioned pro rata among the persons who are shareholders of such corporation on the last day of such taxable year; and

“(2) any person to whom any investment has been apportioned under paragraph (1) shall be treated (for purposes of this subpart) as the taxpayer with respect to such investment, and such investment shall not (by reason of such apportionment) lose its character as an investment in new section 38 property or used section 38 property, as the case may be.

Ante, p. 968

“(f) **ESTATES AND TRUSTS.**—In the case of an estate or trust—

“(1) the qualified investment for any taxable year shall be apportioned between the estate or trust and the beneficiaries on the basis of the income of the estate or trust allocable to each,

“(2) any beneficiary to whom any investment has been apportioned under paragraph (1) shall be treated (for purposes of this subpart) as the taxpayer with respect to such investment, and such investment shall not (by reason of such apportionment) lose its character as an investment in new section 38 property or used section 38 property, as the case may be, and

“(3) the \$25,000 amount specified under subparagraphs (A) and (B) of section 46(a)(2) applicable to such estate or trust shall be reduced to an amount which bears the same ratio to \$25,000 as the amount of the qualified investment allocated to the estate or trust under paragraph (1) bears to the entire amount of the qualified investment.

Ante, p. 963.

“(g) **ADJUSTMENTS TO BASIS OF PROPERTY.**—

“(1) **IN GENERAL.**—The basis of any section 38 property shall be reduced, for purposes of this subtitle other than this subpart, by an amount equal to 7 percent of the qualified investment as determined under section 46(c) with respect to such property.

“(2) **CERTAIN DISPOSITIONS, ETC.**—If the tax under this chapter is increased for any taxable year under paragraph (1) or (2) of section 47(a) or an adjustment in carrybacks or carryovers is made under paragraph (3) of such section, the basis of the property described in such paragraph (1) or (2), as the case may be (immediately before the event on account of which such paragraph (1), (2), or (3) applies), shall be increased by an amount equal to the portion of such increase and the portion of such adjustment attributable to such property.

Ante, p. 966.

“(h) **CROSS REFERENCE.**—

“For application of this subpart to certain acquiring corporations, see section 381(c)(23).”

Post, p. 971.

(c) **DEDUCTION FOR UNUSED CREDIT.**—Part VI of subchapter B of chapter 1 (relating to itemized deductions for individuals and corpo-

26 USC 161-180.

rations) is amended by adding at the end thereof the following new section:

"SEC. 181. DEDUCTION FOR CERTAIN UNUSED INVESTMENT CREDIT.

Ante, p. 963.

"If the amount of the credit determined under section 46(a)(1) for any taxable year exceeds the limitation provided by section 46(a)(2) for such taxable year and if the amount of such excess has not, after the application of section 46(b), been allowed to the taxpayer as a credit under section 38 for any taxable year, then an amount equal to the amount of such excess not so allowed as a credit shall be allowed to the taxpayer as a deduction for the first taxable year following the last taxable year in which such excess could under section 46(b) have been allowed as a credit. If a taxpayer dies or ceases to exist prior to the first taxable year following the last taxable year in which the excess described in the preceding sentence could under section 46(b) have been allowed as a credit, the amount described in the preceding sentence, or the proper portion thereof, shall, under regulations prescribed by the Secretary or his delegate, be allowed to the taxpayer as a deduction for the taxable year in which such death or cessation occurs."

Ante, p. 962.

26 USC 381.

(d) **CERTAIN CORPORATE ACQUISITIONS.**—Section 381(c) (relating to items taken into account in certain corporate acquisitions) is amended by adding at the end thereof the following new paragraph:

"(23) **CREDIT UNDER SECTION 38 FOR INVESTMENT IN CERTAIN DEPRECIABLE PROPERTY.**—The acquiring corporation shall take into account (to the extent proper to carry out the purposes of this section and section 38, and under such regulations as may be prescribed by the Secretary or his delegate) the items required to be taken into account for purposes of section 38 in respect of the distributor or transferor corporation."

(e) **STATUTES OF LIMITATIONS AND INTEREST RELATING TO INVESTMENT CREDIT CARRYBACKS.**—

26 USC 6501.

(1) **ASSESSMENT AND COLLECTION.**—Section 6501 (relating to limitations on assessment and collection) is amended by redesignating subsection (j) as subsection (k), and inserting after subsection (i) the following new subsection:

"(j) **INVESTMENT CREDIT CARRYBACKS.**—In the case of a deficiency attributable to the application to the taxpayer of an investment credit carryback, such deficiency may be assessed at any time before the expiration of the period within which a deficiency for the taxable year of the unused investment credit which results in such carryback may be assessed."

26 USC 6511.

(2) **CREDIT OR REFUND.**—Subsection (d) of section 6511 (relating to limitations on credit or refund) is amended by adding after paragraph (3) thereof the following new paragraph:

"(4) **SPECIAL PERIOD OF LIMITATION WITH RESPECT TO INVESTMENT CREDIT CARRYBACKS.**—

"(A) **PERIOD OF LIMITATION.**—If the claim for credit or refund relates to an overpayment attributable to an investment credit carryback, in lieu of the 3-year period of limitation prescribed in subsection (a), the period shall be that period which ends with the expiration of the 15th day of the 40th month (or 39th month, in the case of a corporation) following the end of the taxable year of the unused investment credit which results in such carryback, or the period prescribed in subsection (c) in respect of such taxable year, whichever expires later. In the case of such a claim, the amount of the credit or refund may exceed the portion of the tax paid within the period provided in subsection (b)(2) or (c), whichever is applicable, to the extent of the amount of the overpayment attributable to such carryback.

“(B) APPLICABLE RULES.—If the allowance of a credit or refund of an overpayment of tax attributable to an investment credit carryback is otherwise prevented by the operation of any law or rule of law other than section 7122, relating to compromises, such credit or refund may be allowed or made, if claim therefor is filed within the period provided in subparagraph (A) of this paragraph. In the case of any such claim for credit or refund, the determination by any court, including the Tax Court, in any proceeding in which the decision of the court has become final, shall not be conclusive with respect to the investment credit, and the effect of such credit, to the extent that such credit is affected by a carryback which was not in issue in such proceeding.”

26 USC 7122.

(3) INTEREST ON UNDERPAYMENTS.—Section 6601(e) (relating to interest on underpayment, nonpayment, or extensions of time for payment, of tax) is amended to read as follows:

“(e) INCOME TAX REDUCED BY CARRYBACK.—

“(1) NET OPERATING LOSS CARRYBACK.—If the amount of any tax imposed by subtitle A is reduced by reason of a carryback of a net operating loss, such reduction in tax shall not affect the computation of interest under this section for the period ending with the last day of the taxable year in which the net operating loss arises.

“(2) INVESTMENT CREDIT CARRYBACK.—If the credit allowed by section 38 for any taxable year is increased by reason of an investment credit carryback, such increase shall not affect the computation of interest under this section for the period ending with the last day of the taxable year in which the investment credit carryback arises.”

(4) INTEREST ON OVERPAYMENTS.—Section 6611(f) (relating to interest on overpayments) is amended to read as follows:

“(f) REFUND OF INCOME TAX CAUSED BY CARRYBACK.—

“(1) NET OPERATING LOSS CARRYBACK.—For purposes of subsection (a), if any overpayment of tax imposed by subtitle A results from a carryback of a net operating loss, such overpayment shall be deemed not to have been made prior to the close of the taxable year in which such net operating loss arises.

“(2) INVESTMENT CREDIT CARRYBACK.—For purposes of subsection (a), if any overpayment of tax imposed by subtitle A results from an investment credit carryback, such overpayment shall be deemed not to have been made prior to the close of the taxable year in which such investment credit carryback arises.”

(f) TECHNICAL AMENDMENT.—Section 1016(a) (relating to adjustments to basis) is amended—

(1) by striking out the period at the end of paragraph (18) and inserting in lieu thereof a semicolon; and

(2) by adding after paragraph (18) the following new paragraph:

“(19) to the extent provided in section 48(g) in the case of property which is or has been section 38 property (as defined in section 48(a));”.

Ante, p. 9

(g) CLERICAL AMENDMENTS.—

(1) Part IV of subchapter A of chapter 1 is amended by inserting after the heading and before the table of sections the following:

26 USC 31-3

“Subpart A. Credits allowable.

“Subpart B. Rules for computing credit for investment in certain depreciable property.

"Subpart A—Credits Allowable"

Ante, p. 962.

(2) The table of sections for part IV of subchapter A of chapter 1 is amended by striking out

"Sec. 38. Overpayments of tax."

and inserting in lieu thereof

"Sec. 38. Investment in certain depreciable property.

"Sec. 39. Overpayments of tax."

Ante, p. 963.

(3) The table of sections for part VI of subchapter B of chapter 1 is amended by adding at the end thereof the following:

"Sec. 181. Deduction for certain unused investment credit."

(h) **EFFECTIVE DATE.**—The amendments made by this section shall apply with respect to taxable years ending after December 31, 1961.

SEC. 3. APPEARANCES, ETC., WITH RESPECT TO LEGISLATION.

26 USC 162.

(a) **IN GENERAL.**—Section 162 (relating to trade or business expenses) is amended by redesignating subsection (e) as subsection (f) and by inserting after subsection (d) the following new subsection:

"(e) **APPEARANCES, ETC., WITH RESPECT TO LEGISLATION.**—

"(1) **IN GENERAL.**—The deduction allowed by subsection (a) shall include all the ordinary and necessary expenses (including, but not limited to, traveling expenses described in subsection (a)(2) and the cost of preparing testimony) paid or incurred during the taxable year in carrying on any trade or business—

"(A) in direct connection with appearances before, submission of statements to, or sending communications to, the committees, or individual members, of Congress or of any legislative body of a State, a possession of the United States, or a political subdivision of any of the foregoing with respect to legislation or proposed legislation of direct interest to the taxpayer, or

"(B) in direct connection with communication of information between the taxpayer and an organization of which he is a member with respect to legislation or proposed legislation of direct interest to the taxpayer and to such organization, and that portion of the dues so paid or incurred with respect to any organization of which the taxpayer is a member which is attributable to the expenses of the activities described in subparagraphs (A) and (B) carried on by such organization.

"(2) **LIMITATION.**—The provisions of paragraph (1) shall not be construed as allowing the deduction of any amount paid or incurred (whether by way of contribution, gift, or otherwise)—

"(A) for participation in, or intervention in, any political campaign on behalf of any candidate for public office, or

"(B) in connection with any attempt to influence the general public, or segments thereof, with respect to legislative matters, elections, or referendums."

(b) **EFFECTIVE DATE.**—The amendments made by this section shall apply to taxable years beginning after December 31, 1962.

SEC. 4. DISALLOWANCE OF CERTAIN ENTERTAINMENT, ETC., EXPENSES.**(a) DENIAL OF DEDUCTION.—**

(1) Part IX of subchapter B of chapter 1 (relating to items not deductible in computing taxable income) is amended by adding at the end thereof the following new section:

“SEC. 274. DISALLOWANCE OF CERTAIN ENTERTAINMENT, ETC., EXPENSES.**“(a) ENTERTAINMENT, AMUSEMENT, OR RECREATION.—**

“(1) IN GENERAL.—No deduction otherwise allowable under this chapter shall be allowed for any item—

“(A) ACTIVITY.—With respect to an activity which is of a type generally considered to constitute entertainment, amusement, or recreation, unless the taxpayer establishes that the item was directly related to, or, in the case of an item directly preceding or following a substantial and bona fide business discussion (including business meetings at a convention or otherwise), that such item was associated with, the active conduct of the taxpayer's trade or business, or

“(B) FACILITY.—With respect to a facility used in connection with an activity referred to in subparagraph (A), unless the taxpayer establishes that the facility was used primarily for the furtherance of the taxpayer's trade or business and that the item was directly related to the active conduct of such trade or business,

and such deduction shall in no event exceed the portion of such item directly related to, or, in the case of an item described in subparagraph (A) directly preceding or following a substantial and bona fide business discussion (including business meetings at a convention or otherwise), the portion of such item associated with, the active conduct of the taxpayer's trade or business.

“(2) SPECIAL RULES.—For purposes of applying paragraph (1)—

“(A) Dues or fees to any social, athletic, or sporting club or organization shall be treated as items with respect to facilities.

“(B) An activity described in section 212 shall be treated as a trade or business.

“(b) GIFTS.—

“(1) LIMITATION.—No deduction shall be allowed under section 162 or section 212 for any expense for gifts made directly or indirectly to any individual to the extent that such expense, when added to prior expenses of the taxpayer for gifts made to such individual during the same taxable year, exceeds \$25. For purposes of this section, the term ‘gift’ means any item excludable from gross income of the recipient under section 102 which is not excludable from his gross income under any other provision of this chapter, but such term does not include—

“(A) an item having a cost to the taxpayer not in excess of \$4.00 on which the name of the taxpayer is clearly and permanently imprinted and which is one of a number of identical items distributed generally by the taxpayer,

“(B) a sign, display rack, or other promotional material to be used on the business premises of the recipient, or

“(C) an item of tangible personal property having a cost to the taxpayer not in excess of \$100 which is awarded to an employee by reason of length of service or for safety achievement.

26 USC 162;
Ante, p. 973.

“(2) SPECIAL RULES.—

“(A) In the case of a gift by a partnership, the limitation contained in paragraph (1) shall apply to the partnership as well as to each member thereof.

“(B) For purposes of paragraph (1), a husband and wife shall be treated as one taxpayer.

“(c) TRAVELING.—In the case of any individual who is traveling away from home in pursuit of a trade or business or in pursuit of an activity described in section 212, no deduction shall be allowed under section 162 or section 212 for that portion of the expenses of such travel otherwise allowable under such section which, under regulations prescribed by the Secretary or his delegate, is not allocable to such trade or business or to such activity. This subsection shall not apply to the expenses of any travel away from home which does not exceed one week or where the portion of the time away from home which is not attributable to the pursuit of the taxpayer's trade or business or an activity described in section 212 is less than 25 percent of the total time away from home on such travel.

“(d) SUBSTANTIATION REQUIRED.—No deduction shall be allowed—

“(1) under section 162 or 212 for any traveling expense (including meals and lodging while away from home),

“(2) for any item with respect to an activity which is of a type generally considered to constitute entertainment, amusement, or recreation, or with respect to a facility used in connection with such an activity, or

“(3) for any expense for gifts, unless the taxpayer substantiates by adequate records or by sufficient evidence corroborating his own statement (A) the amount of such expense or other item, (B) the time and place of the travel, entertainment, amusement, recreation, or use of the facility, or the date and description of the gift, (C) the business purpose of the expense or other item, and (D) the business relationship to the taxpayer of persons entertained, using the facility, or receiving the gift. The Secretary or his delegate may by regulations provide that some or all of the requirements of the preceding sentence shall not apply in the case of an expense which does not exceed an amount prescribed pursuant to such regulations.

“(e) SPECIFIC EXCEPTIONS TO APPLICATION OF SUBSECTION (a).—Subsection (a) shall not apply to—

“(1) BUSINESS MEALS.—Expenses for food and beverages furnished to any individual under circumstances which (taking into account the surroundings in which furnished, the taxpayer's trade, business, or income-producing activity and the relationship to such trade, business, or activity of the persons to whom the food and beverages are furnished) are of a type generally considered to be conducive to a business discussion.

“(2) FOOD AND BEVERAGES FOR EMPLOYEES.—Expenses for food and beverages (and facilities used in connection therewith) furnished on the business premises of the taxpayer primarily for his employees.

“(3) EXPENSES TREATED AS COMPENSATION.—Expenses for goods, services, and facilities, to the extent that the expenses are treated by the taxpayer, with respect to the recipient of the entertainment, amusement, or recreation, as compensation to an employee on the taxpayer's return of tax under this chapter and as wages to such employee for purposes of chapter 24 (relating to withholding of income tax at source on wages).

“(4) REIMBURSED EXPENSES.—Expenses paid or incurred by the taxpayer, in connection with the performance by him of serv-

26 USC 212.

26 USC 162;

Ante, p. 973.

ices for another person (whether or not such other person is his employer), under a reimbursement or other expense allowance arrangement with such other person, but this paragraph shall apply—

“(A) where the services are performed for an employer, only if the employer has not treated such expenses in the manner provided in paragraph (3), or

“(B) where the services are performed for a person other than an employer, only if the taxpayer accounts (to the extent provided by subsection (d)) to such person.

“(5) RECREATIONAL, ETC., EXPENSES FOR EMPLOYEES.—Expenses for recreational, social, or similar activities (including facilities therefor) primarily for the benefit of employees (other than employees who are officers, shareholders or other owners, or highly compensated employees). For purposes of this paragraph, an individual owning less than a 10-percent interest in the taxpayer's trade or business shall not be considered a shareholder or other owner, and for such purposes an individual shall be treated as owning any interest owned by a member of his family (within the meaning of section 267(c)(4)). 26 USC 267.

“(6) EMPLOYEE, STOCKHOLDER, ETC., BUSINESS MEETINGS.—Expenses incurred by a taxpayer which are directly related to business meetings of his employees, stockholders, agents, or directors.

“(7) MEETINGS OF BUSINESS LEAGUES, ETC.—Expenses directly related and necessary to attendance at a business meeting or convention of any organization described in section 501(c)(6) (relating to business leagues, chambers of commerce, real estate boards, and boards of trade) and exempt from taxation under section 501(a). 26 USC 501.

“(8) ITEMS AVAILABLE TO PUBLIC.—Expenses for goods, services, and facilities made available by the taxpayer to the general public.

“(9) ENTERTAINMENT SOLD TO CUSTOMERS.—Expenses for goods or services (including the use of facilities) which are sold by the taxpayer in a bona fide transaction for an adequate and full consideration in money or money's worth.

For purposes of this subsection, any item referred to in subsection (a) shall be treated as an expense.

“(f) INTEREST, TAXES, CASUALTY LOSSES, ETC.—This section shall not apply to any deduction allowable to the taxpayer without regard to its connection with his trade or business (or with his income-producing activity). In the case of a taxpayer which is not an individual, the preceding sentence shall be applied as if it were an individual.

“(g) TREATMENT OF ENTERTAINMENT, ETC., TYPE FACILITY.—For purposes of this chapter, if deductions are disallowed under subsection (a) with respect to any portion of a facility, such portion shall be treated as an asset which is used for personal, living, and family purposes (and not as an asset used in the trade or business).

“(h) REGULATORY AUTHORITY.—The Secretary or his delegate shall prescribe such regulations as he may deem necessary to carry out the purposes of this section, including regulations prescribing whether subsection (a) or subsection (b) applies in cases where both such subsections would otherwise apply.”

(2) The table of sections for such part IX is amended by Ante, p. 974. adding at the end thereof the following:

“Sec. 274. Disallowance of certain entertainment, etc., expenses.”

(b) TRAVELING EXPENSES.—Section 162(a)(2) (relating to traveling expenses) is amended by striking out “(including the entire 26 USC 162.

amount expended for meals and lodging)" and inserting in lieu thereof "(including amounts expended for meals and lodging other than amounts which are lavish or extravagant under the circumstances)".

(c) **EFFECTIVE DATE.**—The amendments made by this section shall apply with respect to taxable years ending after December 31, 1962, but only in respect of periods after such date.

SEC. 5. AMOUNT OF DISTRIBUTION WHERE CERTAIN FOREIGN CORPORATIONS DISTRIBUTE PROPERTY IN KIND.

(a) **AMOUNT DISTRIBUTED.**—Section 301(b)(1) (relating to amount distributed to corporate distributees) is amended by adding at the end thereof the following new subparagraph:

"(C) **CERTAIN CORPORATE DISTRIBUTEES OF FOREIGN CORPORATION.**—Notwithstanding subparagraph (B), if the shareholder is a corporation and the distributing corporation is a foreign corporation, the amount taken into account with respect to property (other than money) shall be the fair market value of such property; except that if any deduction is allowable under section 245 with respect to such distribution, then the amount taken into account shall be the sum (determined under regulations prescribed by the Secretary or his delegate) of—

"(i) the proportion of the adjusted basis of such property (or, if lower, its fair market value) properly attributable to gross income from sources within the United States, and

"(ii) the proportion of the fair market value of such property properly attributable to gross income from sources without the United States."

(b) **BASIS.**—Section 301(d) (relating to basis of property) is amended by adding at the end thereof the following new paragraph:

"(3) **CERTAIN CORPORATE DISTRIBUTEES OF FOREIGN CORPORATION.**—In the case of property described in subparagraph (C) of subsection (b)(1), the basis shall be determined by substituting the amount determined under such subparagraph (C) for the amount described in paragraph (2) of this subsection."

(c) **DIVIDENDS RECEIVED FROM CERTAIN FOREIGN CORPORATIONS.**—

(1) Section 245 (relating to dividends received from certain foreign corporations) is amended by adding at the end thereof the following new subsection:

"(b) **PROPERTY DISTRIBUTIONS.**—For purposes of subsection (a), the amount of any distribution of property other than money shall be the amount determined by applying section 301(b)(1)(B)."

(2) Section 245 is amended by striking out "In the case of" and inserting in lieu thereof "(a) **GENERAL RULE.**—In the case of".

(d) **EFFECTIVE DATE.**—The amendments made by this section shall apply to distributions made after December 31, 1962.

SEC. 6. MUTUAL SAVINGS BANKS, ETC.

(a) **RESERVES FOR LOSSES ON LOANS.**—Section 593 is amended to read as follows:

"SEC. 593. RESERVES FOR LOSSES ON LOANS.

"(a) **ORGANIZATIONS TO WHICH SECTION APPLIES.**—This section shall apply to any mutual savings bank not having capital stock represented by shares, domestic building and loan association, or cooperative bank without capital stock organized and operated for mutual purposes and without profit.

26 USC 301;
Post, p. 1035.

26 USC 245.

26 USC 301;
Post, p. 1035.

“(b) ADDITION TO RESERVES FOR BAD DEBTS.—

“(1) IN GENERAL.—For purposes of section 166(c), the reasonable addition for the taxable year to the reserve for bad debts of any taxpayer described in subsection (a) shall be an amount equal to the sum of—

26 USC 166.

“(A) the amount determined under section 166(c) to be a reasonable addition to the reserve for losses on nonqualifying loans, plus

“(B) the amount determined by the taxpayer to be a reasonable addition to the reserve for losses on qualifying real property loans, but such amount shall not exceed the amount determined under paragraph (2), (3), or (4), whichever amount is the largest, but the amount determined under this subparagraph shall in no case be greater than the larger of—

“(i) the amount determined under paragraph (4), or

“(ii) the amount which, when added to the amount determined under subparagraph (A), equals the amount by which 12 percent of the total deposits or withdrawable accounts of depositors of the taxpayer at the close of such year exceeds the sum of its surplus, undivided profits, and reserves at the beginning of such year (taking into account any portion thereof attributable to the period before the first taxable year beginning after December 31, 1951).

“(2) PERCENTAGE OF TAXABLE INCOME METHOD.—The amount determined under this paragraph for the taxable year shall be the excess of—

“(A) an amount equal to 60 percent of the taxable income for such year, over

“(B) the amount referred to in paragraph (1)(A) for such year,

but the amount determined under this paragraph shall not exceed the amount necessary to increase the balance (as of the close of the taxable year) of the reserve for losses on qualifying real property loans to 6 percent of such loans outstanding at such time. For purposes of this paragraph, taxable income shall be computed (i) by excluding from gross income any amount included therein by reason of subsection (f), and (ii) without regard to any deduction allowable for any addition to the reserve for bad debts.

“(3) PERCENTAGE OF REAL PROPERTY LOANS METHOD.—The amount determined under this paragraph for the taxable year shall be an amount equal to the amount necessary to increase the balance (as of the close of the taxable year) of the reserve for losses on qualifying real property loans to an amount equal to—

“(A) 3 percent of such loans outstanding at such time, plus

“(B) in the case of a taxpayer which is a new company and which does not have capital stock with respect to which distributions of property (as defined in section 317(a)) are not allowable as a deduction under section 591, an amount equal to—

26 USC 317.

26 USC 591;

Post, p. 984.

“(i) 2 percent of so much of the amount of such loans outstanding at such time as does not exceed \$4,000,000, reduced (but not below zero) by

“(ii) the amount, if any, of the balance (as of the close of such taxable year) of the taxpayer's supplemental reserve for losses on loans.

For purposes of subparagraph (B), a taxpayer is a new company for any taxable year only if such taxable year begins not more than 10 years after the first day on which it (or any predecessor) was authorized to do business as an organization described in subsection (a).

26 USC 166.

“(4) **EXPERIENCE METHOD.**—The amount determined under this paragraph for the taxable year shall be an amount equal to the amount determined under section 166(c) (without regard to this subsection) to be a reasonable addition to the reserve for losses on qualifying real property loans.

Post, p. 983.
Post, p. 992.

“(5) **LIMITATION IN CASE OF CERTAIN DOMESTIC BUILDING AND LOAN ASSOCIATIONS.**—If the percentage of the assets of a domestic building and loan association which are not assets described in section 7701(a)(19)(D)(ii) exceeds 36 percent for the taxable year (as determined for purposes of section 7701(a)(19) for such year), the amount determined under paragraph (2), and the amount determined under paragraph (3), shall in each case be the amount (determined without regard to this paragraph but with regard to the limits contained in paragraphs (2), (3), and (1)(B)) reduced by the amount determined under the following table:

If the percentage exceeds—	but does not exceed—	the reduction shall be the following proportion of the amount so determined without regard to this paragraph—
36 percent.	37 percent.	1/12
37 percent.	38 percent.	1/6
38 percent.	39 percent.	1/4
39 percent.	40 percent.	1/3
40 percent.	41 percent.	5/12

“(c) **TREATMENT OF RESERVES FOR BAD DEBTS.**—

“(1) **ESTABLISHMENT OF RESERVES.**—Each taxpayer described in subsection (a) which uses the reserve method of accounting for bad debts shall establish and maintain a reserve for losses on qualifying real property loans, a reserve for losses on nonqualifying loans, and a supplemental reserve for losses on loans. For purposes of this title, such reserves shall be treated as reserves for bad debts, but no deduction shall be allowed for any addition to the supplemental reserve for losses on loans.

“(2) **ALLOCATION OF PRE-1963 RESERVES.**—For purposes of this section, the pre-1963 reserves shall, as of the close of December 31, 1962, be allocated to, and constitute the opening balance of—

“(A) the reserve for losses on nonqualifying loans,

“(B) the reserve for losses on qualifying real property loans, and

“(C) the supplemental reserve for losses on loans.

“(3) **METHOD OF ALLOCATION.**—The allocation provided by paragraph (2) shall be made—

“(A) first, to the reserve described in paragraph (2)(A), to the extent such reserve is not increased above the amount which would be a reasonable addition under section 166(c) for a period in which the nonqualifying loans increased from zero to the amount thereof outstanding at the close of December 31, 1962;

“(B) second, to the reserve described in paragraph (2)(B), to the extent such reserve is not increased above the amount which would be determined under paragraph (3)(A) or (4) of subsection (b) (whichever such amount is the larger) for a period in which the qualifying real property loans increased

from zero to the amount thereof outstanding at the close of December 31, 1962; and

“(C) then to the supplemental reserve for losses on loans.

“(4) **PRE-1963 RESERVES DEFINED.**—For purposes of this subsection, the term ‘pre-1963 reserves’ means the net amount, determined as of the close of December 31, 1962 (after applying subsection (d)(1)), accumulated in the reserve for bad debts pursuant to section 166(c) (or the corresponding provisions of prior revenue laws) for taxable years beginning after December 31, 1951. 26 USC 166.

“(5) **CERTAIN PRE-1952 SURPLUS.**—If after the application of paragraph (3), the opening balance of the reserve described in paragraph (2)(B) is less than the amount described in paragraph (3)(B), then, for purposes of this subsection, the term ‘pre-1963 reserves’ includes so much of the surplus, undivided profits, and bad debt reserves (determined as of December 31, 1962) attributable to the period before the first taxable year beginning after December 31, 1951, as does not exceed the amount by which such opening balance is less than the amount described in paragraph (3)(B). For purposes of the preceding sentence, the surplus, undivided profits, and bad debt reserves attributable to the period before the first taxable year beginning after December 31, 1951, shall be reduced by the amount thereof which is attributable to interest which would have been excludable from gross income under section 22(b)(4) of the Internal Revenue Code of 1939 (relating to interest on governmental obligations) or the corresponding provisions of prior laws. Notwithstanding the second sentence of paragraph (1), any amount which, by reason of the application of the first sentence of this paragraph, is allocated to the reserve described in paragraph (2)(B) shall not be treated as a reserve for bad debts for any purpose other than determining the amount referred to in subsection (b)(1)(B), and for such purpose such amount shall be treated as remaining in such reserve. 53 Stat. 10.

“(6) **CHARGING OF BAD DEBTS TO RESERVES.**—Any debt becoming worthless or partially worthless in respect of a qualifying real property loan shall be charged to the reserve for losses on such loans, and any debt becoming worthless or partially worthless in respect of a nonqualifying loan shall be charged to the reserve for losses on nonqualifying loans; except that any such debt may, at the election of the taxpayer, be charged in whole or in part to the supplemental reserve for losses on loans.

“(d) **TAXABLE YEARS BEGINNING IN 1962 AND ENDING IN 1963.**—In the case of a taxable year beginning before January 1, 1963, and ending after December 31, 1962, of a taxpayer described in subsection (a) which uses the reserve method of accounting for bad debts, the taxable income shall be the sum of—

“(1) that portion of the taxable income allocable to the part of the taxable year occurring before January 1, 1963, reduced by the amount of the deduction for an addition to a reserve for bad debts which would be allowable under section 166(c) (without regard to the amendments made by section 6 of the Revenue Act of 1962) if such part year constituted a taxable year, plus

“(2) that portion of the taxable income allocable to the part of the taxable year occurring after December 31, 1962, reduced by the amount of the deduction for an addition to a reserve for bad debts which would be allowed under section 166(c) (taking into account the amendments made by section 6 of the Revenue Act of 1962) if such part year constituted a taxable year.

26 USC 166.

For purposes of the preceding sentence, the taxable income shall be determined without regard to any deduction under section 166(c), and the portion thereof allocable to each part year shall be determined on the basis of the ratio which the number of days in such part year bears to the number of days in the entire taxable year.

“(e) LOANS DEFINED.—For purposes of this section—

“(1) QUALIFYING REAL PROPERTY LOANS.—The term ‘qualifying real property loan’ means any loan secured by an interest in improved real property or secured by an interest in real property which is to be improved out of the proceeds of the loan, but such term does not include—

26 USC 165.

“(A) any loan evidenced by a security (as defined in section 165(g)(2)(C));

“(B) any loan, whether or not evidenced by a security (as defined in section 165(g)(2)(C)), the primary obligor on which is—

“(i) a government or political subdivision or instrumentality thereof;

“(ii) a bank (as defined in section 581); or

“(iii) another member of the same affiliated group;

“(C) any loan, to the extent secured by a deposit in or share of the taxpayer; or

“(D) any loan which, within a 60-day period beginning in one taxable year of the creditor and ending in its next taxable year, is made or acquired and then repaid or disposed of, unless the transactions by which such loan was made or acquired and then repaid or disposed of are established to be for bona fide business purposes.

26 USC 1504.

For purposes of subparagraph (B) (iii), the term ‘affiliated group’ has the meaning assigned to such term by section 1504(a); except that (i) the phrase ‘more than 50 percent’ shall be substituted for the phrase ‘at least 80 percent’ each place it appears in section 1504(a), and (ii) all corporations shall be treated as includible corporations (without any exclusion under section 1504(b)).

“(2) NONQUALIFYING LOANS.—The term ‘nonqualifying loan’ means any loan which is not a qualifying real property loan.

“(3) LOAN.—The term ‘loan’ means debt, as the term ‘debt’ is used in section 166.

“(f) DISTRIBUTIONS TO SHAREHOLDERS.—

26 USC 317.

“(1) IN GENERAL.—For purposes of this chapter, any distribution of property (as defined in section 317(a)) by a domestic building and loan association to a shareholder with respect to its stock, if such distribution is not allowable as a deduction under section 591, shall be treated as made—

“(A) first out of its earnings and profits accumulated in taxable years beginning after December 31, 1951, to the extent thereof,

“(B) then out of the reserve for losses on qualifying real property loans, to the extent additions to such reserve exceed the additions which would have been allowed under subsection (b) (4),

“(C) then out of the supplemental reserve for losses on loans, to the extent thereof,

“(D) then out of such other accounts as may be proper.

This paragraph shall apply in the case of any distribution in redemption of stock or in partial or complete liquidation of the association, except that any such distribution shall be treated as made first out of the amount referred to in subparagraph (B), second out of the amount referred to in subparagraph (C), third

out of the amount referred to in subparagraph (A), and then out of such other accounts as may be proper.

"(2) AMOUNTS CHARGED TO RESERVE ACCOUNTS AND INCLUDED IN GROSS INCOME.—If any distribution is treated under paragraph (1) as having been made out of the reserves described in subparagraphs (B) and (C) of such paragraph, the amount charged against such reserve shall be the amount which, when reduced by the amount of tax imposed under this chapter and attributable to the inclusion of such amount in gross income, is equal to the amount of such distribution; and the amount so charged against such reserve shall be included in gross income of the taxpayer.

"(3) SPECIAL RULES.—

"(A) For purposes of paragraph (1)(B), additions to the reserve for losses on qualifying real property loans for the taxable year in which the distribution occurs shall be taken into account.

"(B) For purposes of computing under this section the amount of a reasonable addition to the reserve for losses on qualifying real property loans for any taxable year, any amount charged during any year to such reserve pursuant to the provisions of paragraph (2) shall not be taken into account."

(b) FORECLOSURE ON PROPERTY SECURING LOANS.—Part II of subchapter H of chapter 1 (relating to mutual savings banks, etc.) is amended by adding at the end thereof the following new section: 26 USC 591-594.

"SEC. 595. FORECLOSURE ON PROPERTY SECURING LOANS.

"(a) NONRECOGNITION OF GAIN OR LOSS AS A RESULT OF FORECLOSURE.—In the case of a creditor which is an organization described in section 593(a), no gain or loss shall be recognized, and no debt shall be considered as becoming worthless or partially worthless, as the result of such organization having bid in at foreclosure, or having otherwise reduced to ownership or possession by agreement or process of law, any property which was security for the payment of any indebtedness. Ante, p. 977.

"(b) CHARACTER OF PROPERTY.—For purposes of sections 166 and 1221, any property acquired in a transaction with respect to which gain or loss to an organization was not recognized by reason of subsection (a) shall be considered as property having the same characteristics as the indebtedness for which such property was security. Any amount realized by such organization with respect to such property shall be treated for purposes of this chapter as a payment on account of such indebtedness, and any loss with respect thereto shall be treated as a bad debt to which the provisions of section 166 (relating to allowance of a deduction for bad debts) apply. 26 USC 166, 1221.

"(c) BASIS.—The basis of any property to which subsection (a) applies shall be the basis of the indebtedness for which such property was security (determined as of the date of the acquisition of such property), properly increased for costs of acquisition.

"(d) REGULATORY AUTHORITY.—The Secretary or his delegate shall prescribe such regulations as he may deem necessary to carry out the purposes of this section."

(c) DEFINITION OF DOMESTIC BUILDING AND LOAN ASSOCIATION.—Paragraph (19) of section 7701(a) (definition of domestic building and loan association) is amended to read as follows:

"(19) DOMESTIC BUILDING AND LOAN ASSOCIATION.—The term 'domestic building and loan association' means a domestic building and loan association, a domestic savings and loan association, and a Federal savings and loan association—

48 Stat. 1255.

“(A) which either (i) is an insured institution within the meaning of section 401(a) of the National Housing Act (12 U.S.C., sec. 1724(a)), or (ii) is subject by law to supervision and examination by State or Federal authority having supervision over such associations;

“(B) substantially all of the business of which consists of acquiring the savings of the public and investing in loans described in subparagraph (C);

“(C) at least 90 percent of the amount of the total assets of which (as of the close of the taxable year) consists of (i) cash, (ii) obligations of the United States or of a State or political subdivision thereof, stock or obligations of a corporation which is an instrumentality of the United States or of a State or political subdivision thereof, and certificates of deposit in, or obligations of, a corporation organized under a State law which specifically authorizes such corporation to insure the deposits or share accounts of member associations, (iii) loans secured by an interest in real property and loans made for the improvement of real property, (iv) loans secured by a deposit or share of a member, (v) property acquired through the liquidation of defaulted loans described in clause (iii), and (vi) property used by the association in the conduct of the business described in subparagraph (B);

“(D) of the assets of which taken into account under subparagraph (C) as assets constituting the 90 percent of total assets—

“(i) at least 80 percent of the amount of such assets consists of assets described in clauses (i), (ii), (iv), and (vi) of such subparagraph and of loans secured by an interest in real property which is (or, from the proceeds of the loan, will become) residential real property or real property used primarily for church purposes, loans made for the improvement of residential real property or real property used primarily for church purposes, or property acquired through the liquidation of defaulted loans described in this clause; and

“(ii) at least 60 percent of the amount of such assets consists of assets described in clauses (i), (ii), (iv), and (vi) of such subparagraph and of loans secured by an interest in real property which is (or, from the proceeds of the loan, will become) residential real property containing 4 or fewer family units or real property used primarily for church purposes, loans made for the improvement of residential real property containing 4 or fewer family units or real property used primarily for church purposes, or property acquired through the liquidation of defaulted loans described in this clause;

“(E) not more than 18 percent of the amount of the total assets of which (as of the close of the taxable year) consists of assets other than those described in clause (i) of subparagraph (D), and not more than 36 percent of the amount of the total assets of which (as of the close of the taxable year) consists of assets other than those described in clause (ii) of subparagraph (D); and

“(F) except for property described in subparagraph (C), not more than 3 percent of the assets of which consists of stock of any corporation.

The term 'domestic building and loan association' also includes any association which, for the taxable year, would satisfy the requirements of the first sentence of this paragraph if '41 percent' were substituted for '36 percent' in subparagraph (E). Except in the case of the taxpayer's first taxable year beginning after the date of the enactment of the Revenue Act of 1962, the second sentence of this paragraph shall not apply to an association for the taxable year unless such association (i) was a domestic building and loan association within the meaning of the first sentence of this paragraph for the first taxable year preceding the taxable year, or (ii) was a domestic building and loan association solely by reason of the second sentence of this paragraph for the first taxable year preceding the taxable year (but not for the second preceding taxable year). At the election of the taxpayer, the percentages specified in this paragraph shall be applied on the basis of the average assets outstanding during the taxable year, in lieu of the close of the taxable year, computed under regulations prescribed by the Secretary or his delegate."

(d) CLERICAL AMENDMENTS.—The table of sections for part II of subchapter H of chapter 1 is amended—

26 USC 591-
594.

(1) by striking out the third item and inserting in lieu thereof the following:

"Sec. 593. Reserves for losses on loans."

and

(2) by adding at the end thereof the following:

"Sec. 595. Foreclosure on property securing loans."

(e) REPEAL OF EXEMPTION FROM CERTAIN TAXES.—

(1) AMENDMENT TO HOME OWNERS' LOAN ACT OF 1933.—Section 5(h) of the Home Owners' Loan Act of 1933, as amended (12 U.S.C. sec. 1464(h)), is amended to read as follows:

48 Stat. 133;
65 Stat. 490.

"(h) No State, county, municipal, or local taxing authority shall impose any tax on such associations or their franchise, capital, reserves, surplus, loans, or income greater than that imposed by such authority on other similar local mutual or cooperative thrift and home financing institutions."

(2) CERTAIN DOCUMENTARY STAMP TAXES.—Section 4382(a) (2) (relating to exemptions from documentary stamp taxes) is amended to read as follows:

26 USC 4382.

"(2) DOMESTIC BUILDING AND LOAN ASSOCIATIONS AND MUTUAL DITCH OR IRRIGATION COMPANIES.—Shares or certificates of stock issued by domestic building and loan associations and cooperative banks, to the extent such shares or certificates represent deposits or withdrawable accounts; or shares or certificates of stock and certificates of indebtedness issued by mutual ditch or irrigation companies."

(f) DEDUCTION FOR DIVIDENDS OR INTEREST PAID ON DEPOSITS.—Section 591 (relating to deduction for dividends paid on deposits) is amended—

(1) by striking out "and domestic building and loan associations" and inserting in lieu thereof the following: "domestic building and loan associations, and other savings institutions chartered and supervised as savings and loan or similar associations under Federal or State law"; and

(2) by inserting after "dividends" the following: "or interest".

(g) EFFECTIVE DATES.—

(1) The amendment made by subsection (a) shall apply to taxable years ending after December 31, 1962, except that section 593(f) of the Internal Revenue Code of 1954 shall apply to dis-

Ante, p. 981.

tributions after December 31, 1962, in taxable years ending after such date.

(2) The amendment made by subsection (b) shall apply to transactions described in section 595(a) of the Internal Revenue Code of 1954 occurring after December 31, 1962, in taxable years ending after such date.

(3) The amendment made by subsection (c) shall apply to taxable years beginning after the date of the enactment of this Act.

(4) Subsection (e) of this section shall become effective on January 1, 1963, except that—

(A) in the case of the tax imposed by section 4251 of the Internal Revenue Code of 1954, such subsection shall apply only with respect to amounts paid pursuant to bills rendered after December 31, 1962; and

(B) in the case of the tax imposed by section 4261 of such Code, such subsection shall apply only with respect to transportation beginning after December 31, 1962.

SEC. 7. DISTRIBUTIONS BY FOREIGN TRUSTS.

(a) DEFINITIONS.—

(1) INCOME OF FOREIGN TRUST.—Section 643(a)(6) (relating to modifications taken into account in computing distributable net income) is amended to read as follows:

“(6) INCOME OF FOREIGN TRUST.—In the case of a foreign trust—

“(A) There shall be included the amounts of gross income from sources without the United States, reduced by any amounts which would be deductible in respect of disbursements allocable to such income but for the provisions of section 265(1) (relating to disallowance of certain deductions).

“(B) Gross income from sources within the United States shall be determined without regard to section 894 (relating to income exempt under treaty).

“(C) Paragraph (3) shall not apply to a foreign trust created by a United States person. In the case of such a trust, (i) there shall be included gains from the sale or exchange of capital assets, reduced by losses from such sales or exchanges to the extent such losses do not exceed gains from such sales or exchanges, and (ii) the deduction under section 1202 (relating to deduction for excess of capital gains over capital losses) shall not be taken into account.”

(2) FOREIGN TRUSTS.—Section 643 (relating to definitions) amended by adding at the end thereof the following new subsection:

“(d) FOREIGN TRUSTS CREATED BY UNITED STATES PERSONS.—For purposes of this part, the term ‘foreign trust created by a United States person’ means that portion of a foreign trust (as defined in section 7701(a)(31)) attributable to money or property transferred directly or indirectly by a United States person (as defined in section 7701(a)(30)), or under the will of a decedent who at the date of his death was a United States citizen or resident.”

(b) ACCUMULATION DISTRIBUTIONS OF FOREIGN TRUSTS.—

(1) Section 665(b) (relating to definitions applicable to subpart D) is amended by striking out “(b) ACCUMULATION DISTRIBUTION.—For purposes of this subpart,” and inserting in lieu thereof the following:

“(b) ACCUMULATION DISTRIBUTIONS OF TRUSTS OTHER THAN CERTAIN FOREIGN TRUSTS.—For purposes of this subpart, in the case of

Ante, p. 982.

26 USC 4251.

Post, p. 988.

Post, p. 988.

a trust (other than a foreign trust created by a United States person).”

(2) Section 665 is amended by redesignating subsections (c) and (d) as (d) and (e), respectively, and by inserting after subsection (b) the following new subsection:

26 USC 665.

“(c) ACCUMULATION DISTRIBUTION OF CERTAIN FOREIGN TRUSTS.—For purposes of this subpart, in the case of a foreign trust created by a United States person, the term ‘accumulation distribution’ for any taxable year of the trust means the amount by which the amounts specified in paragraph (2) of section 661(a) for such taxable year exceed distributable net income, reduced by the amounts specified in paragraph (1) of section 661(a). For purposes of this subsection, the amount specified in paragraph (2) of section 661(a) shall be determined without regard to section 666. Any amount paid to a United States person which is from a payor who is not a United States person and which is derived directly or indirectly from a foreign trust created by a United States person shall be deemed in the year of payment to have been directly paid by the foreign trust.”

(c) ALLOCATION OF ACCUMULATION DISTRIBUTIONS TO PRECEDING YEARS.—Section 666(a) (relating to accumulation distribution allocated to 5 preceding years) is amended—

26 USC 666.

(1) by striking out “(a) AMOUNT ALLOCATED.—In the case of a trust” and inserting in lieu thereof the following:

“(a) AMOUNT ALLOCATED.—In the case of a trust (other than a foreign trust created by a United States person)” ; and

(2) by adding at the end thereof the following new sentence:

“In the case of a foreign trust created by a United States person, this subsection shall apply to the preceding taxable years of the trust without regard to any provision of the preceding sentences which would (but for this sentence) limit its application to the 5 preceding taxable years.”

(d) AMOUNTS TREATED AS RECEIVED IN PRIOR YEARS.—Section 668(a) (relating to amounts treated as received in prior taxable years) is amended by adding at the end thereof the following new sentence: “Except as provided in section 669, in the case of a foreign trust created by a United States person the preceding sentence shall not apply to any beneficiary who is a United States person.”

(e) SPECIAL RULES FOR FOREIGN TRUSTS.—Subpart D of part I of subchapter J of chapter 1 (relating to treatment of excess distributions by trusts) is amended by adding at the end thereof the following new section:

26 USC 665-668.

SEC. 669. SPECIAL RULES APPLICABLE TO CERTAIN FOREIGN TRUSTS.

“(a) LIMITATION ON TAX.—

“(1) GENERAL RULE.—At the election of a beneficiary who is a United States person (as defined in section 7701(a)(30)) and who satisfies the requirements of subsection (b), the tax attributable to the amounts treated under section 668(a) as having been received by him from a foreign trust created by a United States person on the last day of a preceding taxable year of the trust shall not be greater than—

Post, p. 988.

“(A) the tax determined under the next to the last sentence of section 668(a), or

“(B) the tax determined by multiplying by the number of preceding taxable years of the trust, on the last day of each of which an amount is deemed under section 666(a) to have been distributed, the average of the increase in tax attributable to recomputing the beneficiary’s gross income for the taxable year and each of his 2 taxable years immediately preceding

Supra.

26 USC 668;
Ante, p. 986.

the year of the accumulation distribution by adding to the income of each of such years an amount determined by dividing the amount required to be included in income under section 668(a) by such number of preceding taxable years of the trust. The recomputation for the taxable year shall be made without regard to the inclusion in income required by section 668(a) of any amount other than pursuant to this paragraph.

“(2) EXCEPTIONS.—

26 USC 666;
Ante, p. 986.

“(A) When an accumulation distribution is deemed under section 666(a) to have been distributed on the last day of less than 3 taxable years of the trust, the taxable years of the beneficiary for which a recomputation is made under subsection (a)(1)(B) shall equal the number of years to which section 666(a) applies, commencing with the most recent taxable year of the beneficiary.

“(B) If a beneficiary was not alive on the last day of each preceding taxable year of the trust with respect to which a distribution is deemed made under section 666(a), paragraph (1)(A) of this subsection shall not apply. In applying paragraph (1)(B) of this subsection, no recomputation shall be made for a beneficiary for a taxable year for which he was not alive; if he has no preceding taxable year, the recomputation shall be made on the basis of his taxable year without regard to the inclusion in income required by section 668(a) of any amount other than pursuant to paragraph (1)(B).

“(3) EFFECT OF PRIOR ELECTION.—In computing the limitation on tax under paragraph (1) of this subsection for any beneficiary—

“(A) SUBSEQUENT ELECTION UNDER PARAGRAPH (1)(A).—If an election has been made under paragraph (1)(B) of this subsection, for purposes of a subsequent election under paragraph (1)(A) the income of any year with respect to which an amount is deemed distributed to a beneficiary under section 666(a) shall include amounts previously deemed distributed to such beneficiary for such year as a result of an accumulation distribution with respect to which an election under paragraph (1)(B) was made.

“(B) SUBSEQUENT ELECTION UNDER PARAGRAPH (1)(B).—If with respect to an accumulation distribution an election has been made under either paragraph (1)(A) or paragraph (1)(B) of this subsection, or the next to the last sentence of section 668(a) has applied, for purposes of a subsequent election under paragraph (1)(B) the number of preceding taxable years of the trust with respect to which an amount is deemed distributed to a beneficiary under section 666(a) shall be determined without regard to any such year with respect to which an amount was previously deemed distributed to such beneficiary.

“(b) INFORMATION REQUIREMENT.—The election of a beneficiary to apply the limitations on tax provided in subsection (a) of this section shall not be effective unless the beneficiary at the time of making the election supplies such information with respect to the operation and accounts of the trust, for each taxable year on the last day of which an amount is deemed distributed under section 666(a), as the Secretary or his delegate may by regulations prescribe.”

(f) INFORMATION RETURNS WITH RESPECT TO FOREIGN TRUSTS.—Subpart B of part III of subchapter A of chapter 61 (relating to infor-

mation concerning transactions with other persons) is amended by adding at the end thereof the following new section:

"SEC. 6048. RETURNS AS TO CREATION OF OR TRANSFERS TO CERTAIN FOREIGN TRUSTS.

"(a) GENERAL RULE.—On or before the 90th day after—

"(1) the creation of any foreign trust by a United States person,

or

"(2) the transfer of any money or property to a foreign trust by a United States person,

the grantor in the case of an inter vivos trust, the fiduciary of an estate in the case of a testamentary trust, or the transferor, as the case may be, shall make a return in compliance with the provisions of subsection (b).

"(b) FORM AND CONTENTS OF RETURNS.—The returns required by subsection (a) shall be in such form and shall set forth, in respect of the foreign trust, such information as the Secretary or his delegate prescribes by regulation as necessary for carrying out the provisions of the income tax laws.

"(c) CROSS REFERENCES.—

"(1) For provisions relating to penalties for violations of this section, see sections 6677 and 7203.

"(2) For definition of the term 'foreign trust created by a United States person', see section 643(d)."

Infra; 26 USC 7203.

Ante, p. 985.

(g) FAILURE TO FILE INFORMATION RETURNS.—Subchapter B of chapter 68 (relating to assessable penalties) is amended by adding at the end thereof the following new section:

26 USC 6651-6659.

"SEC. 6677. FAILURE TO FILE INFORMATION RETURNS WITH RESPECT TO CERTAIN FOREIGN TRUSTS.

"(a) CIVIL PENALTY.—In addition to any criminal penalty provided by law, any person required to file a return under section 6048 who fails to file such return at the time provided in such section, or who files a return which does not show the information required pursuant to such section, shall pay a penalty equal to 5 percent of the amount transferred to a trust, but not more than \$1,000, unless it is shown that such failure is due to reasonable cause.

"(b) DEFICIENCY PROCEDURES NOT TO APPLY.—Subchapter B of chapter 63 (relating to deficiency procedures for income, estate, and gift taxes) shall not apply in respect of the assessment or collection of any penalty imposed by subsection (a)."

26 USC 6211-6216.

(h) UNITED STATES PERSON DEFINED.—Section 7701 (a) is amended by adding at the end thereof the following new paragraphs:

26 USC 7701.

"(30) UNITED STATES PERSON.—The term 'United States person' means—

"(A) a citizen or resident of the United States,

"(B) a domestic partnership,

"(C) a domestic corporation, and

"(D) any estate or trust (other than a foreign estate or foreign trust, within the meaning of section 7701 (a) (31)).

"(31) FOREIGN ESTATE OR TRUST.—The terms 'foreign estate' and 'foreign trust' mean an estate or trust, as the case may be, the income of which from sources without the United States is not includible in gross income under subtitle A."

(i) TECHNICAL AMENDMENTS.—

(1) The table of sections for subpart D of subchapter J of chapter 1 (relating to treatment of excess distributions by trusts) is amended by adding at the end thereof

"Sec. 669. Special rules applicable to certain foreign trusts."

(2) The table of sections for subpart B of part III of subchapter A of chapter 61 (relating to information concerning transactions with other persons) is amended by adding at the end thereof

"Sec. 6048. Returns as to creation of or transfers to certain foreign trusts."

(3) The table of sections for subchapter B of chapter 68 (relating to assessable penalties) is amended by adding at the end thereof

"Sec. 6677. Failure to file information returns with respect to certain foreign trusts."

(j) **EFFECTIVE DATE.**—The amendments made by this section (other than by subsections (f), (g), and (h)) shall apply with respect to distributions made after December 31, 1962.

SEC. 8. MUTUAL INSURANCE COMPANIES (OTHER THAN LIFE, MARINE, AND CERTAIN FIRE OR FLOOD INSURANCE COMPANIES), ETC.

26 USC 821-826;
Ante, p. 114.

(a) **IMPOSITION OF TAX.**—So much of part II of subchapter L (relating to mutual insurance companies, other than life or marine or fire insurance companies issuing perpetual policies) of chapter 1 precedes section 822 is amended to read as follows:

"PART II—MUTUAL INSURANCE COMPANIES (OTHER THAN LIFE AND CERTAIN MARINE INSURANCE COMPANIES AND OTHER THAN FIRE OR FLOOD INSURANCE COMPANIES WHICH OPERATE ON BASIS OF PERPETUAL POLICIES OR PREMIUM DEPOSITS)

"Sec. 821. Tax on mutual insurance companies to which part II applies.

"Sec. 822. Determination of taxable investment income.

"Sec. 823. Determination of statutory underwriting income or loss.

"Sec. 824. Adjustments to provide protection against losses.

"Sec. 825. Unused loss deduction.

"Sec. 826. Election by reciprocal.

"SEC. 821. TAX ON MUTUAL INSURANCE COMPANIES TO WHICH PART II APPLIES.

"(a) **IMPOSITION OF TAX.**—A tax is hereby imposed for each taxable year beginning after December 31, 1962, on the mutual insurance company taxable income of every mutual insurance company (other than a life insurance company and other than a fire, flood, or marine insurance company subject to the tax imposed by section 831). Such tax shall consist of—

Post, pp. 997,
998.

"(1) **NORMAL TAX.**—

"(A) **TAXABLE YEARS BEGINNING BEFORE JULY 1, 1963.**—

In the case of taxable years beginning before July 1, 1963, a normal tax of 30 percent of the mutual insurance company taxable income, or 60 percent of the amount by which such taxable income exceeds \$6,000, whichever is the lesser;

"(B) **TAXABLE YEARS BEGINNING AFTER JUNE 30, 1963.**—

In the case of taxable years beginning after June 30, 1963, a normal tax of 25 percent of the mutual insurance company taxable income, or 50 percent of the amount by which such taxable income exceeds \$6,000, whichever is the lesser; plus

"(2) **SURTAX.**—A surtax of 22 percent of the mutual insurance company taxable income (computed without regard to the deduction provided in section 242 for partially tax-exempt interest) in excess of \$25,000.

26 USC 242.

"(b) **MUTUAL INSURANCE COMPANY TAXABLE INCOME DEFINED.**—For purposes of this part, the term 'mutual insurance company tax-

able income' means, with respect to any taxable year, the amount by which—

“(1) the sum of—

“(A) the taxable investment income (as defined in section 822(a)(1)),

Post, p. 992.

“(B) the statutory underwriting income (as defined in section 823(a)(1)), and

Post, p. 992.

“(C) the amounts required by section 824(d) to be subtracted from the protection against loss account, exceeds

Post, p. 993.

“(2) the sum of—

“(A) the investment loss (as defined in section 822(a)(2)),

“(B) the statutory underwriting loss (as defined in section 823(a)(2)), and

“(C) the unused loss deduction provided by section 825(a).

Post, p. 995.

“(c) **ALTERNATIVE TAX FOR CERTAIN SMALL COMPANIES.—**

“(1) **IMPOSITION OF TAX.**—In the case of taxable years beginning after December 31, 1962, there is hereby imposed for each taxable year on the income of each mutual insurance company to which this subsection applies a tax (which shall be in lieu of the tax imposed by subsection (a)) computed as follows:

“(A) **NORMAL TAX.**—

“(i) **TAXABLE YEARS BEGINNING BEFORE JULY 1, 1963.**—

In the case of taxable years beginning before July 1, 1963, a normal tax of 30 percent of the taxable investment income, or 60 percent of the amount by which such taxable income exceeds \$3,000, whichever is the lesser;

“(ii) **TAXABLE YEARS BEGINNING AFTER JUNE 30, 1963.**—

In the case of taxable years beginning after June 30, 1963, a normal tax of 25 percent of the taxable investment income, or 50 percent of the amount by which such taxable income exceeds \$3,000, whichever is the lesser; plus

“(B) **SURTAX.**—A surtax of 22 percent of the taxable investment income (computed without regard to the deduction provided in section 242 for partially tax-exempt interest) in excess of \$25,000.

26 USC 242.

“(2) **GROSS AMOUNT RECEIVED, OVER \$150,000 BUT LESS THAN \$250,000.**—If the gross amount received during the taxable year from the items described in section 822(b) (other than paragraph (1)(D) thereof) and premiums (including deposits and assessments) is over \$150,000 but less than \$250,000, the tax imposed by paragraph (1) shall be reduced to an amount which bears the same proportion to the amount of the tax determined under paragraph (1) as the excess over \$150,000 of such gross amount received bears to \$100,000.

“(3) **COMPANIES TO WHICH SUBSECTION APPLIES.**—

“(A) **IN GENERAL.**—Except as provided in subparagraph (B), this subsection shall apply to every mutual insurance company (other than a life insurance company and other than a fire, flood, or marine insurance company subject to the tax imposed by section 831) which received during the taxable year from the items described in section 822(b) (other than paragraph (1)(D) thereof) and premiums (including deposits and assessments) a gross amount in excess of \$150,000 but not in excess of \$500,000.

Post, pp. 997, 996.

“(B) **EXCEPTIONS.**—This subsection shall not apply to a mutual insurance company for the taxable year if—

“(i) there is in effect an election by such company made under subsection (d) to be taxable under subsection (a); or

“(ii) there is any amount in the protection against loss account at the beginning of the taxable year.

“(d) ELECTION TO INCLUDE STATUTORY UNDERWRITING INCOME OR LOSS.—

“(1) IN GENERAL.—Any mutual insurance company which is subject to the tax imposed by subsection (c) may elect, in such manner and at such time as the Secretary or his delegate may by regulations prescribe, to be subject to the tax imposed by subsection (a).

“(2) EFFECT OF ELECTION.—If an election is made under paragraph (1), the electing company shall be subject to the tax imposed by subsection (a) (and shall not be subject to the tax imposed by subsection (c)) for the first taxable year for which such election is made and for all taxable years thereafter unless the Secretary or his delegate consents to a revocation of such election.

“(e) NO UNITED STATES INSURANCE BUSINESS.—Foreign mutual insurance companies (other than a life insurance company and other than a fire, flood, or marine insurance company subject to the tax imposed by section 831) not carrying on an insurance business within the United States shall not be subject to this part but shall be taxable as other foreign corporations.

“(f) SPECIAL TRANSITIONAL UNDERWRITING LOSS.—

“(1) COMPANIES TO WHICH SUBSECTION APPLIES.—This subsection shall apply to every mutual insurance company which has been subject to the tax imposed by this section (as in effect before the enactment of this subsection) for the 5 taxable years immediately preceding January 1, 1962, and has incurred an underwriting loss for each of such 5 taxable years.

“(2) REDUCTION OF STATUTORY UNDERWRITING INCOME.—For purposes of this part, the statutory underwriting income of a company described in paragraph (1) for the taxable year shall be the statutory underwriting income for the taxable year (determined without regard to this subsection) reduced by the amount by which—

“(A) the sum of the underwriting losses of such company for the 5 taxable years immediately preceding January 1, 1962, exceeds

“(B) the total amount by which the company's statutory underwriting income was reduced by reason of this subsection for prior taxable years.

“(3) UNDERWRITING LOSS DEFINED.—For purposes of this subsection, the term ‘underwriting loss’ means statutory underwriting loss, computed without any deduction under section 824(a) and without any deduction under section 832(c) (11).

“(4) YEARS TO WHICH SUBSECTION APPLIES.—This subsection shall apply with respect to any taxable year beginning after December 31, 1962, and before January 1, 1968, for which the taxpayer is subject to the tax imposed by subsection (a).

“(g) CROSS REFERENCES.—

“(1) For exemption from tax of certain mutual insurance companies, see section 501(c)(15).

“(2) For alternative tax in case of capital gains, see section 1201(a).”

(b) TAXABLE INVESTMENT INCOME.—

(1) IN GENERAL.—Section 822 (relating to determination of mutual insurance company taxable income) is amended by strik-

Post, pp. 997,
998.

Post, p. 993.
Post, p. 997.

26 USC 501;
Post, p. 997.
26 USC 1201;
Post, p. 999.
26 USC 822;
Post, p. 992.

ing out the heading and subsection (a) and inserting in lieu thereof the following:

"SEC. 822. DETERMINATION OF TAXABLE INVESTMENT INCOME.

"(a) DEFINITIONS.—For purposes of this part—

"(1) The term 'taxable investment income' means the gross investment income, minus the deductions provided in subsection (c).

"(2) The term 'investment loss' means the amount by which the deductions provided in subsection (c) exceed the gross investment income."

(2) CONFORMING AMENDMENTS.—Subsections (c) and (e) of section 822 are each amended by striking out "mutual insurance company taxable income" each place it appears and inserting in lieu thereof "taxable investment income".

26 USC 822.

(3) DIVIDENDS RECEIVED DEDUCTION.—Section 822(c)(7) (relating to special deductions) is amended by adding at the end thereof the following new sentence: "In applying section 246(b) (relating to limitation on aggregate amount of deductions for dividends received) for purposes of this paragraph, the reference in such section to 'taxable income' shall be treated as a reference to 'taxable investment income'."

26 USC 246.

(4) REDESIGNATION OF SECTION 823.—Part II of subchapter L of chapter 1 is amended by striking out

"SEC. 823. OTHER DEFINITIONS.

"For purposes of this part—",

and inserting in lieu thereof (at the end of section 822) the following:

"(f) DEFINITIONS.—For purposes of this part—"

(c) STATUTORY UNDERWRITING INCOME OR LOSS.—Part II of subchapter L of chapter 1 is amended by adding after section 822(f) (as redesignated by subsection (b)(4) of this section) the following new sections:

"SEC. 823. DETERMINATION OF STATUTORY UNDERWRITING INCOME OR LOSS.

"(a) IN GENERAL.—For purposes of this part—

"(1) The term 'statutory underwriting income' means the amount by which—

"(A) the gross income which would be taken into account in computing taxable income under section 832 if the taxpayer were subject to the tax imposed by section 831, reduced by the gross investment income, exceeds

26 USC 832.

Post, pp. 997, 998.

"(B) the sum of (i) the deductions which would be taken into account in computing taxable income if the taxpayer were subject to the tax imposed by section 831, reduced by the deductions provided in section 822(c), plus (ii) the deductions provided in subsection (c) and section 824(a).

Supra;

26 USC 822.

"(2) The term 'statutory underwriting loss' means the excess of the amount referred to in paragraph (1)(B) over the amount referred to in paragraph (1)(A).

"(b) MODIFICATIONS.—In applying subsection (a)—

"(1) NET OPERATING LOSS DEDUCTION.—The deduction for net operating losses provided in section 172 shall not be allowed.

26 USC 172.

"(2) INTERINSURERS.—In the case of a mutual insurance company which is an interinsurer or reciprocal underwriter—

"(A) there shall be allowed as a deduction the increase for the taxable year in savings credited to subscriber accounts, or

"(B) there shall be included as an item of gross income the decrease for the taxable year in savings credited to subscriber accounts.

For purposes of the preceding sentence, the term 'savings credited to subscriber accounts' means such portion of the surplus as is credited to the individual accounts of subscribers before the 16th day of the third month following the close of the taxable year, but only if the company would be obligated to pay such amount promptly to such subscriber if he terminated his contract at the close of the company's taxable year. For purposes of determining his taxable income, the subscriber shall treat any such savings credited to his account as a dividend paid or declared.

"(c) SPECIAL DEDUCTION FOR SMALL COMPANY HAVING GROSS AMOUNT OF LESS THAN \$1,100,000.—

"(1) IN GENERAL.—If the gross amount received during the taxable year by a taxpayer subject to the tax imposed by section 821(a) from the items described in section 822(b) (other than paragraph (1)(D) thereof) and premiums (including deposits and assessments) does not equal or exceed \$1,100,000, then in determining the statutory underwriting income or loss for the taxable year there shall be allowed an additional deduction of \$6,000; except that if such gross amount exceeds \$500,000, such additional deduction shall be equal to 1 percent of the amount by which \$1,100,000 exceeds such gross amount.

"(2) LIMITATION.—The amount of the deduction allowed under paragraph (1) shall not exceed the statutory underwriting income for the taxable year, computed without regard to any deduction under this subsection or section 824(a).

"SEC. 824. ADJUSTMENTS TO PROVIDE PROTECTION AGAINST LOSSES.

"(a) ALLOWANCE OF DEDUCTION.—

"(1) IN GENERAL.—In determining the statutory underwriting income or loss for any taxable year there shall be allowed as a deduction the sum of—

"(A) an amount equal to 1 percent of the losses incurred during the taxable year (as determined under section 832(b)(5)), plus

"(B) an amount equal to 25 percent of the underwriting gain for the taxable year, plus

"(C) if the concentrated windstorm, etc., premium percentage for the taxable year exceeds 40 percent, an amount determined by applying so much of such percentage as exceeds 40 percent to the underwriting gain for the taxable year.

For purposes of this paragraph, the term 'underwriting gain' means statutory underwriting income, computed without any deduction under this subsection.

"(2) SPECIAL RULE FOR COMPANIES HAVING CONCENTRATED WINDSTORM, ETC., RISKS.—For purposes of paragraph (1)(C), the term 'concentrated windstorm, etc., premium percentage' means, with respect to any taxable year, the percentage obtained by dividing—

"(A) the amount of the premiums earned on insurance contracts during the taxable year (as defined in section 832(b)(4)), to the extent attributable to insuring against losses arising, either in any one State or within 200 miles of any fixed point selected by the taxpayer, from windstorm, hail, flood, earthquake, or similar hazards, by

"(B) the amount of the premiums earned on insurance contracts during the taxable year (as so defined).

"(b) PROTECTION AGAINST LOSS ACCOUNT.—Each insurance company subject to the tax imposed by section 821(a) for any taxable year shall, for purposes of this part, establish and maintain a protection against loss account.

26 USC 832.

26 USC 832;
Post, p. 997.

Ante, p. 989.

"(c) ADDITIONS TO ACCOUNT.—There shall be added to the protection against loss account for each taxable year an amount equal to the amount allowable as a deduction for the taxable year under subsection (a) (1).

"(d) SUBTRACTIONS.—

"(1) ANNUAL SUBTRACTIONS.—After applying subsection (c), there shall be subtracted for the taxable year from the protection against loss account—

"(A) first, an amount equal to the excess (if any) of the deduction allowed under subsection (a) for the taxable year over the underwriting gain (within the meaning of subsection (a) (1)) for the taxable year,

"(B) then, the amount (if any) by which—

"(i) the sum of the investment loss for such year and the statutory underwriting loss (reduced by the amount referred to in subparagraph (A)) for such year, exceeds

"(ii) the sum of the statutory underwriting income for such taxable year and the taxable investment income for such taxable year,

"(C) next (in the order in which the losses occurred), amounts equal to the unused loss carryovers to such year,

"(D) next, any amount remaining which was added to the account for the fifth preceding taxable year, minus one-half of the amount remaining in the account for such taxable year which was added by reason of subsection (a) (1) (B), and

"(E) finally, the amount by which the total amount in the account exceeds whichever of the following is the greater:

"(i) 10 percent of premiums earned on insurance contracts during the taxable year (as defined in section 832 (b) (4)) less dividends to policyholders (as defined in section 832 (c) (11)), or

"(ii) the total amount in the account at the close of the preceding taxable year.

"(2) RULES FOR CEILING ON PROTECTION AGAINST LOSS ACCOUNT.—For purposes of paragraph (1) (E), the total amount in the account shall be determined—

"(A) after the application of this section without regard to paragraph (1) (E), and

"(B) without taking into consideration amounts remaining in the account which were added, with respect to all taxable years, by reason of subsection (a) (1) (C).

"(3) PRIORITIES.—The amounts required to be subtracted from the protection against loss account—

"(A) under subparagraphs (A), (B), and (C) of paragraph (1) shall be subtracted—

"(i) first (on a first-in, first-out, basis) from amounts in the account with respect to the five preceding taxable years and the taxable year, and

"(ii) then from amounts in the account with respect to earlier years,

"(B) under subparagraph (E) of paragraph (1) shall be subtracted only from amounts in the account with respect to the taxable year, and

"(C) under paragraphs (A), (B), (C), and (E) of paragraph (1) shall, if the amount to be subtracted from the total amounts in the account with respect to any taxable year is less than such total, be subtracted from each of the amounts (referred to in subsection (a) (1)) in the account with respect to such year in the proportion which each bears to such total.

Post, p. 997.

Ante, p. 989.

“(4) **TERMINATION OF TAXABILITY UNDER SECTION 821.**—If the taxpayer is not subject to tax under section 821 for any taxable year, the entire amount in the account at the close of the preceding taxable year shall be subtracted from the account in such preceding taxable year.

“(5) **ELECTION TO SUBTRACT AMOUNT FROM ACCOUNT.**—

“(A) A taxpayer may elect for any taxable year for which it is subject to tax under section 821(a) to subtract from its protection against loss account any amount which, but for the application of this subparagraph, would be in such account as of the close of such taxable year.

“(B) The election provided by subparagraph (A) for any taxable year shall be made (in such manner and in such form as the Secretary or his delegate may by regulations prescribe) after the close of such taxable year and not later than the time prescribed by law for filing the return (including extensions thereof) for the taxable year following such taxable year. Such an election, once made, may not be revoked.

“SEC. 825. UNUSED LOSS DEDUCTION.

“(a) **AMOUNT OF DEDUCTION.**—For purposes of this part, the unused loss deduction for the taxable year shall be an amount equal to the unused loss carryovers or carrybacks to the taxable year.

“(b) **UNUSED LOSS DEFINED.**—For purposes of this part, the term ‘unused loss’ means, with respect to any taxable year, the amount (if any) by which—

“(1) the sum of the statutory underwriting loss and the investment loss, exceeds

“(2) the sum of—

“(A) the taxable investment income,

“(B) the statutory underwriting income, and

“(C) the amounts required by section 824(d) to be subtracted from the protection against loss account.

“(c) **LOSS YEAR DEFINED.**—For purposes of this part, the term ‘loss year’ means, with respect to any company subject to the tax imposed by section 821(a), any taxable year in which the unused loss (as defined in subsection (b)) of such taxpayer is more than zero.

“(d) **YEARS TO WHICH CARRIED.**—The unused loss for any loss year shall be—

“(1) an unused loss carryback to each of the 3 taxable years preceding the loss year, and

“(2) an unused loss carryover to each of the 5 taxable years following the loss year.

“(e) **AMOUNT OF CARRYBACKS AND CARRYOVERS.**—The entire amount of the unused loss for any loss year shall be carried to the earliest of the taxable years to which such loss may be carried. The portion of such loss which shall be carried to each of the other taxable years shall be the excess (if any) of the amount of such loss over the sum of the offsets (as defined in subsection (f)) for each of the prior taxable years to which such loss may be carried.

“(f) **OFFSET DEFINED.**—For purposes of subsection (e), the term ‘offset’ means with respect to any taxable year (hereinafter referred to as the ‘offset year’)—

“(1) in the case of an unused loss carryback from the loss year to the offset year, the mutual insurance company taxable income for the offset year; or

“(2) in the case of an unused loss carryover from the loss year to the offset year, an amount equal to the sum of—

Ante, p. 994.

“(A) the amount required to be subtracted from the protection against loss account under section 824(d)(1)(C) for the offset year, plus *Ante*, p. 994.

“(B) the mutual insurance company taxable income for the offset year.

For purposes of paragraphs (1) and (2)(B), the mutual insurance company taxable income for the offset year shall be determined without regard to any unused loss carryback or carryover from the loss year or any taxable year thereafter.

“(g) LIMITATIONS.—For purposes of this part, an unused loss shall not be carried—

“(1) to or from any taxable year beginning before January 1, 1963,

“(2) to or from any taxable year for which the insurance company is not subject to the tax imposed by section 821(a), nor *Ante*, p. 989.

“(3) to any taxable year if, between the loss year and such taxable year, there is an intervening taxable year for which the insurance company was not subject to the tax imposed by section 821(a).

SEC. 826. ELECTION BY RECIPROCAL.

“(a) IN GENERAL.—Except as otherwise provided in this section, any mutual insurance company which is an interinsurer or reciprocal underwriter (hereinafter in this section referred to as a ‘reciprocal’) subject to the taxes imposed by section 821(a) may, under regulations prescribed by the Secretary or his delegate, elect to be subject to the limitation provided in subsection (b). Such election shall be effective for the taxable year for which made and for all succeeding taxable years, and shall not be revoked except with the consent of the Secretary or his delegate.

“(b) LIMITATION.—The deduction for amounts paid or incurred in the taxable year to the attorney-in-fact by a reciprocal making the election provided in subsection (a) shall be limited to, but in no case increased by, the deductions of the attorney-in-fact allocable, in accordance with regulations prescribed by the Secretary or his delegate, to the income received by the attorney-in-fact from the reciprocal.

“(c) EXCEPTION.—An election may not be made by a reciprocal under subsection (a) unless the attorney-in-fact of such reciprocal—

“(1) is subject to the taxes imposed by section 11 (b) and (c); *26 USC 11;*

“(2) consents in such manner as the Secretary or his delegate shall prescribe by regulations to make available such information as may be required during the period in which the election provided in subsection (a) is in effect, under regulations prescribed by the Secretary or his delegate; *Ante*, p. 114.

“(3) reports the income received from the reciprocal and the deductions allocable thereto under the same method of accounting under which the reciprocal reports deductions for amounts paid to the attorney-in-fact; and

“(4) files its return on the calendar year basis.

“(d) SPECIAL RULE.—In applying section 824(d)(1)(D), any amount which was added to the protection against loss account by reason of an election under this section shall be treated as having been added by reason of section 824(a)(1)(A). *Ante*, pp. 994, 993.

“(e) CREDIT.—Any reciprocal electing to be subject to the limitation provided in subsection (b) shall be credited with so much of the tax paid by the attorney-in-fact as is attributable, under regulations prescribed by the Secretary or his delegate, to the income received by the attorney-in-fact from the reciprocal in such taxable year.

“(f) **SURTAX EXEMPTION DENIED.**—Any increase in taxable income of a reciprocal attributable to the limitation provided in subsection (b) shall be taxed without regard to the surtax exemption provided in section 821(a)(2).

Ante, p. 989.

“(g) **ADJUSTMENT FOR REFUND.**—If for any taxable year an attorney-in-fact is allowed a credit or refund for taxes paid with respect to which credit or refund to the reciprocal resulted under subsection (e), the taxes of such reciprocal for such taxable year shall be properly adjusted under regulations prescribed by the Secretary or his delegate.

“(h) **TAXES OF ATTORNEY-IN-FACT UNAFFECTED.**—Nothing in this section shall increase or decrease the taxes imposed by this chapter on the income of the attorney-in-fact.”

26 USC 501.

(d) **EXEMPTION FROM TAX.**—Section 501(c)(15) (relating to exemption from tax of certain mutual insurance companies) is amended by striking out “\$75,000” and in lieu thereof inserting “\$150,000”.

(e) **MUTUAL FIRE INSURANCE COMPANIES OPERATING ON BASIS OF PREMIUM DEPOSITS.**—

(1) **APPLICATION OF SECTION 831(a).**—Section 831(a) (imposing a tax on certain mutual marine and fire insurance companies and on stock insurance companies which are not life insurance companies) is amended to read as follows:

26 USC 11;
Ante, p. 114.

“(a) **IMPOSITION OF TAX.**—Taxes computed as provided in section 11 shall be imposed for each taxable year on the taxable income of—

“(1) every insurance company (other than a life or mutual insurance company),

“(2) every mutual marine insurance company, and

“(3) every mutual fire or flood insurance company—

“(A) exclusively issuing perpetual policies, or

“(B) whose principal business is the issuance of policies for which the premium deposits are the same, regardless of the length of the term for which the policies are written, if the unabsorbed portion of such premium deposits not required for losses, expenses, or establishment of reserves is returned or credited to the policyholder on cancellation or expiration of the policy.”

26 USC 832.

(2) **TREATMENT OF UNABSORBED PREMIUM DEPOSITS.**—Section 832(b)(4) (relating to definition of premiums earned) is amended by adding at the end thereof the following new sentence: “For purposes of this subsection, unearned premiums of mutual fire or flood insurance companies described in section 831(a)(3)(B) means (with respect to the policies described in section 831(a)(3)(B)) the amount of unabsorbed premium deposits which the company would be obligated to return to its policyholders at the close of the taxable year if all of its policies were terminated at such time; and the determination of such amount shall be based on the schedule of unabsorbed premium deposit returns for each such company then in effect. Premiums paid by the subscriber of a mutual flood insurance company referred to in paragraph (3) of section 831(a) shall be treated, for purposes of computing the taxable income of such subscriber, in the same manner as premiums paid by a policyholder to a mutual fire insurance company referred to in such paragraph (3).”

Supra.

26 USC 832.

(3) **CONFORMING AMENDMENT.**—Section 832(b)(1)(C) is amended by striking out “section 831(a),” and inserting in lieu thereof “section 831(a)(3)(A).”

(4) **ADJUSTMENT OF PREMIUM DEPOSIT.**—Section 832(c)(11) is amended to read as follows:

“(11) dividends and similar distributions paid or declared to policyholders in their capacity as such, except in the case of a

mutual fire insurance company described in section 831(a)(3) (A). For purposes of the preceding sentence, the term 'dividends and similar distributions' includes amounts returned or credited to policyholders on cancellation or expiration of policies described in section 831(a)(3)(B). For purposes of this paragraph, the term 'paid or declared' shall be construed according to the method of accounting regularly employed in keeping the books of the insurance company; and".

(5) **ADDITIONAL ITEM OF INCOME.**—Section 832(b)(1) is amended by striking out "and" at the end of subparagraph (B), by striking out the period at the end of subparagraph (C) and inserting in lieu thereof ", and", and by adding at the end thereof the following new subparagraph: 26 USC 832.

"(D) in the case of a mutual fire or flood insurance company described in section 831(a)(3)(B), an amount equal to 2 percent of the premiums earned on insurance contracts during the taxable year with respect to policies described in section 831(a)(3)(B) after deduction of premium deposits returned or credited during the same taxable year."

(f) **ELECTION OF CERTAIN MUTUAL COMPANIES TO BE TAXED ON TOTAL INCOME.**—Section 831 is amended by redesignating subsection (c) as subsection (d), and by inserting after subsection (b) the following new subsection: Ante, p. 997.

"(c) **ELECTION FOR MULTIPLE LINE COMPANY TO BE TAXED ON TOTAL INCOME.**—

"(1) **IN GENERAL.**—Any mutual insurance company engaged in writing marine, fire, and casualty insurance which for any 5-year period beginning after December 31, 1941, and ending before January 1, 1962, was subject to the tax imposed by section 831 (or the tax imposed by corresponding provisions of prior law) may elect, in such manner and at such time as the Secretary or his delegate may by regulations prescribe, to be subject to the tax imposed by section 831, whether or not marine insurance is its predominant source of premium income.

"(2) **EFFECT OF ELECTION.**—If an election is made under paragraph (1), the electing company shall (in lieu of being subject to the tax imposed by section 821) be subject to the tax imposed by this section for taxable years beginning after December 31, 1961. Such election shall not be revoked except with the consent of the Secretary or his delegate." Ante, p. 989.

(g) **TECHNICAL AMENDMENTS, ETC.**—

(1) **CREDIT FOR FOREIGN TAXES.**—Section 841 (relating to credit for foreign taxes) is amended by striking out "and" at the end of paragraph (1), by renumbering paragraph (2) as paragraph (3), and by inserting after paragraph (1) the following new paragraph: 26 USC 841.

"(2) in the case of the tax imposed by section 821(a), the mutual insurance company taxable income (as defined in section 821(b)); and in the case of the tax imposed by section 821(c), the taxable investment income (as defined in section 822(a)), and".

(2) **ADJUSTMENTS TO BASIS FOR DEPRECIATION SUSTAINED.**—Section 1016(a)(3) (relating to adjustments to basis for depreciation, etc., sustained) is amended by striking out "and" at the end of subparagraph (B), by inserting "and" at the end of subparagraph (C), and by inserting after subparagraph (C) the following new subparagraph: 26 USC 1016.

"(D) since February 28, 1913, during which such property was held by a person subject to tax under part II of subchapter L (or the corresponding provisions of prior income tax laws), to the extent that paragraph (2) does not apply,".

26 USC 1201.

(3) **ALTERNATIVE TAX ON CAPITAL GAINS.**—Section 1201(a) (relating to alternative tax on corporations) is amended by striking out “821 (a) (1) or (b),” and inserting in lieu thereof “821 (a) or (c).”

Ante, p. 989.

(4) **CLERICAL AMENDMENTS.**—

(A) The table of parts for subchapter L is amended by striking out the portion referring to part II and inserting in lieu thereof the following:

“Part II. Mutual insurance companies (other than life and certain marine insurance companies and other than fire or flood insurance companies which operate on basis of perpetual policies or premium deposits).”

(B) The heading to section 831 is amended to read as follows:

“SEC. 831. TAX ON INSURANCE COMPANIES (OTHER THAN LIFE OR MUTUAL), MUTUAL MARINE INSURANCE COMPANIES, AND CERTAIN MUTUAL FIRE OR FLOOD INSURANCE COMPANIES.”

(C) The table of sections for part III of subchapter L is amended by striking out the portion referring to section 831 and inserting in lieu thereof the following:

“Sec. 831. Tax on insurance companies (other than life or mutual), mutual marine insurance companies, and certain mutual fire or flood insurance companies.”

(h) **EFFECTIVE DATE.**—The amendments made by this section (other than by subsection (f)) shall apply with respect to taxable years beginning after December 31, 1962.

SEC. 9. DOMESTIC CORPORATIONS RECEIVING DIVIDENDS FROM FOREIGN CORPORATIONS.

26 USC 902.

(a) **FOREIGN TAXES DEEMED PAID BY DOMESTIC CORPORATIONS.**—Section 902 (relating to credit for corporate stockholder in foreign corporations) is amended to read as follows:

“SEC. 902. CREDIT FOR CORPORATE STOCKHOLDER IN FOREIGN CORPORATION.

“(a) **TREATMENT OF TAXES PAID BY FOREIGN CORPORATION.**—For purposes of this subpart, a domestic corporation which owns at least 10 percent of the voting stock of a foreign corporation from which it receives dividends in any taxable year shall—

“(1) to the extent such dividends are paid by such foreign corporation out of accumulated profits (as defined in subsection (c) (1) (A)) of a year for which such foreign corporation is not a less developed country corporation, be deemed to have paid the same proportion of any income, war profits, or excess profits taxes paid or deemed to be paid by such foreign corporation to any foreign country or to any possession of the United States on or with respect to such accumulated profits, which the amount of such dividends (determined without regard to section 78) bears to the amount of such accumulated profits in excess of such income, war profits, and excess profits taxes (other than those deemed paid); and

“(2) to the extent such dividends are paid by such foreign corporation out of accumulated profits (as defined in subsection (c) (1) (B)) of a year for which such foreign corporation is a less developed country corporation, be deemed to have paid the same proportion of any income, war profits, or excess profits taxes paid or deemed to be paid by such foreign corporation to any foreign country or to any possession of the United States on or with respect to such accumulated profits, which the amount of such dividends bears to the amount of such accumulated profits.

Post, p. 1001.

"(b) FOREIGN SUBSIDIARY OF FOREIGN CORPORATION.—If such foreign corporation owns 50 percent or more of the voting stock of another foreign corporation from which it receives dividends in any taxable year, it shall be deemed to have paid the same proportion of any income, war profits, or excess profits taxes paid by such other foreign corporation to any foreign country or to any possession of the United States, on or with respect to the accumulated profits of the corporation from which such dividends were paid which—

"(1) for purposes of applying subsection (a)(1), the amount of such dividends bears to the amount of the accumulated profits (as defined in subsection (c)(1)(A)) of such other foreign corporation from which such dividends were paid in excess of such income, war profits, and excess profits taxes, or

"(2) for purposes of applying subsection (a)(2), the amount of such dividends bears to the amount of the accumulated profits (as defined in subsection (c)(1)(B)) of such other foreign corporation from which such dividends were paid.

"(c) APPLICABLE RULES.—

"(1) ACCUMULATED PROFITS DEFINED.—For purposes of this section, the term 'accumulated profits' means with respect to any foreign corporation—

"(A) for purposes of subsections (a)(1) and (b)(1), the amount of its gains, profits, or income computed without reduction by the amount of the income, war profits, and excess profits taxes imposed on or with respect to such profits or income by any foreign country or any possession of the United States; and

"(B) for purposes of subsections (a)(2) and (b)(2), the amount of its gains, profits, or income in excess of the income, war profits, and excess profits taxes imposed on or with respect to such profits or income.

The Secretary or his delegate shall have full power to determine from the accumulated profits of what year or years such dividends were paid, treating dividends paid in the first 60 days of any year as having been paid from the accumulated profits of the preceding year or years (unless to his satisfaction shown otherwise), and in other respects treating dividends as having been paid from the most recently accumulated gains, profits, or earnings.

"(2) ACCOUNTING PERIODS.—In the case of a foreign corporation, the income, war profits, and excess profits taxes of which are determined on the basis of an accounting period of less than 1 year, the word 'year' as used in this subsection shall be construed to mean such accounting period.

"(d) LESS DEVELOPED COUNTRY CORPORATION DEFINED.—For purposes of this section, the term 'less developed country corporation' means—

"(1) a foreign corporation which, for its taxable year, is a less developed country corporation within the meaning of section 955(c)(1) or (2), and

"(2) a foreign corporation which owns 10 percent or more of the total combined voting power of all classes of stock entitled to vote of a foreign corporation which is a less developed country corporation within the meaning of section 955(c)(1), and—

"(A) 80 percent or more of the gross income of which for its taxable year meets the requirement of section 955(c)(1)(A); and

"(B) 80 percent or more in value of the assets of which on each day of such year consists of property described in section 955(c)(1)(B).

A foreign corporation which is a less developed country corporation for its first taxable year beginning after December 31, 1962, shall, for purposes of this section, be treated as having been a less developed country corporation for each of its taxable years beginning before January 1, 1963.

“(e) CROSS REFERENCES.—

“(1) For inclusion in gross income of an amount equal to taxes deemed paid under subsection (a)(1), see section 78.

“(2) For application of subsections (a) and (b) with respect to taxes deemed paid in a prior taxable year by a United States shareholder with respect to a controlled foreign corporation, see section 960.

“(3) For reduction of credit with respect to dividends paid out of accumulated profits for years for which certain information is not furnished, see section 6038.”

Infra.

Post, p. 1020.

Post, p. 1059.

26 USC 71-77.

(b) INCLUSION IN GROSS INCOME OF AMOUNT EQUAL TO TAXES DEEMED PAID.—Part II of subchapter B of chapter 1 (relating to items specifically included in gross income) is amended by adding at the end thereof the following new section:

“SEC. 78. DIVIDENDS RECEIVED FROM CERTAIN FOREIGN CORPORATIONS BY DOMESTIC CORPORATIONS CHOOSING FOREIGN TAX CREDIT.

“If a domestic corporation chooses to have the benefits of subpart A of part III of subchapter N (relating to foreign tax credit) for any taxable year, an amount equal to the taxes deemed to be paid by such corporation under section 902(a)(1) (relating to credit for corporate stockholder in foreign corporation) or under section 960(a)(1)(C) (relating to taxes paid by foreign corporation) for such taxable year shall be treated for purposes of this title (other than section 245) as a dividend received by such domestic corporation from the foreign corporation.”

Ante, p. 999.

Post, p. 1020.

26 USC 245;

Ante, p. 977.

(c) DETERMINATION OF SOURCE OF DIVIDENDS RECEIVED FROM CERTAIN FOREIGN CORPORATIONS.—Section 861(a)(2)(B) (relating to dividends from foreign corporations treated as income from sources within the United States) is amended by striking out “to the extent exceeding the amount of the deduction allowable under section 245 in respect of such dividends” and inserting in lieu thereof “to the extent exceeding the amount which is 100/85ths of the amount of the deduction allowable under section 245 in respect of such dividends”.

(d) TECHNICAL AMENDMENTS.—

(1) The table of sections for part II of subchapter B of chapter 1 is amended by adding at the end thereof the following:

“Sec. 78. Dividends received from certain foreign corporations by domestic corporations choosing foreign tax credit.”

26 USC 535,
545.

(2) Section 535(b)(1) and the first sentence of section 545(b)(1) are each amended by striking out “accrued during the taxable year,” and inserting in lieu thereof “accrued during the taxable year or deemed to be paid by a domestic corporation under section 902(a)(1) or 960(a)(1)(C) for the taxable year.”

26 USC 901.

(3) Section 901(d) is amended by adding the following new paragraph:

“(4) For reduction of credit for failure of a United States person to furnish certain information with respect to a foreign corporation controlled by him, see section 6038.”

(e) EFFECTIVE DATE.—The amendments made by this section shall apply—

(1) in respect of any distribution received by a domestic corporation after December 31, 1964, and

(2) in respect of any distribution received by a domestic corporation before January 1, 1965, in a taxable year of such

corporation beginning after December 31, 1962, but only to the extent that such distribution is made out of the accumulated profits of a foreign corporation for a taxable year (of such foreign corporation) beginning after December 31, 1962.

For purposes of paragraph (2), a distribution made by a foreign corporation out of its profits which are attributable to a distribution received from a foreign subsidiary to which section 902(b) applies shall be treated as made out of the accumulated profits of a foreign corporation for a taxable year beginning before January 1, 1963, to the extent that such distribution was paid out of the accumulated profits of such foreign subsidiary for a taxable year beginning before January 1, 1963.

Ante, p. 1000.

SEC. 10. SEPARATE LIMITATION ON FOREIGN TAX CREDIT WITH RESPECT TO CERTAIN INTEREST INCOME.

(a) **LIMITATION ON FOREIGN TAX CREDIT.**—Section 904 (relating to limitations on foreign tax credit) is amended by redesignating subsection (f) as subsection (g) and by inserting after subsection (e) the following new subsection:

26 USC 904.

Post, p. 1031.

“(f) **APPLICATION OF SECTION IN CASE OF CERTAIN INTEREST INCOME.**—

“(1) **IN GENERAL.**—The provisions of subsections (a), (c), (d), and (e) of this section shall be applied separately with respect to—

“(A) the interest income described in paragraph (2), and

“(B) income other than the interest income described in paragraph (2).

“(2) **INTEREST INCOME TO WHICH APPLICABLE.**—For purposes of this subsection, the interest income described in this paragraph is interest other than interest—

“(A) derived from any transaction which is directly related to the active conduct of a trade or business in a foreign country or a possession of the United States,

“(B) derived in the conduct of a banking, financing, or similar business,

“(C) received from a corporation in which the taxpayer owns at least 10 percent of the voting stock, or

“(D) received on obligations acquired as a result of the disposition of a trade or business actively conducted by the taxpayer in a foreign country or possession of the United States or as a result of the disposition of stock or obligations of a corporation in which the taxpayer owned at least 10 percent of the voting stock.

“(3) **OVERALL LIMITATION NOT TO APPLY.**—The limitation provided by subsection (a)(2) shall not apply with respect to the interest income described in paragraph (2). The Secretary or his delegate shall by regulations prescribe the manner of application of subsection (e) with respect to cases in which the limitation provided by subsection (a)(2) applies with respect to income other than the interest income described in paragraph (2).

“(4) **TRANSITIONAL RULES FOR CARRYBACKS AND CARRYOVERS.**—

“(A) **CARRYBACKS TO YEARS PRIOR TO REVENUE ACT OF 1962.**—Where, under the provisions of subsection (d), taxes (i) paid or accrued to any foreign country or possession of the United States in any taxable year beginning after the date of the enactment of the Revenue Act of 1962 are deemed (ii) paid or accrued in one or more taxable years beginning on or before the date of enactment of the Revenue Act of 1962, the amount of such taxes deemed paid or accrued shall be determined without regard to the provisions of this sub-

section. To the extent the taxes paid or accrued to a foreign country or possession of the United States in any taxable year described in clause (i) are not, with the application of the preceding sentence, deemed paid or accrued in any taxable year described in clause (ii), such taxes shall, for purposes of applying subsection (d), be deemed paid or accrued in a taxable year beginning after the date of the enactment of the Revenue Act of 1962, with respect to interest income described in paragraph (2), and with respect to income other than interest income described in paragraph (2), in the same ratios as the amount of such taxes paid or accrued with respect to interest income described in paragraph (2), and the amount of such taxes paid or accrued with respect to income other than interest income described in paragraph (2), respectively, bear to the total amount of such taxes paid or accrued to such foreign country or possession of the United States.

“(B) CARRYOVERS TO YEARS AFTER REVENUE ACT OF 1962.—Where, under the provisions of subsection (d), taxes (i) paid or accrued to any foreign country or possession of the United States in any taxable year beginning on or before the date of the enactment of the Revenue Act of 1962 are deemed (ii) paid or accrued in one or more taxable years beginning after the date of the enactment of the Revenue Act of 1962, the amount of such taxes deemed paid or accrued in any year described in clause (ii) shall, with respect to interest income described in paragraph (2), be an amount which bears the same ratio to the amount of such taxes deemed paid or accrued as the amount of the taxes paid or accrued to such foreign country or possession for such year with respect to interest income described in paragraph (2) bears to the total amount of the taxes paid or accrued to such foreign country or possession for such year; and the amount of such taxes deemed paid or accrued in any year described in clause (ii) with respect to income other than interest income described in paragraph (2) shall be an amount which bears the same ratio to the amount of such taxes deemed paid or accrued for such year as the amount of taxes paid or accrued to such foreign country or possession for such year with respect to income other than interest income described in paragraph (2) bears to the total amount of the taxes paid or accrued to such foreign country or possession for such year.”

(b) EFFECTIVE DATE.—The amendments made by subsection (a) shall apply with respect to taxable years beginning after the date of the enactment of this Act, but only with respect to interest resulting from transactions consummated after April 2, 1962.

SEC. 11. EARNED INCOME FROM SOURCES WITHOUT THE UNITED STATES.

(a) LIMITATION ON AMOUNT AND TYPE OF INCOME EXCLUDED.—Section 911 (relating to earned income from sources without the United States) is amended to read as follows:

“SEC. 911. EARNED INCOME FROM SOURCES WITHOUT THE UNITED STATES.

“(a) GENERAL RULE.—The following items shall not be included in gross income and shall be exempt from taxation under this subtitle:

“(1) BONA FIDE RESIDENT OF FOREIGN COUNTRY.—In the case of an individual citizen of the United States who establishes to the satisfaction of the Secretary or his delegate that he has been a bona fide resident of a foreign country or countries for an uninterrupted period which includes an entire taxable year, amounts

received from sources without the United States (except amounts paid by the United States or any agency thereof) which constitute earned income attributable to services performed during such uninterrupted period. The amount excluded under this paragraph for any taxable year shall be computed by applying the special rules contained in subsection (c).

“(2) PRESENCE IN FOREIGN COUNTRY FOR 17 MONTHS.—In the case of an individual citizen of the United States who during any period of 18 consecutive months is present in a foreign country or countries during at least 510 full days in such period, amounts received from sources without the United States (except amounts paid by the United States or any agency thereof) which constitute earned income attributable to services performed during such 18-month period. The amount excluded under this paragraph for any taxable year shall be computed by applying the special rules contained in subsection (c).

An individual shall not be allowed, as a deduction from his gross income, any deductions (other than those allowed by section 151, relating to personal exemptions) properly allocable to or chargeable against amounts excluded from gross income under this subsection. 26 USC 151.

“(b) DEFINITION OF EARNED INCOME.—For purposes of this section, the term ‘earned income’ means wages, salaries, or professional fees, and other amounts received as compensation for personal services actually rendered, but does not include that part of the compensation derived by the taxpayer for personal services rendered by him to a corporation which represents a distribution of earnings or profits rather than a reasonable allowance as compensation for the personal services actually rendered. In the case of a taxpayer engaged in a trade or business in which both personal services and capital are material income-producing factors, under regulations prescribed by the Secretary or his delegate, a reasonable allowance as compensation for the personal services rendered by the taxpayer, not in excess of 30 percent of his share of the net profits of such trade or business, shall be considered as earned income.

“(c) SPECIAL RULES.—For purposes of computing the amount excludable under subsection (a), the following rules shall apply:

“(1) LIMITATIONS ON AMOUNT OF EXCLUSION.—The amount excluded from the gross income of an individual under subsection (a) for any taxable year shall not exceed an amount which shall be computed on a daily basis at an annual rate of—

“(A) except as provided in subparagraph (B), \$20,000 in the case of an individual who qualifies under subsection (a), or

“(B) \$35,000 in the case of an individual who qualifies under subsection (a) (1), but only with respect to that portion of such taxable year occurring after such individual has been a bona fide resident of a foreign country or countries for an uninterrupted period of 3 consecutive years.

“(2) ATTRIBUTION TO YEAR IN WHICH SERVICES ARE PERFORMED.—For purposes of applying paragraph (1), amounts received shall be considered received in the taxable year in which the services to which the amounts are attributable are performed.

“(3) TREATMENT OF COMMUNITY INCOME.—In applying paragraph (1) with respect to amounts received for services performed by a husband or wife which are community income under community property laws applicable to such income, the aggregate amount excludable under subsection (a) from the gross income of such husband and wife shall equal the amount which would be excludable if such amounts did not constitute such community income.

"(4) REQUIREMENT AS TO TIME OF RECEIPT.—No amount received after the close of the taxable year following the taxable year in which the services to which the amounts are attributable are performed may be excluded under subsection (a).

"(5) CERTAIN AMOUNTS NOT EXCLUDABLE.—No amount—

26 USC 402. "(A) received as a pension or annuity, or
26 USC 403. "(B) included in gross income by reason of section 402(b) (relating to taxability of beneficiary of non-exempt trust), section 403(c) (relating to taxability of beneficiary under a non-qualified annuity), or section 403(d) (relating to taxability of beneficiary under certain forfeitable contracts purchased by exempt organizations),
may be excluded under subsection (a).

"(6) TEST OF BONA FIDE RESIDENCE.—A statement by an individual who has earned income from sources within a foreign country to the authorities of that country that he is not a resident of that country, if he is held not subject as a resident of that country to the income tax of that country by its authorities with respect to such earnings, shall be conclusive evidence with respect to such earnings that he is not a bona fide resident of that country for purposes of subsection (a) (1).

"(7) CERTAIN NONCASH REMUNERATION.—If an individual who qualifies under subsection (a) (1) receives compensation from sources without the United States (except from the United States or any agency thereof) in the form of the right to use property or facilities, the limitation under paragraph (1) applicable with respect to such individual—

 "(A) for a taxable year ending in 1963, shall be increased by an amount equal to the amount of such compensation so received during such taxable year;

 "(B) for a taxable year ending in 1964, shall be increased by an amount equal to two-thirds of such compensation so received during such taxable year; and

 "(C) for a taxable year ending in 1965, shall be increased by an amount equal to one-third of such compensation so received during such taxable year.

"(d) CROSS REFERENCES.—

"For administrative and penal provisions relating to the exclusion provided for in this section, see sections 6001, 6011, 6012(c), and the other provisions of subtitle F."

26 USC 72; (b) COMPUTATION OF EMPLOYEES' CONTRIBUTIONS.—Section 72(f)
Post, p.1006. (relating to special rules for computing employees' contributions) is amended by adding after paragraph (2) the following new sentences:
"Paragraph (2) shall not apply to amounts which were contributed by the employer after December 31, 1962, and which would not have been includible in the gross income of the employee by reason of the application of section 911 if such amounts had been paid directly to the employee at the time of contribution. The preceding sentence shall not apply to amounts which were contributed by the employer, as determined under regulations prescribed by the Secretary or his delegate, to provide pension or annuity credits, to the extent such credits are attributable to services performed before January 1, 1963, and are provided pursuant to pension or annuity plan provisions in existence on March 12, 1962, and on that date applicable to such services."
Ante, p.1003.

(c) EFFECTIVE DATES.—

(1) AMENDMENT TO SECTION 911.—The amendment made by subsection (a) shall apply to taxable years ending after September 4, 1962, but only with respect to amounts—

(A) received after March 12, 1962, which are attributable to services performed after December 31, 1962, or

(B) received after December 31, 1962, which are attributable to services performed on or before December 31, 1962, unless on March 12, 1962, there existed a right (whether forfeitable or nonforfeitable) to receive such amounts.

(2) AMENDMENT TO SECTION 72(f).—The amendment made by subsection (b) shall apply to taxable years ending after December 31, 1962. *Ante*, p. 1005.

SEC. 12. CONTROLLED FOREIGN CORPORATIONS.

(a) IN GENERAL.—Part III of subchapter N of chapter 1 (relating to income from sources without the United States) is amended by adding at the end thereof the following new subparts: 26 USC 901 *et seq.*

“Subpart F—Controlled Foreign Corporations

“Sec. 951. Amounts included in gross income of United States shareholders.

“Sec. 952. Subpart F income defined.

“Sec. 953. Income from insurance of United States risks.

“Sec. 954. Foreign base company income.

“Sec. 955. Withdrawal of previously excluded subpart F income from qualified investment.

“Sec. 956. Investment of earnings in United States property.

“Sec. 957. Controlled foreign corporations: United States persons.

“Sec. 958. Rules for determining stock ownership.

“Sec. 959. Exclusion from gross income of previously taxed earnings and profits.

“Sec. 960. Special rules for foreign tax credit.

“Sec. 961. Adjustments to basis of stock in controlled foreign corporations and of other property.

“Sec. 962. Election by individuals to be subject to tax at corporate rates.

“Sec. 963. Receipt of minimum distributions by domestic corporations.

“Sec. 964. Miscellaneous provisions.

“SEC. 951. AMOUNTS INCLUDED IN GROSS INCOME OF UNITED STATES SHAREHOLDERS.

“(a) AMOUNTS INCLUDED.—

“(1) IN GENERAL.—If a foreign corporation is a controlled foreign corporation for an uninterrupted period of 30 days or more during any taxable year beginning after December 31, 1962, every person who is a United States shareholder (as defined in subsection (b)) of such corporation and who owns (within the meaning of section 958(a)) stock in such corporation on the last day, in such year, on which such corporation is a controlled foreign corporation shall include in his gross income, for his taxable year in which or with which such taxable year of the corporation ends— *Post*, p. 1018.

“(A) the sum of—

“(i) except as provided in section 963, his pro rata share (determined under paragraph (2)) of the corporation's subpart F income for such year, and *Post*, p. 1023.

“(ii) his pro rata share (determined under section 955(a)(3)) of the corporation's previously excluded subpart F income withdrawn from investment in less developed countries for such year; and

“(B) his pro rata share (determined under section 956(a)(2)) of the corporation's increase in earnings invested in United States property for such year (but only to the extent not excluded from gross income under section 959(a)(2)). *Post*, p. 1015.

“(2) PRO RATA SHARE OF SUBPART F INCOME.—The pro rata share referred to in paragraph (1)(A)(i) in the case of any United States shareholder is the amount— *Post*, p. 1019.

“(A) which would have been distributed with respect to the stock which such shareholder owns (within the meaning of section 958(a)) in such corporation if on the last day, in its taxable year, on which the corporation is a controlled foreign corporation it had distributed pro rata to its shareholders an amount (i) which bears the same ratio to its subpart F income for the taxable year, as (ii) the part of such year during which the corporation is a controlled foreign corporation bears to the entire year, reduced by

“(B) the amount of distributions received by any other person during such year as a dividend with respect to such stock, but only to the extent of the dividend which would have been received if the distribution by the corporation had been the amount (i) which bears the same ratio to the subpart F income of such corporation for the taxable year, as (ii) the part of such year during which such shareholder did not own (within the meaning of section 958(a)) such stock bears to the entire year.

“(3) LIMITATION ON PRO RATA SHARE OF PREVIOUSLY EXCLUDED SUBPART F INCOME WITHDRAWN FROM INVESTMENT.—For purposes of paragraph (1) (A) (ii), the pro rata share of any United States shareholder of the previously excluded subpart F income of a controlled foreign corporation withdrawn from investment in less developed countries shall not exceed an amount (A) which bears the same ratio to his pro rata share of such income withdrawn (as determined under section 955(a)(3)) for the taxable year, as (B) the part of such year during which the corporation is a controlled foreign corporation bears to the entire year.

“(4) LIMITATION ON PRO RATA SHARE OF INVESTMENT IN UNITED STATES PROPERTY.—For purposes of paragraph (1) (B), the pro rata share of any United States shareholder in the increase of the earnings of a controlled foreign corporation invested in United States property shall not exceed an amount (A) which bears the same ratio to his pro rata share of such increase (as determined under section 956(a)(2)) for the taxable year, as (B) the part of such year during which the corporation is a controlled foreign corporation bears to the entire year.

“(b) UNITED STATES SHAREHOLDER DEFINED.—For purposes of this subpart, the term ‘United States shareholder’ means, with respect to any foreign corporation, a United States person (as defined in section 957(d)) who owns (within the meaning of section 958(a)), or is considered as owning by applying the rules of ownership of section 958(b), 10 percent or more of the total combined voting power of all classes of stock entitled to vote of such foreign corporation.

“(c) COORDINATION WITH ELECTION OF A FOREIGN INVESTMENT COMPANY TO DISTRIBUTE INCOME.—A United States shareholder who, for his taxable year, is a qualified shareholder (within the meaning of section 1247(c)) of a foreign investment company with respect to which an election under section 1247 is in effect shall not be required to include in gross income, for such taxable year, any amount under subsection (a) with respect to such company.

“(d) COORDINATION WITH FOREIGN PERSONAL HOLDING COMPANY PROVISIONS.—A United States shareholder who, for his taxable year, is subject to tax under section 551(b) (relating to foreign personal holding company income included in gross income of United States shareholders) on income of a controlled foreign corporation shall not be required to include in gross income, for such taxable year, any amount under subsection (a) with respect to such company.

Post, p. 1018.

Post, p. 1013.

Post, p. 1039.

26 USC 551.

"SEC. 952. SUBPART F INCOME DEFINED.

"(a) **IN GENERAL.**—For purposes of this subpart, the term 'subpart F income' means, in the case of any controlled foreign corporation, the sum of—

"(1) the income derived from the insurance of United States risks (as determined under section 953), and

"(2) the foreign base company income (as determined under section 954).

Infra.

"(b) **EXCLUSION OF UNITED STATES INCOME.**—Subpart F income does not include any item includible in gross income under this chapter (other than this subpart) as income derived from sources within the United States of a foreign corporation engaged in trade or business in the United States.

"(c) **LIMITATION.**—For purposes of subsection (a), the subpart F income of any controlled foreign corporation for any taxable year shall not exceed the earnings and profits of such corporation for such year reduced by the amount (if any) by which—

"(1) an amount equal to—

"(A) the sum of the deficits in earnings and profits for prior taxable years beginning after December 31, 1962, plus

"(B) the sum of the deficits in earnings and profits for taxable years beginning after December 31, 1959, and before January 1, 1963 (reduced by the sum of the earnings and profits for such taxable years); exceeds

"(2) an amount equal to the sum of the earnings and profits for prior taxable years beginning after December 31, 1962, allocated to other earnings and profits under section 959(c)(3).

Post, p. 1019.

For purposes of the preceding sentence, any deficit in earnings and profits for any prior taxable year shall be taken into account under paragraph (1) for any taxable year only to the extent it has not been taken into account under such paragraph for any preceding taxable year to reduce earnings and profits of such preceding year.

"(d) **SPECIAL RULE IN CASE OF INDIRECT OWNERSHIP.**—For purposes of subsection (c), if—

"(1) a United States shareholder owns (within the meaning of section 958(a)) stock of a foreign corporation, and by reason of such ownership owns (within the meaning of such section) stock of any other foreign corporation, and

"(2) any of such foreign corporations has a deficit in earnings and profits for the taxable year,

then the earnings and profits for the taxable year of each such foreign corporation which is a controlled foreign corporation shall, with respect to such United States shareholder, be properly reduced to take into account any deficit described in paragraph (2) in such manner as the Secretary or his delegate shall prescribe by regulations.

"SEC. 953. INCOME FROM INSURANCE OF UNITED STATES RISKS.

"(a) **GENERAL RULE.**—For purposes of section 952(a)(1), the term 'income derived from the insurance of United States risks' means that income which—

"(1) is attributable to the reinsurance or the issuing of any insurance or annuity contract—

"(A) in connection with property in, or liability arising out of activity in, or in connection with the lives or health of residents of, the United States, or

"(B) in connection with risks not included in subparagraph (A) as the result of any arrangement whereby another corporation receives a substantially equal amount of premiums or other consideration in respect to any reinsurance or the issuing of any insurance or annuity contract in connection

with property in, or liability arising out of activity in, or in connection with the lives or health of residents of, the United States. and

“(2) would (subject to the modifications provided by paragraphs (1), (2), and (3) of subsection (b)) be taxed under subchapter L of this chapter if such income were the income of a domestic insurance corporation.

This section shall apply only in the case of a controlled foreign corporation which receives, during any taxable year, premiums or other consideration in respect of the reinsurance, and the issuing, of insurance and annuity contracts described in paragraph (1) in excess of 5 percent of the total of premiums and other consideration received during such taxable year in respect of all reinsurance and issuing of insurance and annuity contracts.

“(b) SPECIAL RULES.—For purposes of subsection (a)—

“(1) In the application of part I of subchapter L, life insurance company taxable income is the gain from operations as defined in section 809(b).

“(2) A corporation which would, if it were a domestic insurance corporation, be taxable under part II of subchapter L shall apply subsection (a) as if it were taxable under part III of subchapter L.

“(3) The following provisions of subchapter L shall not apply:

“(A) Section 809(d)(4) (operations loss deduction).

“(B) Section 809(d)(5) (certain nonparticipating contracts).

“(C) Section 809(d)(6) (group life, accident, and health insurance).

“(D) Section 809(d)(10) (small business deduction).

“(E) Section 817(b) (gain on property held on December 31, 1958, and certain substituted property acquired after 1958).

“(F) Section 832(b)(5) (certain capital losses).

“(4) The items referred to in—

“(A) section 809(c)(1) (relating to gross amount of premiums and other considerations),

“(B) section 809(c)(2) (relating to net decrease in reserves),

“(C) section 809(d)(2) (relating to net increase in reserves), and

“(D) section 832(b)(4) (relating to premiums earned on insurance contracts),

shall be taken into account only to the extent they are in respect of any reinsurance or the issuing of any insurance or annuity contract described in subsection (a)(1).

“(5) All items of income, expenses, losses, and deductions (other than those taken into account under paragraph (4)) shall be properly allocated or apportioned under regulations prescribed by the Secretary or his delegate.

“SEC. 954. FOREIGN BASE COMPANY INCOME.

“(a) FOREIGN BASE COMPANY INCOME.—For purposes of section 952(a)(2), the term ‘foreign base company income’ means for any taxable year the sum of—

“(1) the foreign personal holding company income for the taxable year (determined under subsection (c) and reduced as provided in subsection (b)(5)),

“(2) the foreign base company sales income for the taxable year (determined under subsection (d) and reduced as provided in subsection (b)(5)), and

26 USC 809.

26 USC 821-826;
Ante, pp. 114,
989-999.

"(3) the foreign base company services income for the taxable year (determined under subsection (e) and reduced as provided in subsection (b) (5)).

"(b) EXCLUSIONS AND SPECIAL RULES.—

"(1) EXCLUSION OF CERTAIN DIVIDENDS, INTEREST, AND GAINS FROM QUALIFIED INVESTMENTS IN LESS DEVELOPED COUNTRIES.—For purposes of subsection (a), foreign base company income does not include—

"(A) dividends and interest received during the taxable year from investments which at the time of receipt are qualified investments in less developed countries (as defined in section 955(b)), or

"(B) if the gains from the sale or exchange during the taxable year of investments which at the time of sale or exchange are qualified investments in less developed countries exceed the losses from the sale or exchange during the taxable year of such qualified investments, the amount by which such gains exceed such losses.

Post, p. 1013.

The preceding sentence shall apply only to the extent that the sum of the dividends and interest described in subparagraph (A) and the amount described in subparagraph (B) does not exceed the increase for the taxable year in qualified investments in less developed countries of the controlled foreign corporation (as determined under subsection (f)).

"(2) EXCLUSION OF CERTAIN SHIPPING INCOME.—For purposes of subsection (a), foreign base company income does not include income derived from, or in connection with, the use (or hiring or leasing for use) of any aircraft or vessel in foreign commerce, or the performance of services directly related to the use of any such aircraft or vessel.

"(3) SPECIAL RULE WHERE FOREIGN BASE COMPANY INCOME IS LESS THAN 30 PERCENT OR MORE THAN 70 PERCENT OF GROSS INCOME.—For purposes of subsection (a)—

"(A) If the foreign base company income (determined without regard to paragraphs (1) and (5)) is less than 30 percent of gross income, no part of the gross income of the taxable year shall be treated as foreign base company income.

"(B) If the foreign base company income (determined without regard to paragraphs (1) and (5)) exceeds 70 percent of gross income, the entire gross income of the taxable year shall, subject to the provisions of paragraphs (1), (2), (4), and (5), be treated as foreign base company income.

"(4) EXCEPTION FOR FOREIGN CORPORATIONS NOT AVAILABLE TO REDUCE TAXES.—For purposes of subsection (a), foreign base company income does not include any item of income received by a controlled foreign corporation if it is established to the satisfaction of the Secretary or his delegate with respect to such item that the creation or organization of the controlled foreign corporation receiving such item under the laws of the foreign country in which it is incorporated does not have the effect of substantial reduction of income, war profits, or excess profits taxes or similar taxes.

"(5) DEDUCTIONS TO BE TAKEN INTO ACCOUNT.—For purposes of subsection (a), the foreign personal holding company income, the foreign base company sales income, and the foreign base company services income shall be reduced, under regulations prescribed by the Secretary or his delegate, so as to take into account deductions (including taxes) properly allocable to such income.

26 USC 553.

“(c) FOREIGN PERSONAL HOLDING COMPANY INCOME.—

“(1) IN GENERAL.—For purposes of subsection (a) (1), the term ‘foreign personal holding company income’ means the foreign personal holding company income (as defined in section 553), modified and adjusted as provided in paragraphs (2), (3), and (4).

“(2) RENTS INCLUDED WITHOUT REGARD TO 50 PERCENT LIMITATION.—For purposes of paragraph (1), all rents shall be included in foreign personal holding company income without regard to whether or not such rents constitute 50 percent or more of gross income.

“(3) CERTAIN INCOME DERIVED IN ACTIVE CONDUCT OF TRADE OR BUSINESS.—For purposes of paragraph (1), foreign personal holding company income does not include—

“(A) rents and royalties which are derived in the active conduct of a trade or business and which are received from a person other than a related person (within the meaning of subsection (d) (3)), or

“(B) dividends, interest, and gains from the sale or exchange of stock or securities derived in the conduct of a banking, financing, or similar business, or derived from the investments made by an insurance company of its unearned premiums or reserves ordinary and necessary for the proper conduct of its insurance business, and which are received from a person other than a related person (within the meaning of subsection (d) (3)).

“(4) CERTAIN INCOME RECEIVED FROM RELATED PERSONS.—For purposes of paragraph (1), foreign personal holding company income does not include—

“(A) dividends and interest received from a related person which (i) is created or organized under the laws of the same foreign country under the laws of which the controlled foreign corporation is created or organized, and (ii) has a substantial part of its assets used in its trade or business located in such same foreign country;

“(B) interest received in the conduct of a banking, financing, or similar business from a related person engaged in the conduct of a banking, financing, or similar business if the businesses of the recipient and the payor are predominantly with persons other than related persons; and

“(C) rents, royalties, and similar amounts received from a related person for the use of, or the privilege of using, property within the country under the laws of which the controlled foreign corporation is created or organized.

“(d) FOREIGN BASE COMPANY SALES INCOME.—

“(1) IN GENERAL.—For purposes of subsection (a) (2), the term ‘foreign base company sales income’ means income (whether in the form of profits, commissions, fees, or otherwise) derived in connection with the purchase of personal property from a related person and its sale to any person, the sale of personal property to any person on behalf of a related person, the purchase of personal property from any person and its sale to a related person, or the purchase of personal property from any person on behalf of a related person where—

“(A) the property which is purchased (or in the case of property sold on behalf of a related person, the property which is sold) is manufactured, produced, grown, or extracted outside the country under the laws of which the controlled foreign corporation is created or organized, and

“(B) the property is sold for use, consumption, or disposition outside such foreign country, or, in the case of property purchased on behalf of a related person, is purchased for use, consumption, or disposition outside such foreign country.

“(2) CERTAIN BRANCH INCOME.—For purposes of determining foreign base company sales income in situations in which the carrying on of activities by a controlled foreign corporation through a branch or similar establishment outside the country of incorporation of the controlled foreign corporation has substantially the same effect as if such branch or similar establishment were a wholly owned subsidiary corporation deriving such income, under regulations prescribed by the Secretary or his delegate the income attributable to the carrying on of such activities of such branch or similar establishment shall be treated as income derived by a wholly owned subsidiary of the controlled foreign corporation and shall constitute foreign base company sales income of the controlled foreign corporation.

“(3) RELATED PERSON DEFINED.—For purposes of this section, a person is a related person with respect to a controlled foreign corporation, if—

“(A) such person is an individual, partnership, trust, or estate which controls the controlled foreign corporation;

“(B) such person is a corporation which controls, or is controlled by, the controlled foreign corporation; or

“(C) such person is a corporation which is controlled by the same person or persons which control the controlled foreign corporation.

For purposes of the preceding sentence, control means the ownership, directly or indirectly, of stock possessing more than 50 percent of the total combined voting power of all classes of stock entitled to vote. For purposes of this paragraph, the rules for determining ownership of stock prescribed by section 958 shall apply.

“(e) FOREIGN BASE COMPANY SERVICES INCOME.—For purposes of subsection (a) (3), the term ‘foreign base company services income’ means income (whether in the form of compensation, commissions, fees, or otherwise) derived in connection with the performance of technical, managerial, engineering, architectural, scientific, skilled, industrial, commercial, or like services which—

“(1) are performed for or on behalf of any related person (within the meaning of subsection (d) (3)), and

“(2) are performed outside the country under the laws of which the controlled foreign corporation is created or organized.

The preceding sentence shall not apply to income derived in connection with the performance of services which are directly related to the sale or exchange by the controlled foreign corporation of property manufactured, produced, grown, or extracted by it and which are performed prior to the time of the sale or exchange, or of services directly related to an offer or effort to sell or exchange such property.

“(f) INCREASE IN QUALIFIED INVESTMENTS IN LESS DEVELOPED COUNTRIES.—For purposes of subsection (b) (1), the increase for any taxable year in qualified investments in less developed countries of any controlled foreign corporation is the amount by which—

“(1) the qualified investments in less developed countries (as defined in section 955(b)) of the controlled foreign corporation at the close of the taxable year, exceeds Post, p. 1013.

“(2) the qualified investments in less developed countries (as so defined) of the controlled foreign corporation at the close of the preceding taxable year.

“SEC. 955. WITHDRAWAL OF PREVIOUSLY EXCLUDED SUBPART F INCOME FROM QUALIFIED INVESTMENT.

“(a) GENERAL RULES.—

“(1) **AMOUNT WITHDRAWN.**—For purposes of this subpart, the amount of previously excluded subpart F income of any controlled foreign corporation withdrawn from investment in less developed countries for any taxable year is an amount equal to the decrease in the amount of qualified investments in less developed countries of the controlled foreign corporation for such year, but only to the extent that the amount of such decrease does not exceed an amount equal to—

“(A) the sum of the amounts excluded under section 954

(b) (1) from the foreign base company income of such corporation for all prior taxable years, reduced by

“(B) the sum of the amounts of previously excluded subpart F income withdrawn from investment in less developed countries of such corporation determined under this subsection for all prior taxable years.

“(2) **DECREASE IN QUALIFIED INVESTMENTS.**—For purposes of paragraph (1), the amount of the decrease in qualified investments in less developed countries of any controlled foreign corporation for any taxable year is the amount by which—

“(A) the amount of qualified investments in less developed countries of the controlled foreign corporation at the close of the preceding taxable year, exceeds

“(B) the amount of qualified investments in less developed countries of the controlled foreign corporation at the close of the taxable year,

to the extent the amount of such decrease does not exceed the sum of the earnings and profits for the taxable year and the earnings and profits accumulated for prior taxable years beginning after December 31, 1962. For purposes of this paragraph, if qualified investments in less developed countries are disposed of by the controlled foreign corporation during the taxable year, the amount of the decrease in qualified investments in less developed countries of such controlled foreign corporation for such year shall be reduced by an amount equal to the amount (if any) by which the losses on such dispositions during such year exceed the gains on such dispositions during such year.

“(3) **PRO RATA SHARE OF AMOUNT WITHDRAWN.**—In the case of any United States shareholder, the pro rata share of the amount of previously excluded subpart F income of any controlled foreign corporation withdrawn from investment in less developed countries for any taxable year is his pro rata share of the amount determined under paragraph (1).

“(b) QUALIFIED INVESTMENTS IN LESS DEVELOPED COUNTRIES.—

“(1) **IN GENERAL.**—For purposes of this subpart, the term ‘qualified investments in less developed countries’ means property which is—

“(A) stock of a less developed country corporation held by the controlled foreign corporation, but only if the controlled foreign corporation owns 10 percent or more of the total combined voting power of all classes of stock of such less developed country corporation;

“(B) an obligation of a less developed country corporation held by the controlled foreign corporation, which, at the

time of its acquisition by the controlled foreign corporation, has a maturity of one year or more, but only if the controlled foreign corporation owns 10 percent or more of the total combined voting power of all classes of stock of such less developed country corporation; or

“(C) an obligation of a less developed country.

“(2) COUNTRY CEASES TO BE LESS DEVELOPED COUNTRY.—For purposes of this subpart, property which would be a qualified investment in less developed countries, but for the fact that a foreign country has, after the acquisition of such property by the controlled foreign corporation, ceased to be a less developed country, shall be treated as a qualified investment in less developed countries.

“(3) SPECIAL RULE.—For purposes of this subpart, a United States shareholder of a controlled foreign corporation may, under regulations prescribed by the Secretary or his delegate, make the determinations under subsection (a) (2) of this section and under subsection (f) of section 954 as of the close of the years following the years referred to in such subsections, or as of the close of such longer period of time as such regulations may permit, in lieu of on the last day of such years. Any election under this paragraph made with respect to any taxable year shall apply to such year and to all succeeding taxable years unless the Secretary or his delegate consents to the revocation of such election.

Ante, p. 1012.

“(4) EXCEPTION.—For purposes of this subpart, property shall not constitute qualified investments in less developed countries if such property is disposed of within 6 months after the date of its acquisition.

“(5) AMOUNT ATTRIBUTABLE TO PROPERTY.—The amount taken into account under this subpart with respect to any property described in paragraph (1) or (2) shall be its adjusted basis, reduced by any liability to which such property is subject.

“(c) LESS DEVELOPED COUNTRY CORPORATIONS.—

“(1) IN GENERAL.—For purposes of this subpart, the term ‘less developed country corporation’ means a foreign corporation which during the taxable year is engaged in the active conduct of one or more trades or businesses and—

“(A) 80 percent or more of the gross income of which for the taxable year is derived from sources within less developed countries; and

“(B) 80 percent or more in value of the assets of which on each day of the taxable year consists of—

“(i) property used in such trades or businesses and located in less developed countries,

“(ii) money, and deposits with persons carrying on the banking business,

“(iii) stock, and obligations which, at the time of their acquisition, have a maturity of one year or more, of any other less developed country corporation,

“(iv) an obligation of a less developed country,

“(v) an investment which is required because of restrictions imposed by a less developed country, and

“(vi) property described in section 956(b) (2).

Post, p. 1016.

For purposes of subparagraph (A), the determination as to whether income is derived from sources within less developed countries shall be made under regulations prescribed by the Secretary or his delegate.

“(2) SHIPPING COMPANIES.—For purposes of this subpart, the term ‘less developed country corporation’ also means a foreign corporation—

“(A) 80 percent or more of the gross income of which for the taxable year consists of—

“(i) gross income derived from, or in connection with, the using (or hiring or leasing for use) in foreign commerce of aircraft or vessels registered under the laws of a less developed country, or from, or in connection with, the performance of services directly related to use of such aircraft or vessels, or from the sale or exchange of such aircraft or vessels, and

“(ii) dividends and interest received from foreign corporations which are less developed country corporations within the meaning of this paragraph and 10 percent or more of the total combined voting power of all classes of stock of which are owned by the foreign corporation, and gain from the sale or exchange of stock or obligations of foreign corporations which are such less developed country corporations, and

“(B) 80 percent or more of the assets of which on each day of the taxable year consists of (i) assets used, or held for use, for or in connection with the production of income described in subparagraph (A), and (ii) property described in section 956(b) (2).

Post, p. 1016.

“(3) LESS DEVELOPED COUNTRY DEFINED.—For purposes of this subpart, the term ‘less developed country’ means (in respect of any foreign corporation) any foreign country (other than an area within the Sino-Soviet bloc) or any possession of the United States with respect to which, on the first day of the taxable year, there is in effect an Executive order by the President of the United States designating such country or possession as an economically less developed country for purposes of this subpart. For purposes of the preceding sentence, an overseas territory, department, province, or possession may be treated as a separate country. No designation shall be made under this paragraph with respect to—

Australia

Austria

Belgium

Canada

Denmark

France

Germany (Federal Republic)

Hong Kong

Italy

Japan

Liechtenstein

Luxembourg

Monaco

Netherlands

New Zealand

Norway

Union of South Africa

San Marino

Sweden

Switzerland

United Kingdom

After the President has designated any foreign country or any possession of the United States as an economically less developed country for purposes of this subpart, he shall not terminate such designation (either by issuing an Executive order for that purpose or by issuing an Executive order under the first sentence of this paragraph which has the effect of terminating such designation) unless, at least 30 days prior to such termination, he has notified the Senate and the House of Representatives of his intention to terminate such designation.

“SEC. 956. INVESTMENT OF EARNINGS IN UNITED STATES PROPERTY.

“(a) GENERAL RULES.—For purposes of this subpart—

“(1) AMOUNT OF INVESTMENT.—The amount of earnings of a controlled foreign corporation invested in United States property at the close of any taxable year is the aggregate amount of such property held, directly or indirectly, by the controlled foreign

corporation at the close of the taxable year, to the extent such amount would have constituted a dividend (determined after the application of section 955(a)) if it had been distributed.

Ante, p. 1013.

"(2) PRO RATA SHARE OF INCREASE FOR YEAR.—In the case of any United States shareholder, the pro rata share of the increase for any taxable year in the earnings of a controlled foreign corporation invested in United States property is the amount determined by subtracting his pro rata share of—

"(A) the amount determined under paragraph (1) for the close of the preceding taxable year, reduced by amounts paid during such preceding taxable year to which section 959(c)(1) applies, from

Post, p. 1019.

"(B) the amount determined under paragraph (1) for the close of the taxable year.

The determinations under subparagraphs (A) and (B) shall be made on the basis of stock owned (within the meaning of section 958(a)) by such United States shareholder on the last day during the taxable year on which the foreign corporation is a controlled foreign corporation.

Post, p. 1018.

"(3) AMOUNT ATTRIBUTABLE TO PROPERTY.—The amount taken into account under paragraph (1) or (2) with respect to any property shall be its adjusted basis, reduced by any liability to which the property is subject.

• (b) UNITED STATES PROPERTY DEFINED.—

"(1) IN GENERAL.—For purposes of subsection (a), the term 'United States property' means any property acquired after December 31, 1962, which is—

"(A) tangible property located in the United States;

"(B) stock of a domestic corporation;

"(C) an obligation of a United States person; or

"(D) any right to the use in the United States of—

"(i) a patent or copyright,

"(ii) an invention, model, or design (whether or not patented),

"(iii) a secret formula or process, or

"(iv) any other similar property right,

which is acquired or developed by the controlled foreign corporation for use in the United States.

"(2) EXCEPTIONS.—For purposes of subsection (a), the term 'United States property' does not include—

"(A) obligations of the United States, money, or deposits with persons carrying on the banking business;

"(B) property located in the United States which is purchased in the United States for export to, or use in, foreign countries;

"(C) any obligation of a United States person arising in connection with the sale or processing of property if the amount of such obligation outstanding at no time during the taxable year exceeds the amount which would be ordinary and necessary to carry on the trade or business of both the other party to the sale or processing transaction and the United States person had the sale or processing transaction been made between unrelated persons;

"(D) any aircraft, railroad rolling stock, vessel, motor vehicle, or container used in the transportation of persons or property in foreign commerce and used predominantly outside the United States;

"(E) an amount of assets of an insurance company equivalent to the unearned premiums or reserves ordinary and necessary for the proper conduct of its insurance business

attributable to contracts which are not contracts described in section 953(a)(1); and

Ante, p. 1008.

“(F) an amount of assets of the controlled foreign corporation equal to the earnings and profits accumulated after December 31, 1962, and excluded from subpart F income under section 952(b).

Ante, p. 1008.

“(c) PLEDGES AND GUARANTEES.—For purposes of subsection (a), a controlled foreign corporation shall, under regulations prescribed by the Secretary or his delegate, be considered as holding an obligation of a United States person if such controlled foreign corporation is a pledgor or guarantor of such obligation.

“SEC. 957. CONTROLLED FOREIGN CORPORATIONS; UNITED STATES PERSONS.

“(a) GENERAL RULE.—For purposes of this subpart, the term ‘controlled foreign corporation’ means any foreign corporation of which more than 50 percent of the total combined voting power of all classes of stock entitled to vote is owned (within the meaning of section 958(a)), or is considered as owned by applying the rules of ownership of section 958(b), by United States shareholders on any day during the taxable year of such foreign corporation.

Post, p. 1018.

“(b) SPECIAL RULE FOR INSURANCE.—For purposes only of taking into account income described in section 953(a) (relating to income derived from insurance of United States risks), the term ‘controlled foreign corporation’ includes not only a foreign corporation as defined by subsection (a) but also one of which more than 25 percent of the total combined voting power of all classes of stock is owned (within the meaning of section 958(a)), or is considered as owned by applying the rules of ownership of section 958(b), by United States shareholders on any day during the taxable year of such corporation, if the gross amount of premiums or other consideration in respect of the reinsurance or the issuing of insurance or annuity contracts described in section 953(a)(1) exceeds 75 percent of the gross amount of all premiums or other consideration in respect of all risks.

“(c) CORPORATIONS ORGANIZED IN UNITED STATES POSSESSIONS.—For purposes of this subpart, the term ‘controlled foreign corporation’ does not include any corporation created or organized in the Commonwealth of Puerto Rico or a possession of the United States or under the laws of the Commonwealth of Puerto Rico or a possession of the United States if—

“(1) 80 percent or more of the gross income of such corporation for the 3-year period immediately preceding the close of the taxable year (or for such part of such period immediately preceding the close of such taxable year as may be applicable) was derived from sources within the Commonwealth of Puerto Rico or a possession of the United States; and

“(2) 50 percent or more of the gross income of such corporation for such period, or for such part thereof, was derived from the active conduct within the Commonwealth of Puerto Rico or a possession of the United States of any trades or businesses constituting the manufacture or processing of goods, wares, merchandise, or other tangible personal property; the processing of agricultural or horticultural products or commodities (including but not limited to livestock, poultry, or fur-bearing animals); the catching or taking of any kind of fish or the mining or extraction of natural resources, or any manufacturing or processing of any products or commodities obtained from such activities; or the ownership or operation of hotels.

For purposes of paragraphs (1) and (2), the determination as to whether income was derived from sources within the Commonwealth

of Puerto Rico or a possession of the United States and was derived from the active conduct of a described trade or business within the Commonwealth of Puerto Rico or a possession of the United States shall be made under regulations prescribed by the Secretary or his delegate.

"(d) UNITED STATES PERSON.—For purposes of this subpart, the term 'United States person' has the meaning assigned to it by section 7701(a) (30) except that—

Ante, p. 988.

"(1) with respect to a corporation organized under the laws of the Commonwealth of Puerto Rico, such term does not include an individual who is a bona fide resident of Puerto Rico, if a dividend received by such individual during the taxable year from such corporation would, for purposes of section 933(1), be treated as income derived from sources within Puerto Rico,

26 USC 933.

"(2) with respect to a corporation organized under the laws of the Virgin Islands, such term does not include an individual who is a bona fide resident of the Virgin Islands and whose income tax obligation under this subtitle for the taxable year is satisfied pursuant to section 28(a) of the Revised Organic Act of the Virgin Islands, approved July 22, 1954 (48 U.S.C. 1642), by paying tax on income derived from all sources both within and outside the Virgin Islands into the treasury of the Virgin Islands, and

68 Stat. 508.

"(3) with respect to a corporation organized under the laws of any other possession of the United States, such term does not include an individual who is a bona fide resident of any such other possession and whose income derived from sources within possessions of the United States is not, by reason of section 931 (a), includible in gross income under this subtitle for the taxable year.

SEC. 958. RULES FOR DETERMINING STOCK OWNERSHIP.

"(a) DIRECT AND INDIRECT OWNERSHIP.—

"(1) GENERAL RULE.—For purposes of this subpart (other than sections 955(b)(1) (A) and (B), 955(c)(2) (A) (ii), and 960 (a) (1)), stock owned means—

Ante, p. 1013.
Post, p. 1020.

"(A) stock owned directly, and

"(B) stock owned with the application of paragraph (2).

"(2) STOCK OWNERSHIP THROUGH FOREIGN ENTITIES.—For purposes of subparagraph (B) of paragraph (1), stock owned, directly or indirectly, by or for a foreign corporation, foreign partnership, or foreign trust or foreign estate (within the meaning of section 7701(a) (31)) shall be considered as being owned proportionately by its shareholders, partners, or beneficiaries. Stock considered to be owned by a person by reason of the application of the preceding sentence shall, for purposes of applying such sentence, be treated as actually owned by such person.

Ante, p. 988.

"(3) SPECIAL RULE FOR MUTUAL INSURANCE COMPANIES.—For purposes of applying paragraph (1) in the case of a foreign mutual insurance company, the term 'stock' shall include any certificate entitling the holder to voting power in the corporation.

"(b) CONSTRUCTIVE OWNERSHIP.—For purposes of sections 951(b), 954(d) (3), and 957, section 318(a) (relating to constructive ownership of stock) shall apply to the extent that the effect is to treat any United States person as a United States shareholder within the meaning of section 951(b), to treat a person as a related person within the meaning of section 954(d) (3), or to treat a foreign corporation as a controlled foreign corporation under section 957, except that—

26 USC 318.

"(1) In applying paragraph (1) (A) of section 318(a), stock owned by a nonresident alien individual (other than a foreign trust or foreign estate) shall not be considered as owned by a citizen or by a resident alien individual.

26 USC 318.

"(2) In applying the first sentence of subparagraphs (A) and (B), and in applying clause (i) of subparagraph (C), of section 318(a) (2), if a partnership, estate, trust, or corporation owns, directly or indirectly, more than 50 percent of the total combined voting power of all classes of stock entitled to vote of a corporation, it shall be considered as owning all the stock entitled to vote.

"(3) Stock owned by a partnership, estate, trust, or corporation, by reason of the application of the second sentence of subparagraphs (A) and (B), and the application of clause (ii) of subparagraph (C), of section 318(a) (2), shall not be considered as owned by such partnership, estate, trust, or corporation, for purposes of applying the first sentence of subparagraphs (A) and (B), and in applying clause (i) of subparagraph (C), of section 318(a) (2).

"(4) In applying clause (i) of subparagraph (C) of section 318(a) (2), the phrase '10 percent' shall be substituted for the phrase '50 percent' used in subparagraph (C).

"(5) The second sentence of subparagraphs (A) and (B), and clause (ii) of subparagraph (C), of section 318(a) (2) shall not be applied so as to consider a United States person as owning stock which is owned by a person who is not a United States person.

"SEC. 959. EXCLUSION FROM GROSS INCOME OF PREVIOUSLY TAXED EARNINGS AND PROFITS.

"(a) **EXCLUSION FROM GROSS INCOME OF UNITED STATES PERSONS.**—For purposes of this chapter, the earnings and profits for a taxable year of a foreign corporation attributable to amounts which are, or have been, included in the gross income of a United States shareholder under section 951(a) shall not, when—

"(1) such amounts are distributed to, or

"(2) such amounts would, but for this subsection, be included under section 951(a) (1) (B) in the gross income of,

Ante, p. 1006.

such shareholder (or any other United States person who acquires from any person any portion of the interest of such United States shareholder in such foreign corporation, but only to the extent of such portion, and subject to such proof of the identity of such interest as the Secretary or his delegate may by regulations prescribe) directly, or indirectly through a chain of ownership described under section 958(a), be again included in the gross income of such United States shareholder (or of such other United States person).

"(b) **EXCLUSION FROM GROSS INCOME OF CERTAIN FOREIGN SUBSIDIARIES.**—For purposes of section 951(a), the earnings and profits for a taxable year of a controlled foreign corporation attributable to amounts which are, or have been, included in the gross income of a United States shareholder under section 951(a), shall not, when distributed through a chain of ownership described under section 958(a), be also included in the gross income of another controlled foreign corporation in such chain for purposes of the application of section 951(a) to such other controlled foreign corporation with respect to such United States shareholder (or to any other United States shareholder who acquires from any person any portion of the interest of such United States shareholder in the controlled foreign corporation, but only to the extent of such portion, and subject to such proof of identity of such interest as the Secretary or his delegate may prescribe by regulations).

"(c) **ALLOCATION OF DISTRIBUTIONS.**—For purposes of subsections (a) and (b), section 316(a) shall be applied by applying paragraph (2) thereof, and then paragraph (1) thereof—

"(1) first to earnings and profits attributable to amounts included in gross income under section 951(a) (1) (B) (or which

26 USC 316.

would have been included except for subsection (a)(2) of this section),

"(2) then to earnings and profits attributable to amounts included in gross income under section 951(a)(1)(A) (but reduced by amounts not included under section 951(a)(1)(B) because of the exclusion in subsection (a)(2) of this section), and

Ante, p. 1006.

"(3) then to other earnings and profits.

"(d) DISTRIBUTIONS EXCLUDED FROM GROSS INCOME NOT TO BE TREATED AS DIVIDENDS.—Except as provided in section 960(a)(3), any distribution excluded from gross income under subsection (a) shall be treated, for purposes of this chapter, as a distribution which is not a dividend.

Infra.

"SEC. 960. SPECIAL RULES FOR FOREIGN TAX CREDIT.

"(a) TAXES PAID BY A FOREIGN CORPORATION.—

"(1) GENERAL RULE.—For purposes of subpart A of this part, if there is included, under section 951(a), in the gross income of a domestic corporation any amount attributable to earnings and profits—

"(A) of a foreign corporation at least 10 percent of the voting stock of which is owned by such domestic corporation, or

"(B) of a foreign corporation at least 50 percent of the voting stock of which is owned by a foreign corporation at least 10 percent of the voting stock of which is in turn owned by such domestic corporation,

then, under regulations prescribed by the Secretary or his delegate, such domestic corporation shall be deemed to have paid the same proportion of the total income, war profits, and excess profits taxes paid (or deemed paid) by such foreign corporation to a foreign country or possession of the United States for the taxable year on or with respect to the earnings and profits of such foreign corporation which the amount of earnings and profits of such foreign corporation so included in gross income of the domestic corporation bears to—

"(C) if the foreign corporation at least 10 percent of the voting stock of which is owned by such domestic corporation referred to in subparagraph (A) or (B) is not a less developed country corporation (as defined in section 902(d)) for such taxable year, the entire amount of the earnings and profits of such foreign corporation for such taxable year, or

Ante, p. 1000.

"(D) if the foreign corporation at least 10 percent of the voting stock of which is owned by such domestic corporation referred to in subparagraph (A) or (B) is a less developed country corporation (as defined in section 902(d)) for such taxable year, the sum of the entire amount of the earnings and profits of such foreign corporation for such taxable year and the total income, war profits, and excess profits taxes paid by such foreign corporation to foreign countries or possessions of the United States for such taxable year.

"(2) TAXES PREVIOUSLY DEEMED PAID BY DOMESTIC CORPORATION.—If a domestic corporation receives a distribution from a foreign corporation, any portion of which is excluded from gross income under section 959, the income, war profits, and excess profits taxes paid or deemed paid by such foreign corporation to any foreign country or to any possession of the United States in connection with the earnings and profits of such foreign corporation from which such distribution is made shall not be taken into account for purposes of section 902, to the extent such taxes

Ante, p. 1019.

were deemed paid by a domestic corporation under paragraph (1) for any prior taxable year.

“(3) TAXES PAID BY FOREIGN CORPORATION AND NOT PREVIOUSLY DEEMED PAID BY DOMESTIC CORPORATION.—Any portion of a distribution from a foreign corporation received by a domestic corporation which is excluded from gross income under section 959 (a) shall be treated by the domestic corporation as a dividend, solely for purposes of taking into account under section 902 any income, war profits, or excess profits taxes paid to any foreign country or to any possession of the United States, on or with respect to the accumulated profits of such foreign corporation from which such distribution is made, which were not deemed paid by the domestic corporation under paragraph (1) for any prior taxable year.

“(b) SPECIAL RULES FOR FOREIGN TAX CREDIT IN YEAR OF RECEIPT OF PREVIOUSLY TAXED EARNINGS AND PROFITS.—

“(1) INCREASE IN SECTION 904 LIMITATION.—In the case of any taxpayer who—

“(A) either (i) chose to have the benefits of subpart A of this part for a taxable year in which he was required under section 951 (a) to include in his gross income an amount in respect of a controlled foreign corporation, or (ii) did not pay or accrue for such taxable year any income, war profits, or excess profits taxes to any foreign country or to any possession of the United States, and

“(B) chooses to have the benefits of subpart A of this part for the taxable year in which he receives a distribution or amount which is excluded from gross income under section 959 (a) and which is attributable to earnings and profits of the controlled foreign corporation which was included in his gross income for the taxable year referred to in subparagraph (A), and

“(C) for the taxable year in which such distribution or amount is received, pays, or is deemed to have paid, or accrues income, war profits, or excess profits taxes to a foreign country or to any possession of the United States with respect to such distribution or amount,

the applicable limitation under section 904 for the taxable year in which such distribution or amount is received shall be increased as provided in paragraph (2), but such increase shall not exceed the amount of such taxes paid, or deemed paid, or accrued with respect to such distribution or amount.

“(2) AMOUNT OF INCREASE.—The amount of increase of the applicable limitation under section 904 (a) for the taxable year in which the distribution or amount referred to in paragraph (1) (B) is received shall be an amount equal to—

“(A) the amount by which the applicable limitation under section 904 (a) for the taxable year referred to in paragraph (1) (A) was increased by reason of the inclusion in gross income under section 951 (a) of the amount in respect of the controlled foreign corporation, reduced by

“(B) the amount of any income, war profits, and excess profits taxes paid, or deemed paid, or accrued to any foreign country or possession of the United States which were allowable as a credit under section 901 for the taxable year referred to in paragraph (1) (A) and which would not have been allowable but for the inclusion in gross income of the amount described in subparagraph (A).

Ante, p. 999.

Ante, p. 1006.

26 USC 904.

74 Stat. 1010.
26 USC 904.

26 USC 901;
Ante, p. 99.
Post, p. 1031.

"(3) CASES IN WHICH TAXES NOT TO BE ALLOWED AS DEDUCTION.—
In the case of any taxpayer who—

"(A) chose to have the benefits of subpart A of this part for a taxable year in which he was required under section 951(a) to include in his gross income an amount in respect of a controlled foreign corporation, and

"(B) does not choose to have the benefits of subpart A of this part for the taxable year in which he receives a distribution or amount which is excluded from gross income under section 959(a) and which is attributable to earnings and profits of the controlled foreign corporation which was included in his gross income for the taxable year referred to in subparagraph (A),

no deduction shall be allowed under section 164 for the taxable year in which such distribution or amount is received for any income, war profits, or excess profits taxes paid or accrued to any foreign country or to any possession of the United States on or with respect to such distribution or amount. 26 USC 164.

"(4) INSUFFICIENT TAXABLE INCOME.—If an increase in the limitation under this subsection exceeds the tax imposed by this chapter for such year, the amount of such excess shall be deemed an overpayment of tax for such year.

"SEC. 961. ADJUSTMENTS TO BASIS OF STOCK IN CONTROLLED FOREIGN CORPORATIONS AND OF OTHER PROPERTY.

"(a) INCREASE IN BASIS.—Under regulations prescribed by the Secretary or his delegate, the basis of a United States shareholder's stock in a controlled foreign corporation, and the basis of property of a United States shareholder by reason of which he is considered under section 958(a)(2) as owning stock of a controlled foreign corporation, shall be increased by the amount required to be included in his gross income under section 951(a) with respect to such stock or with respect to such property, as the case may be, but only to the extent to which such amount was included in the gross income of such United States shareholder. In the case of a United States shareholder who has made an election under section 962 for the taxable year, the increase in basis provided by this subsection shall not exceed an amount equal to the amount of tax paid under this chapter with respect to the amounts required to be included in his gross income under section 951(a). Ante, p. 1018. Ante, p. 1006. Post, p. 1023.

"(b) REDUCTION IN BASIS.—

"(1) IN GENERAL.—Under regulations prescribed by the Secretary or his delegate, the adjusted basis of stock or other property with respect to which a United States shareholder or a United States person receives an amount which is excluded from gross income under section 959(a) shall be reduced by the amount so excluded. In the case of a United States shareholder who has made an election under section 962 for any prior taxable year, the reduction in basis provided by this paragraph shall not exceed an amount equal to the amount received which is excluded from gross income under section 959(a) after the application of section 962(d). Ante, p. 1019.

"(2) AMOUNT IN EXCESS OF BASIS.—To the extent that an amount excluded from gross income under section 959(a) exceeds the adjusted basis of the stock or other property with respect to which it is received, the amount shall be treated as gain from the sale or exchange of property.

"SEC. 962. ELECTION BY INDIVIDUALS TO BE SUBJECT TO TAX AT CORPORATE RATES.

"(a) **GENERAL RULE.**—Under regulations prescribed by the Secretary or his delegate, in the case of a United States shareholder who is an individual and who elects to have the provisions of this section apply for the taxable year—

"(1) the tax imposed under this chapter on amounts which are included in his gross income under section 951(a) shall (in lieu of the tax determined under section 1) be an amount equal to the tax which would be imposed under section 11 if such amounts were received by a domestic corporation, and

"(2) for purposes of applying the provisions of section 960 (relating to foreign tax credit) such amounts shall be treated as if they were received by a domestic corporation.

"(b) **ELECTION.**—An election to have the provisions of this section apply for any taxable year shall be made by a United States shareholder at such time and in such manner as the Secretary or his delegate shall prescribe by regulations. An election made for any taxable year may not be revoked except with the consent of the Secretary or his delegate.

"(c) **SURTAX EXEMPTION.**—For purposes of applying subsection (a)(1), the surtax exemption provided by section 11(c) shall not exceed, in the case of any United States shareholder, an amount which bears the same ratio to \$25,000 as the amounts included in his gross income under section 951(a) for the taxable year bears to his pro rata share of the earnings and profits for the taxable year of all controlled foreign corporations with respect to which such United States shareholder includes any amount in gross income under section 951(a).

"(d) **SPECIAL RULE FOR ACTUAL DISTRIBUTIONS.**—The earnings and profits of a foreign corporation attributable to amounts which were included in the gross income of a United States shareholder under section 951(a) and with respect to which an election under this section applied shall, when such earnings and profits are distributed, notwithstanding the provisions of section 959(a)(1), be included in gross income to the extent that such earnings and profits so distributed exceed the amount of tax paid under this chapter on the amounts to which such election applied.

"SEC. 963. RECEIPT OF MINIMUM DISTRIBUTIONS BY DOMESTIC CORPORATIONS.

"(a) **GENERAL RULE.**—In the case of a United States shareholder which is a domestic corporation and which consents to all the regulations prescribed by the Secretary or his delegate under this section prior to the last day prescribed by law for filing its return of the tax imposed by this chapter for the taxable year, no amount shall be included in gross income under section 951(a)(1)(A)(i) for the taxable year with respect to the subpart F income of a controlled foreign corporation, if—

"(1) in the case of a controlled foreign corporation described in subsection (c)(1), the United States shareholder receives a minimum distribution of the earnings and profits for the taxable year of such controlled foreign corporation;

"(2) in the case of controlled foreign corporations described in subsection (c)(2), the United States shareholder receives a minimum distribution with respect to the consolidated earnings and profits for the taxable year of all such controlled foreign corporations; or

"(3) in the case of controlled foreign corporations described in subsection (c)(3), the United States shareholder receives a min-

Ante, p. 1006.

Ante, p. 1020.

68A Stat. 11.
26 USC 11.

Ante, p. 1019.

imum distribution of the consolidated earnings and profits for the taxable year of all such controlled foreign corporations.

“(b) **MINIMUM DISTRIBUTIONS.**—For purposes of this section, a minimum distribution with respect to the earnings and profits for the taxable year of any controlled foreign corporation or corporations shall, in the case of any United States shareholder, be its pro rata share of an amount determined in accordance with the following table:

If the effective foreign tax rate is (percentage)—	The required minimum distribution of earnings and profits is (percentage)—
Under 10.....	90
10 or over but less than 20.....	86
20 or over but less than 28.....	82
28 or over but less than 34.....	75
34 or over but less than 39.....	68
39 or over but less than 42.....	55
42 or over but less than 44.....	40
44 or over but less than 46.....	27
46 or over but less than 47.....	14
47 or over.....	0

“(c) **AMOUNTS TO WHICH SECTION APPLIES.**—

“(1) **FOREIGN SUBSIDIARIES.**—Subsection (a) (1) shall apply to amounts which (but for the provisions of this section) would be included in the gross income of the United States shareholder under section 951(a) (1) (A) (i) by reason of its ownership, within the meaning of section 958(a) (1) (A), of stock of a controlled foreign corporation. *Ante*, p. 1006.

“(2) **CHAIN OF CONTROLLED FOREIGN CORPORATIONS.**—Subsection (a) (2) shall apply to amounts which (but for the provisions of this section) would be included in the gross income of the United States shareholder under section 951(a) (1) (A) (i)—

“(A) by reason of its ownership, within the meaning of section 958(a) (1) (A), of stock of a controlled foreign corporation, and

“(B) to the extent that the United States shareholder so elects, by reason of its ownership, within the meaning of section 958(a) (2), of stock of any other controlled foreign corporation (on account of its ownership of the stock described in subparagraph (A) or of stock described in this subparagraph), but only if there is taken into account the earnings and profits of each foreign corporation, whether or not a controlled foreign corporation, by reason of which the United States shareholder owns, within the meaning of section 958(a) (2), stock of such controlled foreign corporation.

“(3) **ALL CONTROLLED FOREIGN CORPORATIONS.**—Except as provided in paragraph (4), subsection (a) (3) shall apply to amounts which (but for the provisions of this section) would be included in the gross income of the United States shareholder under section 951(a) (1) (A) (i)—

“(A) by reason of its ownership, within the meaning of section 958(a) (1) (A), of stock of all controlled foreign corporations in which it owns stock within the meaning of such section, and

“(B) by reason of its ownership, within the meaning of section 958(a) (2), of stock of all controlled foreign corporations in which it owns stock within the meaning of such section, but only if there is taken into account the earnings and profits of each foreign corporation, whether or not a controlled foreign corporation, by reason of which the United States shareholder owns, within the meaning of section 958(a), stock of any of such controlled foreign corporations.

“(4) EXCEPTIONS AND SPECIAL RULES.—

Ante, p.1006.

“(A) LESS DEVELOPED COUNTRY CORPORATIONS.—If the United States shareholder so elects, subsection (a)(3) and paragraph (3) of this subsection shall not apply to amounts which would be included in the gross income of such shareholder under section 951(a)(1)(A)(i) by reason of its ownership, within the meaning of section 958(a), of stock of controlled foreign corporations which are less developed country corporations (as defined in section 955(c)). This subparagraph shall not apply with respect to a less developed country corporation if, by reason of the ownership of the stock of such corporation, the United States shareholder owns, within the meaning of section 958(a)(2), stock of any other controlled foreign corporation which is not a less developed country corporation. Except as provided in the preceding sentence, an election under this subparagraph may be made only with respect to all controlled foreign corporations which are less developed country corporations and with respect to which the domestic corporation making the election is a United States shareholder.

“(B) FOREIGN BRANCHES.—In applying subsection (a)(3) and paragraph (3) of this subsection, if a United States shareholder so elects, all branches maintained by such shareholder in foreign countries, the Commonwealth of Puerto Rico, or possessions of the United States shall, under regulations prescribed by the Secretary or his delegate, be treated as wholly owned subsidiary corporations of such shareholder organized under the laws of such foreign countries, the Commonwealth of Puerto Rico, or possessions of the United States, as the case may be. Each branch so treated shall, for purposes of this section, be considered to have distributed to the United States shareholder all of its earnings and profits for the taxable year. This subparagraph shall not apply to a branch maintained by a United States shareholder in the Commonwealth of Puerto Rico or a possession of the United States unless—

“(i) such branch would be a controlled foreign corporation (as defined in section 957) if it were incorporated under the laws of the Commonwealth of Puerto Rico or the possession of the United States, as the case may be, and

“(ii) the gross income of the United States shareholder for the taxable year includes income derived from sources within the Commonwealth of Puerto Rico and possessions of the United States.

“(C) BLOCKED FOREIGN INCOME.—If a United States shareholder so elects, the provisions of subsection (a)(3) and of paragraph (3) of this subsection shall not apply with respect to any foreign corporation, if it is established to the satisfaction of the Secretary or his delegate that the earnings and profits of such foreign corporation could not have been distributed to United States shareholders who own (within the meaning of section 958(a)) stock of such foreign corporation because of currency or other restrictions or limitations imposed under the laws of any foreign country.

"(d) EFFECTIVE FOREIGN TAX RATE.—For purposes of this section, the term 'effective foreign tax rate' means—

"(1) with respect to a single controlled foreign corporation, the percentage which—

"(A) the income, war profits, or excess profits taxes paid or accrued to foreign countries or possessions of the United States by the controlled foreign corporation for the taxable year on or with respect to its earnings and profits for the taxable year, is of

"(B) the sum of (i) the earnings and profits of the controlled foreign corporation described in subparagraph (A) and (ii) the taxes described in subparagraph (A); and

"(2) with respect to two or more foreign corporations, the percentage which—

"(A) the total income, war profits, or excess profits taxes paid or accrued to foreign countries or possessions of the United States by such foreign corporations for the taxable year on or with respect to the consolidated earnings and profits of such foreign corporations for the taxable year, is of

"(B) the sum of (i) the consolidated earnings and profits of such foreign corporations described in subparagraph (A) and (ii) the taxes described in subparagraph (A).

For purposes of the preceding sentence, in the case of any United States shareholder, the computation of the effective foreign tax rate applicable with respect to any controlled foreign corporation or corporations shall be made without regard to distributions made by such controlled foreign corporation or corporations to such United States shareholder.

"(e) SPECIAL RULES.—

"(1) YEAR FROM WHICH DISTRIBUTIONS ARE MADE.—For purposes of this section, the second sentence of section 902(c) (1) shall apply in determining from the earnings and profits of what year distributions are made by any foreign corporation, except that the Secretary or his delegate may by regulations provide a period in excess of 60 days in lieu of the 60-day period prescribed in such section.

Ante, p. 1000.

"(2) INSUFFICIENT DISTRIBUTIONS.—If—

"(A) a United States shareholder, in making its return of the tax imposed by this chapter for any taxable year, applies the provisions of this section with respect to any controlled foreign corporation,

"(B) it is subsequently determined that this section did not apply with respect to such controlled foreign corporation for such taxable year due to the failure of the United States shareholder to receive a minimum distribution with respect to such controlled foreign corporation, and

"(C) such failure is due to reasonable cause, then a subsequent distribution made with respect to such controlled foreign corporation may, if made at a time and in a manner prescribed by the Secretary or his delegate by regulations, be treated, for purposes of this chapter, as having been made for, and received in, the taxable year of the United States shareholder for which such shareholder applied the provisions of this section.

"(3) AFFILIATED GROUPS OF CORPORATIONS.—An affiliated group of corporations which makes a consolidated return under section 1501 for the taxable year, may, if it so elects, be treated as a single United States shareholder for purposes of applying this section for the taxable year. 26 USC 1501.

"(f) **REGULATIONS.**—The Secretary or his delegate shall prescribe such regulations as he may deem necessary to carry out the provisions of this section, including regulations for the determination of the amount of foreign tax credit in the case of distributions with respect to the earnings and profits of two or more foreign corporations.

"SEC. 964. MISCELLANEOUS PROVISIONS.

"(a) **EARNINGS AND PROFITS.**—For purposes of this subpart, the earnings and profits of any foreign corporation, and the deficit in earnings and profits of any foreign corporation, for any taxable year shall be determined according to rules substantially similar to those applicable to domestic corporations, under regulations prescribed by the Secretary or his delegate.

"(b) **BLOCKED FOREIGN INCOME.**—Under regulations prescribed by the Secretary or his delegate, no part of the earnings and profits of a controlled foreign corporation for any taxable year shall be included in earnings and profits for purposes of sections 952, 955, and 956, if it is established to the satisfaction of the Secretary or his delegate that such part could not have been distributed by the controlled foreign corporation to United States shareholders who own (within the meaning of section 958(a)) stock of such controlled foreign corporation because of currency or other restrictions or limitations imposed under the laws of any foreign country.

"(c) **RECORDS AND ACCOUNTS OF UNITED STATES SHAREHOLDERS.**—

"(1) **RECORDS AND ACCOUNTS TO BE MAINTAINED.**—The Secretary or his delegate may by regulations require each person who is, or has been, a United States shareholder of a controlled foreign corporation to maintain such records and accounts as may be prescribed by such regulations as necessary to carry out the provisions of this subpart and subpart G.

"(2) **TWO OR MORE PERSONS REQUIRED TO MAINTAIN OR FURNISH THE SAME RECORDS AND ACCOUNTS WITH RESPECT TO THE SAME FOREIGN CORPORATION.**—Where, but for this paragraph, two or more United States persons would be required to maintain or furnish the same records and accounts as may by regulations be required under paragraph (1) with respect to the same controlled foreign corporation for the same period, the Secretary or his delegate may by regulations provide that the maintenance or furnishing of such records and accounts by only one such person shall satisfy the requirements of paragraph (1) for such other persons.

"Subpart G—Export Trade Corporations

"Sec. 970. Reduction of subpart F income of export trade corporations.

"Sec. 971. Definitions.

"Sec. 972. Consolidation of group of export trade corporations.

"SEC. 970. REDUCTION OF SUBPART F INCOME OF EXPORT TRADE CORPORATIONS.

"(a) **EXPORT TRADE INCOME CONSTITUTING FOREIGN BASE COMPANY INCOME.**—

"(1) **IN GENERAL.**—In the case of a controlled foreign corporation (as defined in section 957) which for the taxable year is an export trade corporation, the subpart F income (determined without regard to this subpart) of such corporation for such year shall be reduced by an amount equal to so much of the export trade income (as defined in section 971(b)) of such corporation for such year as constitutes foreign base company income (as defined

in section 954), but only to the extent that such amount does not exceed whichever of the following amounts is the lesser:

“(A) an amount equal to $1\frac{1}{2}$ times so much of the export promotion expenses (as defined in section 971(d)) of such corporation for such year as is properly allocable to the export trade income which constitutes foreign base company income of such corporation for such year, or

“(B) an amount equal to 10 percent of so much of the gross receipts for such year (or, in the case of gross receipts arising from commissions, fees, or other compensation for its services, so much of the gross amount upon the basis of which such commissions, fees, or other compensation is computed) accruing to such export trade corporation from the sale, installation, operation, maintenance, or use of property in respect of which such corporation derives export trade income as is properly allocable to the export trade income which constitutes foreign base company income of such corporation for such year.

The allocations with respect to export trade income which constitutes foreign base company income under subparagraphs (A) and (B) shall be made under regulations prescribed by the Secretary or his delegate.

“(2) OVERALL LIMITATION.—The reduction under paragraph (1) for any taxable year shall not exceed an amount which bears the same ratio to the increase in the investments in export trade assets (as defined in section 971(c)) of such corporation for such year as the export trade income which constitutes foreign base company income of such corporation for such year bears to the entire export trade income of such corporation for such year.

“(b) INCLUSION OF CERTAIN PREVIOUSLY EXCLUDED AMOUNTS.—Each United States shareholder of a controlled foreign corporation which for any prior taxable year was an export trade corporation shall include in his gross income under section 951(a)(1)(A)(ii), as an amount to which section 955 (relating to withdrawal of previously excluded subpart F income from qualified investment) applies, his pro rata share of the amount of decrease in the investments in export trade assets of such corporation for such year, but only to the extent that his pro rata share of such amount does not exceed an amount equal to—

Ante, p. 1006.

“(1) his pro rata share of the sum of (A) the amounts by which the subpart F income of such corporation was reduced for all prior taxable years under subsection (a), and (B) the amounts not included in subpart F income (determined without regard to this subpart) for all prior taxable years by reason of the application of section 972, reduced by

“(2) the sum of the amounts which were included in his gross income under section 951(a)(1)(A)(ii) under the provisions of this subsection for all prior taxable years.

“(c) INVESTMENTS IN EXPORT TRADE ASSETS.—

“(1) AMOUNT OF INVESTMENTS.—For purposes of this section, the amount taken into account with respect to any export trade asset shall be its adjusted basis, reduced by any liability to which the asset is subject.

“(2) INCREASE IN INVESTMENTS IN EXPORT TRADE ASSETS.—For purposes of subsection (a), the amount of increase in investments in export trade assets of any controlled foreign corporation for any taxable year is the amount by which—

“(A) the amount of such investments at the close of the taxable year, exceeds

“(B) the amount of such investments at the close of the preceding taxable year.

“(3) DECREASE IN INVESTMENTS IN EXPORT TRADE ASSETS.—For purposes of subsection (b), the amount of decrease in investments in export trade assets of any controlled foreign corporation for any taxable year is the amount by which—

“(A) the amount of such investments at the close of the preceding taxable year (reduced by an amount equal to the amount of net loss sustained during the taxable year with respect to export trade assets), exceeds

“(B) the amount of such investments at the close of the taxable year.

“(4) SPECIAL RULE.—A United States shareholder of an export trade corporation may, under regulations prescribed by the Secretary or his delegate, make the determinations under paragraphs (2) and (3) as of the close of the 75th day after the close of the years referred to in such paragraphs in lieu of on the last day of such years. A United States shareholder of an export trade corporation may, under regulations prescribed by the Secretary or his delegate, make the determinations under paragraphs (2) and (3) with respect to export trade assets described in section 971(c)(3) as of the close of the years following the years referred to in such paragraphs, or as of the close of such longer period of time as such regulations may permit, in lieu of on the last day of such years and in lieu of on the day prescribed in the preceding sentence. Any election under this paragraph made with respect to any taxable year shall apply to such year and to all succeeding taxable years unless the Secretary or his delegate consents to the revocation of such election.

“SEC. 971. DEFINITIONS.

“(a) EXPORT TRADE CORPORATIONS.—For purposes of this subpart, the term ‘export trade corporation’ means—

“(1) IN GENERAL.—A controlled foreign corporation (as defined in section 957) which satisfies the following conditions:

“(A) 90 percent or more of the gross income of such corporation for the 3-year period immediately preceding the close of the taxable year (or such part of such period subsequent to the effective date of this subpart during which the corporation was in existence) was derived from sources without the United States, and

“(B) 75 percent or more of the gross income of such corporation for such period constituted gross income in respect of which such corporation derived export trade income.

“(2) SPECIAL RULE.—If 50 percent or more of the gross income of a controlled foreign corporation in the period specified in subsection (a)(1)(A) is gross income in respect of which such corporation derived export trade income in respect of agricultural products grown in the United States, it may qualify as an export trade corporation although it does not meet the requirements of subsection (a)(1)(B).

“(b) EXPORT TRADE INCOME.—For the purposes of this subpart, the term ‘export trade income’ means net income from—

“(1) the sale to an unrelated person for use, consumption, or disposition outside the United States of export property (as defined in subsection (e)), or from commissions, fees, compensation, or other income from the performance of commercial, industrial, financial, technical, scientific, managerial, engineering, architectural, skilled, or other services in respect of such sales or

in respect of the installation or maintenance of such export property;

“(2) commissions, fees, compensation, or other income from commercial, industrial, financial, technical, scientific, managerial, engineering, architectural, skilled, or other services performed in connection with the use by an unrelated person outside the United States of patents, copyrights, secret processes and formulas, goodwill, trademarks, trade brands, franchises, and other like property acquired or developed and owned by the manufacturer, producer, grower, or extractor of export property in respect of which the export trade corporation earns export trade income under paragraph (1);

“(3) commissions, fees, rentals, or other compensation or income attributable to the use of export property by an unrelated person or attributable to the use of export property in the rendition of technical, scientific, or engineering services to an unrelated person; and

“(4) interest from export trade assets described in subsection (c) (4).

For purposes of paragraph (3), if a controlled foreign corporation receives income from an unrelated person attributable to the use of export property in the rendition of services to such unrelated person together with income attributable to the rendition of other services to such unrelated person, including personal services, the amount of such aggregate income which shall be considered to be attributable to the use of the export property shall (if such amount cannot be established by reference to transactions between unrelated persons) be that part of such aggregate income which the cost of the export property consumed in the rendition of such services (including a reasonable allowance for depreciation) bears to the total costs and expenses attributable to such aggregate income.

“(c) EXPORT TRADE ASSETS.—For purposes of this subpart, the term ‘export trade assets’ means—

“(1) working capital reasonably necessary for the production of export trade income,

“(2) inventory of export property held for use, consumption, or disposition outside the United States,

“(3) facilities located outside the United States for the storage, handling, transportation, packaging, or servicing of export property, and

“(4) evidences of indebtedness executed by persons, other than related persons, in connection with payment for purchases of export property for use, consumption, or disposition outside the United States, or in connection with the payment for services described in subsections (b) (2) and (3)

“(d) EXPORT PROMOTION EXPENSES.—For purposes of this subpart, the term ‘export promotion expenses’ means the following expenses paid or incurred in the receipt or production of export trade income—

“(1) a reasonable allowance for salaries or other compensation for personal services actually rendered for such purpose,

“(2) rentals or other payments for the use of property actually used for such purpose,

“(3) a reasonable allowance for the exhaustion, wear and tear, or obsolescence of property actually used for such purpose, and

“(4) any other ordinary and necessary expenses of the corporation to the extent reasonably allocable to the receipt or production of export trade income.

No expense incurred within the United States shall be treated as an export promotion expense within the meaning of the preceding sentence, unless at least 90 percent of each category of expenses described in such sentence is incurred outside the United States.

“(e) EXPORT PROPERTY.—For purposes of this subpart, the term ‘export property’ means any property or any interest in property manufactured, produced, grown, or extracted in the United States.

“(f) UNRELATED PERSON.—For purposes of this subpart, the term ‘unrelated person’ means a person other than a related person as defined in section 954(d)(3).

Ante, p. 1013.

“SEC. 972. CONSOLIDATION OF GROUP OF EXPORT TRADE CORPORATIONS.

“For purposes of this subpart and subpart F of this part, a United States shareholder of a controlled foreign corporation which is an export trade corporation may, under regulations prescribed by the Secretary or his delegate, treat as a single controlled foreign corporation—

“(1) such controlled foreign corporation,

“(2) all controlled foreign corporations which are export trade corporations and 80 percent or more of the total combined voting power of all classes of stock entitled to vote of which is owned by such controlled foreign corporation; and

“(3) all controlled foreign corporations which are export trade corporations and 80 percent or more of the total combined voting power of all classes of stock entitled to vote of which is owned by controlled foreign corporations described in paragraph (2).”

(b) TECHNICAL AND CLERICAL AMENDMENTS.—

(1) Section 901 (relating to foreign tax credit) is amended by striking out “section 902” and inserting in lieu thereof “sections 902 and 960”.

Ante, p. 1002.

(2) Section 904(g) (as redesignated by section 10(a) of this Act) is amended to read as follows:

“(g) CROSS REFERENCES.—

“(1) For increase of applicable limitation under subsection (a) for taxes paid with respect to amounts received which were included in the gross income of the taxpayer for a prior taxable year as a United States shareholder with respect to a controlled foreign corporation, see section 960(b).

Ante, p. 1020.

“(2) For special rule relating to the application of the credit provided by section 901 in the case of affiliated groups which include Western Hemisphere trade corporations for years in which the limitation provided by subsection (a)(2) applies, see section 1503(d).

74 Stat. 1011.

26 USC 901.

(3) The table of subparts for part III of subchapter N of chapter 1 is amended by adding at the end thereof the following:

“Subpart F. Controlled foreign corporations.

“Subpart G. Export trade corporations.”

Ante, p. 972.

(4) Section 1016(a) (relating to adjustments to basis) is amended by adding after paragraph (19) (as added by section 2(f) of this Act) the following new paragraph:

“(20) to the extent provided in section 961 in the case of stock in controlled foreign corporations (or foreign corporations which were controlled foreign corporations) and of property by reason of which a person is considered as owning such stock.”

(c) EFFECTIVE DATE.—The amendments made by this section shall apply with respect to taxable years of foreign corporations beginning after December 31, 1962, and to taxable years of United States shareholders within which or with which such taxable years of such foreign corporations end.

SEC. 13. GAIN FROM DISPOSITIONS OF CERTAIN DEPRECIABLE PROPERTY.**(a) IN GENERAL.—**

(1) Part IV of subchapter P of chapter 1 (relating to special rules for determining capital gains and losses) is amended by adding at the end thereof the following new section: 26 USC 1231-1244.

“SEC. 1245. GAIN FROM DISPOSITIONS OF CERTAIN DEPRECIABLE PROPERTY.**“(a) GENERAL RULE.—**

“(1) **ORDINARY INCOME.**—Except as otherwise provided in this section, if section 1245 property is disposed of during a taxable year beginning after December 31, 1962, the amount by which the lower of—

“(A) the recomputed basis of the property, or

“(B) (i) in the case of a sale, exchange, or involuntary conversion, the amount realized, or

“(ii) in the case of any other disposition, the fair market value of such property,

exceeds the adjusted basis of such property shall be treated as gain from the sale or exchange of property which is neither a capital asset nor property described in section 1231. Such gain shall be recognized notwithstanding any other provision of this subtitle.

“(2) **RECOMPUTED BASIS.**—For purposes of this section, the term ‘recomputed basis’ means, with respect to any property, its adjusted basis recomputed by adding thereto all adjustments, attributable to periods after December 31, 1961, reflected in such adjusted basis on account of deductions (whether in respect of the same or other property) allowed or allowable to the taxpayer or to any other person for depreciation, or for amortization under section 168. For purposes of the preceding sentence, if the taxpayer can establish by adequate records or other sufficient evidence that the amount allowed for depreciation, or for amortization under section 168, for any period was less than the amount allowable, the amount added for such period shall be the amount allowed.

“(3) **SECTION 1245 PROPERTY.**—For purposes of this section, the term ‘section 1245 property’ means any property (other than livestock) which is or has been property of a character subject to the allowance for depreciation provided in section 167 and is either—

“(A) personal property, or

“(B) other property (not including a building or its structural components) but only if such other property is tangible and has an adjusted basis in which there are reflected adjustments described in paragraph (2) for a period in which such property (or other property)—

“(i) was used as an integral part of manufacturing, production, or extraction or of furnishing transportation, communications, electrical energy, gas, water, or sewage disposal services, or

“(ii) constituted research or storage facilities used in connection with any of the activities referred to in clause (i).

“(b) EXCEPTIONS AND LIMITATIONS.—

“(1) **GIFTS.**—Subsection (a) shall not apply to a disposition by gift.

“(2) TRANSFERS AT DEATH.—Except as provided in section 691 (relating to income in respect of a decedent), subsection (a) shall not apply to a transfer at death.

“(3) CERTAIN TAX-FREE TRANSACTIONS.—If the basis of property in the hands of a transferee is determined by reference to its basis in the hands of the transferor by reason of the application of section 332, 351, 361, 371(a), 374(a), 721, or 731, then the amount of gain taken into account by the transferor under subsection (a) (1) shall not exceed the amount of gain recognized to the transferor on the transfer of such property (determined without regard to this section). This paragraph shall not apply to a disposition to an organization (other than a cooperative described in section 521) which is exempt from the tax imposed by this chapter.

“(4) LIKE KIND EXCHANGES; INVOLUNTARY CONVERSIONS, ETC.—If property is disposed of and gain (determined without regard to this section) is not recognized in whole or in part under section 1031 or 1033, then the amount of gain taken into account by the transferor under subsection (a) (1) shall not exceed the sum of—

“(A) the amount of gain recognized on such disposition (determined without regard to this section), plus

“(B) the fair market value of property acquired which is not section 1245 property and which is not taken into account under subparagraph (A).

“(5) SECTION 1071 AND 1081 TRANSACTIONS.—Under regulations prescribed by the Secretary or his delegate, rules consistent with paragraphs (3) and (4) of this subsection shall apply in the case of transactions described in section 1071 (relating to gain from sale or exchange to effectuate policies of FCC) or section 1081 (relating to exchanges in obedience to SEC orders).

“(6) PROPERTY DISTRIBUTED BY A PARTNERSHIP TO A PARTNER.—

“(A) IN GENERAL.—For purposes of this section, the basis of section 1245 property distributed by a partnership to a partner shall be deemed to be determined by reference to the adjusted basis of such property to the partnership.

“(B) ADJUSTMENTS ADDED BACK.—In the case of any property described in subparagraph (A), for purposes of computing the recomputed basis of such property the amount of the adjustments added back for periods before the distribution by the partnership shall be—

“(i) the amount of the gain to which subsection (a) would have applied if such property had been sold by the partnership immediately before the distribution at its fair market value at such time, reduced by

“(ii) the amount of such gain to which section 751(b) applied.

“(c) ADJUSTMENTS TO BASIS.—The Secretary or his delegate shall prescribe such regulations as he may deem necessary to provide for adjustments to the basis of property to reflect gain recognized under subsection (a).

“(d) APPLICATION OF SECTION.—This section shall apply notwithstanding any other provision of this subtitle.”

(2) The table of sections for such part IV is amended by adding at the end thereof the following:

“Sec. 1245. Gain from dispositions of certain depreciable property.”

(b) CHANGE IN METHOD OF DEPRECIATION.—Subsection (e) of section 167 (relating to depreciation) is amended to read as follows:

26 USC 167.

“(e) CHANGE IN METHOD.—

“(1) CHANGE FROM DECLINING BALANCE METHOD.—In the absence of an agreement under subsection (d) containing a provision to the contrary, a taxpayer may at any time elect in accordance with regulations prescribed by the Secretary or his delegate to change from the method of depreciation described in subsection (b) (2) to the method described in subsection (b) (1).

“(2) CHANGE WITH RESPECT TO SECTION 1245 PROPERTY.—A taxpayer may, on or before the last day prescribed by law (including extensions thereof) for filing his return for his first taxable year beginning after December 31, 1962, and in such manner as the Secretary or his delegate shall by regulations prescribe, elect to change his method of depreciation in respect of section 1245 property (as defined in section 1245(a) (3)) from any declining balance or sum of the years-digits method to the straight line method. An election may be made under this paragraph notwithstanding any provision to the contrary in an agreement under subsection (d).”

Ante, p. 1032.

(c) SALVAGE VALUE OF PERSONAL PROPERTY.—

(1) AMOUNT TAKEN INTO ACCOUNT.—Section 167 (relating to depreciation) is amended by redesignating subsections (f), (g), and (h) as (g), (h), and (i), respectively, and by inserting after subsection (e) the following new subsection:

“(f) SALVAGE VALUE.—

“(1) GENERAL RULE.—Under regulations prescribed by the Secretary or his delegate, a taxpayer may, for purposes of computing the allowance under subsection (a) with respect to personal property, reduce the amount taken into account as salvage value by an amount which does not exceed 10 percent of the basis of such property (as determined under subsection (g) as of the time as of which such salvage value is required to be determined).

“(2) PERSONAL PROPERTY DEFINED.—For purposes of this subsection, the term ‘personal property’ means depreciable personal property (other than livestock) with a useful life of 3 years or more acquired after the date of the enactment of the Revenue Act of 1962.”

(2) CONFORMING AMENDMENTS.—

(A) Sections 179(d) (5) and 642(e) are each amended by striking out “167(g)” and inserting in lieu thereof “167(h)”. 26 USC 179.

(B) Section 179(d) (8) is amended by striking out “167(f)” and inserting in lieu thereof “167(g)”. 26 USC 179.

(d) SPECIAL RULE FOR CHARITABLE CONTRIBUTIONS OF SECTION 1245 PROPERTY.—Section 170 (relating to charitable, etc., contributions and gifts) is amended by redesignating subsections (e) and (f) as (f) and (g), respectively, and by inserting after subsection (d) the following new subsection:

26 USC 170.

“(e) SPECIAL RULE FOR CHARITABLE CONTRIBUTIONS OF SECTION 1245 PROPERTY.—The amount of any charitable contribution taken into account under this section shall be reduced by the amount which would have been treated as gain to which section 1245(a) applies if the property contributed had been sold at its fair market value (determined at the time of such contribution).”

Ante, p. 1032.

(e) COMPUTATION OF TAXABLE INCOME FOR PURPOSES OF LIMITATION ON PERCENTAGE DEPLETION DEDUCTION.—Section 613(a) (relating to percentage depletion) is amended by inserting after the second sentence thereof the following new sentence: “For purposes of the preceding sentence, the allowable deductions taken into account with

26 USC 613.

76 STAT. 1035.

respect to expenses of mining in computing the taxable income from the property shall be decreased by an amount equal to so much of any gain which (1) is treated under section 1245 (relating to gain from disposition of certain depreciable property) as gain from the sale or exchange of property which is neither a capital asset nor property described in section 1231, and (2) is properly allocable to the property."

26 USC 1231.

(f) TECHNICAL AMENDMENTS.—

26 USC 751.

(1) SPECIAL RULE FOR PARTNERSHIPS.—Section 751(c) (relating to definition of "unrealized receivables" for purposes of subchapter K) is amended by adding after paragraph (2) the following:

Ante, p. 1032.

"For purposes of this section and sections 731, 736, and 741, such term also includes section 1245 property (as defined in section 1245 (a) (3)), but only to the extent of the amount which would be treated as gain to which section 1245(a) would apply if (at the time of the transaction described in this section or section 731, 736, or 741, as the case may be) such property had been sold by the partnership at its fair market value."

(2) CORPORATE DISTRIBUTION OF PROPERTY.—Subsections (b) and (d) of section 301 (relating to amount distributed) are each amended by striking out "subsection (b) or (c) of section 311" and inserting in lieu thereof "subsection (b) or (c) of section 311 or under section 1245(a)".

(3) EFFECT ON EARNINGS AND PROFITS.—Section 312(c) (3) (relating to adjustments of earnings and profits) is amended by striking out "subsection (b) or (c) of section 311" and inserting in lieu thereof "subsection (b) or (c) of section 311 or under section 1245(a)".

26 USC 341.

(4) COLLAPSIBLE CORPORATIONS.—Section 341(e) (relating to collapsible corporations) is amended by inserting after paragraph (11) the following new paragraph:

"(12) NONAPPLICATION OF SECTION 1245(a).—For purposes of this subsection, the determination of whether gain from the sale or exchange of property would under any provision of this chapter be considered as gain from the sale or exchange of property which is neither a capital asset nor property described in section 1231(b) shall be made without regard to the application of section 1245(a)."

(5) INSTALLMENT OBLIGATIONS IN CERTAIN LIQUIDATIONS.—

(A) Section 453(d) (4) (A) (relating to distribution of installment obligations in section 332 liquidations) is amended by adding at the end thereof the following new sentence: "If the basis of the property of the liquidating corporation in the hands of the distributee is determined under section 334(b) (2) then the preceding sentence shall not apply to the extent that under paragraph (1) gain to the distributing corporation would be considered as gain to which section 1245(a) applies."

(B) Section 453(d) (4) (B) (relating to distribution of installment obligations in liquidations to which section 337 applies) is amended by adding at the end thereof the following new sentence: "The preceding sentence shall not apply to the extent that under paragraph (1) gain to the distributing corporation would be considered as gain to which section 1245(a) applies."

(g) EFFECTIVE DATES.—The amendments made by this section (other than the amendments made by subsection (c)) shall apply to taxable years beginning after December 31, 1962. The amendments

made by subsection (c) shall apply to taxable years beginning after December 31, 1961, and ending after the date of the enactment of this Act.

SEC. 14. FOREIGN INVESTMENT COMPANIES.

(a) TREATMENT OF SALE OF STOCK OF FOREIGN INVESTMENT COMPANIES.—

(1) IN GENERAL.—Part IV of subchapter P of chapter 1 (relating to special rules for determining capital gains and losses) is amended by adding after section 1245 (as added by section 13 of this Act) the following new sections:

26 USC 1231-1244.

Ante, p. 1032.

“SEC. 1246. GAIN ON FOREIGN INVESTMENT COMPANY STOCK.

“(a) TREATMENT OF GAIN AS ORDINARY INCOME.—

“(1) GENERAL RULE.—In the case of a sale or exchange (or a distribution which, under section 302 or 331, is treated as an exchange of stock) after December 31, 1962, of stock in a foreign corporation which was a foreign investment company (as defined in subsection (b)) at any time during the period during which the taxpayer held such stock, any gain shall be treated as gain from the sale or exchange of property which is not a capital asset, to the extent of the taxpayer's ratable share of the earnings and profits of such corporation accumulated for taxable years beginning after December 31, 1962.

“(2) RATABLE SHARE.—For purposes of this section, the taxpayer's ratable share shall be determined under regulations prescribed by the Secretary or his delegate, but shall include only his ratable share of the accumulated earnings and profits of such corporation—

“(A) for the period during which the taxpayer held such stock, but

“(B) excluding such earnings and profits attributable to any amount previously included in the gross income of such taxpayer under section 951 (but only to the extent the inclusion of such amount did not result in an exclusion of any other amount from gross income under section 959).

Ante, p. 1006.

Ante, p. 1019.

“(3) TAXPAYER TO ESTABLISH EARNINGS AND PROFITS.—Unless the taxpayer establishes the amount of the accumulated earnings and profits of the foreign investment company and the ratable share thereof for the period during which the taxpayer held such stock, all the gain from the sale or exchange of stock in such company shall be considered as gain from the sale or exchange of property which is not a capital asset.

“(4) HOLDING PERIOD OF STOCK MUST BE MORE THAN 6 MONTHS.—This section shall not apply with respect to the sale or exchange of stock where the holding period of such stock as of the date of such sale or exchange is 6 months or less.

“(b) DEFINITION OF FOREIGN INVESTMENT COMPANY.—For purposes of this section, the term ‘foreign investment company’ means any foreign corporation which, for any taxable year beginning after December 31, 1962, is—

“(1) registered under the Investment Company Act of 1940, as amended (15 U.S.C. 80a-1 to 80b-2), either as a management company or as a unit investment trust, or

54 Stat. 789.

“(2) engaged (or holding itself out as being engaged) primarily in the business of investing, reinvesting, or trading in securities (within the meaning of section 3(a)(1) of such Act, as limited by paragraphs (2) through (10) (except paragraph (6)(C)) and paragraphs (12) through (15) of section 3(c) of such Act) at a time when more than 50 percent of the total com-

76 STAT. 1037.

Ante, p. 1018.
Ante, p. 988.

bined voting power of all classes of stock entitled to vote, or of the total value of shares of all classes of stock, was held, directly or indirectly (within the meaning of section 958(a)), by United States persons (as defined in section 7701(a)(30)).

“(c) STOCK HAVING TRANSFERRED OR SUBSTITUTED BASIS.—To the extent provided in regulations prescribed by the Secretary or his delegate, stock in a foreign corporation, the basis of which (in the hands of the taxpayer selling or exchanging such stock) is determined by reference to the basis (in the hands of such taxpayer or any other person) of stock in a foreign investment company, shall be treated as stock of a foreign investment company and held by the taxpayer throughout the holding period for such stock (determined under section 1223).

26 USC 1223.

“(d) RULES RELATING TO ENTITIES HOLDING FOREIGN INVESTMENT COMPANY STOCK.—To the extent provided in regulations prescribed by the Secretary or his delegate—

26 USC 677.

“(1) trust certificates of a trust to which section 677 (relating to income for benefit of grantor) applies, and

“(2) stock of a domestic corporation, shall be treated as stock of a foreign investment company and held by the taxpayer throughout the holding period for such certificates or stock (determined under section 1223) in the same proportion that the investment in stock in a foreign investment company by the trust or domestic corporation bears to the total assets of such trust or corporation.

“(e) RULES RELATING TO STOCK ACQUIRED FROM A DECEDENT.—

26 USC 1014.

“(1) BASIS.—In the case of stock of a foreign investment company acquired by bequest, devise, or inheritance (or by the decedent's estate) from a decedent dying after December 31, 1962, the basis determined under section 1014 shall be reduced (but not below the adjusted basis of such stock in the hands of the decedent immediately before his death) by the amount of the decedent's ratable share of the earnings and profits of such company accumulated after December 31, 1962. Any stock so acquired shall be treated as stock described in subsection (c).

“(2) DEDUCTION FOR ESTATE TAX.—If stock to which subsection (a) applies is acquired from a decedent, the taxpayer shall, under regulations prescribed by the Secretary or his delegate, be allowed (for the taxable year of the sale or exchange) a deduction from gross income equal to that portion of the decedent's estate tax deemed paid which is attributable to the excess of (A) the value at which such stock was taken into account for purposes of determining the value of the decedent's gross estate, over (B) the value at which it would have been so taken into account if such value had been reduced by the amount described in paragraph (1).

“(f) INFORMATION WITH RESPECT TO CERTAIN FOREIGN INVESTMENT COMPANIES.—Every United States person who, on the last day of the taxable year of a foreign investment company beginning after December 31, 1962, owns 5 percent or more in value of the stock of such company shall furnish with respect to such company such information as the Secretary or his delegate shall by regulations prescribe.

“(g) CROSS REFERENCE.—

“For special rules relating to the earnings and profits of foreign investment companies, see section 312(l).

“SEC. 1247. ELECTION BY FOREIGN INVESTMENT COMPANIES TO DISTRIBUTE INCOME CURRENTLY.

“(a) ELECTION BY FOREIGN INVESTMENT COMPANY.—

“(1) IN GENERAL.—If a foreign investment company which is described in section 1246(b)(1) elects (in the manner provided

Ante, p. 1036.

in regulations prescribed by the Secretary or his delegate) on or before December 31, 1962, with respect to each taxable year beginning after December 31, 1962, to—

“(A) distribute to its shareholders 90 percent or more of what its taxable income would be if it were a domestic corporation;

“(B) designate in a written notice mailed to its shareholders at any time before the expiration of 45 days after the close of its taxable year the pro rata amount of the excess (determined as if such corporation were a domestic corporation) of the net long-term capital gain over the net short-term capital loss of the taxable year; and the portion thereof which is being distributed; and

“(C) provide such information as the Secretary or his delegate deems necessary to carry out the purposes of this section,

then section 1246 shall not apply with respect to the qualified shareholders of such company during any taxable year to which such election applies. Ante, p. 1036.

“(2) SPECIAL RULES.—

“(A) COMPUTATION OF TAXABLE INCOME.—For purposes of paragraph (1) (A), the taxable income of the company shall be computed without regard to—

“(i) the excess of the net long-term capital gain over the net short-term capital loss referred to in paragraph (1) (B),

“(ii) section 172 (relating to net operating losses), 26 USC 172. and

“(iii) any deduction provided by part VIII of subchapter B (other than the deduction provided by section 248, relating to organizational expenditures). 26 USC 248.

“(B) DISTRIBUTIONS AFTER THE CLOSE OF THE TAXABLE YEAR.—For purposes of paragraph (1) (A), a distribution made after the close of the taxable year and on or before the 15th day of the third month of the next taxable year shall be treated as distributed during the taxable year to the extent elected by the company (in accordance with regulations prescribed by the Secretary or his delegate) on or before the 15th day of such third month.

“(C) CARRYOVER OF CAPITAL LOSSES FROM NONELECTION YEARS DENIED.—In computing the excess of the net long-term capital gain over the net short-term capital loss referred to in paragraph (1) (B), section 1212 shall not apply to losses incurred in or with respect to taxable years before the first taxable year to which the election applies. 26 USC 1212.

“(b) YEARS TO WHICH ELECTION APPLIES.—The election of any foreign investment company under this section shall terminate as of the close of the taxable year preceding its first taxable year in which any of the following occurs:

“(1) the company fails to comply with the provisions of subparagraph (A), (B), or (C) of subsection (a) (1), unless it is shown that such failure is due to reasonable cause and not due to willful neglect,

“(2) the company is a foreign personal holding company, or

“(3) the company is not a foreign investment company which is described in section 1246(b) (1).

Ante, p. 988.

“(c) QUALIFIED SHAREHOLDERS.—For purposes of this section—

“(1) IN GENERAL.—The term ‘qualified shareholder’ means any shareholder who is a United States person (as defined in section 7701(a)(30)), other than a shareholder described in paragraph (2).

“(2) CERTAIN UNITED STATES PERSONS EXCLUDED FROM DEFINITION.—A United States person shall not be treated as a qualified shareholder for the taxable year if for such taxable year (or for any prior taxable year) he did not include, in computing his long-term capital gains in his return for such taxable year, the amount designated by such company pursuant to subsection (a)(1)(B) as his share of the undistributed capital gains of such company for its taxable year ending within or with such taxable year of the taxpayer. The preceding sentence shall not apply with respect to any failure by the taxpayer to treat an amount as provided therein if the taxpayer shows that such failure was due to reasonable cause and not due to willful neglect.

“(d) TREATMENT OF DISTRIBUTED AND UNDISTRIBUTED CAPITAL GAINS BY A QUALIFIED SHAREHOLDER.—Every qualified shareholder of a foreign investment company for any taxable year of such company with respect to which an election pursuant to subsection (a) is in effect shall include, in computing his long-term capital gains—

“(1) for his taxable year in which received, his pro rata share of the distributed portion of the excess of the net long-term capital gain over the net short-term capital loss for such taxable year of such company, and

“(2) for his taxable year in which or with which the taxable year of such company ends, his pro rata share of the undistributed portion of the excess of the net long-term capital gain over the net short-term capital loss for such taxable year of such company.

“(e) ADJUSTMENTS.—Under regulations prescribed by the Secretary or his delegate, proper adjustment shall be made—

“(1) in the earnings and profits of the electing foreign investment company and a qualified shareholder’s ratable share thereof, and

“(2) in the adjusted basis of stock of such company held by such shareholder, to reflect such shareholder’s inclusion in gross income of undistributed capital gains.

“(f) ELECTION BY FOREIGN INVESTMENT COMPANY WITH RESPECT TO FOREIGN TAX CREDIT.—A foreign investment company with respect to which an election pursuant to subsection (a) is in effect and more than 50 percent of the value (as defined in section 851(c)(4)) of whose total assets at the close of the taxable year consists of stock or securities in foreign corporations may, for such taxable year, elect the application of this subsection with respect to income, war profits, and excess profits taxes described in section 901(b)(1) which are paid by the foreign investment company during such taxable year to foreign countries and possessions of the United States. If such election is made—

“(1) the foreign investment company—

“(A) shall compute its taxable income, for purposes of subsection (a)(1)(A), without any deductions for income, war profits, or excess profits taxes paid to foreign countries or possessions of the United States, and

“(B) shall treat the amount of such taxes, for purposes of subsection (a)(1)(A), as distributed to its shareholders;

26 USC 851.

26 USC 901.

"(2) each qualified shareholder of such foreign investment company—

"(A) shall include in gross income and treat as paid by him his proportionate share of such taxes, and

"(B) shall treat, for purposes of applying subpart A of part III of subchapter N, his proportionate share of such taxes as having been paid to the country in which the foreign investment company is incorporated, and

"(C) shall treat as gross income from sources within the country in which the foreign investment company is incorporated, for purposes of applying subpart A of part III of subchapter N, the sum of his proportionate share of such taxes and any dividend paid to him by such foreign investment company.

"(g) NOTICE TO SHAREHOLDERS.—The amounts to be treated by qualified shareholders, for purposes of subsection (f) (2), as their proportionate share of the taxes described in subsection (f) (1) (A) paid by a foreign investment company shall not exceed the amounts so designated by the foreign investment company in a written notice mailed to its shareholders not later than 45 days after the close of its taxable year.

"(h) MANNER OF MAKING ELECTION AND NOTIFYING SHAREHOLDERS.—The election provided in subsection (f) and the notice to shareholders required by subsection (g) shall be made in such manner as the Secretary or his delegate may prescribe by regulations.

"(i) LOSS ON SALE OR EXCHANGE OF CERTAIN STOCK HELD LESS THAN 6 MONTHS.—If—

"(1) under this section, any qualified shareholder treats any amount designated under subsection (a) (1) (B) with respect to a share of stock as long-term capital gain, and

"(2) such share is held by the taxpayer for less than 6 months, then any loss on the sale or exchange of such share shall, to the extent of the amount described in paragraph (1), be treated as loss from the sale or exchange of a capital asset held for more than 6 months."

(2) The table of sections for such part IV is amended by adding at the end thereof the following:

"Sec. 1246. Gain on foreign investment company stock.

"Sec. 1247. Election by foreign investment companies to distribute income currently."

(b) CONFORMING AMENDMENTS.—

(1) EARNINGS AND PROFITS OF FOREIGN INVESTMENT COMPANIES.—

Section 312 (relating to effect on earnings and profits) is amended by adding after subsection (k) the following new subsection:

Ante, p. 6.
26 USC 312.

"(1) EARNINGS AND PROFITS OF FOREIGN INVESTMENT COMPANIES.—

"(1) ALLOCATION WITHIN AFFILIATED GROUP.—In the case of a sale or exchange of stock in a foreign investment company (as defined in section 1246(b)) by a United States person (as defined in section 7701(a)(30)), if such company is a member of an affiliated group, then the accumulated earnings and profits of all members of such affiliated group shall be allocated, under regulations prescribed by the Secretary or his delegate, in such manner as is proper to carry out the purposes of section 1246.

Ante, p. 1036.
Ante, p. 988.

"(2) AFFILIATED GROUP DEFINED.—For purposes of paragraph (1) of this subsection, the term 'affiliated group' has the meaning assigned to such term by section 1504(a); except that (A) 'more than 50 percent' shall be substituted for '80 percent or more', and (B) all corporations shall be treated as includible corporations (without regard to the provisions of section 1504(b)).

26 USC 1504.

“(3) PARTIAL LIQUIDATIONS AND REDEMPTIONS.—

Ante, p. 1036.
26 USC 302,
303.

“(A) IN GENERAL.—If a foreign investment company (as defined in section 1246) distributes amounts in partial liquidation or in a redemption to which section 302(a) or 303 applies, the part of such distribution which is properly chargeable to earnings and profits shall be an amount which is not in excess of the ratable share of the earnings and profits of the company accumulated after February 28, 1913, attributable to the stock so redeemed.

“(B) EFFECTIVE DATE.—Subparagraph (A) shall apply only with respect to distributions made after December 31, 1962.”

26 USC 751.

(2) SALE OR EXCHANGE OF INTEREST IN PARTNERSHIP.—Section 751(d) (2) (relating to inventory items which have appreciated substantially in value) is amended by striking out “and” at the end of subparagraph (B), and by striking out subparagraph (C) and inserting in lieu thereof the following new subparagraphs:

“(C) any other property of the partnership which, if sold or exchanged by the partnership, would result in a gain taxable under subsection (a) of section 1246 (relating to gain on foreign investment company stock), and

“(D) any other property held by the partnership which, if held by the selling or distributee partner, would be considered property of the type described in subparagraph (A), (B), or (C).”

26 USC 1223.

(3) HOLDING PERIOD OF PROPERTY.—Section 1223 (relating to holding period of property) is amended by redesignating paragraph (10) as paragraph (11) and inserting after paragraph (9) the following paragraph:

“(10) In determining the period for which the taxpayer has held trust certificates of a trust to which subsection (d) of section 1246 applies, or the period for which the taxpayer has held stock in a corporation to which subsection (d) of section 1246 applies, there shall be included the period for which the trust or corporation (as the case may be) held the stock of foreign investment companies.”

(c) EFFECTIVE DATE.—The amendments made by this section shall apply with respect to taxable years beginning after December 31, 1962.

SEC. 15. GAIN FROM CERTAIN SALES OR EXCHANGES OF STOCK IN CERTAIN FOREIGN CORPORATIONS.

(a) TREATMENT OF GAIN FROM THE REDEMPTION, CANCELLATION, OR SALE OF STOCK IN CERTAIN FOREIGN CORPORATIONS.—Part IV of subchapter P of chapter 1 (relating to special rules for determining capital gains and losses) is amended by adding after section 1247 (as added by section 14 of this Act) the following new section:

Ante, p. 1037.

“SEC. 1248. GAIN FROM CERTAIN SALES OR EXCHANGES OF STOCK IN CERTAIN FOREIGN CORPORATIONS.

“(a) GENERAL RULE.—If—

26 USC 302,
331.

“(1) a United States person sells or exchanges stock in a foreign corporation, or if a United States person receives a distribution from a foreign corporation which, under section 302 or 331, is treated as an exchange of stock, and

Ante, p. 1018.

“(2) such person owns, within the meaning of section 958(a), or is considered as owning by applying the rules of ownership of section 958(b), 10 percent or more of the total combined voting power of all classes of stock entitled to vote of such foreign corporation at any time during the 5-year period ending on the date of the sale or exchange when such foreign corporation was a controlled foreign corporation (as defined in section 957),

Ante, p. 1017.

then the gain recognized on the sale or exchange of such stock shall be included in the gross income of such person as a dividend, to the extent of the earnings and profits of the foreign corporation attributable (under regulations prescribed by the Secretary or his delegate) to such stock which were accumulated in taxable years of such foreign corporation beginning after December 31, 1962, and during the period or periods the stock sold or exchanged was held by such person while such foreign corporation was a controlled foreign corporation.

“(b) LIMITATION ON TAX APPLICABLE TO INDIVIDUALS.—In the case of an individual, if the stock sold or exchanged is a capital asset (within the meaning of section 1221) and has been held for more than 6 months, the tax attributable to an amount included in gross income as a dividend under subsection (a) shall not be greater than a tax equal to the sum of—

26 USC 1221.

“(1) a pro rata share of the excess of—

“(A) the taxes that would have been paid by the foreign corporation with respect to its income had it been taxed under this chapter as a domestic corporation (but without allowance for deduction of, or credit for, taxes described in subparagraph (B)), for the period or periods the stock sold or exchanged was held by the United States person in taxable years beginning after December 31, 1962, while the foreign corporation was a controlled foreign corporation, adjusted for distributions and amounts previously included in gross income of a United States shareholder under section 951, over

Ante, p. 1006.

“(B) the income, war profits, or excess profits taxes paid by the foreign corporation with respect to such income; and

“(2) an amount equal to the tax that would result by including in gross income, as gain from the sale or exchange of a capital asset held for more than 6 months, an amount equal to the excess of (A) the amount included in gross income as a dividend under subsection (a), over (B) the amount determined under paragraph (1).

“(c) DETERMINATION OF EARNINGS AND PROFITS.—

“(1) IN GENERAL.—For purposes of this section, the earnings and profits of any foreign corporation for any taxable year shall be determined according to rules substantially similar to those applicable to domestic corporations, under regulations prescribed by the Secretary or his delegate.

“(2) EARNINGS AND PROFITS OF SUBSIDIARIES OF FOREIGN CORPORATIONS.—If—

“(A) subsection (a) applies to a sale or exchange by a United States person of stock of a foreign corporation and, by reason of the ownership of the stock sold or exchanged, such person owned within the meaning of section 958(a) (2) stock of any other foreign corporation; and

Ante, p. 1018.

“(B) such person owned, within the meaning of section 958(a), or was considered as owning by applying the rules of ownership of section 958(b), 10 percent or more of the total combined voting power of all classes of stock entitled to vote of such other foreign corporation at any time during the 5-year period ending on the date of the sale or exchange when such other foreign corporation was a controlled foreign corporation (as defined in section 957),

Ante, p. 1017.

then, for purposes of this section, the earnings and profits of the foreign corporation the stock of which is sold or exchanged which are attributable to the stock sold or exchanged shall be deemed

to include the earnings and profits of such other foreign corporation which—

“(C) are attributable (under regulations prescribed by the Secretary or his delegate) to the stock of such other foreign corporation which such person owned within the meaning of section 958(a)(2) (by reason of his ownership within the meaning of section 958(a)(1)(A) of the stock sold or exchanged) on the date of such sale or exchange; and

“(D) were accumulated in taxable years of such other corporation beginning after December 31, 1962, and during the period or periods—

“(i) such other corporation was a controlled foreign corporation, and

“(ii) such person owned within the meaning of section 958(a)(2) the stock of such other foreign corporation.

“(d) EXCLUSIONS FROM EARNINGS AND PROFITS.—For purposes of this section, the following amounts shall be excluded, with respect to any United States person, from the earnings and profits of a foreign corporation:

“(1) AMOUNTS INCLUDED IN GROSS INCOME UNDER SECTION 951.—Earnings and profits of the foreign corporation attributable to any amount previously included in the gross income of such person under section 951, with respect to the stock sold or exchanged, but only to the extent the inclusion of such amount did not result in an exclusion of an amount from gross income under section 959.

“(2) GAIN REALIZED FROM THE SALE OR EXCHANGE OF PROPERTY IN PURSUANCE OF A PLAN OF COMPLETE LIQUIDATION.—If a foreign corporation adopts a plan of complete liquidation in a taxable year of a foreign corporation beginning after December 31, 1962, and if section 337(a) would apply if such foreign corporation were a domestic corporation, earnings and profits of the foreign corporation attributable (under regulations prescribed by the Secretary or his delegate) to any net gain from the sale or exchange of property.

“(3) LESS DEVELOPED COUNTRY CORPORATIONS.—Earnings and profits accumulated by a foreign corporation while it was a less developed country corporation (as defined in section 902(d)), if the stock sold or exchanged was owned for a continuous period of at least 10 years, ending with the date of the sale or exchange, by the United States person who sold or exchanged such stock. In the case of stock sold or exchanged by a corporation, if United States persons who are individuals, estates, or trusts (each of whom owned within the meaning of section 958(a), or were considered as owning by applying the rules of ownership of section 958(b), 10 percent or more of the total combined voting power of all classes of stock entitled to vote of such corporation) owned, or were considered as owning, at any time during the 10-year period ending on the date of the sale or exchange more than 50 percent of the total combined voting power of all classes of stock entitled to vote of such corporation, this paragraph shall apply only if such United States persons owned, or were considered as owning, at all times during the remainder of such 10-year period more than 50 percent of the total combined voting power of all classes of stock entitled to vote of such corporation. For purposes of this paragraph, stock owned by a United States person who is an individual, estate, or trust which was acquired by reason of the death of the predecessor in interest of such United States

Ante, p. 1018.

Ante, p. 1006.

26 USC 337.

Ante, p. 1000.

person shall be considered as owned by such United States person during the period such stock was owned by such predecessor in interest, and during the period such stock was owned by any other predecessor in interest if between such United States person and such other predecessor in interest there was no transfer other than by reason of the death of an individual.

“(4) UNITED STATES INCOME.—Any item includible in gross income of the foreign corporation under this chapter as income derived from sources within the United States of a foreign corporation engaged in trade or business in the United States.

“(5) AMOUNTS INCLUDED IN GROSS INCOME UNDER SECTION 1247.—If the United States person whose stock is sold or exchanged was a qualified shareholder (as defined in section 1247(c)) of a foreign corporation which was a foreign investment company (as described in section 1246(b)(1)), the earnings and profits of the foreign corporation for taxable years in which such person was a qualified shareholder.

Ante, p. 1039.
Ante, p. 1036.

“(e) SALES OR EXCHANGES OF STOCK IN CERTAIN DOMESTIC CORPORATIONS.—Under regulations prescribed by the Secretary or his delegate, if—

“(1) a United States person sells or exchanges stock of a domestic corporation, or receives a distribution from a domestic corporation which, under section 302 or 331, is treated as an exchange of stock, and

26 USC 302,
331.

“(2) such domestic corporation was formed or availed of principally for the holding, directly or indirectly, of stock of one or more foreign corporations,

such sale or exchange shall, for purposes of this section, be treated as a sale or exchange of the stock of the foreign corporation or corporations held by the domestic corporation.

“(f) EXCEPTIONS.—This section shall not apply to—

“(1) distributions to which section 303 (relating to distributions in redemption of stock to pay death taxes) applies;

26 USC 303.

“(2) gain realized on exchanges to which section 356 (relating to receipt of additional consideration in certain reorganizations) applies; or

26 USC 356.

“(3) any amount to the extent that such amount is, under any other provision of this title, treated as—

“(A) a dividend,

“(B) gain from the sale of an asset which is not a capital asset, or

“(C) gain from the sale of an asset held for not more than 6 months.

“(g) TAXPAYER TO ESTABLISH EARNINGS AND PROFITS.—Unless the taxpayer establishes the amount of the earnings and profits of the foreign corporation to be taken into account under subsection (a), all gain from the sale or exchange shall be considered a dividend under subsection (a), and unless the taxpayer establishes the amount of foreign taxes to be taken into account under subsection (b), the limitation of such subsection shall not apply.”

(b) CLERICAL AMENDMENT.—The table of sections for such part IV is amended by adding at the end thereof the following:

“Sec. 1248. Gain from certain sales or exchanges of stock in certain foreign corporations.”

(c) EFFECTIVE DATE.—The amendments made by this section shall apply with respect to sales or exchanges occurring after December 31, 1962.

76 STAT. 1045.

SEC. 16. SALES AND EXCHANGES OF PATENTS, ETC., TO CERTAIN FOREIGN CORPORATIONS.

(a) **TREATMENT OF GAIN AS ORDINARY INCOME.**—Part IV of subchapter P of chapter 1 (relating to special rules for determining capital gains and losses) is amended by adding after section 1248 (as added by section 15 of this Act) the following new section:

Ante, p. 1041.

“SEC. 1249. GAIN FROM CERTAIN SALES OR EXCHANGES OF PATENTS, ETC., TO FOREIGN CORPORATIONS.

“(a) **GENERAL RULE.**—Except as provided in subsection (c), gain from the sale or exchange after December 31, 1962, of a patent, an invention, model, or design (whether or not patented), a copyright, a secret formula or process, or any other similar property right to any foreign corporation by any United States person (as defined in section 7701(a)(30)) which controls such foreign corporation shall, if such gain would (but for the provisions of this subsection) be gain from the sale or exchange of a capital asset or of property described in section 1231, be considered as gain from the sale or exchange of property which is neither a capital asset nor property described in section 1231.

Ante, p. 988.

26 USC 1231.

“(b) **CONTROL.**—For purposes of subsection (a), control means, with respect to any foreign corporation, the ownership, directly or indirectly, of stock possessing more than 50 percent of the total combined voting power of all classes of stock entitled to vote. For purposes of this subsection, the rules for determining ownership of stock prescribed by section 958 shall apply.”

Ante, p. 1018.

(b) **CLERICAL AMENDMENT.**—The table of sections for such part IV is amended by adding at the end thereof the following:

“Sec. 1249. Gain from certain sales or exchanges of patents, etc., to foreign corporations.”

(c) **EFFECTIVE DATE.**—The amendments made by this section shall apply to taxable years beginning after December 31, 1962.

SEC. 17. TAX TREATMENT OF COOPERATIVES AND PATRONS.

(a) **IN GENERAL.**—Chapter 1 (relating to normal taxes and surtaxes) is amended by adding at the end thereof the following new subchapter:

“Subchapter T—Cooperatives and Their Patrons

“Part I. Tax treatment of cooperatives.

“Part II. Tax treatment by patrons of patronage dividends.

“Part III. Definitions; special rules.

“PART I—TAX TREATMENT OF COOPERATIVES

“Sec. 1381. Organizations to which part applies.

“Sec. 1382. Taxable income of cooperatives.

“Sec. 1383. Computation of tax where cooperative redeems non-qualified written notices of allocation.

“SEC. 1381. ORGANIZATIONS TO WHICH PART APPLIES.

“(a) **IN GENERAL.**—This part shall apply to—

26 USC 521.

“(1) any organization exempt from tax under section 521 (relating to exemption of farmers' cooperatives from tax), and

“(2) any corporation operating on a cooperative basis other than an organization—

26 USC 1

et seq.

26 USC 591-

595.

“(A) which is exempt from tax under this chapter,

“(B) which is subject to the provisions of—

“(i) part II of subchapter H (relating to mutual savings banks, etc.), or

“(ii) subchapter L (relating to insurance companies), 26 USC 801-843.

or

“(C) which is engaged in furnishing electric energy, or providing telephone service, to persons in rural areas.

“(b) TAX ON CERTAIN FARMERS’ COOPERATIVES.—An organization described in subsection (a) (1) shall be subject to the taxes imposed by section 11 or 1201.

“SEC. 1382. TAXABLE INCOME OF COOPERATIVES.

26 USC 11,
1201.

“(a) GROSS INCOME.—Except as provided in subsection (b), the gross income of any organization to which this part applies shall be determined without any adjustment (as a reduction in gross receipts, an increase in cost of goods sold, or otherwise) by reason of any allocation or distribution to a patron out of the net earnings of such organization.

“(b) PATRONAGE DIVIDENDS.—In determining the taxable income of an organization to which this part applies, there shall not be taken into account amounts paid during the payment period for the taxable year—

“(1) as patronage dividends (as defined in section 1388(a)), to the extent paid in money, qualified written notices of allocation (as defined in section 1388(c)), or other property (except nonqualified written notices of allocation (as defined in section 1388(d))) with respect to patronage occurring during such taxable year; or Post, p. 1049.

“(2) in money or other property (except written notices of allocation) in redemption of a nonqualified written notice of allocation which was paid as a patronage dividend during the payment period for the taxable year during which the patronage occurred. Post, p. 1051.

For purposes of this title, any amount not taken into account under the preceding sentence shall be treated in the same manner as an item of gross income and as a deduction therefrom.

“(c) DEDUCTION FOR NONPATRONAGE DISTRIBUTIONS, ETC.—In determining the taxable income of an organization described in section 1381(a) (1), there shall be allowed as a deduction (in addition to other deductions allowable under this chapter)— Ante, p. 1045.

“(1) amounts paid during the taxable year as dividends on its capital stock; and

“(2) amounts paid during the payment period for the taxable year—

“(A) in money, qualified written notices of allocation, or other property (except nonqualified written notices of allocation) on a patronage basis to patrons with respect to its earnings during such taxable year which are derived from business done for the United States or any of its agencies or from sources other than patronage, or

“(B) in money or other property (except written notices of allocation) in redemption of a nonqualified written notice of allocation which was paid, during the payment period for the taxable year during which the earnings were derived, on a patronage basis to a patron with respect to earnings derived from business or sources described in subparagraph (A).

“(d) PAYMENT PERIOD FOR EACH TAXABLE YEAR.—For purposes of subsections (b) and (c) (2), the payment period for any taxable year is the period beginning with the first day of such taxable year and ending with the fifteenth day of the ninth month following the close of such year. For purposes of subsections (b) (1) and (c) (2) (A), a

qualified check issued during the payment period shall be treated as an amount paid in money during such period if endorsed and cashed on or before the 90th day after the close of such period.

“(e) **PRODUCTS MARKETING UNDER POOLING ARRANGEMENTS.**—For purposes of subsection (b), in the case of a pooling arrangement for the marketing of products, the patronage shall (to the extent provided in regulations prescribed by the Secretary or his delegate) be treated as patronage occurring during the taxable year in which the pool closes.

“(f) **TREATMENT OF EARNINGS RECEIVED AFTER PATRONAGE OCCURRED.**—If any portion of the earnings from business done with or for patrons is includible in the organization's gross income for a taxable year after the taxable year during which the patronage occurred, then for purposes of applying subsection (b) to such portion the patronage shall, to the extent provided in regulations prescribed by the Secretary or his delegate, be considered to have occurred during the taxable year of the organization during which such earnings are includible in gross income.

“SEC. 1383. COMPUTATION OF TAX WHERE COOPERATIVE REDEEMS NONQUALIFIED WRITTEN NOTICES OF ALLOCATION.

Ante, p. 1046.

“(a) **GENERAL RULE.**—If, under section 1382(b) (2) or (c) (2) (B), a deduction is allowable to an organization for the taxable year for amounts paid in redemption of nonqualified written notices of allocation, then the tax imposed by this chapter on such organization for the taxable year shall be the lesser of the following:

“(1) the tax for the taxable year computed with such deduction; or

“(2) an amount equal to—

“(A) the tax for the taxable year computed without such deduction, minus

“(B) the decrease in tax under this chapter for any prior taxable year (or years) which would result solely from treating such nonqualified written notices of allocation as qualified written notices of allocation.

“(b) **SPECIAL RULES.**—

“(1) If the decrease in tax ascertained under subsection (a) (2) (B) exceeds the tax for the taxable year (computed without the deduction described in subsection (a)) such excess shall be considered to be a payment of tax on the last day prescribed by law for the payment of tax for the taxable year, and shall be refunded or credited in the same manner as if it were an overpayment for such taxable year.

“(2) For purposes of determining the decrease in tax under subsection (a) (2) (B), the stated dollar amount of any nonqualified written notice of allocation which is to be treated under such subsection as a qualified written notice of allocation shall be the amount paid in redemption of such written notice of allocation which is allowable as a deduction under section 1382(b) (2) or (c) (2) (B) for the taxable year.

“(3) If the tax imposed by this chapter for the taxable year is the amount determined under subsection (a) (2), then the deduction described in subsection (a) shall not be taken into account for any purpose of this subtitle other than for purposes of this section.

"PART II—TAX TREATMENT BY PATRONS OF PATRONAGE DIVIDENDS

"Sec. 1385. Amounts includible in patron's gross income.

"SEC. 1385. AMOUNTS INCLUDIBLE IN PATRON'S GROSS INCOME.

"(a) **GENERAL RULE.**—Except as otherwise provided in subsection (b), each person shall include in gross income—

"(1) the amount of any patronage dividend which is paid in money, a qualified written notice of allocation, or other property (except a nonqualified written notice of allocation), and which is received by him during the taxable year from an organization described in section 1381(a), and

"(2) any amount, described in section 1382(c)(2)(A) (relating to certain nonpatronage distributions by tax-exempt farmers' cooperatives), which is paid in money, a qualified written notice of allocation, or other property (except a nonqualified written notice of allocation), and which is received by him during the taxable year from an organization described in section 1381(a)

(1).

"(b) **EXCLUSION FROM GROSS INCOME.**—Under regulations prescribed by the Secretary or his delegate, the amount of any patronage dividend, and any amount received on the redemption, sale, or other disposition of a nonqualified written notice of allocation which was paid as a patronage dividend, shall not be included in gross income to the extent that such amount—

"(1) is properly taken into account as an adjustment to basis of property, or

"(2) is attributable to personal, living, or family items.

"(c) **TREATMENT OF CERTAIN NONQUALIFIED WRITTEN NOTICES OF ALLOCATION.**—

"(1) **APPLICATION OF SUBSECTION.**—This subsection shall apply to any nonqualified written notice of allocation which—

"(A) was paid as a patronage dividend, or

"(B) was paid by an organization described in section 1381(a)(1) on a patronage basis with respect to earnings derived from business or sources described in section 1382(c)(2)(A).

"(2) **BASIS; AMOUNT OF GAIN.**—In the case of any nonqualified written notice of allocation to which this subsection applies, for purposes of this chapter—

"(A) the basis of such written notice of allocation in the hands of the patron to whom such written notice of allocation was paid shall be zero,

"(B) the basis of such written notice of allocation which was acquired from a decedent shall be its basis in the hands of the decedent, and

"(C) gain on the redemption, sale, or other disposition of such written notice of allocation by any person shall, to the extent that the stated dollar amount of such written notice of allocation exceeds its basis, be considered as gain from the sale or exchange of property which is not a capital asset.

Ante, p. 1045.

Ante, p. 1046.

"PART III—DEFINITIONS; SPECIAL RULES

"Sec. 1388. Definitions; special rules.

"SEC. 1388. DEFINITIONS; SPECIAL RULES.

"(a) PATRONAGE DIVIDEND.—For purposes of this subchapter, the term 'patronage dividend' means an amount paid to a patron by an organization to which part I of this subchapter applies—

"(1) on the basis of quantity or value of business done with or for such patron,

"(2) under an obligation of such organization to pay such amount, which obligation existed before the organization received the amount so paid, and

"(3) which is determined by reference to the net earnings of the organization from business done with or for its patrons.

Such term does not include any amount paid to a patron to the extent that (A) such amount is out of earnings other than from business done with or for patrons, or (B) such amount is out of earnings from business done with or for other patrons to whom no amounts are paid, or to whom smaller amounts are paid, with respect to substantially identical transactions.

"(b) WRITTEN NOTICE OF ALLOCATION.—For purposes of this subchapter, the term 'written notice of allocation' means any capital stock, revolving fund certificate, retain certificate, certificate of indebtedness, letter of advice, or other written notice, which discloses to the recipient the stated dollar amount allocated to him by the organization and the portion thereof, if any, which constitutes a patronage dividend.

"(c) QUALIFIED WRITTEN NOTICE OF ALLOCATION.—

"(1) DEFINED.—For purposes of this subchapter, the term 'qualified written notice of allocation' means—

"(A) a written notice of allocation which may be redeemed in cash at its stated dollar amount at any time within a period beginning on the date such written notice of allocation is paid and ending not earlier than 90 days from such date, but only if the distributee receives written notice of the right of redemption at the time he receives such written notice of allocation; and

"(B) a written notice of allocation which the distributee has consented, in the manner provided in paragraph (2), to take into account at its stated dollar amount as provided in section 1385(a).

Such term does not include any written notice of allocation which is paid as part of a patronage dividend or as part of a payment described in section 1382(c)(2)(A), unless 20 percent or more of the amount of such patronage dividend, or such payment, is paid in money or by qualified check.

"(2) MANNER OF OBTAINING CONSENT.—A distributee shall consent to take a written notice of allocation into account as provided in paragraph (1)(B) only by—

"(A) making such consent in writing,

"(B) obtaining or retaining membership in the organization after—

"(i) such organization has adopted (after the date of the enactment of the Revenue Act of 1962) a bylaw providing that membership in the organization constitutes such consent, and

"(ii) he has received a written notification and copy of such bylaw, or

Ante, p. 1048.

Ante, p. 1046.

“(C) if neither subparagraph (A) nor (B) applies, endorsing and cashing a qualified check, paid as a part of the patronage dividend or payment of which such written notice of allocation is also a part, on or before the 90th day after the close of the payment period for the taxable year of the organization for which such patronage dividend or payment is paid.

“(3) PERIOD FOR WHICH CONSENT IS EFFECTIVE.—

“(A) GENERAL RULE.—Except as provided in subparagraph (B)—

“(i) a consent described in paragraph (2)(A) shall be a consent with respect to all patronage of the distributee with the organization occurring (determined with the application of section 1382(e)) during the taxable year of the organization during which such consent is made and all subsequent taxable years of the organization; and

Ante, p. 1047.

“(ii) a consent described in paragraph (2)(B) shall be a consent with respect to all patronage of the distributee with the organization occurring (determined without the application of section 1382(e)) after he received the notification and copy described in paragraph (2)(B)(ii).

“(B) REVOCATION, ETC.—

“(i) Any consent described in paragraph (2)(A) may be revoked (in writing) by the distributee at any time. Any such revocation shall be effective with respect to patronage occurring on or after the first day of the first taxable year of the organization beginning after the revocation is filed with such organization; except that in the case of a pooling arrangement described in section 1382(e), a revocation made by a distributee shall not be effective as to any pool with respect to which the distributee has been a patron before such revocation.

“(ii) Any consent described in paragraph (2)(B) shall not be effective with respect to any patronage occurring (determined without the application of section 1382(e)) after the distributee ceases to be a member of the organization or after the bylaws of the organization cease to contain the provision described in paragraph (2)(B)(i).

“(4) QUALIFIED CHECK.—For purposes of this subchapter, the term ‘qualified check’ means only a check (or other instrument which is redeemable in money) which is paid as a part of a patronage dividend, or as a part of a payment described in section 1382(c)(2)(A), to a distributee who has not given consent as provided in paragraph (2)(A) or (B) with respect to such patronage dividend or payment, and on which there is clearly imprinted a statement that the endorsement and cashing of the check (or other instrument) constitutes the consent of the payee to include in his gross income, as provided in the Federal income tax laws, the stated dollar amount of the written notice of allocation which is a part of the patronage dividend or payment of which such qualified check is also a part. Such term does not include any check (or other instrument) which is paid as part of a patronage dividend or payment which does not include a written notice of allocation (other than a written notice of allocation described in paragraph (1)(A)).

Ante, p. 1046.

76 STAT. 1051.

“(d) **NONQUALIFIED WRITTEN NOTICE OF ALLOCATION.**—For purposes of this subchapter, the term ‘nonqualified written notice of allocation’ means a written notice of allocation which is not described in subsection (c) or a qualified check which is not cashed on or before the 90th day after the close of the payment period for the taxable year for which the distribution of which it is a part is paid.

“(e) **DETERMINATION OF AMOUNT PAID OR RECEIVED.**—For purposes of this subchapter, in determining amounts paid or received—

“(1) property (other than a written notice of allocation) shall be taken into account at its fair market value, and

“(2) a qualified written notice of allocation shall be taken into account at its stated dollar amount.”

(b) **TECHNICAL AMENDMENTS.**—

26 USC 521.

(1) Section 521(a) (relating to exemption of farmers’ cooperatives from tax) is amended by striking out “section 522” each place it appears therein and inserting in lieu thereof “part I of subchapter T (sec. 1381 and following)”.

Ante, p. 1045.

Repeal.

26 USC 522.

(2) Section 522 (relating to tax on farmers’ cooperatives) is hereby repealed.

26 USC 6072.

(3) Section 6072(d) (relating to time for filing income tax returns of exempt cooperative associations) is amended to read as follows:

“(d) **RETURNS OF COOPERATIVE ASSOCIATIONS.**—In the case of an income tax return of—

Ante, p. 1045.

“(1) an exempt cooperative association described in section 1381(a) (1), or

Ante, p. 1049.

“(2) an organization described in section 1381(a) (2) which is under an obligation to pay patronage dividends (as defined in section 1388(a)) in an amount equal to at least 50 percent of its net earnings from business done with or for its patrons, or which paid patronage dividends in such an amount out of the net earnings from business done with or for patrons during the most recent taxable year for which it had such net earnings,

a return made on the basis of a calendar year shall be filed on or before the 15th day of September following the close of the calendar year, and a return made on the basis of a fiscal year shall be filed on or before the 15th day of the 9th month following the close of the fiscal year.”

(4) The table of subchapters for chapter 1 is amended by adding at the end thereof the following:

“SUBCHAPTER T. Cooperatives and their patrons.”

(5) The table of sections for part III of subchapter F of chapter 1 is amended by striking out the last line thereof.

(c) **EFFECTIVE DATES.**—

(1) **FOR THE COOPERATIVES.**—Except as provided in paragraph (3), the amendments made by subsections (a) and (b) shall apply to taxable years of organizations described in section 1381(a) of the Internal Revenue Code of 1954 (as added by subsection (a)) beginning after December 31, 1962.

Ante, p. 1048.

(2) **FOR THE PATRONS.**—Except as provided in paragraph (3), section 1385 of the Internal Revenue Code of 1954 (as added by subsection (a)) shall apply with respect to any amount received from any organization described in section 1381(a) of such Code, to the extent that such amount is paid by such organization in a taxable year of such organization beginning after December 31, 1962.

(3) **APPLICATION OF EXISTING LAW.**—In the case of any money, written notice of allocation, or other property paid by any organization described in section 1381(a)—

(A) before the first day of the first taxable year of such organization beginning after December 31, 1962, or

(B) on or after such first day with respect to patronage occurring before such first day,
the tax treatment of such money, written notice of allocation, or other property (including the tax treatment of gain or loss on the redemption, sale, or other disposition of such written notice of allocation) by any person shall be made under the Internal Revenue Code of 1954 without regard to subchapter T of chapter 1 of such Code.

Ante, p. 1045.

SEC. 18. INCLUSION OF FOREIGN REAL PROPERTY IN GROSS ESTATE.

(a) AMENDMENTS TO INCLUDE FOREIGN REAL PROPERTY.—

(1) Section 2031(a) (relating to definition of gross estate) is amended by striking out “, except real property situated outside of the United States”.

26 USC 2031.

(2) The following provisions of chapter 11 (imposing an estate tax) are amended by striking out “(except real property situated outside of the United States)”:

26 USC 2001
et seq.

(A) section 2033 (relating to property in which the decedent had an interest),

(B) section 2034 (relating to dower or curtesy interests),

(C) section 2035(a) (relating to transactions in contemplation of death),

(D) section 2036(a) (relating to transfers with retained life estate),

(E) section 2037(a) (relating to transfers taking effect at death),

(F) section 2038(a) (relating to revocable transfers),

(G) section 2040 (relating to joint interests), and

(H) section 2041(a) (relating to powers of appointment).

(b) EFFECTIVE DATE.—

(1) Except as provided in paragraph (2), the amendments made by subsection (a) shall apply to the estates of decedents dying after the date of the enactment of this Act.

(2) In the case of a decedent dying after the date of the enactment of this Act and before July 1, 1964, the value of real property situated outside of the United States shall not be included in the gross estate (as defined in section 2031(a)) of the decedent—

(A) under section 2033, 2034, 2035(a), 2036(a), 2037(a), or 2038(a) to the extent the real property, or the decedent's interest in it, was acquired by the decedent before February 1, 1962;

26 USC 2033-
2038.

(B) under section 2040 to the extent such property or interest was acquired by the decedent before February 1, 1962, or was held by the decedent and the survivor in a joint tenancy or tenancy by the entirety before February 1, 1962; or

26 USC 2040.

(C) under section 2041(a) to the extent that before February 1, 1962, such property or interest was subject to a general power of appointment (as defined in section 2041) possessed by the decedent.

26 USC 2041.

In the case of real property, or an interest therein, situated outside of the United States (including a general power of appointment in respect of such property or interest, and including property held by the decedent and the survivor in a joint tenancy or tenancy by the entirety) which was acquired by the decedent after January 31, 1962, by gift within the meaning of section 2511, or from a prior decedent by devise or inheritance, or by reason of death, form of ownership, or other conditions (including the exer-

26 USC 2511.

76 STAT. 1053.

cise or nonexercise of a power of appointment), for purposes of this paragraph such property or interest therein shall be deemed to have been acquired by the decedent before February 1, 1962, if before that date the donor or prior decedent had acquired the property or his interest therein or had possessed a power of appointment in respect of the property or interest.

SEC. 19. REPORTING OF INTEREST, DIVIDEND, AND PATRONAGE DIVIDEND PAYMENTS OF \$10 OR MORE DURING A YEAR.

26 USC 6042.

(a) RETURNS REGARDING PAYMENT OF DIVIDENDS.—Section 6042 (relating to returns regarding corporate dividends, earnings, and profits) is amended to read as follows:

“SEC. 6042. RETURNS REGARDING PAYMENTS OF DIVIDENDS AND CORPORATE EARNINGS AND PROFITS.

“(a) REQUIREMENT OF REPORTING.—

“(1) IN GENERAL.—Every person—

“(A) who makes payments of dividends aggregating \$10 or more to any other person during any calendar year, or

“(B) who receives payments of dividends as a nominee and who makes payments aggregating \$10 or more during any calendar year to any other person with respect to the dividends so received,

shall make a return according to the forms or regulations prescribed by the Secretary or his delegate, setting forth the aggregate amount of such payments and the name and address of the person to whom paid.

“(2) RETURNS REQUIRED BY THE SECRETARY.—Every person who makes payments of dividends aggregating less than \$10 to any other person during any calendar year shall, when required by the Secretary or his delegate, make a return setting forth the aggregate amount of such payments, and the name and address of the person to whom paid.

“(b) DIVIDEND DEFINED.—

“(1) GENERAL RULE.—For purposes of this section, the term ‘dividend’ means—

“(A) any distribution by a corporation which is a dividend (as defined in section 316); and

“(B) any payment made by a stockbroker to any person as a substitute for a dividend (as so defined).

“(2) EXCEPTIONS.—For purposes of this section, the term ‘dividend’ does not include—

“(A) to the extent provided in regulations prescribed by the Secretary or his delegate, any distribution or payment—

“(i) by a foreign corporation, or

“(ii) to a foreign corporation, a nonresident alien, or a partnership not engaged in trade or business in the United States and composed in whole or in part of nonresident aliens; and

“(B) any amount described in section 1373 (relating to undistributed taxable income of electing small business corporations).

“(3) SPECIAL RULE.—If the person making any payment described in subsection (a) (1) (A) or (B) is unable to determine the portion of such payment which is a dividend or is paid with respect to a dividend, he shall, for purposes of subsection (a) (1), treat the entire amount of such payment as a dividend or as an amount paid with respect to a dividend.

26 USC 316.

26 USC 1373.

"(c) STATEMENTS TO BE FURNISHED TO PERSONS WITH RESPECT TO WHOM INFORMATION IS FURNISHED.—Every person making a return under subsection (a) (1) shall furnish to each person whose name is set forth in such return a written statement showing—

"(1) the name and address of the person making such return, and

"(2) the aggregate amount of payments to the person as shown on such return.

The written statement required under the preceding sentence shall be furnished to the person on or before January 31 of the year following the calendar year for which the return under subsection (a) (1) was made. No statement shall be required to be furnished to any person under this subsection if the aggregate amount of payments to such person as shown on the return made under subsection (a) (1) is less than \$10.

"(d) STATEMENTS TO BE FURNISHED BY CORPORATIONS TO SECRETARY.—Every corporation shall, when required by the Secretary or his delegate—

"(1) furnish to the Secretary or his delegate a statement stating the name and address of each shareholder, and the number of shares owned by each shareholder;

"(2) furnish to the Secretary or his delegate a statement of such facts as will enable him to determine the portion of the earnings and profits of the corporation (including gains, profits, and income not taxed) accumulated during such periods as the Secretary or his delegate may specify, which have been distributed or ordered to be distributed, respectively, to its shareholders during such taxable years as the Secretary or his delegate may specify; and

"(3) furnish to the Secretary or his delegate a statement of its accumulated earnings and profits and the names and addresses of the individuals or shareholders who would be entitled to such accumulated earnings and profits if divided or distributed, and of the amounts that would be payable to each."

(b) RETURNS REGARDING PAYMENT OF PATRONAGE DIVIDENDS.—Section 6044 (relating to returns regarding patronage dividends) is amended to read as follows: 26 USC 6044.

SEC. 6044. RETURNS REGARDING PAYMENTS OF PATRONAGE DIVIDENDS.

"(a) REQUIREMENT OF REPORTING.—

"(1) IN GENERAL.—Except as otherwise provided in this section, every cooperative to which part I of subchapter T of chapter 1 applies, which makes payments of amounts described in subsection (b) aggregating \$10 or more to any person during any calendar year, shall make a return according to the forms or regulations prescribed by the Secretary or his delegate, setting forth the aggregate amount of such payments and the name and address of the person to whom paid. Ante, p. 1045.

"(2) RETURNS REQUIRED BY THE SECRETARY.—Every such cooperative which makes payments of amounts described in subsection (b) aggregating less than \$10 to any person during any calendar year shall, when required by the Secretary or his delegate, make a return setting forth the aggregate amount of such payments and the name and address of the person to whom paid.

"(b) AMOUNTS SUBJECT TO REPORTING.—

"(1) GENERAL RULE.—Except as otherwise provided in this section, the amounts subject to reporting under subsection (a) are—

Ante, p. 1049.

“(A) the amount of any patronage dividend (as defined in section 1388(a)) which is paid in money, qualified written notices of allocation (as defined in section 1388(c)), or other property (except nonqualified written notices of allocation as defined in section 1388(d)),

Ante, p. 1046.

“(B) any amount described in section 1382(c)(2)(A) (relating to certain nonpatronage distributions) which is paid in money, qualified written notices of allocation, or other property (except nonqualified written notices of allocation) by an organization exempt from tax under section 521 (relating to exemption of farmers’ cooperatives from tax), and

26 USC 521.

“(C) any amount described in section 1382(b)(2) (relating to redemption of nonqualified written notices of allocation) and, in the case of an organization described in section 1381(a)(1), any amount described in section 1382(c)(2)(B) (relating to redemption of nonqualified written notices of allocation paid with respect to earnings derived from sources other than patronage).

Ante, p. 1045.

“(2) EXCEPTIONS.—The provisions of subsection (a) shall not apply, to the extent provided in regulations prescribed by the Secretary or his delegate, to any payment—

“(A) by a foreign corporation, or

“(B) to a foreign corporation, a nonresident alien, or a partnership not engaged in trade or business in the United States and composed in whole or in part of nonresident aliens.

“(c) EXEMPTION FOR CERTAIN CONSUMER COOPERATIVES.—A cooperative which the Secretary or his delegate determines is primarily engaged in selling at retail goods or services of a type that are generally for personal, living, or family use shall, upon application to the Secretary or his delegate, be granted exemption from the reporting requirements imposed by subsection (a). Application for exemption under this subsection shall be made in accordance with regulations prescribed by the Secretary or his delegate.

“(d) DETERMINATION OF AMOUNT PAID.—For purposes of this section, in determining the amount of any payment—

“(1) property (other than a qualified written notice of allocation) shall be taken into account at its fair market value, and

“(2) a qualified written notice of allocation shall be taken into account at its stated dollar amount.

“(e) STATEMENTS TO BE FURNISHED TO PERSONS WITH RESPECT TO WHOM INFORMATION IS FURNISHED.—Every cooperative making a return under subsection (a)(1) shall furnish to each person whose name is set forth in such return a written statement showing—

“(1) the name and address of the cooperative making such return, and

“(2) the aggregate amount of payments to the person as shown on such return.

The written statement required under the preceding sentence shall be furnished to the person on or before January 31 of the year following the calendar year for which the return under subsection (a)(1) was made. No statement shall be required to be furnished to any person under this subsection if the aggregate amount of payments to such person as shown on the return made under subsection (a)(1) is less than \$10.”

(c) RETURNS REGARDING PAYMENT OF INTEREST.—Subpart B of part III of subchapter A of chapter 61 (relating to information returns) is amended by adding after section 6048 (as added by section 7(f) of this Act) the following new section:

Ante, p. 988.

"SEC. 6049. RETURNS REGARDING PAYMENTS OF INTEREST.**"(a) REQUIREMENT OF REPORTING.—****"(1) IN GENERAL.—Every person—**

"(A) who makes payments of interest (as defined in subsection (b)) aggregating \$10 or more to any other person during any calendar year, or

"(B) who receives payments of interest as a nominee and who makes payments aggregating \$10 or more during any calendar year to any other person with respect to the interest so received,

shall make a return according to the forms or regulations prescribed by the Secretary or his delegate, setting forth the aggregate amount of such payments and the name and address of the person to whom paid.

"(2) RETURNS REQUIRED BY THE SECRETARY.—Every person who makes payments of interest (as defined in subsection (b)) aggregating less than \$10 to any other person during any calendar year shall, when required by the Secretary or his delegate, make a return setting forth the aggregate amount of such payments and the name and address of the person to whom paid.

"(3) OTHER RETURNS REQUIRED BY SECRETARY.—Every corporation making payments, regardless of amounts, of interest other than interest as defined in subsection (b) shall, when required by regulations prescribed by the Secretary or his delegate, make a return according to the forms or regulations prescribed by the Secretary or his delegate, setting forth the amount paid and the name and address of the recipient of each such payment.

"(b) INTEREST DEFINED.—

"(1) GENERAL RULE.—For purposes of subsections (a) (1) and (2), the term 'interest' means—

"(A) interest on evidences of indebtedness (including bonds, debentures, notes, and certificates) issued by a corporation in registered form, and, to the extent provided in regulations prescribed by the Secretary or his delegate, interest on other evidences of indebtedness issued by a corporation of a type offered by corporations to the public;

"(B) interest on deposits with persons carrying on the banking business;

"(C) amounts (whether or not designated as interest) paid by a mutual savings bank, savings and loan association, building and loan association, cooperative bank, homestead association, credit union, or similar organization, in respect of deposits, investment certificates, or withdrawable or repurchasable shares;

"(D) interest on amounts held by an insurance company under an agreement to pay interest thereon; and

"(E) interest on deposits with stockbrokers and dealers in securities.

"(2) EXCEPTIONS.—For purposes of subsections (a) (1) and (2), the term 'interest' does not include—

"(A) interest on obligations described in section 103(a) (1) or (3) (relating to interest on certain governmental obligations); 26 USC 103.

"(B) to the extent provided in regulations prescribed by the Secretary or his delegate, any amount paid by or to a foreign corporation, a nonresident alien, or a partnership not engaged in trade or business in the United States and composed in whole or in part of nonresident aliens; and

76 STAT. 1057.

26 USC 1451.

“(C) any amount on which the person making payment is required to deduct and withhold a tax under section 1451 (relating to tax-free covenant bonds), or would be so required but for section 1451(d) (relating to benefit of personal exemptions).

“(c) STATEMENTS TO BE FURNISHED TO PERSONS WITH RESPECT TO WHOM INFORMATION IS FURNISHED.—Every person making a return under subsection (a) (1) shall furnish to each person whose name is set forth in such return a written statement showing—

“(1) the name and address of the person making such return, and

“(2) the aggregate amount of payments to the person as shown on such return.

The written statement required under the preceding sentence shall be furnished to the person on or before January 31 of the year following the calendar year for which the return under subsection (a) (1) was made. No statement shall be required to be furnished to any person under this subsection if the aggregate amount of payments to such person as shown on the return made under subsection (a) (1) is less than \$10.”

26 USC 6652.

(d) PENALTIES FOR FAILURE TO FILE INFORMATION RETURNS.—Section 6652 (relating to failure to file certain information returns) is amended to read as follows:

“SEC. 6652. FAILURE TO FILE CERTAIN INFORMATION RETURNS.

“(a) RETURNS RELATING TO PAYMENTS OF DIVIDENDS, INTEREST, AND PATRONAGE DIVIDENDS.—In the case of each failure to file a statement of the aggregate amount of payments to another person required by section 6042(a) (1) (relating to payments of dividends aggregating \$10 or more), section 6044(a) (1) (relating to payments of patronage dividends aggregating \$10 or more), or section 6049(a) (1) (relating to payments of interest aggregating \$10 or more), on the date prescribed therefor (determined with regard to any extension of time for filing), unless it is shown that such failure is due to reasonable cause and not to willful neglect, there shall be paid (upon notice and demand by the Secretary or his delegate and in the same manner as tax), by the person failing to so file the statement, \$10 for each such statement not so filed, but the total amount imposed on the delinquent person for all such failures during any calendar year shall not exceed \$25,000.

Ante, p. 1053.

Ante, p. 1054.

Ante, p. 1056.

“(b) OTHER RETURNS.—In the case of each failure to file a statement of a payment to another person required under authority of section 6041 (relating to certain information at source), section 6042(a) (2) (relating to payments of dividends aggregating less than \$10), section 6044(a) (2) (relating to payments of patronage dividends aggregating less than \$10), section 6049(a) (2) (relating to payments of interest aggregating less than \$10), section 6049(a) (3) (relating to other payments of interest by corporations), or section 6051(d) (relating to information returns with respect to income tax withheld), on the date prescribed therefor (determined with regard to any extension of time for filing), unless it is shown that such failure is due to reasonable cause and not to willful neglect, there shall be paid (upon notice and demand by the Secretary or his delegate and in the same manner as tax) by the person failing to so file the statement, \$1 for each such statement not so filed, but the total amount imposed on the delinquent person for all such failures during the calendar year shall not exceed \$1,000.

26 USC 6051.

"(c) ALCOHOL AND TOBACCO TAXES.—

"For penalties for failure to file certain information returns with respect to alcohol and tobacco taxes, see, generally, subtitle E."

(e) PENALTIES FOR FAILURE TO FURNISH STATEMENTS TO PERSONS WITH RESPECT TO WHOM RETURNS ARE FILED.—Subchapter B of chapter 68 (relating to assessable penalties) is amended by adding after section 6677 (as added by section 7(g) of this Act) the following new section:

Ante, p. 988.

"SEC. 6678. FAILURE TO FURNISH CERTAIN STATEMENTS.

"In the case of each failure to furnish a statement under section 6042(c), 6044(e), or 6049(c) on the date prescribed therefor to a person with respect to whom a return has been made under section 6042(a)(1), 6044(a)(1), or 6049(a)(1), respectively, unless it is shown that such failure is due to reasonable cause and not to willful neglect, there shall be paid (upon notice and demand by the Secretary or his delegate and in the same manner as tax), by the person failing to so furnish the statement, \$10 for each such statement not so furnished, but the total amount imposed on the delinquent person for all such failures during any calendar year shall not exceed \$25,000."

Ante, pp. 1054-1056.

(f) TECHNICAL AMENDMENTS.—Section 6041 (relating to information at source) is amended—

26 USC 6041.

(1) by striking out, in subsection (a) thereof, "(other than payments described in section 6042(1) or section 6045)" and inserting in lieu thereof "(other than payments to which section 6042(a)(1), 6044(a)(1), or 6049(a)(1) applies, and other than payments with respect to which a statement is required under the authority of section 6042(a)(2), 6044(a)(2), 6045, 6049(a)(2), or 6049(a)(3))"; and

(2) by striking out subsection (c) thereof.

(g) CLERICAL AMENDMENTS.—

(1) The table of sections for subpart B of part III of subchapter A of chapter 61 is amended—

(A) by striking out

"Sec. 6042. Returns regarding corporate dividends, earnings, and profits."

and inserting in lieu thereof

"Sec. 6042. Returns regarding payments of dividends and corporate earnings and profits.";

(B) by striking out

"Sec. 6044. Returns regarding patronage dividends."

and inserting in lieu thereof

"Sec. 6044. Returns regarding payments of patronage dividends.";

and

(C) by adding at the end of such table the following:

"Sec. 6049. Returns regarding payments of interest."

(2) The table of sections for subchapter B of chapter 68 is amended by adding at the end thereof the following:

"Sec. 6678. Failure to furnish certain statements."

(h) EFFECTIVE DATES.—

(1) **DIVIDENDS AND INTEREST.—**The amendments made by this section shall apply to payments of dividends and interest made on or after January 1, 1963.

(2) **PATRONAGE DIVIDENDS.—**The amendments made by this section shall apply to payments of amounts described in section 6044(b) of the Internal Revenue Code of 1954 made on or after January 1, 1963, with respect to patronage occurring on or after the first day of the first taxable year of the cooperative beginning on or after January 1, 1963.

SEC. 20. INFORMATION WITH RESPECT TO CERTAIN FOREIGN ENTITIES.

(a) INFORMATION TO BE FURNISHED BY INDIVIDUALS, DOMESTIC CORPORATIONS, ETC., WITH RESPECT TO CERTAIN FOREIGN CORPORATIONS.—Section 6038 is amended to read as follows:

“SEC. 6038. INFORMATION WITH RESPECT TO CERTAIN FOREIGN CORPORATIONS.

“(a) REQUIREMENT.—

“(1) IN GENERAL.—Every United States person shall furnish, with respect to any foreign corporation which such person controls (within the meaning of subsection (d) (1)), such information as the Secretary or his delegate may prescribe by regulations relating to—

“(A) the name, the principal place of business, and the nature of business of such foreign corporation, and the country under whose laws incorporated;

“(B) the accumulated profits (as defined in section 902(c)) of such foreign corporation, including the items of income (whether or not included in gross income under chapter 1) deductions (whether or not allowed in computing taxable income under chapter 1), and any other items taken into account in computing such accumulated profits;

“(C) a balance sheet for such foreign corporation listing assets, liabilities, and capital;

“(D) transactions between such foreign corporation and—

“(i) such person,

“(ii) any other corporation which such person controls, and

“(iii) any United States person owning, at the time the transaction takes place, 10 percent or more of the value of any class of stock outstanding of such foreign corporation; and

“(E) a description of the various classes of stock outstanding, and a list showing the name and address of, and number of shares held by, each United States person who is a shareholder of record owning at any time during the annual accounting period 5 percent or more in value of any class of stock outstanding of such foreign corporation.

The Secretary or his delegate may also require the furnishing of any other information which is similar or related in nature to that specified in the preceding sentence.

“(2) PERIOD FOR WHICH INFORMATION IS TO BE FURNISHED, ETC.—

The information required under paragraph (1) shall be furnished for the annual accounting period of the foreign corporation ending with or within the United States person's taxable year. The information so required shall be furnished at such time and in such manner as the Secretary or his delegate shall by regulations prescribe.

“(3) LIMITATION.—No information shall be required to be furnished under this subsection with respect to any foreign corporation for any annual accounting period unless such information was required to be furnished under regulations in effect on the first day of such annual accounting period.

“(b) EFFECT OF FAILURE TO FURNISH INFORMATION.—

“(1) IN GENERAL.—If a United States person fails to furnish, within the time prescribed under paragraph (2) of subsection (a), any information with respect to any foreign corporation required under paragraph (1) of subsection (a), then—

74 Stat. 1014.
26 USC 6038.

Ante, p. 1000.

"(A) in applying section 901 (relating to taxes of foreign countries and possessions of the United States) to such United States person for the taxable year, the amount of taxes (other than taxes reduced under subparagraph (B)) paid or deemed paid (other than those deemed paid under section 904(d)) to any foreign country or possession of the United States for the taxable year shall be reduced by 10 percent, and

26 USC 901;
Ante, pp. 1001,
1031.

26 USC 904.

"(B) in applying sections 902 (relating to foreign tax credit for corporate stockholder in foreign corporation) and 960 (relating to special rules for foreign tax credit) to any such United States person which is a corporation (or to any person who acquires from any other person any portion of the interest of such other person in any such foreign corporation, but only to the extent of such portion) for any taxable year, the amount of taxes paid or deemed paid by each foreign corporation with respect to which such person is required to furnish information during the annual accounting period or periods with respect to which such information is required under paragraph (2) of subsection (a) shall be reduced by 10 percent.

Ante, p. 999.

Ante, p. 1020.

If such failure continues 90 days or more after notice by the Secretary or his delegate to the United States person, then the amount of the reduction under this paragraph shall be 10 percent plus an additional 5 percent for each 3-month period, or fraction thereof, during which such failure to furnish information continues after the expiration of such 90-day period.

"(2) **LIMITATION.**—The amount of the reduction under paragraph (1) for each failure to furnish information with respect to a foreign corporation required under subsection (a) (1) shall not exceed whichever of the following amounts is the greater:

"(A) \$10,000, or

"(B) the income of the foreign corporation for its annual accounting period with respect to which the failure occurs.

"(3) **SPECIAL RULES.**—

"(A) No taxes shall be reduced under this subsection more than once for the same failure.

"(B) For purposes of this subsection, the time prescribed under paragraph (2) of subsection (a) to furnish information (and the beginning of the 90-day period after notice by the Secretary) shall be treated as being not earlier than the last day on which (as shown to the satisfaction of the Secretary or his delegate) reasonable cause existed for failure to furnish such information.

"(C) In applying subsections (a) and (b) of section 902, and in applying subsection (a) of section 960, the reduction provided by this subsection shall not apply for purposes of determining the amount of accumulated profits in excess of income, war profits, and excess profits taxes.

"(c) **TWO OR MORE PERSONS REQUIRED TO FURNISH INFORMATION WITH RESPECT TO SAME FOREIGN CORPORATION.**—Where, but for this subsection, two or more United States persons would be required to furnish information under subsection (a) with respect to the same foreign corporation for the same period, the Secretary or his delegate may by regulations provide that such information shall be required only from one person. To the extent practicable, the determination of which person shall furnish the information shall be made on the basis of actual ownership of stock.

“(d) DEFINITIONS.—For purposes of this section—

“(1) CONTROL.—A person is in control of a corporation if such person owns stock possessing more than 50 percent of the total combined voting power of all classes of stock entitled to vote, or more than 50 percent of the total value of shares of all classes of stock, of a corporation. If a person is in control (within the meaning of the preceding sentence) of a corporation which in turn owns more than 50 percent of the total combined voting power of all classes of stock entitled to vote of another corporation, or owns more than 50 percent of the total value of the shares of all classes of stock of another corporation, then such person shall be treated as in control of such other corporation. For purposes of this paragraph, the rules prescribed by section 318(a) for determining ownership of stock shall apply; except that—

26 USC 318.

“(A) the second sentence of subparagraphs (A) and (B), and clause (ii) of subparagraph (C), of section 318(a) (2) shall not be applied so as to consider a United States person as owning stock which is owned by a person who is not a United States person, and

“(B) in applying clause (i) of subparagraph (C) of section 318(a) (2), the phrase ‘10 percent’ shall be substituted for the phrase ‘50 percent’ used in subparagraph (C).

“(2) ANNUAL ACCOUNTING PERIOD.—The annual accounting period of a foreign corporation is the annual period on the basis of which such corporation regularly computes its income in keeping its books.

“(e) CROSS REFERENCES.—

“(1) For provisions relating to penalties for violations of this section, see section 7203.

“(2) For definition of the term ‘United States person’, see section 7701(a)(30).”

(b) INFORMATION AS TO ORGANIZATION OR REORGANIZATION OF FOREIGN CORPORATIONS AND AS TO ACQUISITIONS OF THEIR STOCK.—Section 6046 (relating to returns as to creation or organization, or reorganization, of foreign corporations) is amended to read as follows:

74 Stat. 1016.
26 USC 6046.

“SEC. 6046. RETURNS AS TO ORGANIZATION OR REORGANIZATION OF FOREIGN CORPORATIONS AND AS TO ACQUISITIONS OF THEIR STOCK.

“(a) REQUIREMENT OF RETURN.—A return complying with the requirements of subsection (b) shall be made by—

“(1) each United States citizen or resident who is on January 1, 1963, an officer or director of a foreign corporation, 5 percent or more in value of the stock of which is owned by a United States person (as defined in section 7701(a) (30)), or who becomes such an officer or director at any time after such date,

“(2) each United States person who on January 1, 1963, owns 5 percent or more in value of the stock of a foreign corporation, or who, at any time after such date—

“(A) acquires stock which, when added to any stock owned on January 1, 1963, has a value equal to 5 percent or more of the value of the stock of a foreign corporation, or

“(B) acquires an additional 5 percent or more in value of the stock of a foreign corporation, and

“(3) each person who at any time after January 1, 1963, becomes a United States person while owning 5 percent or more in value of the stock of a foreign corporation.

“(b) FORM AND CONTENTS OF RETURNS.—The returns required by subsection (a) shall be in such form and shall set forth, in respect of

Ante, p. 988.

the foreign corporation, such information as the Secretary or his delegate prescribes by forms or regulations as necessary for carrying out the provisions of the income tax laws, except that in the case of persons described only in subsection (a) (1) the information required shall be limited to the names and addresses of persons described in subsection (a) (2).

"(c) OWNERSHIP OF STOCK.—For purposes of subsection (a), stock owned directly or indirectly by a person (including, in the case of an individual, stock owned by members of his family) shall be taken into account. For purposes of the preceding sentence, the family of an individual shall be considered as including only his brothers and sisters (whether by the whole or half blood), spouse, ancestors, and lineal descendants.

"(d) TIME FOR FILING.—Any return required by subsection (a) shall be filed on or before the 90th day after the day on which, under any provision of subsection (a), the United States citizen, resident, or person becomes liable to file such return.

"(e) LIMITATION.—

"(1) GENERAL RULE.—Except as provided in paragraph (2), no information shall be required to be furnished under this section with respect to any foreign corporation unless such information was required to be furnished under regulations which have been in effect for at least 90 days before the date on which the United States citizen, resident, or person becomes liable to file a return required under subsection (a).

"(2) EXCEPTION.—In the case of liability to file a return under subsection (a) arising on or after January 1, 1963, and before June 1, 1963—

"(A) no information shall be required to be furnished under this section with respect to any foreign corporation unless such information was required to be furnished under regulations in effect on or before March 1, 1963, and

"(B) if the date on which such regulations become effective is later than the day on which such liability arose, any return required by subsection (a) shall (in lieu of the time prescribed by subsection (d)) be filed on or before the 90th day after such date.

"(f) CROSS REFERENCE.—

"For provisions relating to penalties for violations of this section, see sections 6679 and 7203."

"(c) CIVIL PENALTY FOR FAILURE TO FILE RETURN.—Subchapter B of chapter 68 (relating to assessable penalties) is amended by adding after section 6678 (as added by section 19(e) of this Act) the following Ante, p. 1058. new section:

SEC. 6679. FAILURE TO FILE RETURNS AS TO ORGANIZATION OR REORGANIZATION OF FOREIGN CORPORATIONS AND AS TO ACQUISITIONS OF THEIR STOCK.

"(a) CIVIL PENALTY.—In addition to any criminal penalty provided by law, any person required to file a return under section 6046 Ante, p. 1061. who fails to file such return at the time provided in such section, or who files a return which does not show the information required pursuant to such section, shall pay a penalty of \$1,000, unless it is shown that such failure is due to reasonable cause.

"(b) DEFICIENCY PROCEDURES NOT TO APPLY.—Subchapter B of chapter 63 (relating to deficiency procedure for income, estate, and gift taxes) shall not apply in respect of the assessment or collection of any penalty imposed by subsection (a)." 26 USC 6211-6216.

26 USC 318.

(d) TECHNICAL AMENDMENTS.—

(1) Section 318(b) (relating to cross references) is amended by striking out “and” at the end of paragraph (5), by striking out the period at the end of paragraph (6) and inserting in lieu thereof “; and”, and by adding at the end thereof the following:

“(7) section 6038(d)(1) (relating to information with respect to certain foreign corporations).”

(2) The table of sections for subpart B of part III of subchapter A of chapter 61 is amended by striking out

“Sec. 6046. Returns as to creation or organization, or reorganization, of foreign corporations.”

and inserting in lieu thereof

“Sec. 6046. Returns as to organization or reorganization of foreign corporations and as to acquisitions of their stock.”

(3) The table of sections for subchapter B of chapter 68 is amended by adding at the end thereof the following:

“Sec. 6679. Failure to file returns as to organization or reorganization of foreign corporations and as to acquisitions of their stock.”

(e) EFFECTIVE DATE.—

(1) The amendments made by subsection (a) shall apply with respect to annual accounting periods of foreign corporations beginning after December 31, 1962.

(2) The amendments made by subsection (b) shall take effect on January 1, 1963.

SEC. 21. EXPENDITURES BY FARMERS FOR CLEARING LAND.

(a) **ALLOWANCE OF DEDUCTION.**—Part VI of subchapter B of chapter 1 (relating to itemized deductions for individuals and corporations) is amended by adding after section 181 (as added by section 2(c) of this Act) the following new section:

Ante, p. 971.

“SEC. 182. EXPENDITURES BY FARMERS FOR CLEARING LAND.

“(a) **IN GENERAL.**—A taxpayer engaged in the business of farming may elect to treat expenditures which are paid or incurred by him during the taxable year in the clearing of land for the purpose of making such land suitable for use in farming as expenses which are not chargeable to capital account. The expenditures so treated shall be allowed as a deduction.

“(b) **LIMITATION.**—The amount deductible under subsection (a) for any taxable year shall not exceed whichever of the following amounts is the lesser:

“(1) \$5,000, or

“(2) 25 percent of the taxable income derived from farming during the taxable year.

For purposes of paragraph (2), the term ‘taxable income derived from farming’ means the gross income derived from farming reduced by the deductions allowed by this chapter (other than by this section) which are attributable to the business of farming.

“(c) **DEFINITIONS.**—For purposes of subsection (a)—

“(1) The term ‘clearing of land’ includes (but is not limited to) the eradication of trees, stumps, and brush, the treatment or moving of earth, and the diversion of streams and watercourses.

“(2) The term ‘land suitable for use in farming’ means land which as a result of the activities described in paragraph (1) is suitable for use by the taxpayer or his tenant for the production of crops, fruits, or other agricultural products or for the sustenance of livestock.

“(d) EXCEPTIONS, ETC.—

“(1) EXCEPTIONS.—The expenditures to which subsection (a) applies shall not include—

“(A) the purchase, construction, installation, or improvement of structures, appliances, or facilities which are of a character which is subject to the allowance for depreciation provided in section 167, or

26 USC 167.

“(B) any amount paid or incurred which is allowable as a deduction without regard to this section.

“(2) CERTAIN PROPERTY USED IN THE CLEARING OF LAND.—

“(A) ALLOWANCE FOR DEPRECIATION.—The expenditures to which subsection (a) applies shall include a reasonable allowance for depreciation with respect to property of the taxpayer which is used in the clearing of land for the purpose of making such land suitable for use in farming and which, if used in a trade or business, would be property subject to the allowance for depreciation provided by section 167.

“(B) TREATMENT AS DEPRECIATION DEDUCTION.—For purposes of this chapter, any expenditure described in subparagraph (A) shall, to the extent allowed as a deduction under subsection (a), be treated as an amount allowed under section 167 for exhaustion, wear and tear, or obsolescence of the property which is used in the clearing of land.

“(e) ELECTION.—The election under subsection (a) for any taxable year shall be made within the time prescribed by law (including extensions thereof) for filing the return for such taxable year. Such election shall be made in such manner as the Secretary or his delegate may by regulations prescribe. Such election may not be revoked except with the consent of the Secretary or his delegate.”

(b) CONFORMING AMENDMENT.—Section 263(a)(1) (relating to disallowance of deductions for capital expenditures) is amended by striking out “or” at the end of subparagraph (C), by striking out the period at the end of subparagraph (D) and inserting “, or”, and by adding at the end thereof the following new subparagraph:

26 USC 263.

“(E) expenditures by farmers for clearing land deductible under section 182.”

(c) CLERICAL AMENDMENT.—The table of sections for such part VI is amended by adding at the end thereof the following:

“Sec. 182. Expenditures by farmers for clearing land.”

(d) EFFECTIVE DATE.—The amendments made by this section shall apply with respect to taxable years beginning after December 31, 1962.

SEC. 22. CHARITABLE CONTRIBUTIONS MADE FROM INCOME ATTRIBUTABLE TO SEVERAL TAXABLE YEARS.

(a) TREATMENT FOR PURPOSES OF PART I OF SUBCHAPTER Q.—Section 1307 (relating to rules applicable to part I of subchapter Q) is amended by adding at the end thereof the following new subsection:

26 USC 1307.

“(e) ELECTION WITH RESPECT TO CHARITABLE CONTRIBUTIONS.—In the case of an individual who elects (in such manner and at such time as the Secretary or his delegate prescribes by regulations) to have the provisions of this subsection apply, an amount received or accrued to which this part applies shall be reduced, for purposes of computing the tax liability of the taxpayer under this part with respect to the amount so received or accrued, by an amount equal to that portion of (1) the amount of charitable contributions made by the taxpayer during the taxable year in which the amount is so received or accrued

26 USC 170.

which are allowable as a deduction for such year under section 170 (determined without regard to this part), as (2) the amount received or accrued to which this part applies is of the adjusted gross income for the taxable year (determined without regard to this part). In any case in which the taxpayer elects to have the provisions of the preceding sentence apply, for purposes of computing the limitation on tax under this part—

“(1) only the same proportion of the amount to which this part applies shall be taken into account for purposes of computing the limitations under section 170(b)(1) (A) and (B) for taxable years before the taxable year in which such amount is received or accrued as (A) the excess of the maximum amount which could, if the taxpayer had made additional contributions described in clause (i), (ii), or (iii) of section 170(b)(1)(A), have been described in clause (1) of the preceding sentence over the amount described in such clause (1), bears to (B) such maximum amount, and

“(2) the portion of the amount of charitable contributions described in the preceding sentence shall not be taken into account in computing the tax for the taxable year in which the amount to which this part applies is received or accrued.”

(b) **EFFECTIVE DATE.**—The amendment made by subsection (a) shall apply with respect to amounts received or accrued in taxable years beginning after December 31, 1961.

SEC. 23. EFFECTIVE DATE OF SECTION 1371(c) OF THE INTERNAL REVENUE CODE OF 1954.

26 USC 1371.

(a) **IN GENERAL.**—Subject to the provisions of subsection (b), section 1371(c) of the Internal Revenue Code of 1954 (as added by section 2(a) of the Act entitled “An Act to amend the Internal Revenue Code of 1954 to provide a personal exemption for children placed for adoption and to clarify certain provisions relating to the election of small business corporations as to taxable status”, approved September 23, 1959 (Public Law 86-376)), shall (notwithstanding the provisions of the first sentence of section 2(d) of such Act) also apply to taxable years beginning after December 31, 1957, and before January 1, 1960.

(b) **ELECTION AND CONSENT BY CORPORATIONS; CONSENTS BY SHAREHOLDERS.**—Subsection (a) shall apply with respect to any corporation and its shareholders only if, within one year after the date of the enactment of this Act—

(1) such corporation (in such manner as the Secretary of the Treasury or his delegate prescribes by regulations) elects to have the provisions of subsection (a) apply and consents to the application of subsection (c); and

(2) each person who is a shareholder of such corporation on the date on which such corporation makes such election, and each person who was a shareholder of such corporation during any taxable year of such corporation beginning after December 31, 1957, and ending before the date of such election, consents (in such manner and at such time as the Secretary of the Treasury or his delegate prescribes by regulations) to such election and to the application of subsection (c).

(c) **TOLLING OF STATUTES OF LIMITATIONS.**—In any case in which a corporation makes an election under subsection (b)—

(1) if the assessment of any deficiency against the corporation making such election, or any shareholder of such corporation

who consents to such election, for any taxable year is prevented, at any time on or before the expiration of one year after the date of such election, by the operation of any law or rule of law, assessment of such deficiency may, nevertheless, be made, to the extent such deficiency is attributable to the application of subsection (a), at any time on or before the expiration of such one-year period; and

(2) if credit or refund of any overpayment of tax by the corporation making such election, or any shareholder of such corporation who consents to such election, for any taxable year is prevented, at any time on or before the expiration of one year after the date of such election, by the operation of any law or rule of law, credit or refund of such overpayment may, nevertheless, be allowed or made, to the extent such overpayment is attributable to the application of subsection (a), if claim therefor is filed on or before the expiration of such one-year period.

SEC. 24. CERTAIN LOSSES SUSTAINED IN CONVERTING FROM STREET RAILWAY TO BUS OPERATIONS.

(a) **IN GENERAL.**—If a corporation has a net operating loss for the taxable year ending December 31, 1953, or the taxable year ending December 31, 1954, principally as the result of conversion from street railways to bus operations with respect to part or all of the company's operations, then its unused conversion loss will be subject to the treatment provided in subsection (c).

(b) **UNUSED CONVERSION LOSS DEFINED.**—The amount of the unused conversion loss shall be the sum of the part of the net operating loss for each year described in subsection (a) which (without regard to this section) would be carried over to the sixth taxable year following the loss year if section 172(b) of the Internal Revenue Code of 1954 (or, where applicable, section 122(b) (2) (B) of the Internal Revenue Code of 1939) permitted such a carryover.

26 USC 172.

64 Stat. 938.

(c) **TREATMENT OF UNUSED CONVERSION LOSS.**—If a taxpayer has an unused conversion loss, then in determining the amount of the net operating loss carryover from the taxable year ending December 31, 1959, to each of the 5 taxable years following such taxable year for purposes of section 172 of the Internal Revenue Code of 1954, such unused conversion loss shall be treated as a net operating loss for the taxable year ending December 31, 1959. This subsection shall apply only for years in which the taxpayer is engaged in the furnishing or sale of transportation (as defined in section 1503(c) (1) (A) of the Internal Revenue Code of 1954).

26 USC 1503.

(d) **REGULATIONS.**—The Secretary of the Treasury, or his delegate, may prescribe by regulation such rules as may be necessary to carry out the purposes of this section.

SEC. 25. PENSION PLAN OF LOCAL UNION NUMBERED 435, INTERNATIONAL HOD CARRIERS' BUILDING AND COMMON LABORERS' UNION OF AMERICA.

The pension plan of Local Union Numbered 435 of the International Hod Carriers' Building and Common Laborers' Union of America, which was negotiated to take effect May 1, 1960, pursuant to an agreement between such union and the Building Trades Employers Association of Rochester, New York, Incorporated, and which has been held by the Internal Revenue Service to constitute a qualified trust under section 401(a) of the Internal Revenue Code of 1954, and to be exempt from taxation under section 501(a) of such Code, shall be held and considered to have been a qualified trust under such sec-

26 USC 401.

26 USC 501.

26 USC 401.
26 USC 501.

tion 401(a), and to have been exempt from taxation under such section 501(a), for the period beginning May 1, 1960, and ending April 20, 1961, but only if it is shown to the satisfaction of the Secretary of the Treasury or his delegate that the trust has not in this period been operated in a manner which would jeopardize the interests of its beneficiaries.

SEC. 26. CONTINUATION OF A PARTNERSHIP YEAR FOR SURVIVING PARTNER IN A TWO-MAN PARTNERSHIP WHERE ONE DIES.

53 Stat. 71.

(a) **CLOSE OF TAXABLE YEAR OF TWO-MAN PARTNERSHIP WHEN ONE PARTNER DIES.**—Section 188 of the Internal Revenue Code of 1939 (relating to different taxable years of partner and partnership) is amended—

(1) by striking out “If” and inserting in lieu thereof “(a) GENERAL RULE.—If”; and

(2) by adding at the end of such section 188 the following new subsection:

“(b) **TWO-MAN PARTNERSHIP.**—For the purpose of this chapter, the death of one of the partners of a partnership consisting of two members shall not, if the surviving partner so elects within one year after the date of enactment of this subsection, result in the termination of the partnership or in the closing of the taxable year of the partnership with respect to the surviving partner prior to the time the partnership year would have closed if neither partner had died or disposed of his interest.”

53 Stat. 462.
26 USC 7121.
53 Stat. 462.
26 USC 7122.

(b) **EFFECTIVE DATE, ETC.**—The amendments made by subsection (a) shall apply with respect to taxable years of a partnership beginning after December 31, 1946, to which the Internal Revenue Code of 1939 applies. If refund or credit of any overpayment resulting from the application of the amendments made by subsection (a) of this section (including interest, additions to the tax, and additional amounts), is prevented on the date of enactment of this Act, or within one year from such date, by the operation of any law or rule of law (other than section 3760 of the Internal Revenue Code of 1939 or section 7121 of the Internal Revenue Code of 1954, relating to closing agreements, and other than section 3761 of the Internal Revenue Code of 1939 or section 7122 of the Internal Revenue Code of 1954, relating to compromises), such refund or credit of such overpayment, may, nevertheless, be made or allowed if claim therefor is filed within one year after the date of the enactment of this Act. No interest shall be allowed or paid on any overpayment resulting from the enactment of this section.

SEC. 27. EXCLUSION FROM GROSS INCOME OF CERTAIN AWARDS MADE PURSUANT TO EVACUATION CLAIMS OF JAPANESE-AMERICAN PERSONS.

53 Stat. 4.
26 USC 1 et seq.

(a) **IN GENERAL.**—No amount received as an award under the Act entitled “An Act to authorize the Attorney General to adjudicate certain claims resulting from evacuation of certain persons of Japanese ancestry under military orders”, approved July 2, 1948, as amended by Public Law 116, Eighty-second Congress, and Public Law 673, Eighty-fourth Congress (50 U.S.C. App., secs. 1981–1987), shall be included in gross income for purposes of chapter 1 of the Internal Revenue Code of 1939 or chapter 1 of the Internal Revenue Code of 1954.

(b) **EFFECTIVE DATE, ETC.**—Subsection (a) shall apply with respect to taxable years ending after July 2, 1948. If refund or credit of any overpayment of Federal income tax resulting from the application

of subsection (a) (including interest, additions to the tax, additional amounts, and penalties) is prevented on the date of the enactment of this Act, or within one year from such date, by the operation of any law or rule of law, the refund or credit of such overpayment may nevertheless be made or allowed if claim therefor is filed within one year after the date of enactment of this Act. In the case of a claim to which the preceding sentence applies, the amount to be refunded or credited as an overpayment shall not be diminished by any credit or setoff based upon any item other than the amount of the award referred to in subsection (a). No interest shall be allowed or paid on any overpayment resulting from the application of this section.

SEC. 28. DEDUCTION FOR DEPRECIATION BY TENANT-STOCKHOLDER OF COOPERATIVE HOUSING CORPORATION.

(a) **ALLOWANCE OF DEDUCTION.**—Section 216 (relating to deductions by tenant-stockholders of a cooperative housing corporation) is amended by—

(1) amending the heading thereof to read as follows:

“SEC. 216. DEDUCTION OF TAXES, INTEREST, AND BUSINESS DEPRECIATION BY COOPERATIVE HOUSING CORPORATION TENANT-STOCKHOLDER.”; and

(2) adding at the end of section 216 the following new subsection:

“(c) TREATMENT AS PROPERTY SUBJECT TO DEPRECIATION.—So much of the stock of a tenant-stockholder in a cooperative housing corporation as is allocable, under regulations prescribed by the Secretary or his delegate, to a proprietary lease or right of tenancy in property subject to the allowance for depreciation under section 167(a) shall, to the extent such proprietary lease or right of tenancy is used by such tenant-stockholder in a trade or business or for the production of income, be treated as property subject to the allowance for depreciation under section 167(a).”

(b) **CLERICAL AMENDMENT.**—The table of sections for part VII of subchapter B of chapter 1 is amended by striking out the item relating to section 216 and inserting in lieu thereof the following:

“Sec. 216. Deduction of taxes, interest, and business depreciation by cooperative housing corporation tenant-stockholder.”

(c) **EFFECTIVE DATE.**—The amendments made by subsection (a) shall be effective with respect to taxable years beginning after December 31, 1961.

SEC. 29. DEDUCTION FOR INCOME TAX PURPOSES OF CONTRIBUTIONS TO CERTAIN ORGANIZATIONS FOR JUDICIAL REFORM.

For purposes of section 170 of the Internal Revenue Code of 1954 (relating to deduction for charitable, etc., contributions and gifts), a contribution or gift made after December 31, 1961, with respect to a referendum occurring during the calendar year 1962 to or for the use of any nonprofit organization created and operated exclusively—

(1) to consider proposals for the reorganization of the judicial branch of the government of any State of the United States or political subdivision of such State, and

(2) to provide information, make recommendations, and seek public support or opposition as to such proposals, shall be treated as a charitable contribution if no part of the net earnings of such organization inures to the benefit of any private shareholder or individual. The provisions of the preceding sentence shall not apply to any organization which participates in, or intervenes in, any political campaign on behalf of any candidate for public office.

SEC. 30. EFFECTIVE DATE OF AMENDMENT TO SECTION 1374(b).

The amendment made by section 2(b) of Public Law 86-376 (73 Stat. 699) shall take effect on September 2, 1958.

SEC. 31. TREATIES.

26 USC 7852.

Section 7852(d) of the Internal Revenue Code of 1954 (relating to treaty obligations) shall not apply in respect of any amendment made by this Act.

Approved October 16, 1962, 10:30 a. m.

